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Hisense

KELON

Ronshen

海信科龍電器股份有限公司

Hisense Kelon Electrical Holdings Company Limited

Stock Code: 00921



Annual Report 07

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Company Profile

Hisense Kelon Electrical Holdings Company Ltd. (the “Company”) and its subsidiaries (collectively referred as “Hisense Kelon” or the “Group”) are currently one of the largest manufacturer household electrical appliances in the People’s Republic of China (the “PRC” or “China”), and play an important role in the domestic and overseas refrigerator and air-conditioner markets.

Headquartered in Shunde District, Foshan City, Guangdong Province, Hisense Kelon, as one of the first refrigerators manufacturing enterprises commenced its production of refrigerators in 1984. The sales volume of Hisense Kelon’s refrigerators and air-conditioners has been among the highest in China for many years. In particular, Hisense Kelon’s refrigerators have embraced the biggest market share for a decade. The “Kelon” and “Ronshen” brand names are appraised as “The Chinese Well-known marks”. The Group adheres to its corporate philosophy of “relying on technology and the talents of its people to build up the Group”, and considers technology as the basic motivation for the Group’s development. Leveraging on its superior refrigeration technology and application of high technology on its products, Hisense Kelon’s refrigerators and air-conditioners have won good reputation in the industry and have earned the Group many honors for technology and products at a national level. For example, Hisense Kelon obtained the “National Scientific and Technological Advance Award” in 1996 for its CFC-free technology and only a few enterprises in the industry have ever won such award; Hisense Kelon obtained the same honor in 2000 for its refrigeration system by using hydrocarbon substances instead of CFC; In 2002, its proprietary “Independent Multi Cycling Refrigeration” technology was invented, with which Kelon’s refrigerators are equipped with independent temperature controls for both the cooling and freezing compartments. In 2003, its refrigerator “209S” was awarded the “United Nations Energy Saving Grand Prix; and the double-efficiency technique of Kelon’s air-conditioners broke the world record of air-conditioner energy-efficiency by achieving a ratio of 7.0 in 2004. The Group has reinforced its quality control based on its strength in technology, and Kelon’s products are highly praised by both consumers and authorities for its reliable and notable advantages in quality. In December 2005, the Company was pleased to be acknowledged as one of the “Top 500 Quality Companies in China” which is one of the most reliable labels by consumers. The “Kelon” brand air-conditioners and the “Ronshen” brand refrigerators were awarded the “Top 10 Quality Air-Conditioner Brands in China” and the “Top 10 Quality Refrigerator Brands in China”, respectively, and Kelon air-conditioners and Ronshen refrigerators were also ranked first and second, respectively, in the household electrical appliances sector. At the “Appliance World Expo Beijing 2006” held in Beijing, Kelon’s KFR-35GW/S3F and KFR-27GW/S3F air-conditioners and Kelon’s BCD-209S/E and BCD-215YMB refrigerators won the “Super Energy-saving Award”, as well as Ronshen’s BCD-568WYM refrigerator won the “Industrial Design Excellence Award”. “Ronshen” ’s “Energy Saving Grand Prix” series of refrigerators have been honored with the “United Nations Energy Saving Grand Prix” at a grand award ceremony jointly organized by the United Nations Development Programmed, the Global Environmental Protection and the China Household Electrical Appliances Association.

In 2007, Kelon Air-conditioner’s VC split type air-conditioners and VC cabinet type air-conditioners were formally granted the certificates of the “4th China Industrial Design IF Award”.

The Group will continue leveraging on the strength of Hisense, a major shareholder, in management and experience to implement a comprehensive reform to facilitate the healthy and stable development of the Group in the best interest of its shareholders. In solving the Group’s problems, the Company will begin with strengthening the operational management and will propose and implement the operational objectives of “creating competitive advantages for its products, improving the quality of products, making use of the synergy effect and providing more training to its staff”.

The Company will strictly carry out the operational objectives above, continuously promote operational quality, enhance its brand names’ recognition and awareness, and make outstanding achievement.

2007 Major Events Calendar

MARCH

The Share Reform Proposal of the Company was approved by the Ministry of Commerce of the People's Republic of China on 22 March 2007, and has been formally implemented on 29 March 2007. Meanwhile, the abbreviated name of the Company's A shares was changed from "S*ST Kelon" to "*ST Kelon".

APRIL

The construction of large refrigerator production line in Shunde was kicked off, which will have an annual production capacity of 160,000 Series SBS refrigerators.

Ronshen Freezer has established a strategic partnership with Pepsi Co. Thereby Ronshen Freezer has successfully developed a series of display cabinet type freezers which fit the marketing requirement of Pepsi Co and achieved a leap-forward development in 2007.

Kelon Air-conditioner's VC split type air-conditioners and VC cabinet type air-conditioners were formally granted the certificates of the "4th China Industrial Design IF Award", marking Kelon's air-conditioners to be the only air-conditioner products winning the "2006-07 IF Industrial Design Award", also known as the industrial design Oscar.

JUNE

After consideration and approval at the 2006 Annual General Meeting and subsequently approved by the Administration for Industry and Commerce of Guangdong Province, the Chinese and English names of the Company have been changed to 海信科龍電器股份有限公司 and HISENSE KELON ELECTRICAL HOLDINGS COMPANY LIMITED, respectively, which were officially effective since 21 June 2007.

The construction of the large refrigerator production line in Yangzhou, with a total investment of RMB36 million, was kicked off. The new production line was completed and commenced production in January 2008, resulting in the quality of double-door refrigerators, particularly multi-door refrigerators, surpassing that of the leading producers in the PRC.

JULY

Since the Company's operation result had returned to profit as shown in the audited annual report for the year 2006, Shenzhen Stock Exchange withdrew the special treatment of labeling the Company with a delisting risk warning sign. Accordingly, the abbreviated name of the Company's A shares was changed from "*ST Kelon" to "ST Kelon".

As effective from 26 July 2007, the Chinese and English abbreviations of H shares of the Company changed from "廣東科龍 (GUANGDONG KELON)" to "海信科龍 (HISENSE KELON)", and the stock code (0921) of its H shares remained unchanged.

OCTOBER

Totally RMB350 million was spent on removing and rebuilding Chengdu Refrigerator Production Base, with a designed annual capacity of 800,000 units.

DECEMBER

On 10 December 2007, the Company entered into the "Contract on Introducing Refrigerator Technology" with Toshiba Consumer Marketing Corporation (東芝電器營銷株式會社) with a view to enhance the competitive edge of its products by introducing advanced technology.

Chairman's Statement

Dear Shareholders,

I am pleased to present the annual report of the Company for the year ended 31 December 2007.

During the Reporting Period, the Company was exposed to operating pressure brought along by the changes in the macroeconomic environment including significant increase in raw material prices, accelerated appreciation of Renminbi and the macroeconomic environment monetary stringency in the PRC. Against the challenges, the Company adhered to its operating strategy of “creating product advantages, accelerating liquidity, enhancing management efficiency, reinforcing people training, achieving synergy”. With continuous efforts in improving our product sales structure to enhance the gross profit margin of its products and utilizations of reserved fund, intensifying technology renovation and disposal of idle assets, enhancing the geographical layout of production bases, as well as the contribution from all of its staff and other parties, the overall production and operation of the Company are on the track of sustainable healthy development and have achieved better results, whereas the profitability of the products needs to be further improved.

During the Reporting Period, the Company generated sales revenue of RMB8,320 million for the year, of which of refrigerators amounted to sales revenue amounted to RMB4,325 million, representing an increase of 29.96% as compared to the previous year; the sales revenue of air-conditioner business amounted to RMB3,215 million, representing an increase of 26.90% as compared to the previous year.

In 2007, the Company has introduced and actively promoted the scientific management in respect of project management; reinforced the training of talents and introduction of outstanding talents and advanced technologies; continuously improved its systems, expanded the sales and distribution channels, refreshed the self-owned brands to accelerate the development of the international market to lay new milestones for the industry. In addition, the Company, in prompt response to the changes in the market, capitalized the opportunities brought along by the “Taking Household Appliances to Rural Areas” policy as promulgated by the State government. Taking energy-saving and high-efficiency as the two directions for development, the Company, on the one hand, will continue to fine-tune its sales channels, improve product structures, explore new product markets and increase the brand awareness. On the other hand, the Company has reinforced the R&D, design and quality control for its products and technologies so as to enhance the quality of its products, forming a solid foundation for the establishment of core competitiveness. At December 2007, the Company entered into the “Contract on Introducing Refrigerator Technology” with Toshiba Consumer Marketing Corporation (東芝電器營銷株式會社) with a view to further consolidated in the refrigerator technology aspect leading position and has laid the solid foundation for the making core competitiveness.

Looking into 2008, the Company will uphold the strategy of “creating product advantages, enhancing product quality, mitigate the risk of production capacity, accelerating cash flow, reinforcing people training”, and further strengthen the R&D and design efforts to continuously improve the core competitiveness of its products; perfect the business layout to streamline and enhance the resource allocation; enhance the capital management to mitigate the risk of capital appropriation; monitor the progress of salary and assessment scheme so as to establish the long-term talent training and recruitment system and expand its strategic talent pool, with the ultimate objective of invigorating the healthy growth of the Company.

During the past year, the Company has regained the stability and growth basically, which is mainly attributable to the enthusiastic expectation and sincere trust of all our shareholders and the support of all social parties such as the government, financial instruction and partner, as well as our directors and supervisors together with excellent leadership of the management and the restless contribution of all our staff. I would like to take this opportunity to express my deepest gratitude to all of them and hope to receive your continuous support in the coming year!

The Chinese economy will hopefully maintain its robust growth momentum despite the numerous challenges confronting the PRC and global economy in the new year. The pursuit for higher living standard will continue to drive the growth and development of the home appliances sector. The Board of Directors is optimistic about the prospects of the Company in 2008. I also earnestly look forward to sharing a better and brighter future of Kelon with you all.

Tang Ye Guo
Chairman

The PRC, 24 April 2008

Management Discussion And Analysis

PERFORMANCE REVIEW

Year 2007 was a challenging year. During the past year, while the prices of global energy and raw materials surged; the consumer price index and production price index climbed up incessantly; the financing environment became worsen under domestic monetary stringency and increasing financing costs; the export sector was aggravated by the expanding trade surplus under continued appreciation of Renminbi. Against this background, enterprises were exposed to mounting pressure on operation and difficulties in the internationalization process, and the influence is expected to continue in 2008.

In response to such critical situation, the Company adhered to its operating strategy of “creating product advantages, accelerating cash flow, enhancing management efficiency, reinforcing people training, achieving synergy”. During the Reporting Period, the Company recorded a turnover from its principal operations of RMB8,319,960,000, representing an increase of 26.75% as compared to the corresponding period in 2006. Net profit was RMB203,657,000, representing an increase of 154,408,000 as compared to the corresponding period of 2006, and the profit attributable to equity holders was RMB238,712,000.

Operation Structure

During the Reporting Period, the sales revenues of refrigerator business, air-conditioner business and freezer and other businesses accounted for 51.98%, 38.64%, 3.90% and 5.48% of the total turnover of the principal operations of the Company, respectively, representing an increase of 29.96%, 26.90%, 40.03% and -3.31% as compared to the same period last year.

On the other hand, domestic and export sales accounted for 57.95% and 42.05% of the total turnover of the principal operations of the Company, respectively, representing an increase of 12.13% and 54.51% as compared to the same period last year.

Refrigerator Business

During the Reporting Period, with aggressive exploration of different markets, the Company successfully achieved substantial increases in sales and relatively significant enhancement of its products' overall profitability. For the domestic market, apart from adopting a number of measures such as reinforced product promotion, increased investments in research and development, and improved production efficiency, the Company also intensified advertising efforts to exert and amplify the advantages of the “Ronshen” brand, and effectively enhanced the operating results of the refrigerator business and obtained significant increases in sales and effective enhancement of profitability. The refrigerator business reached its annual sales target in domestic market in 2007. In respect of the export market, the Company fostered strong strategic cooperation with most of its international customers and achieved noticeable increases in its scale. However, because of a number of other factors such as the increases in the prices of major raw materials for the manufacture of refrigerators in 2007, appreciation of Renminbi, the profit margin of exported refrigerators narrowed and led to a decrease in the overall profit margin of refrigerator products as compared to the previous reporting period. In the next reporting period, the Company will focus on improving the sales structure of export products through expanding the overseas market for large-volume refrigerator, especially the export business of hi-tech products under its own brand with higher gross profit margin, with the objective to further enhance the overall profitability of refrigerator products.

During the Reporting Period, the refrigerator business of the Company achieved a sales revenues of approximately RMB4,325 million, representing a year-on-year growth of 29.96%, maintaining a leading position in the industry in the PRC.

Air-conditioner Business

During the Reporting Period, the Company aggressively developed the domestic and overseas markets, achieving considerable increase in the sales of air-conditioners. For the domestic market, the Company further developed its core technologies and launched a number of energy-saving, high efficiency products to expand its scale of sales. However, as the air-conditioner product market in the PRC concentrated and homogeneous competition of air-conditioner products intensified, the scale of domestic sales of air-conditioners still lagged behind that of its major competitors. For the export market, the Company successfully regained its lost major accounts upon resumption of operation, and achieved an increase in sales of air-conditioners which significantly outperformed the industry average, coupled with an increasing market share. The Company strengthened its efforts in increasing the technological content of its products and enhancing its product structures in response to the pressure from intense market competition and rising costs of raw materials.

During the Reporting Period, the air-conditioner business of the Company realized a sales income of approximately RMB3,215 million, representing a year-on-year growth of 26.90%.

Management Discussion And Analysis

Freezer Business

During the Reporting Period, the Company aggressively explored the domestic and international markets, especially the direct sales market, and achieved remarkable results. The direct sales business was set to target. At the medium-to-high-end customers with the provision of custom-made services to develop unique and customerized products. Currently, the Company has established strong strategic cooperation with a number of customers of well-known brands with the aim to refresh the market image of its freezers and to ensure sustainable and stable growth of the freezer business.

Technology, Research and Development

During the Reporting Period, the Company upheld the operation objective of “creating product advantages and talent training” and strengthen the development of research and development capabilities, especially the research and development of medium-to-high-end products to the technological quality, healthy and energy-saving capabilities of the products. In 2007, the Company obtained 103 patents in total, of which 39 patents were related to refrigerators and 56 were related to air-conditioners;

In 2007, the Company was accredited as “outstanding” in the examination of the First Enterprises with Intellectual Property Right Advantages in the Guangdong Province. Also, its key research and development programs including “mobile air-conditioners with indoor/ outdoor ventilation”, “high efficiency air duct parameter design and test of air duct with high efficiency and value enhancement research” were awarded Top Patent Award of the Guangdong Province and Science and Technology Award of Guangdong Province in 2007, respectively.

At the 2007 Innovation Design Ceremony & China Wuxi International Industrial Design Expo, Ronshen BCD-288WYM refrigerator was awarded the only “Best Outlook Award” in the refrigerators section; whereas the “Fengshang” series dual high-efficiency air-conditioner launched by Kelon air-conditioners in 2007 was awarded the “iF Industrial Design Award” for its innovative and unique outlook.

In respect of the research and development for freezer products, the Company enjoys a leading position within the industry in the PRC for its core technologies such as energy-saving and preservation, as well as its testing and management capabilities. On the other hand, “Ronshen” refrigerators has completed the introduction and assimilation of Japan’s Toshiba refrigerators products during the Reporting Period, which further consolidated and confirmed the leading position of the Company’s refrigerators in the PRC in terms of technology.

Analysis on the Influence Factors of the Results

The management of the Company was of the view that, the growth in the turnover from its principal operations and net profits was mainly attributable to the overall growth of the PRC economy and the industry, increase in idle assets disposal and revitalized revenues, as well as to the operation quality enhancement measures adopted by the Company during the Reporting Period. However, as the Company was generally in a stage of recovery, the results for the Reporting Period still fell below the planned objectives as a result of the multiple operation difficulties brought by historical problems and the pre-investment made by the Company for the purpose of long-term development.

Analysis of the main reasons for the growth in results:

- (1) The amount of cash recovered from the disposal of idle assets during the Reporting Period played an important role in meeting the demand for production capital by the Company during the peak season and in protecting the reputation of the Company, and enhanced its assets structure and quality to a certain extent. It also made significant contribution to the profits for the Reporting Period.
- (2) Expanded scale of sales generated increasing turnover from domestic and export sales. In respect of domestic sales, the Company focused on the important regions and reinforced the support for the sales network of the third and fourth markets, which gradually regained the confidence of the distributors. For export sales, the Company leveraged on its technology and product advantages to forcefully explore the overseas markets, strengthening the cooperation with its major international customers and regaining the market shares lost in the prior periods, realizing an increase in sales that outperformed the industry average.

Management Discussion And Analysis

- (3) During the Reporting Period, the Company continued to strengthen its research and development efforts to enhance the embedded technological content of the products in respect of health and energy-saving and successively launched French door refrigerators featuring innovative designs and air-conditioner products with high energy-saving efficiency, which were highly appraised by the market. In particular, the Company stepped up the technological cooperation at the international level in respect of high-end technologies, and completed the introduction of Japan's Toshiba freezer multi-door refrigerator during the Reporting Period. This has established a new height in the manufacture of refrigerators and brought along new development opportunities for the refrigerator industry.
- (4) Proactively enhancement of product sales structure, and deepening of brand position efforts to various segments including product research and development, production and manufacture and marketing, expansion into the high-end product market and improvement of the product profit margin. The concept provided a strong guidance for the corresponding operating activities of the Company and as a result successfully enhanced the profit margin of the Company's principal products. Of which, the profit margin of refrigerator products for domestic sales showed a notable increase as compared to the corresponding period of last year and enhanced the overall operating results of the Group.
- (5) During the Reporting Period, fundamental management standard represented by reinforced capital control was enhanced. The Company stepped up its fundamental management with a particular focus on the fundamental management of capital control. The reserve and production cash flow for all business segments of the Company was unanimously accelerated as compared to the corresponding periods. In particular, the reserve cash flow of the production bases has basically reached the advanced level in the industry. At the same time, the internal procedures of the Company were further streamlined, whereas various systems were implemented scientifically and specifically. These measures have invigorated the environment of management and promoted the management efficiency.
- (6) Implementation of a number of informatization projects, such as the SAP project and PLM project of the air-conditioner business, and the CRM project of the marketing section. The implementation of these projects have significantly promoted the operation efficiency of the Company and facilitated the management standardization of the Company.

Through the above offers, the operation quality of the Company showed considerable improvement as compared to the previous periods, but on the other hand, the results of the Company was adversely affected by the following factors.

- (1) With the consolidation of the air-conditioner industry and increasing brand concentration, although the Company recorded significant growth in revenues from the air-conditioner business of the Company during the Reporting Period, the growth was still below the planned objectives and economies of scale were not achieved. The overall scale of the Company's air-conditioner business still needed to be improved.
- (2) Increase in sales expense of the Company exceeded the increase in revenues. It was one of the important factors that affected the results of the Company during the Reporting Period. Aimed at enhancing its brand image and reputation, the Company significantly increased its advertising input and brand promotion during the Reporting Period and reinforced the establishment of channels and sales network to regain market confidence for the long-term development of the Company.
- (3) Some production bases of the Company were still out of production and in a state of sustained loss due to historical reasons. This has to a certain extent impaired the scale of operation of the Company and its recovery and growth.

OUTLOOK OF 2008

Look forward 2008, we are open to exceptional business opportunities: continuous growth of the PRC economy; the significant business opportunities brought to China by the 2008 Olympic Games; the forceful implementation of the State's policy on agriculture, rural areas and farmers, as well as the Project for "Taking Household Appliances to Rural Areas" recently promulgated by the Ministry of Commerce. All these will strongly stimulate the expenditure on the home appliances market, creating an immense headroom of growth for the market. At the same time, the consumer, suppliers and distributors resumed their confidence in the Company as its branding and sales network gradually recuperated; the Company's products possess advantages in energy-saving, high-efficiency and environmental friendliness, which are fully compatible with the State's energy-saving and environmental protection policies, and empower the Company with remarkable technological and product advantages. These opportunities will enable the Company to maintain positive growth for the forthcoming year. However, at the same time, it is foreseeable that the competition on the global household appliances market would intensify in 2008, taking into account significant increase in the prices of energy and raw materials around the world; worsening of financing environment under stringent domestic credit and increased financing costs; continued rapid appreciation of Renminbi; increased costs of sea freight and non-tariff barriers. All these have exposed home appliances enterprises to additional risks.

Management Discussion And Analysis

In 2008, the Company will uphold the operating strategy of “creating product advantages, enhancing product quality, maximizing production capacity, accelerating cash flow, reinforcing talent training”, with the objective to improve the operating results of the Company:

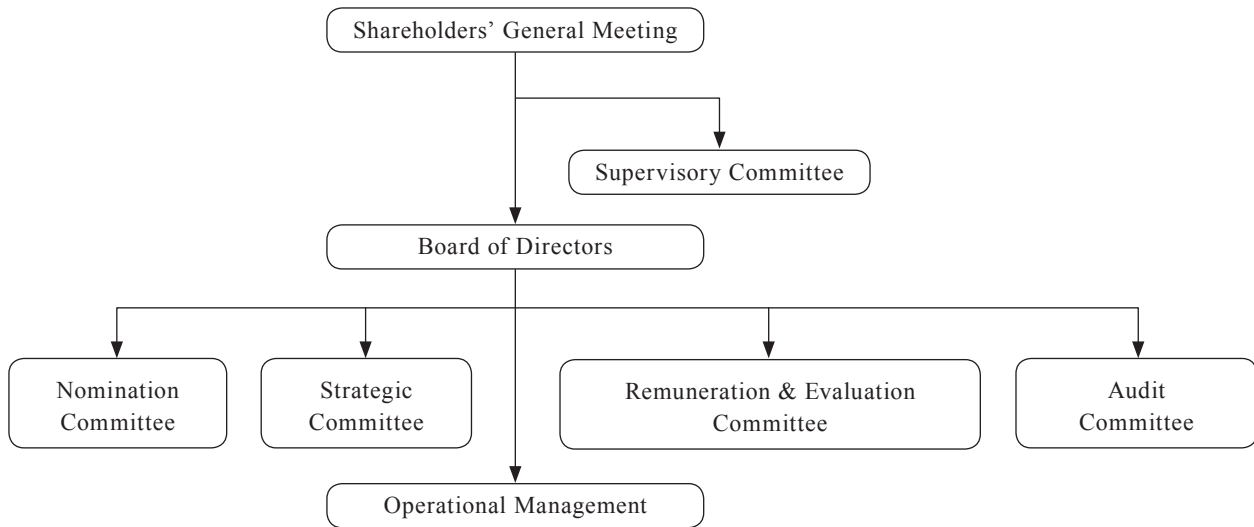
- (1) Originally, the direction of our research and development work was further confirmed to be: fortify research of foundation technologies and track our competitors and internationally advanced technologies, complemented by other measures such as self-development, introduction and assimilation and external cooperation, with the objective of mastering the most advanced technologies on the international and domestic levels. On the one hand, we will devote to closely tracking the demand and construct a reliable, enhanced and consistent technological platform to rapidly implement the transition to technology-oriented products, in order to enable the launch of new products with competitive edge timely. In view of the specific products, for refrigerators, we will continue to increase our investment in energy-saving technologies to further consolidate and reinforce our leading position in the industry, while at the same time we will pinpoint our efforts to enhance the preservation technologies, design of product structure and industrial outlook design. For the air-conditioner products, we will also continue to increase our investment in energy-saving technologies to further consolidate and reinforce our leadership in the industry, while at the same time we will look into the details such as adoption of new models of heat exchanger to improve comfort, reliability and compatibility. On the other hand, we will implement a series of measures including reinforcing talent training and introduction, strengthening the introduction of external technologies and external cooperation, as well as adjusting the internal research and development system, with the objective to systematically rationalize the management of the research and development section and thereby increase the research and development efficiency and enhance the quality of work. In 2008, the research and development efforts of the Company will be put more on the transformation of high technology contents, with an effective enhancement of the technological content of our products. With this actual inifination for enhancement of the current and future competitiveness of our products, we look forward to enhancing our brand image and stimulating sales with our products.
- (2) In 2008, the Company will continue to leverage on its quality advantages to maintain the establishment of the quality system, and adopt the approach of preventive management. Product quality control is further reinforced through multi-point quality control such as stringent quality inspection for external components, control of design responsibility, standardization of production site.
- (3) In order to ensure the supply of materials to satisfy the demand from the expansion of the after market, the Company will concentrate on enhancing the production capacity for its products and breaking through the production bottlenecks. On one hand, the Company will actively promote the renovation work in respect of various technologies, including the commencement of production line for large volume refrigerator sand renovation of production facilities involved in the key bottlenecks to increase the production efficiency. On the other hand, the Company will renovate the staff quarters and canteens for junior grade staff to improve the living conditions of the employees, so as to retain and attract talents and resolve the lack of labor supply.
- (4) In respect of the domestic market, the Company will continue to strengthen its marketing capabilities with the forceful construction and enhancement of the channels. Coupled with the existing network of each different product, channel exploration and innovation of marketing models will be conducted in response to the specific situation with reinforced planning.
- (5) In respect of overseas business, the Company will further enhance the structure of export products, expand the export channels, increase the proportion of high-end products, continue to consolidate the advantages of cooperation with international major brand and customers, create long-term strategic partnerships, continue to increase the scale of export, improve the profitability of export sales and facilitate the process of internationalization.
- (6) Parallel to the training of talents, the Company will make an effort to recruit external talents and project teams upon appropriate organization and planning, with a special focus on the recruitment of high-end talents from overseas to resolve the major conflicts such as business, lack of technical supervisors, structural shortage of talents from the fundamentals, in order to accommodate to the needs of enterprise upgrade and internationalization.
- (7) The Company will aggressively proceed with the assets reorganization with the Hisense Group to increase the operating scale of the Company’s principal products, enhance the Company’s assets quality and further promote its financial structure, with the objective of upgrading the Company’s competitiveness.

Management Discussion And Analysis

Looking ahead, the Company faces both opportunities and challenges. The management will ride on the trend of the industry and leverage on its own advantages, striving for improvements and enhancement. The management of the Company is of the view that the Company has successfully go through the most difficult situation and is on the track of sustained healthy development. Backed by the enthusiastic expectation and sincere trust of its shareholders and the relentless efforts of all our staff, the Company will do its best to accomplish the operating objectives for 2008.

Corporate Governance Report

The following diagram sets forth the Company's corporate governance structure:



(a) Corporate Governance Practices

Good corporate governance practices are essential for a company listed in two regions. The Board acknowledges its responsibility to ensure the formulation of good Corporate governance practices and procedures, which shall be prepared strictly in compliance with the Code on Corporate Governance Practices (the "Code"). To the best knowledge of the Company and as far as information is available, the Company has complied with the Code during the Reporting Period.

In order to improve the corporate governance and management of the Company and supervise the Company's operation, the Company established the nomination committee and strategy committee during Reporting Period, and established the corresponding work rules, details of which set out in "Corporate Governance Structure Introduction" on page 14 of the report.

In 2007, a total of 17 person comprising directors, supervisors and senior management of the Company participated in the training course for directors, supervisors and senior management of listed companies held by the China Securities Regulatory Commission. In addition, pursuant to the requirements of the "Circular of Securities Regulatory Commission on Conduct of Projects to Strengthen Corporate Governance of Listed Companies", the Company seriously commenced the works of corporate governance and self-inspection and established the "Report of Self-inspection and Reform Proposal in respect of corporate governance". According to the reform proposal, the Company has formulated the "System of Internal Control" and "Management Method of Connected Transaction", amended the "Management Method of Information Disclosure", and arranged related staff to undergo specialized training in the "Management Method of Connected Transaction" and the "Management Method of Information Disclosure" so as to achieve thorough understanding and enable implementation. In addition, in response to the actual situation, the Company has amended the "Articles of Association" and "Management Method of Information Disclosure", respectively, in addition to formulating various internal management systems including the "System of Reception and Promotion", the "Management System for Shares of the Company Held by the Directors, Supervisors and Senior Management and the Changes" and "System of Internal Control".

(b) Securities Transactions by Directors

The Company has adopted all the requirements of the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") as set out in Appendix 10 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") as its code for securities transaction by Directors. Having made specific enquiries, Mr. Tang Ye Guo, Mr. Wang Shi Lei, Ms. Yu Shu Min, Mr. Lin Lan, Mr. Liu Chun Xin, Mr. Zhang Sheng Ping, Mr. Lu Qing and Mr. Cheung Yui Kai, the directors of the sixth Board of the Company, have confirmed that they have fully complied with the Model Code throughout the Reporting Period. In addition, Mr. Yang Yun Duo and Mr. Xiao Jian Lin, acted as former Directors of the sixth Board of the Company and the newly appointed Director Mr. Zhang Ming have also confirmed that they have fully complied with the Model Code during their terms as the Directors of the Company.

Corporate Governance Report

Governance Structure

(c) The Board of Directors

The sixth Board of the Company was elected and established at the extraordinary general meeting of the Company. The Board comprised 9 directors from 4 January 2007 to 20 June 2007, where Mr. Tang Ye Guo, Mr. Yang Yun Duo, Mr. Wang Shi Lei, Ms. Yu Shu Min, Mr. Lin Lan and Mr. Xiao Jian Lin were appointed as executive directors, and Mr. Zhang Sheng Ping, Mr. Lu Qing and Mr. Cheung Yui Kai, Warren were appointed as independent non-executive directors. As a result of the resignation of Mr. Xiao Jian Lin on 21 June 2007, the Board comprised 8 directors from 21 June 2007 to 7 August 2007. While Ms. Liu Chun Xin was elected as the director of the sixth Board of the Company on 8 August 2007, the Board comprised 9 directors. As a result of the resignation of Mr. Yang Yun Duo on 26 February 2008, the Board comprised 8 directors from 26 February 2008 to 15 April 2008. While Mr. Zhang Ming was elected as the director of the sixth Board of the Company on 16 April 2008, the Board comprised 9 directors until now. Members of the Board have different background, possessing rich experience in fields such as science and technology, corporate management and finance and accounting. The biographies and roles of the aforesaid Directors are set out on pages 18 to 21 of this annual report.

The primary duties of the Board include: convening shareholders' general meetings and reporting its work at the shareholders' general meetings, and exercising its decision-making rights according to powers and duties conferred by the shareholders' general meetings in aspects including strategic development plans for the Company, establishment of the management structure, investment and financing plans, financial monitoring, disposal of material assets, material transactions and human resources. The Board is responsible for formulating the Company's overall strategy and annual business and budget plans, and ensuring that its production operations are properly planned, approved, implemented and monitored. In addition, the Board is in charge of the appointment of members of the operational management and also the supervision and evaluation of the performance of the operational management. The Board have established, within its structure, four special committees including the audit committee, the remuneration and evaluation committee, the nomination committee and the strategic committee.

Directors are also responsible for supervising and preparing accounts for each fiscal period to ensure that such accounts truly and fairly reflect the Company's business conditions, results and cash flow performance during that period. The operational management of the Company provides proper explanations and sufficient information to the Board so as to enable it to make an informed assessment of the financial information and other information submitted to it for approval. In preparing the accounts ended 31 December 2007, the Directors:

- selected and consistently applied the appropriate accounting policies;
- approved early adoption of all standards as set out in Hong Kong Financial Reporting Standards that are consistent with International Financial Reporting Standards; and
- made prudent and reasonable judgments and estimates and prepared the accounts on an ongoing concern basis.

The operational management of the Company is responsible for implementing decisions made by the Board and making its own decisions on the Company's business operation matters within the scope of delegation by the Board, which includes: carrying out the Company's production and operation management, organizing and implementing the Company's annual operation and investment plans, preparing the proposal of the Company's internal control structure, formulating the Company's basic management system and setting up the Company's basic regulations. Meanwhile, as requested by the Board, the Operational Management reports to the Board the conclusion of the Company's major contracts, status of the performance of the contract, use of capital and the Company's profit and loss conditions and ensures that such information is true and complete.

The Company has formulated relevant rules in accordance with the Listing Rules and related regulations to remind the Directors that they shall perform their obligations, including making disclosures to the regulatory authorities on a timely basis about their interests, potential conflicts of interests and changes in their personal information details, etc. Each Director also undertakes that he has sufficient energy and time to handle the Company's affairs.

Corporate Governance Report

In 2007, the sixth Board of the Company convened 23 meetings to discuss the Company's operating results, overall strategies, investment schemes as well as operating and financial performance. The Directors took part in the meetings in person and by proxy, and the attendance is detailed in the following table:

The attendance of the Sixth Board Meeting				
Name	Number of Meetings Should Be Attended for the Year	Number of Attendance in Person	Number of Attendance by proxy	Attendance Rate for the Year
Mr. Tang Ye Guo (<i>Chairman</i>)	23	23	0	100%
Mr. Yang Yun Duo	23	21	0	91.30%
Mr. Wang Shi Lei	23	23	0	100%
Ms. Yu Shu Min	23	17	0	73.91%
Mr. Lin Lan	23	19	0	82.61%
Ms. Liu Chun Xin	12	12	0	100%
Mr. Zhang Sheng Ping	23	22	0	95.65%
Mr. Lu Qing	23	23	0	100%
Mr. Cheung Yui Kai, Warren	23	23	0	100%
Mr. Xiao Jian Lin	9	9	0	100%

As at the date of this annual report, the Directors of the sixth Board of the Company confirmed that the following significant uncertainties will affect the operation and development of the Company:

- As at the date of this report, the Group has taken legal actions against Guangdong Greencool and its related companies (the "Greencool Companies") for damaging the interests of the Group, and has claimed compensation for the losses. Although some cases have been judged, as the Group is not completely aware of the assets and liabilities situation of the Greencool Companies, there are risks that such claims, even if awarded, may be unable to enforce. Therefore, the outcome of such claims may have a material impact on the assets of the Company.
- Due to the fact that the reorganization of assets of the Company has not been approved By CSRC, as at the date of this report, the matter of industry competition between the Company, Hisense Air-conditioner, the controlling shareholder, and Hisense Group, the actual controller, is not yet eliminated. The Company will continue discussing and promoting the reorganization of assets and related issues with Hisense Air-conditioner in order to solve the matter of industry competition with the controlling shareholder.

(d) Chairman and President

The Chairman and president of the Company are appointed by the Board. The persons appointed as the Chairman and president of the Company during the Reporting Period herein are as follows:

POST	Chairman	President
NAME	Mr. Tang Ye Guo	Mr. Wang Shi Lei
TERM OF OFFICE	26 June 2006 to the date of this Report	13 November 2006 to the date of this Report

The Chairman is responsible for presiding general meetings convening and presiding Board meetings, ensuring proper function of the Board and that the Board will review and discuss all the significant issues in a timely and effective manner, reviewing the results of implementation of the Board's resolutions as well as performing duties of the legal representative of the Company. The president is in charge of the production, operation and management of the Company, and is responsible for organizing resources for implementing the Board's resolutions, the Company's annual operation and investment plans and making decisions on other issues within the authorities granted to him by the Board.

(e) Independent Non-Executive Directors

The sixth Board of the Company consists of three independent non-executive Directors, which account for one-third of the total number of Directors. The independent non-executive Directors of the Company are in compliance with Rules 3.10 (1), (2) and 3.13 of the Listing Rules and are assumed by persons who are independent of any Directors, Supervisors, chief executives and substantial shareholders (as defined in the Listing Rules) or such individuals or corporate bodies without any connection thereto (the “independent third party”). The Company has received confirmation of independence from each of the independent non-executive Directors. The term of office of all independent non-executive directors are from 26 June 2006 to 26 June 2009.

(f) Remuneration and Evaluation Committee

The Company has established the remuneration and evaluation committee of the sixth Board, the members of which consist of Mr. Tang Ye Guo and Ms. Yu Shu Min, being executive directors, and Mr. Zhang Sheng Ping, Mr. Lu Qing, and Mr. Cheung Yui Kai, being independent non-executive directors. Mr. Zhang Sheng Ping acts as the chairman of the committee.

The main functions performed by the remuneration and evaluation committee are set out below:

- (1) studying the standard for assessment of Directors and members of the senior management of the Company, conducting the assessment and putting forward suggestions; studying and examining the remuneration policy and plan for the Directors and members of the senior management of the Company;
- (2) carrying out the responsibility delegated from the Board, i.e. to determine the specific remuneration packages for all executive Directors and members of the senior management of the Company, including non-pecuniary interest, pension rights and compensation payments, including any compensation payable for loss or termination of their office or appointment, and make recommendations of the remuneration of independent non-executive Directors to the Board;
- (3) the remuneration and evaluation committee should consider factors such as:

The salaries paid by similar companies, the time commitment and responsibilities of the Directors, the employment conditions of other positions in the Group and the desirability of performance-based remuneration;

Reviewing and approving performance-based remuneration by reference to corporate goals and objectives passed by the Board from time to time;

Reviewing and approving the compensation payable to executive Directors and members of the senior management of the Company in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms; and

Reviewing and approving compensation arrangements relating to dismissal or removal of Directors for misconduct to ensure that such arrangements are determined in accordance with the relevant contractual terms.

The remuneration and evaluation committee shall have access to professional advice if considered necessary.

The Directors and senior management of the Company cannot decide on their own remuneration.

The aim of the remuneration policies adopted by the Remuneration and Evaluation Committee is to attract and retain Directors and members of the senior management who faithfully and diligently discharge their duties and are loyal to their responsibilities and, accordingly, is extremely important to the Company.

The remuneration and evaluation committee of the sixth Board of the Company held two meetings during the Reporting Period. All members of the remuneration and evaluation committee attended the meeting. Members of the Remuneration and Evaluation Committee confirmed that the remunerations of directors, supervisors and members of the senior management are complied with the remuneration evaluation system setup by the Company during Reporting Period. In addition, the Remuneration and Evaluation Committee established the “Working Rules of the Remuneration and Evaluation Committee”.

Corporate Governance Report

Details of the remuneration of the Directors and the members of the senior management of the Company for the year ended 31 December 2007 are set out on pages 17 of this annual report.

(g) Director Nomination

The sixth Board of the Company has established the nomination committee on 15 October 2007. The nomination committee comprises of 3 independent directors, the members of which include, Mr. Tang Ye Guo and Mr. Wang Shi Lei, both of them are executive directors and Mr. Zhang Sheng Ping, Mr. Lu Qing, Mr. Cheung Yui Kai, Warren all of them are independent non-executive directors. Mr. Zhang Sheng Ping acts as the Chairman of the committee.

The nomination committee is a special body under the Board, it is primarily responsible for the candidate selection, selection requirements and procedures of selection in connection to the Company's directors and members of the senior management and make proposals.

The nomination committee comprises of five directors, which include three independent directors who are nominated by the Chairman of the Board, more than half of the independent non-executive directors or more than one third of the directors, and are elected by the Board. The Nomination Committee shall have one chairman (convener) who should be an independent non-executive director in charge of presiding over the committee. The convener shall be voted among the commissioners, and submitted to the Board for approval. The term of office of the commissioners of nomination committee is consistent with those of which he served in the Board, during which if some commissioners don't serve as directors of the Company, his/her commissioner's qualification will lapse automatically, and the vacancy should be filled with the person elected by the Board in accordance with the requirements. The human resources department of the Company would assist the Nomination Committee with the daily work such as selection and nomination of the right person.

The Nomination Committee of the sixth Board of the Company held one meeting during the Reporting Period. All members of the Nomination Committee attended the meeting. The work rules of the Nomination Committee were considered and passed at the meeting.

(h) Strategic Committee

The sixth Board of the Company established the strategic committee on 15 October 2007. During the Reporting Period, the strategic committee of the sixth Board comprised of Mr. Tang Ye Guo, Mr. Yang Yun Duo, Mr. Wang Shi Lei, Ms. Yu Shu Min and Mr. Lin Lan, and Mr. Tang Ye Guo was the Chairman.

The strategic committee of the Board is a special body subject to the Board, mainly in charge of making research and giving advice with respect to long-term development strategy and significant investment decision-making of the Company.

The strategic committee comprises of five directors, among which 3 are independent non-executive directors who are nominated by the Chairman, more than half of the independent directors or one third of all the directors, and are elected by the Board. The committee shall have one chairman (convener), which was occupied by the Chairman of the Company. The term of office of the strategic committee is consistent with those of the Board, and the commissioner can be re-elected upon his/her expiration. During which if some commissioners don't served as a director of the Company, his/her commissioner's qualification will lapse automatically, and the vacancy should be filled with the person elected by the Board in accordance with the requirements.

The strategic committee of the sixth Board of the Company held one meeting during the Reporting Period. All the commissioners were present, and at which the "Working Rules of the Strategic Committee" were approved.

(i) Audit Committee

The Board holds ultimate responsibility for the Company's internal control system. To achieve the best corporate governance practice, the Company has set up an audit committee to review the efficiency of the relevant systems. The audit committee is a specialized structure established under the Board, and is responsible for the communication, supervision and inspection of the internal and external audit work of the Company. The audit committee reports to the Board and its proposals will be submitted to the Board for approval.

Corporate Governance Report

The Audit Committee mainly performs the following duties under the delegation by the Board:

1. To propose engaging or changing the external auditing organization;
2. To supervise the internal audit system of the Company and its implementation;
3. To be responsible for the communication between the internal auditor and external auditor;
4. To review the financial information of the Company and its disclosure;
5. To review the internal control system of the Company;
6. Other matters authorized by the board of directors.

The members of the sixth audit committee of the Company include independent non-executive directors, Mr. Zhang Sheng Ping, Mr. Lu Qing and Mr. Cheung Yui Kai, Warren and Mr. Lu Qing is the chairman of the committee.

In 2007, the audit committee of the sixth Board of the Company held two meetings. All members of the audit committee attended both meetings. At the first meeting, it was deliberated and decided to establish the auditing department as the daily agency of the auditing committee of the sixth Board of the Company, and engaged Ms. Dai Hui Jiao as the director of the auditing department. At the second meeting, the “Working Rules of the Auditing Committee” were approved. All discussions and resolutions passed at the meetings were recorded in accordance with relevant rules and filed after being reviewed and signed by all members of the audit committee.

In 2007, the audit committee of the sixth Board of the Company accomplished the following tasks:

1. Reviewed the annual and interim financial reports, together with the advices provided by the auditors and the responses of the members of the senior management of the Company;
2. Made recommendations on the Company’s internal control and the Company’s control over its subsidiaries;
3. Reviewed the accounting policies adopted by the Group and the matters concerning accounting practice;
4. Reviewed the connected transactions of the Company and ensured that the connected transactions are in compliance with the principles of fairness, impartiality and transparency with sufficient protection to the minority shareholders; and
5. Made recommendations on significant events of the Company and reminded the members of the senior management of the Company of the relevant risks.

Internal Control and Internal Audit

To strengthen the internal management of the Company, realize the objectives of corporate governance, enhance the quality of information disclosure, ensure the safety of the Company’s operation and management and the reliability of the financial information, prevent and resolve different types of risks, and improve the operation efficiency and profitability, the Company has established the “System of Internal Control” which mainly standardizes the controlling procedures in respect of the environment, business, accounting system, electronic information system, information circulation, internal audit and other areas.

During the Reporting Period, the Company has improved the internal control system for reviewing the Company’s financial, operating and supervisory controlling procedures to protect shareholders’ interests and the Company’s assets. The Audit Committee is responsible for reviewing the effectiveness of the internal control systems. The Company has established the internal audit department for implementing the internal control functions to inspect, monitor and assess the disclosure of financial information, operations and internal control activities of the Company and its subsidiaries on a regular basis and as needed, based on the potential risks and the importance of internal control systems for different businesses operations. In particular, during the Reporting Period, the audit department was confirmed to be the apparatus for daily routine works to the audit committee of the sixth session of the Board. The audit department performed audit

on the Company's financial income and expenditure, financial budget, final financial account, quality and quantity of assets, results of operation and other related economic activities. It also reviewed and supervised the economic activities and significant economic contracts of the Company and its subsidiaries, including the proposal, budget, final account and delivery for use upon completion, sourcing of materials, sales of products, invitation of work tender, external investment, and risk control of infrastructure and major technical reform and renovation projects; appraised the integrity, rationality, effectiveness and risk control of the Company and its subsidiaries; evaluated the operational risks of the related businesses of the Company; and supervised and assessed the operation results and the related economic activities of the Company and its subsidiaries. These have effectively promoted and fortified the operation and management of the Company and enhanced the operation results.

The sixth Board reviewed the effectiveness of the internal control system of the Company during the Reporting Period, and during the review, the Board observed that the system has an ideal improvement as compared to last year. And the Company has established an appropriate internal control system based on the actual situations, and prepared a comprehensive summary and explanation as to the goal, the details, the modes and the duties of the internal control system.

(j) General Meeting

As the highest authority of the Company, the general meeting exercises its rights under the laws to make decisions on significant events of the Company. The Company establishes and maintains different communication channels with its shareholders through the publication of annual reports, interim reports and press releases.

In 2007, the Company convened an annual general meeting ("AGM") and four extraordinary general meetings ("EGM"). The shareholding held by shareholders who attended the AGM and the EGM represented 9.38%; 35.43%; 33.16%; 32.94% and 33.17% respectively, of all the issued shares of the Company.

(k) Supervisory Committee

The Supervisory Committee was established in accordance with the PRC laws. It independently performs its supervisory duties under the laws to protect the legal interests of shareholders, the Company and its staff. It also investigates the Company's finances as required by the articles of association of the Company, and supervises misconducts of the Directors and members of senior management of the Company who disobey the laws and administrative regulations in performing their duties. The sixth Supervisory Committee of the Company is composed of two shareholders' representatives, namely Mr. Guo Qing Cun and Mr. Zhou Zhao Li and one staff representative of the Company, Mr. Liu Zhan Cheng, with Mr. Guo Qing Cun acting as the chairman of the committee. Details of the above-mentioned supervisors' biographies are set out on pages 20 of this annual report.

Details relating to the work performed by and the meetings convened by the Supervisory Committee of the Company in 2007 are set out on page 50-51 of this Annual Report.

(l) Auditors' Remuneration

In 2007, the Company appointed Shenzhen Dahua Tiancheng Certified Public Accountants and BDO McCabe Lo Limited as the Company's domestic and foreign auditors, respectively. Their remuneration was determined by the Board as authorised in the general meeting. The Company agreed to pay a total of approximately RMB4.8 million (The exchange rate of Hong Kong dollars against RMB is 1:0.95), for the remuneration of its domestic and foreign auditors for the provision of review and audit services on the financial statements for the six months ended 30 June 2007 and year ended 31 December 2007.

Profiles of Directors, Supervisors & Members of the Senior Management

1. PARTICULARS OF THE CHANGES IN SHARES HELD BY DIRECTORS, SUPERVISORS AND MEMBERS OF THE SENIOR MANAGEMENT AND THE REMUNERATION.

Name	Current Position	Sex	Age	Term of Office	No. of shares held at the beginning of the year	No. of shares held at the end of the year	Total remuneration (including taxes) received from the Company during the Reporting Period (RMB ten thousand)	Received in shareholder's entities or other related companies
Tang Ye Guo	Director, Chairman	Male	45	2006.6.26-2009.6.26	0	0	80	No
Wang Shi Lei	Director President	Male	40	2007.1.4-2009.6.26 2006.11.13-2009.11.13	0	0	64	No
Yu Shu Min	Director	Female	57	2006.6.26-2009.6.26	0	0	0	Yes
Lin Lan	Director	Male	50	2006.6.26-2009.6.26	0	0	0	Yes
Liu Chun Xin	Director Vice President	Female	39	2007.8.8-2009.6.26 2006.10.31-2009.10.31	0	0	40	No
Zhang Ming	Vice President Director	Male	37	2006.6.26-2009.6.26 2008.4.16-2009.6.26	0	0	24	No
Zhang Sheng Ping	Independent Non-Executive Director	Male	43	2006.6.26-2009.6.26	0	0	6	No
Lu Qing	Independent Non-Executive Director	Male	41	2006.6.26-2009.6.26	0	0	6	No
Cheung Yui Kai, Warren	Independent Non-Executive Director	Male	40	2006.6.26-2009.6.26	0	0	23.28	No
Guo Qing Cun	Supervisor	Male	54	2006.12.5-2009.6.26	0	0	0	Yes
Zhou Zhao Li	Supervisor	Male	39	2006.12.5-2009.6.26	0	0	0	Yes
Liu Zhan Cheng	Supervisor	Male	30	2006.6.23-2009.6.26	0	0	20	No
Su Yu Tao	Vice President	Male	42	2007.3.23-2010.3.23	0	0	29	No
Wang Jiu Cun	Vice President	Female	54	2006.6.26-2009.6.26	13,800	15,456	40.30	No
Jia Shao Qian	Vice President	Male	36	2007.1.30-2010.1.30	0	0	21.33	No
Shi Yong Chang	Vice President	Male	48	2008.1.30-2011.1.30	0	0	0	No
Zhou Xiao Tian	Vice President	Male	49	2008.3.3-2011.3.3	0	0	0	No
Zhong Liang	Secretary to the Board	Male	30	2006.9.7 to date	0	0	16.05	No
Yang Yun Duo	Former Director, Former Vice Chairman	Male	52	2007.1.4-2008.2.26	0	0	56	No
Xiao Jian Lin	Former Director	Male	40	2006.6.26-2007.6.21	0	0	0	Yes
Dai Zu Mian	Former Company Secretary	Male	31	2006.9.7-2007.8.28	0	0	42.48	No
Total	—	—	—	—	13,800	15,456	468.44	—

Note:

- Except for the non-executive directors, no directors of the Company have received director's fees from the Company. For certain directors who are also members of the senior management of the Company, their remunerations as members of the senior management of the Company are determined by the remuneration and evaluation committee and the Board. Among these directors, the remunerations received by the Directors, namely Tang Ye Guo, Yang Yun Duo, Wang Shi Lei and Liu Chun Xin, were the remunerations for serving as the Chairman of the Board or the senior management of the Company during the Reporting Period. Details of the remunerations (including taxes) received by the existing directors, supervisors and members of the senior management from the Company during the Reporting Period are set out in the table above.
- The exchange rate of Hong Kong dollars against RMB is 1:0.97.

Profiles of Directors, Supervisors & Members of the Senior Management

- (3) Except for Ms. Wang Jiu Cun (Vice President) holding shares of the Company, none of other Directors, supervisors and members of the senior managements hold any share of the Company. Particulars of the changes of the shares of the Company held by Ms. Wang Jiu Cun during the Reporting Period are set out as follows:

Name	Position	No. of shares held at the beginning of the year	No. of shares increased during the Reporting Period	No. of shares decreased during the Reporting Period	No. of shares held at the end of the period	Reasons for the change
Wang Jiu Cun	Vice President	13,800	1,656	—	15,456	As a result of the share reform, 1,656 shares were granted during the Reporting Period.

2. BIOGRAPHIES DETAILS OF THE CURRENT DIRECTORS, SUPERVISORS AND MEMBERS OF THE SENIOR MANAGEMENT

Directors:

Mr. Tang Ye Guo, has served as the deputy general manager and chief accountant of 青島海信電器股份有限公司 (Qingdao Hisense Electric Co., Ltd.) (“Hisense Electrical”); the general manager of Hisense Electrical from November 1999 to August 2003; an assistant to the president and later the vice president of Hisense Group Company Limited (“Hisense Group”), and the general manager and chairman of the board of directors of Qingdao Hisense Air-Conditioning Company Limited (“Hisense Air-Conditioner”) and a director of Hisense Electrical from August 2003 to September 2005. Mr. Tang was appointed as the chairman of the board of directors of Hisense Air-Conditioner and a director of Hisense Electrical and the president of Hisense Kelon Electrical Holdings Company Limited from September 2005 to June 2006. He has been acted as the chairman of the board of directors of Hisense Air-Conditioner and the chairman of the board of directors of Hisense Kelon Electrical Holdings Company Limited since June 2006.

Mr. Wang Shi Lei, has been served as the deputy general manager and general manager of Hisense Air-Conditioner; the standing deputy general manager of Qingdao Hisense Communications Company Limited from January 2002 to June 2002; the general manager of Hisense (Beijing) Electrical Appliances Company Limited from July 2002 to December 2003; the general manager of Hisense Electrical from January 2004 to January 2006; and the general manager of Qingdao Hisense Network Technology Company Limited from February 2006 to November 2006. Since November 2006, Mr. Wang has acted as the president of Hisense Kelon Electrical Holdings Company Limited. Starting from January 2007, he has also served as a director of Hisense Kelon Electrical Holdings Company Limited.

Ms. Yu Shu Min, has successively served as the deputy to the party committee secretary of 青島市電子儀錶工業總公司 (Qingdao Municipal Electronics Instrument Industrial Corporation), the deputy secretary to the party committee and the vice president of Hisense Group, the general manager of Hisense Electrical, the chief executive officer of Hisense Group and the chairman of the board of directors of Hisense Electrical. Ms. Yu has been the vice chairman of the board of directors and the president of Hisense Group and the chairman of the board of directors of Hisense Electrical since July 2001. She was appointed as an executive director of Hisense Kelon Electrical Holdings Company Limited since June 2006.

Mr. Lin Lan, was the manager of the Power System Software Development Department of 西門子諮詢公司 (Siemens, now known as “AMEC Limited” in the UK) between 1995 and 1998, and was responsible for the development and management of the simulative systems for dynamic power systems, large scale paper manufacturing plants and large chemical plants. From 1998 to May 2002, Mr. Lin has worked as a senior project manager and senior engineer for GE 動力系統公司 (GE Power Systems Company), responsible for the advancement of equipment and technologies of several thermal power plants and atomic power plants. Mr. Lin was appointed as the vice president of Hisense Kelon Electrical Holdings Company Limited from September 2002 to June 2006. Since July 2006, he has served as the vice president of Hisense Group. He was appointed as an executive director of Hisense Kelon Electrical Holdings Company Limited in June 2006.

Profiles of Directors, Supervisors & Members of the Senior Management

Ms. Liu Chun Xin, a certified public accountant, a registered tax advisor and an economist. She served as project manager, department manager and senior manager in various accountant firms for years. She has years of experience in auditing and consultation on financial management and has been responsible for conducting the planning on the corporate restructuring, restructuring and conversion, asset and capital verification and provision of management consultation for corporate restructuring several enterprises. She has served a vice chairman of Hisense Kelon Electrical Holdings Company Limited since November 2006. From August 2007, she has been a director of Hisense Kelon Electrical Holdings Company Limited.

Mr. Zhang Ming, joined Hisense in July 1995, has successively served as the deputy head of capital operation department, the deputy chief officer of the strategy study department and chief officer of the strategy development department of Hisense Group from August 1998 to February 2004. Mr. Zhang has been appointed as the chief supervisor at the capital operation department of Hisense Group from February 2004 to June 2006. He has worked as a director of Hisense Kelon Electrical Holdings Company from 26 June 2006 to 13 November 2006; From 28 June 2006 to date, Mr. Zhang has been working in Huayi Compressor Holdings Company Limited as a director. He was appointed as a vice president of Hisense Kelon Electrical Holdings Company Limited since June 2006. Since August 2007, he has served as a director of Qingdao Hisense Air-Conditioning, and on 16 April 2008, he has appointed to be a director of Hisense Kelon Electrical Holdings Company Limited.

Mr. Zhang Sheng Ping, graduated from Shandong University with a master's degree of Science, from Nankai University with a doctorate in Economics, and from Peking University with a doctorate in finance. From July 1987 to June 2000, he has worked as a teaching fellow, lecturer and an associate professor at the School of Economics of Shandong University. Since August 2002, he has been an associate professor at the Guanghua School of Management of Peking University. He was appointed as an independent non-executive director of Hisense Kelon Electrical Holdings Company Limited since June 2006.

Mr. Lu Qing, a postgraduate of the master's degree in finance, senior accountant, a partner of 中和正信會計師事務所 (Zhonghe ZhengXin Certified Public Accountants), and a council member of 山東省會計學會 (Shandong Provincial Accounting Society). He is also a registered accountant on securities and futures and a certified assets valuer in the PRC. Since 2003 to date, he has been a partner of 中和正信會計師事務所 (Zhonghe ZhengXin Certified Public Accountants). In January 2002, he completed the training course for independent directors of listed companies jointly organized by the CSRC and Fudan University. He was appointed as an independent non-executive director of Hisense Kelon Electrical Holdings Company Limited since June 2006.

