

A. FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC GAAP

BALANCE SHEET

AS AT 31ST DECEMBER, 2006

		31st December, 2006		31st December, 2005	
		The Group	The Company	The Group	The Company
ASSETS		Note			
CURRENT ASSETS:					
Bank balances and cash	5.1	166,794,262.63	113,884,419.17	171,876,071.40	116,260,474.57
Short-term investments	5.2	11,902,402.80	11,902,402.80	12,773,633.85	12,773,633.85
Bills receivable	5.3	52,131,390.23	30,149,988.21	19,057,802.00	14,968,802.00
Dividends receivable		—	2,000,000.00	—	2,000,000.00
Interest receivable		—	—	—	—
Accounts receivable	5.4	134,782,948.68	88,050,935.92	86,505,238.20	39,739,434.81
Other receivable	5.5	14,285,967.61	20,485,951.98	23,806,326.81	26,077,578.74
Prepayments	5.6	43,385,358.17	9,227,357.17	26,107,189.35	5,394,947.04
Subsidies receivable		504,995.71	504,995.71	—	—
Inventories	5.7	260,784,768.61	171,945,236.11	274,502,685.89	175,648,964.45
Prepaid expenses		12,574.20	—	24,301.00	—
Net loss on deferred current assets		—	—	—	—
Long-term debt investment due within one year		—	—	—	—
TOTAL CURRENT ASSETS		684,584,668.64	448,151,287.07	614,653,248.50	392,863,835.46
LONG-TERM INVESTMENTS:					
Long-term equity investments	5.8	41,365,734.92	117,011,845.76	32,208,719.62	106,264,789.33
Comprising: consolidated differences in value	5.8	6,024,016.42	6,024,016.42	8,389,904.87	8,389,904.87
Comprising: difference in equity investment	5.8	6,024,016.42	6,024,016.42	8,389,904.87	8,389,904.87
Long-term debt investment		—	—	—	—
Total Long-term investments		41,365,734.92	117,011,845.76	32,208,719.62	106,264,789.33
FIXED ASSETS:					
Fixed assets at cost	5.9	571,146,028.54	470,853,162.93	525,962,003.16	427,594,988.77
Less: accumulated depreciation	5.9	211,099,118.62	182,986,033.69	188,265,610.41	164,479,548.96
FIXED ASSETS, NET BOOK VALUE	5.9	360,046,909.92	287,867,129.24	337,696,392.75	263,115,439.81
Less: provision for impairment loss	5.9	8,345,232.87	2,681,481.88	6,929,723.60	2,700,616.95
FIXED ASSETS, NET REALISABLE VALUE	5.9	351,701,677.05	285,185,647.36	330,766,669.15	260,414,822.86
Project materials		—	—	—	—
Construction in progress	5.10	58,552,347.28	26,859,057.05	46,594,318.14	18,119,165.03
Disposal of fixed assets		—	—	—	—
Loss on deferred fixed assets, net		—	—	—	—
TOTAL FIXED ASSETS		410,254,024.33	312,044,704.41	377,360,987.29	278,533,987.89
INTANGIBLE AND OTHER ASSETS					
Intangible assets	5.11	45,491,602.22	23,243,334.54	54,910,745.06	24,773,777.87
Long-term deferred expenditures		198,479.70	—	50,649.20	—
Other long-term investments		—	—	—	—
TOTAL INTANGIBLE AND OTHER ASSETS		45,690,081.92	23,243,334.54	54,961,394.26	24,773,777.87
DEFERRED TAXATION					
Deferred taxation		—	—	—	—
TOTAL ASSETS		1,181,894,509.81	900,451,171.78	1,079,184,349.67	802,436,390.55

Unit: RMB

Company's Legal Representative: Gao Minghui
Financial Controller: Pi Jianguo
Prepared by: Zhao Qiongfeng

BALANCE SHEET

AS AT 31ST DECEMBER, 2006

LIABILITIES AND SHAREHOLDER'S EQUITY	Note	31st December, 2006 The Group	31st December, 2006 The Company	31st December, 2005 The Group	31st December, 2005 The Company
CURRENT LIABILITIES:					
Short-term loans	5.12	40,000,000.00	20,000,000.00	60,000,000.00	40,000,000.00
Bills payable		—	—	—	—
Accounts payable	5.13	113,675,973.10	71,824,401.84	100,037,194.40	40,920,291.77
Advances from customers	5.14	218,325,953.57	115,126,650.06	196,375,494.03	99,153,631.92
Accrued salary	5.15	6,511,810.09	6,506,281.22	3,574,234.94	3,547,327.14
Accrued welfare		4,351,460.07	1,459,558.82	6,421,806.45	3,949,579.01
Dividends payable		1,176,869.81		2,101,732.59	
Taxes payable	5.16	23,375,089.60	19,114,039.09	30,237,113.95	24,632,724.84
Other payable	5.17	140,082.22		763,673.42	568,537.40
Other Accrued	5.18	45,844,183.60	20,072,754.40	29,713,634.55	8,391,004.42
Accrued expenses	5.19	3,140,549.14	2,885,875.52	1,562,213.45	1,392,915.45
Estimated liabilities		—	—	—	—
Long-term loans due within one year	5.20	684,337.80	684,337.80	342,168.90	342,168.90
Other current liabilities		—	—	—	—
TOTAL CURRENT LIABILITIES		457,226,309.00	257,673,898.75	431,129,266.68	222,898,180.85
LONG-TERM LIABILITIES:					
Long-term loans	5.21	20,000,000.00	20,000,000.00	40,000,000.00	40,000,000.00
Long-term payable	5.22	10,055,966.60	2,855,966.60	10,269,175.70	3,069,175.70
Specific project payable	5.23	11,311,680.50	3,211,680.50	6,782,628.78	2,675,616.01
Deferred gain	5.24	5,237,046.60	5,237,046.60	—	—
TOTAL LONG-TERM LIABILITIES		46,604,693.70	31,304,693.70	57,051,804.48	45,744,791.71
DEFERRED TAXATION					
Deferred taxation		—	—	—	—
TOTAL LIABILITIES		503,831,002.70	288,978,592.45	488,181,071.16	268,642,972.56
MINORITY INTERESTS		67,311,674.82	—	59,009,040.36	—
SHAREHOLDER'S EQUITY					
Share capital	5.25	245,007,400.00	245,007,400.00	245,007,400.00	245,007,400.00
Less: Returned on investment		—	—	—	—
Share capital, net		245,007,400.00	245,007,400.00	245,007,400.00	245,007,400.00
Capital reserves	5.26	314,797,956.97	314,797,956.97	314,193,651.63	314,193,651.63
Surplus reserves	5.27	20,298,114.29	20,298,114.29	16,812,657.84	16,812,657.84
Including: Statutory public welfare fund	5.27	—	—	8,406,328.92	8,406,328.92
Unappropriated profits	5.28	30,648,361.03	31,369,108.07	(44,019,471.32)	(42,220,291.48)
TOTAL SHAREHOLDERS' EQUITY		610,751,832.29	611,472,579.33	531,994,238.15	533,793,417.99
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		1,181,894,509.81	900,451,171.78	1,079,184,349.67	802,436,390.55

Company's Legal Representative: Gao Minghui
Financial Controller: Pi Jianguo
Prepared by: Zhao Qiongfen

STATEMENT OF INCOME

FOR THE YEAR ENDED 31ST DECEMBER, 2006

Unit: RMB

ITEMS	Note	2006		2005	
		The Group	The Company	The Group	The Company
1. Principle operating income	5.29	848,419,448.35	644,001,780.51	672,642,923.86	438,834,545.34
Less: Principal operating cost	5.29	618,794,939.80	472,027,873.72	495,526,468.49	324,366,538.29
Principal operation tax and addition	5.30	1,469,873.90	–	1,826,834.56	–
2. Principal operating profit		228,154,634.65	171,973,906.79	175,289,620.81	114,468,007.05
Add: Profit from other operations	5.31	3,619,317.68	3,621,547.55	(483,467.59)	1,222,352.23
Less: Selling expenses		38,417,340.82	26,558,553.97	32,898,369.10	19,570,041.54
Administrative expenses		83,808,219.65	49,466,843.42	86,334,906.61	50,638,195.60
Financial expenses	5.32	4,771,019.58	2,858,559.16	3,731,668.72	2,325,365.23
3. Operating profit		104,777,372.28	96,711,497.79	51,841,208.79	43,156,756.91
Add: Investment income	5.33	(586,923.83)	(6,446,207.58)	(2,999,313.31)	(16,531,788.54)
Subsidy income	5.34	5,485,047.73	2,000,000.00	2,922,171.67	2,000,000.00
Non-operating income	5.35	924,758.32	347,832.67	372,680.28	293,867.00
Less: Non-operating expenses	5.36	9,374,785.06	1,534,886.62	13,783,067.15	2,374,871.21
4. Profit before income tax		101,225,469.44	91,078,236.26	38,353,680.28	26,543,964.16
Less: Income tax	5.37	15,068,558.77	14,003,380.26	9,751,501.09	6,423,731.99
Minority interest		8,003,621.87	–	10,281,126.86	–
5. Net profit for the period		78,153,288.80	77,074,856.00	18,321,052.33	20,120,232.17

Unit: RMB

SUPPLEMENTARY INFORMATION:	Note	2006		2005	
		The Group	The Company	The Group	The Company
1. Profit from sale and disposal of investee companies		–	–	–	–
2. Loss arising from natural disasters		–	–	–	–
3. Increase (decrease) in profit due to change in accounting policies		–	–	–	–
4. Increase (decrease) in profit due to change in accounting estimates		–	–	–	–
5. Loss arising from debt restructuring		–	–	–	–
6. Others		–	–	–	–

Company's Legal Representative: Gao Minghui

Financial Controller: Pi Jianguo

Prepared by: Zhao Qiongfeng

STATEMENT OF APPROPRIATION

FOR THE YEAR ENDED 31ST DECEMBER, 2006

Unit: RMB

ITEMS	Note	2006		2005	
		The Group	The Company	The Group	The Company
1. Net profit for the period	5.28	78,153,288.80	77,074,856.00	18,321,052.33	20,120,232.17
Add: Accumulated losses at the beginning of the year	5.28	(44,019,471.32)	(42,220,291.48)	(62,340,523.65)	(62,340,523.65)
Other transfer					
2. Profit for distribution	5.28	34,133,817.48	34,854,564.52	(44,019,471.32)	(42,220,291.48)
Less: Statutory surplus reserves		3,485,456.45	3,485,456.45	—	—
Statutory public welfare fund		—	—	—	—
Employee welfare and bonus		—	—	—	—
Reserve fund		—	—	—	—
Corporate development fund		—	—	—	—
Return on investment		—	—	—	—
3. Profit available for distribution	5.28	30,648,361.03	31,369,108.07	(44,019,471.32)	(42,220,291.48)
Less: Preference shares dividend paid					
Surplus reserve					
Ordinary share dividend paid					
Convertible share dividend					
4. Unappropriate profit	5.28	30,648,361.03	31,369,108.07	(44,019,471.32)	(42,220,291.48)

Company's Legal Representative: Gao Minghui

Financial Controller: Pi Jianguo

Prepared by: Zhao Qiongfeng

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2006

ITEMS	Note	Unit: RMB	
		The Group	The Company
1. Cash flow from operating activities:			
Cash received from sales of goods or rendering of services		891,324,584.09	663,388,195.35
Refund of taxes and surcharges received		3,664,276.18	2,242,231.35
Other cash received relating to operating activities		41,339,971.45	4,149,464.78
Sub-total of cash inflows		936,328,831.72	669,779,891.48
Cash paid for goods and services		570,192,947.24	380,219,013.89
Cash paid to and on behalf of employees		100,705,115.57	86,547,630.76
Taxes and surcharges paid		81,655,391.17	63,784,436.59
Other cash paid relating to operating activities	5.39	83,450,606.19	42,351,830.15
Sub-total of cash outflows		836,004,060.17	572,902,911.39
Net cash flows from operating activities		100,324,771.55	96,876,980.09
2. Cash flow from investing activities:			
Receipt of investment proceed		11,000,000.00	1,000,000.00
Dividend income received		105,747.07	105,747.07
Net cash received from disposal of fixed assets, intangible assets and other long-term assets		1,451,730.96	1,451,730.96
Other cash received relating to investing activities	5.40	10,000,000.00	10,000,000.00
Sub-total of cash inflows		22,557,478.03	12,557,478.03
Cash paid to acquire fixed assets, intangible assets and long-term assets		64,588,229.76	56,764,606.44
Cash paid for investment		10,000,000.00	10,500,000.00
Other cash paid relating to investing activities	5.41	21,098,700.00	21,098,700.00
Sub-total cash outflows		95,686,929.76	88,363,306.44
Net cash flows from investing activities		(73,129,451.73)	(75,805,828.41)
3. Cash flows from financing activities			
Cash from proceeds for use of investment		—	—
Including: cash from proceeds arising from minority fund		—	—
Cash from borrowings		60,000,000.00	40,000,000.00
Other cash received relating to financing activities		4,000,000.00	—
Sub-total cash inflows		64,000,000.00	40,000,000.00
Loan interest paid		100,000,000.00	80,000,000.00
Cash payments for distribution of dividends on, profits and payments of interest expenses		5,414,793.84	2,584,872.33
Including: Dividend paid by subsidiaries to minority shareholders		—	—
Other cash paid relating to financing activities		—	—
Sub-total cash outflows		105,414,793.84	82,584,872.33
Net cash flows from financing activities		(41,414,793.84)	(42,584,872.33)
4. Effect of foreign exchange rate changes on cash		—	—
5. Net increase in cash and cash equivalents		(14,219,474.02)	(21,513,720.65)

