OVERVIEW

The Group is the leading train-borne electrical system provider and integrator for the PRC Railway industry. The Group possesses comprehensive capabilities in research and development, design, manufacture, sales and customer service. The Group is also engaged in developing, manufacturing and selling train power converters, auxiliary power supply equipment and control systems for trains for urban rail systems, which is a focus of the Group's future business expansion. In addition, the Group designs, manufactures and sells electrical components for the PRC Railway industry, the urban rail industry and non-railway applications. The Group's electrical component products include power semiconductor devices, sensors and related products.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's total turnover was RMB658.8 million, RMB787.8 million, RMB998.0 million and RMB633.9 million and the Group's profit attributable to equity holders of the Company was RMB98.5 million, RMB162.7 million, RMB211.7 million and RMB153.3 million.

The Group's products are divided into two categories, namely, train-borne electrical systems and electrical components. The table below sets forth the main products in each category.

Products

Train-borne Electrical Systems

- Train power converters, auxiliary power supply equipment and control systems
- Train operation safety equipment
- Electrical control systems for large railway maintenance vehicles

Electrical Components

- Power semiconductor devices
- Sensors and related products
- Others (includes primarily PCBs and low inductance busbars for train-borne electrical systems and other applications)

As measured by the number of systems or components sold by the Group to PRC rail vehicle manufacturers divided by the total number of such systems or components procured by PRC rail vehicle manufacturers pursuant to the MOR's annual purchase plan in 2005, which was provided by the MOR's Research Institute of Science, Technology and Information, the Group's train power converters and electronic control systems represented approximately 40% and 69% market shares in the domestic new rail vehicle market (including locomotives and large railway maintenance vehicles, but not including rail vehicles for urban rail systems) in 2005, the Group's train operation safety equipment, electrical control system for large railway maintenance vehicles and power semiconductor devices represented approximately 63%, 100% and 51% market shares in the domestic new rail vehicle market, respectively, in 2005.

The Group's train-borne electrical systems are used in locomotives, passenger cars and trains for urban rail systems as the key equipment for power supply, controlling train operation and ensuring the safe operation of trains. The Group's train-borne electrical systems are also used in large railway maintenance vehicles. The Company is in the process of acquiring a 50% and 17% equity interest in Shiling and Siemens Zhuzhou, respectively. Shiling is principally engaged in the development and manufacture of electrical systems used for trains for urban rail systems. To the best of the Group's knowledge, Siemens Zhuzhou may focus on the development and manufacture of AC propulsion locomotives and related key equipment in the future. The Group's electrical components are primarily used as components in train-borne electrical systems used by both the PRC Railway industry and the urban rail industry. They are also used in non-railway applications such as power transmission, metal processing, mining and chemical engineering. The Group has been designated by General Electric Company to supply all its requirements for four types of power semiconductors from 2006 to 2008.

The following table sets forth the amount and percentage of the Group's turnover derived from each of the Group's two principal categories of products for the periods indicated:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
							(unaudited)			
	Turnover (RMB millions)	*% of Total Turnover*	*Turnover (RMB millions)*	*% of Total Turnover*	*Turnover (RMB millions)*	*% of Total Turnover*	*Turnover (RMB millions)*	*% of Total Turnover*	*Turnover (RMB millions)*	*% of Total Turnover*
Train-borne electrical systems	495.6	75.2%	607.2	77.1%	781.0	78.3%	438.6	81.0%	529.0	83.5%
Electrical components	163.2	24.8%	180.6	22.9%	217.0	21.7%	102.8	19.0%	104.9	16.5%
Total	658.8	100.0%	787.8	100.0%	998.0	100.0%	541.4	100.0%	633.9	100.0%

The Group's key customers are the MOR and its local railway administrations, rail vehicle manufacturers and urban rail operators in the PRC. The Group supplies its train-borne electrical systems to rail vehicle manufacturers and urban rail operators to be installed on new rail vehicles for the PRC Railways and the urban rail systems and to the MOR's local railway administrations and urban rail operators for repair and replacement applications. For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's sales to its top five customers accounted for approximately 49.9%, 41.9%, 35.7% and 45.9%, respectively, of the Group's total turnover. All the top five customers were rail vehicle manufacturers and local railway administrations or agents of either of them except for two for the year ended 31 December 2003, which were associated with the Parent Company and are now part of the Group after the Reorganisation. Sales to those two customers accounted for 11.0% of the Group's total turnover for the year ended 31 December 2003. During the same periods, approximately 7.8%, 7.2%, 4.8% and 3.4% of the Group's total annual turnover was derived from the Group's direct export sales. The Group exports its train-borne electrical systems primarily to Hong Kong and certain other countries in Asia, and exports its electrical components primarily to the US and Europe.

COMPETITIVE STRENGTHS

The Directors believe that the Group's historical success and potential future growth are primarily attributable to the following competitive strengths.

Leading position in train-borne electrical system technology in the PRC

The Group is the leading train-borne electrical system provider and integrator in the PRC. The Group and the Parent Company have been in the train-borne electrical system business for more than 40 years. The Group possesses core technologies in a wide range of train-borne electrical system products, including train power converters, auxiliary power supply equipment and control systems, train operation safety equipment and electrical control systems for large railway maintenance vehicles. The Group's mature DC train power converter and control technologies have been developed during its long-term co-operation with domestic locomotive works. Most of the PRC's domestically manufactured locomotives have been developed and manufactured under the joint efforts of the Group and various domestic locomotive works. The Group has also developed and manufactured technologically advanced AC train-borne electrical systems such as those installed on the China Star EMU, which has recorded a speed of 321.5 km/h, the highest measured speed in PRC railway history. The Group intends to expand its co-operation with domestic rail vehicle manufacturers to enter into commercial production of EMUs in the future. The Directors believe that the Group's core technologies, combined with its research and development capability, will enable the Group to maintain its leading market position in the PRC Railway industry and to explore opportunities in other markets.

As part of its strategy to achieve "leap-forward" development, the MOR started to acquire 200 km/h EMUs and related technologies from leading foreign rail transportation equipment suppliers in late 2004. The acquired technologies were further transferred by the MOR to various domestic manufacturers before the Company was incorporated, and the Parent Company was one of the transferees of train power converter and control technologies. The Parent Company was also designated to supply train-borne electrical systems. Since the Company was incorporated, the Company has been implementing the 200 km/h EMU project for the Parent Company as it possesses the technology, personnel and equipment relating to the research and development and manufacture of train power converters and control systems. The Company has benefited from the manufacture of train power converters, auxiliary power supply equipment and control systems for the 200 km/h EMU project. The Company and the Parent Company are in the process of procuring relevant contract parties to agree in writing to the assignment of the rights and obligations of the Parent Company under the relevant technology transfer agreement and supply agreement to the Company. In addition, the Parent Company is party to a supply agreement and a technology transfer agreement with CSEE Transport to develop an ATP system. The Company has also been implementing the ATP project for the Parent Company and has benefited from implementing the ATP project. The Company and the Parent Company are in the process of procuring CSEE Transport to agree in writing to the assignment of the rights and obligations of the Parent Company in relation to the supply agreement and the technology transfer agreements to

the Company. However, the Company may be exposed to certain risks if the consents to such assignments are not obtained. See "Risk Factors — Risks relating to the Group — The Group may be subject to intellectual property right disputes if the relevant agreements in relation to the 200 km/h and ATP projects cannot be assigned from the Parent Company to the Company".

The Group has also benefited from certain industry-related regulations in maintaining its leading position in terms of both technology and market share. The PRC Railway industry is highly regulated by the MOR, which mandates stringent manufacturer certification and qualification, and product testing, certification and approval processes. The Directors believe that those regulations create relatively high entry barriers for new entrants in the PRC train-borne electrical systems business.

Close relationships with key customers and brand recognition

The MOR and its local railway administrations are key end-users of the Group's products. The Directors believe that the Group has been the primary supplier of train-borne electrical systems to the MOR and its local railway administrations since the establishment of the Parent Company. Moreover, the Group has formed close and stable relationships with domestic locomotive works through long-term co-operation in product development and joint efforts in selling products and providing customer service to common end-users — the MOR and its local railway administrations.

The Group also has well-established relationships with urban rail customers such as MTR Corporation Limited and with non-railway customers such as General Electric Company. The Group was accredited by Guangzhou Metro Corporation as an outstanding supplier in 2003. As a supplier of SIV systems since 2002, the Company was granted a Partnering Award for E&M Works Project (機電工程項目伙伴合作獎) by the MTR Corporation Limited in September 2004. The Group has supplied power semiconductor devices, sensors and other products to General Electric Company since 1999 and became one of General Electric Company's strategic suppliers in 2005. The Company has also been acknowledged by General Electric Company as one of its best partners world-wide.