Mr. Cheung Yui Kai, Warren, a Hong Kong permanent resident, graduated from the University of Southern Queensland in Australia with a bachelor's degree in business and is a CPA in Hong Kong. He has over 16 years of investment banking experiences in the Asian Pacific Region. He has worked successively as a senior manager in 渣打(亞洲)有限公司 (Standard Chartered (Asia) Limited) ; a senior manager in 渣打澳洲有限公司 (Standard Chartered Australia Limited) and a vice director in 荷銀融資亞洲有限公司 (ABN AMRO Corporate Finance (Asia) Limited). From 2000 to 2003, he served as a director in 軟庫金(香港)有限公司(SB1 E2-Capital (HK) Limited). From 2003 to 2005, he served as a director in 凱利融資有限公司 (Hercules Capital Limited). Since 2005, he has been appointed as a managing director in 寶來資本(亞洲)有限公司 (Polaris Capital (Asia) Limited). He was appointed as an independent non-executive director of Hisense Kelon Electrical Holdings Company Limited in June 2006.

Former Directors:

Mr. Yang Yun Duo, has been served as a manager of the sales company and the deputy general manager of Hisense Electrical, the deputy general manager of Hisense Air-Conditioner from August 2002 to July 2003; the general manager and the secretary to the party committee of 青島海銷信營銷有限公司 (Qingdao Hisense Marketing Company Limited) from July 2003 to January 2004; an assistant to the president of Hisense Group and the general manager and the secretary to the party committee of Qingdao Hisense Marketing Company Limited from January 2004 to January 2006. Mr. Yang served as the general manager of the domestic marketing Company of Hisense Kelon Electrical Holdings Company and was appointed as the vice chairman of the Board of the Company for a term from January 2007 to February 2008.

Profiles of Directors, Supervisors & Members of the Senior Management

Mr. Xiao Jian Lin, has been worked as deputy controller of the Operation Center, director, assistant to the president, and chief officer of the Finance Centre of Hisense Group; director, vice president and head of the accounting and finance department of Hisense Group from February 2002 to September 2005. Mr. Xiao has been a director of Hisense Group since September 2005, and as a director of Hisense Air-Conditioner from September 2005 to August 2007; He also acted as vice president of Hisense Kelon Electrical Holdings Company Limited from September 2005 to November 2006. He was appointed as director of Hisense Kelon Electrical Holdings Company Limited from June 2006 to June 2007.

Supervisors:

Mr. Guo Qing Cun, has been a lecturer, associate professor and professor of Shandong University and held various positions at the university, including the deputy president of the Institute of Science, the a assistant to the head of School of Management and the chief officer of the Research Centre of Techology Law and Intellectual Property Right, In 1998, he was nominated as a Professional Techology Talent in Shandong Province. from 1987 to 2002. Mr. Guo was a visiting scholar of the faculty of law at Peking University in 1995. After attaining the qualification of practicing lawyer in the national examination in 1986, he acted as part-time lawyer in the legal advisory office in Shandong and Wenhan Law Firm (文翰律師事務所). From 2002 to date, he served as an assistant to the president and vice president at Hisense Group. He also took the position of standing deputy head of Hisense Research Institute (海信研究院) of Shandong University. He was appointed as a supervisor of Hisense Kelon Electrical Holdings Company Limited on 5 December 2006.

Mr. Zhou Zhao Li, graduated from Jinan University with a master's degree in business administration in June 2000. Mr. Zhou is an economist. He had been working in the Foshan Branch of the China Construction Bank and the Foshan business department of Everbright Securities Company Limited. Mr. Zhou has been working in the Guangzhou office of China Finance Asset Management Corporation from March 2002 to September 2007. From October 2007 to date, Mr. Zhou has been working in the business Department of China Finance Securities Limited (華融證券股份有限公司). He was appointed as a supervisor of Hisense Kelon Electrical Holdings Company Limited on 5 December 2006.

Mr. Liu Zhan Cheng, graduated from Zhongnan University of Finance (中南財經大學) in 1999. He has been working in Kelon after graduation. He was the deputy manager and manager of the accounting division of the finance department of Hisense Kelon Electrical Holdings Company Limited from April 2001 to November 2002. He was the deputy department head of the operations and management department of Guangdong Kelon Refrigerator/Freezer Co., Ltd (廣東冰箱/冷柜有限公司). from November 2002 to September 2003 and was the department head of the material control department of Guangdong Kelon Refrigerator Freezer Co., Ltd and the purchase department International marketing department of the Company from September 2003 to September 2005. From September 2005 to May 2006, Mr. Liu was the department head of the supply department and the assistant to general manager and the deputy general manager of Guangdong Kelon Air-Conditioner Co., Ltd from September 2005 to March 2008. He has been the assistant to general manager and department head of the purchase department of Hisense RonShen (Guangdong) Refrigerator Co., Ltd. from February 2008 to date. He has served as supervisor of Hisense Kelon Electrical Holdings Company Limited from June 2006 to date.

Senior Management Members:

Mr. Su Yu Tao, has worked successively as a deputy manager of the supply department and property management department of Hisense Electrical; and the deputy manager and manager of the production planning department and purchase department of Hisense Air-Conditioner. He has worked as an assistant to general manager; deputy general manager and general manager of Hisense Air-Conditioner from October 2000 to January 2004; general manager of 海信(北京)電器有限公司 (Hisense (Beijing) Electrical Appliances Company Limited) from February 2004 to September 2005. Mr. Su was a director of Hisense Air-Conditioner from September 2005 to date and a vice president of Hisense Kelon Electrical Holdings Company Limited from September 2005 to 26 June 2006. He was a director and president of Hisense Kelon Electrical Holdings Company Limited from 26 June 2006 to 14 November 2006. He was appointed as a vice president of Hisense Kelon Electrical Holdings Company Limited since March 2007.

Profiles of Directors, Supervisors & Members of the Senior Management

Ms. Wang Jiu Cun, has worked as the deputy division head and division head of manufacturing division and department, the head of the marketing management department and the sale department of Guangdong Kelon Air-Conditioner Co., Ltd., She was the chief of the first plant and the chief of the second plant of Guangdong Kelon Air-Conditioner Co., Ltd. from 2000 to July 2002, and the deputy general manager of production and the head of the production department of Guangdong Kelon Air-Conditioner Co., Ltd. from August 2002 to August 2004. From September 2004 to 17 May 2006, Ms. Wang worked as deputy general manager of production, and from 18 May 2006 to June 2006, an assistant to president of Hisense Kelon Electrical Holdings Company Limited. She has served as the vice president of Hisense Kelon Electrical Holdings Company Limited since June 2006.

Mr. Jia Shao Qian, he has served as a legal adviser in the corporate legal department of Hisense Group, supervisor of public relations in the president office of Hisense Group from January 2000 to January 2003, deputy manager of president office of Hisense Group from January 2003 to July 2005 and manager of president office of Hisense Group Company from July 2005 to January 2007. He serves as chairman of the supervisory committee of Hisense Electric Company Limited from June 2006 to date. He has served as vice president of Hisense Kelon Electrical Holdings Company Limited since January 2007.

Mr. Shi Yong Chang, graduated with a college degree, he has worked as vice factory manager of Hisense Electrical and the manager of office of Saling Company of Hisense Electrical at Guiyang and the deputy general manager of Hisense (Beijing) Electrical CO.,LTD (海信(北京) 電器有限公司) and the deputy general manager of Hisense Agent Co., Ltd (青島海信營銷公司). From September 2005 to November 2006, has acted as the vice president of Hisense Kelon Electrical Holdings Company Limited. From November 2006 to January 2008, has acted as the general manager of Qingdao Hisense Communication Company Limited. Since 30 January 2008, has acted as the vice president of Hisense Kelon Electrical Holdings Company Limited.

Mr. Zhou Xiao Tian, doctor of engineering of Universität Karlsruhe in Germany, German. Mr. Zhou has been the project engineer of refrigerant department, production line planning engineer, refrigerant system engineer, inspection center manager of BSH Bosch Siemens Hausgeraete GmbH. From January 2005 to August 2006, he has been the general manager of the PRC technical center of BSH Bosch Siemens Hausgeraete GmbH, PRC region and technical manager of Chuzhou refrigerator factory; from September 2006 to February 2008, he has been the department head of the refrigerant department and refrigerant system department of BSH Bosch Siemens Hausgeraete GmbH. Since 3 March 2008, Mr.Zhou has been the vice-president of Hisense Kelon Electrical Holdings Company Limited.

Mr. Zhong Liang, a postgraduate of master's degree, has acted as the representative of the Company on securities affairs since he joined the Company in 2001. He has acted as the deputy manager and manager of the office of secretary to the board of directors and head of the securities department of the Company since July 2006. He has acted as the secretary to the board of directors of Hisense Kelon Electrical Holdings Company Limited since September 2006.

Mr. Dai Zu Mian, graduated with a bachelor's degree in economics, an associate member of the Association of Chartered Certified Accountants in the United Kingdom and is a certified public accountant in the PRC. He had held various positions in internationally renowned accounting firms in the past including PricewaterhouseCoopers Zhongtian Certified Public Accountants. He was appointed as the company secretary and qualified accountant of Hisense Kelon Electrical Holdings Company Limited from September 2006 to August 2007.

Report of the Directors

PRINCIPAL ACTIVITIES

The Group is principally engaged in development and manufacture of refrigerators, air-conditioners, freezers, domestic appliances and the relevant fittings and domestic and overseas sales of these products and provision of after-sale services.

FINAL DIVIDENDS

The Group recorded a profit of RMB203,657,000 for the year 2007. The Board resolved not to pay any dividend for the year 2007 and not to capitalize any reserve funds (no dividend was paid by the Group for the year ended 31 December 2006).

LIQUIDITY AND SOURCES OF FUNDS

Net cash used in operating activities was approximately RMB10,418,000 (2006: net cash generated from operating activities amounted to approximately RMB883,996,000) for the year ended 31 December 2007.

As at 31 December 2007, the Company had bank deposits and cash (including pledged bank balances) amounting to approximately RMB146,528,000 (2006: RMB390,504,000), and bank loans amounting to approximately RMB1,310,972,000 (2006: RMB1,556,702,000).

Total capital expenditures for the year 2007 amounted to approximately RMB374,143,000 (2006: RMB142,652,000).

HUMAN RESOURCES AND EMPLOYEES' REMUNERATION

As at 31 December 2007, the Group had approximately 22,141 employees, mainly comprising 2,484 technical staff, 6,234 sales representatives, 415 financial staff, 741 administrative staff and 12,267 production staff. Four of the Company's employees hold a doctorate degree while 80 and 1,826 Company's employees hold master's degree and bachelor's degree, respectively. There were 382 employees with an title at mid-level or above. In addition, the Company currently has 31 resigned or retired staff. For the year ended 31 December 2007, the staff costs of the Company amounted to approximately RMB630,870,000 (2006: RMB538,066,000).

CHARGES ON THE GROUP'S FIXED ASSETS

As at 31 December 2007, the Group's property, plant and equipment (including leasehold land held for own use) and investment properties of approximately RMB694,080,000 (2006 (restated): RMB817,907,000) were pledged as security for the Group's bank borrowings.

EXPOSURE TO EXCHANGE RATE FLUCTUATION

Since the majority of the Group's purchase and overseas sales during the Reporting Period were denominated in foreign currency, the Group had certain extent of exposure to exchange rate fluctuation; The Group has used financial instruments such as discounted export bills, import/export documentary bills, and hedge risk.

PUBLIC FLOAT

As at 24 April 2008, based on publicly available information and to the knowledge of the Directors, 25% or above of the total issued share capital of the Company are held by the public. Therefore, the public float of the Company satisfies the requirements stipulated under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules").

MATERIAL LITIGATIONS

As at 24 April 2008, the Company and its subsidiaries were involved in 23 litigations which, in each cases the target claim amount was more than RMB 10 million the total target claim amount was RMB922,009,100.

Report of the Directors

AUDIT COMMITTEE

The sixth session of the audit committee of the Company has reviewed the announcement and report of the final results of the Company for the year ended 31 December 2007.

CAPITAL EXPENDITURE

The Group expects that the capital expenditure for 2008 will be approximately RMB233,130,000.

DEPOSIT IN TRUST

As at 31 December 2007, the Company did not own any deposit in trust in any financial institution in the PRC. All of the Company's deposits are placed with the commercial banks in the PRC and Hong Kong.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

As at 31 December 2007, the Group had long-term bank borrowings of RMB Nil (2006: RMB Nil) and cash and cash equivalents of RMB76,395,000 (2006: RMB142,247,000), of which over 53.34% are denominated in Renminbi.

RATIO OF TOTAL ASSETS TO TOTAL LIABILITIES

As at 31 December 2007, the ratio of total assets to total liabilities of the Group was 87.50%.

INDEPENDENCE OF THE INDEPENDENT NON-EXECUTIVE DIRECTORS

The sixth session of the Board has received the written confirmations from all of the independent non-executive Directors in respect of their independence in accordance with the requirements under Rule 3.13 of the Listing Rules, and considers that all the existing independent non-executive Directors are in compliance with the relevant requirements under Rule 3.13 of the Listing Rules and are still independent persons.

PROPERTY, PLANT AND EQUIPMENT

During the year, the Group spent approximately RMB309,021,000 on acquisition of property, plant and equipment. The details of the movements in property, plant and equipment of the Group during the year are set out in note 16 to the financial statements.

PENSION SCHEMES

Details of the Group's pension schemes for the year ended 31 December 2007 are set out in note 40 to the financial statements.

RESERVES

Details of movements in reserves of the Group and the Company during the year 2007 are set out in statement of changes in equity on page 61 of the financial statements.

DISTRIBUTABLE RESERVES

There was no distributable reserves of the Company as at 31 December 2007.

Report of the Directors

SERVICE CONTRACTS AND INTERESTS IN CONTRACTS OF DIRECTORS AND SUPERVISORS

No service contract has been entered into with any Directors and supervisors of the sixth Board. The Directors and supervisors of the sixth Board of the Company have not directly or indirectly held any material interests in any material contracts during 2007.

INDEPENDENT NON-EXECUTIVE DIRECTORS' REVIEWS OF CONTINUING CONNECTED TRANSACTIONS

The independent non-executive Directors of the sixth Board have reviewed the continuing connected transactions of the Company for the year 2007 and confirmed that these transactions were conducted in the ordinary course of business of the Company on normal commercial terms which were fair and reasonable and in the interests of the shareholders of the Company as a whole.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in the Listing Rules as its code for securities transactions by the Directors. After specific enquiries made to the Directors of the sixth session of the Board, Mr. Tang Ye Guo, Mr. Wang Shi Lei, Ms. Yu Shu Min, Mr. Lin Lan, Ms. Liu Chun Xin, Mr. Zhang Sheng Ping, Mr. Lu Qing and Mr. Cheung Yui Kai, Warren and to the former directors, Mr. Yang Yun Duo and Mr. Xiao Jian Lin and to the newly appointed Director, Mr. Zhang Ming, they all confirmed that they had complied with the Model Code during their terms of office.

SHARE CAPITAL STRUCTURE

As at 31 December 2007, the share capital structure of the Company was as follows:

Class of shares	Number of shares	Percentage to the total issued share capital(%)
A Shares	532,416,755	53.67%
H Shares	459,589,808	46.33%
Total	992,006,563	100%

Report of the Directors

TOP TEN/SUBSTANTIAL SHAREHOLDERS

(1) As at 31 December 2007, the Company has a total of 41,399 shareholders, of which the top ten/substantial shareholders were as follows:

Shareholdings of the top ten shareholders

Name of Shareholder	Nature of Shareholder	Percentage to the total issued shares capital of the Company	Percentage to the issued class shares of the Company	No. of Shares Held	No. of Shares Held Subject to Selling Restrictions	No. of Pledged or Frozen Shares
Qingdao Hisense Air-conditioning Company Limited	Domestic Non-stated-owned Person	24.08%	70.69%	238,872,074	238,872,074	0
The Hongkong and Shanghai Banking Corporation Limited	Foreign Shareholder	9.35%	20.19%	92,781,829	0	Unknown
Foshan City Shunde District Economic Consultancy Company	Domestic Non-stated-owned Person	6.92%	20.32%	68,666,667	68,666,667	0
Shenyin Wanguo Securities (H.K.) Limited	Foreign Shareholder	5.55%	11.99%	55,097,000	0	Unknown
Bank of China (Hong Kong) Limited	Foreign Shareholder	4.92%	10.62%	48,794,000	0	Unknown
Guotai Junan Securities (Hong Kong) Limited	Foreign Shareholder	4.12%	8.90%	40,920,000	0	Unknown
First Shanghai Securities Limited	Foreign Shareholder	2.61%	5.63%	25,860,000	0	Unknown
Hang Seng Securities Limited	Foreign Shareholder	2.04%	4.40%	20,235,000	0	Unknown
Standard Chartered Bank (HK) Ltd.	Foreign Shareholder	1.12%	2.42%	11,109,500	0	Unknown
BOCI Securities Limited	Foreign Shareholder	0.83%	1.79%	8,216,000	0	Unknown

Notes: As at 31 December 2007, as shown in the register of substantial shareholders kept according to Section 336 of the Securities and Futures Ordinance under the Laws of Hong Kong (the "SFO"), the top seven shareholders among the above top 10 shareholders above maintained short positions in the issued share capital of the Company:

Report of the Directors

Shareholdings of top ten tradable without selling restrictions Shareholders

Name of Shareholder	Number of Tradable Shares without Selling Restrictions	Class of Shares
The Hongkong and Shanghai Banking Corporation Limited	92,781,829	H Shares
Shenyin Wanguo Securities (H.K.) Limited	55,097,000	H Shares
Bank of China (Hong Kong) Limited	48,794,000	H Shares
Guotai Junan Securities (Hong Kong) Limited	40,920,000	H Shares
First Shanghai Securities Limited	25,860,000	H Shares
Hang Seng Securities Limited	20,235,000	H Shares
Standard Chartered Bank (HK) Ltd.	11,109,500	H Shares
BOCI Securities Limited	8,216,000	H Shares
Sun Hung Kai Investment Services LTD.	7,983,000	H Shares
Chiyu Banking Corporation LTD.	6,868,000	H Shares

Notes: The Company is not aware whether any one of the top ten holders of listed shares is connected with each other or any one of them is a party acting in concert with any of the other nine shareholders as defined in Administrative Measures for Information Disclosure of the Shareholders of Listed Companies.

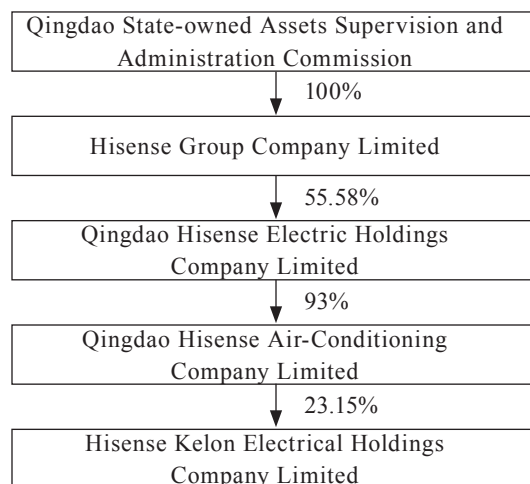
(2) Profile of the controlling shareholder of the Company

- (1) Qingdao Hisense Air-Conditioning Co., Ltd., the controlling shareholder of the Company, was incorporated on 17 November 1995 with a registered capital of RMB674.79 million. Its registered address is Changsha Road, Hi-tech Industrial Zone, Qingdao, the PRC and the legal representative is Mr. Tang Ye Guo. It is primarily engaged in researching and manufacturing of air-conditioners, injection moulds and provision of after-sale repairing services for its products.
- (2) The beneficial controller of the Company is Hisense Group Company Limited which was incorporated at No. 17, Donghai West Road, Shinan, Qingdao in August 1979. Zhou Houjian is the legal representative of Hisense Group, a wholly state-owned enterprise with a registered capital of RMB806,170,000. Its scope of business are: the entrusted operation of state-owned assets; the manufacture and sale of, and provision of after-sale services for TV sets, VCD and DVD players, audio sets, broadcasting appliances, air-conditioners, electronic computers, telephones, communication products, internet products and electronic products; software development and internet services; consultation advices for technical development; the self-operated import and export business; foreign economic and technical cooperation; self-operated ownership transaction, brokerage and information services; the engagement in the property and casualty business as approved by the China Insurance Regulatory Commission; and the in industrial travel (expiring on 6 June 2008).

The final beneficial controller of the Company is the State-owned Assets Supervision and Administration Commission of Qingdao People's Government.

Report of the Directors

(3) Relationship between the Company and its Beneficial Controlling Shareholders:



(4) During the Reporting Period, there was no change in the controlling shareholder of the Company.

(5) No shareholders of the Company own more than 10% (including 10%) of its shares.

INTERESTS OF DIRECTORS, SUPERVISORS AND CHIEF EXECUTIVES IN THE SHARES

As at 31 December 2007, none of the members of the sixth Board, supervisors and the chief executive of the Company and any of their associates held any interests or short positions in any shares, underlying shares and debentures of the Company and any of its associated corporations, as recorded in the register maintained by the Company pursuant to Section 352 of the SFO.

MAJOR CUSTOMERS AND SUPPLIERS

For the year ended 31 December 2007, the aggregate amount of the Company's purchases from the top five suppliers was RMB 894 million, representing 12.88% of total purchase amount of the Company for the year and the aggregate sales amount of the top five customers was RMB1,588 million, representing 19.08% of total sales amount of the Company for the year. As at 31 December 2007, none of the Directors, their associates or shareholders of the Company, who, to the knowledge of the Company, hold 5% or more of the shares in the Company, have any interest in the above suppliers or customers.

PURCHASE, SALE OR REDEMPTION OF SHARES

For the year ended 31 December 2007, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed shares.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Articles of Association of the Company.

TAX RELIEF AND EXEMPTION

The Company is not aware of any particulars of tax relief and exemption available to shareholders by reason of their holding of the Company's H shares.

AUDITORS

The reappointment of Shenzhen Dahua Tiancheng Certified Public Accountants and BDO McCabe Lo Limited as the Company's local and foreign auditors respectively was reviewed and approved by the 2006 AGM of the Company.

Note: Supplementary information as required by The Stock Exchange of Hong Kong Limited in relation to the Company's A share annual results announcement (prepared in accordance with PRC GAAP)

Report of the Directors

I. INVESTMENTS OF THE COMPANY DURING THE REPORTING PERIOD

1. During the Reporting Period, the Company did not raise any capital and no capital raised during any prior period was used during the Reporting Period.
2. Material Investment excluding rising of capital during the Reporting Period
 - (1) As at the end of the Reporting Period, the equity transfer procedures in relation to the transfer of the 30% equity interest of Chengdu Kelon from Chengdu Engine (Group) Company Limited to the Company was completed. The Company is now holding 100% of the equity interest of Chengdu Kelon.
 - (2) During the Reporting Period, the Company has invested the sum of RMB1,500,000 to establish Chengdu Hisense Refrigerator Co., Ltd. with Guangdong Pearl River Electric Refrigerator Company Limited, a wholly owned subsidiary of the Company.

II. THE AUDITOR'S REPORT WAS ISSUED BY SHENZHEN DAHUA TIANCHENG CERTIFIED PUBLIC ACCOUNTANTS FOR THE COMPANY CONTAINING QUALIFIED OPINION. THE BOARD EXPLAINED THE MATTERS RELATING TO THE QUALIFIED AUDITORS' OPINION IN DETAIL AS FOLLOWS:

Reserved Matter 1: “As described in Notes 6.4, 6.6, 11 and 15 to the financial statements of the annual report of A share, a series of related parties’ transactions and unusual cash flows occurred between the Company and its former largest shareholder, Guangdong Greencool Enterprise Development Limited and its related parties (the “Greencool Companies”) during the period from October 2001 to July 2005. In addition, the Greencool Companies, through certain specified third party companies such as Tianjin Lixin Commercial Trading Development Company Limited, involved in a series of unusual cash flows with the Company in the same period. Such transactions and unusual cash flows as well as the suspected fund embezzlement have been reported to the Company, and are pending for judgment. Your Company received Civil Judgment (Fo Zhong Fa Min Er Chu Zi No. 93 and 94 (2006)) from the Guangdong Province Foshan Intermediate Court (hereafter abbreviated “Foshan Intermediate Court”) on 10 September 2007 and Civil Judgment (Fo Zhong Fa Min Er Chu Zi No. 153, 154, 175, 181, 182, 185 and 186 (2006)) from the Guangdong Province Foshan Intermediate Court on 31 March 2008, which stated that Foshan Intermediate Court has made first trial judgment on the nine cases in respect of the litigation initiated by your Company against the Greencool Companies and the case of specified third party companies in favour of your Company. The counterparty of the above nine litigations appealed from the judgment and the case is currently under hearing. As at 31 December 2007, the balance of the accounts receivables of the Company from the Greencool Companies and the above specified third party companies amounted to RMB651 million. The Company has made a provision of RMB364 million in respect of the accounts receivables from Greencool Companies and the above specified third party companies. We were unable to adopt appropriate audit procedures to obtain sufficient and appropriate audit evidence to ascertain whether the estimated provision for bad debts is reasonable and the assessment and calculation of the receivables is reasonable.

Explanation:

As the Company and its former single largest shareholder, Guangdong Greencool Enterprise Development Company Limited, and its related parties or through its third party companies had a series of related parties’ transactions and irregular cash inflow/outflow during the period from 2001 to 2005. The aforesaid transactions, irregular cash inflow/outflow and suspected funds embezzlement have been formally investigated by relevant authorities. As at 31 December 2007 the balance of the accounts receivables of the Company from Greencool Companies and the aforesaid specified third party companies amounted to RMB651,000,000.

Report of the Directors

The Company has estimated, based on the available information about the cases at present, the recoverable amount of accounts receivables due from Greencool Companies and specified third party companies, meanwhile the Company has made a provision of RMB364 million. The bases of the estimate include: the information regarding the properties of Greencool Companies sealed and frozen by the Court as applied by the Company, and the initial analysis report on the aforesaid fund embezzlement prepared by the lawyer of the Company. As analyzed by the lawyer, the properties of Greencool Companies available for settlement amounted to approximately RMB1,000,000,000, and the total claim amount against Greencool Companies by the creditors to the court amounted to approximately RMB2,400,000,000. The amount claimed by the Company for the fund embezzlement of Greencool Companies amounted to RMB792,000,000. There is possibility that the credit balance be settled based on the proportion of property to the debts. Based on the estimated settlement proportion, and that the case is still in the progress, the court has not yet acknowledged the amount of the Company's claim of the debts, the Board of the Company estimated the recoverable amount and made a provision of RMB364,000,000 for bad debts.

Meanwhile, the law firm to this case declared that, apart from the case handled by them, they cannot guarantee the accuracy of the information and the data related to other relevant cases nor the results of those cases. Further, whether the relevant subsidiaries of the Company are qualified to participate in the property appropriation of Greencool Companies is dependent on the decision of the Court.

The Board considers that the provision for bad debts is an accounting estimate, The handling method of this accounts receivable does not contravene any relevant requirements of the Accounting System for Business Enterprises. Although the Guangdong Province Foshan Intermediate Court has made first trial judgment on the nine cases in respect of the litigation initiated by the Company against the Greencool Companies, the counterparty has lodged an appeal, and the abovementioned judgment is therefore not yet effective. The Board is of the view that: as there is no material difference for the degree of judgment for the recoverability of this receivable between 2007 and 2006, this qualified opinion will not affect the fairness in the preparation of the statement of profit of the Company in 2007.

After the court has made its judgment and the settlement proportion, the Company will, pursuant to the determined recoverable proportion, adjust retrospectively the 2005 financial statements (balance sheet and income statement), and the relevant items in the balance sheet as at 31 December 2006 and 31 December 2007. The Company has taken measures to sequester the properties of Greencool Companies which are available for settlement. The Company will also pay attention to the progress of the case and make its best efforts to ensure its rights as a creditor.

III. OTHER DISCLOSEABLE MATTERS

(I) Material litigations and arbitrations of the Company

1. General status of the litigations

As of the date of this report, the Company and its subsidiaries were involved in 153 litigations with a total claim amount of RMB980,410,400, US\$13,750,719.19 and involving land of 125,266.26 square metres.

Among the aforementioned litigations involving the Company and its subsidiaries, the Company and its subsidiaries acted as plaintiffs in 29 cases with a total claim amount of RMB922,454,200 and as defendants in 124 cases involving an amount of RMB57,956,200, US\$13,750,719.19 and land of 125,266.26 square metres.

Among the aforementioned litigations involving the Company and its subsidiaries, there are 23 litigations and arbitrations as disclosed above involving an amount exceeding RMB10,000,000 each (with a total claim amount of RMB922,009,100, US\$13,750,719.19), 130 litigations with a claim amount less than RMB10,000,000 each (with a total claim amount of RMB58,401,300 and land of 125,266.26 square metres).

Report of the Directors

2. Additional new litigations

From 1 January 2007 to the date of this report, the Company and its subsidiaries were involved in 159 new litigations (of which 38 litigations are closed cases with a total claim amount of RMB59,455,900) with a total claim amount of RMB204,719,400. The Company and its subsidiaries acted as plaintiff in 14 cases (of which 6 litigations as disclosed above are closed case with a total claim amount of RMB29,175,100) with a total claim amount of RMB152,004,300. The Company and its subsidiaries acted as defendants in 145 cases (of which 32 litigations are closed cases with a total claim amount of RMB30,280,800) with a total claim amount of RMB52,715,100.

Among the aforementioned new litigations involving the Company and its subsidiaries, there are 4 litigations and arbitrations as disclosed above involving an amount exceeding RMB10,000,000 each (with a total claim amount of RMB147,192,000), 155 litigations with a claim amount less than RMB10,000,000 each (with a total claim amount of RMB57,527,400).

Background information on new litigations involving target claim amount over RMB10,000,000:

(in ten thousand RMB)

No.	Name of case	Date of Prosecution	Target Claim Amount	Background information of the case	Progress of the Case
1	Litigation initiated by Ronshen Refrigerator against Xi'an Kelon	8 June 2007	9,998.41	The Company claimed against the defendant for the repayment of the loan of RMB89.1841 million and the related interest amounting to RMB10.8 million.	Ronshen Refrigerator received Civil Judgment (Fo Zhong Fa Li Bao Zi No. 241 (2007)) and the summon from the Intermediate People's Court of Foshan City on 22 June 2007, which stated that, as applied by Ronshen Refrigerator, on 13 June, 2007, Foshan Intermediate Court issued an order of freezing the bank deposit of Xi'an Kelon amounting to RMB89,000,000 or sealing up and distraining its assets of such equivalent amount. The trial of this case has been postponed.
2	Litigation initiated by the Company against Zhejiang Hangxiao Ganggou Holdings Company Limited ("Hangxiao Ganggou")	28 March 2007	1,154.70	The Company alleged that Hangxiao Ganggou failed to complete the construction works according to the terms of the contract and has to pay default compensation	On 21 November 2007, a judgment on first trial was made in the Intermediate People's Court of Foshan City as follows: dismiss the litigation claim of the Company, and the Company shall be liable for case acceptance fee of RMB67,745. The Company lodged an appeal on receiving the judgment. On 30 January 2008, the case was heard together with the case against the Company by Hangxiao Ganggou in Higher Court of Guangdong, and is now pending for judgment.

Report of the Directors

No.	Name of case	Date of Prosecution	Target Claim Amount	Background information of the case	Progress of the Case
3	Litigation initiated by Guangzhou Mei Kou Jia Food Company Limited (廣州美口佳食品有限公司) against Ronshen Freezer	9 April 2007	1,000.00	The plaintiff filed the litigation alleging that the freezers sold by Kelon failed to meet the requirements stipulated in the contract.	Intermediate People's Court of Foshan City issued a letter of civil conciliation on 14 September 2007.
4	Litigation initiated by the Company against Shangqiu Kelon	21 June 2007	2,566.09	The Company claimed against the defendant for the repayment of the loan of RMB21,590,900, the related interest amounting to RMB4,070,000 and to assume the litigation costs of the case.	Intermediate People's Court of Foshan City made a judgment on 13 December 2007: Shangqiu Kelon to repay all loan amounting to RMB21,590,867.88 and related interest to the Company, and the litigation costs of RMB17,510 and RMB157,594 shall be assumed by the Company and Shangqiu Kelon respectively.

3. The status of completed litigations

From 1 January 2007 to the date of this report, the Company and its subsidiaries were involved in 59 closed litigations with a total claim amount of RMB340,900,000.

The Company and its subsidiaries acted as plaintiffs in 9 cases with a total claim amount of RMB216,421,400 and as defendants in 50 cases involving an amount of RMB124,778,600.

Among the aforementioned closed cases involving the Company and its subsidiaries, there are 6 litigations involving an amount exceeding RMB10,000,000 each (with a total claim amount of RMB290,755,200), 53 litigations with a claim amount less than RMB10,000,000 each (with a total claim amount of RMB22,532,900).

Background information on litigations involving target claim amount over RMB10,000,000:

(in ten thousand RMB)

No.	Name of case	Date of Prosecution	Target Claim Amount	Background Information of the Case	Progress of the Case
1	Litigation initiated by Guangzhou Mei Kou Jia Food Company Limited (廣州美口佳食品有限公司) against Ronshen Freezer	9 April 2007	1,000.00	The plaintiff filed the litigation alleging that the freezers sold by the Company failed to meet the requirements stipulated in the contract.	Intermediate People's Court of Foshan City issued a letter of civil conciliation on 14 September 2007. Ronshen Freezer had provided the freezers according to the contract and the plaintiff shall pay according to the contract.

Report of the Directors

No.	Name of case	Date of Prosecution	Target Claim Amount	Background Information of the Case	Progress of the Case
2	Litigation initiated by the Company against Shangqiu Kelon	21 June 2007	2,566.09	The Company claimed against the defendant for the repayment of the loan of RMB21,590,900, the related interest amounting to RMB4,070,000 and to assume the litigation costs of the case.	Intermediate People's Court of Foshan City made a judgment on 13 December 2007: Shangqiu Kelon to repay all loan amounting to RMB21,590,867.88 and related interest to the Company, and the litigation costs of RMB17,510 and RMB157,594 shall be assumed by the Company and Shangqiu Kelon respectively. The related assets of Shangqiu Kelon have been frozen, but have not been executed yet.
3	Litigation initiated by Jilin City Commercial Bank Jiangbei Branch against Jilin Kelon and the Company	8 December 2006	1,805.79	The Plaintiff claimed for principal and related interest.	On 15 May 2007, It was judged by the Court that the Company did not need to bear any responsibility.
4	Litigation against Jiangxi Kelon and Kaifeng Kelon Air-Conditioner Co., Ltd. ("Kaifeng Kelon") by Kaifeng Economic Technology Development (Group) Company in relation to joint venture contract	30 July 2005	2,716.00	The plaintiff applied for a pre-trial security order from the court to seize properties worth of RMB18,000,000 of Jiangxi Kelon and Kaifeng Kelon. The plaintiff applied for a security order from the court during the trial and the court ordered to seize properties worth of RMB9,160,000 of Jiangxi Kelon and Kaifeng Kelon.	On 27 August 2007, Henan Province Kaifeng Economic Technology Development (Group) Company (河南省開封經濟技術開發(集團)公司) and Jiangxi Kelon signed an Equity Transfer Agreement, pursuant to which, Jiangxi Kelon transferred all the shareholdings held in Kaifeng Kelon to Henan Province Kaifeng Economic Technology Development (Group) Company, and the case was closed (please see the announcement published by the Company on 31 October 2007 for details).

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No.	Name of case	Date of Prosecution	Target Claim Amount	Background Information of the Case	Progress of the Case
5	Litigation against Foshan Shunde Jiegao Investments Company Limited (佛山市順德區捷高投資有限公司) by Kelon Electrical	21 August 2006	18,227.11	In respect of the dispute over the land transfer money, the Company has taken the litigation to the Higher Court of Guangdong to request an order against the counterparty to settle the transfer money of the state-owned land and the related interests incurred for the overdue amount and bear the litigation costs of the case.	The Company and the defendant, Ronggui Rural Credit Cooperative of Shunde signed a "Settlement Agreement" on 18 April 2007, the three parties agreed to dispose the subject land and use the proceeds in repayment of the debt owing by the defendant to the Company and Ronggui Rural Credit Cooperative of Shunde, (please see the announcement published by the Company on 20 April 2007 for details). The Company transferred its rights to the debt to Foshan Shunde Shunrong Investments Company Limited on 31 May 2007 (please see the announcement published by the Company on 13 June 2007).
6	Litigation initiated by China Construction Bank Corporation – Nanchang Changbei Branch against Jiangxi Kelon and the Company	2005	Outstanding amount of 2760.53	China Construction Bank Corporation – Nanchang Changbei Branch applied to the court for pre-trial security order on the basis of disputes over the loan contract and guarantee contract with target claim amount of RMB140 million. On 5 August 2005, the High Court of Jiangxi Province ordered to freeze Jiangxi Kelon's 80% shareholdings in Shangqiu Kelon. With various negotiations between the parties, so far, Jiangxi Kelon has repaid the Plaintiff full amount. The plaintiff is now in the process of withdrawing his claim in High Court of Jiangxi Province.	Jiangxi Kelon has repaid the amount and the plaintiff is in the process of withdrawing the claim.

4. *Progress of material litigations involving target claim amount over RMB10,000,000 that were carried forward from prior years and which have not been closed*

Report of the Directors

(in ten thousand RMB)

Litigation involving Greencool Companies and the specified third parties

No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
1	Litigation initiated by Kelon Air-Conditioner against Guangdong Greencool, Gu Chu Jun and Jiangxi Kesheng Industry and Trading Company Limited ("Jiangxi Kesheng")	Guangdong Greencool, Gu Chu Jun and Jiangxi Kesheng	1,863.00	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the Company that, on 20 February 2005, it infringed the legal interests of the plaintiff by making use of the name of Jiangxi Kesheng so as to avoid the regulatory restrictions on connected transaction and misappropriated RMB18.63 million of the plaintiff	The hearing was commenced in Intermediate People's Court of Foshan City on 27 June 2007. The case is now pending for judgment.
2	Litigation initiated by Jiangxi Kelon Industrial Development Co., Ltd. ("Jiangxi Kelon") against Guangdong Greencool, Gu Chu Jun, Greencool Refrigerant (China) Company Limited ("Tianjin Greencool"), Hainan Greencool Environmental Protection Engineering Co., Ltd. ("Hainan Greencool") and Jinan San Ai Fu Petrochemical Co., Ltd. ("Jinan San Ai Fu")	Guangdong Greencool, Gu Chu Jun, Tianjin Greencool, Hainan Greencool and Jinan San Ai Fu	8,160.00	On 20 January 2005, under the authorisation of Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company in such a that, on 20 January 2005, it made use the name of Jinan San Ai Fu to enter into a sale and purchase contract with Tianjin Greencool and misappropriated RMB81.60 million of the plaintiff	The hearing was commenced in Intermediate People's Court of Foshan City on 14 June 2007. The case is now pending for judgment.
3	Litigation initiated by Shenzhen Kelon Procurement Co Ltd. ("Shenzhen Kelon"), against Guangdong Greencool, Tianjin Lixin Commercial Trading Development Company Limited ("Tianjin Lixin"), Greencool Procurement Centre (Shenzhen) Co., Ltd. ("Shenzhen Greencool") and Gu Chu Jun	Guangdong Greencool, Tianjin Lixin, Shenzhen Greencool and Gu Chu Jun	8,960.03	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the Company to procure the plaintiff to enter into a sale and purchase contract with Tianjin Lixin regarding the purchase of 12,700 tons of steel. The plaintiff made the payments by two installments to Tianjin Lixin on 26 April 2005 and 27 April 2005 respectively, and Tianjin Lixin transferred the amounts collected to Shenzhen Greencool. The plaintiff has not received any steel supply from Tianjin Lixin. Guangdong Greencool and Gu Chu Jun misused their controlling position in the Company and infringed the legal interests of the plaintiff.	The hearing was commenced in Intermediate People's Court of Foshan City on 27 June 2007. The case is now pending for judgment.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
4	Litigation initiated by Kelon Fittings against Guangdong Greencool, Tianjin Xiangrun Commercial Trading Development Company Limited (“Tianjin Xiangrun”), Shenzhen Greencool and Gu Chu Jun	Guangdong Greencool, Tianjin Xiangrun, Shenzhen Greencool and Gu Chu Jun	9,741.22	Under the authorizations by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the Company to procure the plaintiff to enter into a sale and purchase contract with Tianjin Xiangrun regarding the purchase of 8,820 tons of steel from Tianjin Xiangrun. The plaintiff made the payments by installments to Tianjin Xiangrun on 26, 27 and 28 April 2005, respectively, but the plaintiff did not receive any steel supply from Tianjin Xiangrun. Guangdong Greencool and Gu Chu Jun misused their controlling position in the Company and misappropriated RMB97.41 million of the plaintiff.	The hearing was commenced in Intermediate People’s Court of Foshan City on 27 June 2007. The case is now pending for judgment.
5	Litigation initiated by Kelon Air-Conditioner against Guangdong Greencool, Jinan San Ai Fu, Tianjin Greencool, Hainan Greencool and Gu Chu Jun	Guangdong Greencool, Jinan San Ai Fu, Tianjin Greencool, Hainan Greencool and Gu Chu Jun	4,080.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, Tianjin, taking benefits from its role as a substantial shareholder, misused its controlling position in the company to procure the plaintiff to enter into a sale and purchase contract with Jinan San Ai Fu to purchase 300 tons of environment-friendly refrigerant, and paid a price of RMB40,800,000 on 1 April 2005, but Jinan San Ai Fu failed to deliver the goods. The funds was transferred to Greencool companies. Guangdong Greencool and Mr Gu Chu Jun misused their controlling position in the Company and misappropriated RMB40.8 million of the plaintiff	The hearing was commenced in the Intermediate People’s Court of Foshan City on 13 June 2007. The case is now pending for judgment.
6	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Aike Enterprises (Tianjin) Co., Ltd. and Gu Chu Jun	Guangdong Greencool, Tianjin Greencool, Aike Enterprises (Tianjin) Co., Ltd. and Gu Chu Jun	9,000.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company and misappropriated RMB90 million of the plaintiff.	On 30 August 2007, the Intermediate People’s Court of Foshan City made the judgment for Guangdong Greencool, Gu Chu Jun, Greencool Refrigerant (China) Company Limited to pay the plaintiff an amount of RMB90,000,000; the defendant shall be liable for case acceptance fee and claim security expenses in a total of RMB91,0530 The counterparty has already lodged an appeal, the judgment is not yet effective.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
7	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Tianjin Greencool and Gu Chu Jun	Guangdong Greencool, Tianjin Greencool, Gu Chu Jun	7,500.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company and misappropriated RMB75 million of the plaintiff.	On 30 August 2007, the Intermediate People's Court of Foshan City made the judgment for Guangdong Greencool, Gu Chu Jun and Tianjin Greencool to pay the plaintiff an amount of RMB75,000,000; the defendant shall be liable for case acceptance fees and claim security expenses in a total of RMB760,530 The counterparty has already lodged an appeal, the judgment is not yet effective.
8	Litigation initiated by Yangzhou Kelon against Guangdong Greencool, Gu Chu Jun and Yangzhou Greencool Venture Capital Company Limited ("Yangzhou Greencool")	Guangdong Greencool, Gu Chu Jun and Yangzhou Greencool	4,000.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company in such a way that during the course of negotiation conducted in early 2004 by the Company with the management committee of Yangzhou Economic Development Zone (hereinafter referred to as the "Zone") with respect to the production of "Twin Door Freezers" (also named "Huge Freezers") in the Zone, Gu Chu Jun deliberately misrepresented the relationship between the Company and Greencool to the management committee of the Zone for the purpose of attracting the large-sized investment projection. As such, the finance bureau of the Zone granted the "Development Encouragement Fund" amounting to RMB40 million, that should have been paid to Yangzhou Kelon as an incentive subsidy on a "levy first and refund later" basis, to Yangzhou Greencool, a private company owned by Gu Chu Jun	The hearing was commenced in Intermediate People's Court of Foshan City on 23 November 2007 and a judgment on first trial was made on 28 January 2008 in favors of Yangzhou Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
9	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Gu Chu Jun, Jiangxi Keda Plastic Technology Company Limited (“Jiangxi Keda”) and Greencool Procurement (Shenzhen) Co., Ltd. (“Greencool Procurement”)	Guangdong Greencool, Gu Chu Jun, Jiangxi Keda and Shenzhen Greencool	1,300.00	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company, in such a way that, for the purpose of embezzlement of Jiangxi Kelon’s fund, Gu Chu Jun and certain Greencool companies made the Plaintiff transfer a total sum of RMB13 million to Jiangxi Keda on 20 May 2005 and thereafter made Jiangxi Keda transfer such fund immediately to Greencool Procurement. The four defendants failed to return such fund to the Plaintiff as at the date hereof. The transfer of such fund from the Plaintiff to Greencool Procurement was not substantiated by any genuine transaction. Guangdong Greencool and Gu Chu Jun misused their controlling position in the company and misappropriated RMB13 million of the plaintiff.	The hearing was commenced in Intermediate People’s Court of Foshan City on 23 November 2007 and a judgment on first trial was made on 28 January 2008 in favour of Jiangxi Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.
10	Litigation initiated by the Company’s Hubei Branch against Guangdong Greencool, Gu Chu Jun and Wuhan Changrong Electrical Appliance Company Limited (“Wuhan Changrong”)	Guangdong Greencool, Gu Chu Jun and Wuhan Changrong	2,984.37	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company, in such a way that, during the period from 15 December 2004 to 31 December 2004, Wuhan Changrong took delivery of a large number of air-conditioners and other goods from the Plaintiff without making any payment. The defaulted payment of RMB29,843,700 has not yet been settled. The said connected transaction was conducted without going through normal internal approval procedures of the Company and the Plaintiff and no announcement has been issued on it. Therefore it is Guangdong Greencool and Gu Chu Jun misused their controlling position in the Company and misappropriated RMB29.8437 million of the plaintiffs.	The hearing was commenced in the Intermediate People’s Court of Foshan City on 23 November 2007. The case is now pending for judgment.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
11	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Zhuhai City Longjia Refrigerant Co., Ltd. (“Zhuhai Longjia”) and Gu Chu Jun	Guangdong Greencool, Zhuhai Longjia and Gu Chu Jun	2,860.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company to procure Jiangxi Kelon to transfer RMB11 million to the bank account of Zhuhai Longjia on 24 December 2003 and further transferred RMB17.6 million on 15 December, 2004. Such transfers of funds were not supported by any transactions and were not recorded in the Plaintiff’s accounts. Guangdong Greencool and Gu Chu Jun misused their controlling position in the Company and misappropriated RMB28.6 million of the plaintiffs.	Intermediate People’s Court of Foshan City has proceeded with the case on 23 November 2007 and made a judgment on first trial on 25 January 2008 in favour of Jiangxi Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.
12	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Gu Chu Jun and Zhuhai Defa Air-conditioner Fittings Company Limited (“Zhuhai Defa”)	Guangdong Greencool, Gu Chu Jun and Zhuhai Defa	2,140.00	Under the authorization by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company to procure the plaintiff to transfer RMB9 million and RMB12.40 million to the bank account of Zhuhai Defa on 24 December 2003 and on 15 December 2004 respectively. Such transfers of funds were not supported by any transactions and were not recorded in the Plaintiff’s accounts. Guangdong Greencool and Gu Chu Jun misused their controlling position in the company and misappropriated RMB21.40 million of the plaintiffs.	The hearing was commenced in Intermediate People’s Court of Foshan City on 23 November 2007 and a judgment on first trial was commenced on 25 January 2008 in favour of Jiangxi Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.
13	Litigation initiated by Jiangxi Kelon against Guangdong Greencool, Gu Chu Jun and Wuhan Changrong	Guangdong Greencool, Gu Chu Jun and Wuhan Changrong	2,000.00	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company to procure the plaintiff, to transfer RMB20 million to the bank account of Wuhan Changrong on 23 December 2003. Such transfer of funds was not supported by any transactions and was not recorded in the Plaintiff’s accounts. Guangdong Greencool and Gu Chu Jun misused their controlling position in the company and misappropriated RMB20.00 million of the plaintiff.	The hearing was commenced in Intermediate People’s Court of Foshan City on 23 November 2007 and a judgment on first trial was made on 25 January 2008 in favour of Jiangxi Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
14	Litigation initiated by the Company and its Anhui Branch against Guangdong Greencool, Gu Chu Jun and Hefei Weixi Home Appliances Co., Ltd. (“Hefei Weixi”)	Guangdong Greencool, Gu Chu Jun and Hefei Weixi	1,869.48	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the company, in such a way that, Hefei Weixi took delivery of a large number of air-conditioners and refrigerators from the Plaintiffs without making any payment during the period from 31 December 2003 to August 2005, and the defaulted payments of RMB16,075,400 and RMB2,619,400 due to the Anhui Branch and the Company, respectively, have not yet been settled. The connected transaction above was conducted without going through normal internal approval procedures of the Company and no announcement has been issued on it, therefore, it is attributable to the misuse of Guangdong Greencool and Gu Chu Jun of their controlling position in the company against the interests of the plaintiff.	The hearing was commenced in Intermediate People’s Court of Foshan City on 23 November 2007. The case is now pending for judgment.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
15	Litigation initiated by Kelon Air-Conditioner against Guangdong Greencool, Gu Chu Jun and Hainan Greencool Environmental Protection Engineering Co. Ltd. ("Hainan Greencool")	Greencool, Gu Chu Jun and Hainan Greencool	1,228.94	Under the manipulation of Guangdong Greencool and Gu Chu Jun, the plaintiff entered into a purchase and sale agreement with Hainan Greencool under which the plaintiff purchased 100 tons of Greencool refrigerant at a unit price of RMB135,000 per ton. After execution of the above agreement, the Plaintiff made a payment of RMB13,437,900 to Hainan Greencool for the refrigerant under the direction of Guangdong Greencool and Gu Chu Jun. However, according to the subsequent investigation and assessment conducted by the plaintiff, the price of the refrigerant quoted by Hainan Greencool was about 10 times the normal market price and the refrigerant under the agreement was only value at RMB1,148,500. In other words, Hainan Greencool illegally embezzled the funds of the plaintiff in the amount of RMB12,289,400 by way of connected transaction. The above connected transaction was not subject to the normal approval procedures by the Plaintiff and was not disclosed to the public. Therefore, it constitutes an embezzlement of the Plaintiff's funds by the controlling shareholder and its connected companies. Guangdong Greencool and Gu Chu Jun misused their position in the Company and acted against the interests of the plaintiff.	The hearing was commenced in Intermediate People's Court of Foshan City on 23 November 2007. The case is now pending for judgment.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
16	Litigation initiated by the Company against Guangdong Greencool, Zhuhai Greencool Refrigeration and Engineering Co., Limited (“Zhuhai Greencool”), Beijing Greencool Refrigerant Replacement Engineering Co., Limited (“Beijing Greencool”), Hainan Greencool and Gu Chu Jun	Guangdong Greencool, Zhuhai Greencool, Beijing Greencool, Hainan Greencool and Gu Chu Jun	1,375.46	<p>During the course of controlling and operating the Plaintiff, Guangdong Greencool and Gu Chu Jun forcibly integrated the businesses of Greencool Companies with those of the Company, and took control of the manpower, financial resources and materials for promoting the businesses of Greencool at the Company’s cost. Given that “Greencool Authorized Project Agent” did not make payment to Greencool Companies, Guangdong Greencool manipulated the Company to settle the above-mentioned franchise fees and the payment for purchasing refrigerants on behalf of the “Greencool Authorized Project Agent”. With respect to such payments, the Company was manipulated to pay RMB35,175,000 to Zhuhai Greencool, RMB3,960,000 to Beijing Greencool and RMB2,673,000 to Hainan Greencool. So far, there is an outstanding amount of RMB13,754,600 paid by the Company to the companies under the name of Greencool under manipulation not yet recovered. The above actions conducted by the Defendants were neither approved by the Board and the general meeting under the laws and the articles of association of the Company, nor disclosed to the public.</p>	The hearing was commenced in Intermediate People’s Court of Foshan City on 23 November 2007 and a judgment on first trial was made on 29 January 2008 in favour of the Company. But with the counterparty lodging an appeal, the judgment is not yet effective.

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No.	Name of case	Counterparty	Target claim amount	Background Information of the case	Progress of the Case
17	Litigation initiated by Kelon Guangdong Air-Conditioner against Guangdong Greencool, Gu Chu Jun and Greencool Technology Development (Shenzhen) Company Limited ("Shenzhen Greencool Technology")	Guangdong Greencool, Gu Chu Jun and Shenzhen Greencool Technology	3,200.00	From 31 March 2003 to 14 April 2003, under the manipulation of Gu Chu Jun and his Greencool Companies, the plaintiff transferred the cumulative payment to Shenzhen Greencool Technology amounted to RMB32 million, and no repayment has been made to date. As such transfer of funds was not supported by any transactions, the act of the controlling shareholder and its associated companies constitutes an embezzlement of the listed company's funds	The hearing was commenced in Intermediate People's Court of Foshan City on 23 November 2007. The case is now pending for judgment.
18	Litigation initiated by Kelon Air-Conditioner against Guangdong Greencool, Gu Chu Jun and Greencool Technology Environmental Protection Engineering (Shenzhen) Co., Ltd. ("Shenzhen Greencool Environmental")	Guangdong Greencool, Gu Chu Jun and Shenzhen Greencool Environmental	3,300.00	From 6 May 2003 to 23 June 2003, under the manipulation of Guangdong Greencool and Gu Chu Jun, Kelon Air-Conditioner transferred the cumulative amount of RMB33 million from Kelon Air-Conditioner to Shenzhen Greencool Environmental was, and no repayment has been made to date. As the funds transferred from the Plaintiff to Shenzhen Greencool Environmental were not based on any transactions, Guangdong Greencool and Gu Chu Jun misused their controlling position in the company and acted against the interest of the company.	The hearing was commenced in the Intermediate People's Court of Foshan City on 23 November 2007. The case is now pending for judgment.
19	Litigation initiated by Yangzhou Kelon against Guangdong Greencool, Yangzhou Greencool Venture Capital Company Limited and Gu Chu Jun	Guangdong Greencool, Yangzhou Greencool and Gu Chu Jun	3,500.00	Under the authorisation by Gu Chu Jun, Guangdong Greencool, taking benefits from its role as a substantial shareholder, misused its controlling position in the Company in such a way that in the course of investment in Yangzhou Kelon, Gu Chu Jun declared repeatedly to the Management Committee of the Economic Development Zone that the company was a subsidiary of Greencool and Greencool was the owner of the company during the negotiation and purchase of land. Thus, the Finance Bureau of Economic Development Zone was misled to deposit the incentive fund of RMB35 million to the bank account of Yangzhou Greencool, an associated company of Guangdong Greencool (which was a company solely owned by Gu Chu Jun), instead of Yangzhou Kelon.	The hearing was commenced in Intermediate People's Court of Foshan City on 13 June 2007 and a judgment first trial was made on 4 February 2008 in favour of Yangzhou Kelon. But with the counterparty lodging an appeal, the judgment is not yet effective.

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Other litigations

No.	Name of case	Counterparty	Target claim amount	Background information of the case	Progress of the Case
1	Litigation initiated by CNA/MC Appliance Corporation against the Company and Kelon International Incorporation	Can International. Inc./MC Appliance Corporation	USD13,750,719.19	The plaintiff alleged that it entered into a contract with the defendant on 29 December 2003 to purchase 108,108 units of MCBR1000W refrigerators, but the defendant failed to perform its obligations as set out in the contract on a timely basis and that the goods delivered were defective.	The Company has lodged a counter claim. The case is now being heard.
2	Litigation against the Company initiated by Zhejiang Hangzhou Hangxiao Ganggou Holdings Company Limited ("Hangxiao Ganggou")	Hangxiao Ganggou	1,985.30	The plaintiff alleged that it had undertaken the construction works of the Company's plain warehouse factories No. 1 and No. 2 pursuant to a construction contract with the Company. The plaintiff filed proceeding against the Company for the payment of RMB1,193,000 in construction fees and RMB17,660,000 in default penalties and the cost of legal proceedings. The Company defaulted in payment of RMB1,193,000 of construction fees. The proceeding was resumed in Intermediate People's Court of Foshan City in March 2007. Hangxiao Ganggou has amended the claim for construction fees to RMB1,170,000.	The hearing was commenced in the Intermediate People's Court of Foshan City in March 2007. The second court session was scheduled in June 2007 and the case would be tried together with the litigation against Hangxiao Ganggou by the Company. The petition against the Company by Hangxiao Ganggou was dismissed, and Hangxiao Ganggou shall be liable for the case acceptance fees. Hangxiao Ganggou lodged an appeal, and the High Court of Guangdong heard the case together with the case against Hangxiao Ganggou by the Company on 30 January 2008. The case is now pending for judgment.

