

**OVERVIEW**

We are one of the leading automotive engine manufacturers in the independent branded segment of the PRC passenger vehicle, or PV, and light commercial vehicle, or LCV, engine market in terms of sales volume in 2011. We develop, manufacture and sell light-duty gasoline and diesel engines used by various local and foreign-invested PV and LCV manufacturers in the PRC. We were the largest independent branded engine manufacturer of small bus engines in China in 2011 in terms of sales volume, according to the Frost & Sullivan Report. According to the Frost & Sullivan Report, in terms of sales volume in 2011, we accounted for 9.4% of the independent branded segment of the PV and LCV engine market in China, and independent brands accounted for approximately 13.8% of the PV and LCV engine market in China. Our target PV and LCV engine market in China has experienced rapid growth in recent years. According to the Frost & Sullivan Report, the total sales volume of PV and LCV engines in China had grown from 7.9 million units in 2007 to 17.1 million units in 2011. We believe our brand “XCE 新晨動力” enjoys high brand recognition in the PRC automotive industry and it was named as one of the “Top 10 Brands for Diesel Engines” by China Internal Combustion Engine Industry Association and China Automotive News in 2010. We believe that we are one of the few local light-duty gasoline and diesel engine manufacturers in China with the research and development capabilities to independently develop automotive engines. Our Directors confirm that to their best knowledge, our market position in the nine months ended September 30, 2012 has not materially deteriorated from 2011.

Our light-duty gasoline and diesel engines have displacement ranging from 1.0L to 2.7L and engine power ranging from 38.5kW to 120.0kW. As of the Latest Practicable Date, we manufacture and sell 36 models of automotive engines, including 28 models of light-duty gasoline engines, which include 15 models under 1.6L (incl.), three models between 1.6L and 2.0L (incl.), eight models between 2.0L and 2.5L (incl.) and two models between 2.5L and 3.0L (incl.); and eight models of light-duty diesel engines between 2.0L and 2.5L (incl.). All 36 models have obtained necessary regulatory clearance, among which 30 models are in mass production, and six models are not in mass production pending the launch of the compatible vehicles. Our engines are installed in a wide range of PVs and LCVs, including sedans, SUVs, MPVs, small and mini buses, small and light-duty trucks. All vehicles installed with our engines meet the current mandatory National Emission Limits (National III and IV) and Phase II of the Fuel Consumption Limits, or the equivalent overseas standards, and some vehicles installed with our engines meet the Phase III of the PV Fuel Consumption Limits. Our products have received numerous awards in recognition of their quality and performance. For example, China Internal Combustion Engine Industry Association and China Automotive News awarded our D20A light-duty diesel engine with a “2011 Fuel Efficiency Award” in 2011, our 4A13 and 4A15 light-duty gasoline engines with a “2010 Efficient Fuel Consumption Gold Award” in 2010 and our ZD25TCR light-duty diesel engine as one of the “Top 10 Chinese Engines” in 2008, with the other nine engines all being gasoline engines. For the nine months ended September 30, 2012, sales of our gasoline engines and diesel engines accounted for 81.3% and 18.7% of our total engine sales revenue, respectively.

Our customers include local and foreign-invested automotive manufacturers and automotive components companies in China, including well-known automotive manufacturers such as Brilliance China Group, Huachen Group, Zhengzhou Nissan, Xiamen Golden Dragon and GAC Changfeng. We have established stable and long-term relationships with our major customers through joint product development focusing on engine compatibility and by providing high quality products and services. We provide before and after-sales services to our customers through a wide sales network covering all major regions of China. Our independent branding strategy allows us to sell to multiple automotive manufacturers in the fast-growing PV and LCV segments of the automotive industry in China, such as SUVs, minibuses, small trucks, sedans and MPVs.

We have been a jointly controlled entity of Brilliance China and Wuliangye during the Track Record Period. We believe that our close relationship with Brilliance China has provided and will continue to provide us with a competitive edge in our industry. We entered into a non-binding strategic alliance agreement with Dongfeng in January 2007 to jointly develop engines suitable for Dongfeng's vehicles. To solidify this alliance, we established the Dongfeng JV in January 2012 to manufacture engines for Dongfeng's light-duty vehicles. In addition, we entered into a strategic alliance agreement with Zhengzhou Nissan in February 2007 to jointly pursue the research and development and production of engines for Zhengzhou Nissan's SUVs and pickups. We entered into a cooperation agreement in August 2011 and a subsequent engine production line management agreement in November 2011 with FAW Jilin, pursuant to which we will manage and operate one of their engine production lines to manufacture our engines exclusively for their vehicles.

We focus on designing and developing new models of automotive engines based on market demands and trends as well as improving the performance and functionality of our existing engine models. Our research and development team consists of over 160 personnel who have on average over 12 years of automotive engine industry experience in mechanical engineering, internal combustion and other related areas. As we undertake substantially all of our research and development activities in-house, we believe we are able to quickly respond to market demands and changes in market trends. Our research and development capabilities allow us to independently develop our products, which we believe sets us apart from our competitors. Our research and development center was recognized as a "state certified enterprise technology center" by the NDRC and other government authorities in 2004 and our laboratory was accredited by China National Accreditation Service for Conformity Assessment in 2007. As of the Latest Practicable Date, we are in the process of upgrading 11 existing engine models and developing four new engine models, which are in various stages of product development by our in-house research and development team. We plan to bring five engine models out of these 15 models to the market between 2013 and 2014. We have adopted design software, testing and examination equipment made by leading international machinery, auto parts and automotive manufacturers to strengthen our research and development capabilities and to improve the performance of our engines in areas such as power, fuel consumption, emissions and reliability.

All of our current products are manufactured at our production facilities in Mianyang, Sichuan Province. As of the Latest Practicable Date, we had 15 production lines, including three for casting, seven for machining and five for assembly and testing. For the designed engine production capacity, actual engine production volume and utilization rate of our production facilities, see "— Production" in this prospectus.

To meet the increasing demand for our products and to increase our revenue, we plan to expand our current production capacity through construction of new production facilities, improving our production technologies and purchase of new production equipment. Since the end of 2010, we have begun to transition all of our production to new production facilities that are still under construction in the Mianyang High-Tech Development Zone. Upon commencement of full commercial production of our new production facilities by September 30, 2013, our old production facilities will cease operation and our designed annual engine production capacity will increase from the current 255,000 units to 300,000 units. In addition, our Dongfeng JV expects to construct its production facilities with a total planned production capacity of 200,000 units per annum with 100,000 units upon the completion of the phase one of the construction by June 2013. Further, under the engine production line management arrangement with FAW Jilin, we will manage and operate a production line of FAW Jilin, which has a current production capacity of 40,000 units per annum to manufacture our engines exclusively for their vehicles. See "— Production — Production Capacity Expansion" for further details.

We have experienced rapid growth during the Track Record Period. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our revenue was RMB1,285.2 million, RMB1,945.1 million, RMB2,307.7 million and RMB1,946.3 million, respectively. For the same periods, we had net profit of RMB58.3 million, RMB149.5 million, RMB260.4 million and RMB223.8 million, respectively.

## **OUR COMPETITIVE STRENGTHS**

We believe the following competitive strengths have contributed and will continue to contribute to our success:

### **We are one of the leading automotive engine manufacturers in the independent branded segment of the fast-growing PV and LCV engine market in China.**

We are one of the leading automotive engine manufacturers in the independent branded segment of the PRC PV and LCV engine market, with a market share of 9.4% in terms of sales volume among the independent branded engine manufacturers in 2011, according to the Frost & Sullivan Report. We were the largest independent branded engine manufacturer of small bus engines in China in 2011 in terms of sales volume. We focus on producing high quality and high performance/price ratio automotive engines with low fuel consumption, emissions and noise. Our products have received a number of awards over the years. For example, our D20A light-duty diesel engine was awarded “2011 Fuel Efficiency Award” in 2011 and our 4A13 and 4A15 light-duty gasoline engines were awarded a “2010 Efficient Fuel Consumption Gold Award” by China Internal Combustion Engine Industry Association and China Automotive News, and our ZD25TCR light-duty diesel engine was awarded the “Top 10 Chinese Engines” title by the same institutions in 2008, with the other nine engines all being gasoline engines.

China’s automotive industry is growing rapidly as the living standard of Chinese consumers continues to improve, which drives the increasing demand for automotive engines. According to the Frost & Sullivan Report, the PV and LCV engine market in China has experienced rapid growth in recent years. Also, according to the Frost & Sullivan Report, the growing trend is expected to continue from 2012 through 2016, with sales volume expected to reach 34.7 million units in 2016. As one of the leading automotive engine manufacturers in the independent branded segment of the PRC PV and LCV engine market, we believe we are well positioned to take advantage of this expected continued growth of China’s automotive industry.

### **We offer a diversified product portfolio of light-duty engines for a broad range of vehicles.**

We have one of the broadest engine portfolios among local engine manufacturers, according to the Frost & Sullivan Report. As of the Latest Practicable Date, our engine portfolio included 36 models of automotive engines, including 28 models of light-duty gasoline engines and eight models of light-duty diesel engines, supporting a broad range of PVs and LCVs, with displacement ranging from 1.0L to 2.7L and power ratings ranging from 38.5kW to 120.0kW. Some of our engines can be converted into compressed natural gas or mixed fuel engines if required by our customers. We developed the ability to manufacture these convertible engines through our in-house research and development efforts and we believe these engines have significant market potential due to their environment friendly features. All vehicles installed with our engines meet the current mandatory National Emissions Limits (III & IV) and Phase II of the Fuel Consumption Limits, or the equivalent overseas standards. We believe that our broad range of product offerings helps us to satisfy our key customers’ specific needs while appealing to a wide group of customers. Our key customers include several well-known local and foreign-invested automotive manufacturers in the PRC, such as Brilliance China Group, Huachen Group, Zhengzhou Nissan, Xiamen Golden Dragon and GAC Changfeng. We believe that we are well

positioned to benefit from the increasing demand for light-duty gasoline and diesel engines and PRC state policies of encouraging development and purchase of light-duty vehicles with low emissions, high fuel efficiency and reliable engines. For details of such state policies, see “Industry Overview — Overview of the PRC PV and LCV Market — The PRC automotive industry policies and regulations” in this prospectus.

**We have strong research and development capabilities.**

We believe we are one of the few independent branded light-duty gasoline and diesel engine manufacturers in China with the research and development capabilities to independently develop engine products. We do not rely on any third party for our research and development and do not pay technology licensing fees to any third party. We undertake substantially all of our research and development activities in-house. We also have the capabilities of designing and assembling our own production lines based on our product designs, which we believe are cost-efficient and can shorten the lead time from product design to start of production. We have an experienced research and development team consisting of over 160 personnel who have on average over 12 years of automotive engine industry experience in mechanical engineering, internal combustion and other related areas. Our research and development center was recognized as a “state certified enterprise technology center” by the NDRC and other government authorities in 2004 and our laboratory was accredited by China National Accreditation Service for Conformity Assessment in 2007. In February 2009, our D20 light-duty diesel engine development project was included in the National High-Tech Development Plan, or the “863 Plan”, in the modern transportation technology, energy efficiency and new energy automotive areas by the MST in recognition of our strong research and development capabilities. In the past decade, we have independently developed over 36 engine models.

We communicate with our customers on a regular basis to understand their needs, and we design engines that are compatible with their vehicles. As of the Latest Practicable Date, we had 60 effective patents and nine pending patent applications. During the Track Record Period, we had submitted 49 patent applications in the PRC, of which 36 have been granted, four were withdrawn and nine are still pending approval. We have adopted advanced software and equipment of, and entered into collaboration arrangements with leading international machinery, auto parts and automotive manufacturers and consulting firms, such as Wuxi Bosch Automotive Diesel System Co., Ltd. (“Wuxi Bosch”) and Global Optima Automotive Inc. (“Global Optima”), to develop new technologies to improve the performance of our products in areas such as power, fuel consumption, emissions and reliability. We believe these collaborations will help us to further strengthen our research and development capabilities and expand our product portfolio and pipeline.