Company's Legal Representative: Gao Minghui
 Financial Controller: Pi Jianguo
 Prepared by: Zhao Qiongfeng

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 2006

SUPPLEMENTARY INFORMATION	Note	Unit: RMB	
		The Group	The Company
1. Reconciliation of loss to cash flows from operating activities			
Net profit		78,153,288.80	77,074,856.00
Add: Gain or loss of minority shareholders		8,003,621.87	—
Provision for diminution in value of assets		14,717,263.41	(2,625,808.38)
Amortization of deferred income		(5,237,046.60)	(5,237,046.60)
Depreciation of fixed assets		29,050,089.26	22,558,641.94
Amortization of intangible assets		4,620,131.59	2,026,303.33
Amortization of long-term deferred expenses		(249,128.90)	—
Decrease in deferred expenses (less: increase)		11,726.80	—
Increase in accrued expenses (less: decrease)		1,578,335.69	1,492,960.07
Loss on disposal of fixed assets, intangible assets and other long-term assets (less: income)		1,510,275.55	841,685.26
Loss on deserted fixed assets		398,074.69	—
Financial expenses		5,684,533.07	2,858,559.16
Investment loss (less: income)		586,923.83	6,446,207.58
Credit on deferred tax (less: borrowing)		—	—
Decrease in inventory (less: increase)		11,335,447.92	4,376,923.85
Decrease in operating receivables (less: increase)		(116,135,206.53)	(68,180,094.70)
Increase in operating payables (less: decrease)		66,296,441.10	55,243,792.58
Others		—	—
Net cash inflows from operating activities		100,324,771.55	96,876,980.09
2. Financing and Investment activities not involving in cash:			
Debts capitalized		—	—
Convertible bond due within one year		—	—
Fixed assets under financial lease		—	—
3. Net increase in cash and cash equivalents:			
Cash and bank balances at the end of the period	5.38	143,507,132.60	90,597,289.14
Less: Cash and bank balances at the beginning of the period	5.38	157,726,606.62	112,111,009.79
Add: Cash equivalents at the end of the period		—	—
Less: Cash equivalents at the beginning of the period		—	—
Net increase in cash and cash equivalents		(14,219,474.02)	(21,513,720.65)

Company's Legal Representative: Gao Minghui

Financial Controller: Pi Jianguo

Prepared by: Zhao Qiongfen

DETAILED SUMMARY OF ALLOWANCE AND IMPAIRMENT OF CONSOLIDATED ASSETS

FOR THE YEAR ENDED 31ST DECEMBER, 2006

Unit: RMB

ITEMS	As 1st January, 2006	Addition this year	Decrease during the year			Total	As 31st December, 2006
			Written back due to the increase of asset value	Reduction/ transfer out this year			
1. Bad debt provision	51,524,013.56	13,358,548.36	—	—	—	—	64,882,561.92
Comprising: Accounts receivable	44,795,040.87	11,525,297.84	—	—	—	—	56,320,338.71
Other receivable	6,728,972.69	1,833,250.52	—	—	—	—	8,562,223.21
2. Provision for diminution in value of short-term investment	38,226,366.15	—	128,768.95	—	128,768.95	—	38,097,597.20
Comprising: Investment in shares	38,226,366.15	—	128,768.95	—	128,768.95	—	38,097,597.20
Investment in debts	—	—	—	—	—	—	—
3. Provision of diminution in inventory	31,260,972.07	2,601,086.95	—	—	8,561,022.45	8,561,022.45	25,301,036.57
Comprising: Finished goods	12,240,938.16	1,209,197.50	—	919,331.47	919,331.47	—	12,530,804.19
Raw materials	6,104,695.92	388,094.71	—	—	—	—	6,492,790.63
Work in progress	12,915,337.99	1,003,794.74	—	7,641,690.98	7,641,690.98	—	6,277,441.75
4. Provision for diminution in value of long-term investment	2,000,000.00	967,706.05	—	—	—	—	2,967,706.05
Comprising: Long-term equity investment	2,000,000.00	967,706.05	—	—	—	—	2,967,706.05
Long-term debt investment	—	—	—	—	—	—	—
5. Provision for diminution in value of fixed assets	6,929,723.60	1,434,644.34	—	19,135.07	19,135.07	—	8,345,232.87
Comprising: Buildings	—	—	—	—	—	—	—
Plant and machinery	6,505,966.50	1,410,670.56	—	19,135.07	19,135.07	—	7,897,501.99
Furniture, fixture and equipment	423,757.10	23,973.78	—	—	—	—	447,730.88
6. Provision for diminution in value of intangible assets	5,943,257.64	5,294,871.25	—	—	—	—	11,238,128.89
Comprising: Patents	4,574,595.82	3,949,265.29	—	—	—	—	8,523,861.11
Trademarks	1,368,661.82	1,345,605.96	—	—	—	—	2,714,267.78
7. Provision for diminution in value of construction in progress	1,818,489.10	313,663.88	—	—	—	—	2,132,152.98
8. Provision for diminution in value of designated loans	—	—	—	—	—	—	—
9. Total	137,702,822.12	23,970,520.83	128,768.95	8,580,157.52	8,708,926.47	—	152,964,416.48

Company's Legal Representative: Gao Minghui
Financial Controller: Pi Jianguo
Prepared by: Zhao Qiongfeng

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

FOR THE YEAR ENDED 31ST DECEMBER, 2006

Unit: RMB

ITEMS	2006		2005	
	The Group	The Company	The Group	The Company
1. Issue Share Capital				
At the beginning of the year	245,007,400.00	245,007,400.00	245,007,400.00	245,007,400.00
Increase during the year	-	-	-	-
Comprising: Transfer from capital surplus	-	-	-	-
Transfer from statutory surplus reserve	-	-	-	-
Transfer from retained profit	-	-	-	-
Increase in issued share capital	-	-	-	-
Decrease for the year	-	-	-	-
As at year end	<u>245,007,400.00</u>	<u>245,007,400.00</u>	<u>245,007,400.00</u>	<u>245,007,400.00</u>
2. Capital surplus				
At the beginning of the year	314,193,651.63	314,193,651.63	305,291,280.12	305,291,280.12
Increase during the year	604,305.34	604,305.34	8,902,371.51	8,902,371.51
Comprising: Share premium	-	-	-	-
Donation of non-cash items	-	-	-	-
Cash donation	-	-	-	-
Shares investment reserve	604,305.34	604,305.34	8,902,371.51	8,902,371.51
Transfer of general funds	-	-	-	-
Exchange reserve	-	-	-	-
Other capital revenue	-	-	-	-
Decrease for the year	-	-	-	-
Comprising: Transfer of capital	-	-	-	-
As at year end	<u>314,797,956.97</u>	<u>314,797,956.97</u>	<u>314,193,651.63</u>	<u>314,193,651.63</u>
3. Statutory and discretionary surplus revenue:				
At the beginning of the year	8,406,328.92	8,406,328.92	8,406,328.92	8,406,328.92
Increase during the year	11,891,785.37	11,891,785.37	-	-
Comprising: Transfer from retained earnings	3,485,456.45	3,485,456.45	-	-
Comprising: Statutory surplus reserve	3,485,456.45	3,485,456.45	-	-
Discretionary surplus reserve	-	-	-	-
General reserve fund	-	-	-	-
Enterprise development fund	-	-	-	-
Transfer from statutory public welfare fund	8,406,328.92	8,406,328.92	-	-
Decrease for the year	-	-	-	-
Comprising: Loss	-	-	-	-
Transfer of share capital	-	-	-	-
Distribution of dividend or profits	-	-	-	-
Distribution of stock dividend	-	-	-	-
As at year end	<u>20,298,114.29</u>	<u>20,298,114.29</u>	<u>8,406,328.92</u>	<u>8,406,328.92</u>
Comprising: Statutory surplus reserve	20,298,114.29	20,298,114.29	8,406,328.92	8,406,328.92
General reserve fund	-	-	-	-
Enterprise development fund	-	-	-	-
4. Statutory public welfare fund				
At the beginning of the year	8,406,328.92	8,406,328.92	8,406,328.92	8,406,328.92
Increase during the year	-	-	-	-
Comprising: Transfer from retained earnings	-	-	-	-
Decrease for the year	8,406,328.92	8,406,328.92	-	-
As at year end	<u>-</u>	<u>-</u>	<u>8,406,328.92</u>	<u>8,406,328.92</u>
5. Retained profit (loss)				
At the beginning of the year	(44,019,471.32)	(42,220,291.48)	(62,340,523.65)	(62,340,523.65)
Net profit (loss) for the year	78,153,288.80	77,074,856.00	18,321,052.33	20,120,232.17
Appropriation	3,485,456.45	3,485,456.45	-	-
As at year end unappropriated profit	<u>30,648,361.03</u>	<u>31,369,108.07</u>	<u>(44,019,471.32)</u>	<u>(42,220,291.48)</u>

Company's Legal Representative: Gao Minghui
Financial Controller: Pi Jianguo
Prepared by: Zhao Qiongfen

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL

Jiaoda Kunji High-Tech Company Limited (formerly known as Kunming Machine Tool Company Limited) ("the Company") was established in the People's Republic of China as a sino-foreign joint stock limited company as part of the reorganization of a State-owned enterprise known as Kunming Machine Tool Plant ("KMTP"). Pursuant to the reorganization, the operations, assets and liabilities of KMTP were divided between the Company and Kunming Kun Ji Group Company ("Kun Ji Group Company"). The Company was established on 19th October, 1993. The Company's A shares and H shares have been listed on the Shanghai Securities Exchange in Shanghai and the Stock Exchange of Hong Kong Limited in Hong Kong respectively. The Company is engaged principally in the design, development, production and sale of machine tool, precision measuring equipment and precision transducers.

On 25th December, 2000, Xian Jiaotong University Industrial (Group) Incorporation ("Jiaotong Group") entered into an agreement with Yunnan Provincial People's Government ("Yunnan Government"), the Company's former controlling shareholder whereby Yunnan Government would transfer a 29% interest of 71,052,146 State-owned shares in the Company to Jiaotong Group. The Ministry of Finance signed approval of State-owned shares transfer of Jiaoda Kunji High-tech Company Limited (Cai Qi [2001] No. 283), and approved the share transfer. Upon completion of share transfer procedure on 5th June, 2001, Jiaotong Group became substantial shareholder of the Company.

Pursuant to extraordinary general meeting of the Company held on 31st December, 2001. After the assets restructuring, the Company changed from a traditional machinery manufacturing company which focused on production of machine tools to a high-tech and diversified Production Company.

With effective from 29th March, 2002, the Company uses the name "Jiaoda Kunji High Tech Company Limited". The amount of registered capital RMB245,007,400.

On 15th September, 2005, Xian Jiaotong University Industrial (Group) Incorporation and Shenyang Machine Tool (Group) Company Limited entered into an agreement regarding transfer of shares. Shenyang Machine Tool (Group) Company Limited agreed to buy 71,052,146 shares of Jiaoda High-tech Company Limited from Xi'an Jiaotong University Industrial (Group) Incorporation, representing 29% of the total 245,007,400 shares. The transaction was approved by State-owned Assets Supervision and Administration Committee under the State Council and China Securities Regulation Committee. At 1st December, 2006, the register of transfer was finished and Shenyang Group became the largest shareholder of the Company.

On 4th April, 2006, Yunnan Government and State-owned Assets Supervision and Administration Committee, Yunnan Committee issued written reply to agree Yunnan Government transfer its 31,315,600 shares of the Company (representing 12.79% total issued shares) to Yunnan State-owned Assets Operation Company Limited at nil based on the date of 31st December, 2005. By 31st December, 2006, the share transfer was approved by the State-owned Assets Supervision and Administration Committee. The transfer was finished on 19th January, 2007.

The place of registration of the Company is 23 Ciba Road, Kunming City, Yunnan Province. The business registration number is Qi Gu Dian Zong Zi No. 000682.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS

1. Accounting Standards and Accounting System

The financial statements have been prepared in accordance with "Accounting Standards for Business Enterprises", "Accounting System for Business Enterprises" and the complementary regulation.

2. Accounting Fiscal Year

The accounting year of the Company commences on 1st January and ends on 31st December each year.

3. Reporting Currency

The reporting currency of the Company is Renminbi ("RMB").

4. Recording Principles and Accounting Basis

The Company adopts the accrual basis as the basis of accounting and the historical cost as the principle of valuation.

5. Foreign Currency Translation

Transactions in foreign currencies are translated at the market exchange rates (middle rate), ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated into RMB at the market exchange rates (middle rate), ruling on the balance sheet date. Profits and losses arising on exchange are included in financial expenses apart from those relating to the construction in progress.

