*The following is the text of a report, prepared for the purpose of incorporation in this prospectus, received from the Company's reporting accountants, KPMG, Certified Public Accountants, Hong Kong.*

8th Floor

Prince's Building
10 Chater Road
Central
Hong Kong

26 November 2010

The Directors
China Auto System Technologies Limited

DBS Asia Capital Limited
CIMB Securities (HK) Limited

Dear Sirs,

## INTRODUCTION

We set out below our report on the financial information relating to Nanjing Aotecar Refrigerating Co., Ltd. (the "**Company**") including the statement of comprehensive income, the statement of changes in equity and the cash flow statement of the Company for the year ended 31 December 2007 and the balance sheet of the Company as at 31 December 2007, together with the notes thereto (the "**Financial Information**"), for inclusion in the prospectus of China Auto System Technologies Limited dated 26 November 2010 (the "**Prospectus**").

The Company was incorporated in the People's Republic of China (the "**PRC**") on 16 May 2000 as a sino-foreign equity joint venture. The principal activities of the Company are manufacturing and sale of automotive compressors. The Company has adopted 31 December as its financial year end date. The statutory financial statements of the Company for the year ended 31 December 2007 were prepared in accordance with the relevant accounting rules and regulations applicable to entities in the PRC.

The directors of the Company have prepared the financial statements of the Company for the year ended 31 December 2007 in accordance with the accounting policies set out in Section B below (the "**Underlying Financial Statements**"). The Underlying Financial Statements for the year ended 31 December 2007 were audited by us in accordance with Hong Kong Standards on Auditing issued by Hong Kong Institute of Certified Public Accountants (the "**HKICPA**").

The Financial Information has been prepared by the directors of the Company based on the Underlying Financial Statements, with no adjustments made thereon and in accordance with the applicable disclosure provisions of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "**Listing Rules**").

## RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND REPORTING ACCOUNTANTS

The directors of the Company are responsible for the preparation and true and fair presentation of the Financial Information in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board, the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Listing Rules. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the Financial Information that is 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.

Our responsibility is to form an opinion on the Financial Information based on our procedures.

## BASIS OF OPINION

As a basis for forming an opinion on the Financial Information, for the purpose of this report, we have examined the Underlying Financial Statements and have carried out such appropriate procedures as we considered necessary in accordance with Auditing Guideline "Prospectuses and the Reporting Accountant" (Statement 3.340) issued by the HKICPA.

## OPINION

In our opinion, for the purpose of this report, the Financial Information, in accordance with the accounting policies set out in Section B below, gives a true and fair view of the Company's results and cash flows for the year ended 31 December 2007, and the state of affairs of the Company as at 31 December 2007.

## A. FINANCIAL INFORMATION

### 1. Statement of comprehensive income

| | Section B Note | Year ended 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| **Turnover** | 3 | 308,815 |
| Cost of sales | 13(b) | (226,655) |
| **Gross profit** | | 82,160 |
| Other revenue and net income | 4 | 2,059 |
| Distribution expenses | | (21,377) |
| Administrative expenses | | (14,999) |
| Other operating expenses | | (2,491) |
| **Profit from operations** | | 45,352 |
| Finance costs | 5(a) | (4,088) |
| **Profit before taxation** | | 41,264 |
| Income tax | 6(a) | 479 |
| **Profit and total comprehensive income for the year** | | 41,743 |

## 2. Balance sheet

| | Section B Note | At 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| **Non-current assets** | | |
| Property, plant and equipment | 10 | 105,301 |
| Lease prepayments | 11 | 6,232 |
| Intangible assets | 12 | 4,092 |
| Deferred tax assets | 19 | 2,125 |
| | | 117,750 |
| **Current assets** | | |
| Inventories | 13(a) | 68,532 |
| Trade and other receivables | 14 | 146,077 |
| Income tax refundable | | 3,247 |
| Pledged deposits | 15 | 20,691 |
| Cash | 16 | 7,116 |
| | | 245,663 |
| **Current liabilities** | | |
| Trade and other payables | 17 | 102,399 |
| Interest-bearing borrowings | 18 | 55,855 |
| Provision | 20 | 7,985 |
| | | 166,239 |
| **Net current assets** | | 79,424 |
| **Net assets** | | 197,174 |
| **Capital and reserves** | | |
| Paid-in capital | 21(a) | 119,895 |
| Reserves | 21(b) | 77,279 |
| **Total equity** | | 197,174 |

### 3. Statement of changes in equity

*(Expressed in RMB'000)*

| | Attributable to equity holders of the Company | | | | |
|---|---|---|---|---|---|
| | Paid-in capital (Note 21(a)) | General reserve (Note 21(b)) | Enterprise expansion fund (Note 21(b)) | Retained earnings | Total equity |
| **At 1 January 2007** | 119,895 | 1,861 | 930 | 32,745 | 155,431 |
| **Changes in equity for 2007** | | | | | |
| Total comprehensive income for the year | — | — | — | 41,743 | 41,743 |
| Appropriation to reserves | — | 7,898 | 2,369 | (10,267) | — |
| **At 31 December 2007** | 119,895 | 9,759 | 3,299 | 64,221 | 197,174 |