**We have stable and long-term customer relationships.**

Compared to captive brand manufacturers, our independent branding strategy and diversified product portfolio have enabled us to sell our products to multiple customers. We have maintained stable and long-term relationships with our customers, with our average relationship with major customers spanning five years. Our Company has been a jointly controlled entity of Brilliance China during the Track Record Period and one of our largest customers during the Track Record Period was our connected person, Mianyang Ruian, which is a wholly-owned subsidiary of Brilliance China. Our engines purchased by Mianyang Ruian are primarily installed in vehicles manufactured by Brilliance China. We believe that our close relationship with Brilliance China Group has provided and will continue to provide us with a competitive edge in our industry, and we expect to continue to leverage on the growth of Brilliance China Group to sustain our future sales revenue. We have also established strategic alliances with some of our major customers, such as Zhengzhou Nissan and FAW Jilin, to conduct joint product development, and have conducted joint marketing activities with our customers

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to promote our products. We have recently established the Dongfeng JV with Dongfeng in Changzhou, Jiangsu Province, to manufacture automotive engines for Dongfeng's light-duty vehicles and we have entered into an engine production line management arrangement with FAW Jilin to manage and operate one of their engine production lines to manufacture our engines exclusively for their vehicles. We believe that these activities have helped to strengthen our customer relationships.

### **We have a dedicated and experienced management team.**

As of the Latest Practicable Date, the members of our senior management team had on average over 20 years of experience in the PRC automotive engine industry. In particular, Mr. Wang Yunxian, our chief executive officer and executive Director, has 36 years of industry experience in the areas of production, research and development, quality management and marketing. He was awarded numerous honorable titles such as "National Model Worker" by the national government, recognized as an "Outstanding Innovative Talent of Sichuan Province" by the Sichuan provincial government and also enjoys special government expert allowances (engineering class). Mr. Wu Xiao An, our chairman and executive Director, has been the Chairman of Brilliance China since 2002. He has also been the Chairman of BMW Brilliance Automotive, a 50-50 joint venture between Shenyang Jinbei Automotive Industry Holdings Co., Ltd. and BMW Holding B.V., since its inception in 2003. Mr. Wu Xiao An has extensive experience in the overall management and strategic planning of these companies, as well as in the areas of corporate finance and corporate governance. We believe we have a strong management team with a proven track record in, and deep understanding of, the PRC automotive engine industry, which will help us to capture market opportunities, and develop and execute our future strategies. We believe that the quality and stability of our senior management is one of the key factors driving our success.

### **OUR STRATEGIES**

We aim to strengthen our leading position in the independent branded segment of the PRC PV and LCV engine market and to become the supplier of choice for domestic and international automotive manufacturers through the following strategies:

#### **Further enhance our research and development capabilities and strengthen our technologies**

We believe that ongoing enhancement of our technology capabilities is crucial for our development as a PRC independent branded automotive engine manufacturer. We plan to further leverage our years of accumulated experience in the automotive engine industry and our deep understanding of the automotive engine market to enhance our research and development capabilities and to extend our external cooperation with overseas leading automotive manufacturers to adopt their advanced engine technologies. We intend to achieve this by increasing research and development investment, establishing a new research and development center in Chengdu, Sichuan Province by 2014, recruiting more research and development personnel with extensive experience and knowledge in our industry, increasing our collaborations with our existing research partners and establishing collaborations with new research partners. Our research and development activities will be focused on improvement of existing products, development of new models of light-duty engines, and fuel-efficient and environment friendly hybrid engines. For example, our research and development projects include developing fuel-electricity hybrid engine with displacement less than 1.5L. We expect these increased research and development efforts will allow us to broaden our product portfolio, increase our capabilities in the areas of new energy engine technology, key parts manufacturing technology and consolidated testing and analysis.

**Expand our product offerings to cater to evolving market demand**

Leveraging our current leading position in the independent branded segment of the PRC PV and LCV engine market, we intend to expand our product portfolio to meet the evolving market demand for cleaner, more fuel-efficient and higher performance automotive engines. We believe we have the market expertise, technological know-how and execution capabilities to develop successful new models of automotive engines. In particular, we intend to focus on expanding our product offerings of 1.0L to 2.0L gasoline engines as well as diesel engines, as we believe that customers' demand for these engines will continue to increase in the future, and enhancing our product specifications and qualities to meet higher international standards. As of the Latest Practicable Date, we were in the process of upgrading 11 existing engine models and developing four new engine models, which are in various stages of product development by our in-house research and development team. We currently plan to bring five engine models out of these 15 models to the market between 2013 and 2014, including four models of gasoline engines and one model of diesel engines.

**Expand our production capacity to meet the increasing demand for our products**

We plan to increase our production capacity by constructing new production facilities. We are constructing new production facilities in the Mianyang High-Tech Development Zone in Sichuan Province, approximately 11 km from our existing production facilities. Since the end of 2010, we have been in the process of transitioning all of our production to our new production facilities. We expect our new production facilities to commence full commercial production by September 30, 2013. Upon commencement of full commercial production at our new production facilities, we expect our annual production capacity to increase from the current 255,000 units to 300,000 units. Our newly-established Dongfeng JV plans to construct an engine production facility with a total planned annual production capacity of 200,000 units in Changzhou, Jiangsu Province to manufacture the joint venture branded engines for Dongfeng's light-duty vehicles. Under our engine production line management arrangement with FAW Jilin, we have agreed to manage and operate a production line of FAW Jilin to manufacture our engines exclusively for their vehicles. The production line currently has a production capacity of 40,000 units per annum. We intend to hire additional production personnel and purchase advanced equipment to facilitate this increased production capacity. We may also build new manufacturing facilities in closer geographic proximity to our customers to shorten the delivery time of our products to them.

**Increase our market share by strengthening relationships with our existing customers and developing new customer relationships**

We plan to further strengthen relationships with our existing customers through improving our existing products to better meet their needs, increasing the performance/price ratio advantage of our products to differentiate ourselves from our competitors, as well as providing high quality before and after sales customer services. We also plan to create and strengthen our customer relationships through joint development of new products specifically for their vehicles. Once their vehicles are bundled with our engines, it is costly and time-consuming for our customers to replace us with other engine suppliers. We have established a joint venture with our major customer Dongfeng to manufacture engines for their vehicles. We expect such joint venture arrangement to create steady demand for our engines and further align our strategic interests. We also plan to attract new customers by promoting our products through various media platforms and participating in international and domestic conferences that we believe can broaden our customer base. In addition, through engine sales or vehicle sales of our customers, we may expand into overseas markets, including Southeast Asia, the Middle East, South America and certain African countries, which have increasing demand for alternative fuels and environment friendly hybrid engines. We expect to further leverage our relationship with our Controlling Shareholder, Brilliance China, and other customers to increase indirect export of our engines through export of their vehicles installed with our engines.

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**OUR PRODUCTS**

Our principal products are light-duty gasoline and diesel engines. We also manufacture and sell certain spare parts for our engines and provide testing services to external customers. As of the Latest Practicable Date, we manufacture and sell 36 models of automotive engines, including 28 models of light-duty gasoline engines in various displacement ranges, including 15 models under 1.6L (incl.), three models between 1.6L and 2.0L (incl.), eight models between 2.0L and 2.5L (incl.) and two models between 2.5L and 3.0L (incl.); and eight models of light-duty diesel engines between 2.0L and 2.5L (incl.). All 36 models have obtained necessary regulatory clearance, among which 30 models are in mass production, and six models are not in mass production pending the launch of the compatible vehicles. Some of our engines can be converted into compressed natural gas or mixed fuel engines if required by our customers. We developed the ability to manufacture these convertible engines through our in-house research and development efforts and we believe these engines have market potential due to their environment friendly features. Our diversified product portfolio allows us to meet different demands from our customers for a wide range of PVs and LCVs. Substantially all of our products are sold under our “XCE 新晨動力” brand. We believe that our “XCE 新晨動力” brand enjoys high brand recognition in the PRC automotive industry and it was named as one of the “Top 10 Brands for Diesel Engines” by China Internal Combustion Engine Industry Association and China Automotive News in 2010. We focus on producing high quality and high performance/price ratio automotive engines with low fuel consumption, emissions and noise that target the mid to low end automotive markets. All vehicles installed with our engines meet the current mandatory National Emissions Limits (III & IV) and Phase II of the Fuel Consumption Limits, or the equivalent overseas standards, and some of vehicles installed with our engines meet Phase III of the PV Fuel Consumption Limits. Our engines are in compliance with all emission standards, fuel consumption limits and noise limits required for the manufacture and sale of automotive engines in the PRC.

The following table sets forth the revenue and percentage of revenue contribution of our engines sales and other income during the Track Record Period:

|   | Year ended December 31,     |                                    |                             |                                    |                             |                                    | Nine months ended<br>September 30, 2012 |                                    |
|---|-----------------------------|------------------------------------|-----------------------------|------------------------------------|-----------------------------|------------------------------------|---|------------------------------------|
|   | 2009                        |                                    | 2010                        |                                    | 2011                        |                                    | Revenue<br>(RMB<br>million)             | Percentage<br>of<br>Revenue<br>(%) |
|   | Revenue<br>(RMB<br>million) | Percentage<br>of<br>Revenue<br>(%) | Revenue<br>(RMB<br>million) | Percentage<br>of<br>Revenue<br>(%) | Revenue<br>(RMB<br>million) | Percentage<br>of<br>Revenue<br>(%) |   |                                    |
| <b>Light-duty Gasoline<br/>Engines . . . . .</b>              | 983.7                       | 76.5                               | 1,557.8                     | 80.1                               | 1,803.5                     | 78.2                               | 1,559.9                                 | 80.2                               |
| <b>Light-duty Diesel<br/>Engines . . . . .</b>                | 275.2                       | 21.4                               | 352.2                       | 18.1                               | 463.4                       | 20.0                               | 358.6                                   | 18.4                               |
| <b>Engine components<br/>and service<br/>income . . . . .</b> | 26.3                        | 2.1                                | 35.1                        | 1.8                                | 40.8                        | 1.8                                | 27.8                                    | 1.4                                |
| <b>Total . . . . .</b>  | <u>1,285.2</u>              | <u>100</u>                         | <u>1,945.1</u>              | <u>100</u>                         | <u>2,307.7</u>              | <u>100</u>                         | <u>1,946.3</u>                          | <u>100</u>                         |

