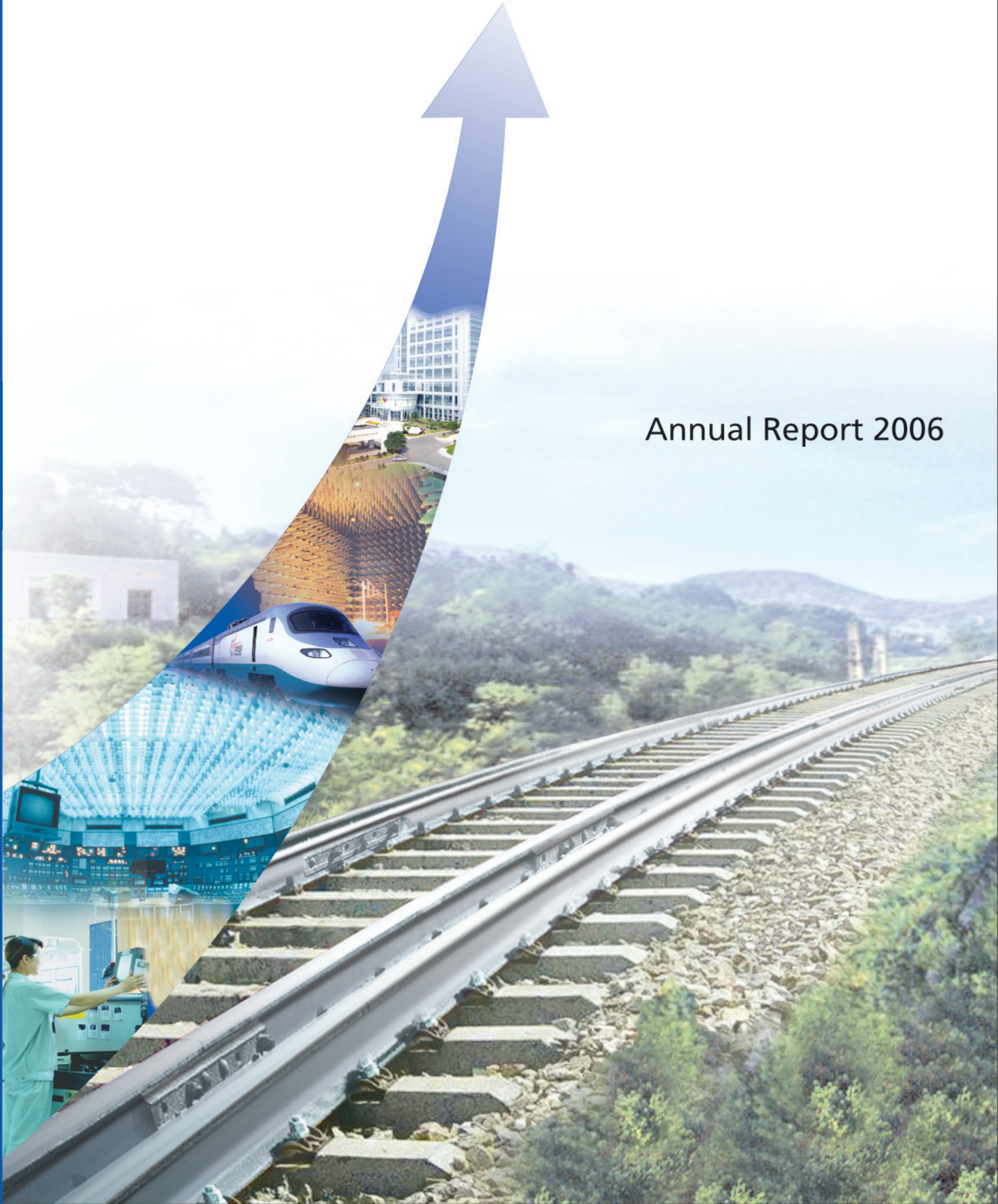
株洲南車時代電氣股份有限公司

ZHUZHOU CSR TIMES ELECTRIC CO., LTD.

(Stock Code : 3898)



Annual Report 2006

Company Profile

The Group is the leading train-borne electrical system provider and integrator for the PRC railway industry. The Group possesses comprehensive capabilities in research and development, design, manufacture, sales and customer service.

The Group is also engaged in developing, manufacturing and selling train power converts, auxiliary power supply equipment and control system for trains for urban rails systems.

In addition, the Group designs, manufactures and sells electrical components for the PRC railway industry, the urban railway industry and non-railway applications. The Group's electrical component products include power semiconductor devices, sensors and related products.

We are the only company within the PRC railway vehicle manufacturing industry that is listed overseas. On 20 December 2006, H shares of the Company were successfully listed on the Main Board of the Stock Exchange of Hong Kong.

Contents

Highlights of the Year

January 2006

The "alternating current transfer system and advanced control technology" State project undertaken by the Company was granted the 2005 State Technological Advancement Second Class Award by the Ministry of Science and Technology.

February 2006

The Company's electrical products for EMUs for high-speed trains of 200 km/h passed initial quality control assessment and were approved for downstream production.

March 2006

The Company was accredited by General Electric Company (USA) as one of its Best Cooperation Partners worldwide.

May 2006

The Company and its business partner jointly won a contract to provide train-borne electrical equipment and control systems for Line 2 of the Beijing Metro.

November 2006

The Company entered into a contract with CSR Sifang Locomotive for the supply of electrical systems for 300 km/h EMUs. The Group's total share of the contract value is approximately RMB1.03 billion.

December 2006

The H shares of the Company were successfully listed on the Main Board of the Stock Exchange of Hong Kong, making the Company the first PRC railway vehicle equipment manufacturer listed outside of the PRC.

Financial Highlights

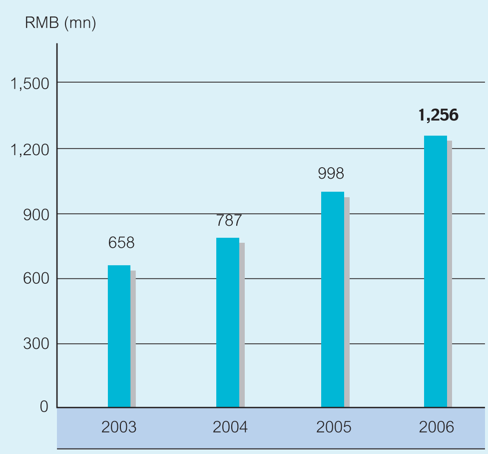
CONSOLIDATED INCOME STATEMENT HIGHLIGHTS

	Year Ended 31 December			
	2006 RMB'000	2005 RMB'000	2004 RMB'000	2003 RMB'000
Revenue	**1,255,926**	997,976	787,756	658,762
Profit from operation	**317,013**	232,375	187,591	86,609
Profit before tax	**302,581**	218,556	185,047	96,412
Profit for the year	**302,268**	217,917	182,421	96,412
Minority Interest	**5,497**	6,184	19,741	(2,118)
Net Profits attributable to equity holders of the parent	**296,771**	211,733	162,680	98,530
Earnings per share attributable to ordinary equity holders of the parent	**RMB0.44**	RMB0.33	RMB0.26	RMB0.16

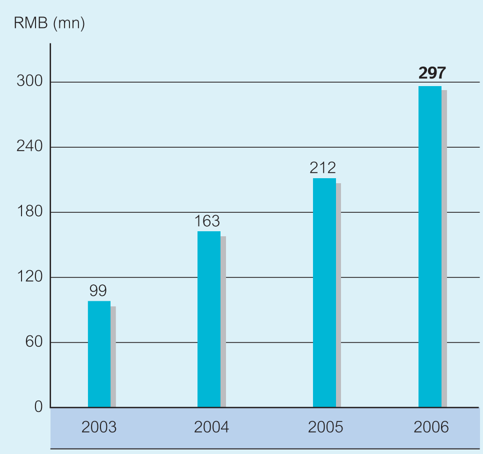
CONSOLIDATED BALANCE SHEET HIGHLIGHTS

	As at 31 December			
	2006 RMB'000	2005 RMB'000	2004 RMB'000	2003 RMB'000
Total Assets	**3,788,256**	1,481,397	1,289,124	1,061,433
Total Liabilities	**940,246**	825,190	770,482	465,243
Net Assets	**2,848,010**	656,207	518,642	596,190

2003-2006 Growth in revenue



2003-2006 Growth in net profit



Chairman's Report

Dear Shareholders,

I am pleased to present the Annual Report of the Group for the year ended 31 December 2006. On behalf of the Board of Directors, I would like to express our gratitude to all the shareholders for their care and support of our Company.

Business Review

2006 was the first year in the Eleventh Five Year Plan period of the PRC, as well as a significant year in the history of the development of the Company. The Company saw remarkable achievements in research and development, production, sales, fund raising from a successful initial public offering and corporate governance.

The Group's turnover in 2006 amounted to RMB1,255,926,000 (2005: RMB997,976,000), an increase of 25.8% over the previous year. Profit attributable to equity holders of parent was RMB296,771,000 (2005: RMB211,733,000), an increase of 40.2% over the previous year. Earnings per share was RMB0.44 (2005: RMB0.33). The Company ranks 40th on the list of the PRC's top 100 software companies.

According to market reports, 2006 was the last year in which the Ministry of Railways purchased direct current locomotives in bulk. Meanwhile, the Company began to deliver its power electrical system products for 200 km/h high speed trains. During the year, the Company was also awarded a number of procurement contracts, including contract to provide products for 300 km/h high speed train electrical systems, contract to provide products for Line 2 of the Beijing Metro and contract to provide products for the Shenyang Metro Line. Annual sales of converters and control systems increased by approximately 37.4% compared with 2005. At the end of 2005, the Ministry of Railways stipulated that all train operation safety equipment of the LKJ93 model across the country should be replaced by the LKJ2000 model prior to the sixth round of nationwide train speed increase. As a result, the Company's sales of train operation safety equipment increased substantially and the total amount was approximately 35.7% higher than that of 2005. However, sales of large railway maintenance vehicles declined by approximately 16.3% compared with 2005.

In December 2006, the H shares of the Company were listed on the Main Board of the Stock Exchange of Hong Kong. The Company has complied with the Listing Rules and the relevant laws and regulations. The Company has enhanced shareholder value, improved the quality of its corporate governance while operating in a regulated manner. The Company is dedicated to establish itself as a transparent and high quality enterprise which is responsible for its shareholders, and devoted to create shareholder value.

Company Outlook

The Company's long-term objective is to consolidate its leading position in the PRC railway train-borne electrical systems market, and to become an internationally renowned train-borne electrical system supplier and integrator. To achieve this, the Company will leverage its core technologies, speed up localisation of overseas technologies, continue its expansion in the domestic market, develop its overseas markets and further strengthen its core competitive advantages.