6. Recognition Criteria for Cash Equivalents

Cash equivalents included in the cash-flow statement are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are within three months of maturity and subject to limited risk on changes in value.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

7. Accounting for Bad Debts

- 1) Recognition criteria for bad debt
 - (i) The irrecoverable amount of a debtor who has gone bankrupt or has died and has insufficient asset or estate to repay;
 - (ii) The irrecoverable amount, demonstrated by sufficient evidence, of a debtor who does not comply with his/her repayment obligation after the debt fall due.

The irrecoverable amount stated above is cancelled as bad debt after hierarchical approval ratified by the Board of Directors.

- 2) The cost of bad debts is calculated on the provision method. Provision for bad debts is made using the provision method based on aging analysis.

The provision percentage is reasonably estimated based on the past experiences of management of the Company, the financial position and cash flows condition of the relevant debtor, as well as other relevant information.

The estimated bad debt loss percentage excluding special provision is as follows: The estimated provision percentage is 5% when the accounts receivable age is within 1 year; the estimated provision percentage is 50% when the accounts receivable age is 1 to 2 years; the estimated provision percentage is 100% when the accounts receivable age is over 2 years

8. Accounting for Inventories

- 1) Inventory category: Inventories include merchandise inventory, self-made semi-finished goods, raw materials, consumables and packaging materials.
- 2) Valuation method of inventories: Purchase of raw materials, packaging materials and consumables are stated at cost incurred. Inventory issued and inventory shipped are recorded based on the weighted average cost method.
- 3) Amortization of consumables: Low value consumables are fully charged to cost when they are issued.
- 4) Inventories are recorded at the lower of cost and net realizable value and provision for loss on realization of inventories is recognized using the single-item comparison method. Net realizable value represents the estimated selling price less the estimated cost of completion and the estimated costs to be incurred in marketing, selling and distribution in general operation.

9. Accounting for Short-term Investment

- 1) Short-term investment is stated at the historical cost. Gain on an investment is recognized when the investment is transferred or repaid on maturity.
- 2) Short-term investment is recorded at the lower of cost and market value at the end of each period. Provision for impairment on short-term investment should be recognized according to the investment collectively.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

10. Accounting for Long-term Investment

- 1) Long-term bond investment is recorded at its initial cost on acquisition. Premium and discount are amortized during the period when bonds are held using the straight-line method. Accrual interest is made at the period end.

- 2) Long-term equity investment

The cost method is adopted when the amount of the investment is below 20 percent of the amount of registered capital of the invested enterprises; the equity method is adopted when the amount of the investment is above 20 percent the amount of registered capital of the investee enterprises; the equity method is adopted and the financial statements are consolidated when the amount of the investment is above 50 percent of the amount of registered capital of the invested enterprises or below 50 percent with control power.

- 3) Method of amortizing equity investment difference

The debit balance of the equity investment difference is amortized on a straight-line basis for the terms in investment as stated in the contract and charged to the profit and loss account. If there is no specific term stated in the contract, amortization is carried out over within 10 years; the credit balance of the equity investment difference is recorded in the account of capital reserve-provision for equity investment

- 4) If the recoverable amount of any long-term equity investment is lower than the carrying amount of that investment as a result of a continuing decline in market value or changes in operating conditions of investee enterprises and the reduced value cannot be recovered in the foreseeable future period, provision should be made for the difference between the recoverable amount and the carrying amount of the investment.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

11. Accounting for and Depreciation of Fixed Assets

- 1) Fixed assets are stated at initial cost.
- 2) Recognition criteria for fixed assets: Fixed assets include buildings, plant, machinery and equipment, transportation equipment and other equipment, tools having useful lives over one year and used in production and operation.

Other major equipment which is not used in production or operation but with unit value over RMB2,000 and having useful lives over two years are recognized as fixed assets.

- 3) Depreciation of fixed assets: Depreciation is provided using the straight-line method at the following rates per annum:

Category of fixed assets	Estimated useful lives	Residual value rate (%)	Annual depreciation rate (%)
Buildings	40	4	2.40
Plant and machinery	12-50	4	1.92-8.00
Furniture, fixture and equipment	10-14	4	6.86-9.60
Motor vehicles	10-14	4	6.86-9.60

The depreciation policy for assets held under finance bases are consistent with that for owned assets. If there is reasonable certainty that the lease will obtain ownership at the end of lease, the asset should be depreciated over the shorter of the lease term and the life of the asset.

- 4) Provision on impairment loss on fixed assets

The Company recognizes an impairment loss on fixed assets when realizable value fall lower than book value as a result of a continuing decline in market value, lagging behind in technology, damage and long-term idling. Provision on impairment loss on fixed assets is provided according to total amount of fixed assets if there exists:

- (i) Fixed assets have been idled for a long period of time and will not be reused in the foreseeable future.
They have no transfer value as well;
- (ii) Fixed assets cannot be utilized because of their obsolete technology;
- (iii) Large quantity of unqualified products are produced when fixed assets are used.
- (iv) Fixed assets have been damaged and have no usage value and transfer value.
- (v) Fixed assets in substance cannot produce economic benefits for the Company.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

12. Accounting for Construction in Progress

Construction in progress is stated at initial cost. Costs on completed construction works are transferred to other categories of fixed assets. Interest incurred before the construction works are ready for their intended use is capitalized as part of the engineered cost. Interest accrued after the construction works are ready for their intended use is provided in the income statement.

Provision on impairment loss on construction in progress

At the period end, based on the investigation on each construction in progress, if there exists:

- i) construction in progress has been ceased for construction for a long period of time and no re-commencement of work is expected in the future 3 years;
- ii) construction in progress was technically and physically obsolete and its economic benefits to the Company are uncertain;
- iii) other evidences can prove the existence of the circumstance of the decline in value on construction in progress, the difference of the recoverable amount and the carrying amount of construction in progress can be made as provision on impairment loss on construction in progress.

The Company recognizes an impairment loss when realizable value fall lower than book value. The impairment loss is calculated based on the difference between book value and net realizable value.

13. Intangible Assets

- 1) Amortization of intangible assets
 - (i) If the contract stipulates the benefiting period and the law does not prescribe the effective period, intangible assets are amortized over the effective period;
 - (ii) If the contract does not stipulate the benefiting period and the law prescribes the effective period, intangible assets are amortized over the effective period;
 - (iii) If the contract stipulates the benefiting period and the law prescribes the effective period, intangible assets are amortized over the shorter of the benefiting period and the effective period;
 - (iv) If the contract does not stipulate the benefiting period and the law does not prescribe the effective period, intangible assets are amortized over 10 years.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

13. Intangible Assets *(Continued)*

2) Provision on impairment loss on intangible assets

At the period end, based on investigation on the intangible assets and estimation of their ability of producing economic benefits, provision should be made for the difference between realizable value and book value, when:

- (i) one term of intangible assets has been replaced by other new technology and its ability of producing economic benefits has been affected significantly;
- (ii) the market value of one item of intangible assets drops sharply in the current period and is expected to be non-recoverable in the rest of the year;
- (iii) one item of intangible assets unprotected by the law still has usage value;
- (iv) other evidence indicates the loss on value of intangible assets.

14. Amortization of Initial Expenses and Long-term Deferred Expenditure

- (i) Initial cost is fully charged to income in the current month when operations begin;
- (ii) Long-term deferred expenditures are evenly amortized during the benefiting period.

15. Borrowing Cost

Interest except for those incurred in connection with specific borrowings for the purchase of fixed assets should be recognized as financial expenses and recorded in the income statement in the current period accordingly.

Interest incurred in connection with specific borrowings for the purchase of fixed assets is capitalized before the relevant fixed asset being acquired or constructed is ready for its intended use. If acquisition and construction of one item of fixed assets are abnormally discontinued for 3 months, interest is temporarily ceased to be capitalized and the interest incurred in this period is recognized as a financial expense. Interest incurred after the construction work is ready for its intended use is made as financial expenses.

16. Accounting for Bonds Payables

Bonds payables are stated at initial cost. Premiums and discounts are amortized during the existent period of bonds using the straight-line method.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

17. Recognition Criteria for Revenue

- (1) Sales of goods: Revenue from sales of goods is recognized when the Company has transferred to the buyers the risk and ownership of the goods and received the relevant revenue or obtained the evidence proving the sales proceeds and the cost relating to sale of goods can be measured reliably.
- (2) Provision of services: When the provision of services is started and completed within the same accounting year, revenue is recognized at the time of completion of the services. When the provision of services is started and completed in different accounting years and the outcome of a transaction involving the rendering of services can be estimated reliably, the Company recognizes the service revenue at the balance sheet date by the use of the percentage of completion period.
- (3) Revenue from assets used by other parties: Interest revenue is calculated based on the length of time for which other parties use cash of the Company and the applicable interest rate; occupancy revenue is calculated by the length of time and the method as stipulated in the contract.

Fund occupancy expense is provided to write off the financial expenses in the current period when fund occupancy expenses which relevant parties pay to the Company can be recognized as revenue and the Company received them. If the amount of fund occupancy expenses received exceed the amount of interest calculated at the rate of one-year-deposit placed with banks, the amount equivalent to that of the latter writes off the amount of the financial expense in the current period and the difference between the former and the latter is provided in capital surplus.

- (4) Revenue from Finance Leases and Operating Leases
 - (i) Rents from operating leases are recognized as revenue in each period using the straight-line method;
 - (ii) Revenue from finance leases in the current period is recognized adopting the real interest rate method.

Unrecognized revenue from finance leases is allocated to each period over the lease term in accordance with the straight-line method. Rents the Company has not received after one period of rent payment should not been recognized as revenue from finance leases. If recognized, recognized revenue should be offset. Revenue from finance leases included in rents is recognized as revenue in the current period when actual receipts incur.

For the two items of finance leases stated above, the initial cost which is incurred in the course of negotiation and contracting and can be attributed directly to items of leases should be recognized as current cost. Contingent rents incurred should be recognized as revenue in the current period.

- (iii) Sale and leaseback transactions

For finance leases resulting from sale and leaseback transactions, any difference between the sale proceeds and the original carrying amount of the assets involved are deferred and amortized as an adjustment to depreciation according to the depreciation pattern of the leased asset. For operating leases resulting from sale and leaseback transactions, any difference between the sales proceeds and the original carrying amount of the assets involved are deferred and amortized according to the proportion of the lease payments during the lease term.

NOTES TO THE FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND PREPARATION OF FINANCIAL STATEMENTS *(Continued)*

18. Accounting for Income Taxes

Income taxes are calculated using the taxes receivable method.

19. Tax Refund

Tax refund is recorded in current year's profit when actual receipts incur.

20. Basis of Consolidation

The consolidated financial statements incorporate the financial statements of the Company and investee enterprises in which the Company holds more than half of the equity or where the Company controls the operation of the investee enterprises.

If there exists some difference between the accounting policies used by subsidiaries included in the consolidation and that used by the Company, the financial statements of subsidiaries are adjusted in accordance to the accounting policies used by the Company.

Pursuant to Cai Kuai Zi (1995) No. 11 "Notice on issuing 'Provisional Regulation on Consolidation of Financial Statements'", the financial statements of the Company and subsidiaries included in the consolidation and relevant materials, the amount of each item in the financial statements is consolidated and the following items are eliminated on consolidation:

- (i) equity investment of the Company and relevant parts of ownership interests of subsidiaries in the scope of consolidation.
- (ii) all significant inter-company transactions and balances between the Company and subsidiaries in the scope of consolidation.

NOTES TO THE FINANCIAL STATEMENTS

3. TAXATION

1. Value Added Tax (VAT)

The amount of taxes payable is recorded after deducting input value added tax in the current period from output value added tax in the current period. Output value added tax is calculated at 17% of the revenue.

Except for Shaanxi Hengtong Intelligent Machine Company Limited, the other subsidiaries of the Company is regarded as the same value added tax payer as the Company and the applicable tax rate is 17%; Shaanxi Hengtong Intelligent Machine Company Limited is a small scale value added tax payer, the applicable tax rate is 6%.

2. Income Tax

According to the notice of Cai Shui Zi (1994) No. 017 jointly by issued by the Ministry of Finance and the State Administration of Taxation, the applicable income tax rate of the Company is 15%.

Shaanxi Hengtong Intelligent Machine Company Limited, Xian Jiaotong University Siyuan Intelligent Electric Apparatus Company Limited, Xian Ser Turbo Machinery Company Limited and Winko Machines Company Limited are all high-tech companies. The applicable income tax rate for them is 15%.

3. Business Tax

Business tax is calculated and paid at 3% or 5% of operating income.

4. Other taxes

Other tax is calculated and paid according to the Law of Taxation.