## 4. Cash flow statement

| | Section B Note | Year ended 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| **Operating activities** | | |
| Profit before taxation | | 41,264 |
| Adjustments for: | | |
| Impairment losses on trade receivables | 14(b) | 481 |
| Depreciation of property, plant and equipment | 10 | 10,268 |
| Amortisation of lease prepayments | 11 | 147 |
| Amortisation of intangible assets | 12 | 2,338 |
| Interest income | 4 | (493) |
| Loss on sale of property, plant and equipment | 4 | 199 |
| Finance costs | 5(a) | 4,088 |
| Foreign exchange gains | | (2,959) |
| **Profit before changes in working capital** | | 55,333 |
| Increase in inventories | | (25,750) |
| Increase in trade and other receivables | | (27,744) |
| Increase in pledged deposits | | (1,479) |
| Increase in trade and other payables | | 36,287 |
| Proceeds from discounted bank acceptance bills | | 6,865 |
| Increase in provisions | | 259 |
| **Cash generated from operating activities** | | 43,771 |
| Finance costs paid | | (4,088) |
| Income tax paid | | (4,540) |
| **Net cash generated from operating activities** | | 35,143 |
| **Investing activities** | | |
| Proceeds from sale of property, plant and equipment | | 198 |
| Acquisition of property, plant and equipment | | (14,221) |
| Interest received | | 493 |
| **Net cash used in investing activities** | | (13,530) |
| **Financing activities** | | |
| Proceeds from bank loans | | 59,500 |
| Repayments of bank loans | | (79,500) |
| **Net cash used in financing activities** | | (20,000) |
| Net increase in cash | | 1,613 |
| Cash at 1 January | | 5,503 |
| **Cash at 31 December** | 16 | 7,116 |

## B NOTES TO THE FINANCIAL INFORMATION

### 1. Significant accounting policies

#### (a) Statement of compliance

The Financial Information set out in this report has been prepared in accordance with International Financial Reporting Standards ("**IFRSs**"), which collective term includes International Accounting Standards ("**IAS**") and related interpretations, promulgated by the International Accounting Standards Board ("**IASB**"). Further details of the significant accounting policies adopted are set out in the remainder of this Section B.

The IASB has issued a number of new and revised IFRSs. For the purpose of preparing this Financial Information, the Company has adopted all these new and revised IFRSs to the year ended 31 December 2007, except for any new standards or interpretations that are not yet effective for the accounting periods prior to 1 January 2010. The revised and new accounting standards and interpretations issued but not yet effective for the accounting periods prior to 1 January 2010 are set out in note 26.

The Financial Information also complies 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 (the "**Stock Exchange**").

#### (b) Basis of measurement

The Financial Information is presented in Renminbi ("**RMB**"), rounded to the nearest thousand. It is prepared on the historical cost basis.

#### (c) Use of estimates and judgments

The preparation of Financial Information in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other 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 Information and major sources of estimation uncertainty are discussed in note 25.

**(d) Foreign currency**

(i) Functional and presentation currency

Items included in the Financial Information are measured at RMB, the currency that best reflects the economic substance of the underlying events and circumstances relevant to the entity (the "**functional currency**"), which is also the presentation currency.

(ii) Foreign currency transactions

Foreign currency transactions during the year are translated at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in profit or loss, except those arising from foreign currency borrowings used to hedge a net investment in a foreign operation which are recognised in other comprehensive income.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was determined.

**(e) Property, plant and equipment**

Items of property, plant and equipment are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 1(h)(ii)):

The cost of self-constructed items of property, plant and equipment includes the cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads and borrowing costs (see note 1(r)).

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognised in profit or loss on the date of retirement or disposal.

Depreciation is calculated to write off the cost or valuation of items of property, plant and equipment, less their estimated residual value, if any, using the straight line method over their estimated useful lives as follows:

| | |
|---|---|
| – Plant and buildings | 20 years |
| – Machinery and equipment | 10 -15 years |
| – Furniture, fixtures and other office equipment | 5 - 10 years |
| – Motor vehicles | 8 years |

Where parts of an item of property, plant and equipment have different useful lives, the cost or valuation of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reviewed annually.

Construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

**(f) Intangible assets (other than goodwill)**

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the Company has sufficient resources and the intention to complete development.

Other intangible assets that are acquired by the Company are stated in the balance sheet at cost less accumulated amortisation (where the estimated useful life is finite) and impairment losses (see note 1(h)(ii)).