Due to the Group's solid relationships with its key customers, leading position in train-borne electrical system technologies and quality products and services, the "TEG" brand is well-known among the MOR and its local railway administrations and domestic rail vehicle manufacturers. The Directors believe that the long-established reputation of the "TEG" brand in the PRC Railway industry is also instrumental in its expansion in the PRC urban rail market.

Strong research and development capabilities

The Group has strong research and development capabilities in conducting basic research, developing new products, improving manufacturing processes and commercialising new technologies. The Group has, through the Reorganisation, obtained from the Parent Company its

technology platforms, testing systems, technical personnel, knowledge, know-how, expertise and experience relating to train-borne electrical system and electrical component technologies and products. The Group owns a number of advanced technology platforms including AC train power converter and control technology and train-borne electrical system simulation technology.

As at July 2006, the Group employed 700 persons engaged in research, development and testing, among whom 80 persons held master's degrees or above, 85 persons were senior engineers and 14 persons received special government allowances in recognition of their contributions to the enterprises and the State in amounts ranging from RMB600 to RMB10,000 a year. Certain technical personnel of the Group are actively involved in drafting PRC national industrial standards in train power converters and control systems for locomotives used on the PRC Railways and IEC/TC9 international railway industrial standards. The Company was accredited as a PRC nationally-recognised software enterprise (認可軟件企業) by the Information Industry Department of Hunan Province in December 2005, and ranked 40th among the top 100 PRC software enterprises accredited by the Ministry of Information Industry of the PRC. For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's research and development expenses inclusive of related staff cost, depreciation and amortisation relating to research and development activities amounted to RMB57.8 million, RMB57.7 million, RMB52.4 million and RMB43.3 million, accounting for 8.8%, 7.3%, 5.3% and 6.8% of the Group's total turnover, respectively.

The Group has adopted a comprehensive set of testing systems comprising various tests. The tests include, among others, system tests, simulation tests and EMC tests. Pursuant to an equipment leasing agreement between the Company and the Parent Company, the Company has obtained the right to manage and use certain advanced laboratories and testing equipment owned by the Parent Group.

The Group has established technological co-operative relationships with a number of domestic and overseas research institutes and manufacturers of train-borne electrical systems and electrical components, including primarily JETS AS, a Norwegian sanitary system manufacturer. The Group's collaborative efforts with these manufacturers and institutes have not only elevated the Group's technology platforms, but have also enabled the Group to keep abreast of the latest technology developments and trends in the industry world-wide.

Strong capabilities in commercialising proprietary core technologies

The Group has grown rapidly through successful commercialisation of its core technologies. The Group's train power converter and control technologies have been widely used in domestic locomotives, including the Shaoshan SS series, the Dongfeng DF series and the China Star EMU. The Group's AC train power converters and control systems were installed on the three locomotives that were exported to Kazakhstan in 2004, which was the first time that PRC-made AC locomotives were exported.

The Group has also made significant progress in commercialising its proprietary core technologies in the urban rail market and non-railway markets, such as power transmission and metal processing. During the Track Record Period, the Group supplied SIVs to the MTR Corporation Limited, and jointly with Mitsubishi Electric Corporation, won the bids to supply train-borne electrical systems to Tianjin Metro Line One and Beijing Metro Line Two. The Group has received an order for a prototype maglev train power converter and control system in early 2006. The Group has also applied its sensor technology in manufacturing automatic sensing sanitary devices and vacuum sanitary units. Expanding the applications of and commercialising the Group's core technologies has greatly enhanced the commercial value of its proprietary core technologies.

An integrated supplier with a broad offering of customised products and an extensive service network

The Group's customers span broad geographic regions and have varying and changing needs for the Group's products. The Group possesses comprehensive capabilities in research and development, design and manufacture and such capabilities have enabled the Group to provide a wide range of customised system products to its customers. The fact that the Group also manufactures major components such as power semiconductors, sensors and PCBs further enhances the Group's ability to design and manufacture customised products and deliver them in a timely manner.

The Group has an established a service network covering all provinces and autonomous regions of China. The service network is maintained by a service team staffed with 188 full time employees. The technical and maintenance personnel of the service team is committed to arriving at any customer site in the PRC within eight hours of a customer's request to provide required services.

Being an integrated supplier with a broad offering of customised products and an extensive service network, the Group is better positioned to meet its customers' preferences for sourcing specific products, services, replacement parts and components from a single supplier.

Experienced and dedicated management team

The Group's management team possesses extensive management experience and in-depth knowledge and understanding of the rail vehicle manufacturing industry in the PRC. Most of the Group's senior management members have worked in the rail vehicle manufacturing industry for more than a decade and many of them are experts in the Group's core technologies. Moreover, the compensation packages of the members of the Group's management team are based on performance indicators for each individual set by the Company, thereby aligning the interests of the management team with those of the Company's shareholders.

BUSINESS STRATEGIES

The Group's objectives are to reinforce its leading position in the PRC train-borne electrical system market in terms of both technology and market share and to become an internationally known train-borne electrical system provider and integrator. The Group intends to achieve such objectives by pursuing the following strategies:

To continue to focus on technology development

The MOR's policy is to increase the speed of passenger trains and the hauling capacity of freight trains, as well as to upgrade the safety and comfort levels of trains. The Group aims to reinforce its leading position in train-borne electrical system technologies with a focus on the areas identified by the MOR. To that end, the Group will:

- develop train power converter and control technologies relating to 300 km/h EMUs, six-axle 9.6 MW freight locomotives and synchronised control of multiple trains;

- upgrade its existing research and development facilities, establish a comprehensive experiment and test system, and set up a research and development centre in each of Shanghai and Beijing. The Board of Directors approved of the establishment of a wholly-owned subsidiary in Beijing, which will primarily focus on developing and commercialising new train operation safety equipment and railway information network projects;

- form strategic alliances or joint ventures with leading foreign manufacturers that possess more advanced technologies. The Group will continue to co-operate with CSEE Transport to develop an ATP system. The Group will own a 50% and a 17% equity interest in each of two joint ventures, namely Shiling and Siemens Zhuzhou, respectively, when the interest transfers (including all necessary consents and approvals) from the Parent Company are completed. Shiling focuses on developing and manufacturing electrical systems used in trains for urban rail systems. To the best of the Group's knowledge, Siemens Zhuzhou may focus on developing and manufacturing AC propulsion locomotives and related key equipment in the future;

- continue to establish technological co-operative relationships with domestic and overseas research institutes and manufacturers of train-borne electrical systems and electrical components; and

- make continuous efforts and investments in technical staff training, including offering specialised training programmes for employees in each department.

The Directors believe that the above efforts will help the Group better capture emerging opportunities in the PRC domestic market.

To increase product and service variety

The expansion of the Group's market share depends to a significant extent on its ability to provide a broad variety of customised products and services. The Group has increased and intends to further increase its product variety through commercialisation of its technologies. The ongoing efforts in this respect include the commercialisation of 200 km/h EMU and eight-axle 9.6 MW heavy-hauling locomotive technologies. The Group will also capitalise on its extensive service network and strong capabilities in research and development, design and manufacturing. Customised product and service capabilities will strengthen the Group's position against competitors that do not have the breadth and depth of the Group's products.

To capitalise on the Group's technologies to further expand into the urban rail market and non-railway markets

The Group's proprietary technologies can be applied in the urban rail market and for non-railway uses. The Directors believe that the commercial potential of such applications is substantial. The urban rail market is one of the Group's focus areas for future business growth. The Group has already made significant progress in marketing and selling its train-borne electrical systems to the urban rail market. See "Business — Competitive Strengths — Strong capabilities in commercialising proprietary core technologies". The Group plans to achieve further expansion through offering customised products and services and forming strategic alliances with foreign partners. The electrical components the Group manufactures have been applied to non-railway uses such as power transmission and metal processing. The Group will continue to explore other non-railway applications for its products through capitalising on its core technologies and strong capabilities in research and development.

To increase production capacity

The Group plans to increase its production capacity by streamlining existing production facilities and building new production lines for both system and component products. The Group plans to invest RMB800 million in increasing production capacity (including expanding existing production facilities, building new production facilities and procuring production equipment). The Group has built a new power semiconductor device production line, which commenced operation in November 2006 and has increased the Group's annual production capacity of power semiconductor devices from 150,000 pieces to 350,000 pieces. The Group is also in the process of renovating its existing production line, which will pave the way for building a platform for production of higher technology products such as larger size semiconductor devices.

To continue to expand sales and service network

The Group will continue to expand its domestic sales network to strengthen its leading position in the PRC Railway industry and to increase its market share in the PRC Railway, the urban rail and non-railway markets. The Group currently has customer service offices that cover all provinces and autonomous regions in China. The Group intends to strengthen the role of those offices by staffing sales personnel. Moreover, the Group will establish more sales and customer service offices close to the MOR's local railway administrations to better service its customers and capture emerging business opportunities.