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The following table sets forth the sales volume and revenue of our engines by fuel type and displacement range during the Track Record Period:

|                                    | Year ended December 31,   |                             |                           |                             |                           |                             | Nine months ended<br>September 30, 2012 |                             |
|------------------------------------|---------------------------|-----------------------------|---------------------------|-----------------------------|---------------------------|-----------------------------|---|-----------------------------|
|                                    | 2009                      |                             | 2010                      |                             | 2011                      |                             | Sales<br>Volume<br>(Unit)               | Revenue<br>(RMB<br>million) |
|                                    | Sales<br>Volume<br>(Unit) | Revenue<br>(RMB<br>million) | Sales<br>Volume<br>(Unit) | Revenue<br>(RMB<br>million) | Sales<br>Volume<br>(Unit) | Revenue<br>(RMB<br>million) |   |                             |
| <b>Light-duty Gasoline Engines</b> |                           |                             |                           |                             |                           |                             |   |                             |
| ≤1.6L .....                        | 32,292                    | 265.8                       | 74,182                    | 589.9                       | 80,326                    | 622.3                       | 86,564                                  | 650.5                       |
| >1.6L — 2.0L .....                 | 37,227                    | 261.7                       | 46,534                    | 321.7                       | 40,320                    | 290.5                       | 34,011                                  | 236.7                       |
| >2.0L — 2.5L .....                 | 49,983                    | 446.3                       | 69,890                    | 635.5                       | 88,238                    | 856.9                       | 65,127                                  | 646.3                       |
| >2.5L — 3.0L .....                 | 438                       | 9.9                         | 478                       | 10.7                        | 1,676                     | 33.8                        | 1,402                                   | 26.3                        |
| Subtotal .....                     | 119,940                   | 983.7                       | 190,084                   | 1,557.8                     | 210,560                   | 1,803.5                     | 187,104                                 | 1,559.9                     |
| <b>Light-duty Diesel Engines</b>   |                           |                             |                           |                             |                           |                             |   |                             |
| >2.0L — 2.5L .....                 | 10,768                    | 275.2                       | 14,817                    | 352.2                       | 19,694                    | 463.4                       | 16,543                                  | 358.6                       |
| <b>Total</b> .....                 | <b>130,708</b>            | <b>1,258.9</b>              | <b>205,901</b>            | <b>1,910.0</b>              | <b>230,254</b>            | <b>2,266.9</b>              | <b>203,647</b>                          | <b>1,918.5</b>              |

### Light-duty Gasoline Engines

As of the Latest Practicable Date, we manufacture and sell 28 models of light-duty gasoline engines, such as JM491Q-ME, XC4G19 and V19. Our gasoline engines have displacements ranging from 1.0L to 2.7L and power ratings ranging from 38.5kW to 120.0kW. Our light-duty gasoline engines are designed to have high performance, low vibration, low noise and low fuel consumption. We have adopted various advanced technologies for our light-duty gasoline engines, such as controlled burn rate (CBR), electronic throttle control (ETC) and variable valve timing-intelligent (VVT) technologies. Our 4A13 and 4A15 models received the “2010 Efficient Fuel Consumption Gold Award” from China Internal Combustion Engine Industry Association and China Automotive News.

The following table sets forth certain details of our main models of light-duty gasoline engines:

| Products     | Key Specifications<br>(Displacement,<br>Power, Torque)        | Applicable Types<br>of Vehicles                               | Emission<br>Standards | Fuel<br>Consumption<br>Standards | Product<br>Launch Year |
|--------------|---|---|-----------------------|----------------------------------|------------------------|
| <b>4A15*</b> | 1.495L,<br>75kW/5600 —<br>6000rpm,<br>135Nm/4000 —<br>4600rpm | A-segment mini<br>cars, mini vans,<br>mini SUVs               | National IV           | Phase III                        | 2008                   |
| <b>V19</b>   | 1.997L,<br>78kW/4600 —<br>4800rpm,<br>180Nm/2400 —<br>3600rpm | SUVs, pickup<br>trucks, small<br>buses, light-<br>duty trucks | National IV           | Phase II                         | 2008                   |



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| <b>Products</b>  | <b>Key Specifications<br/>(Displacement,<br/>Power, Torque)</b> | <b>Applicable Types<br/>of Vehicles</b>      | <b>Emission<br/>Standards</b> | <b>Fuel<br/>Consumption<br/>Standards</b> | <b>Product<br/>Launch Year</b> |
|------------------|---|--|-------------------------------|---|--------------------------------|
| <b>JM491Q-ME</b> | 2.237L,<br>76kW/4200 —<br>4600rpm,<br>193Nm/2600 —<br>3200rpm   | SUVs, pickup<br>trucks, small<br>buses       | National<br>IV                | Phase II                                  | 2010                           |
| <b>4RB2</b>      | 2.438L,<br>102kW/4600 —<br>5000rpm,<br>217Nm/2600 —<br>3200rpm  | MPVs, SUVs,<br>pickup trucks,<br>small buses | National IV                   | Phase II                                  | 2008                           |
| <b>JM495QF-E</b> | 2.693L,<br>110kW/4400 —<br>4800rpm,<br>240Nm/2800 —<br>3600rpm  | MPVs, SUVs,<br>medium<br>buses               | National III                  | Phase II                                  | 2006                           |

\* Awarded “2010 Efficient Fuel Consumption Gold Award” by China Internal Combustion Engine Industry Association and China Automotive News

### Light-duty Diesel Engines

As of the Latest Practicable Date, we manufacture and sell eight models of light-duty diesel engines, such as DK4A, ZD25TCR, D20A and D22A. Our diesel engines have displacements ranging from 2.0L to 2.5L and power ratings ranging from 72kW to 85kW. We have adopted various advanced technologies for our light-duty diesel engines, such as electronic control common rail system, exhaust gas intercooler recirculation system, turbocharger and ETC. We believe that our light-duty diesel engines are compact, powerful, fuel-efficient and produce low emissions, vibration and noise.

The following table sets forth certain details of our current main models of light-duty diesel engines:

| <b>Products</b> | <b>Key Specifications<br/>(Displacement,<br/>Power, Torque)</b> | <b>Applicable Types of<br/>Vehicles</b>                      | <b>Emission<br/>Standards</b> | <b>Fuel<br/>Consumption<br/>Standards</b> | <b>Product<br/>Launch Year</b> |
|-----------------|---|--|-------------------------------|---|--------------------------------|
| <b>DK4A</b>     | 2.498L,<br>75kW/3600rpm,<br>260Nm/1600 —<br>2400rpm             | SUVs, small<br>buses, light-duty<br>trucks, pickup<br>trucks | National III                  | Phase III                                 | 2008                           |
| <b>ZD25TCR</b>  | 2.498L,<br>80kW/3800rpm,<br>260Nm/1600 —<br>2400rpm             | SUVs, small<br>buses, light-duty<br>trucks, pickup<br>trucks | National III                  | Phase III                                 | 2008                           |
| <b>ZD25TCI</b>  | 2.498L,<br>85kW/3800rpm,<br>280Nm/1800 —<br>2600rpm             | SUVs, small<br>buses, light-duty<br>trucks, pickup<br>trucks | National IV                   | Phase III                                 | 2011                           |

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### Our Product Pipeline

According to the Frost & Sullivan Report, market demand for low emission, high fuel-efficiency and high reliability automotive engines has increased both in the PRC in recent years. The demand is largely driven by state policies and regulations and oil price and supply. To take advantage of this market trend, we focus on developing products that have these features. Most of vehicles installed with our latest models of engines comply with National Emissions Limits (IV), and Phase III of the Fuel Consumption Limits, which is a higher standard than the current national fuel consumption limit. We believe we have the market expertise, technological know-how and execution capabilities to develop successful new models of automotive engines. In particular, we intend to focus on expanding our product offerings of 1.0L to 2.0L gasoline engines and diesel engines. As of the Latest Practicable Date, we were in the process of upgrading 11 existing engine models and developing four new engine models, which are in various stages of product development by our in-house research and development team. Among these 15 models, we currently plan to bring five models to the market between 2013 and 2014, including four models of gasoline engines and one models of diesel engines. The table below sets forth the details of these five engine models:

| <b>Products</b> | <b>Type of Engine</b>                               | <b>Key Technology</b>   | <b>Emission Standards</b> | <b>Fuel Consumption Standards</b> | <b>Applicable Types of Vehicles</b>   | <b>Expected Time to Market</b> |
|-----------------|---|---|---------------------------|-----------------------------------|---------------------------------------|--------------------------------|
| 4A15T           | 1.5L turbocharged gasoline engine                   | Turbo charger, intercooler, independent cylinder ignition, lightweight piston, ETC, DOHC, VVT                           | National IV/V             | Phase III                         | Sedans, mid/high-end SUVs             | April 2013                     |
| A15H            | 1.5L hybrid gasoline engine                         | Independent cylinder ignition, lightweight piston, low-tension piston ring, ETC, offset crankshaft                      | National IV/V             | Phase III                         | Mixed fuel vehicle                    | October 2014                   |
| V22             | 2.2L VVT gasoline engine                            | ETC, lightweight piston, low-tension piston ring, VVT   | National IV/V             | Phase II                          | SUVs, MPVs, pickups, light-duty buses | April 2014                     |
| 3TZ             | 2.7L VVT gasoline engine                            | Double balance shaft, multi-point fuel injection, ETC, DOHC   | National IV/V             | Phase III                         | SUVs, MPVs and small buses            | June 2013                      |
| DK5             | 3.0L high pressure common rail system diesel engine | Third generation high pressure common rail system, increased pressure intercooler, EGR, ETC, DOHC, double balance shaft | National IV/V             | Phase III                         | SUVs, MPVs                            | October 2013                   |

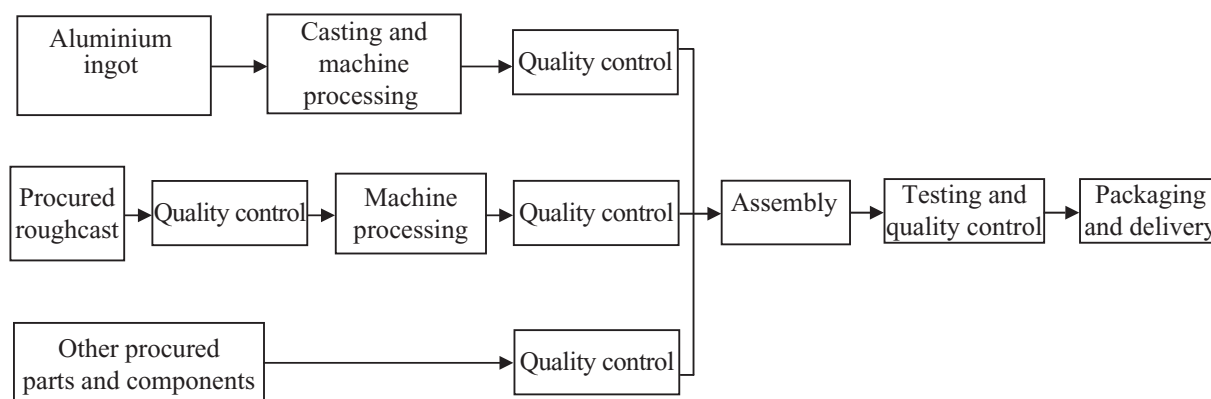
### PRODUCTION

Production of our engines generally requires one principal raw material and over 200 kinds of engine components. We source most of the raw material and engine components used in our production from external suppliers. We manufacture a portion of the key engine components, such as cylinder chambers and cylinder heads to control their quality, to protect our proprietary technology and to save costs. The engine components we produce are mainly used for the manufacture of our engines and sale to our customers for repair and maintenance purposes. Sales of our engine components accounted for less than 5% of total revenue for each of the three years ended December 31, 2011 and

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the nine months ended September 30, 2012. Our main raw material is aluminum ingots. We cast and refine aluminum ingots into roughcast, which are then processed and machined into engine components. We also purchase roughcast from third parties which we process and machine into engine components that fit the specifications of our products. All the engine components either purchased directly from third parties or manufactured by us before being assembled must pass quality control and testing to ensure the quality of the final products. The final products are further tested before delivery to the customer.

The following diagram sets forth the manufacturing process of our engines:



We carry out all of our manufacturing activities at our production facilities located in Mianyang, Sichuan Province. Our current production facilities occupy an aggregate site area of approximately 59,043.94 sq.m. with an aggregate floor area of approximately 32,184.86 sq.m. As of the Latest Practicable Date, we had 15 production lines, including three for casting, seven for machining and five for assembly and testing. Our production lines at our production facilities generally operate 16 hours a day, five days a week, with stoppages for routine repairs and maintenance. Our manufacturing employees generally work eight hours a day and two shifts per day.