2007 will be a year of challenges and opportunities. Foreign competitors with advanced technologies and management experience have gained a foothold in the PRC market. The open market conditions have created intensified competition, placing pressures on the operation of the Company. We anticipate that the Ministry of Railways will concentrate on procuring mainly alternating current locomotives and EMUs after 2006. Market demand for direct current locomotives will decline in 2007. The market for train operation safety equipment products will also dwindle. However, the rapid development of China's economy as well as growth of the railway and urban rail industries will present the Company with great development opportunities. In 2007, the Company will start to deliver products for 300km/h high-speed train projects, and complete the delivery of products for 200km/h high-speed train projects. The market for large railway maintenance vehicles will also come into a new phase of expansion.

In 2007, the Company will adopt the following strategies to realise opportunities and to overcome challenges.

- Expedite construction of key projects as well as enhancing our professional manufacturing and testing capabilities. The Company will also fortify its capabilities in research and development, manufacturing and testing through integration of available resources, so as to enhance the core competitiveness of the Company.
- Continue to focus on technological innovation to reinforce our competitiveness within the market place.
- Continue to exploit potential of its existing markets, achieve breakthrough in the non-railway markets. The Company will strengthen its development in overseas markets and establish its European representative office.
- Continue to enhance the Company's corporate governance, and set up a management system that satisfies international capital market requirements.
- Explore opportunities for integration of upstream and downstream industries and resources.

The Company is fully confident of its future. The Company expects to continue its business growth in 2007 with the upgrading of its core technologies, enhancement of its ability to commercialise core technologies and expansion of its after-sales networks. The Company will persevere to create greater value, and share the fruits of its steady development with all its shareholders.

Liao Bin
Chairman

23 April 2007

Management Discussion and Analysis

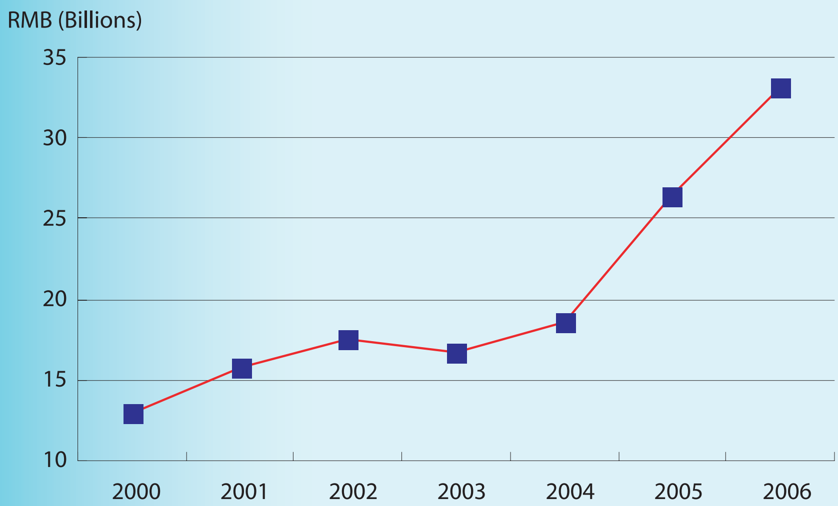
The following discussion and analysis should be read in conjunction with the Group's audited financial statements and the notes in this annual report.

Industry Overview

According to the 2006 Railway Statistics Gazette issued by the Ministry of Railways on 15 March 2007, at the end of 2006, the total operational length of railway in the PRC was approximately 77,000 km, making it the third longest in the world. Of these, approximately 63,400 km were State railways, approximately 8,900 km were joint venture railways, while approximately 4,700 km were local railways. In 2006, there were approximately 17,800 locomotives in the PRC, of which 99.3% were diesel and electric locomotives, operating on all major railway trunk lines. Also, there were approximately 42,600 passenger cars and approximately 566,700 freight cars in the PRC.

In 2006, spending for the acquisition of locomotives in the PRC amounted to RMB33.18 billion, including RMB9.2 billion for payment in relation to imported projects. With a focus on locomotives with speeds over 200 km/h, high-power alternating current locomotives and new freight cars, approximately 447 locomotives, 774 passenger cars and 25,490 freight cars were purchased by the MOR in 2006. Twenty-five EMUs capable of speeds over 200 km/h had passed the speed increase certification testing, and were found to comply with standards for existing and special passenger lines operations, meeting high speed operational requirements. During 2006, eleven high power eight-axle 9.6 MW locomotives and 68 units of six-axle 7.2 MW locomotives, primarily used on coal transportation lines and trunk lines, were put into operation. Additionally, trains with haulage capacity exceeding 20,000 tons were put into operation on the Daqin Line, indicating that the hauling capacity of freight cars in the PRC has reached world leading standard.

New locomotives procured by the Ministry of Railways



Source: 2000 to 2006 Railway Statistics Gazettes published by Railway Statistics Center

Revenue

	2006 (RMB million)	2005 (RMB million)
Train power converters, auxiliary power supply equipment and control systems	**494.2**	359.6
Train operation safety equipment	**369.7**	272.5
Electrical control systems for large railway maintenance vehicles	**124.7**	148.9
Train-borne electrical systems	**988.6**	781.0
Power semiconductor devices	**96.1**	90.1
Sensors and related products	**89.0**	57.0
Others	**82.2**	69.9
Electric components	**267.3**	217.0
Total revenue	**1,255.9**	998.0

Revenue increased by RMB257.9 million from RMB998.0 million for the year ended 31 December 2005 to RMB1,255.9 million for the year ended 31 December 2006. The increase in revenue was mainly due to the growth in the sales of power converters, control system and train operation safety equipment. Of these, growth in the sales of power converters and control system was mainly due to the increase in the sales of 200 km/h EMUs, while growth in the sales of train operation safety equipment was mainly due to new regulatory policies introduced by the Ministry of Railways at the end of 2005 to install LKJ2000 type train operation safety equipment on all trains operating in the PRC.

Cost of sales

Cost of sales increased 18.1% from RMB542.3 million for the year ended 31 December 2005 to RMB640.4 million for the year ended 31 December 2006, which was mainly due to increase in the Group's revenue.

Gross profit

Based on the above factors, the Group's gross profit increased 35.1% from RMB455.7 million for the year ended 31 December 2005 to RMB615.5 million for the year ended 31 December 2006. The Group's gross profit margin rose from 45.7% for the year ended 31 December 2005 to 49.0% for the year ended 31 December 2006, mainly due to changes in its product mix.

Other revenue and gains

Other revenue and gains of the Group increased 248.6% from RMB18.5 million for the year ended 31 December 2005 to RMB64.5 million for the year ended 31 December 2006. This was mainly due to interest income earned in connection with the Company's initial public offering.

Selling and distribution costs

The Group's selling and distribution costs increased 36.0% from RMB87.3 million (representing 8.7% of revenue for the whole year) for the year ended 31 December 2005 to RMB118.7 million (representing 9.5% of revenue for the whole year) for the year ended 31 December 2006. Increase in the selling and distribution costs was mainly due to the overall growth in the Group's business.

Administration expenses

The Group's administration expenses increased 57.4% from RMB154.8 million for the year ended 31 December 2005 to RMB243.7 million for the year ended 31 December 2006, which was mainly due to increase in expenditure in research and development.

Profit from operations

The Group's profit from operations increased 36.4% from RMB232.4 million for the year ended 31 December 2005 to RMB317.0 million for the year ended 31 December 2006, which was mainly due to increases in turnover and interest income. The Group's profit margins from operations for the years ended 31 December 2005 and 2006 were 23.3% and 25.2% respectively.

Finance costs

Finance costs increased 4.3% from RMB13.8 million for the year ended 31 December 2005 to RMB14.4 million for the year ended 31 December 2006, which was mainly due to the increase in the Group's borrowings and the overall increase in interest rates between 2005 and 2006. For the year ended 31 December 2006, the Group's bank loans carried annual interest rates ranging from 5.02% to 7.50%, while for the year ended 31 December 2005, bank loan interest rates ranged from 4.19% to 6.19%.

Profit before tax

Based on the above factors, the Group's profit before tax increased 38.4% from RMB218.6 million for the year ended 31 December 2005 to RMB302.6 million for the year ended 31 December 2006.

Income tax expense

The Group's income tax expenses decreased from RMB639,000 for the year ended 31 December 2005 to RMB313,000 for the year ended 31 December 2006. Income tax expenses in 2005 were mainly income taxes incurred by Times Electronics and Times Guangchuang. Income tax expenses in 2006 were mainly income taxes incurred by Times Guangchuang and which were recognized during the twelve months ended 31 December 2006. The Company, Ningbo Company and Times Electronics are exempt from PRC enterprise income tax up to 30 September 2007.

The Group's effective tax rates for the years ended 31 December 2005 and 2006 were 0.3% and 0.1%, respectively.

Net profit attributable to equity holders of the parent

The Group's net profit attributable to equity holders of the parent increased from RMB211.7 million for the year ended 31 December 2005 to RMB296.8 million for the year ended 31 December 2006. The Group's net profit margins for the years ended 31 December 2005 and 2006 were 21.2% and 23.6%, respectively.

Minority interests

Minority interests decreased from RMB6.2 million for the year ended 31 December 2005 to RMB5.5 million for the year ended 31 December 2006. This was mainly due to the Group's acquisition of 10% interest in Times Electronics in June 2006, after which Times Electronics became a wholly owned subsidiary of the Group, while the Group recognized the minority interests of Times Electronics only for the six months ended 30 June 2006.

Liquidity and source of capital

Cash flow and working capital

The Group's working capital were mainly sourced from cash derived from operations and short-term loans. The Group's cash and cash equivalents increased substantially during the year, which was mainly due to the receipt of proceeds from the Group's initial public offering on the Stock Exchange of Hong Kong on 20 December 2006. All the Directors believe that the Group has sufficient liquidity to meet its present requirements for funds.

Net cash from operation activities

For the year ended 31 December 2006, the Group's net cash from operation activities increased to RMB198.0 million. The increase was mainly due to the increase in profit.

Net cash outflow from investment activities

For the year ended 31 December 2006, the Group's net cash outflow from investment activities was approximately RMB148.0 million, including RMB102.6 million for the purchase of properties, plant and equipment.

Net cash flow from financing activities

For the year ended 31 December 2006, the Group's net cash inflow from financing activities amounted to RMB2,046.2 million, which was mainly comprised of proceeds amounting to HK$2,197,613,000 or RMB2,209,968,000 at the prevailing exchange rate on the date of payment raised from the Company's initial public offering of 414,644,000 H shares at HK$5.30 per share, and interest income of approximately HK$22,537,000 or RMB22,666,000 at the prevailing exchange rate on the date of payment, earned in connection with the Company's initial public offering.

Liquidity

The Directors agree that the Group has sufficient liquidity to meet the Group's present requirements for funds.