Amortisation of intangible assets with finite useful lives is charged to profit or loss on a straight-line basis over the assets' estimated useful lives. The following intangible asset with finite useful life is amortised from the date it is available for use and its estimated useful life is as follows:

| | |
|---|---|
| Patents | 7 years |

Both the period and method of amortisation are reviewed annually.

**(g) Lease prepayments**

Lease prepayments represent cost of land use right paid to the PRC governmental authorities.

Lease prepayments are stated at cost less accumulated amortisation and impairment losses (see note 1(h)(ii)). Amortisation is charged to profit or loss on a straight-line basis over the periods of the rights which are 50 years.

**(h) Impairment of assets**

(i) Impairment of trade and other receivables

Trade and other receivables that are stated at amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. Objective evidence of impairment includes observable data that comes to the attention of the Company about one or more of 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;

– it becoming probable that the debtor will enter bankruptcy or other financial reorganisation; and

– significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor.

If any such evidence exists, any impairment loss is determined and recognised as follows:

For trade and other receivables carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material. This assessment is made collectively where financial assets carried at amortised cost share similar risk characteristics, such as similar past due status, and have not been individually assessed as impaired. Future cash flows for financial assets which are assessed for impairment collectively are based on historical loss experience for assets with credit risk characteristics similar to the collective group.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through profit or loss. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

Impairment losses are written off against the corresponding assets directly, except for impairment losses recognised in respect of trade receivables and bills receivable included within trade and other receivables, whose recovery is considered doubtful but not remote. In this case, the impairment losses for doubtful debts are recorded using an allowance account. When the Company is satisfied that recovery is remote, the amount considered irrecoverable is written off against trade receivables and bills receivable directly and any amounts held in the allowance account relating to that debt are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other changes in the allowance account and subsequent recoveries of amounts previously written off directly are recognised in profit or loss.

(ii) Impairment of other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognised no longer exists or may have decreased:

– property, plant and equipment;

– lease prepayments; and

– intangible assets.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for intangible assets that are not yet available for use and intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

– Calculation of recoverable amount

The recoverable amount of an asset is the greater of its fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

– Recognition of impairment losses

An impairment loss is recognised in profit or loss if the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

– Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the period in which the reversals are recognised.

**(i) Inventories**

Inventories are carried at the lower of cost and net realisable value. Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is 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.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

**(j) Trade and other receivables**

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less allowance for impairment of doubtful debts (see note 1(h)(i)), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less allowance for impairment of doubtful debts.

**(k) Interest-bearing borrowings**

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between the amount initially recognised and redemption value being recognised in profit or loss over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

**(l) Trade and other payables**

Trade and other payables are initially recognised at fair value. Trade and other payables are subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

**(m) Cash**

Cash comprise cash at bank and on hand, and demand deposits with banks and other financial institutions.

**(n) Employee benefits**

(i) Short-term employee benefits

Salaries and annual bonuses are accrued in the period in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Defined contribution retirement plan

Contributions to PRC local retirement schemes pursuant to the relevant labour rules and regulations in the PRC are recognised as an expense in profit or loss as incurred, except to the extent that they are included in the cost of inventories not yet recognised as an expense.

**(o) Income tax**

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to business combinations, or items recognised in other comprehensive income or directly in equity, in which case the relevant amounts of tax are recognised in other comprehensive income or directly in equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rate enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each reporting date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the Company has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

– in the case of current tax assets and liabilities, the Company intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or

– in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  – the same taxable entity; or

  – different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

**(p) Provisions and contingent liabilities**

Provisions are recognised for other liabilities of uncertain timing or amount when the Company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

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, whose existence 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.

**(q) Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable. Provided it is probable that the economic benefits will flow to the Company and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in profit or loss as follows:

(i) Sale of goods

Revenue is recognised when the significant risks and rewards of the ownership of goods have been transferred to the buyers and the Company retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold. Revenue excludes value added tax or other sales taxes and is after deduction of any trade discounts.

(ii) Interest income

Interest income is recognised as it accrues using the effective interest method.

(iii) Government grants

Government grants are recognised in the balance sheet initially when there is reasonable assurance that they will be received and that the Company will comply with the conditions attaching to them. Grants that compensate the Company for expenses incurred are recognised as revenue in profit or loss on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the Company for the cost of an asset are deducted from the carrying amount of the asset and consequently are effectively recognised in profit or loss over the useful life of the asset by way of reduced depreciation expense.

**(r) Borrowing costs**

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset. Other borrowing costs are expensed in the period in which they are incurred.

