

Directors' Report

The directors submit their report together with the audited financial statements for the year ended 31 March 2006.

Principal activities and geographical analysis of operations

The company is an investment holding company. The principal activities of its subsidiaries and associated companies are set out in Note 19 and Note 20 to the financial statements.

Results and appropriations

The results of the Group for the year are set out in the consolidated income statement on page 55.

The interim dividend of approximately RMB20,417,000 was paid on 16 January 2006.

Subject to approval of the directors' recommendation by shareholders at annual general meeting to be held on 1 September 2006, the final dividend will be paid on 8 September 2006.

Reserves

Movements in the reserves of the Group and of the Company during the year are set out on pages 58 and 99 respectively.

Distributable reserves

As at 31 March 2006, the Company's share premium reserve of approximately RMB1,099,998,000 (subject to Section 34 of the Cayman Companies Law and the Article of Association of the Company), and retained earnings of approximately RMB115,797,000 were available for distribution to the Company's shareholders.

Under the Companies Law (Revised) of the Cayman Islands, the funds in the share premium account and the merger reserve account of the Company are distributable to the shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as they fall due in the ordinary course of business.

Dividends

The directors recommend the payment of a final dividend of HK\$0.057 per share to the shareholders on the register of members as of 14 August 2006 amounting to approximately HK\$71,097,000.

Property, plant and equipment

Additions to property, plant and equipment of the Group for the year totaled approximately RMB101,816,000 (2005: RMB389,954,000), comprising principally construction in progress and machinery and equipment.

Details of the movements in property, plant and equipment of the Group are set out in Note 16 to the financial statements.

Share capital

Details of the movements in share capital of the Company are set out in Note 32 to the financial statements.

Share option scheme

The Company has a share option scheme which was adopted on 4 September 2003 ("Share Option Scheme") whereby the directors of the Company ("Directors") are authorized, at their discretion, to invite, inter alia, employees of the Group and directors of any members of the Group, to take up options to subscribe for shares of the Company. The exercise price of the options is the higher of (i) the closing price of the shares as stated in the daily quotations sheet of The Stock Exchange of Hong Kong Limited ("Stock Exchange") on the date of grant and (ii) the average closing price of the shares as stated in the daily quotations sheet of the Stock Exchange for the five business days immediately preceding the date of grant. The options are exercisable for a period to be notified by the directors of the Company to each grantee. Such period will not exceed ten years from the date on which the Share Option Scheme is adopted.

The maximum number of shares which may be issued upon the exercise of all outstanding options and yet to be exercised under the share options scheme and any other scheme of the Company shall, subject to refreshment in accordance with the requirements set out in Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules"), not exceed 10% of the total issued share capital of the Company from time to time. Subject always to the above overall limit, the directors of the Company may grant options under the Share Option Scheme, generally and without further authority, in respect of such number of shares which may be issued upon exercise of all options to be granted under the Share Option Scheme not exceeding 83,000,000 shares of the Company.

In respect of the maximum entitlement of each participant under the Share Option Scheme, the number of shares issued and to be issued upon the exercise of the options granted and to be granted in any 12-month period up to the date of grant to each participant is limited to 1% of the total issued share capital of the Company in issue.

Since the adoption of the Share Option Scheme, no options have been granted.

Pre-emptive rights

There is no provision for pre-emptive rights under the Company's Article of Association and there has been no restriction against such rights under the laws of Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders of the Company.

Financial summary

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on pages 103 to 104.

Purchase, sale or redemption of securities

During the year, neither the Company nor any of its subsidiaries has purchased or redeemed any of the Company's listed shares.

Directors

The directors during the year and up to the date of this report are:

Executive Directors

Ms. Lilly Huang (Chairman)

Mr. Zhou Tian Bao

Ms. Zhang Zhen Juan

Mr. Yang Bin

Mr. Dai Wei (appointed with effect from 27 September 2005)

Mr. Chen Xiang Dong (appointed with effect from 27 September 2005)

Non-Executive Director

Mr. Lee Cheuk Yin, Dannis (re-designated from an executive Director to a non-executive Director with effect from 19 August 2005)

Independent Non-Executive Directors

Mr. Choi Tat Ying, Jacky

Mr. Wu Chao Ying (resigned with effect from 1 April 2006)

Ms. Zhang Xin, Cindy

Mr. Zhang Jian Chun (appointed with effect from 1 April 2006)

Each independent non-executive Director provided an annual confirmation of his or her independence to the Company for the year ended 31 March 2006 and the Company confirmed that each of them was still considered to be independent.