Commitments

The Group's capital commitments at the dates indicated were as follows:

	As at 31 December	
	2006 (RMB'000)	2005 (RMB'000)
Contracted but not provided:		
Acquisitions of properties, plants and equipment	**38,232**	35,487

Indebtedness

The table below sets out the Group's indebtedness on the dates as indicated:

	As at 31 December	
	2006 (RMB'000)	2005 (RMB'000)
Interest bearing loans and other borrowings	**364,537**	252,521

In November 2006, the Group borrowed new short-term bank loans totaling RMB168 million, which were mainly used for payment of special dividends of RMB167,538,000 which the Company declared on 29 November 2006 and distributed on 30 November 2006.

Gearing ratio

As at 31 December 2005 and 31 December 2006, the Group's total borrowings were RMB252.5 million and RMB364.5 million, respectively. Increase in borrowings was mainly due to the new short-term bank loans totaling RMB168 million which the Group obtained in November 2006, and was used for the payment of special dividends of RMB168 declared on 29 November 2006 and distributed on 30 November 2006. The percentage of the Group's total borrowings to total assets as at 31 December 2005 was 17.0%, and 9.6% as at 31 December 2006. The decrease was mainly due to the inflow of the proceeds from the Company's initial public offering.

Contingent liabilities

The Group was not involved in any material litigation, and so far as the Group is aware, the Group has no pending or potential material litigation.

Employees and remunerations

The Group offers salary increments and bonuses to employees with outstanding performance. The bonus scheme is discretionarily determined with reference to the performance of the staff and the Group's operation results. The Group places great emphasis on on-the-job-training and development of its employees. Each staff member is required to participate in departmental training prior to his or her employment. In the subsequent years, all employees, including management representatives, are required to undergo further training as designated by the Group. As at 31 December 2006, the Group has 2,581 full-time employees, and the total salaries (including wages and allowances) paid to the employees in 2006 amounted to approximately RMB139,462,000.

Market risks

The Group is subject to various market risks, including interest rate risks, foreign exchange risks and inflation risks in the ordinary course of its business and those risks as detailed in note 36 to the financial statements.

Directors, Supervisors and Senior Mangagement

Directors

Liao Bin

aged 44, the Chairman of the Board and a non-executive Director of the Company. Mr. Liao joined ZELRI in August 1983 and has held the positions of general manager of Zhuzhou Times Rubber & Plastics Co. Ltd. from 1998 to 2000, deputy director of ZELRI and general manager of Times New Materials from 2000 to 2001, deputy director of ZELRI and chairman of the board of directors of Times New Materials from 2001 to 2004, and director of ZELRI since 2004. Mr. Liao is also a director of Times New Materials, a company listed on the Shanghai Stock Exchange. Mr. Liao graduated from South China University of Science and Engineering with a bachelor's degree in 1983 and finished his master's degree in administration study at the Institute of Commerce of Hunan University in 1996. Mr. Liao was appointed as an executive Director of the Company in September 2005 and re-designated as a non-executive Director of the Company in November 2006.

Tian Lei

aged 43, the Vice Chairman of the Board and a non-executive Director of the Company. Mr. Tian joined the Parent Group in April 1988 and has held the position of director of personnel education division in ZELRI from 1996 to 1998, and appointed deputy director of ZELRI in 1998 and has been the party secretary and deputy director of ZELRI since 2000. Mr. Tian is also a director of Times New Materials, a company listed on the Shanghai Stock Exchange. Mr. Tian graduated from Changsha Railway Institute with a bachelor degree in 1985 and from Shanghai Railway Institute with a master degree in 1988. Mr. Tian was appointed as an executive Director of the Company in September 2005 and re-designated as a non-executive Director of the Company in November 2006

Ding Rongjun

aged 46, an executive Director and the president of the Company. Mr. Ding joined the Parent Group in August 1984 and has held the positions of deputy director and project manager of the scientific research division of ZELRI from 1999 to 2000, and deputy director, deputy chief engineer and chief engineer of ZELRI between 2000 and 2005. Mr. Ding graduated from Southwest Jiaotong University with a bachelor degree in 1984 and from Changsha Railway Institute with a master degree in 1996. Mr. Ding was appointed as an executive Director of the Company in September 2005.

Lu Penghu

aged 41, an executive Director, joint Company secretary, party secretary and chief administration officer of the Company. Mr. Lu joined the Parent Group in November 1990 and has held the positions of deputy director of PCB Factory, director of the general office, acting director of planning and development department in ZELRI. Mr. Lu graduated from Lanzhou University in 1989 with a degree in journalism, from Xiangtan University in 2001 with a bachelor degree in law, and from Wuhan University with a master degree in software engineering in 2005. Mr. Lu was appointed as an executive Director of the Company in November 2006.

Ma Yunkun

aged 53, a non-executive Director of the Company. Mr. Ma has more than 10 years of experience in business management and is the chairman of the board of directors and general manager of Kunming China Railway since 2004. Mr. Ma held the positions of deputy director of Kunming Machine Factory from 1994 to 2003 and vice chairman of the board of directors and general manager of Kunming China Railway from 2003 to 2004. Mr. Ma was appointed as a non-executive Director of the Company in September 2005.

Zhou Heliang

aged 75, an independent non-executive Director. Mr. Zhou is a senior engineer and professor and has more than 45 years of experience in the electro-technical industry. Mr. Zhou was director and deputy director of the Electrical Equipment Industry Bureau in the PRC Ministry of Machinery Industry from 1982 to 1987, director of the Major Technical Equipment Office of the Commission of Machinery Industry of the PRC from 1987 to 1990, director of the Major Technical Equipment Office in the PRC Ministry of Machinery and Electronics Industry from 1990 to 1994, and deputy director general and general secretary of the China Electro-technical Society from 1994 to 2004. Mr. Zhou is an honorary director general of the China Electro-technical Society, a member of the expert committee of the China Machinery Industry Federation, vice chairman of the Asian Electric Automobile Institute and an executive committee member of the Asia Pacific Electric Automobile Association. Mr. Zhou was appointed as an independent non-executive Director of the Company in November 2006.

Gao Yucai

aged 66, an independent non-executive Director. Mr. Gao is a senior engineer and has more than 20 years of experience in the urban rail transportation industry. Mr. Gao was deputy director of Beijing Public Utility Bureau from 1983 to 1990 and general manager of Beijing Metro Corporation from 1990 to 2001. Mr. Gao is a commissioner of China Communication and Transportation Association ("CCTA") and vice director of the urban rail transportation committee of CCTA. Mr. Gao graduated from PLA Engineering Academy (one of the predecessors of PLA University of Science and Technology) in 1966. Mr. Gao was appointed as an independent non-executive Director of the Company in November 2006.

Chan Kam Wing, Clement

aged 49, an independent non-executive Director of the Company. Mr. Chan is a certified public accountant in Hong Kong, a member of the Hong Kong Institute of Certified Public Accountants and the Institute of Chartered Accountants in England and Wales. Mr. Chan possesses the appropriate financial management expertise as required by the Listing Rules. Mr. Chan has been Asia Pacific regional director of Horwath International and the managing director in Horwath Hong Kong CPA Limited since 1996. Prior to that, Mr. Chan operated his own accounting firm. Mr. Chan was appointed as a member of the auditing team of Beijing 2008 Olympics Organisation Committee in 2003. Mr. Chan graduated from City University London with a bachelor degree in accounting and from the University of New South Wales with a master degree in commerce. Mr. Chan was appointed as an independent non-executive Director of the Company in September 2005.

Pao Ping Wing

aged 59, an independent non-executive Director of the Company. Mr. Pao was a Fellow of the Hong Kong Institute of Housing. Mr Pao is an independent non-executive director of Oriental Press Group Limited, UDL Holdings Limited, Sing Lee Software Limited and Hembly International Holdings Limited, and also the Deputy Chairman of Biomax Environment Holdings Limited. Mr. Pao was appointed as a Justice of Peace since 1987. Mr. Pao was appointed by the Hong Kong SAR Government as a member of the Town Planning Board, the Advisory Council on the Environment, the Hong Kong Housing Authority and the Land Development Corporation. Mr. Pao obtained a master degree in science of human settlement planning and development. Mr. Pao was appointed as an independent non-executive Director of the Company in September 2005.

Tan Xiao'ao

aged 43, an independent non-executive Director of the Company. Mr. Tan has been a practising PRC lawyer since 1989 and a law professor at the law faculty of the Central China University and Hunan University since 2003. Mr. Tan was director of the Jiaoyang Law Office from 1996 to 2002, the general counsel of Hunan Taizinai Group from 2003 to 2004, deputy chairman of the board of directors, director and general manager of Hunan Taizinai Group Bio-tech Company Limited since 2004. Mr. Tan graduated from Zhongshan University with a bachelor degree in law in 1987 and from Qinghua University with a master degree of EMBA in 2006. Mr. Tan was appointed as an independent non-executive Director of the Company in June 2006.

Directors, Supervisors and Senior Mangagement

Supervisors

Zhang Liqiang, aged 44, a supervisor of the Company and the chairman of the Company's supervisory committee. Mr. Zhang joined the Parent Group in May 2005 as a senior accountant and has been the chief accountant of ZELRI since May 2005. Mr. Zhang was deputy director and the director of accounting department and the director of audit department in ZELW from 1996 to 2005. Mr. Zhang graduated from Hubei Finance and Economics Institute with a bachelor degree in financial accounting in 1983. Mr. Zhang was appointed as a supervisor of the Company in September 2005.

Pang Yiming, aged 43, a supervisor of the Company. Mr. Pang is the assistant to director of the marketing management department of the distribution center of the Company. Mr. Pang joined the Parent Group in October 1982 and has held positions of the assistant to the general manager of the manufacturing centre of ZELRI and deputy general manager of Times Electronics. Mr. Pang is also the chief production officer and director of the production department of Time Electronics. Mr. Pang graduated from Central South University in 2004 after a three-year study in management and engineering. Mr. Pang held 10% of the issued share capital in Times Guangchuang before transferring his entire shareholding in Times Guangchuang to Times Electronics in December 2006. Mr. Pang is not currently holding any issued share capital in Times Guangchuang. Mr. Pang was appointed as a supervisor of the Company in September 2005.

Jiang Yi, aged 36, a supervisor of the Company. Mr. Jiang is the director of the technical center of the Company. Mr. Jiang joined the Parent Group in August 1992 and has held the positions of deputy general manager of research and development department, director of human resources department, director of quality and service department, director of after-sale service department, deputy director of manufacturing centre of ZELRI. Mr. Jiang graduated from Northern Jiaotong University (predecessor of Beijing Jiaotong University) with a bachelor degree in electric traction and transmission control in 1992. Mr. Jiang was appointed as a supervisor of the Company in September 2005.

Liu Chunru, aged 36, an independent supervisor of the Company. Ms. Liu is a Certified Asset Valuer. She was vice president in Beijing China Enterprise Appraisal Co., Ltd. and has been a deputy general manager of Zhongfa International Appraisal Co., Ltd. since 2003. Ms. Liu graduated from Chongqing University with a bachelor degree in engineering in 1994. Ms. Liu was appointed as a supervisor of the Company in September 2005.