The capitalisation of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalisation of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

**(s) Related parties**

For the purposes of the Financial Information, a party is considered to be related to the Company if:

(i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Company or exercise significant influence over the Company in making financial and operating policy decisions, or has joint control over the Company;

(ii) the Company and the party are subject to common control;

(iii) the party is an associate of the Company or a joint venture in which the Company is a venturer;

(iv) the party is a member of key management personnel of the Company or the Company's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;

(v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or

(vi) the party is a post-employment benefit plan which is for the benefit of employees of the Company or of any entity that is a related party of the Company.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

**(t) Segment reporting**

Operating segments, and the amounts of each segment item reported in the Financial Information, are identified from the financial information provided regularly to the Company's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Company's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of products and services, the nature of production processes, the type or class of customers, the methods used to distribute the products or provide the services, and the nature of the regulatory environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

**2. Segment reporting**

IFRS 8, Operating Segments, requires identification and disclosure of operating segment information based on internal financial reports that are regularly reviewed by the Company's chief operating decision maker for the purpose of resources allocation and performance assessment. On this basis, the Company has determined that it only has one operating segment which is the manufacturing and sale of automotive compressors.

**3. Turnover**

The principal activities of the Company are manufacturing and sale of automotive compressors.

Turnover represents the sales value of goods supplied to customers.

## 4. Other revenue and net income

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| **Other revenue** | |
| Government grants | 475 |
| Interest income | 493 |
| | 968 |
| **Other net income** | |
| Loss on sale of property, plant and equipment | (199) |
| Net foreign exchange gains | 1,290 |
| | 1,091 |
| | 2,059 |

## 5. Profit before taxation

### (a) Finance costs

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| Interest on bank loans | 3,431 |
| Interest on discounted bills | 657 |
| | 4,088 |

### (b) Staff costs

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| Salaries, wages, and other benefits | 17,146 |
| Contributions to defined contribution retirement plan | 960 |
| | 18,106 |

Pursuant to the relevant labour rules and regulations in the PRC, the Company participates in a defined contribution retirement benefit scheme organised by the PRC government authorities whereby the Company is required to make contributions to the scheme at the rate of 21% of the eligible employees' salary.

The government is responsible for the entire pension obligation payable to the retired employees. The Company has no other material obligation for the payment of pension benefits associated with the scheme referred to above beyond the annual contributions described above.

**(c) Other items**

| | Section B Note | Year ended 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| Amortisation | | |
| – lease prepayments | 11 | 147 |
| – intangible assets | 12 | 2,338 |
| Depreciation | 10 | 10,268 |
| Impairment losses on trade receivables | 14(b) | 481 |
| Auditors' remuneration | | 318 |
| Research and development costs | | 1,326 |
| Increase in provisions | 20 | 10,923 |
| Cost of inventories | 13(b), (i) | 226,655 |

Note

(i) Cost of inventories includes RMB 16,793,000 relating to staff costs, depreciation and amortisation, amounts of which are also included in the respective total amounts disclosed separately above for each of these types of expenses.

## 6. Income tax

(a) Income tax in the statement of comprehensive income represents:

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| **Current tax – PRC income tax** | |
| Adjustment for prior year | (275) |
| **Deferred tax** | |
| Origination and reversal of temporary differences | (204) |
| | (479) |

(b) Reconciliation between income tax and profit before taxation at applicable tax rate:

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| Profit before taxation | 41,264 |
| Notional tax on profit before taxation, calculated at the rate applicable to the Company (i) | 4,952 |
| Tax credit for domestic equipment purchases (ii) | (5,288) |
| Adjustments for prior year's income tax | (275) |
| Tax effect of non-deductible expenses | 217 |
| Effect of changes in tax rate (iii) | (85) |
| Actual tax | (479) |

Note

(i) The Company, being a foreign invested enterprise engaged in manufacturing activities in a coastal economic development zone, is granted a preferential income tax rate of 24% and is also entitled to a tax holiday of two-year full exemption from income tax followed by three-year 50% reduction of the applicable income tax rate commencing from the first profit-making year from PRC income tax perspective ("**2+3 tax holiday**"). The Company started its tax holiday in 2004 and accordingly, it is subject to income tax at 12% for 2007.

(ii) Pursuant to the tax regulations of the PRC, the Company is entitled to a tax credit of 40% of the capital expenditure on purchase of domestic equipment.

(iii) On 16 March 2007, the Fifth Plenary Session of the Tenth National People's Congress promulgated the Corporate Income Tax Law of the PRC which changed the statutory income tax rate to 25% with effect from 1 January 2008.

**7. Directors' remuneration**

No remuneration has been paid or is payable in respect of the year ended 31 December 2007 by the Company to the Company's directors.

**8. Individuals with highest emoluments**

The aggregate of the emoluments in respect of the five individuals with the highest emoluments are as follows:

| | **Year ended 31 December 2007** |
|---|---|
| | *RMB'000* |
| Salaries and other emoluments | 774 |
| Discretionary bonus | 575 |
| Retirement scheme contribution | 140 |

The emoluments of the above five individuals are within the following band:

| | **Year ended 31 December 2007** |
|---|---|
| | *Number of individuals* |
| Nil to HKD 1,000,000 | 5 |

**9. Earnings per share**

Information of earnings per share is not presented as such information is not meaningful given the purpose of this report.