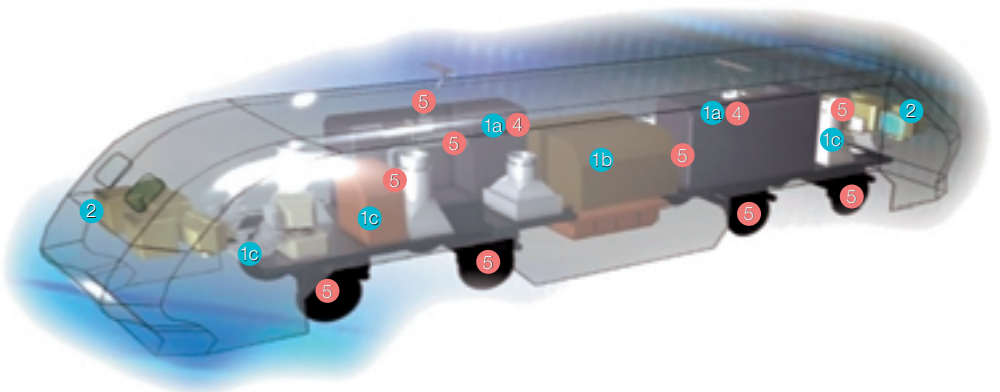
In addition to its sales network within the PRC, the Directors believe that expansion into overseas markets represents a significant opportunity for the Group's future growth. The Group's strategy for the overseas market is to export electrical components primarily to North America and the European Union and to export train-borne electrical systems primarily to other countries and regions in Asia. The Group also plans to raise its profile in overseas markets through strategic alliances with and direct sales to overseas locomotive manufacturers which have a strong presence in their local markets. The Group has established a subsidiary company in the US to explore the North American market and promote the Group's products.

To continue to upgrade management systems to achieve operational excellence and management efficiency

The Company's manufacturing centre adopted Manufacturing Resource Planning (MRP II) in December 2003 to control and monitor demand for and plan ahead the procurement of materials and components, to ensure timely delivery of products, and to minimise inventory. The Directors believe that the implementation of the MRP II system enables the Group to effectively control its costs and improve its profitability, and thus increase its competitiveness. In order to achieve better resource planning and control in research, development, manufacturing, sales and after-sales service, the Group intends to adopt an ERP system in January 2007. Times Electronics implemented the ERP system in June 2006.

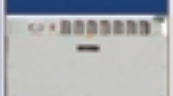
PRODUCTS

The Group supplies a wide range of train-borne electrical systems including train power converters, auxiliary power supply equipment and control systems, train operation safety equipment and electrical control systems for large railway maintenance vehicles. The Group also produces electrical components including power semiconductor devices, sensors and related products and other products to satisfy its own raw material requirements and to sell to third parties. The diagram below illustrates the Group's train-borne electrical system products and their applications.



Train-borne Electrical Systems

Electrical Components

1a Train power converters	1b Auxiliary power supply equipment	1c Control systems	2 Train operation safety equipment	3 Electrical control systems for large railway maintenance vehicles	4 Power semiconductor devices	5 Sensors and related products
						
Function: ■ Providing and controlling power supply to motors	Function: ■ Providing and controlling electric power supply to other train-borne electrical systems on-board equipment including air conditioners, ventilation systems, lighting	Function: ■ Controlling train operation, recording train operation data, communicating between control systems and protecting electrical equipment	Function: ■ Ensuring train operation safety by preventing over speeding and collision of trains ■ Recording the operator's identity and his operating instructions	Function: ■ Controlling the operation of large railway maintenance vehicles ■ Recording the maintenance vehicle operation data ■ Protecting electrical equipment	Function: ■ Primarily used as high-voltage high-current high-speed switches and current control components ■ Major components of the Group's train power converters, auxiliary power supply equipment and control systems	Function: ■ Detecting data relating to speed, temperature, voltage, currents and displacement, and transfering such data to the control systems of the trains

Train power converters, auxiliary power supply equipment and control systems

Train power converters, auxiliary power supply equipment and control systems are critical to the operation of trains. The Group's main train power converters, auxiliary power supply equipment and control systems products and their functions are set forth below:

Products	Functions
• Train power converters	• Providing and controlling power supply to motors
• Auxiliary power supply equipment	• Providing and controlling electric power supply to on-board equipment including air conditioners, ventilation systems, lighting and train-borne electrical systems
• Control systems	• Controlling train operation, recording train operation data, communicating between control systems and protecting electrical equipment
• Others	• Components and plug-ins for train power converters, auxiliary power supply equipment and control systems.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's turnover from the sales of train power converters, auxiliary power supply equipment and control systems was RMB377.5 million, RMB371.8 million, RMB359.6 million and RMB265.6 million, respectively, representing approximately 57.3%, 47.2%, 36.1% and 41.9% of the Group's total turnover for the same periods. As part of the its train power converter business, the Group also purchases motors and sells them to its customers as a package with train power converters for various contracts. The turnover from sales of motors was included in the turnover from the sales of train power converters, auxiliary power supply equipment and control systems during the Track Record Period, and was RMB18.2 million, RMB47.5 million, RMB48.2 million and RMB13.6 million for the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006.

The Group has benefited, and the Directors believe that it will continue to benefit, from its leading position in the PRC Railway market for AC and DC train power converter and control technology as well as the commercial application of the same in other markets, especially in the urban rail market.

Train power converters include both DC and AC train power converters. DC train power converters are installed on locomotives to provide and control power supply to DC motors; AC train power converters are installed on locomotives or EMUs to provide and control power supply to AC motors. Different technical requirements for DC and AC train power converters are primarily reflected in their designs, and there are no major differences in terms of production processes and time or raw materials sourcing.

Most locomotives in service in the PRC are equipped with DC train power converter and control systems. As at the end of 2004, almost all of the DC propulsion locomotives operating in the PRC were developed and manufactured by the PRC locomotive works. As at the end of 2004, most of the PRC-made DC propulsion locomotives were equipped with train power converters and control systems supplied by the Group. The Group's control systems were also installed on the trains operating on the Qinghai-Tibet railway.

The Parent Company started the research, development and sale of AC train power converters and control systems with its own proprietary technology in the 1990s. The Parent Company and the Group have made the following major achievements:

- In 1996, the Parent Company and ZELW jointly developed and manufactured the PRC's first AC propulsion locomotive, the AC4000 type locomotive;

- In 2002, the Parent Company and rail vehicle manufacturers including ZELW, jointly developed and manufactured China Star EMU;

- In 2002, the Parent Company applied its AC train power converter and control technology to auxiliary power supply systems for trains for urban rail systems and was granted a contract from MTR Corporation Limited to supply SIVs with contract value of approximately HK$64.5 million;

- In 2004, the Parent Company developed and manufactured train power converters and control systems for the three AC propulsion locomotives that were exported to Kazakhstan, which was the first time that PRC-made AC propulsion locomotives were exported;

- In 2005, the Parent Company entered into a contract to provide train power converters and control systems to CSR Sifang Locomotive and Rolling Stock Co., Ltd. to be installed on the trains for urban rail systems in Guangzhou with contract value of approximately RMB55.6 million;

- In 2005, the Parent Company, along with three other parties, entered into a contract to supply train power converters and control systems to CSR Sifang Locomotive and Rolling Stock Co., Ltd. and another company to be installed on 200 km/h EMUs, with an approximately RMB460 million contract value attributable to the Parent Company;

- In 2006, the Group, together with Mitsubishi Electric Corporation, won a bid to supply to Beijing Metro Line Two a total of 144 sets of train power converters and control systems for trains for urban rail systems with a RMB66 million contract value attributable to the Group; and

- In November 2006, the Company signed a contract with CSR Sifang Locomotive and Rolling Stock Co., Ltd. to supply electrical systems to be installed on 300 km/h EMUs, with an approximately RMB1,030 million contract value attributable to the Group.

As a tribute to the Group's achievements in applying AC train power converter and control technology to trains for railway systems, the MOST awarded the Group a "State Science and Technology Progress Award (second class)" in 2005.

Train operation safety equipment

Train operation safety equipment plays a major role in ensuring train operation safety by preventing overspeeding and collision of trains and recording operator's identity and his operating instructions. The Group's train operation safety equipment includes primarily LKJ-93 type and LKJ2000 type. The Group's LKJ2000 type train operation safety equipment has been installed on the trains operating on the Qinghai-Tibet railway.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's turnover from sales of train operation safety equipment was RMB118.1 million, RMB190.9 million, RMB272.5 million and RMB179.9 million, respectively, representing approximately 17.9%, 24.3%, 27.3% and 28.4% of the Group's total turnover for the same periods.

Based on the Group's knowledge and experience in the business, the Directors believe that all train operation safety equipment used on the trains operating in the PRC was manufactured by the Group and Henan Siwei Automation Equipment Co., Ltd. (河南思維自動化設備有限公司).