He Hongqu, aged 43, an independent supervisor of the Company. Mr. He has been a professor at the Institute of Commerce of Central South University since 2002. Mr. He was an associate professor at the Institute of Commerce of Central South University, director of accounting department and lecturer in Management Engineering Department in Central South University. Mr. He graduated from Hunan Institute of Finance and Economics with a bachelor degree in enterprise management in 1986 and a master degree in enterprise management in 1989 and graduated from Central South University with a doctorate in management in 2003. Mr. He was appointed as a supervisor of the Company in September 2005.

Senior Management

Lu Penghu, aged 41, an executive Director, joint secretary and chief administration officer of the Company. His biographical details are set out above.

Feng Jianghua, aged 43, chief technology officer of the Company. Mr. Feng is a professor level senior engineer. He joined the Parent Group in August 1989 and has held positions of deputy chief engineer, director of research and development Center and director of system integration department in ZELRI. Mr. Feng graduated from Zhejiang University with a bachelor degree in electric engineering in 1986 and a master degree in electric engineering in 1989.

Li Donglin, aged 40, chief marketing officer of the Company. Mr. Li joined the Parent Group in July 1989 and has held positions of deputy chief engineer, deputy general manager of rail transport department, director of manufacturing centre, deputy general manager of sales and marketing centre in ZELRI. Mr. Li graduated from Southwest Jiaotong University with a bachelor degree in electric traction and transmission control in 1989.

Cao Tianxuan, aged 43, chief financial officer of the Company. Mr. Cao was deputy chief economist of ZELRI from May to September 2005 and assistant to the president of the Company from September 2005 to March 2006. Before joining the Company, Mr. Cao has held the positions of chief financial controller in Hunan Tai Er Pharmaceutical Co., Ltd.. Mr. Cao graduated from Central South Finance and Economics University with a bachelor degree in accounting in 1986.

Shen Yuxiang, aged 44, chief planning officer of the Company. Mr. Shen joined the Parent Group in June 1990 and has held positions of deputy director of research and development division in ZELRI, general manager in Times Electronics. Mr. Shen graduated from Huazhong Institute of Technology (predecessor of Huazhong University of Science and Technology) with a bachelor degree in electrical power engineering in 1985 and a master degree in electrical power engineering in 1990.

Wang Xiaofang, aged 40, president assistant of the Company. Mr. Wang joined the Parent Group in July 1987 and has held positions of deputy chief engineer, general manager of safety equipment division, deputy general manager of rail transport department and deputy director of research and development centre in ZELRI. Mr. Wang graduated from Northern Jiaotong University with a bachelor degree in electrical engineering in 1987 and Central-South University with a master degree in information engineering and control in 2001.

Tang Tuong Hock, Gabriel, aged 54, is the qualified accountant and joint secretary of the Company. Mr. Tang has been a member of the Institute of Chartered Accountants in England and Wales since 1981 and is also a member of the Chartered Association of Certified Accountants in the United Kingdom. Mr. Tang has more than 20 years of experience in accounting and management in various industries.

Corporate Governance Report

The Company has always been dedicated to improving the quality of its management, and to maximizing long-term shareholder value by increasing the Group's accountability and transparency through strict implementation of corporate governance.

I Corporate Governance Practices

The Company places great emphasis on the authority, dependability and prudence of its corporate governance. For the reporting period ended 31 December 2006, the Company has adopted the principles contained in the Code on Corporate Governance Practices set out in Appendix 14 of the Listing Rules. Except for a deviation from clause A.5.4 of the CG Code (Standard code which must be complied with in securities transactions of Directors), the Company has complied with all other provisions of the CG Code.

The Company's Board of Directors makes every effort to comply with the CG Code in order to protect and enhance shareholder interest. As the Company continues to grow, in order to ensure compliance with relevant regulations and standards, the Company will monitor and, when necessary, revise its corporate governance policy on an ongoing basis.

In accordance with relevant laws and regulations, the Company has set up a structure in which corporate mechanisms such as shareholders' general meetings, the Board of Directors, special committees under the Board of Directors, the Supervisory Committee and powers of the management check and balance each other. The division of responsibilities between the shareholders' general meeting, the Board of Directors, special committees under the Board of Directors, the Supervisory Committee and the management are distinct, and each of them is assigned with clearly defined responsibilities. The Company will continue to perfect its corporate governance mechanism, exercise discipline in the fulfilment of corporate duties, and strengthen the disclosure of information concerning its operations.

II Securities Transactions by Directors

As of the end of the reporting period, the Company had not adopted a code of practice contained in the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules regarding securities transaction by its Directors. The main reason why the Company did not adopt this Model Code was the fact that its listing took place on 20 December 2006, and none of its securities was in circulation in the market prior to that date. Even though it had not formally instituted a code of practice, the Company made specific enquiries to its Directors about whether they had complied with the Model Code in their securities transactions. The Company confirms that all its Directors complied with the standards for securities transactions by directors as set out in the Model Code during the reporting period. In order to comply with the Listing Rules, it was resolved at the Ninth Meeting of the first term of the Board of Directors, held on 23 April 2007, that the Model Code be adopted as the Company's code of practice for securities transactions by Directors.

III Board of Directors

1. Composition of the Board of Directors

The Board of Directors consists of ten Directors, among whom Mr. Liao Bin is the Chairman of the Board and Mr. Tian Lei is its Deputy Chairman; Messrs. Ding Rongjun and Lu Penghu are executive Directors; Mr. Ma Yunkun is a non-executive Director; and Messrs. Zhou Heliang, Gao Yucai, Chan Kam Wing, Pao Ping Wing and Tan Xiao'ao are independent non-executive Directors.

Under the terms of their service contracts, Messrs. Liao Bin, Tian Lei, Ding Rongjun, Lu Penghu and Ma Yunkun will retire on the date of the 2008 Annual General Meeting; whereas, Messrs. Zhou Heliang, Gao Yucai, Chan Kam Wing, Pao Ping Wing and Tan Xiao'ao will retire on the date of the 2007 Annual General Meeting. Being eligible, they can offer themselves for re-election.

The Company's Directors have strictly complied with their undertakings, and have been honest, trust-worthy and diligent in the performance of their duties. The number of Directors and the composition of the Board comply with relevant laws and regulatory requirements. There is no relationship between the members of the Board (especially between the Chairman and the Chief Executive), including any financial, business, familial or other material relevant relationship.

The Company has received annual confirmation from Messrs. Zhou Jeliang, Gao Yuchai, Chan Kam Wing, Pao Ping Wing and Tan Xiao'ao of their independence, and considers that they are still independent as of the date of this report.

2. Board Meetings and Directors' attendances at Board Meetings

During the reporting period, the Company held seven Board Meetings, of which three were interim Board Meetings.

The following is the attendance record of Directors at Board Meetings held during the reporting period.

Name	Title	Number of Meetings that the Director should have attended	Number of Board Meetings attended by the Director	Attendance Rate	Remarks
Liao Bin	Chairman of of the Board	7	7	100%	Attended the third interim Board Meeting in 2006 by proxy
Tian Lei	Deputy Chairman of the Board	7	7	100%	Attended the third interim Board Meeting in 2006 by proxy
Ding Rongjun	Executive Director	7	7	100%	Attended the third interim Board Meeting in 2006 by proxy
Lu Penghu	Executive Director	2	2	100%	Elected as a Director at the Sixth Meeting of the First Term of the Board in November 2006

Name	Title	Number of Meetings that the Director should have attended	Number of Board Meetings attended by the Director	Attendance Rate	Remarks
Ma Yunkun	Non-Executive Director	7	7	100%	Attended the third interim Board Meeting in 2006 by proxy
Zhou Heliang	Independent Non-Executive Director	2	2	100%	Elected as a Director at the Sixth Meeting of the First Term of the Board in November 2006. Attended the third interim Board Meeting in 2006 by proxy.
Gao Yucai	Independent Non-Executive Director	2	2	100%	Elected as a Director at the Third Meeting of the First Term of the Board in November 2006. Attended the third interim Board Meeting in 2006 by proxy.
Chan Kam Wing	Independent Non-Executive Director	7	7	100%	Attended the third interim Board Meeting in 2006 by proxy
Pao Ping Wing	Independent Non-Executive Director	7	7	100%	
Tan Xiao'ao	Independent Non-Executive Director	4	4	100%	Elected as a Director at the Fifth Meeting of the First Term of the Board in June 2006. Attended the third interim Board Meeting in 2006 by proxy.

3. Proceedings at Board Meetings

The Board of Directors is responsible to the Shareholders' General Meetings in relation to the leadership and management of the Company. The Board convened Regular and Interim Meetings according to legal procedures and complied strictly with the laws, legal regulations and Articles of Association in the exercise of its authority, with an emphasis on protecting the interests of the Company and its Shareholders.

All Directors are given not less than 10 days' advance notice of Regular Board Meetings, and reasonable advance notice of Board Meetings other than Regular Meetings.

The Secretary to the Board records and prepares documents concerning all matters that are discussed during the Board Meetings. Draft minutes of every Board Meeting are circulated to all the directors for their review. After finalization, the Board minutes are signed by all Directors who have attended the meeting, the Secretary to the Board and the minutes recording person. These documents are permanently kept as an important record of the Company on the Company's premises.

The Board of Directors is responsible to the Shareholders, and it principally exercises the following authorities:

(1) Convening Shareholders' General Meetings, and reporting on its work to Shareholders' General Meetings;

(2) Executing resolutions of the Shareholders' General Meeting;

(3) Making decisions on operational plans and investment schemes;

(4) Formulating the annual financial budget and final accounts;

(5) Formulating the profit distribution scheme and scheme for loss compensation;

(6) Proposing schemes for major investments, major acquisitions or disposals, mergers, divisions or dissolution of the Company; and

(7) Proposing amendments to the Company's Articles of Association.

All Directors have access to the advice and services of the Company Secretary. The Company provides all Directors with the necessary information and data to enable them to make scientific, timely and prudent decisions. Any Director can request the Chief Executive, or, through the Chief Executive, request the Company's relevant department to provide him with any necessary information to enable him to make scientific, timely and prudent decisions. If any of the independent Directors consider necessary, an independent institution can be engaged to provide independent opinions to assist his decision-making. The expenses of engaging such an independent institution will be borne by the Company.

Director(s) with a vested interest in any transaction cannot participate in the vote that the Board of Directors takes with respect to that particular transaction. If a resolution cannot be passed due to the Director(s) exclusion from voting, the resolution will be submitted directly to the Shareholders' General Meeting for consideration by the shareholders.

4. Specialised Committees of the Board

The Company has established separate strategy, audit , risk management and remuneration committees. The function of each specialised committee is to study pertinent issues in its area of expertise and to provide opinions and suggestions for consideration by the Board of Directors. The Company has not yet set up a nomination committee.

a Strategy committee

The Company's strategy committee was established in October 2005. It currently consists of five Directors, two of whom are independent non-executive Directors. The members of the strategy committee are Messrs. Liao Bin, Tian Lei, Ding Rongjun, Zhou Heliang and Pao Ping Wing. Mr. Liao Bin is the strategy committee's chairman.