## 10. Property, plant and equipment

| | Plant and buildings | Machinery and equipment | Furniture, fixtures and office equipment | Motor vehicles | Construction in progress ("CIP") | Total |
|---|---|---|---|---|---|---|
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| ***Cost:*** | | | | | | |
| ***At 1 January 2007*** | 9,326 | 112,804 | 1,370 | 1,941 | 4,128 | 129,569 |
| Additions | 168 | 8,643 | 372 | 966 | 4,798 | 14,947 |
| Transfer from CIP | 3,305 | — | — | — | (3,305) | — |
| Disposals | — | — | — | (560) | — | (560) |
| ***At 31 December 2007*** | 12,799 | 121,447 | 1,742 | 2,347 | 5,621 | 143,956 |
| ***Accumulated depreciation:*** | | | | | | |
| ***At 1 January 2007*** | (1,243) | (25,855) | (754) | (698) | — | (28,550) |
| Charge for the year | (503) | (9,377) | (146) | (242) | — | (10,268) |
| Written back on disposal | — | — | — | 163 | — | 163 |
| ***At 31 December 2007*** | (1,746) | (35,232) | (900) | (777) | — | (38,655) |
| ***Carrying amounts:*** | | | | | | |
| ***At 31 December 2007*** | 11,053 | 86,215 | 842 | 1,570 | 5,621 | 105,301 |
| ***At 1 January 2007*** | 8,083 | 86,949 | 616 | 1,243 | 4,128 | 101,019 |

Carrying amount of buildings pledged as collateral for the Company's bank loans as at 31 December 2007 was RMB 6,455,000 (see note 18).

## 11. Lease prepayments

| | *RMB'000* |
|---|---|
| ***Cost:*** | |
| At 1 January and 31 December 2007 | 6,907 |
| ***Accumulated amortisation:*** | |
| At 1 January 2007 | (528) |
| Charge for the year | (147) |
| At 31 December 2007 | (675) |
| ***Carrying amounts:*** | |
| At 31 December 2007 | 6,232 |
| At 1 January 2007 | 6,379 |

Lease prepayments represented cost of land use rights in respect of land located in the PRC, on which the Company's plant and buildings were built. The Company was granted land use rights for a period of 50 years. None of the leases included contingent rentals.

Carrying amount of lease prepayments pledged as collateral for the Company's bank loans as at 31 December 2007 was RMB 6,232,000 (see note 18).

## 12. Intangible assets

| | Patents |
|---|---|
| | *RMB'000* |
| ***Cost:*** | |
| At 1 January 2007 and 31 December 2007 | 16,563 |
| ***Accumulated amortisation:*** | |
| At 1 January 2007 | (10,133) |
| Charge for the year | (2,338) |
| At 31 December 2007 | (12,471) |
| ***Carrying amounts:*** | |
| At 31 December 2007 | 4,092 |
| At 1 January 2007 | 6,430 |

The amortisation charge for the year ended 31 December 2007 is included in "Other operating expenses" in the statement of comprehensive income.

## 13. Inventories

### (a) Inventories in the balance sheet comprise:

| | At 31 December 2007 |
|---|---|
| | *RMB'000* |
| Raw materials | 27,637 |
| Work in progress | 7,059 |
| Finished goods | 33,836 |
| | 68,532 |

### (b) The analysis of the amount of inventories recognised as an expense and included in profit or loss is as follows:

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| Carrying amount of inventories sold | 224,213 |
| Write-off of inventories | 2,442 |
| | 226,655 |

### 14. Trade and other receivables

| | Section B Note | At 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| Trade receivables | | 116,912 |
| Less: Allowance for doubtful debts | 14(b) | (2,187) |
| | | 114,725 |
| Bills receivable | | 27,828 |
| Other receivables | | 3,524 |
| | | 146,077 |

### (a) Ageing analysis

Included in trade and other receivables are trade receivables and bills receivable (net of allowance for doubtful debts) with the following ageing analysis as at 31 December 2007.

| | At 31 December 2007 |
|---|---|
| | *RMB'000* |
| Less than 3 months | 125,833 |
| 3 to 6 months | 13,068 |
| 6 to 12 months | 2,462 |
| More than 12 months | 1,190 |
| Total | 142,553 |

Trade receivables and bills receivable are due within 90 days to 120 days from the date of billing. Further details on the Company's credit policy are set out in note 22(a).

### (b) Impairment of trade receivables and bills receivable

Impairment losses in respect of trade receivables and bills receivable are recorded using an allowance account unless the Company is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables and bills receivable directly (see note1(h)(i)).

The movement in the allowance for doubtful debts during the year ended 31 December 2007, including both specific and collective loss components, is as follows:

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| At 1 January | (1,798) |
| Impairment loss recognised | (481) |
| Uncollectible amounts written off | 92 |
| At 31 December | (2,187) |

At 31 December 2007, the Company's trade receivables of RMB 2,688,000 were individually determined to be impaired. The individually impaired receivables related to customers that were in financial difficulties and management assessed that only a portion of the receivables is expected to be recovered. Consequently, specific allowances for doubtful debts of RMB 2,187,000 were recognised. The Company does not hold any collateral over these balances.