NOTES TO THE FINANCIAL STATEMENTS

4. SUBSIDIARIES AND JOINT VENTURES

1. General of the Company's Subsidiaries and joint venture

Name of subsidiaries and joint venture	Place of Registration	Scope of Business	Registered capital (RMB'000)	Investment Proportion	Nature	Data of investment	Relationship with the Company
Xi'an Ser Turbo Machinery Company Limited ("Xi'an Ser")	Xi'an city	Design, develop and sales of turbo machinery	5,000	45.00%	Limited liabilities	2001.12	subsidiary
Shaanxi HengTong Intelligent Company Limited ("Shaanxi Hengtong")	Xi'an city	Develop and sales of machines Develop and sales of machine manufacturing mould, machinery, equipment, electronic products, software and hardware	2,796	65.34%	Limited liabilities	2001.12	subsidiary
Xi'an Jiaotong University Siyuan Intelligent Electric Apparatus Company Limited	Xi'an city	Develop, manufacture and sale of electronic products, electronic machine and products of electronic power, provide technology services	3,500	78.03%	Limited liabilities	2002.12	subsidiary
Winko Machines Company Limited	Kunming City	Develop, apply and integrate hardware and software; retail, whole sale, purchase on behalf of other and consign electronic products, machinery and electronic machine	2,023	96.74%	Limited liabilities	2002.11	subsidiary
Tos Kunming Machine Tool Company Limited	Kun Ming (Letter to)	Develop, design, manufacture and sales of turbo machines and high-tech products, and repairs of machine	5 million Euros	50.00%	Limited liabilities	2005.4	Subsidiaries of Xi'an Ser
Changsha Ser Turbo Machinery Equipment Company Limited ("Changsha Ser")	Changsha city	Design, develop and sales of turbo machinery	1,000	95.00%	Limited liabilities	2004.01	Subsidiaries of Xi'an Ser
Hangzhou Ser Gas Engineering Company Limited ("Hangzhou Ser")	Hangzhou city	Design, develop, sales of turbo machinery, technology development, retail, whole sale of construction materials, and import and export business	120	51.00%	Limited liabilities	2004.04	Subsidiaries of Xi'an Ser
Kunji Transportation Company Limited	Kunming city	General cargo transportation	50	100%	Limited liabilities	2006.10	Subsidiary

NOTES TO THE FINANCIAL STATEMENTS

4. SUBSIDIARIES AND JOINT VENTURES *(Continued)*

(2) Increase/decrease within the consolidate statements for the year

Except TOS Kunming, all the above companies are included in the consolidated financial statements.

The Company holds 45% shareholding of Xi'an Ser. Since the majority of the Board of Directors of Xi'an Ser are from the Company, Xian Ser is included in the consolidated financial statements this year.

Since Changsha Ser and Hangzhou Ser are the subsidiaries of Xian Ser, they are included in the consolidated financial statements.

On 7th April, 2005, TOS Kunming Machine Tool Company Limited is established by the contribution of capital by the Company and Tos Varnsdorf, A.S.. The registered capital is EUR5,000,000. The Company owns 50% of capital but do not have the controlling right, thus, the jointly controlled entity is not included in the consolidated financial statement.

The Company has invested RMB500,000 to establish the wholly subsidiary-Kunji Transportation Company Limited. From the date of establishment, Kunji Transportation Company Limited included in the consolidated financial statements

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB)

1. Bank Balances and Cash

Items	At 31st December, 2006		At 1st January, 2006	
	Foreign Currency	RMB	Foreign Currency	RMB
Cash on hand	–	601,786.29	–	774,069.45
RMB	–	390,030.21	–	505,665.89
HKD	37,717.64	37,894.91	29,934.64	31,146.99
USD	17,680.15	138,058.99	27,847.15	224,751.56
IRD	390,000.00	332.86	390,000.00	320.97
EUR	3,454.86	35,469.32	1,271.86	12,184.04
Bank deposit	–	164,004,046.31	–	154,843,663.83
RMB	–	136,722,811.17	–	125,959,318.36
Including: time deposit	–	–	–	–
HKD	24,662,913.23	24,778,828.92	26,969,960.44	28,062,243.84
Including: time deposit	21,000,000.00	21,098,700.00	–	–
USD	320,463.87	2,502,406.22	101,859.97	822,101.63
Other currencies	–	2,188,430.03	–	16,258,338.12
Total		<u>166,794,262.63</u>		<u>171,876,071.40</u>

Note:

Cash in other currency as at 31st December, 2006 included restricted bank deposit (premium of guarantee letter). The reason that other currencies decrease was that banks stopped receiving deposits for L/C.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

2. Short-term investment

Items	At 31st December, 2006		At 1st January, 2006	
	Amount	Provision	Amount	Provision
Stock investment	50,000,000.00	38,097,597.20	50,000,000.00	38,097,597.20
Fund investment	–	–	1,000,000.00	128,768.95
Total	<u>50,000,000.00</u>	<u>38,097,597.20</u>	<u>51,000,000.00</u>	<u>38,226,366.15</u>

Note:

On February, 2004, an agreement for trusteeship of the management of investment in State Bonds was entered into the Company and Chinese Fortune Securities ("China Fortune") pursuant to which the Company entrusted China Fortune to conduct investment on State Bonds with RMB50,000,000 funded by internal sources. But China Fortune fails to comply with agreement to invest in state bonds, but using the fund to invest in A shares and to incurred huge losses. On September, 2004, China Fortune was taken over by China Huarong Assets Management Corporation ("China Huarong"). In January, 2006, Capital Airport Group Company started the restructuring process of China fortune, for the period of 6 months. However, the process was failed after 6 months. On 3rd August, 2006, China Securities Regulation Commission appointed Beijing Gao Peng Tianda Law Firm to establish an administrative liquidation working group for performing the liquidation work and registration of claims. Registration time for debt started from 5th August, 2006 to 3rd November, 2006, for the period of 90 days. By 31st December, 2006, the liquidation process is continuous.

Since there is no enough evidence to infer that the above investment can be received, the Company decided to recognize an impairment loss of RMB38,097,597.20 continuously.

3. Bills receivable

Items	At 31st December, 2006	At 1st January, 2006
Bank acceptance notes	50,360,390.23	19,057,802.00
Commerce acceptance notes	<u>1,771,000.00</u>	<u>–</u>
Total	<u>52,131,390.23</u>	<u>19,057,802.00</u>

Note: Bills receivable has increased 173.54% as compared with the beginning of the year due to sales revenue increased largely.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

4. Accounts receivable

Aged analysis	At 31st December, 2006			At 1st January, 2006		
	Amount	Proportion (%)	Bad debt provision	Amount	Proportion (%)	Bad debt provision
Within 1 year	120,848,831.28	63.24	4,360,776.01	68,507,547.34	52.18	2,900,089.10
1-2 years	28,023,833.06	14.66	11,859,964.65	32,140,167.61	24.48	14,163,940.76
2-3 years	19,406,818.76	10.16	17,530,793.76	11,873,909.73	9.04	10,252,661.79
Over 3 years	22,823,804.29	11.94	22,568,804.29	18,778,654.39	14.30	17,478,349.22
Total	<u>191,103,287.39</u>	<u>100.00</u>	<u>56,320,338.71</u>	<u>131,300,279.07</u>	<u>100.00</u>	<u>44,795,040.87</u>

Note:

- (1) The details regarding amount due from shareholders whose shares exceed 5% (including 5%) of the total shares of the Company are shown in Note 7 "RELATED PARTY RELATIONSHIP AND TRANSACTION".
- (2) Accounts receivable has increased 45.55% as compared with the beginning of the year due to Sales revenue increased.
- (3) The total amount of the 5 largest debtors is RMB27,886,209.33, constituting 14.59% of the total amount of accounts receivable.

5. Other receivables

Aged analysis	At 31st December, 2006			At 1st January, 2006		
	Amount	Proportion (%)	Bad debt provision	Amount	Proportion (%)	Bad debt provision
Within 1 year	12,775,185.13	55.92	1,014,499.24	24,785,559.15	81.17	2,037,662.58
1-2 years	4,965,296.51	21.73	2,440,014.79	1,934,311.49	6.33	875,881.25
2-3 years	1,403,611.91	6.14	1,403,611.91	2,867,067.41	9.39	2,867,067.41
Over 3 years	3,704,097.27	16.21	3,704,097.27	948,361.45	3.11	948,361.45
Total	<u>22,848,190.82</u>	<u>100.00</u>	<u>8,562,223.21</u>	<u>30,535,299.50</u>	<u>100.00</u>	<u>6,728,972.69</u>

Note:

- (1) The details regarding amount due from shareholders whose share exceed 5% (including 5%) of the total shares of the Company is shown in Note 7 "RELATED PARTY RELATIONSHIP AND TRANSACTION".
- (2) The total amount of other receivables from the 5 largest debtors is RMB9,523,688.49, constituting 41.68% of the total amount of accounts receivables.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

6. Prepayments

Aged analysis	At 31st December, 2006		At 1st January, 2006	
	Amount	Proportion (%)	Amount	Proportion (%)
Within 1 year	43,183,443.89	99.53	20,588,757.92	78.86
1-2 years	73,000.00	0.17	5,419,311.65	20.76
2-3 years	128,914.28	0.30	99,119.78	0.38
Over 3 years	—	—	—	—
Total	<u>43,385,358.17</u>	<u>100.00</u>	<u>26,107,189.35</u>	<u>100.00</u>

Note:

- (1) The details regarding prepayments to shareholders whose share exceed 5% (including 5%) of the total shares of the Company are shown in Note 7 "RELATED PARTY RELATIONSHIP AND TRANSACTION".
- (2) As at 31st December, 2006, the amount of prepayments increased 66.18% compared with the end of last year. This is mainly because of Xi'an Ser, one of the subsidiaries of the Company, has increased its prepayments.

7. Inventories

Items	At 31st December, 2006		At 1st January, 2006	
	Amount	Provision	Amount	Provision
Finished goods	70,695,987.26	12,104,630.04	86,461,190.77	11,180,530.82
Raw materials	65,538,654.99	5,032,193.12	51,256,666.00	6,589,220.48
Consumables	3,874,635.15	959,987.63	3,491,446.34	82,781.00
Work in progress	145,038,943.75	6,277,441.75	163,602,559.92	12,915,337.99
Materials purchased	511,409.88	500,609.88	525,620.78	493,101.78
Good sold	426,174.15	426,174.15	426,174.15	—
Total	<u>286,085,805.18</u>	<u>25,301,036.57</u>	<u>305,763,657.96</u>	<u>31,260,972.07</u>

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

8. Long-term equity investment

(1) General of invested enterprises

Name of invested enterprise	Initial investment cost	Investment Proportion	Investment Period	Accounting method	Remark
Yunnan Cheng Jiang Copper Products Plant	2,000,000	40.00%	Nil	Cost method	
Tos Kunming Machine Tool Co., Ltd.	24,739,533.99	50.00%	20 years	Equity method	
Ruite National Fast Prototyping and Manufacturing Research Center Co., Ltd. ("Ruite")	10,000,000.00	16.67%	Nil	Equity method	

(2) Change in long-term equity investment

Name of invested enterprise	At 1st January, 2006	Changes in current year		Changes in accumulated equity		At 31st December, 2006
		Investment cost	Equity adjustment	Investment cost	Equity adjustment	
Yunnan Cheng Jiang Copper Products Plant	2,000,000.00	–	–	–	–	2,000,000.00
Tos Kunming Machine Tool Co., Ltd.	23,818,814.75	–	1,522,903.75	24,739,533.99	602,184.51	25,341,718.50
Ruite National Fast Prototyping and Manufacturing Research Center Co., Ltd. ("Ruite")	–	10,000,000.00	–	10,000,000.00	–	10,000,000.00
Less: provision for diminution in value of long-term investment	2,000,000.00	–	–	–	–	2,000,000.00
Total	23,818,814.75	10,000,000.00	1,522,903.75	34,739,533.99	602,184.51	35,341,718.50

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

8. Long-term equity investment (Continued)

(3) Difference in long-term equity investment

Name of invested enterprise	Initial investment cost	At 1st January, 2006	Increase	Amortization in the current year	At 31st December, 2006	Amortization period
Xi'an Ser	7,296,277.00	4,377,766.12	–	729,627.72	3,648,138.40	10 years
Shaanxi Hengtong	6,849,713.19	4,012,138.75	–	668,554.68	3,343,584.07	10 years
Less: provision for diminution in value of long-term investment	–	–	967,706.05	–	967,706.05	
Total	<u>14,145,990.19</u>	<u>8,389,904.87</u>	<u>967,706.05</u>	<u>1,398,182.40</u>	<u>6,024,016.42</u>	

Note:

- (1) Full provision for impairment loss on long-term investment of Yunnan Cheng Jiang Copper Products Plant was made because the plant has lost of the ability of sustainable operation. According to the agreement entered into Ruite and Shaanxi Hengtong, Shaanxi Hengtong has provision for diminution on difference of equity investment RMB967,706.05 during the year.
- (2) There is no significant difference between the accounting policies used by the invested enterprises and that used by the Company. There is no significant restrictions to realization of investment and investment income outflow as foreign currency.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