The main responsibilities of the strategy committee are:

(1) to provide study reports to the Board of Directors in respect of governmental policies and industrial trends;

(2) to conduct strategic research concerning the Group;

(3) to review and assess major investment and financial strategies;

(4) to review major capital expenditure projects.

The strategy committee did not convene any meetings during the reporting period. However, the Board of Directors considered and approved the Company's annual investment plan and feasibility reports on all major investment projects.

b Audit committee

The Company's audit committee was established in October 2005. It currently consists of five Directors, four of whom are independent non-executive Directors. The committee's members are Messrs. Chan Kam Wing, Zhou Heliang, Gao Yucai, Ma Yunkun and Tan Xiao'ao. Mr. Chan Kam Wing is the audit committee's chairman.

The main responsibilities of the audit committee are: to consider and supervise financial reporting processes and internal control procedures, to exercise its authority to guide and supervise internal audits, and to make suggestions about the appointment or change of external audit firm.

The audit committee held seven meetings during the reporting period. These meetings mainly discussed issues concerning the Company's annual results, half yearly results, audit work carried out for the Company's initial public offering, communication with the Stock Exchange of Hong Kong concerning the review of listing application documents, internal audit and internal controls related issues, etc. Following is the record of attendance of committee members.

Committee member	Attendance rate for meetings held during the year ended 31 December 2006
Chan Kam Wing	6/7
Zhou Heliang	1/1*
Gao Yucai	1/1*
Ma Yunkun	5/7
Tan Xiao'ao	6/6*

*Note: Messrs. Zhou Heliang and Gao Yucai were both appointed as independent non-executive Directors of the Company on November 2006. Mr. Tan Xiao'ao was appointed an independent non-executive Director of the Company in June 2006.

The Company has established an audit division with internal audit functions. The audit division is under the supervision of the audit committee.

c Risk management committee

The Company's risk management committee was established in June 2006. It currently consists of five Directors, three of whom are independent non-executive Directors. The members of the strategy committee are Messrs. Tian Lei, Chan Kam Wing, Ma Yunkun, Pao Ping Wing and Tan Xiao'ao. Mr. Tian Lei is the risk management committee's chairman.

The main responsibility of the risk management committee is to formulate, assess and revise risk management strategies.

The risk management committee did not hold any meetings during the reporting period. In spite of this, members of the risk management committee participated in the discussion of risk management and internal control related issues with Company management and with the Company's sponsors for its initial public offering, during and after the Company's initial public offering.

d Remuneration committee

The Company's remuneration committee was established in October 2005. It currently consists of five Directors, three of whom are independent non-executive Directors. The committee members are Messrs. Pao Ping Wing, Gao Yucai, Ding Rongjun, Chan Kam Wing and Lu Penghu. Mr. Pao Ping Wing is the remuneration committee's chairman.

The main responsibilities of the remuneration committee are to consider the remuneration and benefits of Directors and senior management, and to make recommendations to the Board of Directors about any related adjustments.

Since the Company did not make any major changes in its remuneration scheme during the reporting period, the remuneration committee did not hold any meetings. However, all the remuneration and benefits of the Directors and senior management members, and their service contracts were considered and approved by the Board of Directors.

IV Chairman and Chief Executive

The offices of the Chairman and the Chief Executive of the Company are held by Mr. Liao Bin and Mr. Ding Rongjun, respectively. The division of responsibilities between them has been clearly established and set out in writing. The Chairman is responsible for running the Board and chairing Board meetings whereas the Chief Executive is responsible for the Company's day-to-day operations.

According to the Articles of Association, the Chairman exercises the following authorities:

(1) To preside over Shareholders' General Meetings, and to convene and preside over Board Meetings;

(2) To monitor the implementation of the Board's resolutions;

(3) To sign securities issued by the Company; and

(4) Other authorities conferred on him by the Board of Directors.

The Chief Executive is responsible to the Board of Directors. The Chief Executive and the management team under his leadership have the following authorities:

(1) Management of the Company's manufacturing and sales operations and the implementation of the Board's resolutions;

(2) Implementation of the Company's annual operational plan and investment strategies;

(3) To establish the Company's internal management mechanisms;

(4) Establishment of the Company's basic management systems;

(5) Formulation of the Company's basic regulations;

(6) Proposing the appointment and dismissal of Deputy Chief Executive, Chief Supervisor and assistant to the Chief Executive of the Company;

(7) Appoint or dismissing management staff, except those who should be appointed or dismissed by the Board of Directors; and

(8) Making proposals concerning wages, benefits, bonuses and penalties for employees, and deciding on the appointment and dismissal, promotion or demotion, increases or decreases in salary, appointment, employment, termination of employment or dismissal of employees.

V Non-executive Directors

According to the Articles of Association, the Company's non-executive Directors are elected by Shareholders' General Meetings for a term of three years. Upon retirement, non-executive Directors are eligible for re-election.

VI Nomination of Directors

Directors are elected by the Shareholders' General Meetings in accordance with its articles of association. Written notice of intention to nominate a candidate for the post of Director and the candidate's agreement to be nominated must be given to the Company after the date of the notice of the Annual General Meeting and at least seven days prior to the convening of the Annual General Meeting.

VII Remuneration of the auditors

During the year ended 31 December 2006, the Company appointed Ernst & Young as its reporting accountant for its initial public offering on the Main Board of the Stock Exchange of Hong Kong. Ernst & Young also provides annual audit services to the Company. Details of the external auditors' remuneration are as follows:

Service provided:	**For the year ended 31 December 2006** (RMB' 000)
Annual audit	3,600
Reporting accountant for listing	10,550

VIII Directors' responsibilities in respect of the financial reports

The Directors confirm that they are responsible for the preparation of financial reports, and to give a true and fair view of the Company's and the Group's financial status and operating results for the year ended 31 December 2006.

The Directors also confirm that there were no major unexpected events or conditions that would have a significant impact on the continuity of the Company's operations.

IX Internal controls

The Directors are responsible for maintaining a reliable and effective internal control system. The Company has established an internal audit department. An audit committee and a risk management committee have also been established and are responsible to the Board of Directors. The Directors are in a position to supervise, assess and improve the Company's internal controls at all levels of management, so as to ensure that the Company can withstand changes in its operations and other external influences on its finance, operation and risk management, in order to safeguard the Company's assets and promote Shareholders' interests.

During the reporting period, in accordance with guidance note entitled "internal control and risk management - basic framework" issued by Hong Kong Institute of Certified Public Accountant, the Company employed an independent international risk consultancy firm to fully assess the Company's internal control system from entity and work flow perspectives. Risks are qualified and quantified, and the internal control system is examined with reference to guidance note "internal control - consolidated structure" issued by COSO which examines qualitative and quantitative factors. In relation to detected internal control weaknesses, the Company made appropriate changes, and established a new system of controls. These changes mainly dealt with internal controls in relation to procurement, sales, inventory, finance and connected transactions.

After instilling a new system of internal controls, the Company engaged the same risk consultancy firm to examine whether the new system is operating effectively. The results of the walk-through and entity level tests indicate there were no major detected internal control weaknesses. With reference to the conclusion reached by the risk consultancy firm, the Directors and Company management believe that issues concerning the Company's internal controls have been properly handled.

X Compliance with the non-competition and indemnity agreements by the Controlling Shareholders

ZELRI, the controlling shareholder of the Company, and CSR Group, the ultimate controlling shareholder (hereinafter referred to as "Controlling Shareholders"), have each submitted their "explanations regarding the implementation of the non-competition and indemnity agreement in 2006" to the Company respectively, declaring that they had complied with the terms of the said agreements. The Company's independent non-executive Directors have also reviewed the implementation of the non-competition and indemnity agreements by the controlling shareholders in 2006. The independent non-executive Directors consider that the Parent Group and the CSR Group had complied with the terms of the non-competition and indemnity agreements. The respective businesses, of the Parent Group and the CSR Group were independent of the Group's business, employing different technologies, and have different customers, and will not result in any competition with the Group. The Directors were able to uphold the interests of the Company and the shareholders, and operated and managed the Company's business independently.

Directors' Report

The Directors of the Company are pleased to present the Directors' Report and audited financial statements of the Company and the Group for the year ended 31 December 2006.

The Company's Business Activities

The Group is a leading train-borne electrical system provider and integrator in the PRC railway industry. We also engage in developing, manufacturing and selling train power converters, auxiliary power supply equipment and control systems for urban rail systems. Additionally, the Group designs, manufactures and sells electrical components for the PRC railway industry, the urban rail industry and non-railway applications.

There have been no significant changes in the nature of the Group's key operations during the reporting period.

Results and dividends

Results of the Group for the year ended 31 December 2006, prepared in accordance with the IFRSs, are set out on page 37 to page 90 of this annual report.

On 28 November 2006, the Company paid a special dividend of RMB0.23 per share, amounting to RMB167,538,000.

Based on the lower of the Company's net profit calculated under PRC GAAP and IFRSs, the Company has distributable profits (before the proposed final dividend) of RMB89,299,000 as at 31 December 2006. The Board of Directors of the Company proposed distribution of a cash dividend of RMB0.034 per share (including applicable tax) for the year. The dividend to be distributed is subject to approval by shareholders at the Annual General Meeting to be held on 15 June 2007.

The dividends shall be available to shareholders whose names are listed on the register of members at the close of business on 15 May 2007. The Company's share register will be closed from 16 May 2007 to 15 June 2007 (both days inclusive), during which no transfer of shares will be registered.

In respect of distribution of dividends, dividends for Domestic Shares will be distributed and paid in Renminbi, while dividends for H Shares will be declared in Renminbi, but paid in Hong Kong dollars. (The Hong Kong dollars shall be calculated at the average middle rate of Renminbi to Hong Kong dollars announced by the People's Bank of China five work days prior to the dividend declaration date by the Annual General Meeting on 15 June 2007).

Use of proceeds from the Company's initial public offering

The Company issued 414,644,000 H shares (including H shares issued via the exercise of the over–allotment option) in an initial public offering in December 2006. The issue price was HK$5.30 per share, the proceeds amounted to approximately HK$2,197,613,000 (equivalent to RMB2,209,968,000). The net proceeds from the initial public offering after deducting share issuing expenses amounted to RMB2,109,852,000. All proceeds were received by the Company by 28 December 2006.

The Company intends to put the the proceeds raised from its initial public offering to the following uses:

(1) Investment in relation to train power converter, auxiliary power supply equipment and control systems;

(2) Investment in relation to train operation safety equipment;

(3) Investment in relation to importation of technology and development of a new generation of railway maintenance vehicles;

(4) Investment in relation to large size power semi-conductor devices;

(5) Investment in relation to sensors and related products;

(6) Other areas, such as investment in the establishment of an export and overseas sales networks and implementation of ERP system; and

(7) Supplementing working capital.