In order to ensure the highest level of train operation safety, it is critical that train operation safety equipment is upgraded to be commensurate with train speeds common to the PRC Railway network. The MOR requires that all types of train operation safety equipment be replaced every six to eight years. In late 2005, the MOR required the train operation safety equipment of all trains operating in the PRC be upgraded by substitution of the LKJ-93 type and older types with the LKJ2000 type before the completion of the sixth speed increase of the PRC Railway network. The Directors believe that such requirement will benefit the Group and result in continuous orders for train operation safety equipment. For example, in 2006, the Company entered into a contract with the MOR's Shenyang local railway administration to supply LKJ2000 type train operation safety equipment with contract value of approximately RMB74.8 million.

Electrical control systems for large railway maintenance vehicles

The Group manufactures electrical control systems for large railway maintenance vehicles including tamping vehicles, ballast cleaning machines and track stabilisers. As at 31 December 2005, Kunming China Railway was the only manufacturer of large railway maintenance vehicles in the PRC. The Group is the exclusive supplier in the PRC to Kunming China Railway of electrical control systems for large railway maintenance vehicles in the PRC in addition to being a supplier to the MOR's local railway administrations. The Parent Company, Kunming China Railway (as the leader), and three other entities entered into Articles of Consortium to Develop Large Railway Maintenance Vehicles, pursuant to which (i) all parties will participate in bidding as a consortium and jointly decide product sales prices, and (ii) all other entities will enter into subcontracts with

Kunming China Railway. Kunming China Railway subcontracts the supply of electrical control systems for large railway maintenance vehicles to the Parent Company. The Group has supplied electrical control systems for large railway maintenance vehicles to Kunming China Railway in the past.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's turnover from sales of electrical control systems for large railway maintenance vehicles was nil, RMB44.5 million, RMB148.9 million and RMB83.5 million, respectively, representing 0%, 5.6%, 14.9% and 13.2% of the Group's total turnover for the same periods.

The Directors believe that market demand for large railway maintenance vehicles will continue to grow due to the following reasons:

- The speed increases of the PRC Railway network require higher quality track, which in turn demands more frequent maintenance;

- As substantial investment has been and will be made on PRC Railway infrastructure construction, the aggregate length of the PRC Railways is bound to increase, which would entail a corresponding increase in demand for large railway maintenance vehicles.

Power semiconductor devices

The power semiconductor devices the Group manufactures are primarily used as high-voltage high-current high-speed switches and current control components. They are major components of the Group's train power converters and auxiliary power supply equipment and are applied in other areas such as power transmission, metal processing, mining and chemical engineering.

The Group is one of the few manufacturers with over 40 years' history of research, development and manufacturing of power semiconductor devices in the PRC. The Group's power semiconductor devices are sold in the PRC and exported to the US, Europe and Asia. In particular, the Group has been designated by General Electric Company to supply all its requirements for four types of power semiconductors from 2006 to 2008.

In 2004, the Group launched production of five inch thyristors which are used primarily in high voltage AC power transmission. In 2003, the Group became the first manufacturer in the PRC to develop and manufacture GTO devices using its own proprietary technology.

For the three years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2006, the Group's turnover from external sales of power semiconductor devices was RMB70.0 million, RMB79.1 million, RMB90.1 million and RMB49.5 million, respectively, representing approximately 10.6%, 10.0%, 9.0% and 7.7% of the Group's total turnover for the same periods.

Sensors

The sensors the Group manufactures are important components used in the production of the Group's train-borne electrical systems. The sensors are used to detect data relating to speed, temperature, voltage, currents and displacement, and to transfer such data to the control systems of the trains. The Group's sensor products are also used in other industry sectors such as transportation, power transmission and metal processing. The Group has also extended the application of its sensor products to various other areas, such as vacuum sanitary units installed on trains and automatic sanitary units used in hotels, luxury properties and public toilets.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's turnover from external sales of sensors and related products was RMB56.5 million, RMB61.5 million, RMB57.0 million and RMB29.6 million, respectively, representing approximately 8.6%, 7.8%, 5.7% and 4.7% of the Group's total turnover for the same periods.

Other products

The Group's other products include primarily PCBs and low inductance busbars for train-borne electrical systems and other applications.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's turnover from external sales of other products was RMB36.7 million, RMB40.0 million, RMB69.9 million and RMB25.8 million, respectively, representing approximately 5.6%, 5.1%, 7.0% and 4.1% of the Group's total turnover for the same periods.

PRODUCTION FACILITIES AND PROCESSES

The Group's products are manufactured in the Group's five manufacturing sites, namely the manufacturing center, Times Electronics, the power electronics business unit, Ningbo Company and the PCB business unit. The table below sets forth certain information of the manufacturing facility for each product category.

Products	Manufacturing site	Location	Gross floor area (sq.m.)
Train-borne electrical systems			
Train power converters, auxiliary power supply equipment and control systems	Manufacturing Center	Shidai Road, Shifeng District, Zhuzhou City	28,133
	Times Electronics	High and New Technology Zone, Tianyuan, Zhuzhou	12,719
Train operation safety equipment	Manufacturing Center		
Electrical control systems for large railway maintenance vehicles	Times Electronics		
Electrical components			
Power semiconductor devices	Power Electronics Business Unit	Beimen, Tianxin, Zhuzhou City	15,215
Sensors and related products	Ningbo Company	No.8 Huancheng Road North, Western section, Ningbo City	7,112(1)
Others	PCB Business Unit	Shidai Road, Shifeng District, Zhuzhou City	7,025

Note:

(1) Ningbo Company has purchased 30,851 sq.m. of land to construct a new manufacturing facility, the construction of which is expected to start in 2007.

The table below sets forth the annual production capacity, actual production volume, utilisation rate of production capacity (calculated by dividing actual production volume by annual production capacity) and sales volume of each product category in 2005.

Products	Annual production capacity	Actual production volume	Utilisation rate of production capacity	Sales volume
Train-borne electrical systems				
Train power converters, auxiliary power supply equipment and control systems	850 converters, 1,600 sets of control and communication systems	672 converters, 1,016 sets of control and communication systems	converters: 78%, control and communication systems: 64%	672 converters, 673 sets of control and communication systems
Train operation safety equipment	3,000 sets	3,576 sets	119%	2,373 sets
Electrical control systems for large railway maintenance vehicles	100 sets	79 sets	79%	79 sets
Electrical components				
Power semiconductor devices	150,000 pieces(1)	187,260 pieces	125%	187,873 pieces
Sensors and related products	80,000 pieces of sensors, 40,000 sets of automatic sensing sanitary devices, 100 sets of on-board train vacuum sanitary units	66,581 pieces of sensors, 35,984 sets of automatic sensing sanitary devices, 30 sets of on-board train vacuum sanitary units	sensors: 83%, automatic sensing sanitary devices: 90%, on-board train vacuum sanitary units: 30%	57,805 pieces of sensors
Others	80,000 square metres of PCBs	55,964.53 square meters of PCBs	70%	48,470 square meters of PCBs

Note:

(1) The Group built a new production line in 2006 and is also in the process of renovating the existing production line. The Group expects to invest RMB10 million with cash generated from operations in renovating the existing production line. The new production line commenced operation in November 2006 and the renovation of the existing production line is expected to be completed in 2007. With the new production line in operation, the Group's annual production capacity of power semiconductor devices has increased from 150,000 pieces to 350,000 pieces.

The Group owns a comprehensive set of equipment for manufacturing train-borne electrical systems and electrical components. The following table summarises the key manufacturing equipment and manufacturing processes for the Group's train-borne electrical systems and electrical components.

Products	Key manufacturing equipment	Manufacturing processes
Train-borne electrical systems		
Train power converters, auxiliary power supply equipment and control systems, train operation safety equipment	SMT production lines, numeric control machining equipment, automatic water cleaners, cyclic temperature test chambers, function test equipment, comprehensive system test benches	Sheet-metal parts manufacture, PCB assembly, final assembly and testing
Electrical control systems for large railway maintenance vehicles	Peak-wave soldering machines, cyclic temperature test chambers, comprehensive system test benches developed by the Group	PCB assembly, final assembly and testing
Electrical components		
Power semiconductor devices	Two cleaning workshops (up to 100 particles per cubic metre for key processing section), long temperature zone and high accuracy diffusion ovens, high vacuum electronic beam evaporators, double-side photoengraving machines and double-side lapping machines, comprehensive test benches, AC/DC high-temperature blocking test benches	Diffusion, photoengraving, lapping, sintering, evaporation, electronic inradiation, intermediate examination and testing, packaging, final examination and testing
Sensors and related products	Four production lines developed by the Group, two for sensor production, one for automatic sensing sanitary device production and one for vacuum sanitary unit production	Assembly, wiring and testing

RESEARCH AND DEVELOPMENT

The Directors believe that the Group's strong research and development capability is one of the Group's key competitive strengths. The Group places great focus on research and development with a view to maintaining its leading position in train-borne electrical system technology and increasing its product variety and applications.