9. Fixed assets and accumulated depreciation

Category	At 1st January, 2006	Increase this year	Decrease this year	At 31st December, 2006
Building	197,322,579.21	32,910,873.16	1,904,424.26	228,329,028.11
Furniture, fixtures and equipment	28,600,273.05	1,428,677.40	659,708.59	29,369,241.86
Plant and machinery	278,585,143.08	16,901,485.62	6,713,040.04	288,773,588.66
Motor vehicles	20,190,184.71	5,383,482.86	1,540,355.66	24,033,311.91
Leasehold improvement	1,263,823.11	–	622,965.11	640,858.00
Sub-total	<u>525,962,003.16</u>	<u>56,624,519.04</u>	<u>11,440,493.66</u>	<u>571,146,028.54</u>
ACCUMULATED DEPRECIATION:				
Building	33,193,030.19	7,544,713.84	392,961.91	40,344,782.12
Furniture, fixtures and equipment	18,152,025.97	2,130,550.39	633,584.83	19,648,991.53
Plant and machinery	128,529,902.08	15,692,889.79	2,917,250.94	141,305,540.93
Motor vehicles	7,881,311.25	2,436,773.46	838,240.20	9,479,844.51
Leasehold improvement	509,340.92	–	189,381.39	319,959.53
Sub-total	<u>188,265,610.41</u>	<u>27,804,927.48</u>	<u>4,971,419.27</u>	<u>211,099,118.62</u>
Net book value	<u>337,696,392.75</u>	<u>28,819,591.56</u>	<u>6,469,074.39</u>	<u>360,046,909.92</u>
PROVISION FOR IMPAIRMENT:				
Building				
Furniture, fixtures and equipment	423,757.10	23,973.78		447,730.88
Plant and machinery	6,505,966.50	1,230,447.09	19,135.07	7,717,278.52
Motor vehicles	0.00	180,223.47		180,223.47
Sub-total	<u>6,929,723.60</u>	<u>1,434,644.34</u>	<u>19,135.07</u>	<u>8,345,232.87</u>
NET REALIZABLE VALUE	<u>330,766,669.15</u>	<u>27,384,947.72</u>	<u>6,449,939.32</u>	<u>351,701,677.05</u>

Note:

- (1) Fixed assets was classified during the year and there was a change at the beginning of the year. Provision on impairment is recognized when the book value is higher than the net realizable value.
- (2) Buildings amounting to RMB46,192,910.56 in original cost and RMB44,201,292.56 in net realizable value have been pledged to secure loans.
- (3) The original book value of fixed assets from finance leases is RMB4,264,181.00. The amount of accumulated depreciation is RMB2,624,700.96 and the net realizable value is RMB1,639,480.04 accordingly.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

10. Construction in progress

Construction name	At 1st January, 2006	Increase this year	Transfer to fixed assets	Other transfer out	At 31st December, 2006	Sources of fund
"Nine.Five" Technical improvement projects	50,921.83	—	—	9,499.83	41,422.00	loans
Siyuan Office Building	28,024,099.10	616,112.13	—	—	28,640,211.23	Funds owned
New factory	5,336,659.96	26,423,746.71	21,106,275.68	—	10,654,130.99	Funds owned
Others	15,001,126.35	33,501,194.30	24,258,928.29	2,894,656.32	21,348,736.04	Funds owned
Total	<u>48,412,807.24</u>	<u>60,541,053.14</u>	<u>45,365,203.97</u>	<u>2,904,156.15</u>	<u>60,684,500.26</u>	
Less: provision in impairment loss on construction	<u>1,818,489.10</u>	<u>313,663.88</u>	<u>—</u>	<u>—</u>	<u>2,132,152.98</u>	
NET REALIZABLE VALUE	<u>46,594,318.14</u>	<u>60,227,389.26</u>	<u>45,365,203.97</u>	<u>2,904,156.15</u>	<u>58,552,347.28</u>	

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

11. Intangible assets

Items	Acquired method	Original cost	At 1st January, 2006	Increase this year	Transfer out this year	Amortization this year	At 31st December, 2006	Remaining amortization period
Goodwill (note 1)	Acquisition of business	5,638,632.00	3,383,179.48	–	–	451,090.60	2,932,088.88	5
Goodwill (note 2)	Acquisition of business	3,720,569.00	2,232,341.41	–	–	269,121.19	1,963,220.22	5
The all over controlled vortex technology		11,630,000.00	6,977,999.84	–	–	1,163,000.04	5,814,999.80	5
Technical know-how of fast moulding		14,730,000.00	8,837,999.50	–	–	1,060,785.71	7,777,213.79	5
Intelligent know-how		9,044,400.00	5,426,640.02	–	–	452,220.00	4,974,420.02	5
Technical know-how of embroidery		4,039,667.00	2,401,006.42	–	–	77,553.16	2,323,453.26	5.75
Land use rights	Contributed	30,141,860.00	25,892,085.06	–	–	603,402.64	25,288,682.42	41.95
Usage right to staff quarter	Acquisition of business	4,485,988.00	3,551,407.97	–	–	93,458.04	3,457,949.93	37
Financial software	Acquisition of business	1,227,258.23	921,957.56	97,560.00	–	126,205.68	893,311.88	
Company's website development	Acquisition of business	38,000.00	13,933.46	–	–	7,599.96	6,333.50	1
"Nine.Five" Technical improvement software	Acquisition of business	1,753,662.85	1,215,451.98	–	–	303,229.57	912,222.41	3
Office software	Acquisition of business	–	–	398,300.00	–	12,465.00	385,835.00	4
Sub-total		86,450,037.08	60,854,002.70	495,860.00	–	4,620,131.59	56,729,731.11	
Less: provision on intangible assets								
Goodwill (note 1)		–	676,635.90	–	–	–	676,635.90	
Goodwill (note 2)		–	692,025.92	1,271,194.30	–	–	1,963,220.22	
Fast prototype technical know-how		–	–	3,561,499.50	–	–	3,561,499.50	
Intelligent know-how		–	2,713,320.01	–	–	–	2,713,320.01	
Technical know-how of embroidery machine		–	1,861,275.81	462,177.45	–	–	2,323,453.26	
Sub-total		–	5,943,257.64	5,294,871.25	–	–	11,238,128.89	
Net REALIZABLE VALUE		–	54,910,745.06	(4,799,011.25)	–	4,620,131.59	45,491,602.22	

NOTE:

- (1) Goodwill is made for the difference between the transaction price and the book value when Xi'an Jiaotong University Industrial Group acquired two subsidiaries from Intelligent Electronic Machine and Automatic Machine, in December 2001 during the course of the assets restructuring. The company made the investment of the assets in the two subsidiaries and relevant goodwill stated above and established Xi'an Jiaotong University Siyuan Intelligent Electric Apparatus Company Limited and Winko Machines Company Limited in this year. These two items of goodwill are amortized over 10 years.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

11. Intangible assets (Continued)

- (2) Technical know-how is that the Company acquired from Xian Jiaotong University Industrial (Group) Incorporation in December 2001 during the course of the assets restructuring. The Company made the investment of "Intelligent Technical Know-how" and "Embroidery Machine Technical Know-how" and established Xian Jiaotong University Siyuan Intelligent Electric Apparatus Company Limited and Winko Machines Company Limited. In 2003, the capital injection of the Company in Shaanxi Hengtong was based on the carrying value of "Fast Moulding Technical Know-how".
- (3) Land use right was contributed by Yunnan Government as capital. The addition for current period was due to the purchase of land for Changsha Ser. Land use right amounting to RMB13,586,764.80 has been pledged to secure loans.
- (4) After checking up at the end of the year, Shaanxi Hengtong has RMB3,561,499.50 provision on impairment on loss according to the estimation report. Provision for diminution in value of goodwill and technical know-how of embroidery were the balance of the two items because embroidery business was fully stop.

12. short-term loans

Category	At 31st December, 2006			At 1st January, 2006		
	Amount	Exchange Rate	Currency	Amount	Exchange Rate	Currency
Guaranteed loans	—		RMB	—		RMB
Secured loans	40,000,000.00		RMB	34,000,000.00		RMB
Pledged loans	—		RMB	—		RMB
Credit loans	—		RMB	26,000,000.00		RMB
Total	40,000,000.00			60,000,000.00		RMB

Note:

All the secured bank loans are secured by buildings and land use right in possession of the Company and it's subsidiary, Changsha Ser, details refer to note 5.9(2) and 5.11(3).

13. Accounts payable

As the end of year and at the beginning of the year, the balance of accounts payable amounted to RMB113,675,973.10 and RMB100,037,194.40

The details regarding amount due from shareholders whose shares exceed 5% (including 5%) of the total shares of the Company are shown in Note 7 "RELATED PARTY RELATIONSHIP AND TRANSACTION".

14. Advances from customers

- (1) As at 31st December, 2006 and at 1st January, 2006, the balance of advances from customers amounts to RMB218,325,953.57, RMB196,375,494.03 respectively.
- (2) No The details regarding amount due from shareholders whose shares exceed 5% (including 5%) of the total shares of the Company are shown in Note 7 "RELATED PARTY RELATIONSHIP AND TRANSACTION".

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

15. Accrued salary

As at 31st December, 2006 and at 1st January, 2006, the balance of Accrued salary amount to RMB6,511,810.09, RMB3,574,234.94 respectively.

16. Taxes Payable

Items	At 31st December, 2006	At 1st January, 2006
Value-add tax	12,500,830.04	14,647,753.61
Business tax	190,735.38	272,831.85
City construction tax	239,034.78	196,105.13
Income tax	9,581,962.84	5,730,376.03
Personal income tax	158,590.57	384,162.26
Land appreciation tax	—	8,984,000.00
Others	703,935.99	21,885.07
Total	<u>23,375,089.60</u>	<u>30,237,113.95</u>

Note:

Details of Land appreciation tax (LAT), please refer to point no.1 of note 12-other significant events.

17. Other payables

Items	At 31st December, 2006	At 1st January, 2006
Additional educational fee	140,957.48	178,833.24
Flood controlling fund	(875.26)	16,302.78
Housing fund	—	568,537.40
Total	<u>140,082.22</u>	<u>763,673.42</u>

18. Other accrual

As at 31st December, 2006 and at 1st 1st January, 2006, the balance contains RMB45,844,183.60 and RMB29,713,634.55 respectively, increased 54.29% during the year due to RMB10,000,000 prepayment from Ruite as the fund to purchase the equities of Shaanxi Hengtong. The details of balance due to shareholders whose shares exceed 5% (including 5%) of total shares of the Company are disclosed in Note 7 "Connected Party Relationship and Transaction".

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

19. Accrued expenses

Items	At 31st December, 2006	At 1st January, 2006
Accrued rental	91,131.90	74,516.28
Accrued audit fee	2,722,915.45	1,272,915.45
Accrued water and electricity fee	163,541.72	94,781.72
Accrued consulting fee, legal fee etc.	162,960.07	120,000.00
Others	—	—
Total	<u>3,140,549.14</u>	<u>1,562,213.45</u>

Note:

Accrued expensed has increased 101% as compared with the beginning of the year due to unsettled audit fee.

20. Long-term loans due within one year

Items	At 31st December, 2006	At 1st January, 2006
Obligation under finance leases due within 1 year	<u>684,337.80</u>	<u>342,168.90</u>
Total	<u>684,337.80</u>	<u>342,168.90</u>

21. Long-term loans

Category	At 31st December, 2006			At 1st January, 2006		
	Amount	Exchange rate	Currency	Amount	Exchange rate	Currency
Credit loans	<u>20,000,000.00</u>		RMB	<u>40,000,000.00</u>		RMB
Total	<u>20,000,000.00</u>		RMB	<u>40,000,000.00</u>		RMB

Note: Long-term loans have decreased 50% as compared with the beginning of the year due to repaid bank loans.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

22. Long-term payable

Category	Period	Original amount	As at 1st January, 2006	Increase in this year	Decrease in This year	As at 31st December, 2006
Obligation under finance lease	20 years	6,843,378.00	5,474,702.40	–	–	5,474,702.40
Less: future finance charge		2,579,197.00	2,063,357.80	–	128,959.80	1,934,398.00
Less: amount due for settlement with one year		–	342,168.90	342,168.90	–	684,337.80
Sub-total		4,264,181.00	3,069,175.70	(342,168.90)	(128,959.80)	2,855,966.60
Infrastructure construction						
Appropriation from the office of Finance of Shaanxi province		–	200,000.00	–	–	200,000.00
Appropriation for intelligent electronic machine industrialization exemplary project technology and equipment technology.		–	7,000,000.00	–	–	7,000,000.00
Total		4,264,181.00	10,269,175.70	(342,168.90)	(128,959.80)	10,055,966.60

Note:

- (1) The difference between the present value of minimum lease payment amounting to RMB6,843,378 and the net book value of assets held under finance leases amounting to RMB4,264,181 is made as future charge and is amortized over 20 years using the straight-line method.
- (2) Appropriation for intelligent machine technology and equipment technology industrialization exemplary projects represents appropriation for the project based on Approval of Feasibility of Intelligent Electronic Machine Technology and Equipment Technology Industrialization Exemplary Projects signed by the State Development Plan Committee (Kuai Qi Gao Ji (2000) No.1883).