To the extent that the net proceeds are not immediately applied for the above purposes, it is the intention of the Directors to place such proceeds in interest bearing bank accounts or invest in short-term bonds as permissible under the applicable laws and regulations.

Financial Highlights

Property, plant and equipment

Details of the movements in the property, plant and equipment of the Company and the Group during the year are set out in note 13 to the financial statements.

Borrowings

Details of the Group's borrowings as at 31 December 2006 are set out in note 28 to the financial statements.

Share capital

Details of the movements in the share capital of the Company during the year are set out in note 29 to the financial statements.

Pre-emptive rights

There are no provisions for pre-emptive rights under the Companies Law of the PRC and in the Company's Articles of Association which oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

Purchase, redemption or sale of listed securities of the Company

The H Shares of the Company were listed on the Main Board of the Stock Exchange of Hong Kong on 20 December 2006. During the year, there was no purchase, redemption or sale of any listed securities of the Company by the Company or any of its subsidiaries.

Reserves

Details of the movements in the reserves of the Company during the year are set out in note 30 to the financial statements and the consolidated statement of changes in equity.

Distributable reserves

As at 31 December 2006, calculated in accordance with relevant regulations, the Company's distributive reserves available for distribution amounted to approximately RMB89,299,000, of which approximately RMB36,865,000 has been proposed to be paid as final dividends for the year.

Charitable donations

The Group's total charitable donations for the year amounted to RMB1,120,000.

Major customers and suppliers

The percentage of sales attributable to the Group's five largest customers during the year was approximately 37% of the Group's total sales.

ZELC is the largest customer of the Group, and the percentage of the Group's sales to ZELC during the year was approximately 11% of the Group's total sales. ZELC is owned as to 12.61% by the Parent Company, and is beneficially owned as to 98.74% by CSR.

CSR Sifang Locomotive and Rolling Stock Co., Ltd. is one of the Group's five largest customers, and is owned as to 84.13% by CSR.

CNR Datong Electric Locomotive Co., Ltd. is another one of the Group's five largest customers, and is owned as to 94.16% by CNR.

Kunming China Railway is also one of the Group's five largest customers, and is owned as to 1.06% by the Parent Company. Mr. Ma Yunkun, a Non-executive Director of the Company, is the chairman and general manager of Kunming China Railway.

Save as disclosed above, none of the Directors, their associates or those shareholders so far as is known to the Directors having over 5% in the share capital of the Company, has any interest in any one of the Group's five largest customers during the year.

Purchases from the Group's five largest suppliers during the year were in aggregate less than 30% of the Group's total purchases during the year.

Biographies of Directors

Details of the biographies of the Company's Directors are set out on page 12 to page 13 of this annual report.

Service contracts with Directors and Supervisors

The Company has entered into service contacts with all of its Directors and supervisors, of whom the executive Directors, non-executive Directors and supervisors shall retire at the end of the 2008 Annual General Meeting. Independent non-executive Directors shall retire at the end of the 2007 Annual General Meeting. On retirement and after being re-elected at the Company's Annual General Meeting, they will be eligible to continue in their original offices and under the terms of the original service contracts. Each such re-election will be for a tenure of three years or for a shorter period as decided by the shareholders at the Annual General Meeting.

Remuneration Information of Directors and Supervisors

Remuneration of Directors and supervisors must be approved by shareholders at the Annual General Meeting. Other emoluments are fixed by the Board of Directors according to the Directors' duties and responsibilities and the Company's performance. Details of Directors' and supervisors' emoluments are disclosed in note 8 to the financial statements.

Directors' and supervisors' interests in contracts

During the year none of the Directors had a material interest, whether directly or indirectly, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party.

Interests and short positions of Directors, supervisors and the Chief Executive in the shares of the Company

As at 31 December 2006, none of the Directors, supervisors, the chief executive of the Company or their respective associates had any personal, family, corporate or other interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) required to be notified to the Company and the Stock Exchange of Hong Kong pursuant to Part XV of the SFO, or any interests or short positions in the shares required, pursuant to section 325 of the SFO, to be entered in the register referred to therein, or any personal, family, corporate or other interests or short positions required to be notified to the Company and the Stock Exchange of Hong Kong in other ways pursuant to the Model Code.

Directors' and supervisors' rights to acquire shares or debentures

At no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate granted to any Directors, supervisors or their respective spouse or children under 18 years of age, or were any such rights exercised by them, or was the Company or any of its subsidiaries a party to any arrangement to enable the Directors to acquire such rights in any other body corporate.

Structure of share capital

The Company's share capital structure as at 31 December 2006 was as follows:

		As at 31 December 2006	
Shareholder	**Type**	**Number of shares**	**% of issued share capital**
ZELRI	Domestic share	589,585,699	54.38%
CSR Qishuyan	Domestic share	9,380,769	0.87%
New Leap	Domestic share	9,380,769	0.87%
ZELC	Domestic share	10,000,000	0.92%
Kunming China Railway	Domestic share	9,800,000	0.90%
Shares in public circulation	H shares	456,108,400	42.06%
Total		1,084,255,637	100%

Substantial shareholders

Interests and short positions in the shares and relevant underlying shares of the Company or any of its associated corporations pursuant to the disclosure requirements in Divisions 2 and 3 of Part XV of the SFO (interests and short positions in the shares and relevant underlying shares of the Company disclosed here were interests and short positions of the following persons other than Directors or Chief Executive of the Company) as at 31 December 2006 were as follows:

Name of substantial shareholder	Number of shares held	Capacity	% of domestic share share capital	% of H Share share capital	% of issued share capital
ZELRI	589,585,699(L)	Beneficial owner	93.86%	—	54.38%
CSR (Note 1)	618,347,237(L)	controlling shareholder	98.43%	—	57.03%
Macquarie Bank Limited	54,084,000(L)	Beneficial owner	—	11.86%	4.99%
National Social Security Fund Council	36,647,300(L)	Beneficial owner	—	8.03%	3.38%
UBS AG	27,644,600(L)	Beneficial owner	—	6.06%	2.55%
Prime Capital Management (Cayman) Limited	25,000,000(L)	Beneficial owner	—	5.48%	2.31%

Note:

(1) ZELRI is owned as to 51% by CSR. CSR is a state-owned enterprise. CSR is directly interested as to 100% in the registered capital of CSR Qishuyan, directly and indirectly interested as to 100% in the registered capital of New Leap and directly and indirectly interested as to 98.74% in the registered capital of ZELC. Accordingly, CSR is deemed under the SFO to be interested in the Shares held by each of ZELRI, CSR Qishuyan, New Leap and ZELC.

Connected transactions

Transactions conducted between the Group and the following parties shall constitute continuing connected transactions after the listing of the H shares of the Company on Stock Exchange of Hong Kong under the Listing Rules.

The Directors of the Company, including the independent non-executive Directors of the Company, have reviewed and confirmed that the continuing connected transactions set out below have been entered into:

(1) in the ordinary and usual course of business of the Group;

(2) either on normal commercial terms or on terms no less favourable to the Group than terms available to or from independent third parties; and

(3) in accordance with the terms of the agreements governing the relevant transactions, and on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

Details of the Group's continuing connected transactions are as follows:

1) Continuing connected transactions exempted from reporting, public announcement and independent shareholders' approval requirements

The following transactions constituted continuing connected transactions for the Company under Rule 14A.33(3) of the Listing Rules and thus are exempted from the reporting, announcement and independent shareholders' approval requirements under Chapter 14 of the Listing Rules.

(a) On 1 January 2005, ZELC (as lessor) signed a lease with the Company (as lessee) for leasing a property and certain equipment. ZELC agreed to let to the Company a total area of 4,779.18m^2 of factory premises and relevant equipment for a term of three years from 1 January 2005 to 31 December 2007. The annual lease rental was RMB126,700 (excluding management fees and utility charges). The Company has paid ZELC RMB126,700 up to 31 December 2006.

(b) On 28 July 2006, Times Electronics (as lessor) signed a lease with NERCC (as lessee) for leasing a property. Times Electronics agreed to let to NERCC a total area of 3,116m^2 of factory premises for a term of six months from 1 July 2006 to 31 December 2006. The lease rental was RMB175,000. Rental receivable by Times Electronics from NERCC was RMB175,000 up to 31 December 2006.

(c) On 20 January 2006, the Parent Company (as a franchise grantor) signed a trademark licence agreement with the Company. The Parent Company agreed to franchise a trademark "TEG & device" to the Company and its subsidiaries on a non-exclusive basis for the period up to the validity period from 2012 to 2015 (subject to renewal) with effect from 1 January 2006. The Company has paid the Parent Company franchise fees of RMB10,000 up to 31 December 2006.

2) Continuing connected transactions exempted from independent shareholders' approval requirement but subject to reporting and public announcement requirements ("Exempt Transactions")

The following transactions constituted continuing connected transactions for the Company under Rule 14A.34 of the Listing Rules and thus are exempted from the requirement to obtain independent shareholders' approval, but were subject to the reporting and announcement requirements. The Company had already reported to the Stock Exchange of Hong Kong and the Stock Exchange of Hong Kong has granted a waiver from strict compliance with the announcement requirement under Rule 14A.47 of the Listing Rules.

(a) The Company signed a lease on 29 March 2006 as the lessor with the Parent Company (the lessee). The Company agreed to let to the Parent Company four stories of research administrative building with a total area of 6,960m^2 for a term of three years from 1 January 2006 to 31 December 2008. The annual lease rental was RMB1,867,184. The Company had received from the Parent Company RMB1,867,184 up to 31 December 2006.

(b) The Parent Company signed an equipment leasing agreement on 25 March 2006 as the lessor with the Company. A supplementary agreement was signed on 30 May 2006. The Parent Company agreed to lease certain testing equipment to the Company for three years from 1 January 2006 to 31 December 2008. The annual lease rental was RMB 9,025,072. The Company had paid the Parent Group rental of RMB2,256,268 up to 31 December 2006.

3) Non-exempt continuing connected transactions ("Non-exempt Transactions")

The following transactions constituted non-exempt continuing connected transactions for the Company and thus are subject to reporting, announcement and independent shareholders' approval requirements under Rule 14A.45 to 14A.48 of the Listing Rules. The Stock Exchange of Hong Kong has granted a waiver from strict compliance by the Company with the announcement and independent shareholders' approval requirements in respect of these transactions.

(a) On 4 December 2006, the Company signed a general service agreement with the Parent Company. The Parent Company agreed to provide members of the Group general services for the period from 20 December 2006 (the Company's listing date) to 31 December 2008. The Company had paid RMB 6,780,836 service fee to the Parent Company up to 31 December 2006.