In accordance with Article 108 of the Company's Articles of Association, Ms. Lilly Huang, Mr. Zhou Tian Bao, Ms. Zhang Zhen Juan and Mr. Yang Bin will retire by rotation at the forthcoming annual general meeting of the Company and, being eligible, offer themselves for re-election.

Pursuant to Article 112 of the Company's Articles of Association, Mr. Lee Cheuk Yin, Dannis, Mr. Dai Wei, Mr. Chen Xiang Dong and Mr. Zhang Jian Chun will retire and offer themselves for re-election at the forthcoming annual general meeting of the Company.

Directors' service contracts and letters of appointment

Each of the executive Directors and non-executive Directors of the Company entered into a service agreement with the Company. Each of these service agreements is for an initial term of 3 years renewable automatically for successive terms of one year each commencing from the day next after the expiry of the then current term until terminated by either party for not less than three months' prior written notice and is subject to retirement by rotation and re-election at annual general meeting pursuant to the Articles of Association. Each independent non-executive Director entered into appointment letters with the Company for a term of 2 years from date of the appointment letter and is subject to retirement by rotation and re-election at annual general meeting pursuant to the Articles of Association thereafter.

No Director proposed for re-election at the forthcoming annual general meeting has an unexpired service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than normal statutory obligations.

Directors' emoluments

Details of the remuneration of the Directors pursuant to Appendix 16 of the Listing Rules are set out in Note 15 to the financial statements.

Directors' interests in contacts

Save for those transactions described in the note "Related Party Transaction" in Note 36 to the financial statements and the section "Continuing Connected Transactions" below, none of the Directors had material interest, whether directly or indirectly, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party during the year.

Biographical details of Directors and senior management

Biographical details of Directors and senior management are set out on pages 34 to 36.

Directors' and chief executive's interests and short positions in the shares, underlying shares and debentures

At 31 March 2006, the interests and short positions of each director and chief executive of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO")), as recorded in the register maintained by the Company under Section 352 of the SFO or as notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by directors of Listed Companies were as follows:

Name of director	Number of shares held			Approximate percentage of shareholding
	Personal interest	Corporate interest	Total	
Ms. Lilly Huang (Note 1)	—	600,000,000(L)	600,000,000	55.69%
Mr. Zhou Tian Bao (Note 2)	8,832,000(L)	645,000,000(L)	653,832,000	60.69%

The letter "L" denotes a long position in shares of the Company.

Note:

- (1) The shares are held by Century Founders Group Limited in which Ms. Lilly Huang owns 63% of the interests.
- (2) Mr. Zhou Tian Bao is deemed to be interested in 653,832,000 shares in the Company. These shares are held in the following capacity:
 - i) 8,832,000 shares are held in his personal name.
 - ii) 45,000,000 shares are held by Mark Up Investments Limited which is a company wholly-owned by Mr. Zhou Tian Bao.
 - iii) 600,000,000 shares are held by Century Founders Group Limited in which 37% interest is owned by Mark Up Investments Limited.

Shares held by substantial shareholders

So far as is known to any Directors, as at 31 March 2006, other than the interests of the Directors as disclosed above, the following persons had interests in the Shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register required to be kept by the Company under Section 336 of the SFO, or was otherwise, as at 31 March 2006, interested in 5% or more of any class of the then issued share capital of the Company, or was otherwise, as at 31 March 2006, a substantial shareholder (as defined in Listing Rule) of the Company.

Name of shareholder	Number of shares held	Approximate percentage of shareholding
Century Founders Group Limited (Note 1)	600,000,000(L)	55.69%
Mark Up Investments Limited	645,000,000(L)	59.87%
Ms. Lilly Huang (Note 1)	600,000,000(L)	55.69%
Mr. Zhou Tian Bao	653,832,000(L)	60.69%
Deutsche Bank Aktiengesellschaft	86,977,113(L)	8.07%
Sansar Capital Management, LLC	78,504,000(L)	7.29%
PMA Capital Management Limited	58,256,733(L)	5.41%

The letter "L" denotes a long position in shares of the Company.

Note:

(1) Century Founders Group Limited owns 600,000,000 Shares. Ms. Lilly Huang owns 63% of the interests in Century Founders Group Limited and the remaining 37% interest is owned by Mark Up Investments Limited, a company wholly-owned by Mr. Zhou Tian Bao.