23. Specific Project Payables

Items	At 31st December, 2006	At 1st January, 2006
Specific project appropriation from the Science and Technology Committee of Yunnan Province	3,211,680.50	2,675,616.01
Specific project appropriation for industrial automation from Shaanxi Provincial Development and Reform Commission	8,000,000.00	4,007,012.77
Specific project appropriation from Shaanxi Intellectual Property Office	100,000.00	100,000.00
Total	11,311,680.5	6,782,628.78

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

24. Deferred Gain

Items	Original amount	At 1st January, 2006	Addition this year	Provided for the year	Accumulated amortization	Transfer out this year	At 31st December, 2006
Buildings	1,939,662.40	–	1,939,662.40	228,195.58	228,195.58	–	1,711,466.82
Including:							
Operating lease	847,563.62	–	847,563.62	128,482.21	128,482.21	–	719,081.41
Finance lease	1,092,098.78	–	1,092,098.78	99,713.37	99,713.37	–	992,385.41
Land use right	3,995,657.08	–	3,995,657.08	470,077.30	470,077.30	–	3,525,579.78
Including:							
Operating lease	3,995,657.08	–	3,995,657.08	470,077.30	470,077.30	–	3,525,579.78
Finance lease	–	–	–	–	–	–	–
Total	<u>5,935,319.48</u>	<u>–</u>	<u>5,935,319.48</u>	<u>698,272.88</u>	<u>698,272.88</u>	<u>–</u>	<u>5,237,046.60</u>

Note:

The Company leased back a portion of land use right and premise use right which had been disposal to Yunnan Government in December 2001 when the Company implemented the assets restructuring. The lease term is 20 years. The selling price of these assets is RMB28,438,361 and the book value of these assets is RMB16,127,375. The gain due from the transactions of RMB12,310,986 is to be deferred. For operating lease, deferred gain is to be allocated through the lease period according to rental expenses; for finance lease, deferred gain is to be allocated to adjust depreciation expense according to depreciation rate. According to Document No. 6 in 2005, "In Response to the Land Appreciation Tax Policy regarding Capital Restructuring between Jiaoda Kunji High-Tech Company Limited and Xian Jiaotong University Industrial (Group) Incorporation" issued by Tax Policy Department, Ministry of Finance of People Republic of China in March 2005, the Company should pay for land appreciation tax ("LAT") regarding the above issue. This item would be provided for during the year 2006. According to settlement result with the government tax department, the actual LAT payment of the Company for the year would be RMB5,048,680.52. The difference between actual payment and recognized amount made by the government last year would be written back. Detail refers to item 1 of "Other Important Events" in note 12.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

25. Share Capital

Items	At 1st January, 2006	Increase this year	Decrease this year	At 31st December, 2006
1. Non-trading shares	120,007,400.00	–	–	120,007,400.00
Promoters shares	31,345,554.00	–	–	31,345,554.00
Including: State-Owned shares	31,345,554.00	–	–	31,345,554.00
Legal person shares	88,661,846.00	–	–	88,661,846.00
2. Trading shares	125,000,000.00	–	–	125,000,000.00
Including: A shares	60,000,000.00	–	–	60,000,000.00
H shares	65,000,000.00	–	–	65,000,000.00
Total shares	245,007,400.00	–	–	245,007,400.00

26. Capital Reserve

Items	At 31st December, 2006	At 1st January, 2006
Share premium	295,055,910.50	295,055,910.50
Provision for equity investment	9,506,676.85	8,902,371.51
Donation	10,800.00	10,800.00
Others	10,224,569.62	10,224,569.62
Total	314,797,956.97	314,193,651.63

Note:

The Company's capital reserve is increased by RMB604,305.34, from income derived from debt restructuring of its subsidiaries.

The Company checked the capital reserve account for the previous years and adjusts some items.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

27. Surplus Reserve

Items	At 1st January, 2006	Increase this year	Decrease this year	At 31st December, 2006
Statutory surplus reserve	8,406,328.92	11,891,785.37	–	20,298,114.29
Statutory public reserve	8,406,328.92	–	8,406,328.92	–
Total	<u>16,812,657.84</u>	<u>11,891,785.37</u>	<u>8,406,328.92</u>	<u>20,298,114.29</u>

Note:

The statutory surplus reserve increased for the year: RMB3,489,456.45 was contributed from profit, and according to the document “Notice on enterprises’ accounting after implementation of the Company’s Law” issued by Ministry of Finance (財企[2006]67號), RMB8,406,328.92 was transferred from statutory public reserve to statutory surplus reserve.

28. Unappropriated Profit

Items	Year 2006	Year 2005
Retained profit at the beginning of the year	(44,019,471.32)	(62,340,523.65)
Add: Net profit this year	78,153,288.80	18,321,052.33
Less: Statutory surplus reserve	3,485,456.45	–
Statutory public reserve	–	–
Retained profit at the year end	<u>30,648,361.03</u>	<u>(44,019,471.32)</u>

29. Principal Operation Income and Cost

Items	2006 (Accumulated)		2005 (Accumulated)	
	Principal business revenue	Principal business cost	Principal business revenue	Principal business cost
Machine tool	591,436,621.03	446,607,570.86	396,844,720.66	302,532,952.43
High-effective energy-saving compressors	177,025,679.48	129,956,619.35	209,774,250.37	157,524,813.18
Embroidery machine	3,418,165.68	3,254,712.79	1,885,824.73	2,802,388.67
Intelligent electric appliance	7,110,202.83	3,163,951.11	9,972,656.50	5,046,630.64
Machine processing service	52,732,680.85	25,632,749.10	27,968,233.00	12,688,070.98
Laser prototyping system	7,951,709.42	6,417,756.36	12,795,896.53	9,129,851.13
Precision measuring equipment	2,202,783.67	2,297,922.81	8,226,629.05	3,549,971.21
Others	6,541,605.39	1,463,657.42	5,174,713.02	2,251,790.25
Total	<u>848,419,448.35</u>	<u>618,794,939.80</u>	<u>672,642,923.86</u>	<u>495,526,468.49</u>

Note:

Sales revenue of the Company increased 26.13% as compared with last year due to sales of products of machine tool increased largely.

Total sales of the 5 largest customers was up to RMB92,278,874.13 which constitutes 10.88% of total sales of the Company.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

30. Principal Operation Tax and Addition

Items	Year 2006	Year 2005
Business tax	46,976.53	(13,060.34)
City construction tax	947,472.71	1,130,424.59
Education fee addition	475,424.66	709,470.31
Total	<u>1,469,873.90</u>	<u>1,826,834.56</u>

Note:

City construction tax and education fee addition are calculated and paid at 7% of value added tax and 3% of business tax.

31. Profit from Other Operations

Items	Year 2006			Year 2005		
	Income	Cost	Profit	Income	Cost	Profit
Materials sold	2,854,034.14	1,640,269.61	1,213,764.53	1,827,760.91	2,420,952.00	(593,191.09)
Rental income	37,200.00	226,601.19	(189,401.19)	333,082.47	369,215.28	(36,132.81)
Technical service	2,386,379.43	95,975.00	2,290,404.43	164,976.31	19,120.00	145,856.31
Processing service	304,549.91	—	304,549.91	—	—	—
Total	<u>5,582,163.48</u>	<u>1,962,845.80</u>	<u>3,619,317.68</u>	<u>2,325,819.69</u>	<u>2,809,287.28</u>	<u>(483,467.59)</u>

32. Finance Expenses

Items	Year 2006	Year 2005
Interest expenses	4,863,456.74	6,056,200.39
Less: Interest income	1,601,495.67	3,155,867.34
Exchange loss	1,208,549.73	489,252.11
Bank processing fee	171,548.98	213,123.76
Others	128,959.80	128,959.80
Total	<u>4,771,019.58</u>	<u>3,731,668.72</u>

33. Investment Income

Items	Year 2006	Year 2005
Equity investment income	1,522,903.75	(920,719.24)
Amortization of equity investment difference	(1,376,637.55)	(1,398,182.40)
Provision for diminution in value of investment	(967,706.05)	(680,411.67)
Income from short-term investment	234,516.02	—
Total	<u>(586,923.83)</u>	<u>(2,999,313.31)</u>

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

34. Subsidies

Items	Year 2006	Year 2005
Value-added tax refunded	3,000,762.73	2,922,171.67
Reduce or remit fees for assignment of land	2,484,285.00	—
Total	<u>5,485,047.73</u>	<u>2,922,171.67</u>

Note:

Changsha Ser received reduce or remit fees for assignment of land from the local government this year.

35. Non-operating Income

Items	Year 2006	Year 2005
Gain on disposal of fixed assets	169,121.32	225,813.28
Income from provision of training	—	—
Others	755,637.00	146,867.00
Total	<u>924,758.32</u>	<u>372,680.28</u>

36. Non-operating Expenses

Items	Year 2006	Year 2005
Loss on disposal of fixed assets	2,239,996.49	2,576,585.95
Contribution expenses	20,300.00	28,000.00
Provision on impairment loss on fixed assets	1,434,644.34	4,229,106.65
Provision on impairment loss on construction-in progress	313,663.88	935,645.68
Provision on impairment loss on intangible assets	5,294,871.25	5,943,257.64
Others	71,309.10	70,471.23
Total	<u>9,374,785.06</u>	<u>13,783,067.15</u>

37. Income Taxes

Income tax expense was RMB15,068,588.77 for this year, increased 54.53% as compared with the income tax expense RMB9,751,501.09 last year due to profit increase in this year.

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

38. Cash and cash equivalent

Items	At 31st December, 2006		At 1st January, 2006	
	Consolidated amount	Amount for the Company	Consolidated amount	Amount for the Company
Cash	166,794,262.63	113,884,419.17	171,876,071.40	116,260,474.57
Less: time deposit	21,098,700.00	21,098,700.00	–	–
Less: other currency	2,188,430.03	2,188,430.03	14,149,464.78	4,149,464.78
Cash and cash equivalents	143,507,132.60	90,597,289.14	157,726,606.62	112,111,009.79

39. Other Cash Paid Relating to Operating Activities was RMB83,450,606.19, including:

Items	Amount
Installation fee	5,870,326.94
Warrant fee	5,212,505.98
Office expense	7,095,876.54
Package fee	353,097.88
Insurance fee	898,083.40
Business traveling expense	6,769,942.74
Telephone expense	466,244.57
Board of directors and supervisory committee expense	752,481.40
Leasing expense	319,170.53
Listing management fee	1,141,185.70
Advertising and exhibition fee	700,896.25
Conference fee	316,177.90
Labor protection fee	154,710.21
Labor insurance fee	4,848,280.11
Pollutant discharge fee	160,852.00
Vehicles maintenance fee	647,460.04
Repair and maintenance fee	2,407,115.13
Research & development fee	4,476,129.34
Design fee	2,228,182.99
Communication fee	502,913.27
Compensation fee for Land loss	1,827,911.09
Entertainment fee	3,565,502.82
Service fee due to acceptance of a bid	695,683.50
Human resource administration fee	426,736.00
Assessment fee	2,090,013.00
Consultation fee	6,189,500.00
Others	23,333,626.86
Total	83,450,606.19

NOTES TO THE FINANCIAL STATEMENTS

5. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (REPORTING CURRENCY: RMB) (Continued)

40. Other cash received relating to investing activities amounting to RMB10,000,000.00 represents the prepayment from Ruite for purchasing Shaanxi Hengtong's equity.
41. Other cash paid relating to investing activities amounting to RMB21,098,700.00 represents the time deposit over three months of the currency assets at the end of the period.
42. Non-recurring Items

Items	Amount
Gain on disposal of fixed assets	(1,927,737.84)
Written back on various provision for diminution in previous years	8,708,926.47
Government grants	2,896,585.00
Income (loss) on short-term investment	105,747.07
Net income (loss) of non-operating impact from profits tax	(6,522,288.90)
	32,308.78
Total	3,293,540.58

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (UNIT:RMB)

1. Accounts receivable

Aged analysis	At 31st December, 2006			At 1st January, 2006		
	Amount	Proportion (%)	Provision on bad debt	Amount	Proportion (%)	Provision on bad debt
Within 1 year	82,007,539.23	68.86	2,600,087.25	35,191,194.61	53.36	1,226,728.48
1-2 years	12,854,514.11	10.79	4,952,655.17	9,986,367.03	15.14	4,838,633.52
2-3 years	7,232,469.05	6.07	6,740,844.05	5,484,579.25	8.32	5,484,579.25
Over 3 years	17,002,579.40	14.28	16,752,579.40	15,283,649.76	23.18	14,656,414.59
Total	119,097,101.79	100.00	31,046,165.87	65,945,790.65	100.00	26,206,355.84

Notes:

- (1) No balance due from shareholders with shares exceeds 5% (including 5%) of the total shares of the Company.
- (2) Total amount of the 5 largest debtors is RMB23,957,380.33, constituting 20.12% of the total amount of accounts receivable.

NOTES TO THE FINANCIAL STATEMENTS

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (UNIT:RMB) (Continued)

2. Other Receivables

Aged analysis	At 31st December, 2006			At 1st January, 2006		
	Amount	Proportion (%)	Provision on bad debt	Amount	Proportion (%)	Provision on bad debt
Within 1 year	10,157,994.06	45.41	507,899.70	26,440,698.78	98.44	517,484.94
1-2 Years	11,839,308.43	52.93	1,003,450.81	308,729.80	1.15	154,364.90
2-3 Years	279,464.40	1.25	279,464.40	9,396.75	0.04	9,396.75
Over 3 Years	92,211.55	0.41	92,211.55	99,961.60	0.37	99,961.60
Total	<u>22,368,978.44</u>	<u>100.00</u>	<u>1,883,026.46</u>	<u>26,858,786.93</u>	<u>100.00</u>	<u>781,208.19</u>

Note:

- (1) No balance due from shareholders with shares exceeds 5% (including 5%) of the total shares of the Company.
- (2) Total amount of the 5 largest debtors is RMB17,765,375.30, which constitutes 79.42% of the total amount of other receivables.