The Group's research and development is conducted by the technology centre and the research and development departments in each business unit, with the former focusing on technologies relating to train power converters and control systems and providing a platform for the Group's research and development activities, and the latter focusing on application technologies for the specific business unit.

The Group has also established technological co-operative relationships with domestic and overseas research institutes and manufacturers, including primarily JETS AS. Ningbo Company and JETS AS, a Norwegian sanitary system manufacturer independent from the Group, entered into an industrial research and development contract on 23 September 2005 (witnessed by Innovation Norway, a Norwegian state-owned company) to develop closed toilet and sewage systems for trains, railroad stations and similar public areas/buildings in China. According to the contract, the above mentioned project was to be concluded by the end of 2008 and the maximum total cost of the project is NOK20 million (equivalent to approximately RMB25.5 million), with Ningbo Company, JETS AS and Innovation Norway (by grant) each contributing NOK6.5 million, NOK7.0 million and NOK6.5 million. Both Ningbo Company and JETS AS have assigned personnel to work on the project. Pursuant to the contract, JETS AS takes over the right to own, or the right to utilise in the future, any results, methods and similar in so far as they were produced under the contract. JET AS also has the right to sell the product to a third party. Ningbo Company obtains full ownership to prototypes resulting from the project and also reserves the right to use and dispose of further results of the project to cover its own needs. Ningbo Company and JETS AS have co-operated under the contract on a series of basic research and experiments relating to, among other things, products' adaptation to environment and influence on environment. As at the Latest Practicable Date, the Group has spent approximately RMB1 million on the project.

The Group's research and development expenses inclusive of related staff cost, depreciation and amortisation in the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006 were RMB57.8 million, RMB57.7 million, RMB52.4 million and RMB43.3 million, respectively, representing approximately 8.8%, 7.3%, 5.3% and 6.8% of the Group's total turnover for the same periods. The Group adjusts the focus of its research and development expenses from time to time according to changes in market demand and government policies so as to maintain the Group's leading position in the market.

Due to the Group's strength in its research and development work, the Group's products have been awarded numerous prizes by the MOST, the MOR and the China Railway Society (中國鐵道協會). The table below sets out certain recent major prizes:

Award	Name of Project	The Group's products involved
State science and technology progress award (second class), awarded by the MOST (2005)	AC train power converter and control system and its high performance control technology	Train power converters and control systems
First prize of science and technology progress awarded by China Railway Society (2005)	CD08-475 continuous tamping machine	Electrical control systems for large railway maintenance vehicles
First prize of science and technology progress awarded by China Railway Society (2004)	AC drive microprocessor control system and its modulisation	Control systems
Second prize of science and technology progress awarded by China Railway Society (2002)	DC600V power supply system for passenger trains	Power supply
Excellent scientific and technological progress award for state's key projects in the ninth five year plan awarded jointly by the MOST, the MOF, the State Development Planning Commission and the State Economic and Trade Commission (2001)	200 km/h power-centralised electric passenger trainset	Train power converters and control systems

The Group will continue to devote substantial human and financial resources to research and development. In particular, the Group will focus on developing technologies that can meet the requirements of high speed passenger transportation and heavy hauling freight transportation and are also energy efficient and environmentally friendly, such as high-voltage AC train power converter and control technologies for trains for the PRC Railways and urban rail systems and low speed and medium speed maglev trains. The Group intends to implement the following major research and development projects in the period from 2006 to 2010:

- Train power converters and control systems: The Group is going to study and master advanced train power converter and control technology through participating in the MOR-sponsored high-speed EMU localisation project. The Group has developed a prototype control system platform composed of various modules that can be used in control systems for AC propulsion locomotives, diesel locomotives, passenger cars, EMUs and trains for urban rail systems. The Group has also developed a prototype 32-bit microprocessor control system to replace the 16-bit microprocessor control

systems that are currently used in the PRC Railway industry. The Group hopes to further upgrade those control system platforms after future test runs and achieve commercialisation of both technologies within the next few years.

- Train operation safety equipment: The Group is co-operating with CSEE Transport in developing ATP technologies for high-speed trains. The Group is also co-operating with a domestic company to develop the LKJ05 train operation safety equipment to replace the currently used LKJ2000 train operation safety equipment as the primary train operation safety equipment in the PRC Railway industry.

- Electrical control systems for large railway maintenance vehicles: The Group is developing a control system platform for large railway maintenance vehicles to upgrade the existing systems and to be installed in newly manufactured large railway maintenance vehicles.

- Electrical components: The Group will continue to upgrade and commercialise its technologies relating to electrical components.

The Parent Company has been designated by the MOR to take a lead in setting technical standards for train power converters and control systems. See "Industry Overview — Rail Vehicle Manufacturing Industry in the PRC — Related PRC Regulatory Environment". As the management of the Company concluded that such designation is not material to the Group's production, sales or marketing, the designation has not been transferred to the Group. However, the Group intends to make an application to the MOR to change the designee from the Parent Company to the Company when the MOR issues a new designation list, the timing of which cannot be predicted at this time.

RAW MATERIALS

The raw materials generally used by the Group to produce its products are metal parts and a wide variety of electrical components. The Group's demands for power semiconductor devices, sensors and PCBs are met principally by internal supply. The Group generally procures each type of raw material or component from at least two suppliers to avoid disruption of supply and manage fluctuation in raw material price. In addition, the Group enters into long-term procurement contracts with certain suppliers at fixed prices to reduce the effects of raw material price fluctuation. The Group's raw material procurement policy is to (i) use only vendors that have demonstrated quality control and reliability, and (ii) procure key components from well known suppliers.

The price of raw materials is generally determined by negotiation or bidding process. The Group determines the price of raw materials through a bidding process when the estimated contract value is above a certain amount or when price benchmarks are not available. Most raw materials purchased by the Group are settled by telegraphic transfers and banker's acceptance drafts. Trade settlements with overseas suppliers are usually by telegraphic transfers or letters of

credit. Suppliers located in the PRC generally give the Group a credit term of 90 days. The manufacturing center has adopted a MRP II system and electronic business system in its procurement of raw materials. The Group generally maintains not more than 60 days' supply of key raw materials.

The top five suppliers of raw materials and components for the Group together accounted for less than 30% of the Group's total purchases of raw materials and components for the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006.

The top five largest suppliers of raw materials and components to the Group have at least three years of business relationships with the Group. The Group has not experienced any major problem in obtaining adequate supply of raw materials and components during the Track Record Period. The Directors believe that due to its close and long-term working relationships with its suppliers, the Group should continue to be able to source a significant proportion of its raw material requirements from these suppliers.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's aggregate purchases from state-owned enterprises which were among the Group's top five suppliers were approximately RMB28.2 million, RMB48.5 million, RMB98.8 million and RMB86.2 million, respectively, accounting for 6.2%, 10.4%, 17.6% and 23.1% of the Group's purchases.

SALES, MARKETING AND CUSTOMER SERVICE

The Group had in total 315 full-time employees involved in sales and marketing of the Group's products and customer service as at July 2006.

Sales

The sales of the Group are made through its marketing and sales centre and the marketing and sales department of each business unit. The marketing and sales centre is in charge of the sales of the Group's products to domestic locomotive works, the MOR and its local railway administrations, while the marketing and sales department of each business unit is responsible for sales of their respective products to passenger car works, urban rail operators and other customers.

Products sold by the Group are generally settled either by telegraphic transfers or banker's acceptance upon/after delivery or telegraphic transfers before delivery. Export sales are settled either by letters of credit or telegraphic transfers. The Group generally stipulates payment upon delivery in sales contracts entered into with its customers. With respect to small, new or short-term customers, the Group normally strictly enforces such payment provision and settles payment before or upon delivery of goods or services. The Group, however, does not strictly enforce such payment provision against the MOR and its local railway administrations, the rail vehicle manufacturers and certain long-term customers in light of their funding sources and well-established credit history with the Group. The MOR and its railway administrations generally pay the Group annually or semi-annually when they receive allocated funds from the PRC

Government. Rail vehicle manufacturers make payment in the same pattern as the MOR and its local railway administrations are their key customers. The purchases of the MOR and its railway administrations and the rail vehicle manufacturers are generally within the PRC Government's annual budget and it is therefore unlikely for them to fail to make payment. The Group has not experienced any material payment default from those customers. During the Track Record Period, the Group did not experience any material payment defaults in respect of sales of its products. The Group also has internal control and reporting systems in place to monitor and control its trade receivables. Such systems include (i) a credit limit control policy and system, under which the Group sets a credit limit for each customer based on, among other factors, the customer's market position, reputation, size and relationship and track record with the Group, and such credit limits are subject to the Group's annual review; (ii) monthly trade receivable collection plans for sales department; and (iii) monthly ageing analysis of trade receivables.

The Group's largest customer accounted for approximately 22.2%, 18.2%, 13.4% and 13.8% of the Group's total turnover for the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, respectively, and the top five customers of the Group for the same periods together accounted for approximately 49.9%, 41.9%, 35.7% and 45.9%, respectively, of the Group's total turnover.