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(II) Particulars on the Disposal of Assets, Takeover and Merger during the Reporting Period

1. Acquisition of assets, takeovers and mergers by the Company during the Reporting Period

No acquisition of assets, takeovers and mergers were made by the Company during the Reporting Period.

2. Disposal of assets during the Reporting Period

Unit: RMB ten thousand

Transaction counterpart	Disposed assets	Date of disposal	Net account value	Transaction price	Net profit attributable to the disposed assets from the beginning of the year to the date of disposal	Gain or loss on disposal	Percentage to total profit	Connected transaction or not	Basis of pricing	Completion of transfer of relevant assets
Haogang Commerce	Buildings and land use rights	May 2007	413.14	644.18	192.98	192.98	0.09%	No	By Tender	Yes
Hongke Trade	Buildings and land use rights	May 2007	2,264.94	2,900.00	351.81	351.81	1.73%	No	By Tender	Yes
Gateway Limited	Buildings	March 2007	6,688.40	12,329.54	5,517.84	5,517.84	27.09%	No	Tender	Yes
Fuji Elevator	Buildings	June 2007	676.38	1,635.54	865.00	865.00	4.25%	No	Tender	Yes
Chengdu Arterial Road Company	Buildings and land use rights	December 2007	6,218.12	38,006.40	23,982.21	23,982.21	117.76%	No	By Tender	Yes

Note: The disposals made by the Company during the Reporting Period mainly consisted of idle assets. It would help to optimize the assets structure of the Company. The disposals posed no impact on the continuity of operation and stability of the management of the Company.

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(III) Particulars of the Company's Material Related Parties' Transactions during the Reporting Period

1. Related parties' transactions related to ordinary operation

During the Reporting Period, the Company and Hisense Group Company Limited ("Hisense Group") and its relevant subsidiaries and Huayi Compressor Holdings Company Limited ("Huayi Compressor") and its subsidiaries, entered into certain ordinary related parties' transactions, details of which are as follows:

Unit: RMB ten thousand

Related parties	Subject of the related parties' transaction	Pricing policy	Sale of products and provision of services to related parties		Purchase of goods and receipt of services from related parties	
			Transaction amount	Percentage of total amount of similar transactions	Transaction amount	Percentage of total amount of similar transactions
Hisense Zhejiang	Purchase of air-conditioner products	Arrived at after arm's length negotiations between both parties			33,413.95	4.80%
Hisense Zhejiang	Purchase of materials for air-conditioners	Arrived at after arm's length negotiations between both parties			28.45	0.00%
Hisense Zhejiang	Sales of plastic parts of air-conditioners	Arrived at after arm's length negotiations between both parties	969.00	0.12%		
Hisense Shandong	Purchase of air-conditioner products	Arrived at after arm's length negotiations between both parties			11,456.11	1.65%
Hisense Shandong	Purchase of materials for air-conditioners	Arrived at after arm's length negotiations between both parties			636.23	0.09%
Hisense Shandong	Sales of air-conditioner finished products	Arrived at after arm's length negotiations between both parties	12,459.70	1.50%		
Hisense Shandong	Sales of components of air-conditioner	Arrived at after arm's length negotiations between both parties	566.33	0.07%		

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Related parties	Subject of the related parties' transaction	Pricing policy	Sale of products and provision of services to related parties		Purchase of goods and receipt of services from related parties	
			Transaction amount	Percentage of total amount of similar transactions	Transaction amount	Percentage of total amount of similar transactions
Hisense Nanjing	Purchase of refrigerator finished products	Arrived at after arm's length negotiations between both parties			10,312.81	1.48%
Hisense Nanjing	Purchase materials of refrigerator	Arrived at after arm's length negotiations between both parties			220.11	0.03%
Hisense Beijing	Sales of refrigerator finished products	Arrived at after arm's length negotiations between both parties	11,030.00	1.32%		
Huayi Compressor	Purchase of compressors	Arrived at after arm's length negotiations between both parties			6,299.71	0.91%
Huayi Jingzhou	Purchase of compressors	Arrived at after arm's length negotiations between both parties			430.00	0.06%
Jiaxibeila	Purchase of compressors	Arrived at after arm's length negotiations between both parties			15,450.14	2.22%
Chongqing Kelon	Sale of refrigerators	Agreed price	6,475.64	0.78%		
Total			31,500.67	3.79%	78,247.51	11.27%

Among which, the connected transactions amount for the sale of products or provision of labour service by the Company to its controlling shareholders and its subsidiaries reached RMB250,250,300.

2. Related Parties' Transaction Arising from the Transfer of Assets and Equity

During the Reporting Period, Jiangxi Kelon, a subsidiary of the Company, signed an "Equity Transfer Agreement" with 河南省開封經濟技術開發(集團)公司 (Henan Province Kaifeng Economic Technology Development (Group) Company) ("Henan Development") on 27 August 2007, pursuant to which, Jiangxi Kelon transferred its 70% equity interest in Kaifeng Kelon to Henan Development. Pursuant to the related requirements of the Listing Rules, the above transaction constituted a connection transaction (please see the announcement published by the Company on 31 October 2007 on the designated media for disclosure of information for details). As at today, the equity transfer procedures have been completed.

3. The Company does not have any other material related parties' transactions.

Report of the Directors

(IV) FUNDS EMBEZZLED FOR NON-OPERATING PURPOSES AND THE THEIR SETTLEMENT PROGRESS.

1. Amount of funds embezzled for non-operating purposes at beginning of the Reporting Period and end of the Reporting Period

Unit: RMB (in ten thousand)

Outstanding amount of funds of the Company embezzled by the former substantial shareholders, its subsidiaries, specified third parties and other related parties for non-operating purpose (in ten thousand)		Total amount recovered during this period (in ten thousand)	Settlement Method	Amount recovered	Time of Settlement
1 January 2007	31 December 2007				
68,921.99	65,514.95	3,407.04	Offsetting with the consideration for equity transfer (Note 1)	3,400	24 April 2007
			Collection of outstanding payments (Note 2)	7.04	May 2007

Note 1: On 24 April 2007, the equity transfer procedure of the 30% equity interest of Chengdu Kelon from Chengdu Engine (Group) Co., Ltd. to the Company was completed. According to the agreement, the loan of RMB34,000,000 owed by Chengdu Xinxing to Chengdu Kelon will be repaid by Chengdu Engine (Group) Co., Ltd. and set off against the consideration for the equity transfer of Chengdu Kelon.

Note 2: During the Reporting Period, the Company collected the outstanding payments of RMB70,400 from Shunde Yunlong Consultancy Service Limited.

As at the end of the Reporting Period, the total funds of the Company embezzled by the former substantial shareholder and its subsidiaries, specified third parties and other related parties for non-operating reasons amounted to RMB655.1495 million in aggregate, of which, a total amount of RMB650.6941 million was embezzled by the former substantial shareholder (Guangdong Greencool) and its associated companies (Greencool companies) and specified third parties while the remaining balance of RMB4.4554 million was embezzled by other related parties.

- 2. No additional embezzlement occurred during the Reporting Period.**
- 3. Illustration from the Board on the progress of reclaiming the matter of embezzlement by the Company during Reporting Period:**

During the Reporting Period, the Company has stepped up its effort to recover the embezzled funds pursuant to the requirements of the "Notice on Expediting the Loan Recovering Process" (Zheng Jian Gong Si Zi 2006 No. 92). By the end of 2007, the Company has recovered RMB70,400 from other related parties. The Company has initiated 20 proceedings against the embezzlers, namely Gu Chu Jun and Guangdong Greencool, as the former controlling shareholder, specified third parties and other related parties, of which 9 cases have received judgments on first trial. But with the counterparties lodging appeals, as at the reporting date, the judgments made are not yet effective.

Report of the Directors

Recovering arrangement on the funds embezzled by Greencool companies and the specified third parties and its development:

- (1) The Company has initiated 20 proceedings with the total claim amount of RMB792 million.

As at the reporting date, the Intermediate People's Court of Foshan City heard the above cases separately and judgments on first trial were made in respect of 9 cases (please see "Material Litigations and Arbitrations " of this report). But with the counterparties lodging appeals, the judgments made are not yet effective. The Company is well prepared to respond to the appeals. As at today, the proceedings against Greencool companies and the specified third parties by the Company are still in process.

- (2) Recovering Arrangement on the funds embezzled by other parties and its development

The embezzled funds amounted to RMB34,000,000 was embezzled by a related party, Chengdu Xinxing Electrical Appliance Holdings Company Limited ("Chengdu Xinxing"). During the Reporting Period, the Company entered into an agreement with Chengdu Xinxing and its major shareholder, Chengdu Engine, pursuant to which, the Company acquired 30% shares of Chengdu Kelon held by Chengdu Engine, and the amount of RMB34,000,000 of the Company occupied by Chengdu Xinxing was assumed by Chengdu Engine, and the amount was deducted from the equity transfer price to be paid by the Company, which winded up the outstanding amount of occupation by Chengdu Xinxing. With respect to the embezzlement of the funds of the Company's subsidiary Shunde Huao Electric Company Limited ("Huao") amounting to RMB4,525,800 embezzled by Shunde Yunlong Consultancy Service Company Limited ("Yunlong"), the Company has obtained certain valuable assets from Yunlong. The funds can be recovered after disposal of such assets.

The Company fully understands that the settlement of embezzled funds constitutes an irrevocable obligation of management of Company. The Company will put its greatest effort to recover the funds and reinforce communication with relevant judiciary authorities, gathering more evidence and secure the possible success in litigation to the most extent.

Report of the Directors

(V) MATERIAL CONTRACTS AND THEIR PERFORMANCE

1. External guarantee

Unit: RMB (in ten thousand)

External guarantee made by the Company (excluding guarantees to its subsidiaries)							Whether in favour of any related party (yes or no)
Guaranteed party	Date (the day of signing the agreement)	Guaranteed amount	Type of guarantee	Period of guarantee	Completion or not		
Sichuan Keming	September 2007	1500	Assurance	Six months	No		No
Total actual guaranteed amount during the Reporting Period							1500
Total balance of the actual guaranteed amount at the end of the Reporting Period							1500
Guarantees made by the Company to its subsidiaries							
Total actual guaranteed amount to subsidiaries during the Reporting Period							<u>112,706.07</u>
Total balance of the actual guaranteed amount to subsidiaries at the end of the Reporting Period							<u>28,728.35</u>
Total guarantee made by the Company (including the guarantees to subsidiaries)							
Total guaranteed amount							30,228.35
Percentage of the total guaranteed amount to absolute net assets of the Company							48.87%
Attributable to:							
Guaranteed amount provided to shareholders, actual controlling parties and their related parties							0
Guaranteed amount provided directly or indirectly to guaranteed objects with gearing ratio over 70%							<u>4,042.15</u>
Total guaranteed amount over 50% of the net asset							0
Total guarantee amount of the above three guarantees*							4,042.15

Report of the Supervisory Committee

Dear shareholders:

During the Reporting Period, the supervisory committee (the “Supervisory Committee”) of Hisense Kelon Electrical Holdings Company Limited has complied with the relevant requirements of the Company Law of the PRC, the Listing Rules of Shenzhen Stock Exchange, the Rules Governing The Listing of Securities on The Stock Exchange of Hong Kong Limited, and the articles of association of the Company, and protected the lawful interests of the Company, its staff and shareholders. We would like to report to you the work of the Supervisory Committee during 2007 in accordance with the articles of association of the Company:

I. MEETINGS OF THE SUPERVISORY COMMITTEE DURING THE REPORTING PERIOD

During the Reporting Period, the Supervisory Committee held a total of six meetings:

1. A supervisory committee meeting was held in the meeting room at the headquarter of the Company on 26 April 2007. Three of the three directors attended the meeting. The Company’s 2006 annual report and the relevant issues were approved at the meeting.
2. A supervisory committee meeting was held by way of written resolutions on 27 April 2007. Three of the three directors attended the meeting. The Company’s 2007 first quarterly report was approved at the meeting.
3. A supervisory committee meeting was held in the meeting room at the headquarter of the Company on 23 August 2007. Three of the three directors attended the meeting. The Company’s 2007 interim report was approved at the meeting.
4. A supervisory committee meeting was held in the meeting room at the headquarter of the Company on 24 October 2007. Three of the three directors attended the meeting. The Company’s 2007 third quarterly report was approved at the meeting.
5. A supervisory committee meeting was held by way of written resolutions on 30 October 2007. Three of the three directors attended the meeting. The “Work System for Supervisory Committee” was approved at the meeting.
6. A supervisory committee meeting was held in the meeting room at the headquarter of the Company on 28 December 2007. Three of the three directors attended the meeting. The Company’s plan for assets acquisition by way of issuing new shares was approved at the meeting.

Report of the Supervisory Committee

II. INDEPENDENT OPINIONS OF THE SUPERVISORY COMMITTEE ON RELEVANT MATTERS OF THE COMPANY IN 2007

According to the relevant requirements under the Company Law of the PRC and the articles of association of the Company, the sixth session of the Supervisory Committee of the Company has expressed its independent opinion on relevant affairs of the Company during the Reporting Period as follows:

1. During the Reporting period, the Company has formulated and consummated each control system, all decision-making procedures of the Company were lawful, and no material breach of law, regulations and the articles of association of the Company or any actions against the interest of the Company were found when the directors and members of the Senior Management of the Company performed their duties during the Reporting Period. The self evaluation report on the Company's internal control is true. It reflects the establishment and implementation of the Company's internal control system is an objective way.
2. The actual investment projects financed by the capital raised in the provided time were basically consistent with those promised. During the Reporting Period, the Company had no capital raising investment project and no significant non-capital raising investment project.
3. During the Reporting Period, the prices for disposal of the Company's assets are reasonable. There is neither any insider dealing nor any prejudice to the shareholders' interests or any loss of the assets of the Company.
4. During the Reporting Period, the Company entered into connected transactions with the connected parties which are fair and reasonable at fair prices without causing any prejudice to the interests of any non-connected shareholders and the listed Company.
5. Shenzhen Dahua Tiancheng Certified Public Accountant has audited the Company's financial statement of 2007 and issued an audit report with qualified opinions. In the opinion of the Supervisory Committee, the audit report was fair and objective, and the current financial statement has truly reflected the state of financial condition and operating results of the Company.
6. The Supervisory Committee has reviewed the specific explanations of the sixth session of the Board of the Company regarding the issues contained in the qualified opinions from auditors and the explanations regarding the reasons and effects of the change of the accounting policy and has approved such specific explanations.

Corporate Information

REGISTERED OFFICE IN CHINA

No. 8 Ronggang Road
Ronggui, Shunde
Foshan, Guangdong Province
China

PLACE OF BUSINESS IN HONG KONG

Room 3104-06,
Singa Commercial Centre,
No. 148 Connaught Road West,
Hong Kong

SECRETARY FOR THE BOARD OF DIRECTORS

Secretary for the Board of Directors:
Zhong Liang

AUTHORIZED REPRESENTATIVES

Mr. Zhang Ming
Mr. Xian Jian Lin

SHARE REGISTRAR AND TRANSFER OFFICE

Hong Kong Registrars Limited
17th Floor, Hopewell Center 183
Queen's Road East, Wanchai, Hong Kong

TELEPHONE

(852) 2593 5611
(86-757) 2836 2570

FAX

(852) 2802 8085
(86-757) 2836 1055

EMAIL ADDRESS

kelon@gdkelon.com.hk
kelonsec@hisense.com

INTERNET WEBSITE

<http://www.kelon.com>

AUDITORS

China: BDO Shenzhen Dahua Tinacheng
Certified Public Accountants
11th Floor, Block B, United Plaza
NO. 5022 Binhe Road
Futian District, Shenzhen
Postcode: 518033

Hong Kong: BDO McCabe Lo Limited
25th Floor, Wing On Centre,
111 Connaught Road Central,
Hong Kong

LEGAL ADVISERS

China: Tang Law Group
16th Floor, Anlian Plaza, Building 3,
Beijing International Center,
No. 38 North Road Dongsanhuan,
Chaoyang District,
Beijing, China

Hong Kong: Huen Wong & Co. in association
with Fried, Frank, Harris, Shriver & Jacobson LLP
9th Floor Gloucester Tower
The Landmark 15 Queen's Road Central
Hong Kong

BANKERS IN CHINA

The Industrial and Commercial Bank of China
China Construction Bank
Bank of China
China Everbright Bank
China Minsheng Bank
Shanghai Pudong Development Bank
Guangdong Development Bank
Bank of Communications
China Merchant Bank
Agricultural Bank of China
Industrial Bank
The Rural Credit Cooperative of Shunde District Foshan City
Shenzhen Development Bank
BMO Bank of Montreal – Guangzhou Branch
Standard Chartered Bank PLC Shenzhen Branch

BANKERS IN HONG KONG

Bank of Communications Co. Ltd.
Hong Kong Branch

Definitions

In the report, unless the context requires otherwise, the following terms or expressions shall have the following meanings:

“Company”, “the Company”	Hisense Kelon Electrical Holdings Company Limited
“Hisense Air-Conditioning”	Qingdao Hisense Air-conditioning Company Limited
“Hisense Electrical Appliances”	Qingdao Hisense Electric Co., Ltd.
“Ronshen Freezer”	Hisense Ronshen (Guangdong) Freezer Company Limited
“Hisense Group”	Hisense Group Company
“Hisense Marketing”	Qingdao Hisense Marketing Company Limited
“Economic Consultancy”	Foshan Shunde Economic Consultancy Company
“Dong Heng Consultancy”	Foshan Shunde Dong Heng Information Consultancy Service Company Limited
“Guangdong Greencool”	Guangdong Greencool Enterprise Development Company Limited
“Greencool Companies”	Guangdong Greencool and other related parties
“Kelon Air-Conditioner”	Guangdong Kelon Air-Conditioner Co., Ltd.
“Kelon Fittings”	Guangdong Kelon Fittings Co., Ltd.
“Chengdu Kelon”	Hisense(Chengdu) Refrigerator Co., Ltd.
“Jiangxi Kelon”	Jiangxi Kelon Industrial Development Co., Ltd.
“Yangzhou Kelon”	Hisense Ronshen (Yangzhou) Refrigerator Co., Ltd.
“Kaifeng Kelon”	Kaifeng Kelon Air-Conditioner Co., Ltd., a former subsidiary of the Company and had transferred.
“Jilin Kelon”	Jilin Kelon Electrical Co Ltd.
“Huayi Compressor”	Huayi Compressor Holdings Company Limited
“Jiangxi Kesheng”	Jiangxi Kesheng Industry and Trading Company Limited
“Tianjin Greencool”	Greencool Refrigerant (China) Company Limited
“Hainan Greencool”	Hainan Greencool Environmental Protection Engineering Co. Ltd.
“Jinan San Ai Fu”	Jinan San Ai Fu Petrochemical Company Limited
“Shenzhen Kelon”	Shenzhen Kelon Procurement Co Ltd.
“Greencool Procurement”	Greencool Procurement (Shenzhen) Co., Ltd.

Definitions

“Tianjin Xiangrun”	Tianjin Xiangrun Trading Development Company Limited
“Zhongshan Dongyue”	Zhongshan Dongyue Appliance Company Limited
“Chengdu Xinxing”	Chengdu Xinxing Electrical Appliance Holdings Company Limited
“Yangzhou Greencool”	Yangzhou Greencool Venture Capital Company Limited
“Keda Plastic”	Jiangxi Keda Plastic Technology Company Limited
“Wuhan Changrong”	Wuhan Changrong Electrical Appliance Company Limited
“Zhuhai Longjia”	Zhuhai City Longjia Refrigerant Co., Ltd.
“Zhuhai Defa”	Zhuhai Defa Air-conditioner Fittings Company Limited
“Hefei Weixi”	Hefei Weixi Home Appliances Co., Ltd.
“Zhuhai Greencool”	Zhuhai Greencool Refrigeration and Engineering Co., Limited
“Beijing Greencool”	Beijing Greencool Refrigerant Replacement Engineering Co., Limited
“Shenzhen Greencool Technology”	Greencool Technology Development (Shenzhen) Company Limited
“Shenzhen Greencool Environmental”	Greencool Technology Environmental Protection Engineering (Shenzhen) Co., Ltd.
“Hangxiao Ganggou”	Zhejiang Hangzhou Hangxiao Ganggou Holdings Company Limited
“Construction Bank”	China Construction Bank Corporation
“Gateway Limited “	Gateway Limited (佳瑋有限公司)
“Fuji Elevator”	Guangdong Fuji Elevator Co., LTD.
“Hongke Trade”	Foshan Shunde District Hongke Trade Co., LTD.
“Haogang Commerce”	Foshan Shunde District Haogang Commerce Co., LTD.
“Chengdu Arterial Road Company”	The Headquarters for Arterial Road Construction of Chengdu
“Chengfa Engine”	Chengfa Engine (Group) Co., LTD.
“Sichuan Keming”	Sichuan Keming Electrical Co., LTD.
“KPMG”	KPMG
“Intermediate People’s Court of Foshan City”	Intermediate People’s Court of Foshan City

Definitions

“CSRC”	China Securities Regulatory Commission
“Shenzhen Stock Exchange”	Shenzhen Stock Exchange
“RMB”	Renminbi
“Stock Exchange”	The Stock Exchange of Hong Kong Limited

Independent Auditor's Report



BDO McCabe Lo Limited
Certified Public Accountants
德豪嘉信會計師事務所有限公司

25th Floor Wing On Centre
111 Connaught Road Central
Hong Kong
Telephone : (852) 2541 5041
Facsimile : (852) 2815 2239

香港干諾道中111號
永安中心25樓
電話：(852) 2541 5041
傳真：(852) 2815 2239

**TO THE SHAREHOLDERS OF
HISENSE KELON ELECTRICAL HOLDINGS COMPANY LIMITED
(海信科龍電器股份有限公司)**

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

We have audited the financial statements of Hisense Kelon Electrical Holdings Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 58 to 128, which comprise the consolidated balance sheet 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 International Financial Reporting Standards 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.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. This 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.

Except as described in the basis for qualified opinion paragraph, 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 auditor's judgment, 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 auditor considers 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.

Independent Auditor's Report

BASIS FOR QUALIFIED OPINION

It was reported by the Company that the previous controlling shareholder, Guangdong Greencool Enterprise Development Company Limited ("Greencool Enterprise"), had entered into a series of activities/ transactions during the period from 2001 to 2005 which had been harmful to the Group, including but not limited to unauthorised use of the Group's funds, fictitious sales of goods and scrap materials, unreasonable prepayments and purchases of raw materials and property, plant and equipment at unreasonable quantities and prices. These transactions were conducted through Greencool Enterprise, its affiliates and/or companies suspected to be connected with the Company's former chairman, Mr. Gu Chu Jun ("Mr. Gu"). As at 31 December 2007, the aggregate amount of receivables and aggregate amount of payables due from/to these companies were approximately RMB286 million (net of an accumulated impairment loss of RMB364 million) and RMB132 million respectively which were reflected in the consolidated balance sheet at 31 December 2007 as "Amounts due from Greencool Enterprise and its affiliates" and "Amounts due from companies suspected to be connected with Mr. Gu" within current assets and "Amounts due to Greencool Enterprise and its affiliates" and "Amounts due to companies suspected to be connected with Mr. Gu" within current liabilities. Due to the irregularity of the transactions mentioned above and limitation of information available to us, we were unable to satisfy ourselves concerning the validity of these transactions, the appropriateness of the accumulated impairment and the recoverability of the carrying amounts. Any adjustments found to be necessary would affect the opening accumulated losses as at 1 January 2007, the net liabilities as at 31 December 2007 and the profit for the year then ended.

QUALIFIED OPINION ARISING FROM LIMITATION OF AUDIT SCOPE

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the matters set out in the basis for qualified opinion section of this report, the financial statements give a true and fair view of the state of the Group's affairs as at 31 December 2007 and of its profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Without further qualifying our opinion, we draw attention to note 2(b) to the financial statements which indicates that the Group's current liabilities exceeded its current assets by approximately RMB2,640 million as at 31 December 2007. These conditions, along with other matters as set forth in note 2(b) to the financial statements, indicate the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. The directors are of the opinion that the Group will have sufficient working capital to finance its normal operations and to meet its financial obligations as they fall due for the foreseeable future and have prepared the consolidated financial statements on a going concern basis.

BDO McCabe Lo Limited

Certified Public Accountants

Chow Tak Sing, Peter

Practising Certificate Number P04659

Hong Kong, 24 April 2008

Consolidated Income Statement

For the year ended 31 December 2007

	<i>Notes</i>	2007 RMB'000	2006 RMB'000 (Restated)
Turnover	5	8,319,960	6,564,257
Cost of sales		(6,942,789)	(5,474,785)
Gross profit		1,377,171	1,089,472
Other income and gains	7	570,905	409,305
Distribution costs		(1,126,269)	(869,207)
Administrative expenses		(397,500)	(390,978)
Other operating expenses	8	(133,500)	(56,815)
Profit from operations		290,807	181,777
Dilution loss on share reform of an associate		—	(16,317)
Share of results of associates		2,247	3,590
Finance costs	10	(78,530)	(140,672)
Profit before income tax	11	214,524	28,378
Income tax (expense)/ credit	14	(10,867)	20,871
Profit for the year		203,657	49,249
Attributable to:			
— Equity holders of the Company		238,712	69,989
— Minority interests		(35,055)	(20,740)
		203,657	49,249
Dividends		—	—
Earnings per share attributable to equity holders of the Company	15		
— Basic and diluted		RMB0.24	RMB0.07

Consolidated Balance Sheet

As at 31 December 2007

	<i>Notes</i>	2007 RMB'000	2006 RMB'000 (Restated)
ASSETS			
Non-current assets			
Property, plant and equipment	16	1,383,062	1,612,767
Investment properties	17	38,192	26,144
Payments for leasehold land held for own use under operating leases	18	305,392	372,533
Interests in associates	20	82,839	78,981
Available-for-sale financial assets	21	1,220	—
Intangible assets	22	168,112	125,831
Goodwill	23	—	—
Deferred tax assets	24	11,300	21,387
Total non-current assets		1,990,117	2,237,643
Current assets			
Inventories	25	940,284	919,837
Trade and other receivables	26	1,307,209	1,119,733
Taxation recoverable		585	827
Other financial assets	27	9,479	—
Pledged bank deposits		70,133	248,257
Cash and cash equivalents		76,395	142,247
Total current assets		2,404,085	2,430,901
Non-current assets held for sale	28	20,369	—
Total assets		4,414,571	4,668,544
LIABILITIES			
Current liabilities			
Trade and other payables	29	3,093,181	3,093,956
Trade deposits received		406,379	488,587
Other financial liabilities	27	6,158	—
Provisions	30	144,006	169,995
Taxation payable		27,856	26,663
Other liabilities	31	55,793	46,978
Bank borrowings	32	1,310,972	1,556,702
Total current liabilities		5,044,345	5,382,881

Consolidated Balance Sheet

As at 31 December 2007

	<i>Notes</i>	2007 RMB'000	2006 RMB'000 (Restated)
Non-current liabilities			
Other liabilities	<i>31</i>	—	13,594
Total non-current liabilities		—	13,594
Total liabilities		5,044,345	5,396,475
Net current liabilities		(2,640,260)	(2,951,980)
Total assets less current liabilities		(629,774)	(714,337)
TOTAL NET LIABILITIES		(629,774)	(727,931)
Capital and reserves attributable to equity holders of the Company			
Share capital	<i>33</i>	992,007	992,007
Share premium		1,195,597	1,195,597
Statutory reserves	<i>41(a)</i>	114,581	114,581
Capital reserve		266,672	309,733
Foreign exchange reserve		29,111	14,956
Accumulated losses		(3,382,740)	(3,621,452)
		(784,772)	(994,578)
Minority interests		154,998	266,647
TOTAL EQUITY		(629,774)	(727,931)

On behalf of the Board

Tang Ye Guo
Director

Wang Shi Lei
Director

Consolidated Statement of Changes in Equity

For the year ended 31 December 2007

	Share capital RMB'000	Share premium RMB'000	Statutory reserves (Note 41(a)) RMB'000	Capital reserve RMB'000	Revaluat- ion reserve RMB'000	Foreign exchange reserve RMB'000	Accumu- lated losses RMB'000	Equity attributable to equity holders of Company RMB'000	Minority interests RMB'000	Total equity RMB'000
As at 1 January 2006, as previously stated	992,007	1,195,597	114,581	29,573	373,570	4,954	(3,794,745)	(1,084,463)	284,390	(800,073)
Effect of change in accounting policies (Note 4(a))	—	—	—	280,637	(373,570)	—	103,304	10,371	—	10,371
As at 1 January 2006, as restated	992,007	1,195,597	114,581	310,210	—	4,954	(3,691,441)	(1,074,092)	284,390	(789,702)
Share of reserves of associates	—	—	—	(477)	—	—	—	(477)	—	(477)
Exchange differences on translation	—	—	—	—	—	10,002	—	10,002	2,997	12,999
Profit for the year	—	—	—	—	—	—	69,989	69,989	(20,740)	49,249
As at 31 December 2006	992,007	1,195,597	114,581	309,733	—	14,956	(3,621,452)	(994,578)	266,647	(727,931)
As at 31 December 2006, as previously stated	992,007	1,195,597	114,581	29,096	373,570	14,956	(3,725,527)	(1,005,720)	266,647	(739,073)
Effect of changes in accounting policies (Note 4(a))	—	—	—	280,637	(373,570)	—	104,075	11,142	—	11,142
As at 1 January 2007, as restated	992,007	1,195,597	114,581	309,733	—	14,956	(3,621,452)	(994,578)	266,647	(727,931)
Share of reserves of associates	—	—	—	1,611	—	—	—	1,611	—	1,611
Acquisition of additional interests in a subsidiary (Note 37)	—	—	—	(44,672)	—	—	—	(44,672)	(36,716)	(81,388)
Disposal of a subsidiary (Note 38)	—	—	—	—	—	—	—	—	(36,880)	(36,880)
Exchange differences on translation	—	—	—	—	—	14,155	—	14,155	(2,998)	11,157
Profit for the year	—	—	—	—	—	—	238,712	238,712	(35,055)	203,657
As at 31 December 2007	992,007	1,195,597	114,581	266,672	—	29,111	(3,382,740)	(784,772)	154,998	(629,774)

Consolidated Cash Flow Statement

For the year ended 31 December 2007

	2007 RMB'000	2006 RMB'000 (Restated)
Operating activities		
Profit before income tax	214,524	28,378
Adjustments for:		
Share of results of associates	(2,247)	(3,590)
Dilution loss on share reform of an associate	—	16,317
Interest income	(3,753)	(5,238)
Interest expense	67,905	121,321
Depreciation of property, plant and equipment	236,181	247,512
Depreciation of investment properties	3,687	641
Amortisation of intangible assets	3,919	4,126
Amortisation of payments for leasehold land held for own use under operating leases	15,555	14,449
Impairment loss on property, plant and equipment	26,658	25,159
Impairment loss on intangible assets	1,282	—
Impairment loss on payments for leasehold land held for own use under operating leases	17,189	—
Loss/(gain) on disposal of property, plant and equipment, net	50,556	(5,180)
Impairment loss on trade and other receivables	13,546	—
Partial recovery of an impaired receivable	(57,072)	—
Reversal of impairment loss on trade and other receivables	(12,564)	(61,012)
Write down of inventories to net realisable value, net	11,954	42,700
Gain on disposal of investment properties	(60,258)	—
Reversal of provision for sales rebates	—	(37,593)
Gain on disposal of a subsidiary	(4,509)	—
Gain on disposal of payments for leasehold land held for own use under operating leases	(284,351)	(38,597)
Gain on fair value change of other financial assets and other financial liabilities, net	(3,104)	—
Operating profit before working capital changes	235,098	349,393
(Increase)/decrease in inventories	(33,310)	270,443
(Increase)/decrease in trade and other receivables	(133,790)	396,716
Increase/(decrease) in trade and other payables	32,274	(289,972)
(Decrease)/increase in trade deposits received	(80,577)	210,741
Decrease in provisions	(25,989)	(39,921)
Decrease in other liabilities	(4,779)	(13,352)
Cash (used in)/generated from operations	(11,073)	884,048
Tax refund/(paid), net	655	(52)
Net cash flows (used in)/generated from operating activities	(10,418)	883,996

Consolidated Cash Flow Statement

For the year ended 31 December 2007

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i> (Restated)
Investing activities		
Purchase of property, plant and equipment	(236,149)	(141,477)
Purchase of intangible assets	(47,482)	(1,175)
Proceeds from disposal of property, plant and equipment	197,544	88,372
Decrease/(increase) in pledged bank deposits	178,124	(145,443)
Purchase of investment properties	(1,035)	—
Proceeds from disposal of investment properties	100,289	—
Purchase of payments for leasehold land held for own use under operating leases	(16,605)	—
Investment in available-for-sale financial assets	(1,220)	—
Disposal of a subsidiary, net of cash disposed	(23)	—
Interest received	3,753	5,238
Proceeds from disposal of payments for leasehold land held for own use under operating leases	131,485	90,646
Net cash flows generated from/(used in) investing activities	308,681	(103,839)
Financing activities		
Bank borrowings raised	1,780,780	1,520,864
Interest paid	(67,905)	(121,321)
Proceeds on transfer of trade and other receivables	142,000	—
Repayment of bank borrowings	(2,026,510)	(2,124,009)
Repayment to a shareholder	(191,004)	(110,000)
Net cash flows used in financing activities	(362,639)	(834,466)
Net decrease in cash and cash equivalents	(64,376)	(54,309)
Cash and cash equivalents at beginning of the year	142,247	184,284
Effect of foreign exchange rate changes	(1,476)	12,272
Cash and cash equivalents at end of year representing bank balances and cash	76,395	142,247

Notes to the Financial Statements

31 December 2007

1. GENERAL INFORMATION

Hisense Kelon Electrical Holdings Company Limited (the “Company”) was incorporated in the People’s Republic of China (hereinafter referred to as the “PRC”) on 16 December 1992. Its H shares were listed on The Stock Exchange of Hong Kong Limited on 23 July 1996 and its A shares were listed on the Shenzhen Stock Exchange on 13 July 1999.

The Company was formerly named Guangdong Kelon Electrical Holdings Company Limited (廣東科龍電器股份有限公司) and has changed its name to Hisense Kelon Electrical Holdings Company Limited (海信科龍電器股份有限公司) since 21 June 2007.

As at 31 December 2006, Qingdao Hisense Air-Conditioning Company Limited (“Hisense Air-Conditioner”) held 262,212,194 shares of domestic legal person shares of the Company, representing 26.43% of total share capital of the Company.

On 29 March 2007, the share reform proposed on 19 December 2006 was completed. Upon its completion, the 262,212,194 domestic shares which were non-freely transferable A shares held by Hisense Air-Conditioner were converted into 238,872,074 transferable shares, representing 24.08% of the Company’s total capital. Hisense Air-Conditioner was the substantial shareholder of the Company as at 31 December 2007.

The address of the registered office and principal place of business of the Company is No.8 Ronggang Road, Ronggui, Shunde, Foshan, the PRC.

The Group, comprising the Company and its subsidiaries, is principally engaged in the manufacture and sale of refrigerators and air-conditioners.

The English names by which some of the companies are referred to in these financial statements represent management’s best efforts in translating their Chinese names as no English names have been registered for these companies.

2. BASIS OF PREPARATION

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRSs”) issued by the International Accounting Standards Board (“IASB”) and the International Financial Reporting Interpretations Committee (“IFRIC”) of the IASB. IFRSs include International Financial Reporting Standards, International Accounting Standards (“IAS”) and Interpretations (collectively referred to as “IFRSs”). In addition, the consolidated financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

(b) Basis of preparation

As at 31 December 2007, the Group’s current liabilities exceeded its current assets by approximately RMB2,640 million (2006: RMB2,952 million) in which the Group has outstanding short-term loans in the aggregate of approximately RMB1,311 million (2006: RMB1,557 million) of which approximately RMB18 million (2006: RMB255 million) were overdue as at 31 December 2007. The Company’s management confirmed that most of the Group’s bankers have expressed their intention to renew/grant credit facilities to the Group upon maturity. However, in the absence of written confirmation from the bankers, there is no assurance that there will be an extension of all such facilities as the debts fall due. Based on the operating budget prepared, the directors are of the opinion that the Group will have sufficient working capital to finance its normal operations and to meet its financial obligations as they fall due for the foreseeable future and have prepared the consolidated financial statements on a going concern basis.

Notes to the Financial Statements

31 December 2007

2. BASIS OF PREPARATION *(continued)*

(b) Basis of preparation *(continued)*

The consolidated financial statements for the year ended 31 December 2007 comprise the Company and its subsidiaries and the Group's interests in associates. The measurement basis used in the preparation of the financial statements is historical cost except for certain financial instruments which are measured at fair value as explained in accounting policies.

The accounting policies and bases adopted in the preparation of these financial statements differ in some respects from those used in the statutory accounts of the group entities which are prepared in accordance with generally accepted accounting principles and relevant financial regulations in the PRC.

The Ministry of Finance of the PRC issued a series of new and revised Accounting Standards for Business Enterprises (the "New Chinese Accounting Standards, CAS") on 15 February 2006. The New CAS has become effective from 1 January 2007 for listed companies in the PRC. The Company and all its subsidiaries located in the PRC started to prepare their PRC statutory financial statements in accordance with the New CAS for accounting periods beginning on or after 1 January 2007. The differences arising from the restatement of the result of operations for compliance with IFRSs, if any, are adjusted in these financial statements but will not be taken up in the accounting books of the Group.

(c) Use of estimates and judgments

The preparation of financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and other various factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of IFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next financial year are disclosed in Note 44.

(d) Functional and presentation currency

The consolidated financial statements are presented in Renminbi ("RMB"), which is the functional currency of the group entities.

3. ADOPTION OF NEW OR REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

(a) Application of International Financial Reporting Standards

In the current year, the Group has applied all the new and revised standards, amendments and interpretations ("new IFRSs") issued by the IASB, that are relevant to its operation and effective for accounting periods beginning on or after 1 January 2007. The adoption of the new IFRSs had no material effect on how the results for the current or prior accounting periods have been prepared and presented except for the following items.

Notes to the Financial Statements

31 December 2007

3. ADOPTION OF NEW OR REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS *(continued)*

(a) Application of International Financial Reporting Standards *(continued)*

The adoption of “IFRS 7, Financial Instruments: Disclosure” and “Amendment to IAS 1, Presentation of Financial Statements: Capital Disclosures” resulted in more disclosures in respect of financial instruments and an additional disclosure on capital management policy, respectively. Comparative information has been restated for a consistent presentation or included to reflect the new requirements.

(b) Potential impact arising from the new accounting standards not yet effective

The Group has not yet applied the following new standards, amendment or interpretations that have been issued but are not yet effective. The directors of the Company anticipated that the application of these new IFRSs will have no material impact on the financial statements of the Group.

IAS 1 (Revised)	Presentation of Financial Statements ¹
IAS 23 (Revised)	Borrowing Costs ¹
IAS 27 (Revised)	Consolidated and Separate Financial Statements ⁵
IAS 32 and IAS 1 Amendments	Puttable Financial Instruments and Obligations Arising on Liquidation ¹
IFRS 2 Amendment	Share-based Payments – Vesting Conditions and Cancellations ¹
IFRS 3 (Revised)	Business Combinations ⁵
IFRS 8	Operating Segments ¹
IFRIC – Interpretation 11	Group and Treasury Share Transactions ⁴
IFRIC – Interpretation 12	Service Concession Arrangements ³
IFRIC – Interpretation 13	Customer Loyalty Programmes ²
IFRIC – Interpretation 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction ³

¹ Effective for annual periods beginning on or after 1 January 2009

² Effective for annual periods beginning on or after 1 July 2008

³ Effective for annual periods beginning on or after 1 January 2008

⁴ Effective for annual periods beginning on or after 1 March 2007

⁵ Effective for annual periods beginning on or after 1 July 2009

4. PRINCIPAL ACCOUNTING POLICIES

(a) Summary of the effects of the changes in accounting policies

The financial statements for the year ended 31 December 2007 include a restatement of the 2006 financial statements as a result of the change in accounting policy of the measurement basis of the property, plant and equipment, details and effects of the change are explained below:

	2006 RMB'000
Income statement:	
Decrease in administrative expenses (i)	771
Increase in profit for the year	771
	RMB
Increase in basic earnings per share	0.001

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(a) Summary of the effects of the changes in accounting policies *(continued)*

	2006 RMB'000 Dr/ (Cr)
Balance sheet:	
Increase in cost of property, plant and equipment <i>(ii)</i>	99,229
Increase in accumulated depreciation and impairment losses on property, plant and equipment <i>(ii)</i>	(88,087)
<hr/>	
Increase in total assets	11,142
<hr/>	
Increase in retained earnings as at 1 January	(103,304)
Increase in profit for the year	(771)
Decrease in revaluation reserve as at 1 January <i>(iii)</i>	373,570
Increase in capital reserve as at 1 January <i>(iii)</i>	(280,637)
<hr/>	
Increase in total equity	(11,142)

- (i) In prior years, certain property, plant and equipment held for use in production or supply of goods or services, or for administrative purpose are stated in the balance sheet at their revalued amounts, being the fair value on basis of their existing use at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment loss (revaluation model) in accordance with the provisions of IAS 16. During the year, the Company restated these property, plant and equipment at cost less any subsequent accumulated depreciation and subsequent accumulated impairment loss (cost model) in accordance with the provisions of IAS 16, to be in alignment with the accounting policy for property, plant and equipment adopted in its PRC statutory financial statements.
- (ii) The changes resulted in an increase in the cost by approximately RMB99,229,000, and an increase in accumulated depreciation and impairment losses on property, plant and equipment by approximately RMB88,087,000.
- (iii) Included in the revaluation reserve brought forward of RMB373,570,000 as at 1 January 2006 was an amount of RMB280,637,000 arose from the restructuring of the Company. This amount was reclassified to capital reserve in order to conform with current year's presentation of financial statements.

(b) Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries ("the Group") as at 31 December each year. 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. Inter-company transactions and balances between group companies are therefore eliminated in full in preparing the consolidated financial statements.

On acquisition, the assets and liabilities of the relevant subsidiaries are measured at their fair values at the date of acquisition. The interest of minority shareholders is stated at the minority's proportion of the fair values of the assets and liabilities recognised.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(b) Basis of consolidation *(continued)*

Minority interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Company, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Minority interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity holders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the year attributable to minority interests and the equity shareholders of the Company.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

The Group applies a policy of treating transactions with minority interests as transactions with equity owners of the Group. For purchases from minority interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is deducted from equity. For disposals to minority interests, differences between any proceeds received and the relevant share of minority interests are also recorded in equity.

(c) Subsidiaries

A subsidiary is an entity over which the Company is able to exercise control. Control is achieved where the Company, directly or indirectly, has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

(d) Associates

Where the Group has the power to participate in (but not control) the financial and operating policy decisions of another entity, that other entity is classified as an associate. Associates are accounted for using equity method whereby they are initially recognised in the consolidated balance sheet at cost and thereafter, their carrying values are adjusted for Group's share of the post-acquisition change in the associate's net assets — except that losses in excess of the Group's investment in the associate are not recognised unless there is an obligation to make good those losses.

Profits and losses arising on transactions between the Group and its associates are recognised only to the extent of unrelated investors' interests in the associate. The investor's share in the associate's profits and losses resulting from these transactions is eliminated against the carrying value of the associate.

Any premium paid for an associate above the fair value of the Group's share of the identifiable assets, liabilities and contingent liabilities acquired is capitalised and included in the carrying amount of the associate and subject to impairment testing in the same way as goodwill arising on a business combination described below.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(e) Goodwill

Goodwill represents the excess of the cost of a business combination over the interest in the fair value of identifiable assets, liabilities and contingent liabilities acquired. Cost comprises the fair values of assets given, liabilities assumed and equity instruments issued, plus any direct costs of acquisition.

Goodwill arising from acquisition of a subsidiary is capitalised as a separate asset with any impairment in carrying value being charged to the consolidated income statement.

Where the fair value of identifiable assets, liabilities and contingent liabilities exceed the fair value of consideration paid, the excess is credited in full to the consolidated income statement.

For the purpose of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired.

For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to the other assets of the unit pro rata on the basis of the carrying amount to each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statement. An impairment loss for goodwill is not reversed in subsequent periods.

(f) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

As at 1 January 2007, the Company resolved to change the measurement basis for property, plant and equipment from revaluation model to cost model. The details and the effect of the changes are presented in note 4(a) to the financial statements.

Depreciation is charged to write off the carrying value of property, plant and equipment other than construction in progress over their estimated useful lives, after taking into account their estimated residual value, using the straight-line method. The estimated useful lives are as follows:

Leasehold land and buildings	20 to 50 years
Plant, machinery and equipment	5 to 10 years
Moulds	3 years
Motor vehicles	5 years

An asset is written down immediately to its recoverable amount if its carrying amount is higher than the asset's estimated recoverable amount.

Construction in progress represents buildings, plant and machinery on which construction work has not been completed and which, upon completion, management intends to hold for production purposes. Construction in progress is carried at costs which include development and construction expenditure incurred and interest and other direct costs attributable to the development less any accumulated impairment losses. On completion, construction in progress is transferred to other property, plant and equipment at cost less accumulated impairment losses. No depreciation is provided in respect of construction in progress until it is completed and is ready for its intended use.

The gain or loss on disposal of an item of property, plant and equipment is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the income statement.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(g) Investment properties

Investment properties, principally comprising office buildings, are held for long-term rental yields and are not occupied by the Group. Investment properties are carried at cost less accumulated depreciation and accumulated impairment losses, if any.

Depreciation is provided using the straight-line method to write off the cost of the investment properties over their estimated useful lives of 20 to 50 years. Where the carrying amount of an investment property is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount.

(h) Payments for leasehold land held for own use under operating leases

Payments for leasehold land held for own use under operating leases represent up-front payments to acquire long-term interests in lessee-occupied properties. These payments are stated at cost and are amortised over the period of the lease on a straight-line basis to the income statement.

When the lease payments cannot be allocated reliably between land and building elements, the entire lease payments are included in the cost of the leasehold land and buildings as a finance lease in property, plant and equipment.

(i) Leasing

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

The Group as lessor

Rental income from operating leases is recognised in the income statement on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised as an expense on a straight-line basis over the lease term.

The Group as lessee

Assets held under finance leases are recognised as assets of the Group at the fair value of the leased asset or, if lower, the present value of the minimum lease payments payable over the term of the lease. The corresponding lease commitment is shown as a liability. Lease payments are analysed between capital and interest. The interest element is charged to the income statement over the period of the lease and is calculated so that it represents a constant proportion of the lease liability. The capital element reduces the balance owed to the lessor.

Rentals payable under the lease are charged to the income statement on a straight-line basis over the lease term.

The land and buildings elements of property leases are considered separately for the purposes of lease classification.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(j) Intangible assets (other than goodwill)

(i) *Externally acquired intangible assets*

Externally acquired intangible assets are initially recognised at cost. Subsequently, intangible assets with finite useful lives are carried at cost less accumulated amortisation and accumulated impairment losses. Amortisation is provided on a straight-line basis over their useful lives. Intangible assets with indefinite useful lives are carried at cost less any accumulated losses. The amortisation expense is included within administrative expenses in the income statement.

Intangible assets separate from goodwill, are recognised on business combinations if they are separable from the acquired entity or give rise to other contractual/legal rights. The amounts ascribed to such intangibles are arrived at by using appropriate valuation techniques.

The significant intangibles recognised by the Group, their useful economic lives are as follows:

Intangible	Useful economic life
Trademarks	Indefinite
Software	4 years
Non-patented technologies	4 to 5 years

(ii) *Internally generated intangible assets (research and development costs)*

Expenditure on internally developed products is capitalised if it can be demonstrated that:

- It is technically feasible to develop the product for it to be sold;
- Adequate resources are available to complete the development;
- There is an intention to complete and sell the product;
- The Group is able to sell the product;
- Sale of the product will generate future economic benefits; and
- Expenditure on the project can be measured reliably.

Capitalised development costs are amortised over the periods the Group expects to benefit from selling the products developed. The amortisation expense is included within administrative expenses in the income statement.

Development expenditure not satisfying the above criteria and expenditure on the research phase of internal projects are recognised in the income statement as incurred.

(iii) *Impairment*

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

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(j) Intangible assets (other than goodwill) *(continued)*

(iii) Impairment *(continued)*

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

Intangible assets with finite lives are tested for impairment when there is an indication that an asset may be impaired.

(k) Financial instruments

(i) Financial assets

The Group classifies its financial assets into one of the following categories, depending on the purpose for which the asset was acquired. The Group's accounting policy for each category is as follows:

Financial assets at fair value through profit or loss: include financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss. 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 or financial guarantee contracts. Gains or losses on investments held for trading are recognised in the income statement.

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 the separation of the embedded derivative is prohibited.

Financial assets may be designated upon initial recognition as at fair value through profit or loss if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or loss on them on a different basis; (ii) the assets are part of a group of financial assets which is managed and its performance evaluated on a fair value basis according to a documented management strategy; or (iii) the financial asset contains an embedded derivative that would need to be separately recorded.

At each balance sheet date subsequent to initial recognition, financial assets at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in the income statement in the period in which they arise.

Loans and receivables: These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services to customers (trade debtors), but also incorporate other types of contractual monetary asset. At each balance sheet date subsequent to initial recognition, they are carried at amortised cost using the effective interest method, less any identified impairment losses.

Available-for-sale financial assets: Non-derivative financial assets not included in the above categories are classified as available-for-sale and comprise the Group's strategic investments in entities not qualifying as subsidiaries, associates or jointly controlled entities. They are carried at fair value with changes in fair value recognised directly in equity.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(k) Financial instruments *(continued)*

(i) Financial assets *(continued)*

For available-for-sale equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, they are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition.

(ii) Impairment loss on financial assets

Objective evidence that the asset is impaired includes observable data that comes to the attention of the Group including the following loss events:

- significant financial difficulty of the debtor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- granting concession to a debtor because of debtors' financial difficulty; or
- it becoming probable that the debtor will enter bankruptcy or other financial reorganisation.

For loan and receivables

An allowance for impairment loss is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms. The amount of provision is the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount is recognised in the income statement. When the asset is uncollectible, it is written off against the allowance account. Impairment losses are reversed in subsequent periods when an increase in the asset's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to a restriction that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

For available-for-sale financial assets

Where a decline in the fair value constitutes objective evidence of impairment, the amount of the loss is removed from equity and recognised in the income statement.

Any impairment loss is recognised in the income statement on available-for-sale debt investments, is subsequently reversed if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

For available-for-sale equity investment, any increase in fair value subsequent to an impairment loss is recognized directly in equity.

For available-for-sale equity investment that is carried at cost, the amount of impairment loss is measured as the difference between the carrying amount of the asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss shall not be reversed.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(k) Financial instruments *(continued)*

(iii) Financial liabilities

The Group classifies its financial liabilities into one of two categories, depending on the purpose for which the liabilities were incurred. Other than financial liabilities in a qualifying hedging relationship (see below), the Group's accounting policy for each category is as follows:

Financial liabilities at fair value through profit or loss: Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities 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 liabilities held for trading are recognised in the income statement.

Where a contract contains one or more embedded derivatives, the entire hybrid contract may be designated as a financial liability 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.

Financial liabilities may be designated upon initial recognition as at fair value through profit or loss if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the liabilities or recognising gains or losses on them on a different basis; (ii) the liabilities are part of a group of financial liabilities which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial liability contains an embedded derivative that would need to be separately recorded.

Other financial liabilities include the following items:

- Trade payables and other short-term monetary liabilities, which are initially recognised at fair value and subsequently measured at amortised cost using effective interest method.
- Bank borrowings and the debt element of convertible debt issued by the Group, which are initially recognised at the amount advanced net of any transaction costs directly attributable to the issue of the instrument. Such interest bearing liabilities are subsequently measured at amortised cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the balance sheet. Interest expense in this context includes initial transaction costs and premium payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

(iv) Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. A financial guarantee contract issued by the Group and not designated as at fair value through profit or loss is recognised initially at its fair value less transaction costs that are directly attributable to the issue of the financial guarantee contract. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue.

Notes to the Financial Statements

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4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(k) Financial instruments *(continued)*

(v) *Derecognition*

The Group derecognises a financial asset when the contractual rights to the future cash flows in relation to the financial asset expire or when the financial asset has been transferred and the transfer meets the criteria for derecognition in accordance with IAS 39.

The Group derecognises a financial liability when the obligation under the liability is discharged or cancelled or expired.

(l) Inventories

Inventories are initially recognised at cost, and subsequently at the lower of cost and net realisable value. Cost comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

(m) Non-current assets held for sale

Non-current assets and disposal groups are classified as held for sale when their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is met only when the sale is highly probable and the assets or disposal group is available for immediate sale in its present condition:

Non-current assets classified as held for sale are measured at the lower of:

- their carrying amount immediately prior to being classified as held for sale in accordance with the Group's accounting policy; and
- fair value less costs to sell.

(n) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts and sales related taxes. Sales of goods are recognised when goods are delivered and title has passed.

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

Rental income under operating leases is recognised on a straight-line basis over the term of the relevant lease.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Subsidy income is recognised when the rights to receive the income is established and approved.

Penalty income is recognised when triggering events to receive payment occur and the amount of payment can be reliably measured.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(o) Income taxes

Income taxes for the year comprise current tax and deferred tax.

Current tax is based on the profit or loss from ordinary activities adjusted for items that are non-assessable or disallowable for income tax purposes and is calculated using tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax arises from temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the corresponding amounts used for tax purposes and is accounted for using the balance sheet liability method. Except for recognised assets and liabilities that affect neither accounting nor taxable profits, deferred tax liabilities are recognised for all temporary differences. Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax is measured at the tax rates expected to apply in the period when the liability is settled or the asset is realised based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Income taxes are recognised in the income statement except when they relate to items directly recognised to equity in which case the taxes are also directly recognised in equity.

(p) Foreign currency

Transactions entered into by group entities in currencies other than the currency of the primary economic environment in which it operates (the “functional currency”) are recorded at the rates ruling when the transactions occur. Foreign currency monetary assets and liabilities are translated at the rates ruling at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

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

On consolidation, the results of foreign operations are translated into the presentation currency of the Group (i.e. RMB) at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the rates approximating to those ruling when the transactions took place are used. All assets and liabilities of foreign operations are translated at the rate ruling at the balance sheet date. Exchange differences arising on translating the opening net assets at opening rate and the results of foreign operations at actual rate are recognised directly in equity (the “foreign exchange reserve”). Exchange differences recognised in the income statement of group entities’ separate financial statements on the translation of long-term monetary items forming part of the Group’s net investment in the foreign operation concerned are reclassified to the foreign exchange reserve.

On disposal of a foreign operation, the cumulative exchange differences recognised in the foreign exchange reserve relating to that operation up to the date of disposal are transferred to the income statement as part of the profit or loss on disposal.

Goodwill and fair value adjustments on identifiable assets acquired arising on an acquisition of a foreign operation on or after 1 January 2005 are treated as assets and liabilities of that foreign operation and translated at the rate of exchange prevailing at the balance sheet date. Exchange differences arising are recognised in the foreign exchange reserve.

Notes to the Financial Statements

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4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(q) Employee benefits

Pursuant to the PRC laws and regulations, the Group established in the PRC makes monthly contributions to the basic old age pension for the local staff to a government agency. The contributions are made at a specific percentage on the standard salary set by the provincial government, of which 10% is borne by the Group and the remainder is borne by the staff. The government agency is responsible for the pension liabilities relating to such staff on their retirement.

In addition, the Group manages a defined contribution pension scheme for its employees. The Group makes contributions based on a percentage of the eligible employees' salaries plus a pre-determined amount funded by the Group and are charged to the income statement as they become payable in accordance with the rules of the scheme. When an employee leaves the scheme before his/her interest in the employer contributions is fully vested, the ongoing contributions payable by the Group may be reduced by the relevant amount of forfeited contributions.

The Group accounts for pension contributions on an accrual basis. Accrued contributions are shown as pension liabilities in the consolidated balance sheet.