(b) On 4 December 2006, the Company signed a mutual supply agreement with the Parent Company. The Company and its subsidiaries will supply certain electrical components to Parent Company, while the Parent Company and its subsidiaries also agreed to supply mechanical and electro-mechanical parts and components to the Company. The agreement is valid for three years from 20 December 2006 (the Company's listing date) to 31 December 2008.

Up to 31 December 2006, the amount payable by the Company to the Parent Company for mutual provision of services for the year amounted to RMB140,659,704 (excluding amount payable to Shiling by the Company). The amount paid by the Parent Company to the Company for mutual provision of services for the year amounted to RMB37,900,059.

(c) On 4 December 2006, the Company signed a mutual supply agreement with CSR. The Company and its subsidiaries will sell train-borne electrical systems and electrical components of different segments to the CSR Group while the CSR Group) also agreed to supply certain parts and components for the production of train-borne electrical systems to the Group. The agreement is valid for three years from 20 December 2006 (the Company's listing date) to 31 December 2008.

Up to 31 December 2006, the amount due by the Company to the CSR Group for mutual services it provided to the Company amounted to RMB21,958,573. The amount due by the CSR Group to the Company for mutual supplies services provided to the CSR Group amounted to RMB260,886,171.

(d) On 4 December 2006, Kunming China Railway and the Company entered into a mutual supply agreement under which the Company agreed to supply and procure its subsidiaries to supply certain electrical control systems for large railway maintenance vehicles to Kunming China Railway and its subsidiaries (together the "Kunming China Railway Group") and Kunming China Railway also agreed to supply and procure its subsidiaries and associates to supply certain parts and components in relation to large railway maintenance vehicles to the Group from 20 December 2006 (the Company's listing date) to 31 December 2008. Kunming China Railway, as licensee, entered into a technology license agreement with a European company, as licensor, in relation to the license of the technology for large railway maintenance vehicles. As part of the consideration for the technology license, Kunming China Railway agreed to procure parts and components from the licensor in an amount equal to a fixed percent of its sales income from certain types of large railway maintenance vehicles ("procurement percentage"). Kunming China Railway has in turn formed a consortium with the Parent Company (implemented by the Group) and three other companies to manufacture large railway maintenance vehicles. With respect to each type of large railway maintenance vehicle, the parties would agree on what percentage they will each receive from the sales income ("revenue percentage"). For the type of product Kunming China Railway is obligated to procure parts and components from the licensor, each party of the consortium would also be obligated to procure parts and components from the licensor (through Kunming China Railway) in an amount equal to the sales income from relevant type of products multiplied by procurement percentage and revenue percentage.

For the year ended 31 December 2006, fees payable to the Kunming China Railway Group by the Group amounted to approximately RMB23,816,498. Fees payable to the Group by the Kunming China Railway Group amounted to approximately RMB108,581,997.

(e) As the Parent Group holds 50% equity interest in Shiling and the Company has not completed the acquisition of 50% interest in Shiling in 2006, Shiling is considered as a connected party of the Company. According to the subsisting contracts for 200 km/h EMU projects and the OEM and packaging services of certain city railway projects, the Company will continue to purchase certain imported electronic parts and components from Shiling in 2006-2007.

Up to 31 December 2006, the amount due by the Company to Shiling for supply services it provided to the Company amounted to RMB49,712,849.

Pursuant to Chapter 14A.38 of the Listing Rules, the board of directors engaged the auditors of the Company to perform certain agreed upon procedures in respect of the continuing connected transactions of the Group. The auditors have reported their factual findings on these procedures to the board of directors. The independent non-executive directors have reviewed the continuing connected transactions and the report of the auditors and have confirmed that the transactions have been entered into by the Group in the ordinary course of its business, on terms no less favourable than terms available to and from independent third parties, in accordance with the terms of the agreements governing such transactions that are fair and reasonable and in the interest of the shareholders of the Company as a whole and have not exceeded the limit disclosed in the Company's prospectus dated 8 December 2006.

Mechanism for protecting minority interests

In order to protect minority interests, the Company has (inter alia) established and operated the following governance measures:

(i) Directors who have interests shall announce their respective interests, and waive their rights to attend Board Meetings and abstain from voting in respect of the connected transactions they are interested in. Accordingly, Messrs. Liao Bin and Tian Lei waived their rights to attend the Board Meetings and abstained from the related voting in respect of connected transactions between the Company and the Parent Group. Mr. Ma Yunkun waived his rights to attend the Board Meeting and abstained from the related voting in respect of connected transactions between the Company and Kunming China Railway.

(ii) An independent professional management team of the Group shall be responsible to negotiate and review the terms of transactions to be conducted with the suppliers and customers (including the Parent Group and CSR Group). The members of the management team shall include the staff of the Group with relevant techniques and sales expertise, and the scope of functions of the management team will ensure its ability to make independent business judgments. The management team shall report to the Board of Directors, while the Board of Directors shall be accountable to the Company and the shareholders taken as a whole.

(iii) The Company's auditors shall provide quarterly reports to the independent non-executive Directors on all transactions conducted between the Company and the Parent Group/CSR Group/Kunming China Railway.

(iv) When making purchases, the Group shall make efforts to obtain offers or quotations from a number of independent suppliers, and select successful offers (where applicable) based on objective standards such as the price and quality of products, delivery schedule and services.

(v) Subject to (i) above, Board Meetings attended by all independent non-executive Directors shall decide whether the Group shall conduct special transactions with the Parent Group or CSR Group.

(vi) The terms for supply and purchase arrangements entered into between the Group and the Parent Group or CSR Group shall be subject to quarterly reviews by the independent non-executive Directors, and opinions regarding such transactions shall be disclosed to shareholders by way of announcements. The Company shall make announcements to shareholders in a timely manner. Independent non-executive Directors may request an independent party having at least 10 years experience in the locomotive manufacturing industry to participate in assessing the terms of the sales and purchases agreements, and to provide their discoveries to the independent non-executive Directors.

Non-competition and indemnity agreements:

The Company has signed non-competition and indemnity agreements with the Parent Group and the CSR Group on 30 November 2006. The Parent Group and the CSR Group promised not to carry on businesses that are in competition with the Company's businesses respectively.

Independent directors of the Company have reviewed compliance of the non–competition and indemnity agreements by the Parent Group and the CSR Group for 2006, and reviewed relevant information provided by the Parent Group and the CSR Group. Independent directors of the Company were of the opinion: the Parent Group and CSR Group had complied with the relevant terms of the non–competition and indemnity agreements in 2006. The Parent Group and the CSR Group carried on their own businesses independently of the Company's businesses, each owning different technology applications and have different customers, which will not result in any competition with the Company. The Directors are able to operate and manage the Company's businesses independently on the premises of the Company's and shareholders' interests as a whole.

Sufficiency of public shareholdings

According to publicly available information and as far as the Directors were aware, public shareholders held at least 42.06% of the Company's issued share capital as at the date of this report.

Post Balance Sheet Event

Details of the Group's post balance sheet events are set out in note 37 to the financial statements.

Taxation

For the year ended 31 December 2006, no foreign shareholder who is not resident of the PRC is liable to individual or enterprise income tax, capital gains tax, stamp duty or estate duty of the PRC in relation to their holding of H shares of the Company. Shareholders are urged to consult their tax advisers regarding the applicable PRC, Hong Kong and other tax consequences of owning and disposing of H shares.

Auditors

The financial statements for the year have been audited by Ernst & Young, and a resolution will be tabled at the upcoming Annual General Meeting to re-appoint Ernst & Young as the Company's auditors.

Supervisory Committee's Report

In 2006, pursuant to Company Law, the Articles of Association, the Listing Rules and the Rules of Meeting of the Supervisory Committee, members of the Supervisory Committee performed their duties prudently and effectively with respect to the supervision of company operations and business activities in accordance with applicable rules and regulations so as to safeguard shareholders' and the Company's interests.

I. Meetings of the supervisory committee

The key contents were as follows:

1. During the year, the Company has held one supervisory committee meeting.

   The third meeting of the first term supervisory committee was held on 24 June 2006 at Zhuzhou, Hunan Province. The meeting considered and passed the following resolutions:

   — Approving the 2005 working report of the supervisory committee;

   — Approving the Company's 2006 annual financial budget reports;

   — Approving the signing of connected transection agreements;

   — Approving the resolution on the "appointment of audit firm for 2006";

   — Approving the "resolution on the amendment of the terms of the rules of meeting of the supervisory committee";

   — Approving auditors' reports for 2003, 2004 and 2005 issued by Ernst & Young.

2. During the year, members of the supervisory committee attended the 2005 Annual General Meeting, the first shareholders' meeting in 2006, the second shareholders' meeting in 2006, the fourth meeting of the first term of the Board of Directors, the fifth meeting of the first term of the Board of Directors, the sixth meeting of the first term of the Board of Directors, and the seventh meeting of the first term of the Board of Directors in person or via telecommunications means.

II. Independent opinion of the supervisory committee on certain issues in 2006

1. The Company carried on its operations lawfully

In 2006, in accordance with applicable laws and regulation, the supervisory committee carried out supervision with respect to the Company's shareholders' meeting, procedures adopted in the convening of directors' meetings, resolutions adopted, deliberation procedures, results of voting, implementation of resolutions of shareholders' meeting by Directors, the performance of duties of senior management and the management system of the Company. The supervisory committee believes that the Directors and senior management of the Company had dutifully performed their responsibilities and operated in a lawful manner. Internal control system has been strengthened in 2006, and the

Company accepts supervision by relevant supervisory authorities as well as by domestic and foreign investors. During the reporting period no major breaches of law or actions which would damage the image of the Company or harm the interests of shareholders were found.

2. Financial reports give a true and accurate view

The supervisory committee had reviewed the Group's financial system and financial conditions diligently and carefully. The supervisory committee considers the Group's 2006 financial reports to be true and accurate and present the financial conditions and operating results objectively, and that the audit opinion and other relevant comments made by Ernst & Young are also true and accurate.

3. Use of proceeds

During the year, the Company completed its initial public offering of 414,644,000 H shares (including shares issued pursuant to the over–allotment option) at an issue price of HK$5.30 per share, raising a total of approximately HK$2,197,613,000 and an additional interest income of approximately RMB22.67 million. The net proceeds raised was approximately RMB2,109,852,000 after deduction of listing expenses. The above funds have been deposited into the Company's accounts. There were no deviations in the use of proceeds from what was disclosed in the Company's prospectus.

4. Connected transactions

The supervisory committee considers that transactions between the Group and the Parent Group, CSR Group, Kunming China Railway were purchase and sale of goods in the ordinary course of business. The various transactions complied with the principles of openness, fairness and reasonableness. The transaction prices were set in accordance with terms of the mutually agreed contracts. Those contractual terms were entered into in the interests of the Group and the shareholders as a whole. After completing its review, the supervisory committee found that the Group's transactions in 2006 complied with relevant laws, regulation and policies of the State and had not discovered any connected transactions which would harm the Company's and shareholders' interests, and the total amount of connected transactions was below the upper limit permitted by the Stock Exchange of Hong Kong.