The following table sets forth the designed engine production capacity and actual engine production volume and utilization rates of our production facilities for the periods indicated:

|  | Year ended December 31, |                      |         |                      |
|--|-------------------------|----------------------|---------|----------------------|
|  | 2009                    | 2010                 | 2011    | 2012                 |
| Designed engine production capacity <sup>(1)</sup> (Units) . . . . . | 139,200                 | 200,000              | 220,800 | 255,000              |
| Actual engine production volume (Units) . . . . .                    | 140,323                 | 212,200              | 220,013 | 265,321              |
| Utilization rate (%) <sup>(2)</sup> . . . . .                        | 100.8 <sup>(3)</sup>    | 106.1 <sup>(3)</sup> | 99.6    | 104.0 <sup>(3)</sup> |

(1) Our designed engine production capacity is calculated based on 251 working days per year and two workshifts of eight hours each per day and is the weighted average of the production capacity based on the month of the year in which the production capacity was realized.

(2) Our utilization rate is calculated based on our actual engine production volume divided by our designed engine production capacity.

(3) Over 100% utilization rate was due to the addition of a third workshift during the period.

We maintained an efficient level of facility utilization throughout the Track Record Period due to our prudent capital investment style and ability to design and build flexible production capacity that can be adjusted based on our needs.

We source our core production equipment from leading international machinery manufacturers from countries such as Germany, U.S., Japan and Austria. We also source some of our production equipment from advanced local machinery manufacturers. We select our equipment suppliers mainly

through bidding processes to compare their prices, technologies, delivery times and other factors in order to select the best overall terms for us. We also have the capabilities of designing and assembling our own production lines based on our product design, which we believe can shorten the lead time from product design to the start of production.

### **Production Capacity Expansion**

#### *Mianyang High-Tech Development Zone*

We plan to increase our production capacity by constructing new production facilities, improving our manufacturing technologies and acquiring additional equipment. Currently, we are constructing new production facilities located in the Mianyang High-Tech Development Zone in Sichuan Province, approximately 11 km from our current production facilities. Our whole operation, including our current research and development facilities, will be relocated to the new production facilities as encouraged by Mianyang government after the Wenchuan Earthquake. Construction of the new production facilities commenced in April 2010. Since the end of 2010, we have been in the process of transitioning all of our production lines, equipment and personnel to the new location while minimizing the interruption to our operations. The relocation is expected to be completed by September 30, 2013. The estimated capital expenditures in relation to the land acquisition for, and construction of, the new production facilities is approximately RMB245 million, of which RMB27.2 million had been spent up to January 31, 2013 and funded by cash flows from our operations and bank borrowings. We expect to fund the remaining RMB217.8 million also by cash flows from our operations and bank borrowings. As of the Latest Practicable Date, a part of our production facilities have been relocated and our total production capacity has reached 255,000 units per annum through production technology improvement. Upon full commercial production at our new production facilities, which we currently estimate to be by September 30, 2013, we expect our designed annual engine production capacity to increase from the current 255,000 units to 300,000 units. As during the Track Record Period, the demands for our products had exceeded our production capacity and based on our estimation of the increasing customer demands for our products and the general market environment, we believe that we can sufficiently utilize the expanded capacity.

Upon commencement of full commercial production at our new production facilities, our old production facilities will cease operation. As all of our production and research and development facilities and equipment will be moved to the new site, the old factory and ancillary buildings which have sustained structural damages during the Wenchuan Earthquake will no longer be in use and, although we have no plans yet, we expect to demolish them according to Mianyang city planning as the land has been designated for real estate or other commercial purposes in general. We have no intention to engage in the real estate business even though the old site may be designated for real estate purposes. The local government may claim the land for development and compensate us accordingly, or we may dispose of the land in other ways if necessary. But since Mianyang city has no final plan on how to develop this area, it is impossible for us to evaluate the financial impact at this stage. We do not expect the relocation to new site would result in material write-off of fixed assets and other provisions, as we will relocate substantially all of the equipment and machinery to the new production facilities and the remaining carrying values of buildings and other fixed assets at the old production facilities are immaterial after years of depreciation. As of September 30, 2012, the carrying value of buildings and fixed assets at the old production facilities was approximately RMB5.9 million.

Furthermore, subject to market conditions and the growth of our operations, we plan to construct three new production lines and improve our existing production lines at the new Mianyang production site by investing an additional RMB281.7 million between 2013 and 2016, which will be funded entirely with the net proceeds from the Global Offering.

*Dongfeng Joint Venture*

New production facilities will also be constructed for the Dongfeng JV in Changzhou, Jiangsu Province with a planned production capacity of 200,000 units per annum, to manufacture engines for Dongfeng's light-duty vehicles. Pursuant to the joint venture agreement entered into between Dongfeng and us in December 2011, the production facility construction is expected to be completed in two phases, with the first phase began in July 2012, and currently is expected to be completed by June 2013, and the second phase expected to finish within 12 months from the commencement of construction. Upon the completion of the phase one construction, the production capacity will reach 100,000 units per annum. Pursuant to the joint venture agreement and articles of association of the Dongfeng JV, the board of Dongfeng JV consists of eight members, four from Dongfeng and four from us. The parties will take turns in nominating the chairman of the board and the general manager of the Dongfeng JV, with Dongfeng nominating the first chairman of the board and us nominating the first general manager. The parties will nominate equal numbers of senior management members of the Dongfeng JV to manage its daily operations. The parties shall share the profits and obligations as shareholders in equal proportion. No party can transfer its interest in the Dongfeng JV without prior consent of the other party and each party enjoys pre-emptive rights in acquiring such interest in the Dongfeng JV. The products manufactured by the Dongfeng JV will include our existing engine models compatible with Dongfeng's vehicles or new engine models to be developed for Dongfeng's vehicles. Pursuant to the joint venture agreement, Dongfeng shall ensure Dongfeng JV's production capacity is fully utilized by procuring sufficient orders. The manufacturing technologies used in the production may be introduced by either party or independently developed by the Dongfeng JV or acquired from third parties. The engines manufactured by the Dongfeng JV will display the independent brand of the Dongfeng JV. Dongfeng JV will be accounted as a jointly controlled entity of our Group.

The total estimated capital expenditures in relation to the construction of the new production facilities is approximately RMB800 million, of which RMB250 million will be funded by the joint venture parties through capital injections in equal proportions and the remaining by joint venture itself by cash flows from its operations and bank borrowings. We estimate that our capital expenditures in relation to the Dongfeng JV is approximately RMB125 million, of which RMB50.0 million was incurred for the nine months ended September 30, 2012 as capital injection to the joint venture by us and funded by cash flows from our operations and bank borrowings. We expect to fund the remaining RMB75.0 million also by cash flows from our operations and bank borrowings. Dongfeng JV was established on January 9, 2012 and has a term of 20 years. The parties to the Dongfeng JV are still in the process of finalizing the details of the JV's management and operations.

*FAW Jilin Production Line Management Arrangement*

Furthermore, we entered into a cooperation agreement with FAW Jilin in August 2011 and a subsequent engine production line management agreement in November 2011, pursuant to which we will be a designated engine supplier for FAW Jilin to help satisfy their increasing engine demand. To achieve this strategic cooperation, initially, we will manage, operate and maintain an engine production line owned by FAW Jilin located in Jilin Province. The production line has current annual production capacity of 40,000 units. The engine production line management agreement has a term of five years subject to extension, during which we will manufacture on the production line two of our engine models exclusively for FAW Jilin's vehicles at a supply price that will be accounted as our revenue, with a discount for the benefit of FAW Jilin. We do not pay any separate fees to FAW Jilin to manage and operate its production line. We will provide raw materials and engine components and key employees and are responsible for daily management of the operations. We are not allowed to transfer, sublease or create pledge or guarantee on the production line. We do not expect to incur any capital expenditures in relation to this arrangement as the production facilities belong to FAW Jilin. This operation is currently at production preparation stage. We expect it to commence full production by September 30, 2013.

We plan to manage our production capacity growth by leveraging our experience in managing our existing production facilities and expanding our production capacity cost-efficiently. Our additional production capacity will mainly be applied to satisfy increasing customer demand of our products, especially designated engine models to be installed in Dongfeng and FAW Jilin's vehicles. The new production facilities will be staffed with our existing experienced management staff and employees and newly recruited employees from local labor market. We will continue to provide various training to our employees. We believe that most of our current suppliers are companies who provide their products to multiple customers nationally or even internationally. Therefore, we are confident that they will have sufficient production capacities themselves to provide raw material and engine components to facilitate our production capacity expansion. We will consider procuring from new suppliers based on our production needs who need to comply with our supplier selection process. We will continue to examine our suppliers' production capacities and product quality to ensure that they will be able to support our production capacity growth. Furthermore, we plan to adopt our existing logistics and quality control systems at our new production facilities. For details of such systems, see "— Logistics" and "— Quality Control."

#### *PVM Engine Production Line*

On December 12, 2012, we entered into an engine assembly license agreement and related agreements with a leading European passenger vehicle manufacturer ("PVM") and BMW Brilliance Automotive, which authorizes us to manufacture a specific PVM engine model primarily for supply to Shenyang Jinbei for installation into a Jinbei MPV model under an engine supply agreement to be entered into between Shenyang Jinbei and us. Under this agreement, PVM will grant us a non-exclusive license of its technology to enable us to manufacture the PVM engines, and provide us with relevant technical consulting services in relation to the installation of a production line at our production facilities and training of our employees in the production of the engines. In consideration, we will pay royalties to PVM and relevant remuneration and expenses. Furthermore, pursuant to this agreement, we will procure all related engine parts exclusively from BMW Brilliance Automotive.

As of the Latest Practicable Date, further details of this production plan are yet to be finalized by the parties. We expect the production of this engine model will commence around June 2014 and, we expect to install a new production line at our production facilities with an estimated annual production capacity of 50,000 units. The estimated total capital expenditure related to this production plan is approximately RMB100.6 million, which we expect to incur between 2013 and 2016.

#### **RAW MATERIAL AND ENGINE COMPONENTS AND SUPPLIERS**

Our production involves one principle raw material and over 200 kinds of engine components which we source from over 200 suppliers. Our principal raw material is aluminum ingots and our engine components include cylinder casting, electronic fuel injection systems, crankshafts and other parts and components. We do not have a single raw material or engine component that accounted for more than 10% of our total costs of raw material and engine components during the Track Record Period. We mainly source our raw material and engine components from various independent third-party suppliers in the PRC, and to a lesser extent, from our related companies. Our suppliers include many well-known parts and components suppliers such as Beijing Delphi Automotive Co., Ltd. ("Beijing Delphi") and Wuxi Bosch. These reputable suppliers can provide us with a steady supply of quality engine components, such as ETC and high pressure common rail system, which are crucial to the functionality and performance of our engines. Most of our major suppliers are located within 200 km of our production facilities, which facilitates the timely delivery of our supplies and reduces transportation costs.