For the year ended 31 December 2003, the Parent Company owned 20% and 30% equity interests in Times Fittings and Times Electronics, two of the Group's top five customers. In September 2004, the Parent Company acquired additional 80% and 60% equity interests in Times Fittings and Times Electronics, respectively, making them the Parent Company's subsidiaries. For the two years ended 31 December 2004 and 2005 and the six months ended 30 June 2006, Kunming China Railway, in which the Parent Company held a 1.06% equity interest, was one of the Group's top five customers. For the year ended 31 December 2005 and the six months ended 30 June 2006, ZELC, in which the Parent Company owned a 12.61% equity interest (ownership starting from 31 August 2005), was one of the Group's top five customers.

For the year ended 31 December 2003, ZELW, then a wholly-owned subsidiary of CSR, was one of the Group's top five customers. For the year ended 31 December 2004, two wholly-owned subsidiaries of CSR, ZELW and CSR Qishuyan, were among the Group's top five customers. For the year ended 31 December 2005, ZELC, a company 98.74% beneficially owned by CSR, was one of the Group's top five customers.

中國北車集團大同電力機車有限公司 (CNR Datong Electric Locomotive Co., Ltd.), a company 94.16% owned by CNR, and 中國北車集團大連機車車輛有限公司 (CNR Dalian Locomotive Co., Ltd.), a company 97.07% owned by CNR, were two of the Group's top five customers for each of the three years ended 31 December 2005 and the six months ended 30 June 2006.

Save for the above disclosure, none of the Directors, their respective associates, or to the knowledge of the Directors, shareholders who will own more than 5% of the issued share capital of the Company immediately following the Global Offering had any interests in any of the five top customers of the Group for any of the three years ended 31 December 2005 and the six months ended 30 June 2006.

For the three years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, the Group's aggregate turnover from CSR Group, Kunming China Railway and CNR Group, all of which were state-owned enterprises, were RMB332.4 million, RMB409.9 million, RMB506.0 million and RMB327.7 million, respectively, accounting for 50.5%, 52.0%, 50.7% and 51.7% of the Group's turnover.

Marketing

The Group's marketing strategy is to maintain and reinforce its leading market position in the PRC Railway market and expand into urban rail and non-railway markets and the overseas market.

The Group attends trade fairs and exhibitions every year to promote its corporate image and products and attends biddings held by the MOR. The Group emphasises maintaining and developing good relationships with customers and reliability and quality of its products and services (including after-sales service). The Group's sales force visits its customers on a regular basis to maintain close relationships.

The Group's strategy for the overseas market is to market and export its component products primarily to developed countries and to market and export its system products primarily to developing countries. With a view to expanding its overseas market, the Group established a subsidiary company in the US in 2006.

Customer Service

The Group provides customer service to its customers through a network comprising seven regional divisions that covers all provinces and autonomous regions of China. Due to the special nature of train operation safety equipment which demands prompt response and attention, the safety equipment business unit has its own after-sales service team. The Group also stations staff with certain overseas customers to provide on-site service.

The Group has established a service hotline and website to facilitate communication with customers. Since 2003, the Group has carried out customer satisfaction surveys once every year. The Group also plans to implement a Customer Relationship Management (CRM) system, a technical support and information system, to better service its customers through the introduction of reliable processes and procedures for interacting with those customers.

The MOR requires that all key rail-related equipment and components be sold with warranties. In line with the industry practice, the Group generally provides (i) a 300,000 km or three year warranty for train power converters, auxiliary power supply equipment and control systems, (ii) a 18 month warranty for train operation safety equipment and (iii) a two year warranty for electrical control systems for large railway maintenance vehicles for all defects and repairs. The Group also provides warranties for electrical components, which may vary from contract to contract.

PRICING

In determining product prices, the Group takes into consideration a number of factors, which include market demand and supply, the MOR's price-setting policies, prices set by leading producers and competitors, cost of production, cost of research and development, a reasonable margin target and customer relationship.

The MOR sets a guidance price when a new type of train-borne electrical system for the PRC Railway network is commercially launched. The MOR sets the prices by reference to the prices of similar products, the cost structure of locomotive works and negotiations on the profit margin. Following the commercial launch, the price of a type of train-borne electrical system is normally set through bidding processes. For train-borne electrical systems that are sold to urban rail operators, the prices are also normally set through bidding processes. The Group normally prepares its bidding prices after taking into consideration a reasonable profit margin target.

For electrical components, the prices are determined primarily through negotiation with customers and by reference to reasonable profit margin targets and the market prices for similar products.

QUALITY CONTROL, SAFETY AND ENVIRONMENTAL MATTERS

The Group places significant emphasis on quality of its products to ensure that its products maintain a strong market position and high recognition in the industry. As at July 2006, the Group had over 98 full-time employees responsible for quality control procedures at the various centres and business units.

Strict quality control is carried out throughout the Group's material procurement and production processes and is implemented in the following five major steps:

- testing of quality of raw materials and components supplied (including sourcing raw materials and components from reputable and reliable suppliers to ensure uniformity and quality);
- checkpoints in each step of the production process for monitoring and testing the quality of the goods handled by the production staff in production line;
- product testing before leaving production line;
- issue of compliance certificate (合格證) after passing the quality tests; and
- final product testing before delivery.

The Group obtained an ISO9001:2000 certificate from BSI in December 2005 for its quality management system. The ISO9001:2000 certificate is reviewed by BSI annually. In the Directors' view, there is no impediment for the Group to obtain renewal of the certificate. The Group has not received any major complaints concerning its products and the amount of goods returned by customers in the Track Record Period was negligible.

The Group's proprietary core technologies are primarily reflected in the software the Group develops, and the Group's production processes, especially those of train-borne electrical systems, involve primarily assembly of components. As a result, the Group generates insubstantial amount of water and gas pollution and solid waste, primarily in the production processes of electrical components. The Directors also believe that there are no material potential future risks relating to environmental protection.

As advised by the Company's legal adviser as to PRC law, the Group's operations in the PRC are subject to, among others, the following environmental laws and regulations: (i) The Environmental Protection Law of the PRC (中華人民共和國環境保護法); (ii) The Water Pollution Prevention Law of the PRC (中華人民共和國水污染防治法); (iii) Regulations on Pollutant Emission Permits (排污許可證條例) promulgated by the State Environmental Protection Administration of China and (iv) Cleaner Production Promotion Law (中華人民共和國清潔生產促進法). The Group has installed pollution control facilities to reduce the releases of pollutants and maintain such releases within the levels as required by applicable laws and regulations. The Group has also set up and enforced internal procedures to prevent and manage pollution. The Group's PRC counsel, Grandall Legal Group Hangzhou, has advised the Group that during the Track Record Period, the Group has not violated state or local environmental, safety and health laws and regulations.

During each of the three years ended 31 December 2003, 2004 and 2005, the Group paid environmental protection fees of approximately RMB125,000, RMB65,000 and RMB63,000, respectively and incurred average annual operation costs of pollution control equipment of approximately RMB1.0 million. The Group expects to spend approximately RMB7.0 million in procuring pollution control equipment from 2007 to 2010.

In connection with the expansion of its production facilities, the Group engages professional environmental protection specialists to evaluate potential environmental impacts and factor them into the designs of production facilities to ensure full compliance with environmental laws and regulations.

In addition, the Group obtained an ISO14001:2004 certificate from BSI in 2005 for its environmental management system and an OHSASI8001: 1999 certificate from BSI in 2006 for its health and safety management system. The ISO14001:2004 certificate and the OHSAS18001:1999 certificate are reviewed by BSI annually.

INTELLECTUAL PROPERTY

All intellectual property rights relating to the Group's products are owned by the Group. Save for the train operation safety equipment hardware designs, which were shared with Henan Siwei in order to maintain consistency in train operation safety equipment hardware as required by the MOR, the Group has not licensed any of its intellectual property rights to any third party. Henan Siwei is a privately owned company independent from the Company. Both parties jointly decide man-machine interface and interface protocols with respect to software, but do not share software.

Henan Siwei and the Group have not entered into any written agreement in relation to the sharing of hardware designs. The Company owns two software copyrights for its two types of train operation safety equipment. The Group has limited the usage of shared hardware technologies to itself.

The Group relies on a combination of patent, trademark, software copyrights and trade secret relation details protections, as well as employee confidentiality agreements to safeguard its intellectual property. As at the Latest Practicable Date, the Group had 31 registered patents, 37 patent applications and 20 registered software copyrights in the PRC. The Group is licensed to use the Parent Company's 12 PRC registered trademarks. In addition, every research and development employee has given an undertaking in favour of the Group in his employment contract to keep the research work and related information confidential.

The Group has not been engaged in any litigation or legal proceedings for violation of intellectual property rights, nor is the Group aware of any violation of intellectual property rights on its part.