(r) Borrowing costs

Borrowing costs attributable directly to the acquisition, construction or production of assets which require a substantial period of time to be ready for their intended use or sale, are capitalised as part of the cost of those assets. Income earned on temporary investments of specific borrowings pending their expenditure on those assets is deducted from borrowing costs capitalised.

All other borrowing costs are recognised in the income statement in the period in which they are incurred.

(s) Impairment of other assets

At each balance sheet date, the Group reviews the carrying amounts of the following assets to determine whether there is any indication that those assets have suffered an impairment loss or an impairment loss previously recognised no longer exists or may have decreased:

- property, plant and equipment and investment properties;
- payments for leasehold land held for own use under operating lease; and
- investments in associates.

If the recoverable amount (i.e. the greater of the fair value less costs to sell and value in use) of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

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

(t) Government grants

Government grants are recognised when 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 period 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.

Notes to the Financial Statements

31 December 2007

4. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(u) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, which will probably result in an outflow of economic benefits that can be reasonably estimated.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, the existence of which will only be confirmed by the occurrence or non-occurrence of one or more future events, are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(v) Warranty obligation

The Group provides free repairing services for its products and free replacement of the major components of its products for one to three years after sales.

The costs of the warranty obligation under which the Group agrees to remedy defects in its products are accrued at the time the related sales are recognised. Provision for warranty is accrued based on the estimated costs of fulfilling the total obligation, including handling and transportation costs. The costs are estimated by management based on past experience. The assumptions used to estimate the warranty provision are reviewed periodically in light of actual results.

5. TURNOVER

Turnover and revenue represent the net amounts received and receivable for goods sold during the year. An analysis of the Group's revenue for the year is as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Sales of refrigerators	4,324,808	3,327,896
Sales of air-conditioners	3,214,875	2,533,360
Sales of freezers	324,821	231,972
Sales of product components	455,456	471,029
	<hr/> 8,319,960	<hr/> 6,564,257

6. BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

The Group is organised into four main operating divisions – refrigerators, air-conditioners, freezers and product components. These divisions are the basis on which the Group reports its primary segment information.

Notes to the Financial Statements

31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Segment information about these businesses is presented below:

Year ended 31 December 2007

(i) Consolidated income statement

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Elimination <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Turnover						
External sales	4,324,808	3,214,875	324,821	455,456	—	8,319,960
Inter-segment sales	—	—	—	603,559	(603,559)	—
Total revenue	4,324,808	3,214,875	324,821	1,059,015	(603,559)	8,319,960

Inter-segment sales are charged at prevailing market rates.

Result

Segment result	305,559	9,872	17,464	(24,940)	—	307,955
Unallocated corporate expenses						(17,148)
Profit from operations						290,807
Share of results of associates	1,168	868	88	123	—	2,247
Finance costs						(78,530)
Profit before income tax expense						214,524
Income tax expense						(10,867)
Profit for the year						203,657

(ii) Consolidated balance sheet

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Assets					
Segment assets	2,290,306	1,212,432	166,650	471,722	4,141,110
Interests in associates	49,680	32,247	842	70	82,839
Unallocated corporate assets					190,622
Consolidated total assets					4,414,571
Liabilities					
Segment liabilities	1,871,830	1,375,441	108,200	237,725	3,593,196
Unallocated corporate liabilities					1,451,149
Consolidated total liabilities					5,044,345

Notes to the Financial Statements

31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Year ended 31 December 2007 — Continued

(iii) Other information

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Additions of property, plant and equipment	232,366	44,458	11,464	20,733	309,021
Additions of investment properties	619	405	11	—	1,035
Additions of payments for leasehold land held for own use under operating leases	16,605	—	—	—	16,605
Additions of intangible assets	26,327	20,395	464	296	47,482
Depreciation of property, plant and equipment	115,296	72,579	10,284	38,022	236,181
Depreciation of investment properties	2,462	1,120	29	76	3,687
Amortisation of intangible assets	1,212	1,032	123	1,552	3,919
Amortisation of payments for leasehold land held for own use under operating leases	9,310	4,092	723	1,430	15,555
Impairment loss on property, plant and equipment	1,564	—	—	25,094	26,658
Impairment loss on intangible assets	—	—	—	1,282	1,282
Impairment loss on payments for leasehold land held for own use under operating leases	17,189	—	—	—	17,189
Loss on disposal of property, plant and equipment, net	40,788	7,595	(342)	2,515	50,556
Write down of inventories to net realisable value, net	2,013	846	431	8,664	11,954

Notes to the Financial Statements

31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Year ended 31 December 2006 (Restated)

(i) Consolidated income statement

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Elimination <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Turnover						
External sales	3,327,896	2,533,360	231,972	471,029	—	6,564,257
Inter-segment sales	—	—	—	671,840	(671,840)	—
Total revenue	3,327,896	2,533,360	231,972	1,142,869	(671,840)	6,564,257

Inter-segment sales are charged at prevailing market rates.

Result

Segment result	151,035	22,693	10,027	(11,779)	—	171,976
Unallocated corporate income						9,801
Profit from operations						181,777
Dilution loss on share reform of an associate						(16,317)
Share of results of associates	1,819	1,385	127	259	—	3,590
Finance costs						(140,672)
Profit before income tax credit						28,378
Income tax credit						20,871
Profit for the year						49,249

Notes to the Financial Statements

31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Year ended 31 December 2006 (Restated) *(continued)*

(ii) Consolidated balance sheet

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Assets					
Segment assets	1,909,175	1,509,343	416,819	666,897	4,502,234
Interests in associates	40,041	30,481	2,791	5,668	78,981
Unallocated corporate assets					87,329
Consolidated total assets					<u>4,668,544</u>
Liabilities					
Segment liabilities	1,752,636	1,621,186	184,471	275,021	3,833,314
Unallocated corporate liabilities					1,563,161
Consolidated total liabilities					<u>5,396,475</u>

(iii) Other information

	Refrigerators <i>RMB'000</i>	Air- conditioners <i>RMB'000</i>	Freezers <i>RMB'000</i>	Product components <i>RMB'000</i>	Consolidated <i>RMB'000</i>
Additions of property, plant and equipment	79,256	47,244	8,261	6,716	141,477
Additions of intangible assets	486	443	141	105	1,175
Depreciation of property, plant and equipment	153,127	66,961	15,575	11,849	247,512
Depreciation of investment properties	—	—	—	641	641
Amortisation of intangible assets	3,232	713	125	56	4,126
Amortisation of payments for leasehold land held for own use under operating leases	8,099	4,522	879	949	14,449
Impairment loss on property, plant and equipment	12,999	12,149	6	5	25,159
Write down of inventories to net realisable value, net	35,867	6,434	—	399	42,700

Notes to the Financial Statements

31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(continued)*

Geographical segments

The following table provides an analysis of the Group's turnover by geographical markets with reference to locations of customers:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
The PRC		
Mainland China	4,821,614	4,300,110
Hong Kong	257,188	259,792
	5,078,802	4,559,902
Europe	883,350	525,854
America	926,332	613,349
Others	1,431,476	865,152
	8,319,960	6,564,257

The Group's operations are carried out in the PRC and almost all of the production facilities of the Group are located in the PRC. Therefore, presentation of segment assets by geographical locations is not shown.

7. OTHER INCOME AND GAINS

An analysis of the Group's other income and gains is as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Gain on disposal of raw materials	53,884	114,139
Gain on disposal of property, plant and equipment	16,040	24,588
Gain on disposal of payments for leasehold land held for own use under operating leases	284,351	38,597
Gain on disposal of investment properties	60,258	—
Gain on debts settlement with suppliers	4,422	10,231
Gain on fair value change of other financial assets	9,479	—
Gain on disposal of a subsidiary <i>(Note 38)</i>	4,509	—
Interest income	3,753	5,238
Penalty income	12,166	7,843
Rental income	20,721	7,723
Partial recovery of an impaired receivable <i>(Note 26)</i>	57,072	—
Reversal of impairment loss on trade and other receivables <i>(Note 26)</i>	12,564	61,012
Reversal of provision for sales rebates	—	37,593
Subsidy income	6,236	70,511
Others	25,450	31,830
	570,905	409,305

Notes to the Financial Statements

31 December 2007

8. OTHER OPERATING EXPENSES

An analysis of the Group's other operating expenses is as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Loss on fair value change of other financial liabilities	6,375	—
Loss on disposal of property, plant and equipment	66,596	19,408
Impairment loss on intangible assets	1,282	—
Impairment loss on payments for leasehold land held for own use under operation leases	17,189	—
Impairment loss on property, plant and equipment	26,658	25,159
Loss on disposal of raw materials	—	10,047
Loss on non-deductible input value added tax	4,894	—
Penalty	2,544	1,145
Others	7,962	1,056
	133,500	56,815

9. AMORTISATION OF LONG TERM ASSETS

An analysis of the Group's amortisation of intangible assets and payments for leasehold land held for own use under operating leases is as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Amount included in administrative expenses	19,474	18,575

10. FINANCE COSTS

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Interest on:		
— bank borrowings wholly repayable within five years	63,597	100,196
— discounted note receivables	4,308	21,125
	67,905	121,321
Others	10,625	19,351
	78,530	140,672

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11. PROFIT BEFORE INCOME TAX

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i> (Restated)
Profit before income tax is stated after charging/(crediting):		
Inventories recognised as an expense		
— upon sales of goods	6,944,208	5,515,189
— upon sales of raw materials	425,839	507,582
Staff costs (including directors' and supervisors' remuneration)		
— Basic salaries, housing and other allowances and benefits in kind	589,735	506,843
— Defined contribution pension cost	41,135	31,223
	630,870	538,066
Auditors' remuneration	4,800	5,551
Research and development costs	58,857	11,925
Impairment loss on trade and other receivables (<i>Note 26</i>)	13,546	—
Write down of inventories to net realisable value, net	11,954	42,700
Foreign exchange loss, net	40,970	28,619
Share of income tax of associates	6,277	6,091

Notes to the Financial Statements

31 December 2007

12. DIRECTORS' AND SUPERVISORS' EMOLUMENTS

The amounts of emoluments paid and payable to the directors and supervisors of the Company by the Group are as follows:

Year ended 31 December 2007	Fees <i>RMB'000</i>	Basic salaries, housing and other allowances and benefits in kind <i>RMB'000</i>	Defined contribution pension cost <i>RMB'000</i>	Discretionary bonuses <i>RMB'000</i>	Total <i>RMB'000</i>
Executive directors					
Tang Ye Guo	—	600	15	200	815
Yang Yun Duo (i)	—	400	15	160	575
Yu Shu Min	—	—	—	—	—
Lin Lan	—	—	—	—	—
Xiao Jian Lin (ii)	—	—	—	—	—
Wang Shi Lei (iii)	—	460	13	180	653
Liu Chun Xin (iv)	—	117	2	50	169
Independent non-executive directors					
Zhang Sheng Ping	60	—	—	—	60
Lu Qing	60	—	—	—	60
Cheung Yui Kai, Warren	233	—	—	—	233
Supervisors					
Guo Qing Cun	—	—	—	—	—
Zhou Zhao Li	—	—	—	—	—
Liu Zhan Cheng	—	100	4	100	204
	353	1,677	49	690	2,769

(i) Mr. Yang Yun Duo was appointed on 4 January 2007 and resigned on 26 February 2008.

(ii) Mr. Xiao Jian Lin resigned on 21 June 2007.

(iii) Mr. Wang Shi Lei was appointed on 4 January 2007.

(iv) Ms. Liu Chun Xin was appointed on 8 August 2007.

Notes to the Financial Statements

31 December 2007

12. DIRECTORS' AND SUPERVISORS' EMOLUMENTS (continued)

The amounts of emoluments paid and payable to the directors and supervisors of the Company by the Group are as follows:

Year ended 31 December 2006	Fees RMB'000	Basic salaries, housing and other allowances and benefits in kind RMB'000	Defined contribution pension cost RMB'000	Discretionary bonuses RMB'000	Total RMB'000
Executive directors					
Tang Ye Guo	—	493	4	—	497
Yu Shu Min	—	—	—	—	—
Lin Lan	—	248	—	—	248
Xiao Jian Lin	—	322	3	—	325
Liu Cong Meng (i)	—	—	—	—	—
Li Zhen Hua (i)	—	—	—	—	—
Fang Zhi Guo (i)	—	—	—	—	—
Gu Chu Jun (i)	—	—	—	—	—
Yan You Song (i)	—	—	—	—	—
Zhang Hong (i)	—	—	—	—	—
Zhang Ming (ii)	—	85	3	—	88
Su Yu Tao (iii)	—	302	3	—	305
Independent non-executive directors					
Zhang Sheng Ping	30	—	—	—	30
Lu Qing	30	—	—	—	30
Cheung Yui Kai, Warren	120	—	—	—	120
Xu Xiao Lu (i)	—	—	—	—	—
Li Kung Man (i)	—	—	—	—	—
Chan Pei Cheong (iv)	—	—	—	—	—
Supervisors					
Guo Qing Cun	—	—	—	—	—
Zhou Zhao Li	—	—	—	—	—
Liu Zhan Cheng	—	60	1	133	194
He Si (v)	—	48	1	—	49
Bai Yun Feng (vi)	—	50	—	—	50
	180	1,608	15	133	1,936

- (i) The above individuals resigned on 26 June 2006.
(ii) Mr. Zhang Ming resigned on 13 November 2006.
(iii) Mr. Su Yu Tao resigned on 14 November 2006.
(iv) Mr. Chan Pei Cheong resigned on 23 January 2006.
(v) Mr. He Si resigned on 23 June 2006.
(vi) Mr. Bai Yun Feng resigned on 5 December 2006.

Notes to the Financial Statements

31 December 2007

12. DIRECTORS' AND SUPERVISORS' EMOLUMENTS *(continued)*

Bonus granted to directors and supervisors are based on performance and subject to directors' discretion.

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration for the years ended 31 December 2006 and 2007.

None of the directors and supervisors received compensation for the loss of office as a director or a supervisor of the Group in connection with the management of the affairs of the Group for the years ended 31 December 2006 and 2007.

13. INDIVIDUALS WITH HIGHEST EMOLUMENTS

Of the five highest paid individuals of the Group, three (2006: four) are directors of the Group. The remaining two individuals (2006: one) are not directors or supervisors of the Group.

The following table sets out the emoluments of the Group's five (2006: five) highest paid individuals for the year ended 31 December 2007 of which two (2006: four) of these individuals were appointed as directors of the Company during the year and their emoluments paid for the period from the dates of being appointed as directors during the year to the end of the year are included in Note 12 above.

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Basic salaries, housing and other allowances and benefits in kind	2,219	4,695
Discretionary bonuses	660	—
	2,879	4,695

The emoluments set out above of these individuals are within the following bands:

	2007 Number of staff	2006 Number of staff
Nil — RMB 969,000 (2006: Nil — RMB1,022,000) (equivalent to Nil — HKD1,000,000)	5	4
RMB 969,001 — RMB1,454,000 (2006: RMB1,022,001 — RMB1,533,000) (equivalent to HKD 1,000,001 — HKD 1,500,000)	—	1
	5	5

14. INCOME TAX EXPENSE/(CREDIT)

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Income taxes consist of:		
Current tax		
— PRC enterprise income tax ("EIT")	266	516
— Hong Kong Profits Tax	514	—
Deferred tax	10,087	(21,387)
	10,867	(20,871)

Notes to the Financial Statements

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14. INCOME TAX EXPENSE/(CREDIT) *(continued)*

Taxation is calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

The Company and its subsidiaries provide for taxation on the basis of their statutory profits for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes after considering all available tax benefits.

The Company and its subsidiaries which are established and operating in the PRC are subject to EIT at a statutory rate of 33% for 2007.

The Company was established in Shunde, Guangdong Province and, pursuant to the “Income Tax Law of the PRC for Enterprises with Foreign Investment and Foreign Enterprises” (“Income Tax Law”), is normally subject to national EIT at a rate of 24%, which is applicable to enterprises located in coastal open economic zones. Together with the local EIT rate of 3%, the aggregate EIT is at a rate of 27%. Since June 2003, the Company has been classified as a high new technology enterprise and is entitled to national EIT at a rate of 15%. Together with the local EIT at a rate of 3%, the aggregate EIT is at a rate of 18%.

The Company’s subsidiaries, Guangdong Kelon Air-Conditioner Co., Ltd., Hisense Ronshen (Guangdong) Freezer Co., Ltd, Guangdong Kelon Mould Co., Ltd, Shunde Rongsheng Plastic Products Co., Ltd., Hisense Ronshen Yingkou Refrigerator Co. Ltd., and Hisense Ronshen Yangzhou Refrigerator Co., Ltd established in coastal open economic zones, are subject to national EIT at a rate of 24%. Together with the local EIT at a rate of 3%, the aggregate EIT are at a rate of 27%. Hisense Ronshen (Guangdong) Refrigerator Co., Ltd, as a company established in coastal open economic zones, is also classified as a high new technology enterprise in year 2007 and entitled to national EIT at a rate of 15%, together with the local EIT at a rate of 3%, the aggregate EIT is at a rate 18%.

Guangdong Kelon Fittings Co., Ltd (“Kelon Fittings”) established in coastal open economic zones and was classified as advanced technology enterprise. In year 2007, Kelon Fittings is entitled to EIT at a preferential rate of 12%, which is half deduction of national EIT with fully exemption from local EIT.

Pursuant to Income Tax Regulations related to Development Strategy of Western Region of Mainland China, Chengdu Kelon Refrigerator Co., Ltd. (“Chengdu Kelon”), a subsidiary of the Company is subject to a preferential EIT at a rate of 24%. Together with the local EIT at a rate of 3%, Chengdu Kelon is subject to the aggregate EIT at a rate of 27%.

Other subsidiaries of the Group which are established and operating in the PRC are subject to EIT at a statutory rate of 33% for the year 2007.

Except for Kelon Electric Appliance Co., Ltd., no provision for Hong Kong Profits Tax has been made as the subsidiaries in Hong Kong did not generate assessable profits during the year. Hong Kong Profits Tax has been provided at the rate of 17.5% on the estimated assessable profit for the year 2007.

On 16 March 2007, the Fifth Plenary Session of the Tenth National People’s Congress passed the Corporate Income Tax Law of the PRC (“new tax law”) which will take effect on 1 January 2008. As a result of the new tax law, the statutory income tax rate will change from 33% to 25% with effect from 1 January 2008. The preferential tax rate currently enjoyed by the Company will be gradually transitioned to the new standard rate of 25% over a five-year transitional period. The Group estimates that the preferential income tax rate currently enjoyed by the Group will expire at the earlier of the end of the existing preferential tax period or the five-year transitional period. The change in the carrying amount of the deferred tax assets and liabilities, as a result of the change in tax rate, is reflected in the consolidated financial statements for the year ended 31 December 2007.

Notes to the Financial Statements

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14. INCOME TAX EXPENSE/(CREDIT) (continued)

A reconciliation between income tax expense/(credit) and accounting profit at applicable tax rate is as follows:

	2007	2006
	RMB'000	RMB'000
		(Restated)
Profit before income tax	214,524	28,378
Less: Share of results of associates	2,247	3,590
	212,277	24,788
Tax at the PRC statutory rate of 33%	70,051	8,180
Effect of different tax rates of subsidiaries operating in other jurisdictions	(3,087)	1,560
Effect of exemption granted and preferential tax treatment	(60,314)	(18,718)
Tax effect of expenses not deductible for tax purposes	25,622	1,826
Tax effect of revenue not taxable for tax purposes	(9,503)	(290)
Tax effect of tax losses and other deductible temporary differences not recognised	24,387	165,844
Utilisation of tax losses previously not recognised	(36,289)	(179,273)
Income tax expense/(credit)	10,867	(20,871)

At the balance sheet date, deferred tax assets arising on tax losses carried forward had been recognised to the extent it is probable that future taxable profit will be available against which the unused tax losses can be utilised.

15. EARNINGS PER SHARE

The calculation of basic and diluted earnings per share attributable to equity holders of the Company for the year is based on the net profit attributable to equity holders of the Company for the year of RMB238,712,000 (2006 (restated): RMB69,989,000) and 992,006,563 shares (2006: 992,006,563 shares) outstanding during the year. There were no dilutive potential ordinary shares in issue in both years.

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16. PROPERTY, PLANT AND EQUIPMENT

Year ended 31 December 2007

	Leasehold land and buildings RMB'000	Plant, machinery and equipment RMB'000	Moulds RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
Cost						
At 1 January 2007, as previously stated	1,239,926	2,055,752	204,835	43,596	236,920	3,781,029
Effect of change in accounting policies (Note 4(a))	19,134	4,491	22,182	(164)	53,586	99,229
At 1 January 2007, as restated	1,259,060	2,060,243	227,017	43,432	290,506	3,880,258
Exchange differences	(1,302)	(243)	—	(111)	—	(1,656)
Additions at cost	14,004	39,995	63,906	206	190,910	309,021
Disposals	(177,197)	(302,263)	(59,876)	(8,164)	(28,673)	(576,173)
Disposal of a subsidiary (Note 38)	(24,137)	(13,524)	(12,674)	(354)	(15)	(50,704)
Reclassified to investment properties (Note 17)	(81,461)	—	—	—	—	(81,461)
Reclassified to non-current assets held for sale (Note 28)	(56,555)	—	—	—	—	(56,555)
Reclassification	157,744	106,370	9,423	(5)	(273,532)	—
At 31 December 2007	1,090,156	1,890,578	227,796	35,004	179,196	3,422,730
Accumulated depreciation and impairment						
At 1 January 2007, as previously stated	470,086	1,554,697	116,530	38,091	—	2,179,404
Effect of change in accounting policies (Note 4(a))	22,751	(6,858)	22,182	(3,574)	53,586	88,087
At 1 January 2007, as restated	492,837	1,547,839	138,712	34,517	53,586	2,267,491
Exchange differences	(749)	(213)	—	(109)	—	(1,071)
Depreciation for the year	72,473	105,386	56,587	1,735	—	236,181
Impairment provided for the year	—	16,050	62	—	10,546	26,658
Elimination on disposals	(62,669)	(258,648)	(48,130)	(7,585)	(22,042)	(399,074)
Disposal of a subsidiary (Note 38)	(4,201)	(3,245)	(12,674)	(274)	—	(20,394)
Reclassified to investment properties (Note 17)	(25,785)	—	—	—	—	(25,785)
Reclassified to non-current assets held for sale (Note 28)	(44,338)	—	—	—	—	(44,338)
Reclassification	(1,284)	1,105	200	(21)	—	—
At 31 December 2007	426,284	1,408,274	134,757	28,263	42,090	2,039,668
Net book value						
At 31 December 2007	663,872	482,304	93,039	6,741	137,106	1,383,062

Notes to the Financial Statements

31 December 2007

16. PROPERTY, PLANT AND EQUIPMENT (continued)

Year ended 31 December 2006

	Leasehold land and buildings RMB'000	Plant, machinery and equipment RMB'000	Moulds RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
Cost						
At 1 January 2006, as previously stated	1,548,947	1,892,728	168,054	69,811	267,260	3,946,800
Effect of change in accounting policies (Note 4(a))	15,917	(8,951)	15,491	(477)	52,090	74,070
At 1 January 2006, as restated	1,564,864	1,883,777	183,545	69,334	319,350	4,020,870
Exchange differences	(2,267)	(74)	—	(95)	—	(2,436)
Additions at cost	1,290	22,015	80,707	1,211	36,254	141,477
Disposals	(64,152)	(115,959)	(37,500)	(28,020)	(34,022)	(279,653)
Reclassification	(240,675)	270,484	265	1,002	(31,076)	—
At 31 December 2006, as restated	1,259,060	2,060,243	227,017	43,432	290,506	3,880,258
Accumulated depreciation and impairment						
At 1 January 2006, as previously stated	419,045	1,537,641	95,867	65,558	—	2,118,111
Effect of change in accounting policies (Note 4(a))	19,534	(19,529)	15,491	(3,887)	52,090	63,699
At 1 January 2006, as restated	438,579	1,518,112	111,358	61,671	52,090	2,181,810
Exchange differences	(713)	363	—	(80)	—	(430)
Depreciation for the year	76,970	111,635	54,174	4,733	—	247,512
Impairment provided for the year	3,217	13,442	6,691	313	1,496	25,159
Elimination on disposals	(27,380)	(102,445)	(33,411)	(23,324)	—	(186,560)
Reclassification	2,164	6,732	(100)	(8,796)	—	—
At 31 December 2006, as restated	492,837	1,547,839	138,712	34,517	53,586	2,267,491
Net book value						
At 31 December 2006, as restated	766,223	512,404	88,305	8,915	236,920	1,612,767

Notes to the Financial Statements

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16. PROPERTY, PLANT AND EQUIPMENT *(continued)*

The net book value of the Group's leasehold land and buildings comprise properties situated on land held under medium-term leases in:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i> (Restated)
PRC, other than in Hong Kong	640,219	700,580
Hong Kong	—	41,990
Japan	23,653	23,653
	663,872	766,223

“Leasehold land and buildings” and “Plant, machinery and equipment” with net book values of approximately RMB444,444,000 (2006 (restated): RMB437,764,000) and RMB21,033,000 (2006: RMB134,584,000) respectively, have been pledged as security for the Group's bank borrowings.

17. INVESTMENT PROPERTIES

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Cost		
At 1 January	28,201	29,201
Exchange differences	(990)	(1,000)
Additions at cost	1,035	—
Disposals	(52,351)	—
Reclassified from property, plant and equipment <i>(Note 16)</i>	81,461	—
At 31 December	57,356	28,201
Accumulated depreciation and impairment		
At 1 January	2,057	1,478
Exchange differences	(44)	(62)
Depreciation for the year	3,687	641
Elimination on disposals	(12,321)	—
Reclassified from property, plant and equipment <i>(Note 16)</i>	25,785	—
At 31 December	19,164	2,057
Carrying amount at 31 December	38,192	26,144
Directors' valuation at fair value	54,698	40,030

The Group's investment properties are situated in the PRC (2006: in Hong Kong) under medium term leases. The valuation for the investment properties at 31 December 2007 were determined by the directors by reference to the market price of similar properties.

Investment properties with net book values of approximately RMB2,568,000 (2006: Nil) has been pledged as security for the Group's bank borrowings.

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18. PAYMENTS FOR LEASEHOLD LAND HELD FOR OWN USE UNDER OPERATING LEASES

The Group's payments for leasehold land held for own use under operating leases comprise:

	2007 RMB'000	2006 RMB'000
Leasehold land in PRC:		
— Medium-term leases	305,392	372,533
Carrying amount at 1 January	372,533	470,080
Reclassified to non-current assets held for sale (<i>Note 28</i>)	(8,152)	—
Additions at cost	16,605	—
Charge for the year	(15,555)	(14,449)
Impairment provided for the year (<i>i</i>)	(17,189)	—
Disposal of a subsidiary (<i>Note 38</i>)	(13,084)	—
Disposals	(29,766)	(83,098)
Carrying amount at 31 December	305,392	372,533

- (i) In July 2004, Shangqiu Kelon Electrical Company Limited (“Shangqiu Kelon”), Shangqiu Bing Xiong Freezing Facilities Company Limited (“Shangqiu Bing Xiong”), and the Administration Committee of Shangqiu Economic and Technological Development Zone (商丘經濟技術開發區管委會) (“Shangqiu Administrative Committee”) entered into a three-party land transfer agreement under which all parties agreed that Shangqiu Kelon acquires a piece of land use right with 187 acres from Shangqiu Bing Xiong at a consideration of approximately RMB36 million. Under the land transfer agreement, it was agreed that Shangqiu Kelon develops the land and meets minimum production and sales requirements after the development is completed. However, the land has not been developed nor has Shangqiu Kelon met the minimum production and sales requirements thereafter. In August 2005, Shangqiu Kelon received a notice from Shangqiu Administrative Committee claiming that it has breached the three-party land transfer agreement for not fulfilling the minimum production and sales requirements and requesting that Shangqiu Kelon surrenders the land use right. The local court froze the land accordingly. The Company has made an impairment loss of approximately RMB18 million against the carrying amount of the land use right for the possible loss that may arise as a result of the event for the year ended 2005. In mid 2007, through a local source, the Company further realised that the land use right has been confiscated by Henan Shangqiu Bureau of Land and Resources (“SQBLR”) in November 2006 for the reason of delayed development. The Company is reviewing the appropriateness of judicial procedure made by SQBLR. At the date of this report, the case is being handled by the Group's lawyer and has not been resolved. The Company has further made an impairment loss of approximately RMB17 million against the carrying amount of the land use right for the maximum loss that may arise as a result of the event. As at 31 December 2007, the Company has provided an impairment loss of approximately RMB 35 million against the carrying amount of the land use right.
- (ii) At 31 December 2007, the carrying amount of payments for leasehold land held for own use under operating leases pledged as security for the Group's bank borrowings amounted to approximately RMB226,035,000 (2006: RMB245,559,000).

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19. INTERESTS IN SUBSIDIARIES

Details of the Company's principal subsidiaries as at 31 December 2007 are listed under a table as follows:

Name	Place and date of incorporation/ establishment	Registered capital	Percentage of ownership/ profit share		Principal activities
			Directly	Indirectly	
Entities operating in the PRC:					
Shunde Rongsheng Plastic Products Co., Ltd.	PRC (i) 18 October 1991	US\$15,800,000	45%	25%	Manufacture of plastic parts
Guangdong Kelon Mould Co., Ltd.	PRC (i) 20 July 1994	US\$15,000,000	40%	30%	Manufacture of moulds
Hisense Ronshen (Guangdong) Refrigerator Co., Ltd.	PRC (i) 25 December 1995	US\$26,800,000	70%	30%	Manufacture and sale of refrigerators
Hisense Ronshen (Guangdong) Freezer Co., Ltd.	PRC (i) 25 December 1995	RMB237,000,000	44%	56%	Manufacture and sale of freezers
Guangdong Kelon Air-Conditioner Co., Ltd.	PRC (i) 19 March 1996	US\$36,150,000	60%	—	Manufacture and sale of air-conditioners
Chengdu Kelon Refrigerator Co., Ltd.	PRC (i) 19 November 1996	RMB200,000,000	75%	25%	Manufacture and sale of refrigerators
Hisense Ronshen Yingkou Refrigerator Co., Ltd.	PRC (i) 15 December 1996	RMB200,000,000	42%	36.79%	Manufacture and sale of refrigerators
Hisense Ronshen Yangzhou Refrigerator Co., Ltd.	PRC (i) 23 December 1996	US\$29,800,000	74.33%	25.67%	Manufacture and sale of refrigerators
Shunde Kelon Household Electrical Appliance Company Limited	PRC (ii) 16 July 1999	RMB10,000,000	25%	75%	Manufacture and sale of electrical household appliances
Guangdong Kelon Fittings Co., Ltd.	PRC (i) 24 November 1999	US\$5,620,000	70%	30%	Manufacture and sale of spare parts for air-conditioners and refrigerators
Shunde Huao Electronics Co., Ltd. ("Huao Electronics")	PRC (ii) 23 November 2000	RMB10,000,000	—	70%	Manufacture and sale of electronic products
Shunde Wangao Import & Export Co., Ltd.	PRC (ii) 7 June 2001	RMB3,000,000	20%	80%	Import and export business
Shunde Jiake Electronic Company Limited	PRC (ii) 12 October 2001	RMB60,000,000	70%	30%	IT and communication technology and micro-electronics technology development

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19. INTERESTS IN SUBSIDIARIES (continued)

Name	Place and date of incorporation/ establishment	Registered capital	Percentage of ownership/ profit share		Principal activities
			Directly	Indirectly	
Entities operating in the PRC: (continued)					
Xi'an Kelon Cooling Co., Ltd. ("Xi'an Kelon")	PRC (ii) 20 March 2002	RMB202,000,000	60%	—	Manufacture and sale of spare parts for refrigerators
Jiangxi Kelon Industrial Development Co., Ltd.	PRC (i) 24 June 2003	US\$29,800,000	60%	40%	Manufacture and sale of refrigerators, air-conditioners and other household appliances
Hangzhou Kelon Electrical Co., Ltd. ("Hangzhou Kelon")	PRC (i) 22 August 2003	RMB 24,000,000	100%	—	Manufacture and sale of refrigerators
Shangqiu Kelon Electrical Co., Ltd.	PRC (ii) 23 September 2003	RMB150,000,000	—	100%	Manufacture and sale of refrigerators
Zhuhai Kelon Industrial Development Co., Ltd.	PRC (i) 3 December 2003	US\$29,980,000	75%	25%	Manufacture and sale of refrigerators
Hisense (Chengdu) Refrigerator Co., Ltd.	PRC (i) 28 March 2007	RMB5,000,000	75%	25%	Manufacture and sale of refrigerators
Entities operating in Hong Kong:					
Pearl River Electric Refrigerator Company Limited	Hong Kong 26 July 1985	HK\$400,000	—	100%	Trading in materials and parts for refrigerators and import and export business
Kelon Electric Appliances Co., Ltd.	Hong Kong 29 August 1991	HK\$10,000	—	100%	Property investment
Kelon Development Company Limited	Hong Kong 17 August 1993	HK\$5,000,000	100%	—	Investment holding
Kelon International Inc.	British Virgin Islands 13 January 1999	US\$50,000	—	100%	Investment holding and sale of refrigerators and air-conditioners

(i) Established as a sino-foreign equity joint venture in the PRC.

(ii) Established as a limited liability company in the PRC.

(iii) The financial statements of Jiangxi Combine Electrical Appliance Co., Ltd. ("Jiangxi Combine") and Kelon Europe Industrial Design Limited ("Kelon Europe") were excluded from the consolidated financial statements. Jiangxi Combine has not commenced active business since its establishment and Kelon Europe has only very limited activities. The management considers that the impact of not consolidating Jiangxi Combine and Kelon Europe is insignificant to the Group.

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19. INTERESTS IN SUBSIDIARIES *(continued)*

None of the subsidiaries had issued any debt securities at the end of the year.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results or assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

20. INTERESTS IN ASSOCIATES

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Share of net assets	82,839	78,981
Goodwill	—	—
	82,839	78,981
Listed investment	78,179	74,478
Unlisted investment	4,660	4,503
	82,839	78,981
Fair value of listed investment	164,070	43,241

Details of the goodwill are as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Cost		
At 1 January	131,207	137,346
Release on dilution in share reform	—	(6,139)
At 31 December	131,207	131,207
Impairment		
At 1 January	131,207	137,346
Release on dilution in share reform	—	(6,139)
At 31 December	131,207	131,207
Carrying amount at 31 December	—	—

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20. INTERESTS IN ASSOCIATES (continued)

Details of the Group's principal associates as at 31 December 2007 are listed under a table as follows:

Name	Place and date of incorporation/ establishment	Registered capital	Percentage of ownership/ profit sharing		Principal activities
			Directly	Indirectly	
Huayi Compressor Holdings Company Limited ("Huayi")	PRC (i) 13 June 1996	RMB324,581,218	18.26% (iii)	—	Manufacture and sale of compressors
Attend Logistics Co., Ltd. ("Attend Logistics")	PRC (ii) 11 July 2001	RMB10,000,000	20%	—	Provision of logistics and storage services

(i) Established as a joint stock limited company.

(ii) Established as a limited liability company.

(iii) On 20 December 2006, Huayi completed a share reform and converted all of its non-freely transferable shares into listed shares by the allocation of 6.674 newly issued shares to each holder of transferable shares for every 10 shares held by such holder. Accordingly, the shares of Huayi held by the Company, which were previously non-transferable, were converted into freely transferable shares of Huayi and the Company's equity interest in Huayi was reduced from 22.73% to 18.26%. A dilution loss incurred on share reform of the associate arising thereon was charged to the income statement. Notwithstanding the share reform of Huayi, the Company continues to possess the power to participate in the financial and operating policy decision of Huayi and account for its interest in Huayi under the equity method.

The above table lists the associates of the Group which, in the opinion of the directors, principally affected the results of the year or formed a substantial portion of the net assets of the Group. To give details of other associates would, in the opinion of the directors, result in particulars of excessive length.

The summarised financial information in respect of the Group's associates is set out below:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Total assets	2,471,410	2,158,965
Total liabilities	(1,831,894)	(1,572,054)
Net assets	639,516	586,911
Revenue	2,766,448	1,842,149
Profit for the year	8,654	16,017

The financial statements of Huayi and Attend Logistics have been audited by Guangdong Hengxin Delu Certified Public Accountants Co., Ltd. and Shinewing Certified Public Accountants respectively.

21. AVAILABLE-FOR-SALE FINANCIAL ASSETS

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Unquoted long-term equity investments in the PRC, at cost	8,469	7,249
Impairment loss	(7,249)	(7,249)
	1,220	—

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22. INTANGIBLE ASSETS

	Trademarks (i) RMB'000	Non-patented technologies (ii) RMB'000	Software systems (ii) RMB'000	Total RMB'000
Year ended 31 December 2007				
Cost				
At 1 January 2007	521,858	537	33,751	556,146
Additions at cost	—	43,711	3,771	47,482
Disposal of a subsidiary (Note 38)	—	—	(8)	(8)
Write off	—	—	(190)	(190)
At 31 December 2007	521,858	44,248	37,324	603,430
Accumulated amortisation and impairment				
At 1 January 2007	403,480	377	26,458	430,315
Charge for the year	—	137	3,782	3,919
Impairment provided for the year	—	—	1,282	1,282
Disposal of a subsidiary (Note 38)	—	—	(8)	(8)
Elimination on write off	—	—	(190)	(190)
At 31 December 2007	403,480	514	31,324	435,318
Carrying amount				
At 31 December 2007	118,378	43,734	6,000	168,112
Year ended 31 December 2006				
Cost				
At 1 January 2006	521,858	537	32,580	554,975
Additions at cost	—	—	1,175	1,175
Write off	—	—	(4)	(4)
At 31 December 2006	521,858	537	33,751	556,146
Accumulated amortisation and impairment				
At 1 January 2006	403,480	241	22,472	426,193
Charge for the year	—	136	3,990	4,126
Elimination on write off	—	—	(4)	(4)
At 31 December 2006	403,480	377	26,458	430,315
Carrying amount				
At 31 December 2006	118,378	160	7,293	125,831

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31 December 2007

22. INTANGIBLE ASSETS (continued)

(i) Impairment tests for trademarks

Trademarks represent the rights of using 「科龍」, 「容聲」 and 「容升」 brands in producing refrigerators and air-conditioners recognised in October 2003.

Prior to 1 January 2005, the cost of trademarks is amortised on a straight-line basis over their estimated useful lives of 10 years. With effect from 1 January 2005 and in accordance with the provisions of IAS 38, trademarks are assessed to have indefinite useful lives and therefore are not amortised but tested for impairment for each reporting date and where an indicator of impairment exists.

Due to the significant loss incurred in 2005 and the business interruption in May 2005, the management conducted an impairment assessment on the trademarks. The recoverable amount of trademarks was determined based on value-in-use calculations with the support of valuation performed by independent third party valuer. As a result of such assessment, trademarks had been assessed to be impaired by approximately RMB338,247,000 as at 31 December 2005.

As at 31 December 2007, the management performed self-assessment and concluded that there was no further impairment identified.

Details of trademarks allocated to cash generating units for which the amount of trademarks so allocated is significant in comparison to total trademarks are as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Air-conditioners	38,473	38,473
Refrigerators	79,905	79,905
	118,378	118,378

The recoverable amounts of Segment Air-conditioners and Segment Refrigerators have been determined from value in use calculations based on cash flow projections from formally approved budgets covering a five-year period to 31 December 2012 with a discount rate of 15%. The cash flows beyond the five-year period are extrapolated using a steady 2% growth rate. The resulting value of the trademarks as at 31 December 2007 was higher than their carrying amount. Management believes that any possible change in any of these assumptions would not cause the aggregate carrying amount to exceed the aggregate recoverable amount.

- (ii) Non-patented technologies and software systems are amortised over their estimated useful lives of 4 to 5 years.

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31 December 2007

23. GOODWILL

RMB'000

Year ended 31 December 2007

Cost

At 1 January 2007 and 31 December 2007 **47,033**

Impairment

At 1 January 2007 and 31 December 2007 **47,033**

Carrying amount

At 31 December 2007 **—**

Year ended 31 December 2006

Cost

At 1 January 2006 and 31 December 2006 **47,033**

Impairment

At 1 January 2006 and 31 December 2006 **47,033**

Carrying amount

At 31 December 2006 **—**

24. DEFERRED TAX ASSETS

Deferred tax assets of the Group were arising from deductible temporary differences and tax losses. Net movement for the year is as follows:

	2007	2006
	<i>RMB'000</i>	<i>RMB'000</i>
At 1 January	21,387	—
Recognition for the year	7,183	21,387
Utilisation of tax losses for the year	(9,317)	—
Effect of change in tax rate	(7,953)	—
At 31 December	11,300	21,387

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24. DEFERRED TAX ASSETS (continued)

The following are the major deferred tax assets / (liabilities) and movements thereon for the year:

Assets / (liabilities)	Depreciation allowance and provisions <i>RMB'000</i>	Tax losses <i>RMB'000</i>	Total <i>RMB'000</i>
At 1 January 2006	—	—	—
Credit to income statement for the year	—	21,387	21,387
At 31 December 2006	—	21,387	21,387
Credit/(charge) to income statement for the year	7,183	(9,317)	(2,134)
Effect of change in tax rate	—	(7,953)	(7,953)
At 31 December 2007	7,183	4,117	11,300

For the purpose of balance sheet presentation, certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances for financial reporting purposes:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Deferred tax assets	11,300	21,387

The unused tax losses carried forward and deductible temporary differences not recognised in the consolidated financial statements due to unpredictability of future profit streams are as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Unused tax losses	2,170,960	1,846,123
Deductible temporary differences	911,032	691,429
	3,081,992	2,537,552

The PRC tax losses can only be carried forward for a maximum period of five years and the Hong Kong tax losses can be carried forward indefinitely. The expiry of unused tax losses for which no deferred tax assets have been recognised is as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Tax losses will expire in 2007	—	15,179
Tax losses will expire in 2008	7,068	25,601
Tax losses will expire in 2009	44,748	55,489
Tax losses will expire in 2010	1,097,025	1,235,871
Tax losses will expire in 2011	649,153	276,859
Tax losses will expire in 2012	145,268	—
Tax losses can be carried forward indefinitely	227,698	237,124
	2,170,960	1,846,123

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25. INVENTORIES

	2007 RMB'000	2006 RMB'000
Raw materials	195,695	184,013
Work in progress	42,333	33,745
Finished goods	702,256	702,079
	940,284	919,837

As at 31 December 2007, the carrying amount of inventories pledged for bank borrowings amounted to approximately RMB40,000,000 (2006: RMB140,236,000).

26. TRADE AND OTHER RECEIVABLES

	2007 RMB'000	2006 RMB'000
Trade receivables (i)	442,835	290,166
Notes receivable	2,740	77,317
Other receivables	540,497	376,838
Amounts due from Greencool Enterprise and its affiliates (Note 35 III a)	72,061	72,061
Amounts due from companies suspected to be connected with Mr. Gu (Note 35 III b)	214,217	214,217
Amounts due from Hisense Group (Note 35 III c)	28,821	2,187
Amounts due from associates (Note 35 III d)	322	40
Amounts due from other related companies (Note 35 III e)	5,716	86,907
	1,307,209	1,119,733

- (i) As at 31 December 2007, included in trade and notes receivable was an amount of RMB73,072,000 (2006: RMB28,200,000) being pledged for bank borrowings.

The aging analysis of trade receivables is as follows:

	2007 RMB'000	2006 RMB'000
Within three months	396,038	252,966
Three to six months	34,126	30,938
Six months to one year	13,695	9,691
Over one year	186,423	194,211
Less: Provision for impairment of trade receivables	(187,447)	(197,640)
At 31 December	442,835	290,166

Normal credit term of 30 days is granted to customers. The Group allows a credit period of up to one year for large and well-established customers. Sales are usually settled by cash on delivery for small and new customers. Trade receivables are non-interest bearing.

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26. TRADE AND OTHER RECEIVABLES *(continued)*

(i) *(continued)*

The aging analysis of trade receivables using allowed credit term is as follows:

	2007	2006
	RMB'000	RMB'000
Current <i>(Note a)</i>	408,821	274,119
Less than three months past due	20,311	11,071
More than three months but less than twelve months past due	13,531	3,335
More than twelve months past due	172	1,641
Amount past due at balance sheet date but not impaired <i>(Note b)</i>	34,014	16,047
At 31 December	442,835	290,166

(a) The balance that was neither past due nor impaired related to a wide range of customers for whom there was no recent history of default.

(b) The balance that was past due but not impaired related to a number of customers that had a good track record with the Group. Based on the past experience, the management estimated that the carrying amounts could be fully recovered.

(ii) Other receivables principally comprised of receivable from disposal of payments for leasehold land held for own use under operating leases, investment properties and value-added tax recoverable of RMB251,065,000, RMB5,233,000 and RMB147,308,000 respectively. The management has assessed the recoverability of the balance of other receivables and considered no further provision for impairment is needed.

(iii) The below table reconciled the allowance of impairment loss on trade and other receivables for the year:

	2007	2006
	RMB'000	RMB'000
At 1 January	676,758	762,882
Impairment loss recognised	13,546	—
Bad debt written off	(41,508)	(25,112)
Reversal of impairment loss previously recognised	(69,636)	(61,012)
At 31 December	(579,160)	676,758

The Group recognised impairment loss on trade and other receivables by individual assessment based on the accounting policy stated in Note 4(k)(ii).

(iv) As at 31 December 2007, the Group has trade and other receivables denominated in USD of approximately RMB245,000,000 (2006: RMB179,000,000).

(v) As at 31 December 2007 and 2006, accumulated impairment loss of approximately RMB344,968,000 and RMB18,985,000 were recorded in respect of amounts due from companies suspected to be connected with Mr. Gu and amounts due from Greencool Enterprise and its affiliates.

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27. OTHER FINANCIAL ASSETS AND LIABILITIES

During the year, the Group entered into foreign exchange forward contracts to manage its exchange rate exposures arising from ordinary course of business. The instruments purchased are primarily denominated in the currencies of the Group's principal markets. At the balance sheet date, the total notional amount of outstanding foreign exchange forward contracts to which the Group has committed are as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Foreign exchange forward contracts:		
— contracted to buy foreign currency	413,831	—
— contracted to sell foreign currency	411,511	—

The fair value gain/(loss) of the forward exchange contracts for the year ended 31 December 2007 is estimated to be approximately RMB3,104,000 (2006: Nil) and it was recognised in the consolidated income statements. The gain/(loss) is calculated based on market values of equivalent instruments at the balance sheet date.

28. NON-CURRENT ASSETS HELD FOR SALE

In May 2007, the directors resolved to dispose certain factories, warehouses and offices of the Group. The sale transactions will be completed in early next year. As at 31 December 2007, the properties with carrying amount of approximately RMB20,369,000 have been classified as non-current assets held for sale.

29. TRADE AND OTHER PAYABLES

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Trade payables	1,152,853	1,415,803
Notes payable	770,960	507,918
Other payables	616,756	486,073
Accruals	165,679	140,678
Amounts due to Greencool Enterprise and its affiliates (<i>Note 35 III a</i>)	13,050	13,050
Amounts due to companies suspected to be connected with Mr. Gu (<i>Note 35 III b</i>)	118,461	119,316
Amounts due to Hisense Group (<i>Note 35 III c</i>)	205,184	319,526
Amounts due to associates (<i>Note 35 III d</i>)	40,200	51,680
Amounts due to other related companies (<i>Note 35 III e</i>)	10,038	39,912
	3,093,181	3,093,956

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29. TRADE AND OTHER PAYABLES *(continued)*

The aging analysis of trade payables is as follows:

	2007	2006
	RMB'000	RMB'000
Within one year	995,092	1,177,093
One to two years	70,838	196,857
Two to three years	64,796	30,937
Over three years	22,127	10,916
	1,152,853	1,415,803

As at 31 December 2007, the Group has trade and other payables denominated in USD of approximately RMB45,000,000 (2006: RMB31,000,000).

30. PROVISIONS

	Warranty (i)	Legal (ii)	Total
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
At 1 January 2007	165,783	4,212	169,995
Additional provision in the year	66,643	10,471	77,114
Utilisation of provision	(99,006)	(4,097)	(103,103)
At 31 December 2007	133,420	10,586	144,006
At 1 January 2006	204,179	5,737	209,916
Additional provision in the year	90,427	5,444	95,871
Utilisation of provision	(128,823)	(6,969)	(135,792)
At 31 December 2006	165,783	4,212	169,995

- (i) The Group provides free repairing services on its products and free replacement of the major components of its products for one to three years after date of sale. The warranty provision is estimated by management based on past experience. The assumptions used to estimate the warranty provision are reviewed periodically in light of actual results.
- (ii) The Group is currently involved in a number of legal disputes. The amount provided represents the directors' best estimate of the Group's liability having taken legal advice. Uncertainties exist as to whether claims will be settled out of court or if not whether the Group is successful in defending any action.

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31. OTHER LIABILITIES

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Employee benefits (i)	30,820	32,620
Government grants (ii)	24,973	27,952
	55,793	60,572
Amounts due within one year:		
— Employee benefits (i)	30,820	19,026
— Government grants (ii)	24,973	27,952
	55,793	46,978
Amounts due after one year	—	13,594
(i)	The amounts represent accrued contributions to a defined contribution pension scheme for its employees during the period from 1993 to 2001. Settlement of employee benefits payable was mutually agreed by the Company and the committee of the Company's staff union.	
(ii)	The amounts represent government grants received for the Group's research and development activities. Government grants recognised as income for the year amounted to approximately RMB6,236,000 (2006: RMB70,511,000).	

32. BANK BORROWINGS

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Short-term bank loans due within one year	1,310,972	1,556,702
Analysed as:		
Secured	773,812	1,233,294
Unsecured	537,160	323,408
	1,310,972	1,556,702

As at 31 December 2007, the Group has outstanding short-term loans in the aggregate of approximately RMB1,311,972,000 (2006: RMB1,556,702,000) of which approximately RMB18,000,000 (2006: RMB385,000,000) were overdue. The Group negotiated with bankers to refinance the short-term bank loans which are due in 2007. Based on discussion with the Group's bankers to date, the directors expect that these borrowings will be renewed in due course.

The bank borrowings carry interest at fixed rates ranging from 5.47% to 8.35% (2006: 4.65% to 7.84%) per annum. Bank borrowings of approximately RMB773,812,000 (2006: RMB1,233,294,000) were secured by pledge of property, plant and equipment (Note 16), investment properties (Note 17), payments for leasehold land held for own use under operating leases (Note 18), inventories (Note 25) and trade and notes receivable (Note 26).

At 31 December 2007, included in bank borrowings were amount of approximately RMB9,000,000 (2006: Nil) in respect of financial guarantees provided to banks in favor of certain distributors of the Group on bank acceptance notes. Under the guarantee arrangements, the Group assumed the repayment responsibilities of the bank acceptance notes after it utilised the credit facilities granted to the distributors by such banks. The management assessed that the guarantee arrangements would not result in the Group picking up additional credit risks or financial contingencies in favor of the distributors. These financing arrangements would however result in a reclassification of trade deposits received to bank borrowings.

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32. BANK BORROWINGS *(continued)*

At 31 December 2007, included in bank borrowings was an amount of approximately RMB89,946,000 (2006: RMB218,000,000) in respect of notes and trade receivables factored to banks with recourse.

33. SHARE CAPITAL

	2007 RMB'000	2006 RMB'000
Share of RMB1 each:		
314,587,227 (2006:337,986,755) transferable shares that are subject to selling restrictions	314,587	337,987
459,589,808 (2006: 459,589,808) H shares	459,590	459,590
217,829,528 (2006: 194,430,000) A shares	217,830	194,430
	992,007	992,007

- (i) During the year ended 31 December 2007, the Company announced a proposed share reform including conversion of all the non-freely transferable shares into transferable shares of the Company and allocation of 1.2 newly issued shares to each holders of transferable A shares for every 10 transferable shares held by such holders of A shares and such share reform was completed in March 2007.

As a result of the share reform, the 262,212,194 Domestic shares which are non-freely transferable shares held by Hisense Air-Conditioner was converted into 238,872,074 transferable shares that are subject to certain selling restrictions of the Company, representing 24.08% of the Company's total capital.

Except for the currency in which dividends are paid and the restrictions as to whether the shareholders can be PRC investors or foreign investors, Domestic shares, H shares and A shares rank *pari passu* in all respects with each other.

- (ii) The Group's objectives when managing capital are:

- to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and
- to provide an adequate return to shareholders by pricing products and services commensurate with the level of risk.

The Group sets the amount of capital in proportion to risk. The Group manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or sell assets to reduce debt.

Consistent with others in the industry, the Group monitors capital on the basis of the debt-to-adjusted capital ratio. This ratio is calculated as net debt divided by adjusted capital. Net debt is calculated as total debt (as shown in the balance sheet) less cash and cash equivalents. Adjusted capital comprises all components of equity.

During 2007, the Group's strategy, which was unchanged from 2006 was to substantially finance through debt as the Group has deficiency in equity of RMB629,774,000 (2006 (restated): RMB727,931,000). At 31 December 2007, the bank borrowings were approximately RMB1,310,972,000 (2006: RMB1,556,702,000) (*Note 32*).

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34. LEASES

Operating leases – lessee

The Group leases certain leasehold land and buildings and plant and machinery under operating lease arrangements with lease terms ranging from one to five years. The operating lease charges for the year ended 31 December 2007 was as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Operating lease charges		
— leasehold land and buildings	40,434	63,855
— plant and machinery	250	6,500

The total future minimum lease payments under non-cancellable operating leases are due as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Not later than one year	2,196	2,590
Later than one year and not later than five years	457	1,116
	2,653	3,706

Operating leases – lessor

The Group's investment properties are also leased to a number of tenants for varying terms. The sub-lease rental income for the year ended 31 December 2007 was RMB 20,721,000 (2006: RMB 7,723,000).

The minimum rent receivables under non-cancellable operating leases are as follows:

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Not later than one year	3,523	60
Later than one year and not later than five years	8,397	—
	11,920	60

35. RELATED PARTY TRANSACTIONS

Transactions between the Company and its subsidiaries, which are related parties of the Company have been eliminated on consolidation and are not disclosed in this note.

As at 31 December 2007, Hisense Air-Conditioner held 238,872,074 shares of the Company, representing 24.08% of total share capital of the Company.

During the period from 2001 to 2005, the Group had significant transactions and relationships with Greencool Enterprise and its affiliates. The Group also had entered into a series of activities/transactions with companies suspected to be connected with Mr. Gu. Upon the completion of share transfer, Mr. Gu, Greencool Enterprise and its affiliates were no longer connected with the Group. Accordingly, no related party disclosure was made in respect of Mr. Gu, Greencool Enterprise and its affiliates for the year.

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35. RELATED PARTY TRANSACTIONS *(continued)*

During the year, the Group entered into a Business Co-operation Framework Agreement with Hisense Group Company and certain of its subsidiaries (hereinafter collectively referred to as the “Hisense Group”). The Business Co-operation Framework Agreement is valid for a term of one year commencing from 1 January 2007. Pursuant to the Business Co-operation Framework Agreement, the Group agrees to sell and supply moulds, air-conditioners, refrigerators and raw materials to Hisense Group, purchase air-conditioners, refrigerators and raw materials from Hisense Group and Hisense Group agrees to render repair and maintenance services for electrical appliances to the Group. The details of the transactions with Hisense Group are disclosed in note 35 II(b).