**(c) Trade receivables and bills receivable that are not impaired**

The ageing analysis of trade receivables and bills receivable that are neither individually nor collectively considered to be impaired are as follows:

| | **At 31 December 2007** |
|---|---|
| | *RMB'000* |
| Neither past due nor impaired | 125,833 |
| Less than 1 month past due | 7,214 |
| 1 to 3 months past due | 5,854 |
| 3 to 12 months past due | 2,877 |
| Over 12 months past due | 274 |
| | 16,219 |
| Total | 142,052 |

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

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

**15. Pledged deposits**

Pledged deposits can be analysed as follows:

| | **At 31 December 2007** |
|---|---|
| | *RMB'000* |
| Guarantee deposits for issuance of commercial bills and letters of credit | 20,691 |

**16. Cash**

| | **At 31 December 2007** |
|---|---|
| | *RMB'000* |
| Cash at bank and on hand | 7,116 |

## 17. Trade and other payables

| | At 31 December 2007 |
|---|---|
| | *RMB'000* |
| Trade payables | 67,585 |
| Bills payable | 15,750 |
| Other payables | 6,821 |
| Dividends payable | 7,629 |
| Other tax payable | 4,614 |
| | 102,399 |

An ageing analysis of trade payables and bills payable of the Company based on invoice date is as follows:

| | At 31 December 2007 |
|---|---|
| | *RMB'000* |
| Within 1 month | 34,773 |
| Over 1 month but less than 3 months | 24,536 |
| Over 3 months but less than 6 months | 20,121 |
| Over 6 months but less than 1 year | 1,667 |
| Over 1 year | 2,238 |
| | 83,335 |

## 18. Interest-bearing borrowings

| | | At 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| Bank loans | | |
| – Secured | (i) | 30,000 |
| – Unsecured | | 18,991 |
| Bank advances under discounted bills | (ii) | 6,864 |
| | | 55,855 |

All bank loans during the year ended 31 December 2007 were interest-bearing, with interest rates ranging from 6.57% to 9.65%.

(i) At 31 December 2007, the bank loans of the Company were secured by mortgages over buildings and land use rights with aggregate carrying amounts of RMB 6,455,000 and RMB 6,232,000 respectively (see notes 10 and 11).

(ii) The Company's discounted bank acceptance bills have been accounted for as collateralised bank advances, and the corresponding discounted bills are included in "bills receivable" (see note 14).

**19. Deferred tax assets**

The components of deferred tax assets recognised in the balance sheet and movement during the year ended 31 December 2007 are as follows:

| | Allowance for bad debt | Other payables | Intangible assets | Provision | Pre-operating expenses | Total |
|---|---|---|---|---|---|---|
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| Deferred tax arising from: | | | | | | |
| At 1 January 2007 . . . | 174 | 361 | 355 | 927 | 104 | 1,921 |
| Charged/(credited) to profit or loss . . . . . . | 99 | 38 | 100 | 71 | (104) | 204 |
| At 31 December 2007 . . . . . . . . . . . . . | 273 | 399 | 455 | 998 | — | 2,125 |

**20. Provision**

Provision for product warranties

| | *RMB'000* |
|---|---|
| At 1 January 2007 . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 7,726 |
| Additional provisions made . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 10,923 |
| Provisions utilised . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | (10,664) |
| At 31 December 2007 . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 7,985 |

Under the terms of the Company's sales agreements, the Company will rectify any product defects arising within two years of the date of sale. Provision is therefore made for the best estimate of the expected settlement under these agreements in respect of sales made within the two years prior to 31 December 2007. The amount of provision takes into account the Company's recent claim experience and is only made where a warranty claim is probable.

**21. Capital and reserves**

**(a) Paid-in capital**

| | **At 31 December 2007** |
|---|---|
| | *USD'000* |
| Registered capital . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 14,460 |

| | **At 31 December 2007** |
|---|---|
| | *RMB equivalent'000* |
| Paid-in capital . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 119,895 |

**(b) PRC statutory reserves**

Transfers from retained earnings to PRC statutory reserves were made in accordance with the relevant PRC rules and regulations and the articles of association of the Company and were approved by the board of directors.

(i) General reserve fund

The Company is required to transfer 10% of the net profits, as determined in accordance with the PRC accounting rules and regulations, to general reserve fund until the reserve balance reaches 50% of the registered capital. Transfers to this fund must be made before distribution of dividends to equity holders.

General reserve fund can be used to make good previous years' losses, if any, and may be converted into paid-in capital provided that the balance of the general reserve fund after such conversion is not less than 25% of its registered capital.