3. Long-term Equity Investment

(1) General information of Invested companies

Invested company	Original cost	Investment Proportion (%)	Investment Period	Accounting method
Xi'an Ser	22,500,000	45.00%	N/A	Equity Method
Shaanxi Hengtong	23,838,606	65.34%	N/A	Equity Method
Siyuan Intelligent	27,310,000	78.03%	N/A	Equity Method
Winko	19,320,000	96.74%	N/A	Equity Method
TOS Kunming	24,739,534	50.00%	20 years	Equity Method
Yunnan Cheng Jiang Copper Products Plant	2,000,000	40.00%	—	Cost method
Kunji Transportation Company Limited	500,000	100.00%	10 years	Equity Method
Ruite	10,000,000	16.67%	N/A	Cost method

NOTES TO THE FINANCIAL STATEMENTS

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (UNIT:RMB) (Continued)

(2) Changes in Long-term Equity Investment

Invested company	At 1st January, 2006	Increase (decrease) in equity this year				At 31st December, 2006
		Investment Cost	Adjusted Equity	Dividend Paid	Disposal	
Xi'an Ser	34,566,593.19	-	7,619,763.87	-	-	42,186,357.06
Shaanxi Hengtong	15,943,281.39	-	(4,319,159.41)	-	-	11,624,121.98
Siyan Intelligent	21,881,238.96	-	(531,458.57)	-	-	21,349,780.39
Winko	1,664,956.17	-	(1,664,956.17)	-	-	-
Tos Kunming	23,818,814.75	-	1,522,903.75	-	-	25,341,718.50
Yunnan Chengjiang Copper Products Plant	2,000,000.00	-	-	-	-	2,000,000.00
Kunji Transportation	-	500,000.00	(14,148.59)	-	-	485,851.41
Ruite	-	10,000,000.00	-	-	-	10,000,000.00
Less: Provision on impairment loss on long-term investment	2,000,000.00	-	-	-	-	2,000,000.00
Total	97,874,884.46	10,500,000.00	2,612,944.88	-	-	110,987,829.34

Note:

The equity of Shaanxi Hengtong decreased RMB4,923,464.73 by using equity method for the year, and it received donation of RMB604,305.32.

(3) Equity Investment Difference

Invested company	Original cost	At 1st January, 2006	Addition this year	Amortization this year	At 31st December, 2006	Amortization period
Xi'an Ser	7,296,277.00	4,377,766.12	-	729,627.72	3,648,138.40	10 years
Shaanxi Hengtong	6,849,713.19	4,012,138.75	-	668,554.68	3,343,584.07	10 years
Less: Provision on impairment loss on long-term investment	-	-	967,706.05	-	967,706.05	-
Total	14,145,990.19	8,389,904.87	(967,706.05)	1,398,182.40	6,024,016.42	-

Note:

- (1) As Yunnan Cheng Jiang Copper Products Plant cease to be a going concern entity, the Company made the full amount of provision on impairment loss on long-term investment.

According to the agreement entered into between Ruite and the Company regarding selling the equities of Shaanxi Hengtong, the equity investment difference of RMB967,706.05 was provided for Shaanxi Hengtong.

- (2) There is no significant difference between the accounting policies used by invested enterprises and that used by the Company. There is no significant restrictions to investment realization and investment gain inflow.

NOTES TO THE FINANCIAL STATEMENTS

6. NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY (UNIT:RMB) (Continued)

4. Principal Operation Revenue and Cost

Items	Year 2006		Year 2005	
	Revenue	Cost	Revenue	Cost
Machine tool	591,436,621.03	446,607,570.86	403,009,411.32	305,316,858.06
Machine processing service	52,565,159.48	25,420,302.86	30,675,521.00	16,797,889.98
Others	—	—	5,149,613.02	2,251,790.25
Total	<u>644,001,780.51</u>	<u>472,027,873.72</u>	<u>438,834,545.34</u>	<u>324,366,538.29</u>

Note:

The main operation revenue of the Company increased 46.75% for the year due to strong market demand for CNC machines and improved products' structure of the Company.

5. Investment Income

Items	Year 2006	Year 2005
Income from investment in equity	(4,314,835.15)	(14,453,194.47)
Amortization of equity investment difference	(1,398,182.40)	(1,398,182.40)
Provision for diminution in value of equity investment	(967,706.05)	(680,411.67)
Income from short-term investment	<u>234,516.02</u>	<u>—</u>
Total	<u>(6,446,207.58)</u>	<u>(16,531,788.54)</u>

Note:

The Company recognized the net loss of its subsidiaries, which was more than long-term equity investment book value, was RMB6,323,474.69.

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS

1. Details of Related Parties with Control Relationship

(1) Related Parties with Control Relationship

Name	Relationship with the Company	Nature	Place of registration	Scope of business	Legal representative
Xi'an Jiaotong University industrial (Group) Incorporation ("Jiaotong Group")	Former largest substantial shareholder	State-owned	Xi'an City	not allowed to operate business which legally prohibited, should the business need to be approved, not allowed to operate before approval, should the business not required to be legally approved, business should be free to be selected by the Company	Xi You Min
Shenyang Machine Tool (Group) Company Limited ("Shenyang Group")	the largest substantial shareholder	Limited liability	Shenyang City	Production of metal-cutting machines, digital controlled software and machine accessories; General business trading and technology trading within PRC.	Chen Hui Ren
Xi'an Ser	Subsidiary	Limited liability	Xi'an City	Design, develop and sales of turbo-machinery	Wang Shangjin
Shaanxi Hengtong	Subsidiary	Limited liability	Xi'an City	Develop and sales of manufacturing moulds, machinery, equipment, electronic products, software and hardware.	Lu Bingheng
Siyuan Intelligent	Subsidiary	Limited liability	Xi'an City	Develop, manufacture and sales of electronic products, electric machinery and products of electronic power; Provide technology services.	Zhang Hanrong
Winko	Subsidiary	Limited liability	Kunming City	Develop, apply and integrate hardware and software; retail, wholesale, purchase on behalf of others and consign electronic products, machinery and electronic machinery.	Zhang Hanrong
Kunji Transportation	Subsidiary	Limited liability	Kunming City	General cargo Transportation	Zhang Xiaoyi

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

1. Details of Related Parties with Control Relationship *(Continued)*

(2) Registered Capital of Related Parties with Controlling Relationship

Company name	At 1st January, 2006	Increase in this year	Decrease in this year	At 31st December, 2006
Jiaotong Group	30,000,000.00	–	–	30,000,000.00
Shenyang Group	712,840,000.00	–	–	712,840,000.00
Xi'an Ser	50,000,000.00	–	–	50,000,000.00
Shaanxi Hengtong	27,960,000.00	–	–	27,960,000.00
Siyuan Intelligent	35,000,000.00	–	–	35,000,000.00
Winko	20,230,000.00	–	–	20,230,000.00
Kunji Transportation	–	500,000.00	–	500,000.00

(3) Shares and Equity held by Related Parties with Controlled Relationship

Company name	At 1st January, 2006		At 31st December, 2006			
Increase in	Decrease in		this year	this year	Amount	Proportion
	Amount	Proportion (%)				
Jiaotong Group	71,052,146.00	29.00	–	71,052,146.00	–	0.00
Shenyang Group	–	–	71,052,146.00	–	71,052,146.00	29.00
Xi'an Ser	22,500,000.00	45.00	–	–	22,500,000.00	45.00
Shaanxi Hengtong	18,270,000.00	65.34	–	–	18,270,000.00	65.34
Siyuan						
Intelligent	27,310,000.00	78.03	–	–	27,310,000.00	78.03
Winko	19,320,000.00	95.50	250,000.00	–	19,570,000.00	96.74
Kunji Transportation	–	100.00	500,000.00	–	500,000.00	100.00

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

2. Related Parties with Non-controlling Relationship

Company name	Relationship with the Company
Kunji Group Company	Second-largest shareholders designated to manage equity
Yunnan Government	Promoter's shareholders
Tos Kunming	Jointly controlled entity
Ruite	Joint venture
Jiaoda HongFan High-Tech Company Limited	Subsidiary of former substantial shareholder of the Company
The Pharmacy Group Co. Ltd of Xi'an Jiaotong University	Subsidiary of former substantial shareholder of the Company
Czech Tos Vansdorf Company Limited ("Czech Tos")	Shareholder of Tos Kunming
Yunnan CY Group Company Ltd. Products Trading Center ("CY Group Products Trading Center")	Subsidiary of substantial shareholder of the Company

3. Related Party Transaction

(1) Sales of Goods

The Company sold goods at market value amounting to RMB3,794.88 and RMB355,810.26 to related party Kunji Group in 2006 and 2005 respectively.

The Company sold goods at market value amounting to RMB3,938,628.50 and RMB1,912,783.67 to related party Tos Kunming in 2006 and 2005 respectively.

The Company sold goods at market value amounting to RMB2,083,517.12 to related party CY Group Products Trading Center in 2006.

The Company sold goods at market value amounting to RMB4,751,787.47 to related party Czech Tos in 2006.

Subsidiaries sold goods at market value amounting to RMB1,296,500.00 and RMB1,296,500.00 to Xian Jiaotong University and its related parties in 2006 and 2005 respectively.

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

3. Related Party Transaction *(Continued)*

(2) *Provision and Receipt of Services*

- (i) On 15th November, 1993, the Company entered into an agreement with Kunji Group Company relating to the provision of certain services to each other after the reorganization. Pursuant to this agreement, the Company agreed to provide certain public utility services available to the Company such as water and electricity to Kunji group Company, while Kunji Group agreed to provide certain services to the Company including property management, employee's medical services, education and administrative fee for retired staff. Service fee is reviewed by both parties on an annual basis and is determined by reference first to the standards set by the relevant government department for that particular service. If there are no applicable State standards, the Company and Kunji Group Company will determine the service fee based on market price or transaction price at arm's length negotiation. The above transactions between Kunji Group and the Company in 2006 and 2005 are as follows:

Items	Year 2006	Year 2005
Property management fee paid to Kunji Group	956,461.15	956,461.15
Staff medical service fee paid to Kunji Group	75,000.00	75,000.00
Social and education service fee paid to Kunji Group	–	162,500.00
Administrative fee for retired staff	75,384.00	75,384.00
Total	<u>1,106,845.15</u>	<u>1,269,345.15</u>

- (ii) the Company received consultation fee of RNB2,254,900.00 from the related party Tos Kunming in this year.

(3) *Purchase of Goods*

The Company purchased goods of RMB38,923,315.85 and RMB6,600,000.00 from related party TOS Kunming Machine in 2006 and 2005 respectively.

Shaanxi Hengtong, a subsidiary of the Company, purchased accessories amounting to RMB814,529.94 and RMB1,748,408.40 in 2006 and 2005 respectively from related party Jiaoda HongFan High-Tech Company Limited.

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

3. Related Party Transaction *(Continued)*

(4) Leases

The 16th meeting of the 4th term of board of directors held on 18th April, 2004 approved that "The Premise Rental Agreement" and "The Land Use Rental Agreement" signed in 2001 between the Company and Kunji Group Company would be continued. According to the result passed at 26th session meeting of 4th term of board of directors, on August 17, 2005, the Company and Kunji Group entered into the agreements "The Rent Amendment Agreement of the Premises" and "The Rent Amendment Agreement of the Land Use Right", which stated that Kunji Group was authorized by Yunnan government to succeed the rights and obligations of the "The Premise Rental Agreement" and "The Land Use Rental Agreement" signed by Yunnan government in 2001 with the Company. The rental of premises and the rental of land use right would be adjusted to RMB850,080.00 and RMB1,320,000.00 respectively for each year during 2005 to 2007.

The assets mentioned in the above agreements involved the leaseback of part of the premises and land use right from the Yunnan Government after the capital restructuring in 2001.

In 2005, the Company paid the rental of the premises and land use right at annual rent of RMB800,000.00 and RMB1,200,000.00 respectively.

This year, the Company paid the rental of the premises and land use right at annual rent of RMB507,911.09 and RMB1,200,000.00 respectively.

(5) Other Transactions

- (i) The Company and its subsidiaries had the following transactions with Jiaotong Group or companies under its control:

Transactions	Year 2006	Year 2005
Rent, water and electricity fee paid to Jiaoda Group	1,202,117.69	1,363,110.00
Loan to Jiaoda Group	–	30,000,000.00
Interest received from Jiaoda Group	412,300.00	101,141.67
Loan to Pharmacy Group of Xi'an Jiaotong University by Xi'an Ser	(10,000,000.00)	10,000,000.00
Loan to Tos Kunming	–	2,000,000.00

- (ii) Transaction between the Company and its subsidiaries and Xian Jiaotong University (an investor of Jiaotong Group) are as follows:

Transactions	Year 2006	Year 2005
Research fee paid to Xian Jiaotong University	1,150,000.00	1,150,000.00
Total	1,150,000.00	1,150,000.00

- (iii) The Company signed "The Agreement Concerning the Building Demolition" with Kunji Group in this year. Both sides agreed the removal of 8 buildings on lease, and the Company would pay RMB441,400.00 as the compensation to Kunji Group Company.

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

3. Related Party Transaction *(Continued)*

(5) Other Transactions *(Continued)*

- (iv) Xian Jiaotong University Siyuan Intelligent Electric Apparatus Company Limited, a subsidiary of the Company, signed "The Agreement Concerning the Development of the Northern Building No.2 and No. 3 in the University Surroundings" on 26th March, 2003. It would commit capital in these constructions and obtain the right of management for 23 years upon the completion of the project. It would be obligated to pay license fee for operating services in the university at the rate of RMB6.5 per square metre each month. In 2006 and 2006, the fee amounted to RMB2,098,687.50 and RMB1,228,500.00 respectively.
- (v) According to the premises and land use right agreements mentioned above, the amortization of prepaid lease amounted to RMB128,960.00.