We had one supplier of aluminum ingots during the Track Record Period, with whom we have maintained a long-term and stable relationship over the years. We did not experience any shortage or

delay of aluminum ingots supply during the Track Record Period. However, we have in the past experienced delays by our suppliers in the delivery of some of the engine components during peak seasons. These delays had no material adverse effect on our operations and we did not receive any compensation from the suppliers or make any compensation to our customers, because only small quantities of certain engine components were delayed by a few days. On these occasions, we adjusted our production plan to use the production lines to manufacture other engine models temporarily. We have more than one supplier for most types of our key engine components. If there is only one current supplier for any type of key engine component, we strive to ensure that there are suitable alternatives available on short notice if required. We believe that this policy allows us to reduce our reliance on single suppliers and minimizes the risk of supply shortage. We may also adjust our production plan if necessary to avoid any suspension of production caused by any potential delays in delivery of raw material and engine components. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, purchases from our top five suppliers represented 32.0%, 34.1%, 30.8% and 35.9% of our total cost of sales respectively, and purchases from our single largest supplier accounted for 9.3%, 9.1%, 7.7% and 9.9% of our total cost of sales, respectively. These top five suppliers mainly include parts and components suppliers, such as Beijing Delphi, Wuxi Bosch and Xinhua Combustion Engine. Save as disclosed in the “Connected Transactions” section of this prospectus, none of our Directors or substantial Shareholders has any interest, direct or indirect, in our major suppliers.

We procure aluminum ingots and engine components from our list of pre-approved suppliers that meet our quality standards. We normally select suppliers based on their quality assurance, prices, technology capabilities, production capacities and delivery time in order to secure the best terms for us. Before confirming the selection of a supplier, our quality assurance team performs background checks on the supplier’s operating history and market reputation, makes on-site visits to the supplier’s production facilities, obtains product samples for inspection and testing by our quality assurance team and conducts interviews with the supplier to assess its suitability and ability to meet our quality requirements. In addition, our quality assurance team conducts on-site assessments of the supplier’s quality assurance systems. We conduct annual reviews of pre-approved suppliers and evaluate them on the basis of, among other factors, quality of goods, speed of delivery, availability of supply and price. Currently, substantially all our suppliers have obtained ISO/TS16949:2009 or ISO9000 certification for their quality management systems.

We normally enter into supply contracts with our suppliers on a yearly basis at the beginning of the year, which provide for, among others, the unit prices of engine components procured under the contracts which remain valid and effective throughout the year. Such unit prices are usually not adjustable. Our purchase price of aluminum ingots is determined based on the market prices of aluminum ingots of the week of delivery. Under the supply contracts, we give periodic purchase quantity orders, which are based on our customer orders and internal forecast, to our suppliers, normally one to two months before the delivery time at the determined contract prices. Our suppliers are responsible for providing us with aluminum ingots and engine components meeting the determined quality, specification and delivery time requirements. Depending on the bargaining powers of the parties and the ownership of intellectual properties contained in the engine components, the supply contracts may be mutually or unilaterally exclusive. Our suppliers are normally required to provide product warranty and indemnify us for the damages and losses caused by defects of their supplies or delay in their delivery. Although we do not enter into long-term supply contracts with our suppliers, we are able to maintain long-term business relationships with most of our suppliers. We have on average 11 years of relationships with our top five suppliers. Our economies of scale also allow us, in many cases, to negotiate and secure favorable pricing terms with our suppliers. Such favorable pricing terms include discounts, most favorable prices and marked-to-market prices. We believe that these favorable pricing terms allow us to achieve low production costs.

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We also entered into strategic cooperation agreements with some of our suppliers, such as Wuxi Bosch, to secure competitive pricing terms and ensure stable and quality supplies. Pursuant to these strategic cooperation agreements, such suppliers will develop and supply engine components suitable for our engines, assist us to develop new product models, to establish our engine brand in China and overseas markets, and to expand our market share through technology sharing, service training and advertising support. In return, we agree to use their products in certain models of our engines.

Our raw material and engine component suppliers generally offer us credit terms of three months from issuing invoices with a further three to six months for payment by promissory notes issued by banks and financial institutions. The credit term extended by our suppliers may vary, depending on, among others, our relationship with the particular supplier and the volume and prices of our purchases.

### INVENTORY MANAGEMENT

Our inventories comprise mainly aluminum ingots and engine components, work-in-progress and finished goods. As of the Latest Practicable Date, we have four warehouses located within the area of our production facilities in Mianyang, and one warehouse located in Shenyang pursuant to a warehouse management agency agreement entered into between us and an independent third party, with a total storage space of approximately 14,000 sq.m.

We conduct regular assessments on our inventories. We generally manufacture our products and purchase aluminum ingots and engine components according to confirmed purchase orders as well as projected sales, which are determined by our management after taking into account the previous month's sales orders, current inventory levels and the sales department's sales forecast for the next one to two months. Our customers routinely provide us with their monthly orders for the coming month and 15 to 20 days' notice for temporary increases in their demand. We collect, on a daily basis, cumulative product sales information, which enables us to adjust our production and inventory levels accordingly. We also closely monitor the inventory levels of our customers on a monthly basis through feedback we receive from them. Furthermore, we have finished products warehouse in Shenyang located close to our large customers to ensure timely delivery of our products to reduce our inventory levels. We require those of our suppliers who are located within 100 km from our production facilities or have warehouses nearby to deliver engine components on a daily basis according to our production schedule. This reduces the time period we need to prepare our inventories of engine components and therefore reduces our own inventory levels. We also have a quota system to control our inventory levels for aluminum ingots and engine components, work-in-progress and finished goods, respectively. Meeting the inventory quota requirements is a factor in evaluating the performance of our relevant personnel.

We have established inventory control procedures to track in-coming and out-going inventory. We have adopted the cycle counting method of physical inventory management. We conduct regular physical counting of our inventory. The results of each stock-take are verified against and reconciled with inventory records in our accounts and warehouse. Any discrepancies are thoroughly investigated by our finance and inventory personnel and corrective measures are implemented by our inventory personnel. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our turnover days of inventory (net of provision) were 61, 51, 47 and 40 days, respectively. We adapt and recycle unused engine components. Engine components or finished goods that are obsolete are generally written off and disposed of according to relevant environment protection regulations. During the Track Record Period, we wrote off obsolete engine components and finished goods, but the amount of write-offs was insignificant.



**LOGISTICS**

Generally, we engage independent third-party logistics companies to deliver our products to our customers, with the logistics companies bearing the risks associated with the delivery. All of our products are delivered by truck from our production facilities directly to the locations of our customers in the PRC and then despatched to their production facilities according to their requirements. We normally bear the entire delivery cost. Occasionally, our customers choose to pick up the products from our facilities and bear the transportation costs themselves. During the Track Record Period, we did not experience any material disruption in the delivery of our products and we did not suffer any loss or pay any compensation as a result of delays in delivery or poor handling by the independent third-party logistics companies. In the future, as our sales network expands, we may build production facilities near the locations of our customers to shorten the delivery time to our customers.

Our suppliers, except for those located within 100 km from our production facilities, generally ship aluminum ingots and engine components to Mianyang and have them stored in warehouses of independent third-party logistics companies engaged by our suppliers. These logistics companies subsequently deliver aluminum ingots and engine components from their warehouses in Mianyang directly to our production lines or, in limited instances, other places designated by us. The deliveries to our production lines or other places designated by us are made on a daily basis based on our production plans. Upon such deliveries, aluminum ingots and engine components are recorded as our inventories. This practice reduces our logistics and storage costs as compared to maintaining our own transportation team and storage space, because these logistics companies can provide the delivery services at lower costs. It also reduces our inventory levels, because before they are delivered from the logistics companies' warehouses to our production lines or other places designated by us, aluminum ingots and engine components in the logistics companies' possession are considered properties of the suppliers instead of our inventories.

We have stringent criteria for the selection of independent third-party logistics companies, such as market reputation, business scale, track record and cost. We evaluate their performance on a monthly basis. The engagement of independent third-party logistics companies to deliver our products to our customers allows us to reduce our capital investment in establishing our own logistics team and reduce the risk of liability for transportation accidents, delivery delays and loss.

For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our total transportation costs were RMB19.9 million, RMB33.3 million, RMB19.0 million and RMB20.5 million, respectively, accounting for 38.3%, 50.6%, 39.2% and 51.1% of our total selling and distribution expenses for the same periods, respectively.

**RESEARCH AND DEVELOPMENT**

We believe research and development is the cornerstone of our competitiveness, growth and development. Our research and development activities focus on designing and developing new models of automotive engines as well as improving various aspects of the engine performance, such as emission levels, fuel efficiency and reliability. As of the Latest Practicable Date, we had independently developed and commercially launched over 36 gasoline and diesel engines with displacement ranging from 1.0L to 2.7L, which are widely used in PVs and LCVs. We were certified as a High and New Technology Enterprise by the Sichuan Province branch of MST and other applicable authorities in December 2008 for a term of three years, which entitled us to enjoy a reduced enterprise income tax rate of 15%. This certification was renewed in 2011, allowing us to continue to enjoy this reduced tax rate for another three years until December 31, 2014. As of the Latest Practicable Date, we had 60 effective patents and nine pending patent applications. During the Track Record Period, we submitted 49 patent applications in the PRC, of which 36 have been granted, four were withdrawn and nine are

still pending approval. No patent application was rejected during the Track Record Period. Our PRC legal adviser, Jingtian & Gongcheng, has advised us that there is no legal impediment for us to obtain the approvals for the pending patent registration if these patent applications pass the substantive examination where applicable and meet the patentability criteria as set out in the PRC Patent Law and other applicable rules.

We undertake all of our research and development activities in-house. We perform thorough market analysis and feasibility studies before commencing any product research and development project and focus on engines that have the potential to gain widespread market acceptance or become the best among similar classes of products on the market. We reach out to potential customers as early as their product development stage and communicate with our customers on a regular basis to understand their needs. From time to time, we design engines that are compatible with their specific vehicle models through entering into joint development contracts with our customers and third parties. This allows us to secure target customers at the research and development stage. The intellectual property resulting from such research and development may belong to us or our customers, and our customers may bear part or all of the development costs. In February 2009, our D20 light-duty diesel engine development project was included in the National High-Tech Development Plan, or the “863 Plan”, in the modern transportation technology, energy efficiency and new energy automotive areas by the MST as recognition of our strong research and development capabilities. We have successfully developed the D20 engine. In the future, our research and development activities will be focused on improvement of existing products, development of new models of light-duty engines, as well as fuel-efficient and environmental friendly fuel-electricity hybrid engines. For example, our research and development projects include developing a less than 1.5L displacement fuel-electricity hybrid engine. As of the Latest Practicable Date, we were in the process of upgrading 11 existing engine models and developing four new engine models, which are in various stages of product development by our in-house research and development team.

For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our research and development costs, which included research expenses and amortization of capitalized development costs, amounted to RMB24.7 million, RMB31.5 million, RMB29.8 million and RMB14.0 million, respectively, which accounted for 1.9%, 1.6%, 1.3% and 0.7% of our revenue, respectively.

### **Our In-house Research and Development Capabilities**

We have established an advanced research and development team comprising over 160 research and development personnel, including our employees and external consultants. Our research and development personnel have on average over 12 years of relevant industry experience in mechanical engineering, internal combustion and other related areas. We believe that our research and development personnel have deep understanding of the PRC automotive industry and regulatory environment, which allows us to maintain our existing position among our peers while responding quickly to market changes. Our research and development center was recognized as a “state-certified enterprise technology center” by the NDRC and other government authorities in 2004 and our laboratory gained accreditation qualification of the China National Accreditation Service for Conformity Assessment in 2007. Our research facilities are equipped with 50 advanced design software, equipment and instruments from leading international machinery, auto parts and automotive manufacturers to strengthen our research and development capabilities and to improve the performance of our products in areas such as power, fuel consumption, emissions and reliability. Our lead-time for development of a new model of automotive engine is typically not more than two years, which has allowed us to develop and commercially market at least one new product each year during the Track Record Period.

We have entered into confidentiality agreements with our research and development personnel that secure our rights to relevant intellectual property developed by them during their term of employment.