(ii) Enterprise expansion fund

Subsidiaries in the PRC are required to transfer a certain percentage of their net profits, as determined in accordance with the PRC accounting rules and regulations, to the enterprise expansion fund. The percentage of appropriation is determined by the board of directors.

Enterprise expansion fund can be used for the Company's business development and working capital purposes. This fund can also be used to increase paid-in capital of the Company, if approved. This fund is non-distributable other than upon liquidation. Transfers to this fund must be made before distribution of dividends to equity holders.

**(c) Capital management**

The Company's primary objectives when managing capital are to safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns for equity holders and benefits for other stakeholders, by pricing products and services commensurately with the level of risk and by securing access to financing at a reasonable cost.

The Company actively and regularly reviews and manages its capital structure to maintain a balance between the higher equity holder returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

The Company monitors its capital structure on the basis of the net debt-to-capital ratio. Net debt is calculated as interest-bearing borrowings less pledged deposits and cash. Capital comprises all components of equity.

During the year ended 31 December 2007, the Company's strategy was to maintain the net debt-to-capital ratio at a range considered reasonable by management. In order to maintain or adjust the ratio, the Company may adjust the amount of dividends paid to equity holders, issue new shares or raise new debt financing.

The net debt-to-capital ratio at 31 December 2007 was as follows:

| | Section B Note | At 31 December 2007 |
|---|---|---|
| | | *RMB'000* |
| Interest-bearing borrowings | 18 | 55,855 |
| Total debt | | 55,855 |
| Less: Cash | 16 | (7,116) |
| Pledged deposits | 15 | (20,691) |
| **Net debt** | | 28,048 |
| **Capital** | | 197,174 |
| **Net debt-to-capital ratio** | | 14% |

The Company is not subject to any externally imposed capital requirements.

## 22. Financial instruments

Exposure to credit, liquidity, interest rate and currency risks arises in the normal course of the Company's business.

Financial assets of the Company include cash, pledged deposits and trade and other receivables. Financial liabilities of the Company include interest-bearing borrowings, trade and other payables.

The Company's exposure to theses risks and the financial risk management policies and practices used by the Company to manage these risks are described below.

### (a) Credit risk

The Company's credit risk is primarily attributable to trade receivables. Management has a credit policy in place and the exposures to these credit risks are monitored on an ongoing basis.

In respect of trade receivables, individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and take into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. Trade receivables are due within 90 days to 120 days from the date of billing.

The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. The industry in which the customers operate also influences its credit risk. At 31 December 2007, 17% and 55% of the total trade receivables was due from the Company's largest customer and five largest customers respectively.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet after deducting any impairment allowance. The Company does not provide any guarantees which would expose the Company to credit risk.

**(b) Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company's policy is to regularly monitor current and expected liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

The following table details the remaining contractual maturities at 31 December 2007 of the Company's financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the reporting date) and the earliest date the Company can be required to pay:

**At 31 December 2007**

| | Effective interest rates | Carrying amount | Contractual undiscounted cash flow | Within 6 months or on demand | More than 6 months but less than 12 months | More than 12 months |
|---|---|---|---|---|---|---|
| | *%* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| Secured bank loans | 6.57 | 30,000 | 30,898 | 30,898 | — | — |
| Unsecured bank loans | 6.57 | 18,991 | 19,514 | 19,514 | — | — |
| Bank advances under discounted bills | 6.93 – 9.65 | 6,864 | 6,864 | 6,864 | — | — |
| Trade and other payables | | 102,399 | 102,399 | 102,399 | — | — |
| | | 158,254 | 159,675 | 159,675 | — | — |

### (c) Interest rate risk

The Company's interest rate risk arises primarily from cash, pledged deposits and interest-bearing borrowings, issued at variable rates and at fixed rates, exposing the Company to cash flow interest rate risk and fair value interest rate risk respectively.

The interest rate profile of the Company's interest-bearing financial instruments at the reporting date is as follows:

| | At 31 December 2007 | |
|---|---|---|
| | *Effective interest rates % (annual)* | *RMB'000* |
| **Fixed rate borrowings:** | | |
| Bank loans | 6.57 | 30,000 |
| Bank advances under discounted bills | 6.93 – 9.65 | 6,864 |
| | | 36,864 |
| **Net variable rate borrowings:** | | |
| Bank loans | 6.57 | 18,991 |
| Less: Cash | 0.72 | (7,116) |
| Pledged deposits | 3.78 | (20,691) |
| | | (8,816) |
| Total net borrowings | | 28,048 |

Sensitivity analysis:

The Company does not account for any fixed rate borrowings at fair value through profit or loss. Therefore a change in interest rate at the reporting date would not affect profit or loss.

A general increase/decrease of 100 basis points in interest rates of variable rate borrowings prevailing at 31 December 2007, with all other variables held constant, would have decreased/increased the Company's profit after tax and retained earnings by approximately RMB 167,000.