COMPETITION

The Group is a well-established train-borne electrical system supplier in the domestic market, which has a relatively small number of entrants due to certain industry-specific entry barriers for new entrants. See "Industry Overview — Rail Vehicle Manufacturing Industry in the PRC — Related PRC Regulatory Environment" and "Business — Leading Position in train-borne electrical system technology in the PRC" for details of industry-specific entrance barriers. The Group is the leading supplier of train power converters, auxiliary power supply equipment and control systems and the only supplier of electrical control systems for large railway maintenance vehicles in the PRC market. Based on the Group's knowledge and experience in the business, the Directors believe that there are only two suppliers of train operation safety equipment, including the Group, in the PRC.

The Directors believe that the Group currently enjoys competitive strength in the PRC train-borne electrical system market due to its well established relationships with key customers, relatively long operating history, the "TEG" brand recognition in the PRC market, more advanced technology levels, efficient production facilities, product variety and reliability. However, with the establishment of more sino-foreign joint ventures in the PRC and the MOR's recent policy of acquiring advanced foreign products and technologies, the Group expects that competition from overseas competitors in the domestic train-borne electrical system market will become more intense in the future. The Directors believe that it has certain competitive advantages over overseas manufacturers due to its close relationship with key customers and ability to offer customised products and services. However, many of those foreign manufacturers have substantially greater financial, technical and other resources than the Group does.

As a power semiconductor device supplier, the Group competes primarily with a foreign manufacturer and a state-owned company in the PRC Railway market. As a supplier of sensors, the Group competes primarily with a sino-foreign joint venture and a privately owned company in the PRC Railway market. The Directors believe that the Group has a competitive edge in the PRC

Railway market due to its business of supplying system products. Power semiconductor devices and sensors have a variety of applications outside of the PRC Railway market. The Group competes with a number of competitors outside of the PRC Railway market in connection with these products. For power semiconductor devices and sensors, the Group competes with its competitors on the basis of technology, price, marketing and service. Although the Group's technologies may not be as advanced as those of its foreign competitors, the Directors believe that the Group enjoys competitive strengths in its lower costs and marketing and service network compared to foreign competitors. Although the Group has not entered the markets as early as some of its domestic competitors, the Directors believe that the Group enjoys competitive strengths in its strong research and development and commercialisation capabilities compared to its domestic competitors.

INSURANCE

The Group maintains insurance for its fixed assets and inventory. During the Track Record Period, the Group did not make any material insurance claim. The Directors believe that the Group has arranged for insurance coverage which is customary in the Group's industries in China and is adequate to protect against the accident-related risks associated with its operations. The Group does not maintain any product liability insurance, which is not compulsory under PRC law. As at the Latest Practicable Date, the Group had not received any material claims from its customers regarding any of the Group's products.

LEGAL MATTERS AND PROCEEDINGS

The Group has been in material compliance with all applicable laws and regulations in the PRC since its establishment. The Group has not been engaged in any litigation, legal or arbitration proceedings which could have a material adverse effect on the financial condition and/or results of operations of the Group nor is the Group aware of any litigation or arbitration proceedings pending or threatened against the Group or any of its Directors.

SPECIAL EVENT

On 28 April 2005, the People's Procuratorate of Zhuzhou (the "Procuratorate") initiated a formal investigation against certain employees of Times Fittings (a former associate of the Parent Company) for suspected economic crimes. In September 2005, three individuals were charged by the Procuratorate with embezzlement allegedly committed during the period from 1998 to 2005. The Zhuzhou Intermediate People's Court delivered a judgment in December 2005, pursuant to which two of the defendants were sentenced to life imprisonment and the third defendant to 11 years of imprisonment. The amount allegedly misappropriated by the three individuals attributable to the Group during the period from 1998 to 2005 was approximately RMB3.5 million.

Pursuant to the Rule of the Central Committee of Communist Party of China (CPC) on the Implementation of the Responsibility and Accountability System for the Promotion of Anti-corruption Behaviour and the Implementation Measures of the CSR CPC Responsibility and Accountability System for the Promotion of Anti-corruption Behaviour, at a CSR CPC standing committee meeting held on 12 January 2006, Mr Liao Bin and Mr Tian Lei were given criticism and

recorded criticism, respectively, due to the fact that there were CPC members involved in the fraud case who were under Mr Liao Bin and Mr Tian Lei's supervision as the deputy Secretary and the Secretary of CPC committee of the Parent Company. No commercial or political consequences for either Mr. Liao or Mr. Tian were set out in the criticisms. Neither Mr. Liao's or Mr. Tian's position with the Parent Company nor any aspect of their duties or respective authorities have changed as a result of the criticisms. The Directors believe that the aforementioned criticisms have had no commercial or political consequences for either Mr. Liao or Mr. Tian. The Company's PRC legal counsel has confirmed that the criticisms of Mr Liao Bin and Mr Tian Lei do not affect Mr Liao Bin and Mr Tian Lei's suitability under PRC law to act as directors of the Company.

In light of the aforementioned incident, the Group has undertaken a number of measures to enhance its existing internal control systems which had supported the Group's operations since the establishment of the Parent Company. As part of those measures, in May 2005, the Group engaged Protiviti Shanghai Co., Ltd. ("Protiviti"), a firm of independent international risk consultants to review and improve the Group's originally existing internal control systems. The initial scope of engagement includes assisting the Group to improve its systems in the consolidation of financial statements, intra-group reconciliation, inventory control, inventory accounting and valuation, sale and purchase, trade receivable control and risk assessment of corporate information. The scope of engagement was further expanded, upon the request of the Joint Sponsors, to include the improvement of the Group's systems so as to comply with the Stock Exchange's requirements on the internal control systems of companies applying to be listed. The procedures performed by Protiviti include interviewing the persons in charge of each business unit of the Group, assessing the actual operations of the Group and producing procedural manuals for the Group. Based on the findings and weaknesses identified, the measures for improvement, as summarised below, among others, had been recommended:

Findings of weaknesses	Measures for improvement
Most business units of the Group operated independently under each of their own internal control systems.	Internal control systems integrating each business unit of the Group should be implemented.
Delay in the monthly reporting by certain business units resulted in mismatch of information in the monthly consolidated management accounts of the Group, and unclear definition of related party transactions or connected transactions gave rise to difficulties in identification of such transactions for appropriate accounting treatment.	Timely reporting, cross checking of accounts and pre-approval of connected transactions should be implemented.
Guidance and procedures for stock taking were not clearly documented.	Standardised stock taking measures and procedures should be formulated and strictly adhered to.
Analysis of aged, obsolete and scrapped stock had not been made at regular intervals.	Timely stock taking, analysis of aged stock and provision for stock written down should be reflected in the financial statements of the Group.

Findings of weaknesses	Measures for improvement
The policy for recognition of sales upon the transfer of the risk of ownership of products to the customers had not been strictly adhered to. Certain business units recognised sales only upon the issuance of invoices.	The terms of the sales contracts, the policy for recognition of sales and the procedures for recording of sales, warehouse movements, unit prices, discounts and invoicing should be consistently implemented and verified on a regular basis.
The procedures for filing of original accounting records, including vouchers, ledgers, sale and purchase orders, warehousing and credit facilities were not systematically managed.	Accounting records of the Group should be categorised, serial numbered and filed in an orderly basis by account personnel who is also responsible for lending and returning of these documents.
Aged debtors and revenue collection which concentrated in the last quarter of a year affected the normal cash flows of the first three quarters of the year.	The management of customers, including the checking of customers' credit profiles, the granting of credits to customers and the monthly analysis of debtors should be strengthened. Closer liaison with customers to supervise their payments in accordance with contractual terms should be practised.
Information for the management of suppliers, including background information of suppliers, price quotes and placing of orders, was not centralised and lack of periodic confirmation of outstanding accounts with the suppliers.	A centralised suppliers information system should be established for facilitating the identification of approved suppliers and disqualified suppliers, and any differences in accounts with the suppliers should be investigated and follow up closely.
A lack of fraud prevention mechanism to prevent, identify and control the risk of fraud.	See further details below.

The procedural manuals drafted by Protiviti specifically for the Group were first produced to the Group in August 2005. The Group immediately and fully implemented all procedural measures recommended by Protiviti to improve its internal control systems. During the implementation process, on-going minor adjustments had been made in response to feedbacks from various business units, including adjustments to various approval threshold amounts and reporting dates in accordance with the actual business operations of the business units. By March 2006, the Group was satisfied that all recommended measures of Protiviti had been completely and effectively implemented.