I. Relationship with related parties

During the year, for the purpose of this report, the directors are of the view that the following companies are related parties of the Group:

Name of related parties	Relationship
Hisense Air-Conditioner	The substantial shareholder of the Company
Hisense Group Company	The holding company of Hisense Air-Conditioner
Qingdao Hisense Marketing Co., Ltd. (“Hisense Agent”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense Electric Co., Ltd. (“Hisense Electric”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense (Zhejiang) Air-Conditioner Co., Ltd. (“Hisense Zhejiang”)	A subsidiary of Hisense Air-Conditioner
Hisense (Shandong) Air-Conditioner Co., Ltd. (“Hisense Shandong”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense (Nanjing) Electric Co., Ltd. (“Hisense Nanjing”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense (Beijing) Electric Co., Ltd. (“Hisense Beijing”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense (Qingdao) Import & Export Co., Ltd. (“Hisense Import & Export”)	A fellow subsidiary of Hisense Air-Conditioner
Hisense Hitachi Air Conditioning Co., Ltd. (“Hisense Hitachi”)	A fellow subsidiary of Hisense Air-Conditioner
Savor Household Electrical Appliance Service Industry Co., Ltd. (“Savor Service”)	A fellow Subsidiary of Hisense Air-Conditioner

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35. RELATED PARTY TRANSACTIONS *(continued)*

I. Relationship with related parties *(continued)*

Name of related parties	Relationship
Chongqing Kelon Rongsheng Refrigerator Sales Co., Ltd. (“Chongqing Rongsheng”)	An associate of the Group
Attend Logistics	An associate of the Group
Huayi	An associate of the Group
Jiaxibeila Compressor Company Limited (“Jiaxibeila”)	A subsidiary of an associate of the Group
Kelon Europe	An unconsolidated subsidiary of the Company
Jiangxi Combine	An unconsolidated subsidiary of the Company
Chengdu Engine (Group) Company Limited (“Chengdu Engine”)	A minority investor of Chengdu Kelon before 24 April 2007
Chengdu Xinxing Electrical Appliance Holdings Company Limited (“Chengdu Xinxing”)	An associate of Chengdu Engine
Hangzhou Xileng Group Company Limited (“Hangzhou Xileng”)	A minority investor of Hangzhou Kelon before 5 December 2007
Xi’an Gaoke (Group) Limited (“Xi’an Gaoke”)	A minority investor of Xi’an Kelon
Shunde Yunlong Consultancy (“Shunde Yunlong”)	A minority investor of Huaao Electronics

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35. RELATED PARTY TRANSACTIONS *(continued)*

I. Relationship with related parties *(continued)*

For the purpose of this report, the directors are of the views that the following companies controlled by or suspected to be connected with Mr. Gu are no longer related to the Group starting from 13 December 2006 due to the completion of the share transfer transaction between Greencool Enterprise and Hisense Air-Conditioner. As a result, transactions with Mr. Gu, Greencool Enterprise and its affiliates and companies suspected to be connected with Mr. Gu for the year ended 31 December 2007 are not classified as related party transactions.

Name of related parties	Relationship
Greencool Enterprise	The former single largest shareholder of the Company
Mr. Gu	The beneficial owner of Greencool Enterprise and also the former executive director of the Company
Greencool Technology Development (Shenzhen) Company Limited (“Shenzhen Greencool Technology”)	A company controlled by Mr. Gu
Greencool Environmental Protection Engineering (Shenzhen) Company Limited (“Shenzhen Greencool Environmental”)	A company controlled by Mr. Gu
Greencool Refrigerant (China) Company Limited (“Greencool China”)	A company controlled by Mr. Gu
Hainan Greencool Environmental Protection Engineering Company Limited (“Hainan Greencool”)	A company controlled by Mr. Gu
Greencool Procurement (Shenzhen) Co., Ltd. (“Greencool Procurement”)	A company controlled by Mr. Gu
Hefei Meiling Holdings Limited (“Hefei Meiling”)	A company controlled by Mr. Gu

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35. RELATED PARTY TRANSACTIONS *(continued)*

I. Relationship with related parties *(continued)*

Name of related parties	Relationship
Jiangxi Greencool Electrical Appliance Company Limited (“Jiangxi Greencool”)	A company controlled by Mr. Gu
Yangzhou Yaxing Motor Coach Company Limited (“Yangzhou Yaxing”)	A company controlled by Mr. Gu
Chengdu Refrigerating Components Factory (“Chengdu Refrigerating”)	A company suspected to be connected with Mr. Gu
Hefei Weixi Electrical Appliance Company Limited (“Hefei Weixi”)	A company suspected to be connected with Mr. Gu
Jiangxi Keda Plastic Technology Company Limited (“Jiangxi Keda”)	A company suspected to be connected with Mr. Gu
Jiangxi Kesheng Trading Company Limited (“Jiangxi Kesheng”)	A company suspected to be connected with Mr. Gu
Jinan San’ai’fu Chemical Company Limited (“Jinan San’ai’fu”)	A company suspected to be connected with Mr. Gu
Tianjin Lixin Trading Development Company Limited (“Tianjin Lixin”)	A company suspected to be connected with Mr. Gu
Tianjin Taijin Yunye Company Limited (“Tianjin Taijin Yunye”)	A company suspected to be connected with Mr. Gu
Tianjin Xiangrun Trading Development Company Limited (“Tianjin Xiangrun”)	A company suspected to be connected with Mr. Gu
Wuhan Changrong Electrical Appliance Company Limited (“Wuhan Changrong”)	A company suspected to be connected with Mr. Gu

Notes to the Financial Statements

31 December 2007

35. RELATED PARTY TRANSACTIONS *(continued)*

I. Relationship with related parties *(continued)*

Name of related parties	Relationship
Zhongshan Dongyue Electrical Company Limited ("Zhongshan Dongyue")	A company suspected to be connected with Mr. Gu
Zhejiang Guoda Trading Company Limited ("Zhejiang Guoda")	A company suspected to be connected with Mr. Gu
Zhejiang Yuhuan Compressor Factory ("Zhejiang Yuhuan")	A company suspected to be connected with Mr. Gu
Beijing De Heng Solicitors ("Beijing De Heng")	A company suspected to be connected with Mr. Gu
Zhuhai Defa Air-conditioner Fittings Company Limited ("Zhuhai Defa")	A company suspected to be connected with Mr. Gu
Zhuhai Longjia Refrigerating Plant Company Limited ("Zhuhai Longjia")	A company suspected to be connected with Mr. Gu

II. Transactions with related parties

(a) Transactions with Greencool Enterprise and its affiliates

The Group had the following significant transactions with Greencool Enterprise and its affiliates that were carried out in the normal course of business:

	2006 RMB'000
Loan guarantee provided by Greencool Enterprise	
— maximum amount during the year	327,971
— amount as at 31 December	85,709

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35. RELATED PARTY TRANSACTIONS *(continued)*

II. Transactions with related parties *(continued)*

(b) Transactions with Hisense Group

The Group had the following significant transactions with Hisense Group:

	<i>Notes</i>	2007 RMB'000	2006 RMB'000
Sales of goods/raw materials to			
— Hisense Shandong	<i>(i)</i>	132,725	—
— Hisense Agent	<i>(i)</i>	192	1,572,695
— Hisense Zhejiang	<i>(i)</i>	9,693	7,253
— Hisense Import & Export	<i>(i)</i>	6	266
— Hisense Beijing	<i>(i)</i>	110,303	—
— Hisense Nanjing	<i>(i)</i>	429	—
— Hisense Hitachi	<i>(i)</i>	—	286
Sales of property, plant and equipment to			
— Hisense Zhejiang		—	300
— Hisense Shandong		8	—
Sales of moulds to			
— Hisense Electric	<i>(i)</i>	—	2,554
— Hisense Agent	<i>(i)</i>	—	649
Agency fee paid/payable to			
— Hisense Agent	<i>(ii)</i>	—	13,178
Loan interest payable to			
— Hisense Agent		8,684	16,390
Purchases of goods/raw materials from			
— Hisense Air-Conditioner	<i>(i)</i>	—	18
— Hisense Shandong	<i>(i)</i>	120,923	—
— Hisense Agent	<i>(i)</i>	—	209,729
— Hisense Zhejiang	<i>(i)</i>	334,424	69,854
— Hisense Nanjing	<i>(i)</i>	105,329	1,830
— Hisense Beijing	<i>(i)</i>	15	5,520
— Hisense Electric	<i>(i)</i>	32	—
Purchases of property, plant and equipment from			
— Hisense Shandong		32	—
— Hisense Beijing		19	—

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35. RELATED PARTY TRANSACTIONS *(continued)*

II. Transactions with related parties *(continued)*

(b) Transactions with Hisense Group (continued)

	2007	2006
	RMB'000	RMB'000
Repair and maintenance services provided by Savor Service	1,944	—
Loan and note payables guarantee provided by Hisense Group Company		
— amount as at 31 December	1,141,500	—

- (i) Sales and purchases were conducted in accordance with mutually agreed terms with reference to the market rates.
- (ii) Agency fee was based on 1% of the total amount of sales proceeds of products under the sales agency agreement. On 10 May 2006, the sales agency agreement expired.

(c) Transactions with associates

The Group had the following significant transactions with associates:

	<i>Notes</i>	2007	2006
		RMB'000	RMB'000
Sales of goods/raw materials to			
— Chongqing Rongsheng	<i>(i)</i>	64,756	39,601
— Huayi and Jiaxibeila	<i>(i)</i>	18	356
Purchases of goods/ raw materials from			
— Huayi and Jiaxibeila	<i>(ii)</i>	221,801	127,978
Service fee charged to			
— Attend Logistics		103	103
— Hisense Zhejiang		75	—
Logistics management fee/ warehouse rental paid to			
— Attend Logistics	<i>(iii)</i>	29,657	51,538

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35. RELATED PARTY TRANSACTIONS *(continued)*

II. Transactions with related parties *(continued)*

(c) Transactions with associates (continued)

- (i) Sales were conducted in accordance with mutually agreed terms with reference to the market rates.
- (ii) Huayi and Jiaxibeila mainly provide compressors to the Group for production of air-conditioners and refrigerators.
- (iii) The Group and Attend Logistics entered into a logistics service agreement, pursuant to which Attend Logistics provides transportation and warehousing service to the Group. The service fee is based on the actual volume of goods, the distance delivered, the occupancy space of warehouse and charged at a pre-determined rate agreed by both parties.

(d) Transactions with other related parties

The Group had the following significant transactions with other related parties:

	<i>Notes</i>	2007 RMB'000	2006 RMB'000
Sales of goods/raw materials to			
— Chengdu Xinxing		—	3,337
Purchases of goods/raw materials from			
— Chengdu Xinxing		—	25,236
Water and electricity expenses paid to			
— Chengdu Engine	<i>(i)</i>	7,057	6,468
Lease payment in respect of plant and equipment to			
— Hangzhou Xileng	<i>(ii)</i>	—	6,000

- (i) Water and electricity expenses are charged at cost.
- (ii) Lease payment in respect of plant and equipment to Hangzhou Xileng is determined by reference to an equipment lease agreement entered into between Hangzhou Kelon and Hangzhou Xileng. The lease was terminated by a mutual agreement signed on 14 October 2007 and the lease payment accrued for the year was waived accordingly.

Notes to the Financial Statements

31 December 2007

35. RELATED PARTY TRANSACTIONS (continued)

III. Balances with related parties

(a) Balances with Greencool Enterprise and its affiliates

	2006 RMB'000
Included in trade and other receivables, net	
— Greencool Enterprise	6,085
— Hainan Greencool	976
— Shenzhen Greencool Technology	32,000
— Shenzhen Greencool Environmental	33,000
	<hr/> 72,061
Included in trade and other payables	
— Hefei Meiling	50
— Jiangxi Greencool	13,000
	<hr/> 13,050

Amounts due from/to Greencool Enterprise and its affiliates are unsecured, interest-free and repayable on demand.

As at 31 December 2006, accumulated impairment loss of approximately RMB18,985,000 was recorded in respect of amounts due from Greencool Enterprise and its affiliates.

(b) Balances with companies suspected to be connected with Mr. Gu

	2006 RMB'000
Included in trade and other receivables, net	
— Beijing De Heng	1,000
— Hefei Weixi	10,424
— Jiangxi Keda	6,500
— Jiangxi Kesheng	6,072
— Jinan San'ai'fu	56,683
— Tianjin Lixin	44,800
— Tianjin Xiangrun	48,199
— Wuhan Changrong	15,539
— Zhuhai Defa	10,700
— Zhuhai Longjia	14,300
	<hr/> 214,217
Included in trade and other payables	
— Tianjin Taijin Yunye	65,000
— Zhongshan Dongyue	4,377
— Zhuhai Longjia	28,316
— Zhuhai Defa	21,400
— Zhejiang Yuhuan	223
	<hr/> 119,316

Notes to the Financial Statements

31 December 2007

35. RELATED PARTY TRANSACTIONS *(continued)*

III. Balances with related parties *(continued)*

(b) Balances with companies suspected to be connected with Mr. Gu (continued)

Amounts due from/to companies suspected to be connected with Mr. Gu are unsecured, interest-free and repayable on demand.

As at 31 December 2006, accumulated impairment loss of approximately RMB344,968,000 was recorded in respect of amounts due from companies suspected to be connected with Mr. Gu.

(c) Balances with Hisense Group

	2007 RMB'000	2006 RMB'000
Included in trade and other receivables, net		
— Hisense Agent	47	540
— Hisense Air-Conditioner	675	335
— Hisense Zhejiang	—	582
— Hisense Nanjing	—	730
— Hisense Beijing	28,066	—
— Savor Service	33	—
	28,821	2,187
Included in trade and other payables		
— Hisense Air-Conditioner	58	9,281
— Hisense Shandong	54,487	—
— Hisense Agent	38,785	309,965
— Hisense Beijing	—	1
— Hisense Nanjing	545	279
— Hisense Zhejiang	109,236	—
— Savor Service	2,073	—
	205,184	319,526

Amounts due from Hisense Group are unsecured, interest-free and are repayable in accordance with normal commercial terms.

Amounts due to Hisense Group are unsecured, interest-free and repayable on demand.

Notes to the Financial Statements

31 December 2007

35. RELATED PARTY TRANSACTIONS *(continued)*

III. Balances with related parties *(continued)*

(d) Balances with associates

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Included in trade and other receivables, net		
— Chongqing Rongsheng	317	—
— Attend Logistics	5	40
	322	40
Included in trade and other payables		
— Attend Logistics	7,998	20,652
— Chongqing Rongsheng	207	4,083
— Huayi and Jiaxibeila	31,995	26,945
	40,200	51,680

Amounts due from/to associates are unsecured, interest-free and are repayable in accordance with normal commercial terms.

(e) Balances with other related companies

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Included in trade and other receivables, net		
— Chengdu Engine	—	47,191
— Chengdu Xinxing	—	34,000
— Kelon Europe	5,716	5,716
	5,716	86,907
Included in trade and other payables		
— Chengdu Engine	109	5,309
— Chengdu Xinxing	—	11,946
— Hangzhou Xileng	2,471	15,772
— Jiangxi Combine	5,100	5,100
— Xi'an Gaoke	2,358	1,785
	10,038	39,912

Notes to the Financial Statements

31 December 2007

35. RELATED PARTY TRANSACTIONS *(continued)*

III. Balances with related parties *(continued)*

(e) Balances with other related companies (continued)

Amounts due from/to other related companies are unsecured, interest-free and are repayable on demand.

As at 31 December 2007, impairment losses of approximately RMB4,455,000 (2006: RMB4,526,000) were recorded in respect of amounts due from other related companies.

IV. Key management personnel emoluments

	2007 <i>RMB'000</i>	2006 <i>RMB'000</i>
Basic salaries, allowances and benefits-in-kind	4,692	7,422
Defined contribution pension cost	90	34
	<hr/> 4,782	<hr/> 7,456

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, including directors and other senior management, totaling 18 individuals (2006: 33 individuals).

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group is exposed through its operations to one or more of the following financial risks:

- Interest rate risk
- Foreign currency risk
- Liquidity risk
- Credit risk

The Group does not hold or issue any financial derivatives for trading purpose.

Interest rate risk

The Group is exposed to interest rate risks due to changes in interest rates of interest-bearing financial assets and liabilities. Interest-bearing financial assets are mainly deposits with banks which are mostly short-term in nature whereas interest-bearing financial liabilities are primarily short-term bank borrowings. As at 31 December 2007, the Group's short-term bank borrowings were carried at fixed interest rates, and therefore not significantly exposed to both fair value and cash flow interest rate risks.

Notes to the Financial Statements

31 December 2007

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Interest rate risk *(continued)*

The following table indicates the approximate change in the profit after tax in response to reasonably possible changes in an interest rate to which the Group has exposure at the balance sheet date. In determining the effect on profit after tax on the next accounting period until next balance sheet date, the management assumes that the change in interest rate had occurred at the balance sheet date and all other variables remain constant. There is no change in the methods and assumptions used in 2006 and 2007.

	2007 Effect on profit after tax RMB'000	2006 Effect on profit after tax RMB'000
Increase by 100 basis points	(3,000)	(1,000)
Decrease by 100 basis points	3,000	1,000

Foreign currency risk

Foreign exchange risk is the risk of loss due to adverse movements in exchange rates relating to investments and transactions denominated in foreign currencies. The Group's monetary assets and transactions are mainly denominated in RMB, USD and GBP. The exchange rates between RMB, USD and GBP are not pegged, and there is fluctuation of exchange rates between RMB, USD and GBP. The Group currently does not have a foreign currency hedging policy. However, the management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arise.

Certain companies in the Group use foreign exchange forward contracts when major fluctuation in the relevant foreign currency is anticipated to manage their foreign exchange risk arising from future commercial transactions, recognised assets and liabilities and net investments in foreign operations.

The carrying amounts of the Group's monetary assets and monetary liabilities denominated in foreign currency at the reporting date are as follows:

	Liabilities		Assets	
	2007	2006	2007	2006
	RMB'000	RMB'000	RMB'000	RMB'000
USD	1,273,645	527,313	450,298	423,771
GBP	521,614	—	46,042	—
Euro	48,764	563	28,425	3,063

Notes to the Financial Statements

31 December 2007

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Foreign currency risk *(continued)*

The sensitivity analysis on foreign exchange risk includes monetary financial assets and liabilities that are denominated in a foreign currency, i.e. in a currency other than the functional currency in which they are measured. The following table indicates the approximate effect on the profit after tax in the next accounting period and the effect on other component of equity at one year after balance sheet date in response to reasonably possible changes in exchange rates to which the company has significant exposure at the balance sheet date.

	2007	2006
	Effect on	Effect
	profit	on profit
	after tax	after tax
	RMB'000	RMB'000
USD to RMB		
Appreciates by 1%	(6,010)	(756)
Depreciates by 1%	6,010	756
GBP to RMB		
Appreciates by 6%	(20,830)	N/A
Depreciates by 6%	20,830	N/A
Euro to RMB		
Appreciates by 9%	(1,336)	(164)
Depreciates by 9%	1,336	164

Liquidity risk

In the management of liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by management to finance the Group's operations and mitigate the effects of short-term fluctuations in cash flows. The Group's treasury department is responsible for maintaining a balance between continuity and flexibility of funding through the use of bank facilities in order to meet the Group's liquidity requirements. All of the debts of the Group would mature in less than one year as at 31 December 2007.

The contractual maturities of financial liabilities are shown as below:

	2007	2006
	RMB'000	RMB'000
Current	868,417	1,128,137
Within six months	2,823,675	2,989,792
Within one year	1,246,105	539,000
	4,938,197	4,656,929

Notes to the Financial Statements

31 December 2007

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Credit risk

It is the risk that a counterparty is unable to pay amount in full when due. It arises primarily from the Group's trade receivables and amounts due from related parties. The Group limits its exposure to credit risk by vigorously selecting counterparties. There is no concentration of credit risk. The Group mitigates its exposure to risk relating to accounts receivable by dealing with diversified customers with sound financial standing. Certain new customers are required to place cash deposits with the Group to reduce the maximum exposure to credit risk. The Group seeks to maintain strict control over its outstanding receivables and has a credit control policy to minimise credit risk. In addition, all receivable balances are monitored on an ongoing basis and overdue balances are followed up by senior management.

The maximum exposure to credit risk at reporting date is the carrying amount of each class of financial assets is shown on the balance sheet.

37. ACQUISITION OF FURTHER EQUITY INTERESTS IN A SUBSIDIARY

On 24 April 2007, the Company acquired an additional 30% shareholding in a subsidiary, Chengdu Kelon, from Chengdu Engine. After the acquisition, Chengdu Kelon became a wholly-owned subsidiary of the Company.

Details of the identifiable assets and liabilities acquired, and the purchase consideration are as follows:

	<i>RMB'000</i>
Property, plant and equipment	84,365
Payments for leasehold land held for own use under operating leases	19,450
Trade and other receivables	183,516
Inventories	7,361
Cash and cash equivalents	7,525
Trade and other payables	(150,950)
Taxation payable	(3,981)
Bank borrowings	(24,900)
Net assets	122,386
Net assets acquired	36,716
Consideration:	
Satisfied by payment in advance and a note payable	81,388
Net assets acquired	(36,716)
Debited to capital reserve	44,672

Notes to the Financial Statements

31 December 2007

38. DISPOSAL OF A SUBSIDIARY

On 27 August 2007, the Company disposed 70% shareholding in a subsidiary, Kaifeng Kelon Air-Conditioner Co., Ltd (“Kaifeng Kelon”) to the minority equity holder, Henan Province, Kaifeng Economic Technology Development (Group) Company for a consideration of approximately RMB6,123,000 satisfied by waiver of debt settlement by Kaifeng Kelon. Kaifeng Kelon ceased to be a subsidiary of the Company following the disposal and the Company had no more shareholding interest in Kaifeng Kelon.

Details of the identifiable assets and liabilities disposed and the sales consideration are as follows:

	<i>RMB'000</i>
Sale proceeds satisfied by waiver of debt settlement	6,123
Net book value of net assets disposed	(1,614)
Gain on disposal of Kaifeng Kelon	4,509

The assets and liabilities disposed of at the date of disposal were as follows:

Property, plant and equipment	30,310
Payments for leasehold land held for own use under operating leases	13,084
Cash and cash equivalents	23
Trade and other receivables	837
Inventories	782
Trade and other payables	(6,542)
Minority interests	(36,880)
Net book value of net assets disposed	1,614

39. CAPITAL COMMITMENTS

	2007	2006
	<i>RMB'000</i>	<i>RMB'000</i>
Capital expenditure for acquisition of property, plant and equipment contracted for but not provided in the financial statements	90,831	14,004

40. RETIREMENT BENEFITS SCHEMES

The Group contributes mainly to a defined contribution pension scheme, which is administered by the provincial government, in respect of employees of the Group. According to such scheme, the Group shall pay an amount, calculated at a percentage of the total salaries and wages of the employees, to a retirement reserve.

The total cost charged to the consolidated income statement of approximately RMB41,135,000 (2006: RMB31,223,000) represents contributions payable to the scheme by the Group at rates specified in the rules of the scheme.

Notes to the Financial Statements

31 December 2007

41. RESERVES

(a) Statutory reserves

According to the Articles of Association of the Company, when distributing net profit of each year, the Company shall set aside 10% of its after tax profits for the statutory common reserve fund (except where the fund has reached 50% of the Company's registered capital) and 5% to 10% of after tax profits for the statutory common welfare fund. These reserves cannot be used for purposes other than those for which they are created and are not distributable as cash dividends.

(b) Distributable reserves of the Company

In accordance with the Articles of Association of the Company, the accumulated profits of the Company for the purpose of profit distribution will be deemed to be the lesser of (i) the amount determined in accordance with PRC accounting standards and regulations ("PRC GAAP") and (ii) the amount determined in accordance with IFRS.

As at 31 December 2007, the Company did not have reserve available for distribution to its shareholders (2006: Nil).

42. CONTINGENCIES

The Group is a defendant in certain lawsuits as well as the plaintiff in other proceedings arising in the ordinary course of business. The amount involved in the litigations against the Group relate mainly to bank loans, purchases and expenditures incurred by the Group and most of them were recorded as liabilities of the Group as at the balance sheet date. While the outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present, management believes that any resulting liabilities will not have material adverse effect on the financial position or operating results of the Group.

43. SUBSEQUENT EVENTS

The following significant events took place subsequent to 31 December 2007:

- (a) In January 2008, the Group signed share transfer agreement to dispose of its 100% equity interests in a subsidiary-Jilin Kelon. The total share transfer consideration was agreed to be RMB30,000,000 in which RMB29,500,000 was used for the settlement of liabilities of Jilin Kelon. The remaining balance of RMB500,000 has to be settled in cash. The Group had suffered a loss on disposal of the subsidiary of approximately RMB11,000,000 and the transaction for disposal of subsidiary was completed in March 2008.
- (b) In January 2008, the Group entered into a Business Cooperation Framework Agreement with certain subsidiaries of Hisense Group for a term of one year ending on 31 December 2008, which can be terminated before its expiration by mutual agreement of the parties, in connection with the (i) Sale and supply of moulds, (ii) Sale and supply of Air-conditioners, (iii) Sale and supply of Refrigerators, (iv) Sale and supply of raw material and components and (v) Provision of property management service to the subsidiaries of Hisense Group, subject to a maximum cap of RMB47,500,000, RMB120,000,000, RMB100,000,000, RMB92,100,000 and RMB500,000 respectively.

Notes to the Financial Statements

31 December 2007

43. SUBSEQUENT EVENTS *(continued)*

(b) *(continued)*

Under the same business cooperation Framework Agreement, the subsidiaries of Hisense Group agreed to (i) Sales and supply of Air-Conditioners, (ii) Sales and supply of refrigerators, (iii) Sales and supply of raw materials, components and moulds and (iv) Provision of property management service to the Group, subject to a maximum cap of RMB620,000,000, RMB210,000,000, RMB46,100,000 and RMB42,000,000.

The Group also entered into a Business Cooperation Framework Agreement with Huayi Compressor Holdings Company Limited and its associates for a term of one year ending on 31 December 2008, which can be terminated before its expiration by mutual agreement of the parties, in connection with the purchase of compressor by the subsidiaries of the Group, subject to a maximum cap of RMB581,710,000.

(c) The Company has approved in the general meeting of the Company held on 15 February 2008 to provide guarantees in favour of the Group's distributors at an aggregate amount of RMB442,000,000 (2006: RMB267,000,000). The Group and the respective distributors, however, have not reached any mutual commitment and entered into contractual arrangement for the proposed guarantee.

(d) In December 2007, the Company proposed to purchase the White Goods assets of Hisense Air-Conditioner, the substantial shareholder of the Company, including the production companies of refrigerators and air-conditioners and the sale company of White Goods Business (the "Target Assets") by way of private issuance of A shares of the Company to the Hisense Air-conditioning (the Acquisition). The price of the Target Assets of the Acquisition was proposed to be approximately RMB2,541,000,000. For the purpose of determining the consideration, the Company proposed to issue a total of up to and including 365,000,000 domestic ordinary shares (A-shares) with a nominal value of RMB1 each.

On 15 February 2008, the Company held an extraordinary general meeting and passed the Acquisition proposal. On 20 March 2008, the Company announced that the Acquisition has been rejected by the Merger and Reorganisation Review Committee of CSRC ("中國證券監督管理委員會併購重組審核委員會").

(e) In April 2008, the Company announced a notice to confirm that the Acquisition failed to complete by 28 March 2008. Pursuant to the Share Reform Proposal completed on 29 March 2007, Hisense Air-conditioner has undertaken to make a compensation of 9,725,059 shares calculated based on 0.5 share for every 10 transferable A Shares held by such holders as registered on 10 April 2008 under the circumstances that the Acquisition cannot be completed by 29 March 2008.

Notes to the Financial Statements

31 December 2007

44. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF UNCERTAINTY

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal to the related actual results. The estimates and assumptions 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.

Impairment

In considering the impairment losses that may be required for certain of the Group's assets which include property, plant and equipment, construction in progress, investment properties, payments for leasehold land held for own use under operating leases, intangible assets, goodwill and interests in associates, recoverable amounts of the assets need to be determined. The recoverable amount is the greater of the fair value less costs to sell and the value in use. It is difficult to precisely estimate fair value less costs to sell because quoted market prices for these assets may not be readily available. In determining the value in use, expected cash flows generated by the asset are discounted to their present value, which require significant judgment relating to items such as level of sales, selling price and amount of operating costs. The Group uses all readily available information in determining amounts that are reasonable approximations of recoverable amounts, including estimates based on reasonable and supportable assumptions and projections of items such as sales volume, selling price and amount of operating costs.

In considering the impairment losses that may be required for current receivables, future cash flows need to be determined. One of the key assumptions that has to be applied is the ability of the debtors to settle the receivables. Although the Group has used all available information to make this estimation, inherent uncertainty exists and actual may be different from the amount estimated.

Depreciation and amortisation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account their estimated residual values. The Group reviews the estimated useful lives of the assets regularly. The useful lives are based on the Group's historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

Warranty provision

As explained in noted 30(i), the Group makes provisions under the warranties it gives on sales of its electrical products taking into account the Group's recent claim experience. As the Group is continuously upgrading its product designs and launching new models, it is possible that recent claim experience is not indicative of the future claims that it will receive in respect of past sales. Any increase or decrease in the provision would affect profit or loss in future years.

Taxation

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. The Group carefully evaluates tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislations. Where the final tax outcome of these transactions is different from the amounts that were initially recorded, such difference will impact the income tax and deferred tax provisions in the year in which such determination is made.

45. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the Board of Directors on 24 April 2008.

Supplemental Information

31 December 2007

DIFFERENCES BETWEEN IFRS AND PRC GAAP AS APPLICABLE TO THE GROUP

The consolidated shareholders' equity of the Group prepared under IFRS and that prepared under PRC GAAP have the following major differences:

	2007	2006
	RMB'000	RMB'000
		(Restated)
Equity attributable to equity holders of the Company as per financial statements prepared under IFRS	(784,772)	(994,578)
Adjustment on contribution from minority shareholders	—	26,684
Adjustment on restructuring costs expensed	11,684	—
Adjustment on dilution loss on share reform of an associate	16,317	16,317
Amortisation of trademark	(16,712)	(16,712)
Adjustment on impairment and amortisation of goodwill	—	(57,253)
Non-recognition of deferred tax assets	—	(21,387)
<hr/>		
Equity attributable to equity holders of the Company as per financial statements prepared under PRC GAAP as previously reported	(773,483)	(1,046,929)
<hr/>		
Effect of adoption of China Accounting Standards 2006 ("CAS 2006") effective on 1 January 2007		
Write off of equity investment difference arising from business combinations under common control	—	57,253
Recognition of deferred tax assets	—	21,387
<hr/>		
Equity attributable to equity holders of the Company as per financial statements prepared under PRC GAAP, as restated	(773,483)	(968,289)

Supplemental Information

31 December 2007

DIFFERENCES BETWEEN IFRS AND PRC GAAP AS APPLICABLE TO THE GROUP *(continued)*

The consolidated net profit prepared under IFRS and that prepared under PRC GAAP have the following major differences:

	2007 RMB'000	2006 RMB'000 (Restated)
Net profit attributable to equity holders of the Company as per financial statements prepared under IFRS	238,712	69,989
Adjustment on restructuring costs expensed	11,684	—
Recognition of long outstanding payables in capital reserve	—	(27,479)
Amortisation of trademark	—	(16,712)
Adjustment on impairment and amortisation of goodwill	—	(1,396)
Release of negative goodwill to income	—	4,790
Non-recognition of deferred tax assets	—	(21,387)
Adjustment on dilution loss on share reform of an associate	—	16,317
<hr/>		
Net profit attributable to equity holders of the Company as per financial statements prepared under PRC GAAP	250,396	24,122
<hr/>		
Effect of adoption of China Accounting Standards 2006 (“CAS 2006”) effective on 1 January 2007		
Recognition of deferred tax assets	—	21,387
Retrospective adjustment on amortisation of goodwill and release of negative goodwill to income	—	(3,394)
<hr/>		
Net profit attributable to equity holders of the Company as per financial statements prepared under PRC GAAP, as restated	250,396	42,115
<hr/>		

There are differences in other items in the financial statements due to differences in classification between IFRS and PRC GAAP.

Five Years Summary

	Year ended 31 December				
	2007 <i>RMB'000</i>	2006 <i>RMB'000</i> (Restated)	2005 <i>RMB'000</i> (Restated)	2004 <i>RMB'000</i> (Restated)	2003 <i>RMB'000</i> (Restated)
RESULT					
Turnover	8,319,960	6,564,257	6,978,372	7,923,001	6,188,110
Profit/ (loss) before share of results of associates	212,277	24,788	(3,754,514)	(119,550)	263,353
Share of results of associates	2,247	3,590	(31,571)	(84,252)	(41,394)
Profit/ (loss) before income tax	214,524	28,378	(3,786,085)	(203,802)	221,959
Income tax (expense)/ credit	(10,867)	20,871	(1,021)	(23,718)	(13,632)
Profit/ (loss) for the year	203,657	49,249	(3,787,106)	(227,520)	208,327
Attributable to:					
Equity holders of the Company	238,712	69,989	(3,722,565)	(217,064)	202,180
Minority interests	(35,055)	(20,740)	(64,541)	(10,456)	6,147
	203,657	49,249	(3,787,106)	(227,520)	208,327
Dividends	—	—	—	—	—
	As at 31 December				
	2007 <i>RMB'000</i>	2006 <i>RMB'000</i> (Restated)	2005 <i>RMB'000</i> (Restated)	2004 <i>RMB'000</i> (Restated)	2003 <i>RMB'000</i> (Restated)
ASSETS AND LIABILITIES					
Total assets	4,414,571	4,668,544	5,493,770	11,704,220	9,786,355
Total liabilities	(5,044,345)	(5,396,475)	(6,283,472)	(8,778,305)	(6,738,206)
Net (liabilities)/ assets	(629,774)	(727,931)	(789,702)	2,925,915	3,048,149
Capital and reverses attributable to equity holders of the Company	(784,772)	(994,578)	(1,074,092)	2,567,984	2,814,173
Minority interests	154,998	266,647	284,390	357,931	233,976
Total equity	(629,774)	(727,931)	(789,702)	2,925,915	3,048,149

Auditor's Report



BDO Shenzhen Dahua Tiancheng
Certified Public Accountants

11th Floor B Block Union Square 5022
Binhe Road Shenzhen 518033 P.R. China
Telephone: +86-755-82900952
Fax: +86-755-82900965

中国深圳滨河大道5022号联合广场
B座11楼 邮编: 518033
电话: +86-755-82900952
传真: +86-755-82900965

Shenhua (2008) gushenzi No. (28)

To the Shareholders of Hisense Kelon Electrical Holdings Company Limited

We have audited the accompanying financial statements of Hisense Kelon Electrical Holdings Company Limited (the "Company"), including the consolidated and company balance sheets and the consolidated and company statement of changes in equity as at 31 December 2007 and the consolidated and company statements, profit and loss and cash flows for 2007 and the accompanying notes.

1. RESPONSIBILITY OF THE MANAGEMENT

It is the responsibility of the Company's management to prepare the Financial Statements pursuant to the Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises. The responsibility includes: (1) to design, implement and maintain the internal controls related to the preparation of the Financial Statements, so as to ensure that they are free of any material misstatements due to fraud and errors; (2) to choose and apply appropriate accounting policies; and (3) and make reasonable accounting estimations.

2. RESPONSIBILITY OF THE AUDITOR

Our responsibility is to express opinions on the Financial Statements based on our audit. Except as described 3.qualified items in this report, we conducted our audit in accordance with China's Independent Audit Standards of Certified Public Accountants. The audit standards require that we follow the Code of Professional Ethics to plan and perform the audit to obtain reasonable assurance about whether the Financial Statements are free of material misstatements.

An audit involves performing procedures to obtain evidence relevant to the amounts and disclosures in the Financial Statements. The procedures selected depend on the judgments of auditor, which include an assessment of the material misstatement in the Financial Statements due to fraud and errors. When making the assessment, we need to design appropriate audit procedures considering the internal controls related to the preparation of the Financial Statements. However, the purpose of the assessment is not to express opinions on the effectiveness of the internal controls. Our audit also includes an assessment on the appropriateness of accounting policies, reasonableness of accounting estimates used by the management and the overall presentations of the Financial Statements.

We believe that our audit evidence is sufficient and reasonable and provides a reasonable basis for our opinion.

3. QUALIFIED ITEMS

As described in Appendix 6 Note 4, Note 6 and Appendix 11, 15 to the financial statements, a series of related parties' transactions and unusual cash flows occurred between the Company and its former largest shareholder, Guangdong Greencool Enterprise Development Limited and its related parties (the "Greencool Companies") during the period from October 2001 to July 2005. In addition, the Greencool Companies, through certain specified third party companies such as Tianjin Lixin Commercial Trading Development Company Limited, involved in a series of unusual cash flows with the Company in the same period. Such transactions and unusual cash flows as well as the suspected fund embezzlement have been reported to the relevant authority, and are pending for judgment. Such reported matters involve the accounts receivables and payables between the Company and the Greencool Companies as well as the specified third party companies mentioned above. The Company received Civil Judgment (Fo Zhong Fa Min Er Chu Zi No. 93 and 94 (2006)) from the Guangdong Province Foshan Intermediate Court (hereinafter "Foshan Intermediate Court") on 10 September 2007 and Civil

Auditor's Report

Judgment (Fo Zhong Fa Min Er Chu Zi No. 153, 154, 175, 181, 182, 185 and 186 (2006)) from the Guangdong Province Foshan Intermediate Court on 31 March 2008, which stated that Foshan Intermediate Court has made first trial judgment on the nine cases in respect of the litigation initiated by your Company against the Greencool Companies and the case of specified third party companies in favour of your Company. The counterparty of the above nine litigations appealed from the judgment and the case is currently under hearing. As at 31 December 2007, the balance of the accounts receivables of the Company from the Greencool Companies and the above specified third party companies amounted to RMB651 million. The Company has made a provision of RMB364 million in respect of the accounts receivables from Greencool Companies and the above specified third party companies. We were unable to adopt appropriate audit procedures to obtain sufficient and appropriate audit evidence to ascertain whether the estimated provision for bad debts is reasonable and the assessment and calculation of the receivables is reasonable.

4. AUDIT OPINION

In our opinion, except for the item mentioned above, the above-mentioned financial statements have been prepared in compliance with the requirements of the Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises and present fairly, in all material respects, the financial position of the Company as at 31 December 2007, and the results of operations and cash flows of the Company for the year then ended.

BDO Shenzhen Dahua Tiancheng

Shenzhen, PRC

*Certified Public Accountants Registered
in the People's Republic of China*

Hu Chun Yuan

*Certified Public Accountants Registered
in the People's Republic of China*

Wu Jian Hui

24 April 2008

The auditors' report and the accompanying financial statements are English translations of the Chinese auditors' report and statutory financial statements prepared under accounting principles and practices generally accepted in the People's Republic of China. These financial statements are not intended to present the financial position and results of operations and cash flows in accordance with accounting principles and practices generally accepted in other countries and jurisdictions. In case the English version does not conform to the Chinese version, the Chinese version prevails.

Balance Sheet

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Assets	31 December 2007		31 December 2006	
	Consolidation	Company	Consolidation	Company
Current assets:				
Bank balances and cash	146,527,807.16	47,055,872.14	390,503,566.38	205,118,842.75
Transactional financial assets	9,479,410.00	—	2,000.00	2,000.00
Notes receivable	2,740,000.00	100,000.00	77,317,440.80	23,963,736.61
Accounts receivable	618,566,012.70	388,208,800.61	374,911,284.04	220,267,064.25
Prepayments	72,847,598.00	336,124,026.29	81,980,665.92	267,776,312.98
Interests receivable	—	—	—	—
Dividends receivable	—	—	—	—
Others receivable	593,172,778.27	1,109,850,412.61	475,747,191.80	1,396,925,531.98
Inventories	940,284,389.70	615,051,793.84	919,836,622.62	620,785,727.30
Non-current assets due within one year	—	—	—	—
Other current assets	15,376,482.03	13,541,212.89	543,661.62	125,000.00
Total current assets	2,398,994,477.86	2,509,932,118.38	2,320,842,433.18	2,734,964,215.87
Non-current assets:				
Available-for-sale fixed assets	—	—	—	—
Held-to-maturity investments	—	—	—	—
Long-term receivable	—	—	—	—
Long-term equity investment	128,924,101.80	1,901,334,592.62	125,928,171.92	1,813,388,668.41
Investment properties	38,192,137.43	20,728,217.00	64,542,932.84	37,461,097.76
Fixed assets	1,234,496,001.63	380,412,420.05	1,330,768,487.39	439,916,791.97
Construction in progress	137,105,983.23	17,303,509.63	283,719,768.18	2,205,075.77
Construction materials	—	—	—	—
Disposal of fixed assets	5,149,749.16	5,125,440.00	—	—
Productive biological assets	—	—	—	—
Intangible assets	464,944,203.67	291,605,318.88	418,507,966.06	269,114,746.00
Development costs	—	—	—	—
Goodwill	—	—	—	—
Long term deferred expenditures	2,222,788.48	—	880,451.52	—
Deferred income tax assets	11,299,667.77	—	21,386,732.06	—
Other non-current assets	—	—	—	—
Total non-current assets	2,022,334,633.17	2,616,509,498.18	2,245,734,509.97	2,562,086,379.91
Total assets	4,421,329,111.03	5,126,441,616.56	4,566,576,943.15	5,297,050,595.78

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Balance Sheet

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Liabilities and Shareholders' equity	31 December, 2007		31 December, 2006	
	Consolidation	Company	Consolidation	Company
Current liabilities:				
Short-term loans	1,310,971,970.91	895,000,000.00	1,556,702,248.52	866,902,248.52
Transactional financial liability	6,157,782.89	—	—	—
Notes payable	770,959,940.00	733,959,940.00	508,047,387.22	660,069,940.00
Accounts payable	1,352,524,482.02	164,747,880.81	1,467,483,921.58	554,805,693.76
Advance from customers	417,174,192.88	473,580,561.40	760,291,406.34	686,697,652.74
Staff remuneration payables	91,851,650.73	39,546,709.70	37,138,455.20	5,824,765.25
Taxes payables	(65,430,540.63)	(20,372,408.90)	(101,767,764.94)	(85,624,053.90)
Interests payable	4,405,858.84	1,748,914.38	18,446,920.52	13,242,642.73
Dividends payable	2,067.02	—	2,067.02	—
Other payables	658,716,749.14	1,843,584,601.17	570,915,593.57	1,481,510,368.91
Non-current liabilities due within one year	—	—	—	—
Other current liabilities	292,682,611.12	233,115,295.19	247,077,453.29	205,107,283.42
Total Current Liabilities	4,840,016,764.92	4,364,911,493.75	5,064,337,688.32	4,388,536,541.43
Non-current liabilities:				
Long-term loans	—	—	—	—
Bonds payable	—	—	—	—
Long-term payable	55,792,534.72	55,592,534.72	60,572,294.23	58,214,807.25
Specific payables	—	—	—	—
Provisions	144,005,574.26	129,085,638.25	169,995,082.92	165,063,452.10
Deferred income tax liabilities	—	—	—	—
Other non-current liabilities	—	—	—	—
Total Non-current liabilities	199,798,108.98	184,678,172.97	230,567,377.15	223,278,259.35
Total liabilities	5,039,814,873.90	4,549,589,666.72	5,294,905,065.47	4,611,814,800.78
Shareholders' equity:				
Share capital	992,006,563.00	992,006,563.00	992,006,563.00	992,006,563.00
Capital reserve	1,538,356,635.50	1,723,121,352.12	1,608,102,127.20	1,721,510,391.64
Less: Treasury shares	—	—	—	—
Surplus reserves	114,580,901.49	114,580,901.49	114,580,901.49	114,580,901.49
Unappropriated profits	(3,447,561,785.51)	(2,252,856,866.77)	(3,697,957,232.42)	(2,142,862,061.13)
Exchange differences on foreign currency translation	29,133,511.65	—	14,978,392.50	—
Equity attributable to the holders of the parent	(773,484,173.87)	576,851,949.84	(968,289,248.23)	685,235,795.00
Minority Interests	154,998,411.00	—	239,961,125.91	—
Total liabilities and shareholders' equity	(618,485,762.87)	576,851,949.84	(728,328,122.32)	685,235,795.00
Total shareholders' equity	4,421,329,111.03	5,126,441,616.56	4,566,576,943.15	5,297,050,595.78

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Income Statement

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2007		2006	
	Consolidation	Company	Consolidation	Company
1. Revenue	8,822,347,228.40	5,021,911,719.32	6,978,111,131.63	4,035,706,444.84
Including: Revenue from principal operations	8,321,817,250.46	4,457,712,654.83	6,565,241,644.83	3,890,910,582.00
Revenue from other operations	500,529,977.94	564,199,064.49	412,869,486.80	144,795,862.84
Less: Costs	7,368,479,127.09	4,088,689,613.96	5,757,863,658.34	3,504,142,309.61
Including: Costs of principal operations	6,945,444,340.24	3,762,285,515.53	5,473,715,389.14	3,375,313,273.34
Costs of other operations	423,034,786.85	326,404,098.43	284,148,269.20	128,829,036.27
Sales tax and surcharges	1,856,823.76	1,031,322.95	984,962.74	109,337.52
Distribution costs	1,116,923,591.23	961,362,150.53	831,614,349.02	709,322,578.47
Administrative expenses	311,516,093.52	58,605,430.02	365,479,462.69	108,458,103.44
Financial expenses	119,179,346.67	97,093,371.48	158,807,567.00	101,087,326.92
Asset impairment losses	62,425,986.84	4,356,106.28	(18,158,599.04)	(45,935,521.96)
Add: Gain from changes in fair value	3,104,581.01	—	—	—
Investment profit	6,756,455.99	2,226,963.73	3,588,175.99	3,588,175.99
Including: Investment profits from associates and joint ventures	—	—	—	—
Exchange gain	—	—	—	—
2. Operating profits	(148,172,703.71)	(186,999,312.16)	(114,892,093.13)	(337,889,513.17)
Add: Non-operating income	463,679,353.02	86,428,600.16	160,251,086.86	139,875,901.82
Less: Non-operating expenses	89,299,117.37	9,424,093.64	44,952,655.86	19,316,126.27
Including: Losses on disposal of non-current assets	—	—	—	—
3. Total profit	226,207,531.93	(109,994,805.64)	406,337.87	(217,329,737.62)
Less: Income tax expense	10,867,387.46	—	(20,870,766.47)	—
4. Net profit	215,340,144.48	(109,994,805.64)	21,277,104.34	(217,329,737.62)
Net profit attributable to the holders of the parent	250,395,446.91	(109,994,805.64)	42,113,364.14	(217,329,737.62)
Profit or loss of minority shareholders	(35,055,302.43)	—	(20,836,259.80)	—
5. Earnings per share				
(1) Basic earnings per share	0.2524	—	0.0425	—
(2) Diluted earnings per share	0.2524	—	0.0425	—

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Cash Flow Statement

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2007		2006	
	Consolidation	Company	Consolidation	Company
1. Net cash flow from operating activities:				
Cash received from sales of goods and rendering of services	4,522,597,002.35	1,675,242,801.55	3,763,368,880.84	2,195,030,159.18
Refund of tax and levies	214,104,492.78	—	102,202,641.01	—
Cash received from other operation activities	31,414,712.83	1,604,677,347.97	122,665,124.31	110,708,632.44
Sub-total of cash inflow from operating activities	4,768,116,207.96	3,279,920,149.52	3,988,236,646.16	2,305,738,791.62
Cash paid for purchases of goods and services	2,992,877,751.78	2,300,517,630.89	1,422,597,335.82	795,369,172.76
Cash paid to and on behalf of employees	562,760,732.10	197,121,515.83	513,411,138.06	253,198,831.64
Tax paid	180,528,099.70	103,868,423.05	316,489,398.12	158,583,267.54
Cash paid for other operation activities	1,036,345,273.13	854,706,371.93	853,290,523.24	476,211,297.13
Sub-total of cash outflows from operating activities	4,772,511,856.71	3,456,213,941.70	3,105,788,395.24	1,683,362,569.07
Net cash flows from operating activities	(4,395,648.75)	(176,293,792.17)	882,448,250.92	622,376,222.55
2. Cash flows from investing activities:				
Cash received from investment returns	—	—	—	—
Cash received from investment revenues	—	—	—	—
Net Cash received from disposals of fixed assets, intangible assets and other long-term assets	429,318,371.19	163,759,000.14	179,098,710.41	131,907,884.22
Net Cash received from disposals of subsidiaries and other operation units	—	—	—	—
Other cash received from investing activities	4,011,408.82	2,061,207.24	4,754,020.02	1,467,709.78
Sub-total of cash inflow from investing activities	433,329,780.01	165,820,207.38	183,852,730.43	133,375,594.00
Cash paid for acquisition of fixed assets, intangible assets and other long-term assets	301,657,981.60	90,265,898.21	128,802,562.83	19,619,429.85
Cash paid for investments	1,220,000.00	2,720,000.01	—	—
Net increase in secured loans	—	—	—	—
Cash paid for obtaining subsidiaries and other operation units	—	—	—	—
Cash paid for other investing activities	—	—	—	—
Sub-total of cash outflow from investing activities	302,877,981.60	92,985,898.22	128,802,562.83	19,619,429.85
Net cash flows from investing activities	130,451,798.41	72,834,309.16	55,050,167.60	113,756,164.15

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Cash Flow Statement

Items	2007		2006	
	Consolidation	Company	Consolidation	Company
3. Cash flow from financing activities				
Cash contribution from investment	—	—	—	—
Including: Cash contribution from minority shareholders' investment by subsidiaries	—	—	—	—
Cash received from borrowings	1,780,779,623.28	1,029,000,000.00	1,520,863,959.04	745,200,000.00
Cash received from issue of bonds	—	—	—	—
Increase in policyholder deposits and investments	—	—	—	—
Other cash received from investing activities	320,124,523.59	267,537,644.94	—	—
Sub-total of cash inflow from financing activities	2,100,904,146.87	1,296,537,644.94	1,520,863,959.04	745,200,000.00
Cash paid for repayment of borrowings	2,020,809,900.89	995,202,248.52	2,124,684,531.08	1,146,433,011.65
Cash paid for distribution of dividends, profit or interest expenses	75,119,918.47	35,251,849.34	120,271,383.83	86,010,956.67
Including: dividend and profit paid to minority shareholders by subsidiaries	—	—	—	—
Cash paid for other financial activities	196,881,712.79	195,149,389.74	255,443,984.04	259,964,689.19
Sub-total of cash outflow from financing activities	2,292,811,532.15	1,225,603,487.60	2,500,399,898.95	1,492,408,657.51
Net cash flow from financing activities	(191,907,385.28)	70,934,157.34	(979,535,939.91)	(747,208,657.51)
4. Effects of foreign exchange rate changes on cash	—	—	—	—
5. Net increase in cash and cash equivalents	(65,851,235.62)	(32,525,325.67)	(42,037,521.39)	(11,076,270.81)
Add: Balance of cash and cash equivalents at the beginning of the year	142,246,506.14	54,118,987.38	184,284,027.53	65,195,258.19
Balance of cash and cash equivalents at the end of the year	76,395,270.52	21,593,661.71	142,246,506.14	54,118,987.38
Company legal representative: Tang Ye Guo	Principal in charge of accounting: Liu Chun Xin	Principal of the accounting department: Chen Zhen Wen		

Consolidated Statement of Changes of Shareholders' Equity

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2007							
	Equity attributable to the shareholders of the parent					Others (Exchange difference on foreign currency translation)	Minority interests	Total shareholders' interest
	Share capital	Capital reserve	Less: Treasury share	Surplus reserve	Undistributed profit			
1. Closing Balance of previous year	992,006,563.00	1,608,102,127.20	—	114,580,901.49	(3,697,957,232.42)	14,978,392.50	239,961,125.91	(728,328,122.32)
Add: Changes of accounting policies	—	—	—	—	—	—	—	—
Correction for error in previous period	—	—	—	—	—	—	—	—
2. Opening balance of the year	992,006,563.00	1,608,102,127.20	—	114,580,901.49	(3,697,957,232.42)	14,978,392.50	239,961,125.91	(728,328,122.32)
3. Changes in amounts in the year ("—" for decrease)	—	(69,745,491.70)	—	—	250,395,446.91	14,155,119.15	(84,962,714.91)	109,842,359.45
(1) Net Profit	—	—	—	—	250,395,446.91	—	(35,055,302.43)	215,340,144.48
(2) Gains and losses directly accounted for as shareholders' equity	—	—	—	—	—	—	—	—
1. Net changes in fair value of available-for-sale financial assets	—	—	—	—	—	—	—	—
2. Effect of changes of other owners' equity in investee under equity method	—	(25,073,387.07)	—	—	—	—	—	(25,073,387.07)
3. Income tax effect related to items included in shareholders' equity	—	—	—	—	—	—	—	—
4. Others	—	(44,672,104.63)	—	—	—	14,155,119.15	(49,907,412.48)	(80,424,397.96)
Sub-total of (1) and (2) above	—	—	—	—	—	—	—	109,842,359.45
(3) Equity holder contributions and capital reductions	—	—	—	—	—	—	—	—
1. Equity holder contributions	—	—	—	—	—	—	—	—
2. Amount of share-based payment included in equity	—	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—	—
(4) Profit Appropriation	—	—	—	—	—	—	—	—
1. Appropriations to surplus reserve	—	—	—	—	—	—	—	—
2. Distribution to shareholders	—	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—	—
(5) Internal transfer of shareholders' equity	—	—	—	—	—	—	—	—
1. Transfer to share capital from capital reserve	—	—	—	—	—	—	—	—
2. Transfer to share capital from surplus reserve	—	—	—	—	—	—	—	—
3. Compensation of losses by surplus reserve	—	—	—	—	—	—	—	—
4. Others	—	—	—	—	—	—	—	—
4. Closing balance of the year	992,006,563.00	1,538,356,635.50	—	114,580,901.49	(3,447,561,785.51)	29,133,511.65	154,998,411.00	(618,485,762.87)

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Consolidated Statement of Changes of Shareholders' Equity

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2006							
	Equity attributable to the shareholders of the parent					Others (Exchange difference on foreign currency translation)	Minority interests	Total shareholders' interest
	Share capital	Capital reserve	Less: Treasury share	Surplus reserve	Undistributed profit			
1. Closing Balance of previous year	992,006,563.00	1,581,099,648.75	—	114,580,901.49	(3,800,717,444.16)	4,954,274.87	257,705,794.23	(850,370,261.82)
Add: Changes of accounting policies	—	—	—	—	60,646,847.60	—	—	60,646,847.60
Correction for error in previous period	—	—	—	—	—	—	—	—
2. Opening balance of the year	992,006,563.00	1,581,099,648.75	—	114,580,901.49	(3,740,070,596.56)	4,954,274.87	257,705,794.23	(789,723,414.22)
3. Changes in amounts in the year ("—" for decrease)	—	27,002,478.45	—	—	42,113,364.14	10,024,117.63	(17,744,668.32)	61,395,291.90
(1) Net Profit	—	—	—	—	42,113,364.14	10,024,117.63	(20,836,259.80)	31,301,221.97
(2) Gains and losses directly accounted for as shareholders' equity	—	—	—	—	—	—	—	—
1. Net changes in fair value of available-for-sale financial assets	—	—	—	—	—	—	—	—
2. Effect of changes of other owners' equity in investee under equity method	—	—	—	—	—	—	—	—
3. Income tax effect related to items included in shareholders' equity	—	—	—	—	—	—	—	—
4. Others	—	27,002,478.45	—	—	—	—	3,091,591.48	30,094,069.93
Sub-total of (1) and (2) above	—	—	—	—	—	—	—	61,395,291.90
(3) Equity holder contributions and capital	—	—	—	—	—	—	—	—
1. Equity holder contributions	—	—	—	—	—	—	—	—
2. Amount of share-based payment included in equity	—	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—	—
(4) Profit Appropriation	—	—	—	—	—	—	—	—
1. Appropriations to surplus reserve	—	—	—	—	—	—	—	—
2. Distribution to shareholders	—	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—	—
(5) Internal transfer of shareholders' equity	—	—	—	—	—	—	—	—
1. Transfer to share capital from capital reserve	—	—	—	—	—	—	—	—
2. Transfer to share capital from surplus reserve	—	—	—	—	—	—	—	—
3. Compensation of losses by surplus reserve	—	—	—	—	—	—	—	—
4. Others	—	—	—	—	—	—	—	—
Closing balance of the year	992,006,563	1,608,102,127.20	—	114,580,901.49	(3,697,957,232.42)	14,978,392.50	239,961,125.91	(728,328,122.32)

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Statement of Changes of Shareholders' Equity (Parent Company)

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2007						Total shareholders' interest
	Share capital	Capital reserve	Less: Treasury share	Surplus reserve	Undistributed profit	Minority interests	
1. Closing Balance of previous year	992,006,563.00	1,721,510,391.64	—	114,580,901.49	(2,142,862,061.13)	—	685,235,795.00
Add: Changes of accounting policies	—	—	—	—	—	—	—
Correction for error in previous period	—	—	—	—	—	—	—
2. Opening balance of the year	992,006,563.00	1,721,510,391.64	—	114,580,901.49	(2,142,862,061.13)	—	685,235,795.00
3. Changes in amounts in the year ("—" for decrease)	—	1,610,960.48	—	—	(109,994,805.64)	—	(108,383,845.16)
(1) Net Profit	—	—	—	—	(109,994,805.64)	—	(109,994,805.64)
(2) Gains and losses directly accounted for as shareholders' equity	—	—	—	—	—	—	—
1. Net changes in fair value of available-for-sale financial assets	—	—	—	—	—	—	—
2. Effect of changes of other owners' equity in investee under equity method	—	1,610,960.48	—	—	—	—	1,610,960.48
3. Income tax effect related to items included in shareholders' equity	—	—	—	—	—	—	—
4. Others	—	—	—	—	—	—	—
Sub-total of (1) and (2) above	—	—	—	—	—	—	—
(3) Equity holder contributions and capital reductions	—	—	—	—	—	—	—
1. Equity holder contributions	—	—	—	—	—	—	—
2. Amount of share—based payment included in equity	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—
(4) Profit Appropriation	—	—	—	—	—	—	—
1. Appropriations to surplus reserve	—	—	—	—	—	—	—
2. Distribution to shareholders	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—
(5) Internal transfer of shareholders' equity	—	—	—	—	—	—	—
1. Transfer to share capital from capital reserve	—	—	—	—	—	—	—
2. Transfer to share capital from surplus reserve	—	—	—	—	—	—	—
3. Compensation of losses by surplus reserve	—	—	—	—	—	—	—
4. Others	—	—	—	—	—	—	—
4. Closing balance of the year	992,006,563.00	1,723,121,352.12	—	114,580,901.49	(2,252,856,866.77)	—	576,851,949.84

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Statement of Changes of Shareholders' Equity (Parent Company)

Prepared by: Hisense Kelon Electrical Holdings Company Limited

Unit: RMB

Items	2006						Total shareholders' interest
	Equity attributable to the shareholders of the parent						
	Share capital	Capital reserve	Less: Treasury share	Surplus reserve	Undistributed profit	Minority interests	
1. Closing Balance of previous year	992,006,563.00	1,977,086,351.38	—	114,580,901.49	(3,935,014,818.77)	—	(851,341,002.90)
Add: Changes of accounting policies	—	(271,091,958.61)	—	—	2,009,482,495.26	—	1,738,390,536.65
Correction for error in previous period	—	—	—	—	—	—	—
2. Opening balance of the year	992,006,563.00	1,705,994,392.77	—	114,580,901.49	(1,925,532,323.51)	—	887,049,533.75
3. Changes in amounts in the year ("—" for decrease)	—	15,515,998.87	—	—	(217,329,737.62)	—	(201,813,738.75)
(1) Net Profit	—	—	—	—	(217,329,737.62)	—	(217,329,737.62)
(2) Gains and losses directly accounted for as shareholders' equity	—	—	—	—	—	—	—
1. Net changes in fair value of available-for-sale financial assets	—	—	—	—	—	—	—
2. Effect of changes of other owners' equity in investee under equity method	—	(476,546.54)	—	—	—	—	(476,546.54)
3. Income tax effect related to items included in shareholders' equity	—	—	—	—	—	—	—
4. Others	—	15,992,545.41	—	—	—	—	15,992,545.41
Sub-total of (1) and (2) above	—	—	—	—	—	—	—
(3) Equity holder contributions and capital reductions	—	—	—	—	—	—	—
1. Equity holder contributions	—	—	—	—	—	—	—
2. Amount of share-based payment included in equity	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—
(4) Profit Appropriation	—	—	—	—	—	—	—
1. Appropriations to surplus reserve	—	—	—	—	—	—	—
2. Distribution to shareholders	—	—	—	—	—	—	—
3. Others	—	—	—	—	—	—	—
(5) Internal transfer of shareholders' equity	—	—	—	—	—	—	—
1. Transfer to share capital from capital reserve	—	—	—	—	—	—	—
2. Transfer to share capital from surplus reserve	—	—	—	—	—	—	—
3. Compensation of losses by surplus reserve	—	—	—	—	—	—	—
4. Others	—	—	—	—	—	—	—
4. Closing balance of the year	992,006,563.00	1,721,510,391.64	—	114,580,901.49	(2,142,862,061.13)	—	685,235,795.00

Company legal representative:
Tang Ye Guo

Principal in charge of accounting:
Liu Chun Xin

Principal of the accounting department:
Chen Zhen Wen

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

I. COMPANY PROFILE

Hisense Kelon Electrical Holdings Company Limited (hereinafter referred to as the “Company”) is a joint stock limited company incorporated in the PRC on 16 December 1992. The Company’s 459,589,808 overseas listed public shares (the “H Shares”) were listed on The Stock Exchange of Hong Kong Limited on 23 July 1996. In 1998, the Company obtained approval to issue 110,000,000 domestic shares (the “A Shares”), which were listed on the Shenzhen Stock Exchange on 13 July 1999.

