



To shareholders,

Year 2004, a milestone in the development history of Dongfang Electrical Machinery Company Limited (the "Company"), marked its accomplishment of various tasks in production and sales, and a significant growth in key economic indices. I am pleased to present the annual report of the Company for the year ended 31 December 2004 for the review of shareholders.

In 2004, the Company's consolidated production volume of power-generating equipment broke through the 10,000MW threshold by reaching 15,360MW. This amounts to 200% of the historic high production volume which the Company attained in 2003, making the Company rank first in the world in terms of its production volume in power-generating equipment. Thus, the Company's accumulated production volume of power-generating equipment increased to 84,000MW. Besides, the Company also smoothly delivered hydro and thermal power-generating equipment with a total capacity of 11,800MW in one go in the year.

The Company recorded a significant increase in its results in 2004. Based on the PRC GAAP, sales revenue amounted to RMB2.05 billion, up by 71% over that of last year, with a net profit of RMB265 million, up by 699% over that of last year; earnings per share increased by RMB0.514 over that of last year to RMB0.588. Based on the HK

GAAP, its turnover amounted to RMB2.05 billion, up by 71% over that of last year, with a net profit of RMB253 million, up by 1,257% over that of last year; earnings per share increased by RMB0.52 over that of last year to RMB0.561.

The Company's operating results in 2004 was characterised by a rapid growth in total assets amounting to RMB6,370 million, up by 71% from that of last year, and sufficient cash flow with its net cash flow increased by RMB1,709 million, while its net cash flow per share from operating activities amounting to RMB5.59 at the end of 2004. This provides a favourable financial environment for the Company.

Moreover, the Company adjusted its accounting policies in a timely manner which include suitably increasing the proportion of the provision for bad debts in the accounts receivable and applying accelerated depreciation of fixed assets, so as to cater for the demand of production, further optimise the Company's assets and reduce operating risks.

Facing the significant growth in production volume, sales revenue and contracts in 2004, the Company first embarked on the design of production process to regulate management as a way to proactively address and effectively control costs and expenses, and thereby overcame the adverse impact arising from the increasing prices of raw materials, power and outsourcing. Meanwhile, the Company continued to exercise strict control on expenses. As a result, a slight increase was recorded in administrative and operating expenses and the financial cost decreased significantly, demonstrating a sound performance of positive income.

To sum up, the Company has in 2004 completely recovered its loss in the previous years, and has built on this foundation by making a surplus in 2004. With a view of actively implementing its dividend policy and in the hope of rewarding its shareholders, the Board recommended the general meeting to declare a final cash dividend of RMB0.12 per share for 2004, representing a dividend yield of 63%.

The Company will continue to proactively explore the market, strictly control our quality, continuously improve our technology and conscientiously trim costs. This will enhance a stable development and improvement in its efficiency.

Finally, I hereby would like to express my sincere gratitude on behalf of all members of the Board to all shareholders for their trust and support throughout these years.

Zhu Yuanchao
Chairman

21 March 2005