4. Balances of Connected Transactions

Related parties name	Items	At the end of the year	At the beginning of the year	Nature
Jiaotong Group	Accounts receivable	–	322,775.00	Sales of goods
	Prepayments	34,294.50	100,000.00	purchase
	Accounts payable	125,000.00	–	purchase
	Other receivables	307,503.57	–	rental
	Accrued expenses	163,541.72	96,723.34	Accrued water and electricity fee
Jiaotong Group (other group companies)	Other receivable	300,000.00	645,200.00	Deposit and current account
	Other payable	3,327,187.50	1,352,276.00	Current account, License fee
Xi'an Jiaotong University	Accounts receivable	38,250.00	–	Sales of goods
	Other payables	550,000.00	1,150,000.00	Research & development fee
Pharmacy Group of Xi'an Jiaotong University	Other receivables	–	10,000,000.00	Loan
Pharmacy Group of Xi'an Jiaotong University	Other payables	–	500,000.00	Current account
Jiaoda HongFan High-Tech Company Limited	prepayment	122,127.16	(265,109.79)	Payables for purchase of goods
Ruite	Other payables	10,000,000.00	–	Advances receivable for selling Shaanxi Hengtong equities
Kuji Group	Other payables	1,349,716.22	1,782,263.00	Accrued management fee

NOTES TO THE FINANCIAL STATEMENTS

7. RELATED PARTY RELATIONSHIP AND TRANSACTIONS *(Continued)*

4. Balances of Connected Transactions *(Continued)*

Related parties name	Items	At the end of the year	At the beginning of the year	Nature
Kunming Kunji Group Sales Company Limited	Advances from customers	–	30,000.00	Sales of goods
Yunnan Government	Long-term payables due within one year	684,337.80	342,168.90	Payable rent of fixed assets
	Long-term payables	2,855,966.60	3,069,175.70	Payable rent of fixed assets
Tos Kunming	Accounts receivable	4,960,475.33	–	Payables for purchase of goods and consultation fee
	Other receivables	140,205.88	–	Current account
	Accounts payable	17,213,254.55	251,000.00	Payable for purchasing goods
Czech Tos	Advances from customers	621,613.05	–	Sales of goods
CY Group Products Trading Center	prepayment	81,700.00	–	

8. CONTINGENT EVENTS

There are no contingent events required to be disclosed in this year.

9. COMMITMENTS

1. Lease commitments:

For each of the three subsequent years after the balance sheet date and the years afterwards, the minimum lease payments are as follows:

Accounting year	Amount
2007	342,168.90
2008	342,168.90
2009	342,168.90
2010 onwards	4,106,026.80
Total	5,132,533.50

2. by 31st December, 2006, the unsettled L/C amount was RMB8,673,545.08, which the L/C was opened by the Company.

NOTES TO THE FINANCIAL STATEMENTS

10. POST BALANCE SHEET EVENT

Until the balance sheet date, the Company was involved in the following event in which no adjustment is required to be made:

1. Change of substantial shareholder

Approved by Yunnan Government and State-owned Assets Supervision and Administration Commission under the State Council with written reply 雲政複[2006] No.33 and 國資產權[2006] No. 1412 respectively, Yunnan Government-the second largest shareholder transferred all its shares of the Company (representing 12.79% of the total issued share capital of the Company) to Yunnan State-owned Assets Operation Company Limited at nil. The registration of transfer was completed on 19th January, 2007.

2. Share Reform

The Company disclosed its share reform proposal on 7th November, 2006. After considered and passed at the meetings of board of directors and the relevant shareholders' meeting in relation to the A Share market on 22nd December, 2006 and the second extraordinary general meeting of the Company, approved by Liaoning State-owned Assets Supervision and Administration Commission with document 遼國資經營[2006]300號 and approved by Ministry of Commerce with document 商資批[2007]133號, the share reform proposal can be implemented. The Company implemented share increase by transferring capital reserve proposal on 27th February, 2007 (1.5606 new shares would be allocated to every 10 existing shares to all shareholders). Totally increased shares were 38,235,855 shares, of which, 28,091,955 shares were A Shares, and 10,143,900 shares were H Shares. The share reform proposal was implemented on 5th March, 2007, the holders of non-circulating shares of the Company totally pay 18,728,355 shares to holders of circulating A shares (excluding holders of H shares) as the consideration for the circulation of their non-circulating shares. The consideration was that each holder of circulating A shares received 2.7 shares for every 10 existing shares from holders of non-circulating shares. After share reform, the share capital structure of the Company changed as follows:

Type	31st December, 2006	After change	5th March, 2007
Non-circulating shares			
1. state-owned shares	31,345,554	(31,345,554)	–
2. state-owned legal person shares	71,052,146	(71,052,146)	–
3. legal person shares	17,609,700	(17,609,700)	–
Total non-circulating shares	120,007,400	(120,007,400)	–
Restricted circulating shares			
1. state-owned shares	–	31,345,554	31,345,554
2. state-owned legal person shares	–	71,052,146	71,052,146
3. legal person shares	–	17,609,700	17,609,700
Total restricted circulating shares	–	120,007,400	120,007,400
Unrestricted circulating shares			
A shares	60,000,000	28,091,955	88,091,955
H shares	65,000,000	10,143,900	75,143,900
Total unrestricted circulating shares	125,000,000	38,235,855	163,235,855
Total shares	245,007,400	38,235,855	283,243,255

NOTES TO THE FINANCIAL STATEMENTS

10. POST BALANCE SHEET EVENT *(Continued)*

3. Selling equities of a subsidiary

After considered and approved by the 22nd meeting of the 4th term of board of directors on 27 the April, 2005 and the meeting of board of directors on April, 2006, the resolution that the equities of Shaanxi Hengtong would be invested in National Fast Prototyping Manufacturing Research Center was passed. Because the method of capital subscription was limited by the Company Law, the Company invest cash of RMB10,000,000 (representing 16.67% of the proportion of subscribed capital) to establish Ruite with Xi'an Jiaotong University on September, 2006. On 10th February, 2007, after considered and passed at the shareholders' meeting of Ruite, the Company would sell 76.36% equities of Shaanxi Hengtong (including 11.02% equities transferred by the shareholder Lu Bingheng at nil) to Ruite. The consideration of the equities would be RMB14,000,000 by referring to the assessed value and considering the operation results in the second half year of 2006 of Shaanxi Hengtong. The Company agreed to use RMB4,000,000 (at original cost of the equity of Ruite) to purchase 6.66% shareholding of Ruite from a shareholder-Shaanxi Industry Technology Research Institute. This issue was passed at the 22nd meeting of the 5th term of board of directors on 23rd March, 2007. The equity transfer is processing.

4. In accordance with the document《財政部關於引發〈企業會計準則第1號－存貨〉等38項具體準則的通知》(財會[2006]3號文) issued by the Ministry of Finance, the Company adopted the New Accounting Standards on January 1, 2007. The adopting the New Accounting Standards would have some impact on the Company's financial data.

11. DEBT RESTRUCTURING EVENTS

The Company has no debt restructuring events in this year.

12. OTHER SIGNIFICANT EVENTS

1. Land Appreciation Tax (LAT)

During December 2001, the Company implemented capital restructuring and sold several buildings and land use right to Yunnan Provincial Government in the form of leaseback. According to Tax Document No. 1 in 2002 of the Department of Finance of Yunnan Province, "Concerning the Tax Payable Opinion about Capital Restructuring between Jiaoda Kunji High-Tech Company Limited and Xian Jiaotong University Industrial (Group) Incorporation", Paper 3 Document No. 9 in 2002 of the Local Taxation Bureau of Yunnan Province, "Opinion concerning Land Appreciation Tax issue resulted from Capital Restructuring between Jiaoda Kunji High-Tech Company Limited and Xian Jiaotong University Industrial (Group) Incorporation" and Yunnan Provincial Government, the Land Appreciation Tax (LAT) payable of RMB10,984,000 was temporarily waived.

In March 2005, Tax Policy Department, Ministry of Finance issued the Document No. 6 in 2005, "In Response to the Land Appreciation Tax Policy regarding Capital Restructuring between Jiaoda Kunji High-Tech Company Limited and Xi'an Jiaotong University Industrial (Group) Incorporation", referring that the building transfer would result in Land Appreciation Tax payable. According to the above situation, the provision for Land Appreciation Tax for the year was RMB10,984,000, after the reversal of the deferred income of RMB9,714,394.95 at the beginning of 2005, the remaining balance of RMB1,269,605.05 was considered as non-operating expenses. According to settlement result with the government tax department this year, the actual LAT payment of the Company for the year would be RMB5,048,680.52. The difference between actual payment and recognized amount made by the government last year would be transferred to deferred income amortizing within the rest leasing period.

NOTES TO THE FINANCIAL STATEMENTS

12. OTHER SIGNIFICANT EVENTS (Continued)

2. On February, 2004, an agreement for trusteeship of the management of investment in State Bonds was entered into the Company and Chinese Fortune Securities ("China Fortune") pursuant to which the Company entrusted China Fortune to conduct investment on State Bonds with RMB50,000,000 funded by internal sources. But China Fortune fails to comply with agreement to invest in state bonds, but using the fund to invest in A shares and to incur huge losses. On September, 2004, China Fortune was taken over by China Huarong Assets Management Corporation ("China Huarong"). In January, 2006, Capital Airport Group Company started the restructuring process of China fortune, for the period of 6 months. However, the process was failed after 6 months. On 3rd August, 2006, China Securities Regulation Commission appointed Beijing Gao Peng Tianda Law Firm to establish an administrative liquidation working group for performing the liquidation work and registration of claims. Registration time for debt started from 5th August, 2006 to 3rd November, 2006, for the period of 90 days. By 31st December, 2006, the liquidation process is continuous.

Since there is no enough evidence to infer that the above investment can be received, the Company decided to recognize an impairment loss of RMB38,097,597.20 continuously. By 31st December, 2006, the balance of entrusted investment was RMB11,902,402.80, deducting transferring received fund RMB4,250,000, the rest RMB7,652,402.80 would be decided by the result of the liquidation of China Fortune.

3. In accordance with the "Notice of "Pay first, refund later" method for value added tax for numerical control machine products" by the Ministry of Finance & State Administration of Taxation (No. [2006] 149), from January 1, 2006 to December 31, 2008, for numerical control machines products, the value-added tax should be paid first in accordance with the regulations, and then 50% of the paid value-added tax will be refunded. Thus, the Company has enjoyed this preferential policy from year 2006 to year 2008 (The Company had got this preferential policy from year 2003 to year 2005, and had valued-added tax refund RMB2 million per year.) The tax refund is used for the specified purpose for technical innovation, environment protection, developing energy saving products and numerical control machine products. This preferential policy will not have significant effect on the year 2006 revenue. It is estimated that from 2007 to 2009, the Company will have value-added tax refund more than RMB10 million per year.

4. Difference between the PRC GAAP and HK GAAP

These financial statements are prepared in accordance with the PRC GAAP, which are different from those prepared in accordance with HK GAAP.

The consolidated net profit in year 2006 and the consolidated net asset as at 31st December, 2006 are RMB78,153,288.80 and RMB610,751,832.29. According to the HK GAAP, the major adjustments to the consolidated net profit and the consolidated net asset are as follows:

Items	Net profit (RMB'000)	Net assets (RMB'000)
Consolidated results in accordance with PRC GAAP	78,153	610,752
Add: Adjustment value-added tax of land	5,237	5,237
Add: Gain on investment in subsidiaries	(154)	(8,370)
Add: Donation	—	—
Add: Amortization of deferred income	201	—
Add: Amortization of goodwill	(956)	682
Add: Accrual rebate for profits tax of a subsidiary	—	339
Add: Gain on restructuring	—	(3,018)
Consolidated results in accordance with HK GAAP	82,481	605,622

The figures above were audited by Deloitte Touche Tohmatsu in accordance to the HK GAAP.

NOTES TO THE FINANCIAL STATEMENTS

12. OTHER SIGNIFICANT EVENTS *(Continued)*

5. The return on net assets and earnings per share for 2006 and 2005 are as followings:

Items	For the year ended 31st December, 2006				For the year ended 31st December, 2005			
	Return on net assets (%)		Earnings per share (dollar)		Return on net assets (%)		Earnings per share (dollar)	
	Dilutive	Weighted average	Dilutive	Weighted average	Dilutive	Weighted average	Dilutive	Weighted average
Principal operating income	37.36%	39.95%	0.9312	0.9312	32.95%	33.86%	0.7154	0.7154
Operating income	17.16%	18.35%	0.4276	0.4276	9.74%	10.02%	0.2116	0.2116
Net profit	12.80%	13.69%	0.3190	0.3190	3.44%	3.54%	0.0748	0.0748
Net profit after deducting non-recurring items	12.26%	13.11%	0.3055	0.3055	3.01%	3.09%	0.0653	0.0653

6. The Company's 2006 Annual Report was approved at the 21st meeting of the 5th term of board of directors on 18th April, 2007.