In October 2001 and March 2002, the former single largest shareholder of the Company, Guangdong Kelon (Rongsheng) Group Company Limited (hereinafter referred to as “Rongsheng Group”, previously held 34.06% interest in the Company) entered into a share transfer agreement and a supplementary agreement with Shunde Greencool Enterprise Development Company Limited (it was renamed as “Guangdong Greencool Enterprises Development Company Limited in 2004, hereinafter referred to as “Guangdong Greencool”), in connection with the transfer of 20.64% of the total share capital of the Company to Guangdong Greencool. In April 2002, Rongsheng Group transferred its shareholding of 6.92%, 0.71% and 5.79% of the total share capital of the Company to Shunde Economic Consultancy Company, Shunde Dong Heng Development Company Limited and Shunde Xin Hong Enterprise Company Limited, respectively. After the above-mentioned share transfers, Rongsheng Group, the former single largest shareholder of the Company, no longer held any shares of the Company.

On 14 October 2004, Guangdong Greencool, as transferee, had been transferred 5.79% of the total share capital of the Company held by Shunde Xin Hong Enterprise Company. Upon completion of the share transfer, the percentage of total share capital of the Company held by Guangdong Greencool increased to 26.43%.

On 13 December 2006, 26.43% of the total share capital of the Company held by Guangdong Greencool Enterprises Development Company Limited were transferred to Qingdao Hisense Air-Conditioning Company Limited. Upon completion of the transfer, Guangdong Greencool, the former single largest shareholder of the Company, no longer held any share of the Company.

The company’s share reform project was approved on the A shareholders’ meeting on 29 January 2007 and approved by the National Commerce Department on 22 March 2007. The shareholding of the largest shareholder, Qingdao Hisense Air-Conditioning Company Limited, in the Company changed to 24.08% after such share reform.

On 20 June 2007, the name of the Company was changed from “Guangdong Kelon Electrical Holdings Company Limited” to “Hisense Kelon Electrical Holdings Company Limited”.

The Group is principally engaged in the manufacture and sale of refrigerators, air-conditioners and household electricity appliances.

II. BASIS OF PREPARATION OF FINANCIAL STATEMENTS AND STATEMENT OF COMPLIANCE TO ACCOUNTING STANDARDS FOR BUSINESS ENTERPRISES

The Company prepares the financial statements on the basis of ongoing operation and recognizes and measures the transactions and matters actually occurred in accordance with the Accounting Standards for Business Enterprises – Basis Standards and other accounting standard requirements issued by the Ministry of Finance on 15 February 2006, and the “Accounting Standards for Business Enterprises – Application Guidelines”, “Accounting Standards for Business Enterprises Interpretations” and other related requirements issued subsequently (hereinafter “Accounting Standards for Business Enterprises”). The preparation of financial statements in accordance with the PRC Accounting Standards requires the use of estimations and assumptions, which may affect the disclosure of assets, liabilities and contingent liabilities as at the date of financial report and the income and expenses of the Reporting Period. The financial statement prepared by the Company complies with the requirements of the Accounting Standards for Business Enterprises and truly and completely reflects the financial state, operating results, cash flow and other related information of the Company.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

The financial statements of 2007 are the first annual financial statement of the Company prepared in accordance with the Accounting Standards for Business Enterprises. In preparing the related comparative figures of 2006 have been retrospectively adjusted in accordance with the “Accounting Standard for Business Enterprises No. 38 — First time adoption of Accounting Standards for Business Enterprises” and have been reclassified according to the format of disclosure of these financial statements. The related adjusted items are set out in Appendix 4.25.

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT

1. Controlled subsidiaries:

Name of controlling company	Place of registration	Nature of Business	Registered Capital	Actual Investment Amount at the End of the Period	Actual Net Investment Balance to the Subsidiary	Shareholding of the Company			Percentage of Voting Rights
						Direct	Indirect	Total	
1. Subsidiaries acquired through business combination									
(I) Subsidiaries under common control									
Hisense Ronshen (Guangdong) Refrigerator Co Ltd (“Ronshen Refrigerator”)	Foshan	Manufacture and sale of refrigerators	US\$26,800,000	213,822,978.74	213,822,978.74	70%	30%	100%	100%
Guangdong Kelon Air-conditioner Co., Ltd. (“Kelon Air-conditioner”)	Foshan	Manufacture and sale of air-conditioners	US\$36,150,000	281,000,000.00	281,000,000.00	60%	—	60%	60%
Hisense Ronshen (Guangdong) Freezer Co. Ltd. (“Kelon Freezer”)	Foshan	Manufacture and sale of freezers	RMB237,000,000	38,976,927.91	38,976,927.91	44%	56%	100%	100%
Shunde Kelon Household Electrical Appliance Company Limited (“Kelon Household Electrical Appliance”)	Foshan	Manufacture and sale of household electrical appliances	RMB10,000,000	2,500,000.00	2,500,000.00	25%	75%	100%	100%
Guangdong Kelon Fittings Co., Ltd. (“Kelon Fittings”)	Foshan	Manufacture and sale of refrigerators and air-conditioner fittings	US\$5,620,000	44,851,319.79	44,851,319.79	70%	30%	100%	100%
Shunde Rongsheng Plastic Products Co., Ltd. (“Rongsheng Plastic”)	Foshan	Manufacture of plastic fittings	US\$15,800,000	86,987,729.73	86,987,729.73	45%	25%	70%	70%
Guangdong Kelon Mould Co., Ltd. (“Kelon Mould”)	Foshan	Manufacture of moulds	US\$15,000,000	82,474,115.40	82,474,115.40	40%	30%	70%	70%
Shunde Huaao Electronics Co., Ltd. (“Huaao Electronics”)	Foshan	Research and development, manufacture and sale of electronic products	RMB10,000,000	7,000,000.00	7,000,000.00	—	70%	70%	70%
Foshan Shunde Kelon Property Service Co., Ltd (“Kelon Property”)	Foshan	Enterprise consultancy management, catering, household decoration design	RMB1,000,000	927,821.40	927,821.40	—	100%	100%	100%
Shunde Wangao Import & Export Co., Ltd. (“Wangao I&E”)	Foshan	Import and export	RMB3,000,000	3,000,000.00	3,000,000.00	20%	80%	100%	100%
Shunde Jiake Electronic Company Limited (“Kelon Jiake”)	Foshan	IT and communication technology, and micro-electronics technology development	RMB60,000,000	60,000,000.00	60,000,000.00	70%	30%	100%	100%
Guangdong Kelon Weili Electrical Appliances Company Limited (“Weili Electrical Appliances”)	Zhongshan	Production of intelligent washing machine, air-conditioner and after-sale services and technology consultation for other products, 70% products for domestic sale	RMB200,000,000.00	—	—	55%	25%	80%	80%
Chengdu Kelon Refrigerator Co., Ltd. (“Chengdu Kelon”)	Chengdu	Manufacture and sale of refrigerators	RMB200,000,000	215,171,399.84	215,171,399.84	75%	25%	100%	100%
Hisense Ronshen Yingkou Refrigerator Co., Ltd. (“Yingkou Kelon”)	Yingkou	Manufacture and sale of refrigerators	RMB200,000,000	127,720,492.00	127,720,492.00	42%	36.79%	78.79%	78.79%

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT *(continued)*

1. Controlled subsidiaries: *(continued)*

Name of controlling company	Place of registration	Nature of Business	Registered Capital	Actual Investment Amount at the End of the Period	Actual Net Investment Balance to the Subsidiary	Shareholding of the Company			Percentage of Voting Rights
						Direct	Indirect	Total	
Jilin Kelon Electric Co., Ltd. ("Jilin Kelon")	Jilin	Development, manufacture and sale of refrigerator, air-conditioner, freezer and household electrical appliances	RMB200,000,000	200,000,000.00	200,000,000.00	90%	10%	100%	100%
Jiangxi Kelon Industrial Development Co., Ltd. ("Jiangxi Kelon")	Nanchang	Manufacture and sale of household and commercial air-conditioners, refrigerators, freezers and small electrical appliances	US\$29,800,000	256,552,718.23	256,552,718.23	60%	40%	100%	100%
Jiangxi Kelon Combine Electrical Appliances Co., Ltd. ("Jiangxi Combine") *1	Nanchang	Research and development, manufacture and sale of household and commercial air-conditioners, refrigerators, freezers and small household electrical appliances	RMB20,000,000	11,000,000.00	11,000,000.00	—	55%	55%	55%
Hangzhou Kelon Electrical Company Limited ("Hangzhou Kelon")	Hangzhou	Research and development of the technology for environmental friendly refrigerators, production of high efficiency, energy saving and environmental friendly refrigerators, information consultation, warehousing, and sale of the products made by the Company	RMB24,000,000	24,000,000.00	24,000,000.00	100%	—	100%	100%
Yangzhou Kelon Electrical Company Limited ("Yangzhou Kelon")	Yangzhou	Production of energy environmental friendly refrigerators and other energy saving cooling appliances, and sale of products made by the Company	US\$29,800,000	233,382,618.64	233,382,618.64	74.33%	25.67%	100%	100%
Shangqiu Kelon Electrical Company Limited ("Shangqiu Kelon")	Shangqiu	Research, development, production and sale of household and commercial air-conditioners, refrigerators, freezers, small household electrical appliances and parts and accessories, and provision of relevant information and technical consultancy services	RMB150,000,000	150,000,000.00	150,000,000.00	—	100%	100%	100%

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT (continued)

1. Controlled subsidiaries: (continued)

Name of controlling company	Place of registration	Nature of Business	Registered Capital	Actual Investment Amount at the End of the Period	Actual Net Investment Balance to the Subsidiary	Shareholding of the Company			Percentage of Voting Rights
						Direct	Indirect	Total	
Zhuhai Kelon Industrial Development Co., Ltd ("Zhuhai Kelon")	Zhuhai	Research and development of electric refrigerator, air-conditioner, freezer, small household electrical appliances and related accessories	US\$29,980,000	244,549,224.38	244,549,224.38	75%	25%	100%	100%
Xi'an Kelon Cooling Co., Ltd. ("Xi'an Kelon")	Xi'an	Development, manufacture, design, production of chlorofluorocarbon-free refrigerator (freezer) cooling compressor products; sale of products and conducting after-sale services, research and manufacture, development and production of new cooling compressor products subject to the market demands	RMB202,000,000	107,729,620.45	107,729,620.45	60%	—	60%	60%
Shenzhen Kelon Purchase Company Limited ("Shenzhen Kelon")	Shenzhen	Import and export, provision of warehouse and storage, information consultation and technology services (excluding those items limited)	RMB100,000,000	100,000,000.00	100,000,000.00	95%	5%	100%	100%
Beijing Hengsheng Xin Chuang Technology Company Limited ("Beijing Hengsheng")	Beijing	Research, development of industrial and commercial intelligent system	RMB30,000,000	24,000,000.00	24,000,000.00	80%	—	80%	80%
Beijing Kelon Tiandi IT Network Company Limited ("Beijing Tiandi")	Beijing	Operation items are under free-option, excluding those prohibited by laws and regulations	RMB5,000,000	5,000,000.00	5,000,000.00	—	78%	78%	78%
Beijing Kelon Shikong Information Technology Company Limited ("Beijing Shikong")	Beijing	Operation items are under free-option, excluding those prohibited by laws and regulations	RMB5,000,000	5,000,000.00	5,000,000.00	—	78%	78%	78%
Pearl River Electric Refrigerator Company Limited ("Pearl River Refrigerator")	Hong Kong	Trading in materials and parts for refrigerators	HK\$400,000	374,552.00	374,552.00	—	100%	100%	100%
Kelon Electric Appliances Co., Ltd. ("Kelon Electric Appliances")	Hong Kong	Property investment	HK\$10,000	9,363.80	9,363.80	—	100%	100%	100%
Kelon Development Company Limited ("Kelon Development")	Hong Kong	Investment holdings	HK\$5,000,000	11,200,000.00	11,200,000.00	100%	—	100%	100%
Wetherell Development Limited ("Wetherell Development")	British Virgin Islands	Advertising agency	US\$1	7.02	7.02	—	100%	100%	100%

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT (continued)

1. Controlled subsidiaries: (continued)

Name of controlling company	Place of registration	Nature of Business	Registered Capital	Actual Investment Amount at the End of the Period	Actual Net Investment Balance to the Subsidiary	Shareholding of the Company			Percentage of Voting Rights
						Direct	Indirect	Total	
Kelon (Japan) Limited ("Kelon Japan") *1	Japan	Technical research and trading in electrical household appliances	JP¥1,100,000,000	28,548,353.44	28,548,353.44		100%	100%	100%
Kelon (USA) Inc. ("Kelon USA")	USA	Business liaison	US\$100	2,186,269.39	2,186,269.39		100%	100%	100%
Kelon International Incorporation ("Kelon Int")	British Virgin Islands	Investment holding and sale of household electrical appliance	US\$1	7.31	7.31		100%	100%	100%
Sichuan Rongsheng Kelon Refrigerator Sales Company Limited ("Sichuan Kelon Sales")	Chengdu	Sale of refrigerator	RMB2,000,000	1,520,000.00	1,520,000.00	76%		76%	76%
Wuhu Ecan Motors Company Limited ("Wuhu Motors")	Wuhu	Production and sale of motor starter and permanent-magnet current brushless motor, micro alternating current machine and electrical equipment	US\$7,210,000	21,173,970.55	21,173,970.55	40%	40%	80%	80%
Kelon Europe Industrial Design Limited ("Kelon Europe") *2	United Kingdom	Business liaison	—	—	—		100%	100%	100%
Hisense (Chengdu) Refrigerator Co., Ltd. ("Hisense Chengdu")	Chengdu	Manufacture of household electric appliances, refrigerating equipment, sale of the Company's products and provision of related after-sale services	RMB5,000,000.00	1,968,190.00	1,968,190.00	75%	25%	100%	100%

- (1) The Company holds 100% shareholdings of Kelon Europe, 100% shareholdings of Japan Kelon, 55% shareholdings of Jiangxi Combine. The above companies have not been consolidated in the financial statements due to their smaller sizes.
- (2) Since the accounting method for long term equity investments has been changed from the equity method to the cost method, in preparing the consolidated statements, the gains and losses of long term equity investments recognized by the equity method on the accounts of the parent company and other companies have been adjusted and the provisions for equity investments have been reversed, and then the long term investments have been reverted to the initial investment amount. Upon consolidation, the adjusted gains and losses of long term investments and provisions for equity investments were first recognized in accordance with the equity method and then eliminated.
- (3) The Company holds 60% shareholdings of Kelon Air-conditioner, 70% shareholdings of Huao Electronics, but as the Company has committed to bear 100% of the liabilities of these companies, the long term equity investment was accounted for based on 100% beneficiary control.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT *(continued)*

1. Controlled subsidiaries: *(continued)*

(4) Changes in the scope of consolidation for the year are as follows:

① Jiangxi Kelon has transferred its 70% equity interest in Kaifeng Kelon to Henan Province Kaifeng Economic Technology Development (Group) Company and Kaifeng Kelon was no longer consolidated for the year; ② the Company and its wholly-owned subsidiary, Pearl River Refrigerator, established under joint capital contribution Hisense (Chengdu) Refrigerator Company Limited (“Hisense Chengdu”), which is consolidated; ③ during the year, the Company acquired 30% shareholdings of Chengdu Kelon from the minority shareholder, Chengdu Engine, at a consideration of RMB81,000,000. Since then, the Company holds 100% shareholdings of Chengdu Kelon.

Within the scope of consolidation, entities operating overseas whose accounts are denominated in foreign currency include Pearl River Refrigerator, Hong Kong Kelon Electric Appliances, Hong Kong Kelon Development, Wetherell Development, KII and Kelon USA. On the date of consolidation, we have translated the items under assets and liabilities at the prevailing exchange rate at the balance sheet date, whereas items under equity (except unallocated profits) were translated at the historic exchange rate, and items under profit and loss were translated at the average exchange rate. The difference between assets and liabilities and net assets was reflected in “exchange difference on foreign currency translation” and was shown separately under “equity” in the balance sheet.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

III. BUSINESS COMBINATION AND CONSOLIDATED FINANCIAL STATEMENT *(continued)*

1. Controlled subsidiaries: *(continued)*

Particulars of minority shareholders:

Name of subsidiaries	Minority interests	Amount of minority interests used to offset profit and loss of minority shareholders	Amount of parent company interests used to offset minority interests
Shunde Rongsheng Plastic Products Co., Ltd. (“Rongsheng Plastic”)	81,320,990.31	—	—
Guangdong Kelon Mould Co., Ltd. (“Kelon Mould”)	41,924,985.21	—	—
Guangdong Kelon Weili Electrical Appliances Company Limited (“Weili Electrical Appliances”)	(3,242,067.90)	—	—
Chengdu Kelon Refrigerator Co., Ltd. (“Chengdu Kelon”)	—	—	—
Hisense Ronshen Yingkou Refrigerator Co. Ltd. (“Yingkou Kelon”)	26,831,306.10	—	—
Kaifeng Kelon Air-conditioner Co., Ltd. (“Kaifeng Kelon”)	—	—	—
Xi’an Kelon Cooling Co., Ltd. (“Xi’an Kelon”)	—	—	3,665,132.28
Beijing Hengsheng Xin Chuang Technology Company Limited (“Beijing Hengsheng”)	3,872,175.36	—	—
Beijing Kelon Tiandi IT Network Company Limited (“Beijing Tiandi”)	1,087,850.94	—	—
Beijing Kelon Shikong Information Technology Company Limited (“Beijing Shikong”)	1,063,218.64	—	—
Sichuan Rongsheng Kelon Refrigerator Sales Company Limited (“Sichuan Kelon Sales”)	263,795.76	—	—
Wuhu Ecan Motors Company Limited (“Wuhu Motors”)	1,876,156.59	—	—
Total	154,998,411.01	—	3,665,132.28

Notes:

- During the year, Kelon Electric acquired 30% shareholdings of Chengdu Kelon held by Chengdu Engine (Group) Co., Ltd.. As a result, minority interests at the end of 2007 were nil;
- During the year, the Company disposed of Kaifeng Kelon and included the profit and loss of Kaifeng Kelon incurred from the beginning of the year to the date of disposal within the scope of consolidation for recognition as investment gains and minority interests;
- The profit and loss of minority shareholders of Xi’an Kelon for the year according to the actual investment proportion should be RMB-25,613,021.10, and the minority interests should be RMB-3,665,132.28. However, as the Company has undertaken to provide financial support to that company the carrying value of minority interests for that company would not be further reduced when it reduced to zero. Only RMB-21,947,888.82 of minority interests was recognized for the year, and the remaining loss of minority shareholders of RMB3,665,132.28 was assumed by Hisense Kelon.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting regulations and standards

The accounting policies adopted by the Company are in accordance with “Accounting Standards for Business Enterprises” and the supplementary regulations enacted by PRC Ministry of Finance.

2. Accounting year

The Company adopts the Gregorian calendar year as its accounting year, i.e. from 1 January to 31 December of each year.

3. Basis of accounting and principle of measurement

The Company maintains its accounting records on accrual basis. Assets are recorded at historical cost. However, certain fixed assets were restated at assessed value from 1999.

4. Reporting currency

The reporting currency of the Company is Renminbi (“RMB”).

5. Foreign exchange translation

Transactions in foreign currencies are translated into RMB at the applicable rates of exchange (“market exchange rate”) prevailing at the dates of transactions. Monetary accounts denominated in foreign currencies are translated into RMB at the market exchange rate prevailing at the balance sheet date. Gains and losses arising on exchange are included in financial expenses, except from those arising from the special foreign borrowings for the acquisition and construction of fixed assets which were included in the cost of assets before they are ready for use, and those arising in the pre-operating periods which were recorded as long term deferred expenditures for amortisation.

6. Basis of preparation for the consolidated accounting report

Subsidiaries under the control of the Company are within the scope of consolidation. Where the subsidiary adopts accounting policies different from those of the Company, adjustments are made in accordance with the accounting policies of the Company before consolidation. Where the accounting period of the subsidiary is different from that of the Company, the financial statements of the subsidiary will be adjusted in accordance with the accounting period of the parent company.

The equity method is used for acquisition of subsidiaries under the same controlling party by the Company, and the income, expenses and profits incurred from the beginning of the year to the date of consolidation are included in the consolidated statement of income, and the assets and liabilities that the merging party obtains in a business combination shall be measured on the basis of their carrying amount in the merged party on the date of combination. The purchase method is adopted for acquisition of subsidiaries not under the same controlling party to consolidate the accounts of the subsidiary from the dates of obtaining control over the subsidiary, and the identifiable assets and liabilities of the subsidiaries acquired are measured at fair value.

On the basis of full off-set, the unrealized profit and loss of the investments, inter-company accounts and internal transactions between the Company’s controlled subsidiaries and associates of beneficiary control are consolidated individually taking into the account of minority interests. Minority interests refer to third parties not being the Company and its subsidiaries who are entitled to a share of profit (or loss) in the subsidiaries of the Company. The equity method is adopted for joint ventures under the Company.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

7. Method for translation of foreign currency financial statements

The foreign currency financial statements of the Group's overseas subsidiaries are translated into RMB for consolidation by adopting the following methods:

Assets and liabilities are translated into RMB at the market exchange rate prevailing at the balance sheet date. Shareholders' equity, except for retained earnings, are translated into RMB at the market rates at transaction dates. All items in the statements of income and profit appropriation are translated at the applicable average exchange rates for the accounting period of the consolidated financial statements. Retained earnings at the beginning of the year represent the translated closing balance brought forward from the previous year; retained earnings at year end are arrived at after the translation of all other items in the income statement. The difference between translated assets and translated liabilities plus equity is shown separately in the balance sheet as exchange differences arising from the translation of the foreign currency in the financial statements under the item "Unappropriated profit".

The translation of cash flow has been made at the average foreign exchange rate. The effect of foreign exchange rate changes on cash will be treated as adjustments and is shown separately as "Effect of foreign exchange rate changes on cash" in the cash flow statement.

8. Cash equivalents

Cash equivalents are short-term (usually less than three months), highly liquid investments that are readily convertible to known amounts of cash and which are held by enterprises and subject to insignificant risk on changes in value.

9. Financial assets

Financial assets are initially classified as: Financial assets measured at their fair values and variation included into the current profits and losses, receivables, financial assets available for sale and held-to-maturity investments. The classification of financial assets depends on the intention and capability of holding of the Company and its subsidiaries.

(1) *Financial assets measured at their fair values and variation included into the current profits and losses*

Financial assets measured at their fair values and variation included into the current profits and losses, including transactional financial assets and financial assets designated to be measured at their fair values and whose variation is included into the current profits and losses.

(2) *Receivables*

Receivables refers to non-derivative financial assets that are not quoted and has fixed or defined recoverable value, including notes receivable, trade receivables, interests receivable, dividends receivable and other receivables.

(3) *Financial assets available for sale*

Financial assets available for sale include non-derivative financial assets designated as available for sale upon initial recognition and assets not classified as financial assets measured at their fair values and variation included into the current profits and losses, receivables and held-to-maturity investments. Financial assets to be disposed of within 12 months from the balance sheet date are classified as other current assets.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed (in RMB))

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Financial assets *(continued)*

(4) Held-to-maturity investments

Held-to-maturity investments refer to non-derivative financial assets with fixed maturity date, recoverable or defined amount which are held by the Company and its subsidiaries with definite intention and capacity. Held-to-maturity investments maturing within 12 months are classified as non-current assets maturing in one year on the balance sheet.

(5) Recognition and measurement

When the Company and its subsidiaries become a party of financial instrument contracts, the financial assets are initially recognized at fair value. For Financial assets measured at their fair values and variation included into the current profits and losses, the related transaction fees at acquisition are directly accounted for in the profit and loss of the period. The related transaction fees of other financial assets are accounted for as initially recognized amount. Where the contractual rights to receiving cash flow of certain financial assets are terminated or the ownership of the financial assets are substantially transferred to the transferee, the financial assets will ceased to be recognized.

Financial assets measured at their fair values and variation included into the current profits and losses and financial assets available for sale are subsequently measured at fair value.

The fair value of financial assets measured at their fair values and variation included into the current profits and losses are accounted for profit and loss of fair value changes; interests or cash dividends received during the asset-holding period are recognized as investment gains; upon disposal, the difference between the fair value and the carrying amount is recognized as investment profit and loss and profit and loss of changes in fair value is simultaneously adjusted.

Gain and loss from changes in fair value of financial assets available for sale (excluding impairment loss and exchange differences from financial assets in foreign currency) are directly accounted for shareholders' equity and is accounted for the profit and loss of the current period when the financial assets ceased to be recognized.

Receivables and held-to-maturity investments are amortized at cost using the actual interest method.

(6) Financial assets impairment

Except for financial assets measured at their fair values and variation included into the current profits and losses, the Company and its subsidiaries review the carrying value of the financial assets at the balance sheet date if there is any objective evidence that a certain financial asset is impaired, and impairment provision is made.

Where there is a relatively significant or non-temporary decrease in the fair value of financial assets available for sale, the accumulated loss arising from the decrease in fair value from the original amount directly included in the shareholders' equity is accounted for in the impairment loss. For equity instruments available for sale already recognized for impairment loss, the previously recognized impairment loss is reversed and accounted for in shareholders' equity when the fair value subsequently increases and is objectively related to the events happened after the previously recognized impairment loss.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

9. Financial assets *(continued)*

(6) Financial assets impairment (continued)

Where financial assets measured at amortized costs are impaired, the carrying amount of the financial assets are reduced to the present value of anticipated future cash flow (excluding future credit loss that has not happened yet), the reduced amount is recognized as impairment loss of asset and is accounted for in the profit and loss of the period. Where there is objective evidence that the value of the financial assets is recovered, and is objectively related to the events happened after the previously recognized impairment loss, the previously recognized impairment loss is reversed and accounted for in the profit and loss of the period.

For equity instruments that are not quoted on the active market and whose fair value cannot be reliably measured, impairment loss is not reversed when the value is recovered during subsequent periods.

10. Provision for bad debts

(1) Criteria for recognition of bad debts

- a. The irrecoverable amount for a debtor who becomes bankrupt after pursuing the statutory recovery procedures;
- b. The irrecoverable amount for a debtor who dies and has no offsetting estate and obligatory undertakers;
- c. The amount for a debtor who does not comply with repayment obligation after the debt becomes due, with sufficient evidence showing that such amount is irrecoverable or unlikely to be recovered.

(2) Accounting for provision for bad debts

Provisions for general bad debts and special bad debts are accounted for using the allowance method and provided based on with the recoverability of accounts receivable as at year end.

Provision for general bad debts against the account receivables for domestic customers is accounted for with reference to the aging analysis and the provision percentage is as follows:

Age	Provision percentage
Within 3 months	—
Over 3 months and within 6 months	10%
Over 6 months and within one year	50%
Over one year	100%

Bad debt provision is made against trade receivable from overseas customers by individually analyzing large-amount receivables and then bad debts are calculated by using the aging analysis of accounts.

The provision for bad debts of other debtors is provided for individually based on the nature of current accounts and the past experiences of the Company, the actual financial position and cash flows condition of the debtor, and other information.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

11. Inventories

Inventories are stated at actual cost of acquisition. Inventories include raw materials, work-in-progress and finished goods.

Standard cost is applied for the record of raw materials movement. At the end of each period, amortization for cost variances is made to the standard cost to arrive at the actual cost.

Actual cost is applied for the record of movement of work-in-progress and finished goods, and is recognized on a weighted average basis.

Inventories are kept on a periodic inventory system. Inventories at year-end are measured at the lower of cost and net realisable value. Provision for impairment loss of inventories is made when the cost of inventories is higher than the net realisable value because of damage, partially or totally obsolete or the sale price falling below the cost, etc. Provision for impairment loss of inventories is made on an individual basis for the difference between the cost and the net realisable value.

12. Long term equity investments

Long term equity investments include the Company's equity investments in subsidiaries, the Company's equity investments in joint ventures and associates, and the Company's long term investments in the investee that has no control, joint control or significant influence and is not quoted on the active market and the fair value cannot be measured reliably.

(a) Subsidiaries

Subsidiaries are investees in which the Company has power to govern the investees' financial and operating policies and receive benefits from its operating activities. In determining whether control can be exerted on the investee, the potential voting power of bonds convertible during the period, share options exercisable during the period of the investee are also considered. The investments in subsidiaries are set out as the amount recognized in the individual financial statements of the Company using the cost method, and is consolidated after being adjusted using the equity method when preparing the financial statements.

Long term equity investments accounted for using the cost method are measured in accordance with initial investment costs. Cash dividends or profits declared for distribution by the investee are recognized as investment gains for the period. Investment gains recognized are restricted to the allocated accumulated new profits generated after the investment is accepted by the investee, and the part of profit or cash dividend received exceeding the above amount is accounted for as recovery of initial investment costs.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

12. Long term equity investments *(continued)*

(b) Joint ventures and associates

Joint ventures are investees on which the Company and other parties exert joint control; associates are investee in which in the Company exert significant influence on its financial and operating decisions. Investments in joint ventures and associates are initially recognized at actual cost, and subsequently measured using the equity method. Where the initial investment cost exceeds the share of the fair value of the recognizable new assets of the investee, the difference is included in the initial investment cost; where the initial investment cost is below the share of the fair value of the recognizable new assets of the investee, the difference is accounted for in the profit and loss for the period and the cost of the long term equity investment is simultaneously adjusted. When the equity method is used for accounting, the investment profit and loss for the period is recognized based on the share of the profit and loss of the investee by the Company. Upon recognition of net loss of the investee, the carrying value of the long term equity investment and other long term equities that actually form net investment in the investee are debited to zero as a limit. However, where the Company has the additional liability to loss and where it conforms to the conditions of recognizing anticipated liabilities as required by the standard of contingent liabilities, the investment loss and anticipated liabilities are continually recognized. Changes of shareholders' equity of the investee other than net profit and loss are directly accounted for in the capital reserve for the part attributable in proportion to the Company's shareholding, assuming there is no change to the shareholding proportion. Profits or cash dividends distributed by the investee are set off against the carrying value of the long term equity investment upon the time of distribution in accordance with the part attributable to the Company. Unrealized profit and loss from transactions between the Company and the investee are set off within the scope of the equity of the investee held by the Company. However, when the assets transferred in the transaction are impaired, the corresponding unrealized loss is not set off.

(c) Other long term equity investments

For investees in which the Company has no control, joint control or significant influence, and which are not quoted on the active market and whose fair value cannot be reliably measured, they are accounted for using the cost method.

(d) Impairment of long term equity investments

Where the recoverable amount of long term equity investment is less than the carrying value, the carrying value is reduced to its recoverable amount.

13. Investment properties

The investment properties of the Company are classified as leased land use rights, land use rights held and intended for transfer after appreciation, and leased buildings.

The Company adopts the cost method for subsequent measurement of investment properties, and the depreciation or amortization method takes reference from the depreciation method for buildings under fixed assets and amortization method of land use rights under intangible assets, and method for impairment provision and calculation take reference from fixed assets and intangible assets.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed (in RMB))

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

14. Fixed assets and depreciation

Fixed assets are tangible assets held by the Company for production, provision of services, lease or operation, with useful life exceeding one year and with a relatively higher unit cost. Fixed assets are recorded at actual cost on acquisition. Depreciation is provided to write down the cost of each category of fixed assets over their estimated useful lives using straight-line method from the month after they are put into use. The estimated residual values, estimated useful lives and annual depreciation rates of each category of fixed assets are as follows:

Category	Estimated rate of residual value	Estimated Useful life	Annual depreciation rate
Buildings and structures	0-5%	20-50	2-4.75%
Machinery and equipment	5%	10-20	4.75%-9.50%
Furniture, fixtures and office equipment	5%	5	19%
Motor vehicles	5%	5	19%
Moulds	0%	3	33.33%

Provision for impairment of fixed assets:

At the end of each period, the Company assesses if there is any indication that fixed assets are suffered from an impairment loss case by case and determines whether provision for impairment of fixed assets should be made accordingly. When the recoverable amount of any fixed assets is lower than its carrying amount, an impairment loss on fixed assets will be recognised for the difference.

15. Construction in progress

Construction in progress is stated at actual cost incurred for the construction. Actual cost comprises construction expenditure incurred during the construction period, capitalised borrowing costs incurred on a specific borrowing for the construction of fixed assets before it has reached the working condition for its intended use and other relevant expenses. The construction in progress is transferred to fixed assets when it has reached the working condition for its intended use. No depreciation is provided for construction in progress.

Provision for impairment on construction in progress is made when the construction project is suspended for a long period and is not expected to be resumed within three years; the construction project is technically and physically obsolete and its economic benefits to the Company is uncertain; or other evidences can prove the existence of the decline in value of construction project. An impairment loss is recognised individually for the shortfall of the recoverable amount of construction in progress below its carrying amount.

16. Intangible assets

Intangible assets are stated at actual cost at acquisition. The actual cost of the intangible assets injected by the investors is determined by the value having been recognised by each party. The actual cost of acquired intangible assets is determined on the basis of the actual consideration paid. Intangible asset obtained with receivables is recognised at the book value of the receivables plus the cash compensation payable and the related tax expenses which are payable.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

16. Intangible assets *(continued)*

Intangible assets shall be amortised evenly by installments within the estimated tenure of use from the month of acquisition and shall be stated in the profit and loss. Where the estimated tenure of use exceeds the benefited tenure provided in the relevant contract or the valid tenure required by law, the term of amortisation shall not be longer than the benefited tenure or the valid tenure whichever is the shorter. Where it is impossible to foresee the term for which the intangible asset would generate economic benefits to the Group, the intangible asset is deemed as an intangible asset with indefinite life of use and is subject to review of life of use for each accounting period. When there is evidence that its life of use is definite, it will be reclassified as intangible asset with definite life of use. Intangible assets with indefinite life of use are not amortized.

Provision for impairment of intangible assets:

At the end of each period, the Company assesses if there is any indication that intangible assets are suffered from an impairment loss case by case. Where the recoverable amount of any intangible asset is lower than its carrying amount, an impairment loss on intangible assets is recognised for the difference.

17. Long-term deferred expenditures

Unless related to the acquisition or construction of fixed assets, all expenditure incurred during the preoperating period is recognised as an expense in the month in which the enterprise commences operation.

Long-term deferred expenditures are recorded at cost when incurred, and amortised evenly over the expected benefited period.

18. Impairment of assets

Goodwill and intangible assets with indefinite life of use separately set out in the financial statements are tested annually for impairment, notwithstanding whether there is evidence of impairment. Fixed assets, intangible assets, investment properties measured by the cost method and long term equity investments are tested for impairment if there is evidence of impairment at the balance sheet date. When the test result shows that the recoverable value of the asset is lower than its carrying value, provision is made for the difference and accounted for in impairment loss. The recoverable value is calculated as the fair value of the asset minus the higher of the net value after disposal fee and the estimated future cash flow of the asset. Provision for asset impairment is calculated and recognized on an individual basis. Where it is difficult to estimate the recoverable amount of an individual asset, the recoverable amount is determined for the asset group which the asset belongs. An asset group refers to the smallest group of assets capable of generating cash inflow individually.

19. Provision

Provision is recognised when obligations related to contingent items satisfy the following conditions: (1) such obligation is a present obligation of the enterprise, (2) it is probable that an outflow of economic benefits will be required to settle the obligation, and (3) a reliable estimate can be made of the amount of the obligation.

To the extent the amount payable for any provision will be compensated partly or wholly by a third party, such compensation will be recognised only when it is reasonably certain that the amount will be received.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

20. Borrowing costs

Borrowing costs represent costs incurred in connection with the borrowing of funds, including interest charges, amortisation of discount and premium, auxiliary costs, and exchange differences. Borrowing costs are capitalised if they are directly attributable to the acquisition, construction or production of a qualifying asset. Capitalisation of borrowing costs commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Borrowing costs are capitalised until the assets are ready for their intended use. Other borrowing costs are recorded as financial expenses when incurred.

21. Staff remunerations

Staff remunerations mainly include wages, bonus, allowances and compensation, staff benefits, social insurance premiums and housing fund, labour union expenditures and staff education fees, and other expenditures related to receiving the services provided by the staff. Staff remuneration is recognized for the period during which service is provided by the staff, and is included in the related asset costs and expenditures in accordance with the item benefiting from the provision of service by the staff.

22. Basis of revenue recognition

Sales revenue: Sales revenue is recognised when the Company and the subsidiaries have transferred the significant risk and rewards of ownership to the buyer; and the Company neither retains the continuous managing rights usually related to the ownership nor control over the goods sold; the economic benefits associated with the transactions will flow into the Company; and relevant revenue and cost can be reliably measured.

Service income: Service income is recognised when the amount of revenue can be measured reliably; the stage of completion can be measured reliably; the economic benefits associated with the transaction will flow to the enterprise and the costs incurred in respect of the transaction can be measured reliably.

Interest income: Interest income is recognised on a time proportion basis at the applicable interest rates.

23. Leases

Finance lease is the lease having actually transferred all the risks and rewards related to the ownership of assets. The leases other than the finance lease are operating leases.

Rental payment for operating leases is recognised as an expense at the straight line method over the lease term.

Rental income from operating leases is recognised as income at the straight line method over the relevant term.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

24. Income tax

Income tax is provided under tax payable method.

The Company determines its tax base upon acquisition of assets and liabilities. Where there is a difference between the carrying value of the assets and liabilities and the tax base, the deferred income tax assets or deferred income tax liabilities incurred as such are recognized as required. The Company recognizes deferred income tax assets arising from deductible temporal differences to the extent of the income tax payable probably available to off set the deductible temporal differences. For deductible loss and tax deduction that can be carried forward, the Company recognizes the corresponding deferred income tax assets to the extent of the future income tax payable probably available to off set the deductible loss and tax deduction.

At the balance sheet date, current income tax liabilities (or assets) incurred in the current and previous periods are measured at the anticipated income tax payable (or recoverable) amount calculated in accordance with the requirements of the tax laws. Deferred income tax assets and deferred income tax liabilities are measured at the applicable tax rates of the expected period of recovering the assets or settling the liabilities in accordance with the requirements of the tax laws. At the balance sheet date, the carrying value of the deferred income tax assets is reviewed. Where it is probable that the amount of taxable income in the future periods will not be sufficient to set off the benefits of the deferred income tax assets, the carrying value of the deferred income assets will be reduced. Where it is probable that the taxable income will be sufficient, the reduced amount will be reversed.

25. Changes in accounting policies and accounting estimates

- (1) The Ministry of Finance issued the “Accounting Standards for Business Enterprises” on 15 February 2006. Pursuant to the requirements of Accounting Standards for Business Enterprises No. 2 – Long Term Equity Investments, Accounting Standards for Business Enterprises No. 18 – Income Tax and other standards, the Company adopts 1 January 2007 as the date of initial implementation of the Accounting Standards for Business Enterprises, the influence of which on the shareholders’ equity at the beginning of the year is set out in Appendix 19. Apart from changing the accounting method for long term investments in subsidiaries by the parent company from the equity method to the cost method, reversing the differences of long term equity investments, adjusting the unallocated profit at the beginning of the year, and changing the accounting method for enterprise income tax from method of tax payable to balance sheet method during the period, there was no other changes of accounting policies. The effect on the Company for each year during the Reporting Period is as follows:

Changes in accounting policy	Effects on the profit accounted for each year			
	Amount at the beginning of 2006	2006	2007	Accumulated
1. Investment gains	60,646,847.60	(3,394,121.40)	—	57,252,726.20
2. Income tax charges	—	21,386,732.06	(10,087,064.29)	11,299,667.77
Subtotal	60,646,847.60	17,992,610.66	(10,087,064.29)	68,552,393.97

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IV. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(continued)*

25. Changes in accounting policies and accounting estimates *(continued)*

- (2) Pursuant to the requirements of “Memorandum No. 1 on Implementation of New Accounting Standards by Listed Companies on the Shenzhen Securities Exchange” issued by the Shenzhen Securities Exchange, bank acceptance notes received or made in the course of economic activities as payment for goods are not accounted for as receipt or payment of cash. During the prior years, the Company has accounted for them as cash received for sale of goods and provision of services and cash paid for purchase of goods and provision of services on the statement of cash flow. The Company has adjusted this accounting policy and no longer accounted for them as cash inflow on the statement of cash flow.

During the Reporting Period, the Company has adopted the retrospective restatement method to restate the financial statements of 2006. Due to changes in this accounting policy, cash received for sale of goods and provision of services of 2006 decreased by RMB3,565,225,783.22, and cash paid for purchase of goods and provision of services decreased by RMB3,565,225,783.22.

V. TAXATION

1. Value-added Tax

Output tax was calculated based on the 17% of sales revenue for products and industrial services sold in the domestic market, and was charged according to the balance after the deduction of input tax. Products sold to foreign countries are subject to the value-added tax (“VAT”) rate of 0%, with 13% of the VAT included in purchased raw materials refunded.

2. Enterprise Income Tax

The Company was established in Foshan, Guangdong Province and located in Shunde High New Technology Development Zone. The Company was classified as a high new technology enterprise by Department of Science and Technology of Guangdong Province in June 2003. As recognised by the managing tax authority — National Tax Bureau of Shunde, the Company is subject to enterprise income tax (“EIT”) at a rate of 15%. Together with the local EIT rate of 3%, the aggregate effective EIT rate is 18% in 2006.

The Company’s sino-foreign joint venture subsidiaries established in coastal open economic zones in Foshan, Yingkou are subject to an effective EIT rate of 27%.

The Company’s sino-foreign joint venture subsidiaries established in special economic zones in Shenzhen and Zhuhai are subject to an effective EIT rate of 15%.

The Company’s subsidiaries classified as high new technology enterprises are subject to an effective EIT rate of 15%.

The Company’s sino-foreign joint venture subsidiaries established in the economy and technology development zones in cities such as Yangzhou, Wuhu, Kaifeng and Xi’an are subject to an effective EIT rate of 15-18%.

The effective EIT rate applicable for the sino-foreign subsidiaries established in Nanchang and Chengdu is 33% and 24%, respectively.

The Company’s other subsidiaries established in Mainland China are subject to an EIT rate of 33%.

Profits tax for the Company’s subsidiaries in Hong Kong has been provided at a rate of 17.5% on estimated assessable profit which was earned in or derived from Hong Kong.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

V. TAXATION (continued)

3. Other taxes

Sales tax is levied at a rate of 5% on the assessable income.

Urban construction tax is levied at a rate of 1%-7% on the assessable circular tax.

Land appreciation tax ("LAT") is levied at a rate of 0.5-1% of assigned land income on the assignment of land use rights in accordance with relevant provisions set out in the document named "Reply Letter on Adjusting taxation rate of LAT of Land Use Rights" (Fo-fu-ban No. [2003]46) issued by the office of People's Government of Foshan.

Urban real estate tax is levied at a rate of 18% on rental income if the property is held for lease, or at a rate of 70% of the original value of the property multiplying 1.2%. Property owners are given three years' tax exemption commencing on the purchase date or completion date.

Bank protection fee is levied at a rate of 0.12% of the turnover for the applicable period, according to the relevant provisions set out in the Notice on Bank Protection Fee issued by Shunde Water Bureau and Shunde Municipal Tax Bureau.

Land use tax: Pursuant to the related requirements of the Notice of Bureau of Local Taxation of Shunde, Foshan Municipal on Reconfirmation of Land Grading for Land Use Tax and Applicable Tax Amount, it is calculated and levied at RMB4 per year per square metre.

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES)

1. Bank Balance and cash

Items	Items	Amount in original currencies	Exchange rate	At the end of the period	At the beginning of the period
Cash	RMB	1,299,300.03	1.00	1,299,300.03	204,329.73
	HKD	30,083.90	0.9364	28,169.97	30,140.10
	USD	—	—	—	435.33
	Others	—	—	—	78.45
Sub-total				1,327,470.00	234,983.61
Bank deposit	RMB	39,536,311.34	1.00	39,536,311.34	105,422,046.14
	HKD	18,468,137.13	0.9364	17,294,001.99	5,736,562.67
	USD	2,482,802.66	7.3046	18,157,692.06	30,544,829.24
	EUR	7,480.63	10.6669	79,795.13	298,326.02
	Others	—	—	—	9,758.46
Sub-total				75,067,800.52	142,011,522.53
Other monetary assets	RMB	70,087,731.60	1.00	70,087,731.60	248,173,813.93
	EUR	1.77	10.6669	18.87	148.93
	USD	6,131.23	7.3046	44,786.17	83,097.38
Sub-total				70,132,536.64	248,257,060.24
Total				146,527,807.16	390,503,566.38

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

1. Bank Balance and cash *(continued)*

The bank balance and cash at the end of the period as compared with the beginning of the period decreased by RMB243,975,759.22 or 62.48%. This was mainly due to reinforced capital management which substantially reduced the amount of idle capital utilization and therefore in other monetary assets.

2. Transactional financial assets

Item	Amount at the end of the period	Amount at the beginning of the period	Method of fair value determination
1. Transactional bond investments	—	—	
2. Transactional equity instrument investments	—	—	
3. Designated financial assets measured at their fair values and variation included into the current profits and losses	—	—	
4. Derivative financial assets *	9,479,410.00	—	
5. Others	—	2,000.00	
Total	9,479,410.00	2,000.00	

The Company has no material restriction for realizing its investments in transactional financial assets.

* It is mainly the undue foreign exchange forward contracts. The amount is calculated based on the market values of equivalent instruments on 31 December 2007.

3. Notes receivable

Type	At the end of the period	At the beginning of the period
Bank acceptance notes:		
– discounted	—	—
– pledged	—	28,200,000.00
– non-pledged	2,690,000.00	49,117,440.80
Commercial acceptance notes:		
– discounted	—	—
– pledged	—	—
– non-pledged	50,000.00	—
Total	2,740,000.00	77,317,440.80

The amount of notes receivable at the end of the year decreased by 96.46% as compared with that at the beginning of the year. It was mainly due to the Company has improve capital usage efficiency and collection of receivables.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

4. Trade receivables

a. The risks of trade receivables are classified as follows:

Category	Amount at the end of the period			Amount at the beginning of the period		
		Percentage	Provisions		Percentage	Provisions
	RMB	of the total	for bad debts	RMB	of the total	for bad debts
		%	RMB	RMB	%	RMB
I. Significant single-item amount*	—	—	—	—	—	—
II. Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics**	180,643,694.66	21.78	180,643,694.66	184,916,320.67	31.06	184,916,320.67
III. Greencool Companies	38,696,958.28	4.67	22,733,916.64	38,696,958.28	6.50	22,733,916.64
IV. Other not significant	609,850,753.97	73.55	7,247,782.91	371,787,502.53	62.44	12,839,260.13
Total	829,191,406.91	100.00	210,625,394.21	595,400,781.48	100.00	220,489,497.44
Total of the 5 largest	236,561,930.43	28.53	27,038,712.40	127,807,259.42	21.47	19,171,088.91
Amount receivable for appropriation by related parties	29,265,176.35	3.53	—	1,811,408.65	0.30	—

* Significant single-item receivables are classified as such when they account for 10% or more of the total amount of trade receivables.

** Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics are classified as such when the age analysis is over one year.

(1) There was RMB749,987.71 due from shareholders whose shareholding is no less than 5% at the end of the period. See Appendix 10.3.(1).

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

4. Trade receivables (continued)

a. The risks of trade receivables are classified as follows: (continued)

- (2) There were a series of related party transactions and abnormal cash flows between Greencool Companies and the Company during the period between October 2001 and July 2005, and moreover, during the period, the Greencool Companies also had a series of abnormal cash flows with the Company through the specified third-party companies such as Tianjin Lixin Trading Development Company Limited (hereinafter referred to as the "Specified Third Party Companies"). Set out below is the breakdown of the special bad debts provision made to the trade receivable from the Greencool Companies and the aforesaid Specified Third-Party Companies:

Name of companies	Amount at the end of the period	
	Amount	Provisions for bad debts
Hefei Weixi Electrical Appliance Co., Ltd ("Hefei Weixi")	18,229,589.24	7,805,094.62
Wuhan Changrong Electrical Appliance Company Limited ("Wuhan Changrong")	20,460,394.04	14,921,847.02
Total	38,689,983.28	22,726,941.64

Note: There was no change in the amount at the end of the period from the amount at the beginning of the period.

- (3) Particulars of the 5 largest trade receivables and the corresponding provisions for bad debts are as follows:

Name of companies	Amount at the end of the period	
	Amount	Provisions for bad debts
GOME	65,912,961.57	7,827,718.87
ELECTROLUX HOME PRODUCTS	65,637,815.87	3,079,205.52
HI GROUP PLC	55,121,342.26	106,905.02
WHIRL POOL	29,429,416.69	1,103,035.97
Wuhan Changrong Electrical Appliance Company Limited ("Wuhan Changrong")	20,460,394.04	14,921,847.02
Total	236,561,930.43	27,038,712.40

- (4) See Appendix 10.3.(1) and 10.3.(3) for particular of related parties.

- (5) Balance of trade receivables at the end of the period increased by 39.27% from the beginning of the period, due to the increase in the operation scale of the Company during the year.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

4. Trade receivables (continued)

b. Aging analysis of trade receivables are as follows:

Age	At the end of the period			At the beginning of the period		
	Amount	Percentage	Provision for bad debt	Amount total	Percentage	Provision for bad debt
		of total amount			of amount	
Within three months	582,810,692.01	70.28	—	280,031,134.56	47.03	—
Three months to six months	15,680,620.17	1.89	1,568,062.02	98,655,030.57	16.57	8,259,564.01
Six months to one year	11,359,441.79	1.37	5,679,720.89	9,064,379.04	1.52	4,579,696.12
One to two years	18,618,870.65	2.25	13,135,070.46	81,838,674.86	13.75	81,838,674.86
Two to three years	77,033,540.53	9.29	66,554,299.09	20,204,958.59	3.39	20,204,958.59
Over three years	123,688,241.76	14.92	123,688,241.75	105,606,603.86	17.74	105,606,603.86
Total	829,191,406.91	100.00	210,625,394.21	595,400,781.48	100.00	220,489,497.44

The Company's figures of trade receivables are as follows:

a. The risk analysis of the Company's figures of trade receivables are as follows:

Category	Amount at the end of the period			Amount at the beginning of the period		
	Amount RMB	Percentage	Provisions for bad debts RMB	Amount RMB	Percentage	Provisions for bad debts RMB
		of the total %			of the total %	
I. Significant single- item amount	65,912,961.57	11.34	7,827,718.87	48,001,496.08	11.51	—
II. Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics	152,230,097.57	26.18	152,230,097.57	170,515,360.39	40.87	170,515,360.39
III Greencool Companies	38,689,983.28	6.65	22,726,941.64	38,689,983.28	9.27	22,726,941.64
IV Other not significant	324,655,006.95	55.83	10,494,490.68	160,012,059.37	38.35	3,709,532.84
Total	581,488,049.37	100.00	193,279,248.76	417,218,899.12	100.00	196,951,834.87
Total of the 5 largest Amount receivable for appropriation by related parties	198,096,445.91 4,772.00	34.07 0.00	7,827,718.87 —	120,086,384.39 1,950.00	28.78 0.00	39,202,305.37 —

(1) There was no amount due from shareholders whose shareholding is no less than 5% at the end of the period.