Our research and development track record has been acknowledged by the PRC Government and we have received government funding in recognition of these proven capabilities. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, we recognized government grant income of RMB1.4 million, RMB1.9 million, RMB1.4 million and RMB0.3 million, respectively, in the form of government funding or subsidies in relation to various research and development projects to enhance our competitiveness in our industry and to promote our new products. These government grants are non-recurring in nature.

To further strengthen our research and development capabilities and take advantage of the support and incentives offered by the local government, we intend to establish a new research and development center in Chengdu, Sichuan Province, which we expect to start operation in 2014. Chengdu is the capital of Sichuan Province with convenient transportation network and developed infrastructure. In 1993, Chengdu was identified as the Southwest China science and technology, commerce, transportation and financial center and communications hub by the PRC Government. We believe choosing Chengdu as the location of our new research and development center will help us to attract and recruit qualified research and development personnel, to have access to convenient transportation network for communicating with our customers and research and development partners, and to benefit from favorable local government policies. We plan to gradually relocate our current research and development facilities and activities to the Chengdu research and development center once it is completed. We plan to purchase a piece of land with an area of approximately 100,000 sq.m. in Chengdu for our new research and development center. In the future, we also plan to purchase additional advanced equipment and hire additional qualified research and development staff to support the expansion of our research and development activities. We believe our plan to build the Chengdu research and development center is consistent with the industry practice that the manufacturing branch of an auto engine company is located at low labor cost cities whereas its research and development center is located at major cities. The total estimated capital expenditures in relation to the new Chengdu research and development center through 2016 are approximately RMB115.2 million, including RMB11.0 million for acquiring research equipment, RMB99.2 million for construction works and RMB5.0 million for relocating and adjusting existing research equipment which will be funded by cash flows from our operations and the net proceeds from the Global Offering. As of the Latest Practicable Date, the construction of the new Chengdu research and development center is in the planning stage and has not commenced yet. We expect to start investing in and commence the construction of the center in 2013. For further information on our research and development initiatives, see “— Our Products — Our Product Pipeline” in this prospectus.

### **Collaborations with Other Institutions**

In addition to our independent product development, historically we have also entered into collaboration arrangements with leading international machinery, auto parts and automotive manufacturers and consulting firms, such as Wuxi Bosch and Global Optima to develop new technologies to improve the performance of our products in areas such as fuel consumption, emissions and reliability. Such collaborations have enabled us to develop new engine models such as the V19 gasoline engine with CBR, VVT and ETC technologies and the DK4 series diesel engines with electronic control common rail system, EGR (intercooler), turbocharger and ETC technologies. The terms of our collaboration arrangements with leading international machinery manufacturers vary, depending on the subject and nature of the research and our commercial arrangements with them. We provide the necessary equipment and personnel and our research partners offer their expertise. We generally provide funding for these joint research and development projects and we are entitled to

receive the proceeds from the sales of these products and other benefits resulting from the successful development and commercialization of the products. Normally, the intellectual property rights developed during the process, if independently developed by one party, are owned by that party, and if jointly developed, are jointly owned by us and our research partners. We plan to increase our collaborations with our existing research partners as well as new research partners. We believe these collaborations will help us to further strengthen our research and development capabilities and expand our product portfolio and pipeline.

## **CUSTOMERS**

Our customers include local and foreign-invested automotive manufacturers and automotive components companies in China. End customers of our products are automotive manufacturers that install our engines in their vehicle. Our top customers during the Track Record Period include Brilliance China, our Controlling Shareholder, Huachen Group, and their subsidiaries and affiliates, and other well-known automotive manufacturers in China, such as Zhengzhou Nissan, Xiamen Golden Dragon and GAC Changfeng. We have maintained stable and long-term relationships with our customers, with our average relationship with major customers spanning five years. As of December 31, 2009, 2010 and 2011 and September 30, 2012, apart from our Controlling Shareholders and Huachen, we had 24, 26, 24 and 31 customers, respectively. Our engines also reach overseas markets through sales of vehicles installed with our engines, however such sales overseas are not directly conducted by us.

We believe that our core competency lies in our ability to establish stable customer relationships as early as in the product development stage. As engine compatibility is part of the whole vehicle development plan, we strive to become the designated engine supplier to our customers when they develop their vehicle models. Once their vehicles are bundled with our engines, it is costly and time-consuming for our customers to replace us with other engine suppliers, because of the extensive testing required of new engines to be compatible with their vehicles and related registration requirements with relevant regulatory authorities.

Consistent with industry practice in the PRC, before embarking on the sale of new products or sales to new customers, we must first undergo customer approval processes and become an approved supplier of our target customers. Such approval process may take months, during which we are required to submit our sample engines and related specifications and qualifications to our potential customers, who will conduct a series of tests to determine whether the functionality, compatibility and quality of our engines are in compliance with their requirements. This approval process may be carried out in conjunction with joint product development by our customers and us. During the Track Record Period, we did not fail to pass any existing customer's approval process for a new product or fail to maintain existing customer approvals due to our product quality.

## **Supply Agreement**

Once we become a selected engine supplier, we normally enter into a one-year supply agreement with our customer at the beginning of the year. Our supply agreements are normally on a non-exclusive basis. As we are an independent branded engine supplier, we supply our engines to multiple related and unrelated automotive manufacturers in the market. The key terms of the supply agreement generally include but are not limited to the prices of our products, estimated annual purchases, warranty, credit period and return policy. Our customers provide us with an estimate of their annual purchases at the beginning of the year and place orders with us on a periodic basis. Failure to reach the estimated annual purchases does not constitute a breach of the supply agreement by the customer. The unit prices set out in the supply agreement at the beginning of the year usually remain valid and effective throughout the term of the supply agreement. We may give favorable pricing terms to our

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customers, including discounts, most favorable prices and marked-to-market prices. We normally cannot adjust product prices once they are determined in the contracts, unless the contracts have provided for price adjustments in the event of significant fluctuations in engine component costs, in which case, we attempt to adjust the engine prices through good faith negotiation with our customers. Our customers may also ask us to lower the engine prices if they increase order quantities significantly. We generally extend a credit period between 30 to 60 days to our non-related customers and three months to our related companies customers with a further three to six months for payment by promissory notes issued by banks and financial institutions. In certain circumstances, we may require our customer to make a deposit with us before we deliver our products.

### **Warranty Policy**

We provide warranties on our products to all of our customers. Under the warranty, we typically agree to repair and replace defective parts for a period of two to three years or until the product has been running for over 50,000 km to 60,000 km, whichever is earlier. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our warranty costs amounted to RMB4.5 million, RMB12.3 million, RMB8.1 million and RMB7.8 million, respectively.

### **Product Return Policy**

Our product return policy only allows products to be returned due to product defects as assessed and agreed upon by our quality assurance team. During the Track Record Period, we did not receive any material product returns or make any large-scale product recalls due to any quality defects, which would have a material adverse impact on our business and results and operations.

### **Major Customers**

Our single largest customer during the Track Record Period was our connected person, Mianyang Ruian, who is a wholly-owned subsidiary of Brilliance China, for 2009 and 2010, and an independent third-party, Zhengzhou Nissan, for 2011 and the nine months ended September 30, 2012. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our sales to our single largest customer accounted for 29.2%, 23.2%, 27.9% and 26.4% of our revenue, respectively. Our engines purchased by Mianyang Ruian are primarily installed in vehicles manufactured by Brilliance China Group. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, sales to the top five customers of our Group, accounted for 82.9%, 77.8%, 76.0% and 75.3%, of our revenue, respectively.

We sell a substantial portion of our engines to our related companies. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our sales to Brilliance China Group on a group basis accounted for 48.8%, 41.4%, 18.0% and 19.6% of our revenue, respectively, sales to Huachen Group on a group basis accounted for 2.8%, 13.9%, 28.7% and 25.0% of our revenue and sales to our top five customers on a group basis accounted for 86.8%, 86.1%, 84.9% and 81.7% of our revenue, respectively. Such top five customers on a group basis include Brilliance China Group and Huachen Group. The key terms of the supply agreements with our related companies are comparable to those contained in the supply agreements we enter into with other non-related customers. Our Company has been a jointly controlled entity of Brilliance China during the Track Record Period and we have been and expect to continue to leverage on the growth of Brilliance China Group to sustain our future sales revenue and generate a significant portion of our revenue from sales to Brilliance China Group. We believe that our close relationship with our Controlling Shareholders has provided and will continue to provide us with a competitive edge in our industry. For further details, see “Connected Transactions” in this prospectus.

### **Strategic Alliances With Key Customers**

From time to time, we enter into strategic alliance agreements with our key customers to strengthen our existing relationships, to provide for future cooperation and to secure future demands for our products.

We entered into a non-binding strategic alliance agreement with Dongfeng in January 2007 to jointly develop engines compatible with Dongfeng's vehicles. Under the agreement, Dongfeng shall give us priority when selecting engine suppliers based on quality, cost, delivery time and development standards. To solidify this strategic alliance, in January 2012, we established the Dongfeng JV with Dongfeng to manufacture engines primarily for their light-duty vehicles. For further details, see "— Production" in this prospectus.

We entered into a strategic alliance agreement with Zhengzhou Nissan in February 2007 to jointly pursue the research and development and production of advanced engines for Zhengzhou Nissan SUVs and pickups. Pursuant to the strategic alliance agreement, the strategic cooperation is spear-headed by senior managements from both parties who meet every six months and discuss and decide the cooperation plans and operations. We are responsible for the research, manufacture and improvement of the project engines and providing technical support and after-sales services to Zhengzhou Nissan. The project engines are based on our existing engine models but adapted to Zhengzhou Nissan's vehicles to differentiate from our engines supplied to other automotive manufacturers. Intellectual property developed that relates to engine component differentiation shall belong to Zhengzhou Nissan. Our existing cooperations include the installment of DK4 diesel engines and 4RB and 4A15 gasoline engines in Zhengzhou Nissan's National III emission standard-compliant vehicles. Pursuant to the strategic alliance agreement, we provide the project engines exclusively to Zhengzhou Nissan and in return, Zhengzhou Nissan guarantees an unspecified minimum order amount from us. Subsequently, we have entered into sales and purchase agreements with Zhengzhou Nissan on an annual basis, which provide for detailed terms, including the selling prices and quantities of the engines to be procured from us.

We entered into an operation agreement with FAW Jilin in August 2011 and a subsequent engine production line management agreement in November 2011, pursuant to which we will manage, operate and maintain an engine production line owned by FAW Jilin to manufacture on the production line two of our engine models exclusively for FAW Jilin's vehicles. This arrangement fortifies our supplier-customer relationship with FAW Jilin and, to a certain extent, secures our future production quantity under this arrangement. For details of this arrangement, see "— Production" of this prospectus.

One of our strategies is to increase our market share by strengthening relationships with our existing customers and developing new customer relationship. See "— Our Strategies" of this prospectus for more details.

## **SALES AND MARKETING**

### **Sales Team**

As of the Latest Practicable Date, our sales team consisted of 77 sales personnel located in 14 sales regions across China covering local customers in different geographic regions. All of our sales personnel have experience in the automotive and engine industries and are familiar with industry practice and trends. Our local sales teams are managed by our sales department located at our headquarters in Mianyang. Our sales department and our local sales teams are primarily responsible for developing new customers, enhancing relationships with our existing customers, obtaining sales orders, providing after sales services to engine service stations and collecting market information. Our regional sales offices foster strong working relationships with our customers by maintaining regular

contact with them and conducting on-site discussions and inspections. Through such communications, we are able to better understand the latest market developments and our customers' businesses and requirements. This helps us to serve them better and to fulfil their needs in a timely manner.