Save as disclosed above and so far as the Directors are aware, as at 31 March 2006, no other person (other than the Directors) had an interest or short position in the Company's shares which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO and as recorded in the register required to be kept under Section 336 of SFO, or was otherwise a substantial shareholder of the Company.

Management contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

Major customers and suppliers

During the year, the Group purchased 59% and 26% of its goods and services from its 5 largest suppliers and its largest supplier respectively. Also, the Group sold 46% and 10% of its goods and services to its 5 largest customers and its largest customer respectively.

Save as disclosed in Note 36 to the financial statements, none of the Directors, their associates or any shareholder (which to the knowledge of the directors owns more than 5% of the Company's share capital) had an interest in the major suppliers or customers noted above.

Related party transactions

Details of related party transactions undertaken in the normal course of business are set out in Note 36 to the financial statements.

Continuing connected transactions

The following continuing connected transactions were entered into by members of the Group and a conditional waiver from compliance with requirements of Chapter 14 (replaced by Chapter 14A with effect from 31 March 2004) of the Listing Rules in respect of continuing connected transactions was granted by the Stock Exchange on 26 September 2003 for a period of three financial years ending 31 March 2006:

- (1) Pursuant to a lease agreement dated 6 August 2000 (the "Premises Lease Agreement") entered into between Anhui Industries and Trading Corporation ("AITC"), which is a PRC established company jointly owned and managed by Mr. Zhou Tian Bao, a director of the Company, and his spouse, and Norstar Automotive Industrial Inc. ("Norstar Automotive"), a wholly owned subsidiary of the Company as at 31 March 2006, AITC has leased to Norstar Automotive a factory complex at 68 Shanxiang Road, Bengbu, Anhui Province, the PRC (the "Premises") for a term of five years commencing from 6 August 2000 to 5 August 2005 at an annual rent of RMB2.3 million. By a supplemental agreement dated 24 August 2002 (the "Supplemental Premises Lease Agreement") entered into between the parties, the term of the lease agreement was extended for a further five years up to 5 August 2010 with any increase in rent to be agreed between the parties on the basis that the increased rent for each of the five years during the extended term shall not be more than 120% of the rent payable immediately before the extension.

During the year ended 31 March 2006, the amount of rent paid by the Group to AITC for the Premises was approximately RMB2.3 million.

- (2) Pursuant to a lease agreement dated 20 December 1997 (the "First Equipment Lease Agreement") entered into between AITC and Norstar Automotive, AITC has leased to Norstar Automotive certain pressure machineries ("Pressure Machineries") for a term of eight years commencing from 20 December 1997 to 19 December 2005 at an annual rent of RMB3.1 million. By a supplemental agreement dated 4 August 2005 (the "Supplemental First Equipment Lease Agreement") entered into between the parties, the term of the lease agreement was extended for a further five years up to 19 December 2010 and the remaining terms of the First Equipment Lease Agreement remained unchanged.

During the year ended 31 March 2006, the amount of rent paid by the Group to AITC for the Pressure Machineries was approximately RMB3.1 million.

- (3) Pursuant to a lease agreement dated 6 August 2000 (the "Second Equipment Lease Agreement") entered into between AITC and Norstar Automotive, AITC has leased to Norstar Automotive certain production machineries ("Production Machineries") for a term of five years commencing from 6 August 2000 to 5 August 2005 at an annual rent of RMB5.4 million. By a supplemental agreement dated 4 August 2005 (the "Supplemental Second Equipment Lease Agreement") entered into between the parties, the term of the lease agreement was extended for a further five years up to 6 August 2010 and the remaining terms of the Second Equipment Lease Agreement remained unchanged.

During the year ended 31 March 2006, the amount of rent paid by the Group to AITC for the Production Machineries was approximately RMB5.4 million.

As the waiver expired on 31 March 2006, for the purpose of compliance with the relevant rules under Chapter 14A of the Listing Rules, Norstar Automotive entered into the following new continuing connected transactions with AITC on 31 March 2006:

- (1) Pursuant to a lease agreement dated 31 March 2006 (the “New Premises Lease Agreement”), AITC has leased to Norstar Automotive a factory complex at 68 Shanxiang Road, Bengbu, Anhui Province, the PRC (the “Leased Property”) for a term of three years commencing from 1 April 2006 to 31 March 2009, which is subject to early termination by either parties giving the other party a 6-month prior written notice, at an annual rent of RMB2.7 million. As a term of the New Premises Lease Agreement, the Premises Lease Agreement and the Supplemental Premises Lease Agreement were terminated on 31 March 2006. The Leased Property is the same as the Premises subject to the Premises Lease Agreement and the Supplemental Premises Lease Agreement. The aggregate rental payable by the Group to AITC under the New Premises Lease Agreement for each of the three years ending on 31 March 2009 is subject to the annual cap of RMB2.7 million. The annual cap is determined by reference to the terms of the New Premises Lease Agreement.
- (2) Pursuant to a lease agreement dated 31 March 2006 (the “New First Equipment Lease Agreement”), AITC has leased to Norstar Automotive certain pressure machineries (“Leased Machineries”) for a term of three years commencing from 1 April 2006 to 31 March 2009, which is subject to early termination by either parties giving the other party a 6-month prior written notice, at an annual rent of RMB2.7 million. As a term of the New First Equipment Lease Agreement, the First Equipment Lease Agreement and the Supplemental First Equipment Lease Agreement were terminated on 31 March 2006. The Leased Machineries are the same as the Pressure Machineries subject to the First Equipment Lease Agreement and the Supplemental First Equipment Lease Agreement.
- (3) Pursuant to a lease agreement dated 31 March 2006 (the “New Second Equipment Lease Agreement”), AITC has leased to Norstar Automotive certain production machineries and equipment for a term of three years commencing from 1 April 2006 to 31 March 2009, which is subject to early termination by either parties giving the other party a 6-month prior written notice, at an annual rent of RMB2.4 million. As a term of the New Second Equipment Lease Agreement, the Second Equipment Lease Agreement and the Supplemental Second Equipment Lease Agreement were terminated on 31 March 2006. Certain production machineries and equipment which were used to be subject to the Second Equipment Lease Agreement and the Supplemental Second Equipment Lease Agreement were no longer leased from AITC under the New Second Equipment Lease Agreement.

The aggregate rental payable by the Group to AITC under the New First Equipment Lease Agreement and the New Second Equipment Lease Agreement for each of the three years ending on 31 March 2009 is subject to a total annual cap of RMB5.1 million. The annual cap is determined by reference to the terms of the New First Equipment Lease Agreement and the New Second Equipment Lease Agreement.

The Directors, including the independent non-executive Directors, have reviewed the continuing connected transactions and confirmed that:

- (a) the continuing connected transactions and the new continuing connected transactions have been entered into by the Group in the ordinary and usual course of business;
- (b) the continuing connected transactions and the new continuing connected transactions have been entered into on an arm's length basis and, where there are comparable transaction, on normal commercial terms which are no less favorable than terms available to (or from) independent third party (to extent that there are comparable transactions);
- (c) the continuing connected transactions and the new continuing connected transactions are fair and reasonable so far as the shareholders of the Company are concerned;

- (d) the continuing connected transactions and the new continuing connected transactions have been entered into in accordance with the respective terms of the agreements relating to such transactions; and
- (e) the continuing connected transactions are within the applicable upper limits pursuant to the conditional waiver granted by the Stock Exchange as follows:
 - (i) in the financial year ended 31 March 2006, the annual aggregate consideration payable in respect of the Premises Lease Agreement (as supplemented by the Supplemental Premises Lease Agreement) did not exceed RMB2.3 million;
 - (ii) in the financial year ended 31 March 2006, the annual aggregate consideration payable in respect of the First Equipment Lease Agreement and the Second Equipment Lease Agreement did not exceed RMB8.5 million;
 - (iii) in the financial year ended 31 March 2006, the amount of the Group Guarantee did not exceed RMB380 million; and
 - (iv) in the financial year ended 31 March 2006, the annual aggregate consideration payable (i) in respect of the Premises Lease Agreement and (ii) in respect of the First Equipment Lease Agreement and Second Equipment Lease Agreement did not exceed the higher of either HK\$10 million or 3% of the latest published net tangible assets of the Group from time to time.

Directors' interest in competing business

None of the Directors had any interest, either direct or indirect, in any business, which may compete or constitute a competition with the business of the Group.

Retirement schemes

Details of the retirement schemes of the Group are set out in Note 30 to the financial statements.

Sufficiency of public float

According to the information that is publicly available to the Company and within the knowledge of the Directors, the percentage of the Company's shares which are in the hands of the public exceeds 25% of the Company's total number of issued shares.

Auditors

The accounts have been audited by RSM Nelson Wheeler who retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of RSM Nelson Wheeler as auditors of the Company will be proposed at the forthcoming annual general meeting of the Company.

On behalf of the Board

Norstar Founders Group Limited

Lilly Huang

Chairman

Hong Kong, 22 June 2006