Notes to the Financial Statements

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

4. Trade receivables (continued)

a. The risk analysis of the Company's figures of trade receivables are as follows: (continued)

(2) The Company has made provision for the bad debts of trade receivables from Greencool Companies and the Specified Third Party Companies as follows:

Name of companies	Amount at the end of the period	
	Amount	Provisions for bad debts
Hefei Weixi Electrical Appliance Co., Ltd ("Hefei Weixi")	18,229,589.24	7,805,094.62
Wuhan Changrong Electrical Appliance Company Limited ("Wuhan Changrong")	20,460,394.04	14,921,847.02
Total	38,689,983.28	22,726,941.64

b. Aging analysis of the Company's figures of trade receivables are as follows:

Age	At the end of the period			At the beginning of the period		
	Amount	Percentage	Provision for bad debt	Amount	Percentage	Provision for bad debt
		of total amount			of total amount	
Within three months	349,128,282.89	60.04	—	210,038,792.42	50.34	—
Three months to six months	14,739,716.13	2.54	1,473,971.62	8,148,423.73	1.95	814,842.37
Six months to one year	19,703,463.15	3.39	9,851,731.58	5,789,380.94	1.39	2,894,690.47
One to two years	11,995,272.11	2.06	11,995,272.11	79,035,852.86	18.94	79,035,852.86
Two to three years	77,162,230.80	13.27	61,199,189.16	10,458,514.59	2.51	10,458,514.59
Over three years	108,759,084.29	18.70	108,759,084.29	103,747,934.58	24.87	103,747,934.58
Total	581,488,049.37	100.00	193,279,248.76	417,218,899.12	100.00	196,951,834.87

5. Prepayments

Age	At the end of the period		At the beginning of the period	
	Amount RMB	Percentage of	Amount RMB	Percentage of
		total amount %		total amount %
Within one year	71,861,982.53	98.65	80,902,487.23	98.69
One to two years	39,440.93	0.05	239,170.39	0.29
Two to three years	510,284.79	0.70	540,322.02	0.66
Over three years	435,889.75	0.60	298,686.28	0.36
Total	72,847,598.00	100.00	81,980,665.92	100.00

There was no prepayment to shareholders whose shareholding is no less than 5% at the end of the period.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

6. Other receivables

a. The risk analysis of other receivables are as follows:

Category	Amount at the end of the period			Amount at the beginning of the period		
	Amount	Percentage	Provisions	Amount	Percentage	Provisions
		of the total	for bad debts		of the total	for bad debts
	RMB	%	RMB	RMB	%	RMB
I. Significant single-item amount*	—	—	—	169,355,132.63	18.17	84,427,566.32
II. Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics**	166,896,682.02	17.35	23,946,725.06	144,378,123.45	15.49	26,559,752.49
III. Greencool Companies	611,538,997.88	63.58	341,516,669.69	611,538,997.88	65.62	341,516,669.69
IV. Other not significant	183,481,581.58	19.07	3,281,088.46	6,660,346.58	0.72	3,681,420.24
Total	961,917,261.48	100.00	368,744,483.21	931,932,600.54	100.00	456,185,408.74
Total of the 5 largest	406,032,163.45	42.21	256,350,118.20	534,887,296.08	57.40	301,277,684.51
Amount receivable for appropriation by related parties	4,492,371.98	0.47	4,455,375.57	38,851,938.18	4.17	4,525,832.74

* Significant single-item receivables are classified as such when they account for 10% or more of the total amount of other receivables.

** Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics are classified as such when the age analysis is one year or more.

(1) There was no amount due from shareholders whose shareholding is no less than 5% at the end of the period.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

6. Other receivables (continued)

a. The risk analysis of other receivables are as follows: (continued)

(2) The Company has made provision for the bad debts of other receivables from Greencool Companies and the Specified Third Party Companies as follows:

Name of companies	Amount at the end of the period		Amount at the beginning of the period	
	Amount	Provisions for bad debts	Amount	Provisions for bad debts
Guangdong Greencool	13,754,600.00	7,962,961.47	13,754,600.00	7,962,961.47
Hainan Greencool Environmental Protection Engineering Co., Ltd. ("Hainan Greencool")	12,289,357.71	11,313,119.16	12,289,357.71	11,313,119.16
Jiangxi Kesheng Trading Company Limited ("Jiangxi Kesheng")	27,462,676.72	21,390,370.86	27,462,676.72	21,390,370.86
Jinan San Ai Fu Chemical Co., Ltd. ("Jinan San Ai Fu")	121,496,535.45	64,813,858.20	121,496,535.45	64,813,858.20
Tianjin Xiangrun Trading Development Company Limited ("Tianjin Xiangrun")	96,905,328.00	48,706,110.00	96,905,328.00	48,706,110.00
Tianjin Lixin Trading Development Company Limited ("Tianjin Lixin")	89,600,300.00	44,800,150.00	89,600,300.00	44,800,150.00
Greencool Technology Development (Shenzhen) Company Limited (Shenzhen Greencool Technology)	32,000,000.00	—	32,000,000.00	—
Greencool Environmental Engineering Shenzhen Company Limited (Shenzhen Greencool Environmental)	33,000,000.00	—	33,000,000.00	—
Jiangxi Keda Plastic Technology Co., Ltd ("Jiangxi Keda")	13,000,200.00	6,500,100.00	13,000,200.00	6,500,100.00
Zhuhai Longjia Refrigerating Plant Co., Ltd. ("Zhuhai Longjia")	28,600,000.00	14,300,000.00	28,600,000.00	14,300,000.00
Zhuhai Defa Air-conditioner Fittings Company Limited ("Zhuhai Defa")	21,400,000.00	10,700,000.00	21,400,000.00	10,700,000.00
Wuhan Changrong Electrical Appliance Company Limited ("Wuhan Changrong")	20,000,000.00	10,000,000.00	20,000,000.00	10,000,000.00
Beijing Deheng Solicitors	4,000,000.00	3,000,000.00	4,000,000.00	3,000,000.00
Finance Bureau of Yangzhou Economic Development Zone	40,000,000.00	40,000,000.00	40,000,000.00	40,000,000.00
Shangqiu Bingxiong Freezing Facilities Co., Ltd.	58,030,000.00	58,030,000.00	58,030,000.00	58,030,000.00
Total	611,538,997.88	341,516,669.69	611,538,997.88	341,516,669.69

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

6. Other receivables (continued)

a. The risk analysis of other receivables are as follows: (continued)

(3) Particulars of the 5 largest other trade receivables and the corresponding provisions for bad debts are as follows:

Name of companies	Amount at the end of the period	
	Amount	Provisions for bad debts
Jinan San Ai Fu Chemical Co., Ltd. ("Jinan San Ai Fu")	121,496,535.45	64,813,858.20
Tianjin Xiangrun Trading Development Company Limited ("Tianjin Xiangrun")	96,905,328.00	48,706,110.00
Tianjin Lixin Trading Development Company Limited ("Tianjin Lixin")	89,600,300.00	44,800,150.00
Shangqiu Binxiang Freezing Facilities Co., Ltd.	58,030,000.00	58,030,000.00
揚州經濟開發區財政局	40,000,000.00	40,000,000.00
Total	406,032,163.45	256,350,118.20

(4) See Appendix 10.3.(3) for particular of related parties.

(5) During the year, the Company transferred the land transfer amount due from Foshan Shunde Jiegao Investments Co., Ltd to 佛山市順德區順融投資有限公司. The principal of the receivable was RMB168,855,132.63, a bad debt of RMB84,427,566.32 was made and recognized, and the consideration of the transfer was RMB142,000,000.00. A non-operating income of RMB57,572,433.69 was recognized for the period.

b. Aging analysis of other receivables is as follows:

Age	At the end of the period			At the beginning of the period		
	Amount total	Percentage of amount	Provision for Bad Debt	Amount total	Percentage of amount	Provision for Bad Debt
Within one year	183,481,581.58	19.07	3,281,088.46	71,664,346.58	7.69	3,681,420.24
One to two years	67,802,710.48	7.05	4,066,845.99	808,237,698.18	86.73	435,927,721.65
Two to three years	660,468,257.15	68.66	345,449,747.42	12,037,266.32	1.29	11,264,633.24
Over three years	50,164,712.27	5.22	15,946,801.34	39,993,289.46	4.29	5,311,633.61
Total	961,917,261.48	100.00	368,744,483.21	931,932,600.54	100.00	456,185,408.74

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

6. Other receivables (continued)

a. The risk analysis of company figures of other receivables are as follows:

Category	Amount at the end of the period			Amount at the beginning of the period		
	Amount	Percentage	Provisions	Amount	Percentage	Provisions
		of the total	for bad debts		of the total	for bad debts
	RMB	%	RMB	RMB	%	RMB
I. Significant single-item amount*	500,559,716.17	44.08	—	661,734,769.62	43.90	—
II. Receivables not significant on a single-item basis but significant for the risk of the group of items upon grouping according to credit risk characteristics **	21,118,075.18	1.86	15,515,125.39	194,127,847.63	12.88	97,241,990.12
III. Greencool Companies	15,754,600.00	1.39	9,962,961.47	15,754,600.00	1.05	9,962,961.47
IV. Other not significant	598,068,320.82	52.67	172,212.70	635,766,772.47	42.17	3,253,506.15
Total	1,135,500,712.17	100.00	25,650,299.56	1,507,383,989.72	100.00	110,458,457.74
Total of the 5 largest	749,894,446.06	66.04	—	887,950,834.12	58.91	—
Amount receivable for appropriation by related parties	1,465,365.98	0.13	1,455,375.57	1,525,832.74	0.10	1,525,832.74

(1) There was no amount due from shareholders whose shareholding is no less than 5% at the end of the period.

(2) The Company has made provision for the bad debts of other receivables from Greencool Companies and the Specified Third Party Companies as follows:

Name of companies	Amount at the end of the period		Amount at the beginning of the period	
	Amount	Provisions for bad debts	Amount	Provisions for bad debts
Guangdong Greencool	13,754,600.00	7,962,961.47	13,754,600.00	7,962,961.47
Beijing Deheng Solicitors	2,000,000.00	2,000,000.00	2,000,000.00	2,000,000.00
Total	15,754,600.00	9,962,961.47	15,754,600.00	9,962,961.47

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

6. Other receivables (continued)

b. Aging analysis of the Company's figures of other receivables are as follows:

Age	At the end of the period			At the beginning of the period		
	Amount total	Percentage of amount	Provision for bad debt	Amount total	Percentage of amount	Provision for bad debt
Within one year	1,098,628,036.99	96.75	172,212.70	1,297,501,542.09	86.08	3,253,506.15
One to two years	6,788,994.26	0.60	1,888,323.78	196,318,174.98	13.02	94,309,996.43
Two to three years	17,909,655.75	1.58	11,814,371.09	11,611,669.18	0.77	10,942,351.69
Over three years	12,174,025.17	1.07	11,775,391.99	1,952,603.47	0.13	1,952,603.47
Total	1,135,500,712.17	100.00	25,650,299.56	1,507,383,989.72	100.00	110,458,457.74

7. Inventories and provision for inventories

Item	Carrying value at the beginning of the period	Increase during the period	Decrease during the period	Carrying value at the end of the period
1. Raw materials	245,529,272.47	6,957,236,217.95	6,962,648,033.01	240,117,457.41
2. Work-in-progress	46,413,227.41	6,673,646,890.67	6,668,734,165.39	51,325,952.69
3. Storage goods	750,377,339.50	7,705,782,938.96	7,737,882,059.80	718,278,218.66
4. Intermediate materials	—	35,729,975.64	33,529,022.17	2,200,953.47
5. Biological assets of consumptive nature	—	—	—	—
6. Materials in outside processing	—	23,227,829.77	23,202,350.09	25,479.68
Total	1,042,319,839.38	21,395,623,852.99	21,425,995,630.46	1,011,948,061.91
Consists of: Amount of capitalised borrowing costs	—	—	—	—

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1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

7. Inventories and provision for inventories (continued)

Provision for inventories:

Provision for inventories	Amount at the beginning of the period	Increase for the period	Decrease for the period			Percentage to balance at the end of period	Amount at the end of the period
			Reverse on appreciation of asset value	Reversal for other reasons	Total		
Raw Materials	61,479,234.24	11,194,987.09	—	23,852,778.17	23,852,778.17	48.86	48,821,443.16
Work-in-progress	12,485,014.20	127,752.28	—	1,356,051.49	1,356,051.49	12.05	11,256,714.99
Storage goods	48,518,968.32	589,612.00	2,043,484.92	35,479,581.34	37,523,066.26	323.88	11,585,514.06
Intermediate materials	—	—	—	—	—	—	—
Biological assets of consumptive nature	—	—	—	—	—	—	—
Materials in outside processing	—	—	—	—	—	—	—
Total	122,483,216.76	11,912,351.37	2,043,484.92	60,688,411.00	62,731,895.92	87.54	71,663,672.21

- (1) Provision for inventory was reversed by RMB2,043,484.92 due to appreciation of asset values.
- (2) Provisions made for inventory decreased by 41.49% as compared to the beginning of the period, which was attributable to the Company's efforts in disposal of unreasonable inventories such as raw materials, obsolete items and graded items accumulated during the prior periods to dispose ineffective inventory which reversed the corresponding impairment provisions.

8. Other current assets

Category	Amount at the end of the period	Amount at the beginning of the period
Deferred rent	67,944.39	125,000.00
Reconstructing costs	11,683,889.84	—
Others	3,624,647.80	418,661.62
Total	15,376,482.03	543,661.62

Reconstructing costs fee accounted for 75.99% of the balance at the end of the period, which represented agency fees incurred from the seasoned offering to the Company's major shareholder. It will be transferred into capital reserve after the seasoned offering.

Notes to the Financial Statements

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

9. Long-term equity investments

Item	At the end of the period			At the beginning of the period		
	Carrying balance	Provision for impairment	Carrying value	Carrying balance	Provision for impairment	Carrying value
Investment in subsidiaries	39,548,353.44	11,000,000.00	28,548,353.44	41,630,378.96	11,000,000.00	30,630,378.96
Investment in associates	99,155,748.36	—	99,155,748.36	95,297,792.96	—	95,297,792.96
Other equity investment	1,220,000.00	—	1,220,000.00	—	—	—
Total	139,924,101.80	11,000,000.00	128,924,101.80	136,928,171.92	11,000,000.00	125,928,171.92

Among which, particulars of joint ventures and associates are as follows:

Name of investee	Place of registration	Nature of business	Registered capital	Percentage of shareholding	Percentage of voting rights	Total assets at the end of period	Total operating income for the period	Net profit for the period
I. Associates								
1. Huayi Compressor Holdings Company Limited ("Huayi Compressor")	PRC	Manufacture and sale of compressors	RMB324,581,218	18.26%	18.26%	2,409,717,394.85	2,662,555,166.20	7,896,824.41
2. Chongqing Kelon Rongsheng Refrigerator Sales Co., Ltd. ("Chongqing Rongsheng")	PRC	Sales of refrigerators and after-sales services	RMB1,000,000	28%	28%	13,512,493.38	71,184,061.93	71,540.00
3. Guangzhou Antaida Logistic Co., Ltd. ("Antaida")	PRC	Integrated logistic and warehousing	RMB10,000,000	20%	20%	48,180,142.14	32,708,851.66	685,187.73

a. Investments in subsidiaries

Name of investee	Percentage of registered capital of investee	Original cost	At the beginning of the period	Change in equity during the period	Accumulated Changes in equity	At the end of the period
Japan Kelon	100%	31,716,666.40	30,630,378.96	(2,082,025.52)	(3,168,312.96)	28,548,353.44
Combine	55%	11,000,000.00	—	—	—	11,000,000.00
Total		42,716,666.40	30,630,378.96	(2,082,025.52)	(3,168,312.96)	39,548,353.44

Kelon Europe, Kelon (Japan) and Combine, controlling subsidiaries of the Company, are not consolidated as they are too small in size.

Investment to Japan Kelon is HK\$30,488,000.00, and RMB30,630,378.96 at exchange rate at the beginning of the year, and RMB28,548,353.44 at exchange rate at the end of the year; changes in equity for the period and accumulated are caused by changes in exchange rate.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

9. Long-term equity investments (continued)

b. Investments in associates

Name of investee	Percentage to registered capital of investee	Initial investment cost	Amount at the beginning of the period	Equity for the period Changes	Accumulated equity Changes	Amount at the end of the period
Chongqing Rongsheng	28%	280,000.00	384,664.55	20,031.19	124,695.74	404,695.74
Antaida	20%	2,000,000.00	4,118,121.36	137,037.54	2,255,158.90	4,255,158.90
Huayi Compressor	18.26%	118,013,641.00	90,795,007.05	3,700,886.67	(23,517,747.28)	94,495,893.72
Total		120,293,641.00	95,297,792.96	3,857,955.40	(21,137,892.64)	99,155,748.36

The investee, Huayi Compressor, completed share reform on 20 December 2006, the Company's original shareholding percentage was 22.725%. After completion of the share reform, the number of shares remained unchanged, and the shareholding percentage was diluted to 18.26%. As the Company still exerted significant influence on Huayi Compressor, the equity method was adopted for accounting purposes.

c. Other equity investments accounting for with the cost method:

Name of investee	Investment duration	Percentage to registered capital of investee	Initial investment cost	Balance at the beginning of the period	Increase for the period	Decrease for the period	Balance at the end of the period
Fujian Kelon Air-condition Sales Co., Ltd	10	2%	100,000.00	—	100,000.00	—	100,000.00
Foshan Huabao Air-condition Sales Co., Ltd	Long-term	2%	40,000.00	—	40,000.00	—	40,000.00
Xinjiang Hisense Kelon Electrical Sales Co., Ltd	10	2%	100,000.00	—	100,000.00	—	100,000.00
Zhibo Hisense Kelon Electrical Sales Co., Ltd	10	2%	120,000.00	—	120,000.00	—	120,000.00
Hunan Hisense Kelon Electrical Sales Co., Ltd	20	2%	200,000.00	—	200,000.00	—	200,000.00
Qingdao Hisense Kelon Electrical Sales Co., Ltd	10	2%	300,000.00	—	300,000.00	—	300,000.00
Yantai Hisense Kelon Electrical Sales Co., Ltd	10	2%	160,000.00	—	160,000.00	—	160,000.00
Linyi Hisense Kelon Appliances Air-condition Marketing Co., Ltd	10	2%	200,000.00	—	200,000.00	—	200,000.00
Subtotal			1,220,000.00	—	1,220,000.00	—	1,220,000.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

9. Long-term equity investments (continued)

d. Changes in provision for impairment

Name of investee	At the beginning of the period	Increase during the period	Reversal during the period	At the end of the period
Jiangxi Combine	11,000,000.00	—	—	11,000,000.00

Note:

- As at 31 December 2007, Pearl River Refrigerator pledged its 20% shareholdings in the subsidiary, Rongsheng Refrigerator, to the Guangzhou Branch of Shanghai Pudong Development Bank in respect of a finance in an amount of RMB60,000,000; the Company pledged its 42% shareholdings in Rongsheng Refrigerator to the Guangzhou Branch of Industrial Bank in respect of a finance in an amount of RMB90,000,000;
- On 15 December 2007, the Company entered into a “Termination of Joint Venture Relationship Agreement” with Kelon Development Company Limited (“Kelon Development”) and Hangzhou Xileng Group Company Limited (“Hangzhou Xileng”), pursuant to which the three parties agreed to terminate the joint venture relationship of the three parties by way of reducing the registered capital of Hangzhou Kelon, in which the investment amount of US\$7,230,000 would be reduced to zero for each of Kelon Development and Hangzhou Xileng, who would as a result withdraw from the joint venture operation of Hangzhou Kelon and terminate the joint venture relationship. Hangzhou Kelon became a wholly-owned subsidiary of the Company after the capital reduction;
- See Appendix 6 Note 44 for supplementary information on other investments.

Details of long-term investment companies are as follows:

Item	At the end of the period			At the beginning of the period		
	Carrying balance	Provision for impairment	Carrying value	Carrying balance	Provision for impairment	Carrying value
Investments in subsidiaries	1,860,745,181.00	59,381,641.00	1,801,363,540.00	1,777,857,181.00	59,381,641.00	1,718,475,540.00
Investments in associates	98,751,052.62	—	98,751,052.62	94,913,128.41	—	94,913,128.41
Other equity investment	1,220,000.00	—	1,220,000.00	—	—	—
Total	1,960,716,233.62	59,381,641.00	1,901,334,592.62	1,872,770,309.41	59,381,641.00	1,813,388,668.41

Among which, particulars of joint ventures and associates are as follows:

Name of investee	Place of registration	Nature of business	Registered capital	Percentage of shareholding	Percentage of voting rights	Total assets at the end of period	Total operating income for the period	Net profit for the period
1. Huayi Compressor Holdings Company Limited (“Huayi Compressor”)	PRC	Manufacture and sale of compressors	RMB324,581,218	18.26%	18.26%	2,409,717,394.85	2,662,555,166.20	7,896,824.41
2. Guangzhou Antaida Logistic Co., Ltd. (“Antaida”)	PRC	Integrated logistic and warehousing	RMB10,000,000	20%	20%	48,180,142.14	32,708,851.66	685,187.73

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

9. Long-term equity investments (continued)

a Investments in subsidiaries

Name of investee	Percentage of registered capital of investee	At the beginning of the period	Increase during the year	Decrease during the year	At the end of the period
Ronshen Refrigerator	70%	155,552,426.00	—	—	155,552,426.00
Kelon Air-conditioner	60%	281,000,000.00	—	—	281,000,000.00
Kelon Fittings	70%	32,634,554.00	—	—	32,634,554.00
Kelon Mould	40%	49,860,000.00	—	—	49,860,000.00
Rongsheng Plastic	45%	53,270,064.00	—	—	53,270,064.00
Chengdu Kelon	45%	90,000,000.00	81,388,000.00	—	171,388,000.00
Yingkou Kelon	42%	84,000,000.00	—	—	84,000,000.00
Beijing Hengsheng	80%	24,000,000.00	—	—	24,000,000.00
Kelon Development	100%	11,200,000.00	—	—	11,200,000.00
Kelon Jiake	70%	42,000,000.00	—	—	42,000,000.00
Sichuan Kelon Sales	76%	1,520,000.00	—	—	1,520,000.00
Kelon Freezer	44%	15,668,880.00	—	—	15,668,880.00
Wangao Company	20%	600,000.00	—	—	600,000.00
Kelon Household Electrical Appliance	25%	2,500,000.00	—	—	2,500,000.00
Jiangxi Kelon	60%	147,763,896.00	—	—	147,763,896.00
Jilin Kelon	90%	180,000,000.00	—	—	180,000,000.00
Hangzhou Kelon	100%	24,000,000.00	—	—	24,000,000.00
Yangzhou Kelon	74.33%	178,026,998.00	—	—	178,026,998.00
Zhuhai Kelon	75%	189,101,850.00	—	—	189,101,850.00
Xi'an Kelon	60%	107,729,620.00	—	—	107,729,620.00
Shenzhen Kelon	95%	95,000,000.00	—	—	95,000,000.00
Wuhu Motors	40%	12,428,893.00	—	—	12,428,893.00
Weili Electrical Appliances	55%	—	—	—	—
Hisense Chengdu	100%	—	1,500,000.00	—	1,500,000.00
Total		1,777,857,181.00	82,888,000.00	—	1,860,745,181.00

Note: According to the new Accounting Standards for Business Enterprises, enterprises change to adopt the cost method in accounting for the investments in subsidiaries and gains on investments are recognized upon consolidation. As the Company's practice in the prior years was to recognize the direct and indirect gains on investments, the Company has set off the amount of accumulated profit and loss included in the carrying value of long-term investments as at 1 January 2007 against the retained profit and capital reserve at the beginning of the period, and reversed the difference in the amount of amortization of long term equity investments. The adjusted amount of long-term investments represented the actual investment cost.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

9. Long-term equity investments (continued)

b. Investments in associates

Name of investee	Percentage of registered capital of investee	Original cost	At the beginning of the year	Change in equity during the year	Changes in accumulated equity	At the end of the year
Antaida	20%	2,000,000.00	4,118,121.36	137,037.54	2,255,158.90	4,255,158.90
Huayi Compressor	18.26%	118,013,641.00	90,795,007.05	3,700,886.67	(23,517,747.28)	94,495,893.72
Total		120,013,641.00	94,913,128.41	3,837,924.21	(21,262,588.38)	98,751,052.62

An investee, Huayi Compressor, completed its share reform scheme on 20 December 2006. The Company originally held 22.725% of Huayi Compressor's shares, and following completion of the share reform scheme the number of shares held by the Company remained unchanged but the percentage of its shareholdings was diluted to 18.26%. As the Company exercises substantial influence over Huayi Compressor, so Huayi Compressor is accounted for by using equity method.

c. Other equity investments accounting for with the cost method:

Name of investee	Investment duration	Percentage to registered capital of investee	Initial investment cost	Balance at the beginning of the period	Increase for the period	Decrease for the period	Balance at the end of the period
Fujian Kelon Air-Condition Sales Co., Ltd	10	2%	100,000.00	—	100,000.00	—	100,000.00
Foshan Huabao Air-condition Sales Co., Ltd	Long-term	2%	40,000.00	—	40,000.00	—	40,000.00
Xinjiang Hisense Kelon Electrical Sales Co., Ltd	10	2%	100,000.00	—	100,000.00	—	100,000.00
Zhibo Hisense Kelon Electrical Sales Co., Ltd	10	2%	120,000.00	—	120,000.00	—	120,000.00
Hunan Hisense Kelon Electrical Sales Co., Ltd	20	2%	200,000.00	—	200,000.00	—	200,000.00
Qingdao Hisense Kelon Electrical Sales Co., Ltd	10	2%	300,000.00	—	300,000.00	—	300,000.00
Yantai Hisense Kelon Electrical Sales Co., Ltd	10	2%	160,000.00	—	160,000.00	—	160,000.00
Linyi Hisense Kelon Electrical Sales Co., Ltd	10	2%	200,000.00	—	200,000.00	—	200,000.00
Subtotal			1,220,000.00	—	1,220,000.00	—	1,220,000.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

9. Long-term equity investments *(continued)*

d. Changes in provision for impairment of long-term investment

Name of investee	At the beginning of the period	Increase during the period	Decrease during the period	At the end of the period
Kelon Air-conditioner	59,381,641.00	—	—	59,381,641.00
Total	59,381,641.00	—	—	59,381,641.00

10. Investment properties

Items	At the beginning of the year	Increase during the year	Decrease during the year	At the end of the period
1. Total original value	92,447,073.99	19,250,325.79	54,342,033.60	57,355,366.18
Buildings and structures	92,447,073.99	19,250,325.79	54,342,033.60	57,355,366.18
2. Accumulated depreciation or amortisation	26,425,874.85	3,613,554.71	10,876,200.81	19,163,228.75
Buildings and structures	26,425,874.85	3,613,554.71	10,876,200.81	19,163,228.75
3. Total accumulated amount of provision for impairment of investment properties	1,478,266.30	—	1,478,266.30	—
Buildings and structures	1,478,266.30	—	1,478,266.30	—
4. Total book value of investment properties	64,542,932.84			38,192,137.43
Buildings and structures	64,542,932.84			38,192,137.43

- (1) The increase during the year is mainly due to the renting of Factory C of Company's subsidiary Yangzhou Kelon.
- (2) The decrease during the year is mainly due to the Company selling the property Kelon Home Appliances Park located at Ronggui Street Desheng Neighborhood Committee, No. 27, Rongqi Boulevard East, Shunde District;
- (3) As at 31 December 2007, the Company pledged the property located at No. 13, Ronggang Road, Shunde District for bank loans. The original value of the pledged asset is RMB13,982,230.43, and the net value is RMB2,568,132.00.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

11. Fixed assets and accumulated depreciation

Fixed assets, at cost	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	1,231,261,782.97	182,934,340.46	258,163,988.27	1,156,032,135.16
Machinery and equipment	1,874,697,683.45	139,985,010.57	320,635,920.18	1,694,046,773.84
Electronic equipment, fixtures and furniture	258,465,862.12	19,675,079.14	32,940,834.68	245,200,106.58
Motor vehicles	45,708,411.16	490,516.69	9,092,573.78	37,106,354.07
Moulds	225,923,955.56	75,473,304.54	73,601,695.30	227,795,564.80
Total	3,636,057,695.26	418,558,251.40	694,435,012.21	3,360,180,934.45
Accumulated depreciation	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	455,027,669.09	76,599,946.28	81,982,292.47	449,645,322.90
Machinery and equipment	1,269,149,328.15	104,572,369.35	206,958,093.71	1,166,763,603.79
Electronic equipment, fixtures and furniture	218,438,678.38	10,168,201.52	26,150,158.71	202,456,721.19
Motor vehicles	36,889,079.53	1,427,309.72	6,349,139.87	31,967,249.38
Moulds	116,571,258.17	56,742,715.12	44,005,381.62	129,308,591.67
Total	2,096,076,013.32	249,510,541.99	365,445,066.38	1,980,141,488.93
Provision for impairment	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	33,842,410.14	—	25,342,832.06	8,499,578.08
Machinery and equipment	147,556,567.18	15,646,156.99	33,850,850.49	129,351,873.68
Electronic equipment, fixtures and furniture	3,566,371.49	190,598.70	2,456,779.29	1,300,190.90
Motor vehicles	2,066,670.04	14,695.59	1,778,450.07	302,915.56
Moulds	22,181,175.70	262,855.57	16,355,145.60	6,088,885.67
Total	209,213,194.55	16,114,306.85	79,784,057.51	145,543,443.89
Net	1,330,768,487.39			1,234,496,001.63

(1) The increase in fixed assets during the period includes transfer from construction in progress of RMB272,999,507.21.

(2) The decrease in fixed assets with respect to buildings and structures is mainly due to disposal of the property located at 25/F, Harbour Centre, 25 Harbour Road, Wanchai, Hong Kong, the property located at No. 51 Shuangqing Road, Chenghua District, Chengdu City. And the property at the western section of Songcheng Road, Kaifeng City.

(3) As of 31 December, 2007, the original value of the Company's pledged buildings and structures is RMB748,133,957.85, and the net value is RMB444,444,280.65. The original value of pledged machinery and equipment is RMB126,627,846.39, and the net value is RMB21,033,100.89.

(4) the Company's subsidiary Xian Kelon ceased to operate in 2007; therefore, the provision made by the company for impairment of fixed asset is RMB16,050,000.00.

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

11. Fixed assets and accumulated depreciation (continued)

The company's figures of Fixed assets and accumulated depreciation are as follows:

Fixed assets, at cost	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	579,973,813.27	20,782,233.98	48,264,007.09	552,492,040.16
Machinery and equipment	158,963,355.60	1,025,311.73	665,838.00	159,322,829.33
Furniture, fixtures and office equipment	88,331,681.64	8,134,923.99	4,888,115.06	91,578,490.57
Motor vehicles	29,699,196.75	60,900.00	4,590,416.40	25,169,680.35
Moulds	—	—	—	—
Total	856,968,047.26	30,003,369.70	58,408,376.55	828,563,040.41
Accumulated depreciation	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	208,939,064.75	46,017,513.67	18,389,424.82	236,567,153.60
Machinery and equipment	101,795,958.51	5,994,235.68	590,767.00	107,199,427.19
Furniture, fixtures and office equipment	73,919,058.68	4,425,030.79	3,394,165.00	74,949,924.47
Motor vehicles	25,017,182.77	755,548.44	3,718,606.69	22,054,124.52
Moulds	—	—	—	—
Total	409,671,264.71	57,192,328.58	26,092,963.51	440,770,629.78
Provision for impairment	At the beginning of the year	Increase during the period	Decrease during the period	At the end of the year
Buildings and structures	—	—	—	—
Machinery and equipment	7,379,686.47	—	—	7,379,686.47
Furniture, fixtures and office equipment	304.11	—	—	304.11
Motor vehicles	—	—	—	—
Moulds	—	—	—	—
Total	7,379,990.58	—	—	7,379,990.58
Net	439,916,791.97			380,412,420.05

The increase in fixed assets during the period includes transfer from construction in progress of RMB6,419,579.49.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

12. Construction in progress

Project	At the beginning Name of the period	Increase during the period	Transfer to fixed assets during the period	Decrease during the period	At the end of the period	Source of capital
Project for reconstruction of Yangzhou Kelon factories	227,698,617.56	75,976,122.86	193,233,831.40	51,082,372.64	59,358,536.38	Self-raised
Project for Jiangxi Kelon production line	39,569,666.76	—	—	39,569,666.76	—	Self-raised
Project for reconstruction of Huabo Complex	—	2,844,390.95	2,597,990.95	—	246,400.00	Self-raised
Project for staff quarters of Kelon Electrical Appliances	—	16,790,050.63	—	—	16,790,050.63	Self-raised
Project for reconstruction of Hisense Chengdu Kelon factories	—	63,695,303.56	—	—	63,695,303.56	Self-raised
Project for Xi'an Power Control Company compressor production line	9,044,256.34	—	—	—	9,044,256.34	Self-raised
Others	60,993,668.12	53,707,967.62	77,167,684.86	7,472,979.45	30,060,971.43	Self-raised
Total	337,306,208.78	213,013,835.62	272,999,507.21	98,125,018.85	179,195,518.34	

- (1) There is no capitalisation of borrowing costs in increase of construction in progress during the year.
- (2) As at 31 December 2007, the land use right of RMB46,800,000 under the project for reconstruction of Yangzhou Kelon factories was pledged for bank loans.

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

12. Construction in progress (continued)

(3) Provision for impairment of construction in progress is set out below:

Project name	Balance at the beginning of the period	Increase during the period	Decrease for the year		Total	Balance At the end of the period
			Amount reversed for increase in asset value	Amount transferred out for other reasons		
Project for reconstruction of Yangzhou Kelon factories	13,811,879.00	—	—	—	—	13,811,879.00
Project for Jiangxi Kelon production line	23,244,968.30	—	—	23,244,968.30	23,244,968.30	—
Project for Xi'an Power Control Company Compressor Production line	1,181,652.30	9,044,256.34	—	—	—	10,225,908.64
Others	15,347,941.00	2,703,806.47	—	—	—	18,051,747.47
Total	53,586,440.60	11,748,062.81	—	23,244,968.30	23,244,968.30	42,089,535.11

(4) Provision for impairment of construction in progress was made during the year mainly because Xian Kelon and Shangqiu Kelon ceased to operate in 2007.

(5) Provision for impairment of construction in progress was transferred out during the year mainly because Jiangxi Kelon stopped production in the previous year and the construction in progress became obsolete in this year.

13. Fixed assets disposal

Items	At the end of the period	At the beginning of the period	Reason for disposal
Pre-paid tax expense due to disposal of land*1	5,125,440.00	—	In the process of changing the name of owner in a register
Others	24,309.16	—	
Total	5,149,749.16	—	

*1 It is mainly pre-paid tax expense related to the disposal of six plots of land. It will be converted into cost of disposal when the related proceeds is recognised

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

14. Intangible assets

Items	At the beginning of the year	Increase during the year	Decrease during the year	At the end of the period	Remarks
A. Total original value	1,112,135,160.54	123,185,023.54	53,980,274.84	1,181,339,909.24	
1. Land use rights	560,992,835.93	75,188,852.62	53,233,574.84	582,948,113.71	
2. Trademarks	521,857,698.95	—	—	521,857,698.95	
3. Know-how	—	43,711,180.00	—	43,711,180.00	
4. Others	29,284,625.66	4,284,990.92	746,700.00	32,822,916.58	
B. Accumulated amortisation	380,821,470.98	22,892,937.31	18,589,277.55	385,125,130.74	
1. Land use rights	228,181,793.41	18,962,844.25	18,552,279.62	228,592,358.04	
2. Trademarks	134,130,255.55	—	—	134,130,255.55	
3. Know-how	—	—	—	—	
4. Others	18,509,422.02	3,930,093.06	36,997.93	22,402,517.15	
C. Accumulated provision for impairment of intangible assets	312,805,723.50	18,464,851.33	—	331,270,574.83	
1. Land use rights	23,421,758.81	17,189,109.77	—	40,610,868.58	
2. Trademarks	286,061,116.40	—	—	286,061,116.40	
3. Know-how	—	—	—	—	
4. Others	3,322,848.29	1,275,741.56	—	4,598,589.85	
D. Total book value of intangible assets	418,507,966.06			464,944,203.67	
1. Land use rights	309,389,283.71			313,744,887.09	
2. Trademarks	101,666,327.00			101,666,327.00	
3. Know-how	—			43,711,180.00	
4. Others	7,452,355.35			5,821,809.58	

(1) The original value for Land use rights pledged for bank loans as of 31 December, 2007 was RMB311,144,486.53, while the net value was RMB226,035,461.60: By the audit report date, the pledged land of Kelon Freezer with original value of RMB31,513,280.00 and net value of RMB 23,950,093.28 has been released.

(2) Owing to uncertainty of the useful lives of the trademarks, the Company no longer amortise them during the year. No impairment of assets was found after an impairment test was conducted as alternative.

(3) Through Beijing Guo Tu Lian Real Estate Appraising Center Co., Ltd., it has been verified that three plots of land under Shangqiu Kelon were frozen by the local court. As at 31 December 2007, See Appendix 14 Note 1.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

15. Long-term deferred expenditures

Classification	Original amount	At the beginning of the period	Increase for the period	Amortisation for the period	Accumulated amortisation	At the end of the period	Remaining term for amortization
Fixed assets improvements	258,842.20	182,096.52	—	182,096.52	258,842.20	—	0 year
Others	6,495,020.10	698,355.00	2,043,320.10	518,886.62	4,272,231.62	2,222,788.48	1-4 years
Total	6,753,862.30	880,451.52	2,043,320.10	700,983.14	4,531,073.82	2,222,788.48	

16. Deferred income tax assets

Items	At the end of the period	At the beginning of the period	Description
Provision for bad debts	303,078.15	—	
Provision for inventories	85,343.62	—	
Provision for impairment of fixed assets	8,235,802.68	—	
Income tax-deductible loss	4,117,055.67	21,386,732.06	
Other temporary differences	(1,441,612.35)	—	Temporary differences such as accumulated depreciation, amortisation of intangible assets, etc.
Total	11,299,667.77	21,386,732.06	

According to the Company's annual profit forecasts for subsequent years, the deductible tax loss of RMB27,447,037.81 in 2007 can be reversed in 2008. Temporary differences such as provision for impairment of assets, accumulated depreciation and intangible assets, etc. amounted to RMB25,546,971.46 are expected to reverse in 2009 and after. Temporary differences such as accrued maintenance costs, litigation costs and forward exchange transactions, etc. in 2007, amounted to RMB5,305,794.91, are expected to be reversed in 2008.

There is a larger decrease from the deferred income tax assets at the end to that at the beginning of the year mainly because: (1) The profit for the year 2007 of subsidiaries who have recognised the deferred income tax assets causes a sharp decrease in deferred income tax assets which are part of the income tax-deductible loss; (2) the change of income tax rate causes a drop in the tax assets that can be reversed in the subsequent years.

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

16. Deferred income tax assets (continued)

Items not recognised as deferred income tax assets	At the end of the period	At the beginning of the period
Deductible temporary differences	970,414,104.09	1,060,866,202.52
1. Provision for bad debts	380,561,871.97	478,778,111.07
2. Provision for inventories	14,118,858.17	63,759,233.95
3. Provision for impairment of construction in progress	29,159,819.93	29,159,820.00
4. Provision for impairment of long-term equity investments	59,381,641.00	67,219,525.00
5. Fixed assets	115,694,069.50	127,350,795.81
6. Intangible assets	370,727,827.20	294,598,716.69
7. Other temporary differences	770,016.32	—
Deductible loss	2,170,959,853.79	1,846,122,942.40
1. 31 Loss expiring in December 2007	—	15,178,604.23
2. 31 Loss expiring in December 2008	7,068,280.99	25,601,287.16
3. 31 Loss expiring in December 2009	44,748,153.89	55,489,419.94
4. 31 Loss expiring in December 2010	1,097,025,350.23	1,235,870,472.31
5. 31 Loss expiring in December 2011	649,153,430.09	276,858,671.38
6. Loss expiring on 31 December 2012	145,267,289.10	—
7. Loss that can be carried forward indefinitely	227,697,349.49	237,124,487.38
Total	3,141,373,957.88	2,906,989,144.92

These items were not recognised as deferred income tax assets as it was foreseen that the future taxable profit available against which deductible temporary differences could be utilised exceeded the amount of tax payable.

17. Provision for impairment of assets

Items	At the beginning		Decrease during the year		At the end of the period
	of the year	Amount of the year	Reversal	Write-off	
1. Provision for bad debts	676,674,906.18	9,632,967.53	2,206,646.58	104,731,349.71	579,369,877.42
2. Provision for inventories	122,483,216.76	11,912,351.37	2,043,484.92	60,688,411.00	71,663,672.21
3. Provision for impairment of long-term equity investments	11,000,000.00	—	—	—	11,000,000.00
4. Provision for impairment of fixed assets	209,213,194.55	16,114,306.85	—	79,784,057.51	145,543,443.89
5. Provision for impairment of construction in progress	53,586,440.60	10,545,832.80	—	22,042,738.29	42,089,535.11
6. Provision for impairment of intangible assets	312,805,723.50	18,464,851.33	—	—	331,270,574.83
Total	1,385,763,481.59	66,670,309.88	4,250,131.50	267,246,556.51	1,180,937,103.46

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

18. Short term loans

Nature of loan	Currency	At the end of the year		At the beginning of the year	
		Original amount	RMB equivalent	Original amount	RMB equivalent
Guaranteed loan	RMB	148,160,319.00	148,160,319.00	263,708,629.32	263,708,629.32
Secured loan	RMB	953,221,901.34	953,221,901.34	599,493,619.20	599,493,619.20
Pledged loan	RMB	186,589,750.57	186,589,750.57	255,800,000.00	255,800,000.00
Credit loan	RMB	5,000,000.00	5,000,000.00	59,700,000.00	59,700,000.00
Bank acceptance notes financing	RMB	18,000,000.00	18,000,000.00	218,000,000.00	218,000,000.00
Commercial notes financing	RMB	—	—	160,000,000.00	160,000,000.00
Total			1,310,971,970.91		1,556,702,248.52

The balance of overdue loans of the Company as follows:

Borrowed by	Borrowing amount	Interest rate	Use of borrowings	Reason for overdue	Remark
Jilin Kelon	18,000,000.00	5.3625%	Operating purposes	Disposal of entire company which involved transfer of all debts and liabilities	*

* On 7 January 2008, the Company disposed of Jilin Kelon. See appendix 15.4

19. Transaction financial liabilities

Items	At the end of the period	At the beginning of the period
1. Issued transactional bonds	—	—
2. Financial liabilities at fair value through profit or loss	—	—
3. Derivative financial Liabilities*	6,157,782.89	—
4. Others	—	—
Total	6,157,782.89	—

* It is mainly the undue foreign exchange forward contracts. The amount is calculated based on the market values of equivalent instruments on 31 December 2007.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

20. Notes payable

Classification	At the end of the period	Amount due within one year
Bank acceptance notes	770,920,000.00	770,920,000.00
Commercial acceptance notes	39,940.00	39,940.00
Total	770,959,940.00	770,959,940.00

- (1) The year-end balance of Notes payable included no amount due to shareholders holding 5% or above (including 5%) of the share capital of the Company.
- (2) The balance at the end of the year increased by 51.75% compared to that at the beginning of the year, mainly due to the Company expanded sale scale, notes financing increased accordingly.

21. Trade payables

Age of account	At the end of the period		At the beginning of the period	
	Amount RMB	Percentage of total amount %	Amount RMB	Percentage of total amount %
Within one year	1,208,344,799.78	89.34	1,326,942,970.66	90.42
One to two years	53,354,398.45	3.95	117,470,523.08	8.00
Two to three years	70,801,361.57	5.23	16,303,055.92	1.12
Over three years	20,023,922.22	1.48	6,767,371.92	0.46
Total	1,352,524,482.02	100.00	1,467,483,921.58	100.00

The year-end balance of trade payables include no amount due to shareholders holding 5% or more (including 5%) of the share capital of the Company.

22. Advance from customers

- (1) The amount at year-end was RMB417,174,192.88, which included no amount due to shareholders holding 5% or above (including 5%) of the voting rights of the Company
- (2) The 45.13% decrease of the amount from period-end to year-beginning was attributed to advance from Hisense Agent decreased

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

23. Staff remuneration payables

Items	At the beginning of the year	Amount incurred during the period	Payment amount for the period	At the end of the period
A. Salaries, bonuses, allowances and subsidies	33,545,051.17	530,228,830.56	477,468,987.59	86,304,894.14
B. Staff welfare fund	977,300.17	14,335,515.53	14,467,124.71	845,690.99
C. Social insurance premium	—	—	—	—
1. Medical insurance premium	400,493.09	30,380,735.63	30,382,112.43	399,116.29
2. Basic endowment insurance premiums	496,175.34	7,879,421.76	7,881,127.49	494,469.61
3. Annuity	—	—	—	—
4. Unemployment insurance premium	51,271.97	760,436.28	760,612.54	51,095.71
5. Occupational injury insurance premium	11,239.86	736,976.44	737,015.08	11,201.22
6. Childbirth insurance premium	11,835.42	174,550.94	174,591.63	11,794.73
D. Housing provident fund employee education expenses	—	719,755.24	497,679.81	222,075.43
E. Labor union expenses and	1,500,795.28	4,083,663.94	2,272,594.76	3,311,864.46
F. Others	144,292.90	28,174,041.31	28,118,886.06	199,448.15
Total	37,138,455.20	617,473,927.63	562,760,732.10	91,851,650.73

24. Taxes payables

Tax	At the end of the period	At the beginning of the period
Value-added tax (Value-added tax to be credited)	(124,669,162.92)	(141,962,398.98)
Business tax	20,805,127.33	8,193,596.39
Urban Construction Tax	23,188.79	45,716.28
Education fees additional Charges	938.05	—
Enterprise Income tax	27,258,186.65	25,823,702.61
Real estate tax	2,929,020.22	271,865.72
Individual Income tax	1,697,593.46	471,314.23
Land use tax	2,965,155.33	4,070,164.79
Water system construction fund	1,347,345.40	—
Other	2,212,067.06	1,318,274.02
Total	(65,430,540.63)	(101,767,764.94)

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1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

25. Other payables

Age of account	At the end of the period		At the beginning of the period	
	Amount RMB	Percentage of total amount %	Amount RMB	Percentage of total amount %
Within one year	525,735,822.47	79.81	483,134,718.72	84.62
One to two years	50,104,789.20	7.61	51,276,158.94	8.98
Two to three years	50,835,300.66	7.72	11,630,975.32	2.04
Over three years	32,040,836.81	4.86	24,873,740.59	4.36
Total	658,716,749.14	100.00	570,915,593.57	100.00

The year-end balance included no amount due to shareholders holding 5% or more (including 5%) of the voting rights of the Company.

26. Other current liabilities

Items	At the end of the period	At the beginning of the period	Reasons for not settled
Installation fee	45,311,366.51	55,511,614.50	Provision made for the unpaid installation cost of sold products
Sales discounts	111,935,891.68	90,838,732.79	Occurred but not paid
Transportation fee	4,890,136.24	3,781,825.99	Occurred but not paid
Audit and listing fee	13,735,267.37	15,508,531.04	Provision made for audit fee and listing fee
Entertainment fee	32,187,877.18	20,451,092.40	Occurred but not paid
Capital utilization fee	28,483,822.05	19,799,822.42	Occurred but not paid
Others	56,138,250.09	41,185,834.15	Occurred but not paid
Total	292,682,611.12	247,077,453.29	

- (1) Other current liabilities at the end of the year increased by RMB45,605,157.83 with respect to the beginning of the year, mainly because of the expansion of sales in the period.
- (2) The entertainment fee in this period increased by RMB11,736,784.78 compared to that in previous period mainly because the sales during the period increased by RMB1,844,236,096.77 compared to that in previous period, registering a growth of 26.43%.
- (3) Capital utilization expenses represent the interest paid to Hisense Marketing for the capital occupancy. See Appendix 10.2 (6) for details.

Notes to the Financial Statements

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

27. Long-term payables

Long-term payables	At the end of the period	At the beginning of the period
Pension liabilities*	30,820,169.82	32,619,896.33
Special long-term payables**	24,532,364.90	27,952,397.90
Others	440,000.00	—
Total	55,792,534.72	60,572,294.23

* Pension liabilities represent the contributions paid by the employees and the Company, which are payable to the Employees after their retirement or resignation.

** Special long-term payables mainly represent the state debenture projects capital for technical advancement and Industry upgrade and other government exclusive financial grant.

28. Provision

Items	Balance at the end of the period	Balance at the beginning of the period
Litigation costs	11,516,899.81	4,212,299.81
Provision for maintenance*	132,488,674.45	165,782,783.11
Total	144,005,574.26	169,995,082.92

* The provision for maintenance is the estimated product quality guarantee fund. The Company provides for a three-year warranty for its products sold. During the warranty period, the Company will offer a free warranty service to the customers concerned. According to the industry's experience and past data, the warranty costs are calculated and provided based on the remaining years of offered warranty and the average repair fee per unit.

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1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

29. Share capital

Items	Increase (decrease) during the period							At the end of the period
	At the beginning of the period	Number of placing share	Number of bonus shares	Capitalized reserve fund	Additional issues	Others	Sub-total	
A. Restricted circulating shares	—	—	—	—	—	—	—	—
1. Promoter shares	—	—	—	—	—	—	—	—
Including: State owned shares	—	—	—	—	—	—	—	—
State legal person shares	—	—	—	—	—	—	—	—
Domestic legal person shares	—	—	—	—	—	—	—	—
Overseas legal person shares	—	—	—	—	—	—	—	—
Others	—	—	—	—	—	—	—	—
2. Non-promoter shares	—	—	—	—	—	—	—	—
Including: State owned shares	—	—	—	—	—	—	—	—
State legal person shares	262,212,194.00	—	(23,340,120.00)	—	—	—	—	238,872,074.00
Domestic legal person shares	75,703,561.00	—	—	—	—	—	—	75,703,561.00
Overseas legal person shares	—	—	—	—	—	—	—	—
Staff shares	71,000.00	—	8,520.00	—	—	(67,928.00)	—	11,592.00
Transferred allotted shares	—	—	—	—	—	—	—	—
Securities investment fund allotment	—	—	—	—	—	—	—	—
Strategic investment allotment	—	—	—	—	—	—	—	—
General legal person allotment	—	—	—	—	—	—	—	—
Unlisted individual shares	—	—	—	—	—	—	—	—
Others	—	—	—	—	—	—	—	—
3. Preference stock	—	—	—	—	—	—	—	—
Total number of restricted circulating shares	337,986,755.00	—	(23,331,600.00)	—	—	(67,928.00)	—	314,587,227.00
B. Non-restricted circulating shares								
1. Domestic listed ordinary shares denominated in RMB	194,430,000.00	—	23,331,600.00	—	—	67,928.00	—	217,829,528.00
2. Domestic listed foreign shares	—	—	—	—	—	—	—	—
3. Overseas listed foreign shares	459,589,808.00	—	—	—	—	—	—	459,589,808.00
Total number of non-restricted circulating shares	654,019,808.00	—	—	—	—	—	—	677,419,336.00
C. Total number of shares	992,006,563.00	—	—	—	—	—	—	992,006,563.00

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

29. Share capital (continued)

- The par value of the above shares is RMB1 per share. 75,703,561.00 shares became transferable on 29 March 2008.
- The changes in this year took place mainly because of the Share Reform Plan, the Company's non-transferable shares holder Hisense Air-conditioning allotted 1.2 shares of issued shares for every 10 transferable shares to holders of transferable A shares, involving totally 23,340,120.00 shares. After the consideration is executed, Hisense Air-conditioning's share account for 24.08%;
- Natural person non-circulating shares are executive ownership shares. The changes in this year is due to some non-circulating shares being converted to circulating shares and the consideration due to share reform.

30. Capital reserve

Items	At the beginning of the period	Increase during the period	Decrease during the period	At the end of the period	Reason and basis
Share premium	1,468,501,786.00	—	—	1,468,501,786.00	
Other capital reserve	139,600,341.20	1,610,973.03	71,356,464.73	69,854,849.50	
Total	1,608,102,127.20	1,610,973.03	71,356,464.73	1,538,356,635.50	

The capital reserve for this year increased is mainly due to the increase by RMB1,610,960.48 of the associate's capital reserve according to the investment proportion. The decrease in this year is due to the wholly-owned subsidiary Jiangxi Kelon decreased the capital reserve by RMB26,684,360.10 this year and that the Company purchased from the minority shareholder Chengdu Engine Group 30% stake of Chengdu Kelon, for which the amount paid exceeded the generated capital reserve RMB44,672,104.63 that the net assets enjoy proportionally.

31. Surplus reserve

Items	At the beginning of the period	Increase during the period	Decrease during the period	At the end of the period
Statutory common reserve	114,580,901.49	—	—	114,580,901.49

32. Unappropriated profits

At the beginning of the period	Increase during the period	Decrease during the period	At the end of the period
(3,697,957,232.42)	250,395,446.91	—	(3,447,561,785.51)

The unappropriated profit at the end of the year audited in 2006 is -3,776,596,690.68. This year adjustments are made according to the new Accounting Standards for Business Enterprises, correspondingly increasing the total unappropriated profit of RMB78,639,458.26 for the beginning of the year, including an increase of RMB57,252,726.20 in the unappropriated profit for the beginning of the year due to adjustment on the long-term equity investment difference, as well as a decrease of RMB21,386,732.06. in the income tax expense of the year 2006 due to adjustment on deferred income tax assets.

Notes to the Financial Statements

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

33. Revenue

(1) Details of Revenue and cost of sales classified by product segment are as follows

Items	Current period		Preceding period	
	Revenue	Cost	Revenue	Cost
1. Revenue from principal operations				
Refrigerators	4,320,754,737.40	3,485,537,876.16	3,326,980,129.96	2,630,625,473.64
Air-conditioners	3,215,279,886.83	2,746,967,853.85	2,536,816,403.41	2,165,789,630.25
Freezer	324,226,145.05	277,536,336.39	231,972,093.02	226,027,433.50
Small electrical appliances and others	461,556,481.18	435,402,273.84	469,473,018.44	451,272,851.75
Sub-total:	8,321,817,250.46	6,945,444,340.24	6,565,241,644.83	5,473,715,389.14
2. Revenue from other operations				
	Current period		Preceding period	
Items	Revenue	Cost	Revenue	Cost
Materials	400,548,030.20	335,621,078.99	389,538,912.68	277,716,595.88
Others	99,981,947.74	87,413,707.86	23,330,574.12	6,431,673.32
Sub-total:	500,529,977.94	423,034,786.85	412,869,486.80	284,148,269.20
Total	8,822,347,228.40	7,368,479,127.09	6,978,111,131.63	5,757,863,658.34
The aggregate amount of the top five	1,587,832,840.00		2,140,396,162.60	
Percentage to the aggregate	19.08%		32.60%	

(2) By geographic segment

Classification	2007		2006	
	Operational revenue	Operational cost	Operational revenue	Operational cost
Domestic	4,898,800,051.46	4,168,317,495.14	4,031,835,209.92	3,127,524,250.80
Overseas	3,423,017,199.00	2,777,126,845.10	2,533,406,434.91	2,346,191,138.34
Total	8,321,817,250.46	6,945,444,340.24	6,565,241,644.83	5,473,715,389.14

Notes to the Financial Statements

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

33. Revenue (continued)

The company's figures for revenues and costs classified by product segment are as follows:

Items	Current period		Preceding period	
	Revenue	Cost	Revenue	Cost
1 Revenue from principal operations				
Refrigerators	2,664,822,030.53	2,138,729,471.49	2,051,017,229.20	1,778,611,203.10
Air-conditioners	1,743,781,366.07	1,578,750,129.35	1,661,876,879.70	1,442,603,172.32
Freezer	44,926,641.76	41,270,117.01	103,720,687.88	89,862,046.24
Small electrical appliances and others	4,182,616.47	3,535,797.68	74,295,785.22	64,236,851.68
Sub-total:	4,457,712,654.83	3,762,285,515.53	3,890,910,582.00	3,375,313,273.34
2. Revenue from other operations				
Materials	326,848,510.01	325,314,888.63	128,093,073.87	125,927,834.87
Others	21,735,736.85	1,089,209.80	16,702,788.97	2,901,201.40
Service income	215,614,817.63	—	—	—
Sub-total:	564,199,064.49	326,404,098.43	144,795,862.84	128,829,036.27
Total	5,021,911,719.32	4,088,689,613.96	4,035,706,444.84	3,504,142,309.61

34. Distribution expenses

The amount incurred during the report period totaled RMB1,116,923,591.23, increased by RMB285,309,242.21 compared to the previous year, mainly because as the Company's revenue increased, distribution expense was increased correspondingly.

35. Financial expenses

Item	Current period	Preceding Period
Interest expenses	69,762,856.42	116,511,547.30
Less: Interest income	4,011,408.82	4,754,020.02
Exchange loss	41,120,907.23	28,542,983.29
Others	12,306,991.84	18,507,056.43
Total	119,179,346.67	158,807,567.00

Interest expense decreased by 40.12% compared to the previous year of 2006 mainly because the Company strengthened the fund management in this year, actively disposed of invalid capital occupancy, improve capital usage efficiency, significantly reduced the scale of financing, and correspondingly reduced interest expenses.