### **Service Stations**

As of the Latest Practicable Date, our local sales teams supported a national network of over 250 engine service stations operated by independent third parties that are designated by us to provide engine repair and maintenance services. We enter into renewable yearly non-exclusive service contracts with these service stations, pursuant to which they provide engine repair and maintenance services to the end-users, such as automotive drivers and owners, for automobiles installed with our engines during our engine's warranty period. To qualify as our designated service stations, the service station need to locate in an area where there is a sufficient amount of end-users of our engines. It also need to demonstrate sufficient technical and financial capabilities to provide engine repair and maintenance services in accordance with the engine repair and maintenance procedures and standards set out by us. Under these contracts, we mainly provide them with spare parts, technical support, and regular training. We settle our payments to the service stations on a monthly basis. The payments include, based on the detailed repair and maintenance reports submitted by the service stations to our after-sales department, labor costs calculated on an hourly rate, spare parts costs, traveling costs for traveling to customer locations, old parts shipping fees and accessories fees.

### **Pricing Policy**

We determine and adjust our product prices on the basis of market supply and demand, production costs, pricing of comparable products in the market and prevailing market conditions. Pricing is considered as early as in the product development stage when we propose our engine prices to the automotive manufacturers, who take such pricing into consideration when they choose engine suppliers and price their own products. We may price our products at a premium for our reputation and product quality when competing with other domestic manufacturers. For products facing intense competition, we price our products to remain competitive against comparable products in the market and to obtain new market share. We have experienced downward pressure on our product prices as our competitors lower their product prices and at the request of our customers as part of their cost control efforts. We strive to maintain our competitiveness through providing high-quality products and before and after-sales services. We conduct periodic reviews of our pricing strategy. We offer discounts to customers that purchase in large quantities.

### **Marketing**

We conduct both product-specific and more general brand marketing activities as part of our overall marketing strategy. We discover potential customers through market research and then conduct targeted marketing activities, such as customer visits, new technology seminars, product demonstrations and free customer services, to secure such potential customers. We also collect market information and develop products at our customers' requests to increase our brand recognition and product development success rate. We regularly participate in international and domestic industry exhibitions and conferences to identify new customers, promote our products and brand and to keep up to date with market and industry trends and new technologies. We also conduct advertising campaigns through various media, including newspapers, magazines and outdoor advertisements, to raise our brand awareness.

Our current marketing focus is on promoting our light-duty gasoline engines, as we believe that demand for these engines will continue to increase in the future. As customers and potential customers become increasingly environmentally conscious, they tend to purchase more light vehicles with lower

emissions, high fuel efficiency and reliable engines. Our light-duty gasoline engines are well positioned to benefit from this trend and we expect to continue to focus on our light-duty gasoline engines in the future.

### **Customer Service**

We provide a comprehensive range of before and after-sales customer services from engine selection to end-user services. We offer consultation services to our customers as early as at the pre-sale stage. We work closely with our customers and potential customers to understand their needs and offer advice to them to help them select the engine models that are suitable to their requirements and specifications. We carry out joint product development efforts with our customers to satisfy their specific requirements, which we believe gives us a competitive advantage over other engine manufacturers, particularly when we are selected as our customers' designated engine supplier. We offer on-site and off-site technical support from the pre-sale to after-sale stages through over 250 authorized third-party service stations throughout the country. This large service station network ensures that our customers are able to optimize their use of our products and are satisfied that our products are suitable for their requirements and specifications. For our newly developed or custom-designed engines, we visit our customers on a regular basis to follow up on the adaptation of our engines to their vehicles. Our customer service strategy also enables us to obtain feedback from our customers and potential customers which helps us to introduce new products or improve our existing products to meet their needs.

### **QUALITY CONTROL**

We believe that effective quality control is critical to ensuring the quality of our products and maintaining our reputation and success. We seek to ensure that our products consistently meet high industry standards and requirements. We obtained ISO/TS16949:2002 certification and ISO/TS16949:2009 certification for our quality management systems in 2005 and 2010, respectively, which indicates our compliance with internationally recognized standards for quality control. Each year we review the operation of our quality management systems and make appropriate adjustments to maintain the effectiveness of our quality management systems. We have a strict quality control system to monitor and control each stage of our production process, including raw material and engine components procurement, manufacturing and inspection of finished products, to ensure the quality of the final products. As of the Latest Practicable Date, our quality assurance team had 52 employees, including one senior engineer. They are required to become familiar with the relevant PRC national standards, applicable ISO standards, industry standards and the legal and regulatory requirements applicable to our products. They are also required to attend professional training before performing certain quality assurance tasks. We also strive to improve our quality control system and practice by engaging outside consultants and cooperating with leading PRC and overseas vehicle manufacturers. At each stage of the production process, dedicated quality inspectors are assigned to inspect each process according to pre-determined standards and inspection conditions and to record inspection results. Our major customers also conduct periodic review of our quality control system to ensure we comply with their quality standards. As a result of our stringent quality assurance system, we had not experienced any significant product returns, received any material complaints regarding quality or recalled any of our products during the Track Record Period.

### **Raw Material and Engine Components Quality Control**

We select qualified suppliers during the product development stage. Potential suppliers need to pass preliminary, sampling and pre-production testing before becoming our approved suppliers for mass production. All externally supplied raw material and engine components are checked for conformity with the required quality and specifications, either through routine inspection or sample



testing, depending on whether the supplier has strong quality control capabilities and has consistently provided us with high quality supplies. Defective supplies are returned to the suppliers at their cost. We also send our quality control personnel to our suppliers' sites to oversee the manufacturing process and ensure the quality of certain safety-related and other key engine components.

### **Production Quality Control**

Throughout the production process, our products are subject to the inspections of our manufacturing personnel, workshop supervisors and quality assurance department. At each stage of our production process, dedicated quality inspectors are assigned to inspect each process according to pre-determined standards and inspection conditions. Any abnormalities discovered are rectified immediately and recorded. Our production equipment operators are required to adhere strictly to standard equipment operating procedures.

### **Finished Product Quality Control**

All our finished products are subject to engine test runs. In addition, every batch of our finished products is subject to a sample inspection by our quality assurance personnel prior to dispatch to our customers. If no defect is detected, a product approval certificate will be issued and such product will be sent to the warehouse. Our warehouse only releases products that have obtained the product approval certificate.

## **INTELLECTUAL PROPERTY**

We recognize the importance of intellectual property rights to our business and are committed to the development and protection of our intellectual property rights. As of the Latest Practicable Date, we had three registered trademarks in the PRC, and one registered trademark in Hong Kong, 60 effective patents and nine pending patent applications. During the Track Record Period, we submitted 49 patent applications in the PRC, of which 36 have been granted, four were withdrawn and nine are still pending approval.

The validity period for our utility patents is 10 years and the validity period for our invention patents is 20 years, starting from the date the relevant application is filed. All of these patents were issued in the PRC. A patent holder in the PRC enjoys the exclusive right to exclude others from using, licensing and otherwise exploiting the patent in the PRC.

Under PRC law, we have the exclusive right to use a trademark for products and services that we have registered with the PRC Trademark Office of the SAIC. Trademark registration in the PRC is valid for 10 years, starting from the day the registration is approved. If we believe that a third party has infringed upon the exclusive right of our registered trademarks, we may, through appropriate administrative and civil procedures, institute proceedings to request an injunction from the relevant authority or resolution of the infringement through consultation. The relevant authority can also impose fines, and confiscate or destroy the infringing products or equipment used to manufacture the infringing products.

We believe that our primary trademark is well recognized in the PRC automotive engine industry. Our "XCE 新晨动力" brand was named as one of the "Top 10 Brands for Diesel Engines" by the China Internal Combustion Engine Industry Association and China Automotive News in 2010. As our brand name is becoming more recognized in the PRC automotive engine industry, we are devoting our efforts to increasing and enforcing our intellectual property rights, which are critical to our overall branding strategy and reputation.

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During the Track Record Period, we did not experience any infringement of our intellectual property rights, including incidents involving counterfeit or imitation products, that had a material adverse effect on our business.

Some of our manufacturing methods or processes involve unpatented, proprietary technology, processes, know-how or data. With respect to such proprietary know-how that is not patentable and processes for which patents are difficult to enforce, we rely on trade secret protection and confidentiality agreements in order to safeguard our interests. All of our research and development personnel have entered into confidentiality, non-competition and proprietary information agreements with us. These agreements require such employees to assign to us all of their inventions, designs and technologies that they may develop during their periods of employment with us.

### COMPETITION

Our Directors consider the automotive engine industry in which we operate to be highly competitive. Although the industry has high entry barriers, such as technology requirements, equipment requirements and customer recognition, the competition among existing market players is intense in terms of product quality, pricing, performance, reliability, timeliness of delivery, product development capabilities, customer service and overall management. According to the Frost & Sullivan Report, domestic engine brands occupied 43.4% of the Chinese PV and LCV engine market in 2011. We believe that the increase in the market share of local automotive manufacturers encourages the development of local engine suppliers such as us, because local automotive manufacturers in general prefer to source engines from local engine manufacturers. In comparison, global automotive manufacturers in China generally prefer to source engines from their captive brand suppliers.

Our key competitors consist of local automotive engine manufacturers as well as large foreign-invested automotive engine manufacturers in China. In the LCV engine sector, we believe our main competitors include Dongfeng Chaoyang Diesel Engine Co., Ltd. and Beijing Foton Cummins Engine Co., Ltd, both of which are captive brand engine suppliers. In the PV engine sector, we believe our main competitor is Shenyang Xinguang Brilliance. Shenyang Xinguang Brilliance is an independent brand Sino-foreign equity joint venture held as to 50% by Brilliance China. See “Relationship with Our Controlling Shareholders and Huachen — Excluded Business of Brilliance China” in this prospectus. Although our brand may not be as well recognized as some of the foreign-invested automotive engine manufacturers and many of them have substantially greater financial resources than we do, we believe we have advantages in terms of low production costs, better understanding of the PRC market and favorable government support provided to PRC local automotive engine manufacturers. We expect to keep benefiting from these advantages in the future when competing against foreign-invested automotive engine manufacturers. We were one of the first companies in our industry and our brand name and reputation are well recognized in the PRC market. Also, compared with those captive brand engine manufacturers who supply exclusively to the same brand automotive manufacturers, our independent branding strategy allows us to sell our engines to multiple automotive manufacturers and gives us the flexibility to capture the fast-growing PV and LCV engine segment of the automotive industry in China. We believe that the PRC automotive engine industry will remain intensely competitive going forward.

### PROPERTY INTERESTS

Our current production facilities, administrative facilities, research and development facilities, warehouses and employee’s dormitories are primarily located in Mianyang, Sichuan Province and occupy six parcels of land with an aggregate site area of approximately 59,043.94 sq.m., with an aggregate floor area of approximately 32,184.86 sq.m.. We have obtained the land use rights for

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substantially all the site area and the building title certificates for the entire floor area. In addition, we also have several properties for residential purposes located in Mianyang, Guangzhou, Changsha and Shenyang with an aggregate floor area of 1,067.4 sq.m. used by our local sales staff.