This sensitivity analysis above has been determined assuming that the change in interest rates had occurred at 31 December 2007 and had been applied to the exposure to interest rate risk for non-derivative financial instruments held by the Company at the reporting date. The impact on the Company's profit after tax and retained earnings is estimated as an annualised impact on interest expense or income of such a change in interest rates.

### (d) Currency risk

Renminbi is not freely convertible into foreign currencies. All foreign exchange transactions involving Renminbi must take place through the People's Bank of China or other institutions authorised to buy and sell foreign currencies. The exchange rates adopted for the foreign exchange transactions are the rates of exchange quoted by the People's Bank of China that are determined largely by supply and demand.

(i) Exposure to currency risk

The following table details the Company's exposure at 31 December 2007 to currency risk arising from recognised assets or liabilities denominated in a currency other than the functional currency of the entity to which they relate. The amounts of the exposure are shown in Renminbi, translated using the spot rate at 31 December 2007.

| **At 31 December 2007** | **Exposure to foreign currencies** *(Expressed in RMB'000)* | |
|---|---|---|
| | *USD* | *JPY* |
| Bank deposits | 2,104 | 975 |
| Pledged deposits | 2 | — |
| Interest-bearing borrowings | (18,992) | — |
| Net exposure | (16,886) | 975 |

(ii) Sensitivity analysis

The following table indicates the change in the Company's profit after tax and retained earnings that would arise if foreign exchange rates to which the Company has significant exposure at 31 December 2007 had changed at that date, assuming all other risk variables remained constant.

| | **Gain/(Loss) At 31 December 2007** |
|---|---|
| | *RMB'000* |
| USD | |
| – 5% depreciation of RMB | (743) |
| – 5% appreciation of RMB | 743 |
| JPY | |
| – 5% depreciation of RMB | 43 |
| – 5% appreciation of RMB | (43) |

Results of the analysis as presented in the above table represent an aggregation of the effects on the Company's profit after tax and retained earnings measured in the respective foreign currencies, translated into Renminbi at the exchange rate ruling at the reporting date for presentation purposes.

**(e) Fair values**

The carrying amounts of all financial assets and liabilities approximate their respective fair values as at 31 December 2007 due to the short-term maturities of those instruments.

## 23. Capital commitments

Capital commitment outstanding at 31 December 2007, but not provided for in the Financial Information was as follows:

| | At 31 December 2007 |
|---|---|
| | *RMB'000* |
| Contracted for | 572 |

## 24. Material related party transactions

Key management personnel remuneration

Remuneration for key management personnel of the Company, including amounts paid to certain of the highest paid employees as disclosed in note 8 is as follows:

| | Year ended 31 December 2007 |
|---|---|
| | *RMB'000* |
| Short-term employee benefits | 1,490 |

## 25. Significant accounting judgements and estimates

Estimates and judgements 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 selection of critical accounting policies, the judgements and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing the Financial Information. The principal accounting policies are set forth in note 1. Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described as follows:

### (a) Depreciation

Property, plant and equipment is depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual value. The management reviews annually the useful lives of the assets and residual values, if any, in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives and residual values are based on the Company's historical experience with similar assets and taking into account anticipated technological and other changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

**(b) Warranty provisions**

As mentioned in note 19, the Company makes provisions under the warranties it gives on sale of its products after taking into account the Company's recent claim experience. As the Company is continually upgrading its product designs and launching new models, it is possible that the recent claim experience is not indicative of 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.

**(c) Recognition of income taxes and deferred tax assets**

Determining income tax provision involves judgment on the future tax treatment of certain transactions. The management 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 legislation. Deferred tax assets are recognised in respect of temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences can be utilised, management's judgment is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

**26. New standards interpretations not yet adopted**

At the date of issue of the Financial Information, the International Accounting Standards Board has issued the following amendments, new standards and interpretations which are not yet effective for the accounting periods prior to 1 January 2010 and which have not been adopted in preparing the Financial Information.

| | **Effective for accounting periods beginning on or after** |
|---|---|
| Amendments to IAS 32, Financial instruments: Presentation – Classification of rights issues | 1 February 2010 |
| IFRIC 19, Extinguishing financial liabilities with equity instruments | 1 July 2010 |
| Amendment to IFRS 1, First-time adoption of International Financial Reporting Standards – Limited exemption from comparative IFRS 7 disclosure for first-time adopters | 1 July 2010 |
| Revised IAS 24, Related party disclosures | 1 January 2011 |
| Amendments to IFRIC 14, IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction – Prepayments of a minimum funding requirement | 1 January 2011 |
| IFRS 9, Financial instruments: Basis for conclusions on IFRS 9 Amendments to other IFRSs and guidance on IFRS 9 | 1 January 2013 |

The Company is in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the Company's results of operations and financial position.

## C SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by the Company in respect of any period subsequent to 30 June 2010.

Yours faithfully

KPMG
Certified Public Accountants
Hong Kong