During September and October 2005, the Parent Company assigned a team of experienced senior management staff, accountants and other experienced personnel to conduct an initial self-investigation to assess the impact of the above-mentioned economic crimes. During March and April 2006, the Group conducted a further self-investigation to re-assess the impact of the event. The scope of the self-investigations covers the review of inventory control, off-balance sheet bank cash (also known as "small gold box"), procurement control and sale expense control. The work procedures of self-investigations include enquiries with the relevant personnel in charge, review and matching of accounts and related backup materials. The self-investigations conducted by the Group revealed the following fraudulent activities due to weaknesses in its internal control: (a) theft of materials, (b) transfer of contracts for earning contract price differences, (c) payment for phantom inventories with the proceeds received transferred to an off-balance sheet bank cash

for subsequent misappropriation thereof, (d) misappropriation of sales expense, and (e) misappropriation of proceeds from sales of written-off stocks. Both self-investigations led to the same conclusion that there were no further improprieties found apart from those uncovered by the Procuratorate and stated in the judgment delivered by the Zhuzhou Intermediate People's Court in December 2005. On 25 May 2006, based on the detailed investigation of substantially all past transactions and records and the resulting investigation findings, the Board of Directors were satisfied with the above-mentioned conclusion of the self-investigations and approved the self-investigation report after due and careful consideration. The Directors also confirmed that the financial losses suffered during the Track Record Period as a result of the event were not material. On 14 June 2006, the self-investigation results were reported to SASAC and CSR.

In order to improve and strengthen the internal control systems and to improve the Group's ability to prevent fraud events from happening in the future, the Group has, based on the recommendations of Protiviti, adopted the following procedures:

Inventory goods-in and goods-out control: The Group has replaced the inexperienced warehouse personnel with more experienced personnel, and the control over the movement of inventory has been strengthened by inventory goods-in and goods-out recording system. The warehouse personnel must ensure that the physical quantities of stock moved in and out from the warehouse match that in the inventory goods-in and goods-out records. All purchase invoice payment must be supported by inventory goods-in records and all inventory pending invoice issuance will be regularly followed up to ensure that such inventory is covered by subsequent invoicing to the customers to ensure that no materials will be stolen or misappropriated.

Procurement control: In the fraud case, the persons involved have misappropriated certain contract price difference on certain purchases for an ad hoc project performed in 2004, due to loose budgetary control over the performance of such project. To prevent similar events from happening in the future, budgetary control over purchases is exercised in all projects (including ad hoc projects), and tender from suppliers is required for purchases and all purchase contracts must be approved by the Group purchase department. All ad hoc projects are subject to the annual performance evaluation by the Group. In addition, the Group has introduced internal auditing procedures which require audit of all contracts with a value above certain threshold amount or contracts entered into by the Company with new suppliers. The relevant auditing work performed involves auditing of the circumstances of contract formation, contract management and examination of key contractual terms. The new internal auditing procedures will specifically examine the basis upon which contract pricing is determined.

Prohibiting fictitious transactions and off-balance sheet bank cash: Inventory movement to and from the warehouse has been stringently controlled, and goods received notes and goods despatch notes must be issued for any inventory moved into and moved out from the warehouse. The warehouse keeper must ensure consistency of the actual quantity received or despatched with the quantity in the goods received note or the goods despatch note. Purchases must be approved by purchase department with proper tender procedures. Employees are also subject to restrictions in setting up or holding equity interest in outside companies to prevent fictitious transactions conducted between the Group and outside companies which employees have control of or hold equity interest in. In April 2005, all the operations of the small gold box have been

terminated and the remaining funds of the small gold box were frozen by the Company's disciplinary committee to prevent potential mis-use of the funds of the small gold box. The Group issued a notice explicitly banning the formation of any small gold box. The Group has also issued a second notice which explicitly set out penalties applicable to any Group employees found to be involved in small gold box related activities. Furthermore, the Group has introduced a staff rotation policy, whereby key mid-level management and accounting staff are periodically rotated to different posts within the Group in order to promote independence and accountability. Finally, the Group has followed internal control procedures designed by Protiviti and the Group to strengthen its other related internal controls in this area.

Control over sales expense: To prevent misappropriation of sales expense, control over cash payment for selling expense has been strengthened by banning the cash payment of bonus to individuals who collected bonus on behalf of the salesman. Furthermore, selling expense payment must be approved by appropriate level of management and must also be within the cap set by management.

Control over inventory write-off: All inventory must be examined by a specialist team at the operating units level and/or the Company level for its usable condition before it is approved to be written off. The specialist team consists of accountants, manufacturing managers, marketing managers, technical staff, quality control specialists and managers of standardisation.

The Directors are of the view that the aforementioned procedures and the procedural manuals have been designed after due and careful examination of the Group's internal control situations and adequately address the weaknesses identified in the Group's originally existing internal control systems. The Group has also taken measures to ensure that those procedures have been properly implemented and are complied with. First, the Group appointed three employees (including the chief financial officer of the Company and the director of legal and securities department of the Company) in 2005 and the Company's internal auditing department to be in charge of monitoring the implementation and enforcement of the new procedures and procedural manuals. These three employees and the internal auditing department reported regularly to the Company's senior management and had frequent dialogue with Protiviti relating to the implementation and enforcement of the enhanced internal control systems based on their experience and the feedback they collected from the Group's staff. Second, in addition to the constant dialogue the Group promoted among its employees and professionals from Protiviti for the purposes of drafting procedural manuals, the Group has also organised its employees to study the new procedures, which enabled the employees to have a good understanding of the Group's enhanced internal control systems and greatly facilitate the effective operation of the enhanced internal control systems. Third, the Group has documented those procedures and distributed the procedural documents to relevant personnel of the Group.

In addition, the Company has taken the following actions to complement its internal control systems: (i) hired a qualified accountant in July 2006 and recruited additional 18 accounting staff during 2005, of which 11 staff hold professional accounting bachelor degrees or above, (ii) engaged professionals to hold regular training sessions for its accounting, procurement and inventory management personnel since early 2005, (iii) established a system to monitor product

outflows against contracts, sales invoices and related documents in early 2005, (iv) adopted ERP system on a trial basis in Times Electronics from early 2005 to June 2006, and implemented ERP system in Times Electronics in June 2006 and (v) vetted customers' and suppliers' information database to monitor connected transactions in early 2006.

To review and verify the effectiveness of the Group's implementation of Protiviti's recommended measures, Protiviti was also engaged to perform various process-level walk through test of controls between April and June 2006 and entity-level test of controls between June and August 2006.

The scope of process-level walk through test of controls, as set out in the engagement letter dated 30 May 2006, covered the major business units of the Group and examined the implementation of the internal control procedures within each business unit in detail. The walk through test of controls focused on assessing the sales, purchases, inventory management, financial reporting and connected party transactions aspects of the internal control systems and procedures.

The scope of entity-level test of controls, as set out in the engagement letter dated 10 July 2006, covers the assessment of the relevant procedures under control environment, corporate risk, internal control monitoring, control activities and information & communication aspects of the Group's overall internal control systems.

The results of the process-level test of controls show that all measures in the procedural manuals have been effectively and completely implemented and no exception has been identified in the testing samples. The results of the entity-level test of controls show that all major internal control matters have been properly addressed.

The Company has, among other things, strengthened the power of its audit committee to direct, supervise and examine the financial reporting and internal control measures of the Group, channeled the internal and external audit reports to the audit committee rather than directly to the management for commenting, and established the risk management committee (see details below) for managing risks relating to the Group. Further details are set out in Protiviti's reports (see the section headed "Documents available for inspection" in Appendix IX to this Prospectus).

In addition, in the Group's experience, since all the measures recommended by Protiviti were fully implemented in March 2006, the Group's enhanced internal control systems have been operating smoothly and effectively.

The Directors are of the view that the Group's internal controls are adequate considering (i) the Group's enhanced internal control procedures are designed by Protiviti and the Group after due and careful examination of the Group's internal control situations and adequately address the weaknesses identified in the Group's previous internal control systems; (ii) the Directors believe that the Group management's previous internal control experience enabled them to familiarise themselves with the enhanced internal control systems at a relatively fast pace and operate effectively under the enhanced internal control systems; (iii) Protiviti's recommended measures were introduced approximately 15 months ago and the enhanced internal control systems have

been in full and smooth operation for approximately eight months; (iv) Protiviti has conducted walkthrough testing of controls on the Group's internal control systems and the results of such testings are to the Group's satisfaction; (v) the Group's self-investigations led to the conclusion that no further improprieties were found apart from those uncovered by the Procuratorate; and (vi) the Group has taken a number of measures as described above to ensure the enhanced internal control systems are complied with.

Furthermore, following the recommendation of the Joint Sponsors for ongoing good corporate governance, the Company intends to engage Protiviti to perform yearly reviews of the Company's internal control systems, with the first of such review scheduled for January 2007. The Company also put in place a risk management committee to, among other things, monitor and review internal control related matters. The risk management committee consists of five members, two of whom are non-executive Directors and three of whom are independent non-executive Directors. See "Directors, Supervisors, senior management and staff — Risk management committee" for details. The Board has issued internal directives to all relevant departments and business units to strictly adhere to the internal control instructions.