The Wenchuan Earthquake in May 2008 caused damage to our factory buildings and other damage to our equipment and inventories. Our operations were suspended for three days and product deliveries to our customers were temporarily delayed. By the end of 2009, our production capacity had substantially recovered to the pre-earthquake level. The actual impairment loss on our assets caused by the Wenchuan Earthquake was mainly related to scrapped engine components of RMB2.3 million (included in provision of inventories in 2008) and fixed assets slightly damaged by the earthquake. The loss of business due to the Wenchuan Earthquake was estimated to be RMB118 million, which was not accounted for in our financial statements. See “Risk Factors — Our business may be significantly affected because of factors beyond our control” in this prospectus. In early 2009, the Mianyang local government offered us a piece of land in the Mianyang High-Tech Development Zone, approximately 11 km from our existing factory, for the relocation of our production plant. Owing to our need to increase our production capacity and encouraged by the local government as part of the post-earthquake city planning, we decided to relocate to the Mianyang High-Tech Development Zone to construct new production facilities and signed the relevant agreement with the local government in October 2009. The new production facilities occupy two parcels of land with an aggregate site area of approximately 202,588.14 sq.m. and construction area of approximately 88,474 sq.m. We obtained the land use rights for these lands from the Mianyang Bureau of State-owned Land and Resources for a term of 50 years for a total consideration of approximately RMB50.6 million. The new factory buildings are constructed using a steel structure designed to withstand strong earthquakes. We have obtained the necessary construction permits related to this project. We currently expect our new production facilities to finish construction and commence full commercial production by September 30, 2013. Although we have no concrete plans yet, we plan to demolish the old factories and ancillary buildings and dispose of the land where the old factories and buildings are located according to Mianyang city planning.

We do not engage in any property activities as defined in Rule 5.01 of the Listing Rules. The total carrying value of our property interests accounted for approximately 7.6% of our total assets as of September 30, 2012 (calculated by reference to the book value of the relevant property interest, including land costs, buildings and construction in progress, as a percentage of the value of our total assets, both as shown in the Accountants’ Report in Appendix I to this prospectus). Calculated on the same basis, no single property had a carrying value exceeding 15% of our total assets as of September 30, 2012. No property valuation report in respect of the Group’s property interests is required in reliance upon the exemption provided by Section 6(2) of the Companies Ordinance (Exemption of Companies and Prospectuses from Compliance with Provisions) Notice (Chapter 32L of the Laws of Hong Kong).

We confirm that there has not been any major acquisitions or disposals of properties since September 30, 2012.

For further details of the owned and leased properties of our Group, see “Statutory and General Information — B. Further Information about our Business — 5. Properties” in Appendix V to this prospectus.

## ENVIRONMENTAL COMPLIANCE

We are subject to national and local environmental protection regulations in China. Under the relevant PRC laws, we are not allowed to start any projects until we have obtained the required approvals from relevant environmental authorities and such authorities are satisfied with our

environmental impact assessments. Under the Environmental Impact Appraisal Law effective from September 1, 2003, we must submit environmental impact assessment reports to the Ministry of Environmental Protection at the relevant national, provincial or local levels with respect to any environmentally sensitive projects, which, as set forth in the catalogue published by the Ministry of Environmental Protection, include engine and equipment production. For any environmentally sensitive project, we must engage a qualified environmental appraiser to assess the environmental impact of such project and prepare a report for submission to the relevant environmental authorities. In addition, PRC laws do not permit any environmentally sensitive project to begin construction until the government regulators are satisfied with the environmental impact assessment. Further, upon completion of the construction project, we are required to apply for inspection of the completed project with the relevant environmental protection authority. Meanwhile, we must also obtain the relevant emission permits and are required to discharge only the pollutants of the types and quantities specified in the emission permits.

In order to comply with the applicable environmental protection laws, we have engaged qualified agencies to prepare the relevant environmental impact assessment documents, obtained the required approvals from relevant environmental protection authorities, passed relevant inspections, obtained the necessary emissions permits and complied with the terms of such permits. During the Track Record Period, we have complied with applicable national and local environmental protection laws and regulations, and we have not received any warning or sanctions or fines imposed by the PRC environmental authorities for incidents of non-compliance with respect to our production facilities.

The pollutants that we discharge primarily consist of exhaust fumes, solid waste, waste oil and water and noise. We have obtained necessary pollutant discharge permits and complied with applicable PRC laws and regulations in treating and disposing of these pollutants. We believe the pollutions discharged are within the permitted emissions standards and will not have any material impact on the environment.

We strive to reduce the environmental impact from our products and production processes and have adopted a number of measures to achieve this objective. Waste water is processed by our own waste water treatment station to reach national safety standards for disposal. Other wastes are collected and disposed of by qualified industrial waste processing and environmental protection entities. We believe the nature of our operations does not create material risks that give rise to environmental protection issues and the above-mentioned measures taken by us are sufficient to maintain our compliance with applicable environmental protection laws and regulations.

For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our cost of compliance with the applicable environmental rules and regulations was approximately RMB0.05 million, RMB0.07 million, RMB0.08 million and RMB0.1 million, respectively. We expect that the annual cost of compliance with such rules and regulations will amount to approximately RMB0.1 million, RMB0.1 million and RMB0.1 million in years 2012, 2013 and 2014, respectively.

## **HEALTH AND SAFETY COMPLIANCE**

Pursuant to national and local health and safety laws and regulations in China, we are required to ensure a safe production and working environment for our employees by providing them with adequate protective clothing and gear, safety education and training and having dedicated safety management personnel, among other requirements. In addition, operators of some of our heavy equipment must undergo special training and obtain special work permits. In order to comply with such laws and regulations, we have developed and implemented a comprehensive safety guidelines and have established a production safety management committee, which is responsible for the supervision and implementation of the safety guidelines and the investigation and analysis of any employee injury or

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fatality and workplace accidents. We have also provided safety training for all of our personnel and have ensured that the operators of the heavy equipment have undergone the required special training. During the Track Record Period, we have complied with all applicable state and local health and safety laws and regulations in all material respects.

During the Track Record Period, we had six incidents resulting in material injuries to our employees during the production process. The injuries were caused by the non-compliance of our safety guidelines by the injured employees or accidents. In addition, there were two employee deaths, neither of which was related to workplace safety. The first case was related to an employee who died at home as a result of carbon monoxide poisoning, and the other case was related to the sudden death of an employee at work due to his own illness. The employees and their families were compensated by the social insurance and welfare fund and relevant payments have been settled in full. As of the Latest Practicable Date, there was no outstanding claims from the employees or their families against us. As a result of the accidents, we added protective parts to the machinery to prevent human errors. We will also continue our employee safety training and enforce our safety guidelines to avoid occurrence of similar incidents. We did not make any payment to the employees or suffer any government investigation or penalty as a result of the above incidents. See “Risk factors — We are subject to safety and health laws and regulations in the PRC and our production operations entail significant risks of workplace injury or death” in this prospectus for the risk of workplace injury or fatality during our production process.

### EMPLOYEES

As of the Latest Practicable Date, we had 1,020 full-time employees. In addition, we also had eight part-time technology experts. The following table sets forth the breakdown of our full-time employees as of the Latest Practicable Date:

| <u>Function</u>                               | <u>Number of Employees</u> | <u>Percentage of Total (%)</u> |
|---|----------------------------|--------------------------------|
| Management and administration . . . . .       | 137                        | 13.4                           |
| Manufacturing and quality assurance . . . . . | 626                        | 61.4                           |
| Sales and marketing . . . . .                 | 77                         | 7.5                            |
| Research and development . . . . .            | 164                        | 16.1                           |
| Technical support . . . . .                   | <u>16</u>                  | <u>1.6</u>                     |
| <b>Total</b> . . . . .                        | 1,020                      | 100                            |

For the three years ended December 31, 2011 and the nine months ended September 30, 2012, we incurred total staff costs (including salaries, benefits and allowances) of RMB52.7 million, RMB67.6 million, RMB63.2 million and RMB51.6 million, respectively.

### Training and Remuneration

We place significant emphasis on staff training and development. We invest in continuing education and training programs for our management personnel and other employees with a view to constantly upgrading their skills and knowledge. Our staff training is either conducted internally by our management and various department heads or externally by training providers. We have adopted a “multi-function” training model for our production line operation personnel. The objective is to equip them with multiple skills to ensure that they can switch between different positions and we have trained personnel available for every position on our production lines and to upgrade the overall skill set of our manufacturing personnel. In addition, we send our manufacturing personnel to other industry-leading automotive engine manufacturers to observe and gain experience and techniques. We also provide regular training programs for our sales and after-sales personnel which include

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promotional skills, operational knowledge and product knowledge training, all of which seek to improve their sales and after-sales skills to better serve our customers.

We conduct periodic performance reviews for all of our employees and their salaries and bonuses are performance-based.

### **Employee Relations**

We believe we maintain a good working relationship with our personnel. We have not experienced any strikes or significant labor disputes which have materially affected our business, financial condition or results of operations during the Track Record Period.

Our employees (excluding temporary and part-time employees) are members of a trade union affiliated with the All China Federation of Trade Unions. As of the Latest Practicable Date, we have not experienced any major labor dispute or other labor disturbances that have interfered with our operations.

### **Employee Benefits**

In accordance with applicable PRC laws and regulations, we have made contributions to social security insurance funds (including pension plans, medical insurance, work-related injury insurance, unemployment insurance, and maternity insurance) and housing funds for our employees. We also provide medical care subsidies and emergency funds for our employees. As of the Latest Practicable Date, we have complied with all statutory social insurance and housing fund obligations applicable to us under PRC laws and regulations in all material aspects.

## **INSURANCE**

We currently maintain social welfare insurance in accordance with the relevant PRC laws and regulations, personal accident insurance for our employees and insurance that covers our major fixed assets against damage caused by accidents and natural disasters such as fires, earthquakes and floods. For the three years ended December 31, 2011 and the nine months ended September 30, 2012, our expenditures for insurance policy premiums were RMB4.6 million, RMB6.0 million, RMB8.8 million and RMB8.5 million, respectively.

We do not maintain any product liability insurance arising from the manufacture and sale of our products in the PRC. We also do not carry any business interruption insurance for losses or damage arising from accidents relating to our operations. Such insurances are not required under the PRC laws and regulations and we believe our practice in this regard is consistent with industry practices in the PRC. To minimize our product liability risk, we have instituted stringent quality control measures in order to avoid or reduce the incidence of product defects. See “— Quality Control” in this prospectus. Please also see “Risk Factors — Our insurance coverage may not be sufficient to cover the risks related to our operations or any losses” in this prospectus.

Our Directors believe that our current insurance policies provide sufficient coverage of the risks to which we may be exposed, relating to loss of or damage to our equipment, inventory and goods-in-transit and claims from our employees, and are comparable to other manufacturers in our industry in China whose business operations and size are similar to us. During the Track Record Period, we did not submit any material insurance claims.

## **LEGAL PROCEEDINGS AND COMPLIANCE**

During the Track Record Period, we were not involved in any litigation, arbitration or administrative proceeding that, individually or in the aggregate, could have had a material adverse

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## BUSINESS

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effect on our business, financial condition or results of operations, and as of the Latest Practicable Date, there was no existing or threatened litigation, arbitration or administrative proceeding against us or any of our Directors that, individually or in aggregate, could have a material adverse effect on our business, financial condition or results of operations.

Our Directors, as advised by our PRC legal adviser, Jingtian & Gongcheng, confirm that during the Track Record Period and, as of the Latest Practicable Date, our Group was in compliance with all relevant PRC laws and regulations in all material respects and had obtained all material permits and licenses required for the Group's operations in the PRC.

### **Internal Control**

We have adopted certain internal control measures to facilitate the effective operation of our business which includes (i) engaging Hong Kong legal adviser and compliance adviser to facilitate compliance with the relevant requirements under the Listing Rules after Listing; (ii) engaging PRC legal adviser to facilitate compliance with the relevant requirements under the PRC laws and regulations after Listing; (iii) our Hong Kong legal adviser, compliance adviser or other relevant professional parties will provide regular training to our Directors and senior management after Listing to provide, among others, updates to enhance their knowledge on corporate governance and Listing Rules requirements; and (iv) our audit committee which comprises all of our independent non-executive Directors will review the internal control systems and procedures for compliance with the relevant Listing Rules requirements on a regular basis and our audit committee will, upon due and careful inquiries, disclose its view regarding our compliance and internal control related matters in the Company's annual report after Listing.