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

36. Asset impairment losses

Items	Current period	Preceding period
1. Bad debt loss	7,426,320.95	(86,243,637.24)
2. Impairment loss on inventories	9,868,866.45	42,700,140.04
3. Impairment loss on fixed assets	16,114,306.85	23,888,658.43
4. Impairment loss on construction in progress	10,545,832.80	1,496,239.73
5. Impairment loss on intangible assets	18,470,659.79	—
Total	62,425,986.84	(18,158,599.04)

37. Investment profit

Details of combined investment profit are as follows:

Total

Classification	Current period	Preceding period	Note
Proceeds during the periods:			
Dividend from associates and Joint venture	—	—	
Disposal of transactional financial assets	—	—	
Disposal of financial assets available for sale	—	—	
Profit on share of results of associates and Joint venture	2,246,994.93	3,588,175.99	
Profit on dealing with equity	4,509,461.06	—	
Total	6,756,455.99	3,588,175.99	

Details of the Company's investment profit is as follows:

Classification	Previous period	Preceding period	Note
Proceeds during the periods:			
Dividend from associates and Joint venture			
Disposal of transactional financial assets			
Disposal of financial assets available for sale			
Profit on share of results of associates and Joint venture	2,226,963.73	3,588,175.99	
Profit on dealing with equity			
Total	2,226,963.73	3,588,175.99	

- The profits distributed by associates or joint ventures are the paper gain enjoyed by the Company in accordance with the proportion of shares held. There is no major restriction on the inward remittance of investment profits.
- Jiangxi Kelon transferred in this year its 70% stake in Kaifeng Kelon to Henan Province Kaifeng Economic and Technological Development (Group) Corporation. The transfer generated totally RMB4,509,461.06 of investment profit.

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

38. Non-operating income/expenses

1. Non-operating income

Items	Current period	Preceding period
1. Gain on disposal of non-current assets	360,649,383.79	65,362,220.06
2. Disposal of receivable*	57,572,433.69	—
2. Gain from exchange of non-monetary assets	23,049.00	—
3. Penalty income	12,156,440.15	7,665,901.82
4. Gains of debt restructuring	—	—
5. Government subsidy	6,235,697.37	70,510,933.77
6. Inventory profit	228,369.67	4,238,372.60
7. Gain on donation	808,142.04	—
8. Others*	26,005,837.31	12,473,658.61
Total	463,679,353.02	160,251,086.86

The rise by RMB303,428,266.16 of year-end non-operating income compared to year-begin is mainly due to the Company's disposal in 2007 of non-current assets such as Chengdu Kelon's land use rights and Hong Kong Kelon Electrical's Harbour Centre.

* See Appendix 6 Note 6.

2. Non-operating expenses

Items	Current period	Preceding period
1. Loss on disposal of non-current assets	71,211,561.01	19,390,062.70
2. Loss from exchange of non-monetary assets	—	—
3. Penalty outlay	2,543,895.21	2,815,417.59
4. Debt restructuring loss	—	—
5. Charitable contribution expenses	220,455.26	1,483,116.01
6. Extraordinary loss	664,549.28	2,992,489.62
7. Losses on count deficit	—	(32,970.08)
8. Others	14,658,656.61	18,304,540.02
Total	89,299,117.37	44,952,655.86

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) *(continued)*

39. Income tax

a. Composition of income tax expense

Items	Current period	Preceding period
Income tax expense of the current period	780,323.17	515,965.59
Including: income tax expense incurred in the current year	780,323.17	515,965.59
Yearly income tax amount before current adjustment	—	—
Deferred income tax expenses	10,087,064.29	(21,386,732.06)
Including: deferred income tax incurred in the current year	581,850.04	(21,386,732.06)
Yearly deferred income tax amount before current adjustment	—	—
Effect of tax rate changes	9,505,214.25	—
Total	10,867,387.46	(20,870,766.47)

Income tax expense at the end of the period has increased significantly compared to that at the beginning of the year, because the Company's profit in 2007 caused a significant reduction in the deferred income tax assets belong to income tax-deductible loss. The increase of income tax expense in this period is relatively large.

b. Relationship between income tax expense and accounting profit

Items	Current period	Preceding period
Accounting profit	226,207,531.93	406,337.87
Tax at statutory rate of 33%	74,648,485.53	134,091.50
Add:		
1. Expenses not deductible for tax purposes	25,622,346.37	1,825,760.72
2. Difference in tax rate between regions or countries	(3,087,384.85)	1,559,569.48
3. Tax effect of tax losses and deductible temporary differences not recognised	19,790,517.35	171,950,200.55
Less:		
1. Revenue not taxable for tax purposes	9,502,543.05	289,849.26
2. Deductible estimated expenses	—	—
3. Effect of exemption granted and preferential tax treatment	60,315,204.75	16,777,280.02
4. Utilisation of tax losses and deductible temporary differences previously not recognised	36,288,829.14	179,273,259.44
income tax expense	10,867,387.46	(20,870,766.47)

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

40. Other cash related to operation activities

Items	Current period	Preceding period
Cash received from other operation activities		
Subsidy income	5,968,292.49	70,510,933.77
Penalty income, insurance compensation income	9,693,417.88	10,009,698.42
Deposit from suppliers, deposit for freight, etc	15,753,002.46	42,144,492.12
Sub-total	31,414,712.83	122,665,124.31
Cash paid for other operation activities		
Operation expenses	863,161,515.96	738,672,307.44
Administrative expenses	161,759,253.84	110,346,976.15
Financial expenses	1,306,096.25	1,455,822.06
Non-operating expenses and others	10,118,407.08	2,815,417.59
Sub-total	1,036,345,273.13	853,290,523.24
Total	(1,004,930,560.30)	(730,625,398.93)

41. Other cash related to investment activities

Items	Current period	Preceding period
Other cash received from investing activities		
Interest income	4,011,408.82	4,754,020.02
Sub-total	4,011,408.82	4,754,020.02
Cash paid for other investing activities	—	—
Total	4,011,408.82	4,754,020.02

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VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

42. Other cash related to financing activities

Items	Current period	Preceding period
Cash received from other financing activities		
Recovery of security bank deposit	178,124,523.59	—
Other receivables financing	142,000,000.00	—
Sub-total	320,124,523.59	—
Cash paid for other financing activities		
Repayment of Hisense capital support fund	191,004,000.00	110,000,439.20
Payment of restructuring agency fee	5,877,712.79	—
Payment of security bank deposit	—	145,443,544.84
Sub-total	196,881,712.79	255,443,984.04
Total	123,242,810.80	(255,443,984.04)

43. Cash and cash equivalents

Items	Current period	Preceding period
1. Cash	76,395,270.52	142,246,506.14
Including: cash on hand	1,327,470.00	234,983.61
bank deposit always available for payment	75,067,800.52	142,011,522.53
2. Cash equivalents	—	—
3. Cash and cash equivalents at the end of the period	76,395,270.52	142,246,506.14

44. relevant information on obtaining or disposing of subsidiaries and other operation units

I. Obtaining Subsidiaries and Other Operation Units

This year Hisense Kelon Electrical Holdings Company Limited (“Hisense Kelon”) and its subsidiary company Pearl River Electric Refrigerator Company Limited (“Pearl River Refrigerator”) jointly financed to set up Hisense (Chengdu) Refrigerator Co., Ltd (“Hisense Chengdu”). Hisense Chengdu applied to have a registered capital of RMB 5,000,000.00, in which Hisense Kelon subscribed 75% and Pearl River Refrigerator subscribed 25%. As on 31 December 2007, Hisense Kelon has made actual capital contribution of 1,500,000.00, and Pearl River Refrigerator has made actual capital contribution of 499,850.00.

This year Hisense Kelon Electrical Holdings Company Limited acquired from a minority shareholder Chengdu Engine (Group) Co., Ltd. 30% equity of Chengdu Kelon with an actual paid up price of 81,388,000.00. On the transaction date, Chengdu Kelon had a net book value of RMB122,386,317.90, in which paid in capital amounted to RMB200,000,000.00, and undistributed profit amounted to RMB-77,613,682.10.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VI. NOTES TO MAJOR ITEMS OF THE FINANCIAL STATEMENTS (UNLESS OTHERWISE SPECIFIED, THE FOLLOWINGS ARE COMBINED FIGURES) (continued)

44. Relevant Information on Obtaining or Disposing of Subsidiaries and Other Operation Units (continued)

I. Obtaining Subsidiaries and Other Operation Units (continued)

This year Hisense Kelon Electrical Holdings Company Limited and the staff of its branch and distributors made a joint investment to set up 8 companies, namely Xinjiang Hisense Kelon Electrical Sales Company Limited, Zibo Hisense Kelon Electrical Sales Company Limited, Linyi Hisense Kelon Electrical Sales Company Limited, Fujian Kelon Air-conditioner Sales Company Limited, Foshan Huabao Air-conditioner Sales Company Limited, Hunan Hisense Kelon Electrical Sales Company Limited, Qingdao Hisense Kelon Electrical Sales Company Limited, Yantai Hisense Kelon Electrical Sales Company Limited. The actual paid up capital of Hisense Kelon Electrical Sales Company Limited in these 8 companies are 2% in average. Since the shareholding ratio is low and it has no control or major influence to these 8 companies, the Company adopted Cost Method to conduct auditing on the investment of these 8 companies. As on 31 December 2007, these 8 companies have incurred no relevant operation activities.

II. Dispose of Subsidiaries and Other Operation Units

This year Jiangxi Kelon transferred without compensation 70% of equity it held in Kaifeng Kelon to Henan Province Kaifeng Economic Technology Development (Group) Company, where Henan Province Kaifeng Economic Technology Development (Group) Company shall take up all debts of Kaifeng Kelon. At the same time, Jiangxi Kelon, Kaifeng Kelon, Henan Kaifeng Economic Technology Development (Group) Company and Shangqiu Kelon, Hisense Kelon, Kelon Air-conditioner, Kelon Accessories, Huaao Electronics, Kelon Mould and Wuhu Yingjia jointly signed a claim and debt settlement agreement. Shangqiu Kelon, Hisense Kelon, Kelon Air-conditioner, Kelon Accessories, Huaao Electronics, Kelon Mould and Wuhu Yingjia agreed to transfer all their claims and debts with Kaifeng Kelon to Jiangxi Kelon. After the equities and debts of Jiangxi Kelon and Kaifeng Kelon have been off set, Kaifeng Kelon shall waive the receivables from Jiangxi Kelon amounted to 6,122,937.18, and promised not to claim such debt ever in future.

VII. GOVERNMENT SUBSIDY

(1) Categories of government subsidies and related amount included in the profit and loss of the period:

Categories of government subsidies	Amount included in profit and loss of prior years	Amount included in profit and loss of the period	Amount to be deferred	Total	Remark
I. Asset-related government subsidies					
1. National debt capital for enterprise technological advancement and industry upgrade	—	—	21,450,000.00	21,450,000.00	*1
II. Income-related government subsidies					
1. Support capital for independent multi-cycle project	—	2,425,256.64	—	2,425,256.64	*2
2. Capital for international market exploration and export credit insurance	—	2,969,024.78	—	2,969,024.78	*3
3. Allowance for technical reform and innovation	70,000,000.00	—	—	70,000,000.00	*4
4. Other government allowances	510,933.77	841,415.95	3,082,364.90	4,434,714.62	
Subtotal:	70,510,933.77	6,235,697.37	3,082,364.90	79,828,996.04	
Total	70,510,933.77	6,235,697.37	24,532,364.90	101,278,996.04	

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

VII. GOVERNMENT SUBSIDY (continued)

- *1 Government subsidies represented the award of RMB7,150,000 of special purposes fund under the national budget and RMB14,300,000 of special purposes fund under the local budget by the Bureau of Finance of Foshan Municipal to Kelon Electrical on 8 September 2004 according to Fojingmao [2004] No. 212 “Circulating the Circular of the Economy and Trade Commission, Development and Reform Commission and Bureau of Finance of the Province of “Circulating the Circular of NDRC and Ministry of Finance on the Release of the First Batch of 2004 National Debt Capital for Enterprise Technology Advancement and Industry Upgrade” under the principal of Fagaitouzi [2004] No. 1248 of National Development and Reform Commission and Department of Finance, in respect of the reform project of the enterprise’s information platform and resources management system for the introduction of hardware (including servers, network equipments), purchase of system software, construction of the enterprise’s information platform and resources management system.
- *2 The subsidy represented the support provided to Kelon Electrical on 9 December 2002 under Guojingmaojishu [2002] No. 845 “Circular of National Economy and Trade Commission, Development and Ministry of Financial on the Guidelines on Release of 2002 Fundings for Industry Upgrade Research and Development Capital (National Technological Innovation Project)”. On 24 August 2006, the project was inspected and approved by the Economy and Trade Commission of Guangdong Province under the certificate of inspection and approval Yuejingmaojiyanzi [2006] No. 042.
- *3 The capital for international market exploration represented the local funding for exploration of international market provided to Kelon Refrigerator , Kelon Air-conditioner and Wangao Company by the government of Shunde Municipal as an incentive and support for small to medium enterprises.
- *4 It represented the one-off allowance provided to the Company by Ronggui Street Office, Shunde District, Foshan City under the document “Shunrongguijiebanfu (2006) No. 29”.

VIII. SUPPLEMENTARY INFORMATION ON STATEMENT OF CASH FLOW

Supplementary information	Current period	Preceding period	Notes
1. Reconciliation of net profit to cash flows from operating activities:			
Net profit	215,340,144.48	21,277,104.34	
Add: Provision for impairment of assets	62,420,178.38	(324,998,831.94)	
Depreciation of fixed assets, oil/gas assets and productive biological assets	249,510,541.99	184,668,192.04	
Amortisation of intangible assets	22,892,938.19	35,200,966.36	
Amortisation of long-term deferred expenditures	700,983.14	1,419,486.85	
Loss from disposals of fixed assets, intangible assets and other long-term assets	(289,437,822.78)	(5,174,455.75)	
Losses on retirement of fixed assets	—	—	
Loss from change in fair value	(3,104,581.01)	—	
Financial expenses	65,751,447.60	111,757,527.28	
Investment loss	(6,756,455.99)	(3,588,175.99)	
Reduction of deferred income tax assets	10,087,064.29	(21,386,732.06)	
Increase of deferred income tax liabilities	—	—	
Decrease in inventories	(30,316,633.52)	601,149,607.29	
Decrease in operating receivable	(257,455,930.99)	452,080,053.51	
Increase in operating payable	(44,027,522.53)	(169,956,491.01)	
Others	—	—	
2. Major investing and financing activities not involving cash receipts and payment:			
Liabilities convert into assets equity	—	—	
Convertible company bonds due within one year	—	—	
Financial lease fixed assets	—	—	
3. Net change of cash and cash equivalents:			
Cash at the end of the period	76,395,270.52	142,246,506.14	
Less: Cash at the beginning of the period	142,246,506.14	184,284,027.53	
Add: Cash equivalents at the end of the period	—	—	
Less: Cash equivalent at the beginning of the period	—	—	
Net increase of cash and cash equivalents	(65,851,235.62)	(42,037,521.39)	

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

IX. LEASES

- (1) The Company has no fixed assets rented in or out in the form of financing lease.
- (2) Book values of leased assets of the Company as an operating lessor:

Category of operating leased asset	Book value at the end of the period	Book value at the beginning of the year
1. Buildings	38,192,137.43	64,542,932.84

- (3) Enterprises as operating lessees should disclose the following information with respect to major operating leases:

Remaining lease term	31 December 2007	31 December 2006
Within one year	2,195,616.74	2,589,965.37
Two to five years	456,594.34	1,116,463.59
Total	2,652,211.08	3,706,428.96

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

The transfer procedure of 26.43% shares of the Company held by Guangdong Greencool was completed on 13 December 2006. Following the share transfer, Hisense Air-conditioner has become the sole substantial shareholder of the Company.

There occurred a series of connected transactions and abnormal cash flow during the period from October 2001 to July 2005 between Guangdong Greencool Enterprise Development Limited (the former controlling shareholder of the Company) and its related parties (hereinafter referred to as the "Greencool Companies"). The above transactions and capital embezzlement was investigated by the relevant authority. In addition, abnormal cash flow occurred also between the Company and Tianjin Lixin (Please refer to note Appendix 10.1(4) for details) during the period from October 2001 to July 2005. These items involved the accounts receivable from and account payable to Greencool and the specified third parties on 31 December 2007.

Please refer to Appendix 10.2 for details of the connected transactions between the Company and Hisense Group in 2007.

1. Related party relationships

- (1) *Related parties with controlling interests include*

Name of related parties	Enterprise category	Legal representative	Registered Capital	Business Scope	Shares or interests held	Relationship with the Company
Hisense Air-conditioner	Sino-foreign joint venture company	Tang Ye Guo	674,790,000	*	24.08%	Controlling shareholder
Hisense Group	Solely State-owned	Zhou Hou Jian	806,170,000	**	—	Ultimate controlling shareholder
Combine	Limited liability company	Fang Zhi Guo	20,000,000	***	55.00%	Unconsolidated subsidiary of the Company

* Manufacture of air-conditioners, moulds and after-sale service.

** Trust Operation of State-Owned Property of manufacture, sale and services of household appliances and communication products.

*** Research, manufacture and sale of air-conditioners, household electrical appliances and after-sale service.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

1. Related party relationships *(continued)*

(2) *Greencool Companies*

Name of related parties	Relationship with the Company
Guangdong Greencool Enterprise Development Company Limited	Former controlling shareholder of the Company
Greencool Environmental Protection Engineering (Shenzhen) Co., Ltd. “Greencool Technology Environmental Protection (Shenzhen)”	Related party of Guangdong Greencool
Greencool Technology Development (Shenzhen) Company Limited (“Greencool Technology Development (Shenzhen)”)	Related party of Guangdong Greencool
Greencool Procurement (Shenzhen) Co., Ltd. (“Greencool Procurement”)	Related party of Guangdong Greencool
Hainan Greencool	Related party of Guangdong Greencool
Jiangxi Greencool Electrical Appliance Company Limited (“Jiangxi Greencool”)	Related party of Guangdong Greencool
Hefei Meiling Holdings Limited Related party of Guangdong Greencool (“Meiling Holdings”)	Related party of Guangdong Greencool
Yangzhou Yaxing Motor Coach Company Limited (“Yangzhou Yaxing”)	Related party of Guangdong Greencool

(3) *Related parties with no controlling interests include:*

Name of related parties	Relationship with the Company
Huayi Compressor	Associate of the Company
Chongqing Kelon	Associate of the Company
Antaida	Associate of the Company
Chengdu Engine (Group) Company Limited (“Chengdu Engine”)	Minority shareholder of Chengdu Kelon
Chengdu Xinxing Electrical Appliance Holdings Company Limited (“Chengdu Xinxing”)	Subsidiary of the minority shareholder of Chengdu Kelon
Xi’an Gaoke Group Company	Minority shareholder of Xi’an Kelon
Hangzhou Xileng Group Company Limited (“Hangzhou Xileng”)	Minority shareholder of Hangzhou Kelon
Jiaxibeila Compressor Company Limited (“Jiaxibeila”)	Subsidiary of an associate
Shunde Yunlong Consultancy	Minority shareholder of Huao Electronics
Hisense Marketing	Subsidiary of controlling shareholders
Hisense Zhejiang	Subsidiary of controlling shareholders
Hisense Nanjing	Subsidiary of controlling shareholders
Hisense Beijing	Subsidiary of controlling shareholders
Hisense Shandong	Subsidiary of controlling shareholders
Qingdao Hisense Import& Export Co., Ltd.	Subsidiary of controlling shareholders
Hisense-Hitachi Air-conditioner System Co., Ltd.	Subsidiary of controlling shareholders

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X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

1. Related party relationships *(continued)*

(4) *The Greencool Companies had a series of transactions or abnormal cash inflow/outflow through the following “Specified Third Party Companies”*

Name of related parties	Relationship with the Company
Jiangxi Kesheng	Specified third party companies
Zhongshan Dongyue Electrical Co., Ltd. (“Dongyue Zhongshan”)	Specified third party companies
Jinan San'ai'fu	Specified third party companies
Tianjin Xiangrun	Specified third party companies
Tianjin Lixin	Specified third party companies
Jiangxi Keda Plastic Technology Company Limited (“Jiangxi Keda”)	Specified third party companies
Refrigerant Production Consultants Limited	Specified third party companies
Hefei Weixi	Specified third party companies
Zhejiang Guoda Trading Company Limited (“Zhejiang Guoda”)	Specified third party companies
Zhuhai Longjia	Specified third party companies
Zhuhai Defa	Specified third party companies
Wuhan Changrong	Specified third party companies
Tianjin Taijin Yunye Company Limited (“Tianjin Taijin Yunye”)	Specified third party companies
Chengdu Refrigerating Components Factory	Specified third party companies
Beijing De Heng Solicitors	Specified third party companies
Shangqiu Bingxiong Freezing Facilities Company Limited (“Shangqiu Bingxiong”)	Specified third party companies

(5) *Movements in the Company's share capital or equity held by related parties with controlling Interest*

Name of related party	At the beginning of the period	Increase during the period	Decrease during the period	At the end of the period
Hisense Air-conditioner	262,212,194.00	—	23,340,120.00	238,872,074.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

2. Transactions with related parties

(1) *Purchases of goods*

Items	Name of companies	2007	2006
Purchases of products from	Chengdu Xinxing	—	25,235,907.94
	Huayi Compressor	67,300,337.07	35,327,742.94
	Jiayi Beila	154,501,449.14	92,650,029.09
	Hisense Air-conditioner	—	17,503.34
	Hisense Shandong	120,955,728.40	—
	Hisense Marketing	—	209,729,271.60
	Hisense Zhejiang	334,424,034.91	69,854,091.13
	Hisense Nanjing	105,329,153.55	1,829,885.47
	Hisense Beijing	34,241.51	5,519,658.12
Total		782,544,944.58	440,164,089.63

On 5 February 2007, Kelon Electric, Kelon Refrigerator, Kelon Air-conditioner, Kelon Mould (hereinafter referred to as “Party A”) and Hisense Beijing, Hisense Nanjing, Hisense Air-conditioner, Hisense Zhejiang, Hisense Electric Qingdao Saiwei (hereinafter referred to as “Party B”) hereby signs the “Business Cooperation Framework Agreement”, in which it is stipulated that during the period from 1 January 2007 to 31 December 2007, Party A and Party B shall negotiate and agree a price for Party A to purchase from Party B not more than RMB942,500,000, in which Kelon Electric shall accept labour service from Qingdao Saiwei of not more than 10,000,000; Kelon Refrigerator shall purchase raw materials from Hisense Beiing of not more than 25,000,000 and shall assign the manufacturing of finished refrigerator products of not more than 110,000,000; Kelon Refrigerator shall purchase raw materials from Hisense Nanjing not more than 10,000,000 and shall assign the manufacturing of finished refrigerator products of not more than 160,000,000; Kelon Air-conditioner shall purchase raw materials from Hisense Air-conditioner of not more than 20,000,000 and shall assign Hisense Air-conditioner to manufacture finished air-conditioner products of not more than 270,000,000; Kelon Air-conditioner assigns Hisense Zhejiang to manufacture finished air-conditioner products of not more than 337,500,000. During this period Hisense Air-conditioner is detached and forms a newly setup subsidiary called Hisense Shandong Air-conditioner Company Limited (“Hisense Shandong”). After detachment Hisense Shandong shall continue to bear the business rights and responsibilities of this Agreement.

Major terms of the “Business Cooperation Framework Agreement” are as follows:

- (1) Party A and Party B, with reference to the market price of refrigerators and air-conditioners, as well as industry OEM product pricing standards, shall negotiate and agree on the purchasing price.
- (2) In accordance to the following standards, Party A and Party B shall agree on the settlement price of single refrigerator and air-conditioner units:

The settlement price for Party A to purchase single refrigerator and air-conditioner units from Party B Manufacturing cost for Party A to produce single refrigerator and air-conditioner units (Shunde headquarters or other bases) + Management fee + Transportation cost of single refrigerator

Upon full consideration of the above standards and the relevant manufacturing fee and management fee for Party A, with reference to transaction price in the market, both parties hereby negotiate and confirm that the transaction price of various customize refrigerator products are:

Price of a specific refrigerator model ordered by Party A from Party B = Fixed cost of the same refrigerator model of Party A/0.93

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

2. Transactions with related parties *(continued)*

(1) Purchases of goods *(continued)*

Upon full consideration of the above standards and the relevant manufacturing fee and management fee for Party A, with reference to transaction price in the market, both parties hereby negotiate and confirm that the transaction price of various customize air-conditioner products are: Price of a specific air-conditioner model ordered by Party A from Party B = Fixed cost of the same air-conditioner model of Party A/0.95

This year Party A purchased from Party B a total amount of 560,743,158.37.

On 5 February 2007, Kelon Freezer, Kelon Air-conditioner, Kelon Refrigerator, Yingkou Kelon Refrigerator, Hangzhou Kelon Electric, Chengdu Kelon Refrigerator, Yangzhou Kelon Electric (hereinafter referred to as "Party A") and Huayi Compressor Co., Ltd., Jiaxibeila Compressor Co., Ltd., and Huayi Compressor (Jingzhou) Co., Ltd. signed the "Compressor Purchase and Supply Framework Agreement" with the contract that during the period from 1 January 2007 to 31 December 2007, Party A and Party B negotiated and agreed that Party A shall purchase from Party B a total amount of not more than 336,000,000, in which Kelon Freezer shall purchase from Huayi Compressor not more than 29,930,000; Kelon Air-conditioner shall purchase from Huayi Compressor (Jingzhou) not more than 4,280,000; Kelon Refrigerator shall purchase from Huayi Compressor not more than 59,830,000; Kelon Refrigerator shall purchase from Jiaxibeila Compressor not more than 102,600,000; Kelon Refrigerator shall purchase from Huayi Compressor (Jingzhou) not more than 9,406,000; Yingkou Kelon shall purchase from Huayi Compressor not more than 11,130,000; Yingkou Kelon shall purchase from Jiaxibeila Compressor not more than 41,881,000; Hangzhou Kelon shall purchase from Huayi Compressor not more than 1,710,000; Hangzhou Kelon shall purchase from Jiaxibeila Compressor not more than 13,676,000; Chengdu Kelon shall purchase from Huayi Compressor not more than 8,550,000; Chengdu Kelon shall purchase from Jiaxibeila Compressor not more than 22,230,000; Yangzhou Kelon shall purchase from Huayi Compressor not more than 7,700,000; Yangzhou Kelon shall purchase from Jiaxibeila Compressor not more than 23,077,000.

This year Party A purchased from Party B a total amount of 221,801,786.21.

(2) Sale of Goods

Item	Company Name	Year of 2007	Year of 2006
Sale of goods	Chengdu Xinxing	—	3,336,588.68
	Chongqing Kelon	64,756,401.98	39,600,955.87
	Hisense Marketing	192,254.47	1,572,695,090.00
	Hisense Zhejiang	9,692,607.24	7,252,794.06
	Hisense Nanjing	429,021.14	—
	Hisense BeiJing	110,302,681.64	—
	Hisense Shandong	132,725,100.06	—
	Hisense Import & Export	5,669.00	265,885.64
	Hisense Hitachi	—	285,932.31
		17,661.49	355,574.71
Total		318,121,397.02	1,623,792,821.27
Ratio of total sales		3.82%	24.73%

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

2. Transactions with related parties *(continued)*

(2) *Sale of Goods (continued)*

On 5 February 2007, Kelon Electric, Kelon Refrigerator, Kelon Air-conditioner, Kelon Mould (hereinafter referred to as "Party A") and Hisense Beijing, Hisense Nanjing, Hisense Air-conditioner, Hisense zhejiang Hisense Electric and Qingdao Saiwei (hereinafter referred to as "Party B") signed "Business Cooperation Framework Agreement" with the contract that during the period from 1 January 2007 to 31 December 2007, Party A and Party B negotiated and agreed on a price that Party A shall sell to Party B a total amount of not more than 845,500,000, in which Kelon Refrigerator shall sell raw materials from Hisense Beijing of not more than 10,000,000 and shall manufacture finished refrigerator products of not more than 212,500,000; Kelon Refrigerator shall sell raw materials to Hisense Nanjing of not more than 8,000,000; Kelon Air-conditioner shall sell finished air-conditioner products to Hisense Air-conditioner of not more than 580,000,000 and sell raw materials of not more than 8,000,000; Kelon Air-conditioner shall sell raw materials of not more than 9,000,000; Kelon Mould shall sell finished mould products to Hisense Electric of not more than 10,000.00 and shall sell Qingdao Hisense Air-Conditioning mould products of not more than 8,000,000. During this period Hisense Air-conditioner is detached and forms a newly setup subsidiary called Hisense Shandong Air-conditioner Company Limited ("Hisense Shandong"). After detachment Hisense Shandong shall continue to bear the business rights and responsibilities of this Agreement.

Major terms of the "Business Cooperation Framework Agreement" are as follows:

- (1) Party A and Party B, with reference to the market price of refrigerators and air-conditioners, as well as industry OEM product pricing standards, shall negotiate and agree on the purchasing price.
- (2) In accordance to the following standards, Party A and Party B shall agree on the settlement price of single refrigerator and air-conditioner units:

The settlement price for Party A to sell single refrigerator and air-conditioner units to Party B \geq Manufacturing cost for Party A to produce single refrigerator and air-conditioner units (Shunde headquarters or other bases) + Management fee + Transportation cost of a single refrigerator

Upon full consideration of the above standards and the relevant manufacturing fee and management fee for Party A, with reference to transaction price in the market, both parties hereby negotiate and confirm that the transaction price of various customize refrigerator products are:

Price of a specific refrigerator model ordered by Party B from Party A = Fixed cost of the same refrigerator model of Party A/0.93

Upon full consideration of the above standards and the relevant manufacturing fee and management fee for Party A, with reference to transaction price in the market, both parties hereby negotiate and confirm that the transaction price of various customize air-conditioner products are:

Price of a specific air-conditioner model ordered by Party B from Party A = Fixed cost of the same air-conditioner model of Party A/0.95

This year Party A sold to Party B a total amount of 253,149,410.08.

(3) *Sales of fixed assets*

Items	Name of related parties	2007	2006
Sales of moulds to	Hisense Electric	—	2,554,273.50
	Hisense Marketing	—	648,718.00
Sales of equipments to	Hisense Zhejiang	—	300,198.74
	Hisense Shandong	8,202.44	—
Hisense Shandong		8,202.44	3,503,190.24

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

2. Transactions with related parties *(continued)*

(4) Use of land and buildings

A subsidiary of the Company, Jiangxi Kelon, has since October 2003 used the land and buildings of Jiangxi Greencool located in Jiangxi Kelon Greencool Industrial Park. Another subsidiary of the Company, Zhuhai Kelon, has established its small refrigerator manufacturing facility in the land and buildings of the Company's substantial shareholder Greencool. As at 31 December 2007, Jiangxi Kelon and Zhuhai Kelon had not signed any asset rent agreement with the counterparty.

(5) Sales commission

As at 31 December 2007, the commission payable to Hisense Marketing amounted to RMB13,178,420.01 and the capital utilisation fee amounted to 28,483,822.05.

(6) Other transactions

Items	2007	2006
Other amounts received from or (paid to) related parties		
— Amount paid to Hisense Marketing for capital utilization	8,683,999.63	16,390,172.45
— Logistics management fee paid to Antaida	29,656,708.96	51,538,372.05
— Electric and water utilities paid to Chengdu Engine	7,057,356.01	6,467,760.10
— Equipment rent paid to Hangzhou Xileng	—	6,000,000.00
— Services fee paid to Guangzhou Antaida	103,027.32	103,305.56

(7) Guarantees

As at 31 December 2007, Hisense Group Co. Ltd., the beneficial controller of the Company, provided the Company with guarantees for the borrowings of RMB488,000,000 and for the bank acceptance notes of RMB633,500,000.

3. Transactions with related companies and "Specified Third Party Companies"

(1) Transactions with the related companies under control of the Company

Items	Name of related companies	At the end of the year	At the beginning of the year
Trade receivables	Hisense Air-conditioner	749,987.71	335,121.67
Trade payables	Hisense Air-conditioner	—	8,790,332.47
Prepayments	Hisense Air-conditioner	—	490,796.57
Other payables	Combine	5,099,880.00	5,099,880.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

3. Transactions with related companies and “Specified Third Party Companies” *(continued)*

(2) Transactions with Greencool Companies

Items	Name of related companies	At the end of the year	At the beginning of the year
Trade receivables	Hefei Meiling	6,975.00	6,975.00
Other receivables	Guangdong Greencool	13,754,600.00	13,754,600.00
	Shenzhen Greencool Environmental	33,000,000.00	33,000,000.00
	Shenzhen Greencool Technology	32,000,000.00	32,000,000.00
	Hainan Greencool	12,289,357.71	12,289,357.71
Trade payables	Hefei Meiling	50,125.18	50,125.18
Other payables	Jiangxi Greencool	13,000,000.00	13,000,000.00

(3) Transactions with the related companies not controlled by the Company

Items	Name of related companies	At the end of the year	At the beginning of the year
Trade receivables	Chongqing Kelon	424,410.21	107,070.00
	Hisense Marketing	20,163.00	436,224.01
	Hisense Zhejiang	—	590,285.77
	Guangzhou Antaida Logistic Co. Ltd.	4,772.00	8,166.40
	Hisense Hitachi	—	334,540.80
	Hisense Beijing	28,065,843.43	—
Prepayment	Hisense Nanjing	—	730,450.00
	Chengdu Engine	—	47,000,000.00
	Qingdao Saiwei	15,539.26	—
Other receivables	Antaida	—	31,635.44
	Chengdu Engine	—	190,964.00
	Chengdu Xinxing	—	34,000,000.00
	Shunde Yunlong	4,455,375.57	4,525,832.74
	Hisense Marketing	27,006.00	103,506.00
	Qingdao Saiwei	9,990.41	—
Trade payables	Huayi Compressor	11,586,357.99	13,739,250.30
	Chengdu Xinxing	—	11,815,976.65
	Jiaxi Beila	20,208,615.83	12,905,409.58
	Hisense Marketing	47,152.00	—
	Hisense Beijing	—	1,284.40
	Hisense Nanjing	2,708.98	279,020.60
	Hisense Zhejiang	109,236,376.72	—
	Hisense Shandong	54,486,956.95	—

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

X. RELATED PARTY RELATIONSHIPS AND RELATED PARTY TRANSACTIONS *(continued)*

3. Transactions with related companies and “Specified Third Party Companies” *(continued)*

(3) *Transactions with the related companies not controlled by the Company (continued)*

Items	Name of related companies	At the end of the year	At the beginning of the year
Advance from customers	Chongqing Kelon	—	4,082,988.12
	Hisense Marketing	10,206,688.31	290,164,676.95
	Hisense Nanjing	542,576.24	—
	Qingdao Saiwei	45,112.00	—
Other payables	Antaida	7,612,684.75	20,651,902.63
	Xi’an Gaoke	1,785,476.00	1,785,476.00
	Hangzhou Xileng	—	15,772,269.71
	Chengdu Engine	108,840.00	5,308,840.00
	Huayi Compressor	200,000.00	200,000.00
	Jiaxi Beila	—	100,000.00
	Qingdao Saiwei	2,004,769.33	—
	Chongqing Kelon	206,908.08	—

(4) *Transactions with specified third party companies*

Trade receivables	Hefei Weixi	18,229,589.24	18,229,589.24
	Wuhan Changrong	20,460,394.04	20,460,394.04
Prepayment	Hefei Weixi	465,213.00	465,213.00
Other receivables	Jiangxi Kesheng	27,462,676.72	27,462,676.72
	San’ai’fu	121,496,535.45	121,496,535.45
	Tianjin Xiangrun	96,905,328.00	96,905,328.00
	Tianjin Lixin	89,600,300.00	89,600,300.00
	Jiangxi Keda	13,000,200.00	13,000,200.00
	Zhuhai Longjia	28,600,000.00	28,600,000.00
	Zhuhai Defa	21,400,000.00	21,400,000.00
	Wuhan Changrong	20,000,000.00	20,000,000.00
	Beijing De Heng	4,000,000.00	4,000,000.00
	Finance Bureau of Yangzhou Economic Development Zone	40,000,000.00	40,000,000.00
	Shangqiu Bingxiong	58,030,000.00	58,030,000.00
	Zhongshan Dongyue	3,421,375.27	3,876,158.85
	Other payables	Zhuhai Longjia	28,316,425.03
Zhuhai Defa		21,400,000.00	21,400,000.00
Tianjin Taijin		65,000,000.00	65,000,000.00
Zhongshan Dongyue		100,000.00	500,000.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XI. CONTINGENT MATTER

As at the date of approval of the auditors' report, the pending litigations involving the Company are summarized as follows:

(1) The cases with the Company as the plaintiff

Plaintiff	Defendants	Reason	Total amounts involved
The Company	Greencool and Gu Chujun	Fraud in purchase; capital infringement	791,534,264.00*
The Company	Xian Kelon Refrigerating Co., Ltd.	Purchase amount not yet settled	99,984,100.00
The Company	Beijing Diamond Advertising Company Limited	Business fee is not yet settled	5,000,000.00
The Company	Beijing Deheng Solicitors	Legal service fee is not yet settled	4,000,000.00
The Company	Hangxiao Steel Structure Co., Ltd.	Fail to complete works before the expiry date, request settlement of a default fee	11,547,000.00
The Company	Zhongshan City Fusha Town Industrial Development Co., Ltd., Zhongshan City Fusha Town Shunchang Industrial Co., Ltd., Kelon Development Co., Ltd., Zhongshan City Fusha Town Local People's Government	Refund of land sale proceeds	9,398,240.00
The Company	Others		990,600.00
Total			922,454,204.00

* Regarding a case amounting to 336,754,600.00 where the law court ruled in favor of the Company, the other party was not satisfied and lodged an appeal. The above verdict has not been effective as on the date of audit.

(2) Cases Where the Company was Prosecuted

Plaintiff	Defendant	Reason	Amount involved (total)
Material supplier	The Company	Disputes in sale contracts	16,231,192.85
85 small shareholders	The Company	Claims of reimbursement due to false statement	10,813,806.27
Zhejiang Hang Xiao Steel Structure Co., Ltd.	The Company	Construction fees not yet settled	19,853,000.00
CNA/MC Co., Ltd.	The Company	Dispute over product quality	*USD 13,750,719.19
Company staff	The Company	Labor dispute	5,218,172.54
Henan Bingxiong Ice Cube Co., Ltd. and Henan Bingxiong Air-conditioner Co., Ltd.	Greencool and The Company	Failure to perform contract responsibilities on time	5,840,000.00
Administration Committee of Shangqiu Economic and Technology Development Zone	Greencool and The Company	Failure to perform contract responsibilities on time	Termination of investment agreement and return of land
Total			158,399,675.06

* On 31 December 2007, USD1 = RMB7.3046

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XII. GUARANTEES, PLEDGE AND IMPAWN

1. Guarantees

- (1) As at 31 December 2007, the guaranteed amount provided by the Company for its controlling subsidiaries and by its controlling subsidiaries for the Company was RMB723,872,900 and the actual guaranteed amount was RMB2,760,055,600, among which, the guaranteed amount provided by the Company for entities with a gearing ratio of over 70% was RMB340,495,500 and the actual guaranteed amount provided by the Company for entities with a gearing ratio of over 70% was RMB1,145,531,000.
- (2) As at 31 December 2007, balances of loan guarantees provided by Hisense Group Company Limited, being a related party, for the Company and its subsidiary amounted to RMB488,000,000, and the bank acceptance notes with a warranty balance of 653,500,000.
- (3) According to the resolution of the first meeting of the 6th Board of Director meetings held on 12 January 2007, the Company proposed to provide a loan warranty of RMB 267,000,000 to 19 distributors. This year the actual warranty incurred amounted to 15,000,000.

Apart from the above warranty matters, the Company has no other warranty matters.

2. Pledge

- (1) Fixed asset pledge see Appendix VI Note 11.
- (2) Intangible asset pledge see Appendix VI Note 14.

3. Impawn

Long term equity investment impawn see Appendix VI note 9.

XIII. COMMITMENT

Below is the capitalised pay out commitment with the contract signed and not recognised in the financial statement as at the balance sheet date.

Capitalised commitment	31 December 2007	31 December 2006
House, Building and Machine	90,831,251.43	14,004,000.00

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XIV. OTHER SIGNIFICANT EVENTS

1. Land use right of Shangqiu Kelon

Shangqiu Kelon's minority shareholder Shangqiu Bing Xiong Freezing Facilities Company Limited (hereinafter named "Shangqiu Bingxiong") entered into the Land Transfer Agreement with Shangqiu Kelon and the Administration Committee of Shangqiu Economic and Technology Development Zone in July 2004, which stipulated that Shangqiu Bingxiong shall transfer the land use right of the land totaling 187 mu located to the south of Nanjing Road in Shangqiu City, and that Shangqiu Kelon shall construct a project on the land while taking it over from Shangqiu Bingxiong to produce 2 million ice-making machines and sell them for RMB2.5 billion annually and to produce 1.6 million freezers and sell them for RMB1.2 billion. If the project is not completed, the Administration Committee of Shangqiu Economic and Technology Development Zone will reserve its right to recover the remaining land. Shangqiu Kelon has obtained the land use certificate, but as it has not completed "three connections and one leveling", Shangqiu Kelon has never used the land, and has not achieved the output as stipulated in the agreement.

In addition, Shangqiu Kelon received the notice from the local court in August 2005 that the Administration Committee of Shangqiu Economic and Technology Development Zone has lodged a claim to the court against Shangqiu Kelon, requesting to recover the 187 mu of land located in Shangqiu Economic and Technology Development Zone which was transferred from Shangqiu Bingxiong to Shangqiu Kelon. At the same time the Court seized the above mentioned land use right.

In November 2006 the Land and Resources Bureau of Shangqiu City, Henan Province, recovered for state ownership the land use right of Shangqiu Kelon to 125,267.840 sq. m. of land located at the southern side of Nanjing Road and western side of Yuwan Road, Shangqiu City, for the reason delayed development.

Shangqiu Kelon has made a provision for impairment of RMB35,396,116.58 with respect to the land use right. As at 31 December 2007 the case was still under examination.

Through Beijing Guo Tu Lian Real Estate Appraising Center Co., Ltd., it has been verified that as at 31 December 2007 two plots of industrial land of Shangqiu Kelon were seized by the local court in addition in that on the southern side of Nanjing Road seized in the above case; they were located on the western side of Kaixuan South Road (Shang Guo You (2004) No. 2365) and Sifang Yuan, Zhuiyang District (Shang Guo You (2004) No. 2364) in Shangqiu City, Henan Province.

2. Sale of land use right and factory building

On 13 May 2007, the Company and Xin Zhen Hua Real Estate Co., Ltd., Shunde District, Foshan City (hereinafter "Xin Zhen Hua Co.") signed the "Transfer Contract of Land Use right and Factory Building" and the "Supplementary Agreement to the Transfer Contract of Land Use right and Factory Building", with which the Company transferred other six land use rights related to a total area of 69723.6 sq. m. located at Ronggui Street Office, Shunde District, Foshan City and the factory building on the land to Xin Zhen Hua Real Estate, the total transfer amount being RMB91,200,000.00 plus truckage RMB50,000,000.00. As at 31 December 2007, the Company had received from Xin Zhen Hua Co., the total land transfer fee of RMB65.10 million, As of 31 December 2007, the ownership handover procedure for the land use right and the factory building was still in progress.

3. Assets reorganization

As CSRC approval was not adopted with regard to the Company's plan to issue shares to specific objects for purchasing assets and the related transactions, as at 28 March 2008, the Company's controlling shareholder, Qingdao Hisense Air-Conditioning Co., Ltd. had not yet fulfilled the commitment to the share reform, triggering the condition for additional donated shares as set forth in the Share Reform Plan. Hisense Air-conditioner will additionally donate 9,725,050 A shares to all holders of non-restricted circulating A shares and directors, supervisors and executives holding circulating A shares of the Company who are registered on the registration day of addition donated equity. This is equivalent to additionally donating 0.5 share for every 10 shares on the basis of the total number of 194,501,000 shares of the Company's circulating A shares before the implementation of the Share Reform Plan. Hisense Air-conditioner already completed the procedure for the above additional donation of shares on 11 April 2008.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XV. SUBSEQUENT IMPORTANT MATTERS

1. Hisense International Marketing Co., Ltd.

On 24 January 2008, the Company, Qingdao Hisense Import & Export Co., Ltd., Qingdao Hisense Electric Co., Ltd., and 18 natural persons including Liu Qinghua jointly invest to set up Qingdao Hisense International Marketing Co., Ltd. The registered capital is RMB20 million. The Company contributed RMB3.8 million, accounting for 19% of the total capital; Qingdao Hisense Import & Export Co., Ltd. contributed RMB10.4 million, accounting for 52% of the total capital; Qingdao Hisense Electric Co., Ltd. contributed RMB3.8 million, accounting for 19% of the total capital; 18 natural person shareholders contributed RMB2 million, accounting for 10% of the total capital.

2. Subsequent guarantee matters

The second session of the Company's sixth board meeting held in 2008 adopted: the proposal that the Company provides a loan guarantee limit of RMB1.451 billion for its controlling subsidiaries' comprehensive credit line in 2008; the proposal that the Company's subsidiaries provide a loan guarantee limit of RMB1.3452 billion to the Company in 2008; the proposal that the Company's subsidiaries provide to each other a loan guarantee limit of RMB778.2 million in 2008; the proposal that the Company provides its 23 distributors with a loan guarantee limit of RMB442 million in 2008.

3. Subsequent connected transactions

- (1) On 7 January 2008, the Company (hereinafter referred to as "Party A") and its associate Huayi Compressor, and its related companies Jiayi Beila and Huayi (Jingzhou) jointly signed the Compressors Purchase and Supply Framework Agreement, concluding that from the date of signing till 31 December 2008, Party A will purchase from Party B raw materials worth not more than RMB581.71 million at a price decided by both parties through negotiation.
- (2) On 7 January 2008, the Company (hereinafter referred to as "Party A") and the subsidiaries of Hisense Group (hereinafter referred to as "Party B") jointly signed the Business Cooperation Framework Agreement, concluding that from the date of signing till 31 December 2008, both parties will negotiate the pricing; and Party A, as the purchaser, will purchase goods or receive services from Party B worth not more than RMB918.1 million; Party A, as the supplier, will supply goods or provide services to Party B worth not more than RMB360.10 million.
- (3) The Company received Civil Judgment (Fo Zhong Fa Min Er Chu Zi No. 93 and 94 (2006)) from the Guangdong Province Foshan Intermediate Court (hereinafter "Foshan Intermediate Court") on 10 September 2007 and Civil Judgment (Fo Zhong Fa Min Er Chu Zi No. 153, 154, 175, 181, 182, 185 and 186 (2006)) from the Guangdong Province Foshan Intermediate Court on 31 March 2008, which stated that Foshan Intermediate Court has made first trial judgment on the nine cases in respect of the litigation initiated by your Company against the Greencool Companies and the case of specified third party companies in favour of your Company. The counterparty of the above nine litigations appealed from the judgment and the case is currently under hearing.

4. Sale of subsidiary Jilin Kelon

The Company and its wholly owned subsidiary Hisense Rongshen (Guangdong) Refrigerator Co., Ltd. on 7 January 2008 signed an "Equity Transfer Agreement" with Jilin Yinqiao Group Co., Ltd (hereinafter "Yinqiao Group") transferring its 100% stake in Jilin Kelon Electric Co., Ltd 100% (including 90% Hisense Electrical and 10% Rongshen Refrigerators) to Yinqiao Group for RMB30 million. At the same time, the Company and Hisense Rongshen (Guangdong) Refrigerator Co., Ltd. agreed to take up all the carrying debts of Jilin Kelon at the time of execution of the agreement. As at 31 December 2007, Jilin Kelon's net asset value amounted to RMB10,789,248.49.

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XVI. EXTRAORDINARY LOSS AND PROFIT

Nature or content	Amount before income tax		Amount after income tax		Remarks
	Current period	Preceding period	Current period	Preceding period	
1. Loss and profit from disposal of non-current assets					
(1) Income from disposal of long-term assets					
Including: Income from disposal of fixed asset	83,795,226.18	29,001,815.79	83,563,394.60	29,001,815.79	See appendix 5(2) for tax rates
Proceeds from transfer of intangible assets	276,854,157.61	36,360,404.27	276,854,157.61	36,360,404.27	
Proceeds from transfer of equity	4,509,461.06	—	4,509,461.06	—	
Sub-total	365,158,844.85	65,362,220.06	364,927,013.27	65,362,220.06	
(2) Expense for disposal of long-term assets					
Including: Net loss in disposal of fixed assets	71,192,138.03	19,390,062.70	70,893,309.31	19,390,062.70	
Net loss in disposal of intangible assets	19,422.98	—	19,422.98	—	
Sub-total	71,211,561.01	19,390,062.70	70,912,732.29	19,390,062.70	
Net profit or loss from disposal of non-current assets	293,947,283.84	45,972,157.36	294,014,280.98	45,972,157.36	
2. Government subsidy recorded in the profits and losses of the current period (except government subsidy closely related to the Company's business, and of which the amount is determined according to the State's unified standard)	—	70,000,000.00	—	70,000,000.00	
3. Provision for impairment on various assets made because of force majeure such as natural disaster	45,123,028.23	—	45,123,028.23	—	
4. Gain or loss on debt restructuring	10,883,646.16	—	10,883,646.16	—	
5. Gain or loss from estimated debts not related to the Company's main operation	7,304,600.00	—	5,989,772.00	—	
6. Net non-operating income other than above					
(1) Non-operating income:	85,910,625.70	24,377,933.03	84,438,649.07	24,377,933.03	*1
(2) Less: Non-operating expenses:	10,782,956.36	25,562,593.16	10,782,056.36	25,553,072.64	
Net non-operating income	327,530,971.11	114,787,497.23	327,441,719.62	114,787,497.23	
Total extraordinary loss and profit before deducting minority interests	327,530,971.11	114,787,497.23	327,441,719.62	114,787,497.23	
Less: Effect of minority interests	(11,092,916.83)	—	(11,174,811.56)	—	
Total extraordinary loss and profit after deducting minority interests	338,623,887.94	114,787,497.23	338,616,531.18	114,787,497.23	

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XVII. RETURN ON NET ASSETS

	Return on net assets			
	Fully diluted		Weighted average	
	Current period	Preceding period	Current period	Preceding period
Profit for the period				
Net profit attributable to equity holders of the Company	N/A	N/A	N/A	N/A
Net profit attributable to equity holders of the Company less of extraordinary items	N/A	N/A	N/A	N/A

XVIII. EARNINGS PER SHARE

	Earnings per share			
	Basic earnings per share		Diluted earnings per share	
	Current period	Preceding period	Current period	Preceding period
Profit for the period				
Net profit attributable to equity holders of the Company	0.2524	0.0425	0.2524	0.0425
Net profit attributable to equity holders of the Company less of extraordinary items	(0.0889)	(0.0733)	(0.0889)	(0.0733)

Items	2007	2006
Calculation of basic earnings per share and diluted earnings per share		
(I) Numerator:		
Net profit after tax	250,395,446.91	42,113,364.14
Adjustments: Preference stock dividend and other instrumental effects	—	—
Profit and loss attributable to equity holders of the Company in the calculation of earnings per share	250,395,446.91	42,113,364.14
Adjustments: Dividend and interest related to dilutive potential ordinary shares	—	—
Change in proceeds or expense arising from conversion of dilutive potential ordinary shares	—	—
Profit and loss attributable to equity holders of the Company in the accounting of diluted earnings per share	250,395,446.91	42,113,364.14
(II) Denominator:		
Weighted average of outside ordinary shares of the current period in the accounting of basic earnings per share	992,006,563.00	992,006,563.00
Add: Weighted average when all dilutive potential ordinary shares are converted to ordinary shares	—	—
Weighted average of outside ordinary shares of the current period in the accounting of diluted earnings per share	992,006,563.00	992,006,563.00
(III) Earnings per share		
Basic earnings per share	—	—
Net profit attributable to equity holders of the Company	0.2524	0.0425
Net profit attributable to equity holders of the Company less of extraordinary items	(0.0889)	(0.0733)
Diluted earnings per share	—	—
Net profit attributable to equity holders of the Company	0.2524	0.0425
Net profit attributable to equity holders of the Company less of extraordinary items	(0.0889)	(0.0733)

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XIX. ADJUSTMENT PROCESS AND RECTIFICATION WORK ON YEAR-BEGIN HOLDERS' INTEREST ACCORDING TO NEW ACCOUNTING STANDARD

Items	Capital	Capital reserve	Surplus reserve	Unappropriated profit	Foreign currency translation adjustment	minority shareholders' equity	Total
A. Balance at the end of previous year	992,006,563.00	1,608,102,127.20	114,580,901.49	(3,776,596,690.68)	14,978,392.50	239,961,125.91	(806,967,580.58)
Add: Rectification of previous accounting errors	—	—	—	—	—	—	—
Chang of previous accounting estimates	—	—	—	—	—	—	—
B. Balance adjustment process before adjustment at the beginning of this year:	992,006,563.00	1,608,102,127.20	114,580,901.49	(3,776,596,690.68)	14,978,392.50	239,961,125.91	(806,967,580.58)
1. Write-off of differences in long-term equity investments under the same control	—	—	—	57,252,726.20	—	—	57,252,726.20
2. Write-off of difference in long-term equity investment credit accounted for by equity method	—	—	—	—	—	—	—
3. Adjustment of difference between book value and fair value real estate for investment	—	—	—	—	—	—	—
4. Fixed asset cost disposal expenses, additional depreciation not included before adjustment	—	—	—	—	—	—	—
5. Adjustment of compensation for staff remuneration payables due to discharge of labour relationship	—	—	—	—	—	—	—
6. Adjustment of fair value of liabilities on vesting date recognised by payment of shares on or after the first execution day	—	—	—	—	—	—	—
7. Adjustment of restructuring obligation for satisfying recognition condition for estimated liabilities	—	—	—	—	—	—	—
8. Temporary differences in income tax arising from adjusted book values of assets and liabilities and differences in taxation basis	—	—	—	21,386,732.06	—	—	21,386,732.06
9. Write-off of balance after accumulated amortisation of goodwill originally recognised for merger of enterprises under the same control	—	—	—	—	—	—	—
10. Goodwill impairment test for merger not under the same control	—	—	—	—	—	—	—
11. Adjustment of difference between book value and fair value of available-for-sale financial assets	—	—	—	—	—	—	—
12. Adjustment of difference between book value and fair value of financial liabilities	—	—	—	—	—	—	—
13. Others	—	—	—	—	—	—	—
C. Balance at the beginning of the year after adjustment	992,006,563.00	1,608,102,127.20	114,580,901.49	(3,697,957,232.42)	14,978,392.50	239,961,125.91	(728,328,122.32)

Notes to the Financial Statements

1 January 2007 to 31 December 2007 (Unless otherwise specified, expressed in RMB)

XX. DIFFERENCES RECONCILIATION TABLE FOR FINANCIAL REPORT PREPARED ACCORDING TO DOMESTIC AND OVERSEAS ACCOUNTING STANDARDS

As the Company issued B shares (or H shares, N shares or financial listed company or IPO or issue of new shares) , when preparing the financial report according to the Accounting Standards for Business Enterprises, it also followed the International Financial Reporting Standards. The overseas accounting firm hired by the Company is BDO McCabe Lo Limited. Differences in net assets and net profits in the financial report were prepared according to domestic and overseas accounting standards.

Unit: RMB'000

Item	Net asset	Net profit
Based on International Financial Reporting Standards	(784,772)	238,712
1. Agency fee for corporate restructuring.	11,684	11,684
2. Adjustments on amortization loss on share reform of an associate.	16,317	—
3. Adjustment on amortization of intangible assets.	(16,713)	—
Based on Accounting Standards for Business Enterprises*	(773,484)	250,396

* Net assets and net profits based on Accounting Standards for Business Enterprises do not include minority interests or minority profit and loss.

XXI. APPROVAL OF THE FINANCIAL STATEMENT

The parent company of the Company is Qingdao Hisense Air-Conditioning Company Limited; the ultimate parent company of the group is Hisense Group Company Limited.

The Company's financial statements are approved by the Board (or senior management department) of the Company on 24 April 2008.