5. The implementation of non-competition agreements

The supervisory committee was of the opinion that during the year, the Parent Group and the CSR Group had complied with the terms of non-competition and indemnity agreements, performed their undertakings, and had not discovered any businesses in competition with the Group's businesses.

6. The implementation of resolutions of the Annual General Meeting

During the year, members of the supervisory committee attended four board meetings and three shareholders' meetings. There were no objections to the various reports submitted by the Board for consideration at shareholders' meetings and resolutions tabled for shareholders' meetings. The Board of Directors had dutifully carried out resolutions of the Annual General Meeting.

Independent Auditors' Report

ERNST & YOUNG
安永會計師事務所

To the shareholders of Zhuzhou CSR Times Electric Co., Ltd.
(A joint stock company established in the People's Republic of China with limited liability)

We have audited the financial statements of Zhuzhou CSR Times Electric Co., Ltd. (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") set out on pages 39 to 90, which comprise the consolidated and company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of the financial statements in accordance with International Financial Reporting Standards and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. Our report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young
Certified Public Accountants
18th Floor
Two International Finance Centre
8 Finance Street
Central
Hong Kong
23 April 2007

Consolidated Income Statement

Year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
REVENUE	5	**1,255,926**	997,976
Cost of sales		**(640,377)**	(542,314)
Gross profit		**615,549**	455,662
Other revenue and gains	5	**64,473**	18,530
Selling and distribution costs		**(118,657)**	(87,295)
Administrative expenses		**(243,742)**	(154,795)
Other operating revenue/(expenses), net		**(610)**	273
Finance costs	7	**(14,352)**	(13,819)
Share of loss of an associate		**(80)**	—
PROFIT BEFORE TAX	6	**302,581**	218,556
Income tax expense	9	**(313)**	(639)
PROFIT FOR THE YEAR		**302,268**	217,917
Attributable to:			
Equity holders of the parent		**296,771**	211,733
Minority interests		**5,497**	6,184
		302,268	217,917
DIVIDENDS	10	**204,403**	119,852
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	12		
Basic		**RMB0.44**	RMB0.33

Consolidated Balance Sheet

31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	13	**367,884**	303,003
Prepaid land lease payments	14	**32,792**	21,840
Intangible assets	15	**14,930**	14,128
Interest in an associate	17	**1,920**	980
Available-for-sale financial assets	18	**1,200**	1,606
Total non-current assets		**418,726**	341,557
CURRENT ASSETS			
Inventories	19	**357,157**	223,878
Trade receivables	20	**508,153**	509,419
Notes receivable	21	**143,853**	59,037
Prepayments, deposits and other receivables	22	**96,088**	182,380
Pledged deposits	23	**2,969**	—
Cash and cash equivalents	23	**2,261,310**	165,126
Total current assets		**3,369,530**	1,139,840
CURRENT LIABILITIES			
Trade payables	24	**230,312**	190,895
Notes payable	25	**98,672**	17,280
Other payables and accruals	26	**209,698**	161,249
Provision for warranties	27	**36,898**	31,898
Interest-bearing bank and other borrowings	28	**364,537**	252,521
Dividend payable	10(i)	**—**	171,328
Tax payable		**129**	19
Total current liabilities		**940,246**	825,190
NET CURRENT ASSETS		**2,429,284**	314,650
TOTAL ASSETS LESS CURRENT LIABILITIES		**2,848,010**	656,207
NET ASSETS		**2,848,010**	656,207
EQUITY			
Equity attributable to equity holders of the parent			
Issued capital	29	**1,084,256**	669,612
Reserves	30	**1,725,465**	(39,446)
Proposed final dividend	10(iii)	**36,865**	—
		2,846,586	630,166
Minority interests		**1,424**	26,041
TOTAL EQUITY		**2,848,010**	656,207

Consolidated Statement of Changes in Equity

Year ended 31 December 2006

		Attributable to equity holders of the parent							
	Notes	Issued share capital RMB'000	Capital reserve RMB'000	Statutory reserves RMB'000	Proposed final dividend RMB'000	Owners' equity/ retained profits RMB'000	Total RMB'000	Minority interests RMB'000	Total equity RMB'000
At 1 January 2005		—	—	—	—	498,485	498,485	20,157	518,642
Profit for the year		—	—	—	—	211,733	211,733	6,184	217,917
Total income and expense for the year		—	—	—	—	211,733	211,733	6,184	217,917
Capitalisation as a result of the Reorganisation	1	629,812	(176,913)	—	—	(452,899)	—	—	—
Capital contribution from the other promoters	1	39,800	—	—	—	—	39,800	—	39,800
Distribution of pre-incorporation profit	10(i)	—	—	—	—	(119,852)	(119,852)	—	(119,852)
Dividends paid to minority shareholders		—	—	—	—	—	—	(300)	(300)
Transfer to reserves		—	—	13,134	—	(13,134)	—	—	—
At 31 December 2005 and 1 January 2006		669,612	(176,913)*	13,134*	—	124,333*	630,166	26,041	656,207
Profit for the year		—	—	—	—	296,771	296,771	5,497	302,268
Total income and expense for the year		—	—	—	—	296,771	296,771	5,497	302,268
Issue of shares	1,29	414,644	1,795,324	—	—	—	2,209,968	—	2,209,968
Share issuing expenses		—	(122,781)	—	—	—	(122,781)	—	(122,781)
Acquisition of additional interests in subsidiaries	5(i)	—	—	—	—	—	—	(21,999)	(21,999)
Dividends paid to minority shareholders		—	—	—	—	—	—	(8,115)	(8,115)
Transfer to reserves	30	—	—	25,383	—	(25,383)	—	—	—
Dividends paid	10(ii)	—	—	—	—	(167,538)	(167,538)	—	(167,538)
Proposed final dividend	10(iii)	—	—	—	36,865	(36,865)	—	—	—
At 31 December 2006		1,084,256	1,495,630*	38,517*	36,865	191,318*	2,846,586	1,424	2,848,010

* These reserve accounts comprise the consolidated reserves of RMB1,725,465,000 (2005: RMB(39,446,000)) in the consolidated balance sheet.

Consolidated Cash Flow Statement

Year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		**302,581**	218,556
Adjustments for:			
Finance costs	7	**14,352**	13,819
Interest income	5	**(25,048)**	(1,238)
Loss on disposal of an associate	6	**277**	—
Share of loss of an associate		**80**	—
Losses/(gains) on disposal of items of property, plant and equipment, net	6	**(53)**	199
Depreciation of items of property, plant and equipment	6	**33,764**	25,335
Amortisation of prepaid land lease payments	6	**556**	564
Amortisation of intangible assets	6	**2,192**	2,345
Provision for impairment of trade and other receivables, net	6	**17,520**	4,318
Provision for obsolete inventories	6	**12,297**	11,883
Write-off of an available-for-sale financial asset	6	**306**	—
Excess of the acquirers' additional interests in the carrying value of the acquirees' net assets over the cost of acquisition of additional interests in subsidiaries	5	**(7,952)**	—
		350,872	275,781
Increase in trade receivables, notes receivable, prepayments, deposits and other receivables		**(14,778)**	(92,164)
Increase in inventories		**(145,576)**	(53,162)
Increase/(decrease) in trade payables, notes payable, other payables and accruals		**17,025**	(57,112)
Increase in provision for warranties		**5,000**	8,521
Cash generated from operations		**212,543**	81,864
Interest paid		**(14,352)**	(13,819)
Income tax paid		**(203)**	(14,214)
Net cash inflow from operating activities		**197,988**	53,831

	Notes	2006 RMB'000	2005 RMB'000
CASH FLOWS FROM INVESTING ACTIVITIES			
Interest received		**2,382**	1,238
Purchases of items of property, plant and equipment	13	**(102,608)**	(100,396)
Additions to prepaid land lease payments	14	**(11,508)**	(306)
Additions to intangible assets	15	**(2,994)**	(724)
Proceeds from disposal of items of property, plant and equipment		**4,016**	3,677
Proceeds from disposal of an available-for-sale financial asset		**100**	—
Instalments on acquisition of certain subsidiaries in a prior year		**(19,095)**	(17,000)
Acquisition of additional interests in subsidiaries	5(i)	**(14,047)**	—
Investment in an associate		**(2,000)**	—
Disposal of an associate		**703**	—
Increase in pledged deposits		**(2,969)**	—
Net cash outflow from investing activities		**(148,020)**	(113,511)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issue of shares	29	**2,209,968**	—
Interest income received on application funds		**22,666**	—
Share issuing expenses		**(122,781)**	—
New bank and other borrowings		**480,537**	294,541
Repayment of bank and other borrowings		**(368,521)**	(280,519)
Contributions from the other promoters		**—**	39,800
Dividends paid	10(ii)	**(167,538)**	—
Dividends paid to minority shareholders		**(8,115)**	(300)
Net cash inflow from financing activities		**2,046,216**	53,522
NET INCREASE IN CASH AND CASH EQUIVALENTS		**2,096,184**	(6,158)
Cash and cash equivalents at beginning of year		**165,126**	171,284
CASH AND CASH EQUIVALENTS AT END OF YEAR		**2,261,310**	165,126
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	23	**2,261,310**	165,126

Balance Sheet

31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	13	**265,226**	231,034
Prepaid land lease payments	14	**8,788**	8,970
Intangible assets	15	**14,142**	13,638
Investments in subsidiaries	16	**127,067**	112,298
Total non-current assets		**415,223**	365,940
CURRENT ASSETS			
Inventories	19	**267,204**	139,812
Trade receivables	20	**433,230**	386,992
Notes receivable	21	**86,872**	34,193
Prepayments, deposits and other receivables	22	**183,883**	185,569
Pledged deposits	23	**704**	—
Cash and cash equivalents	23	**2,232,766**	122,486
Total current assets		**3,204,659**	869,052
CURRENT LIABILITIES			
Trade payables	24	**253,318**	164,581
Notes payable	25	**92,342**	17,280
Other payables and accruals	26	**185,170**	107,069
Provision for warranties	27	**26,095**	22,115
Interest-bearing bank and other borrowings	28	**364,537**	242,521
Dividend payable	10(i)	**—**	171,328
Total current liabilities		**921,462**	724,894
NET CURRENT ASSETS		**2,283,197**	144,158
TOTAL ASSETS LESS CURRENT LIABILITIES		**2,698,420**	510,098
NET ASSETS		**2,698,420**	510,098
EQUITY			
Issued capital	29	**1,084,256**	669,612
Reserves	30	**1,577,299**	(159,514)
Proposed final dividend	10(iii)	**36,865**	—
TOTAL EQUITY		**2,698,420**	510,098

Notes to the Consolidated Financial Statements

1. GROUP REORGANISATION AND CORPORATE INFORMATION

The Company was established in the People's Republic of China (the "PRC") on 26 September 2005 as a joint stock company with limited liability as a result of a group reorganisation (the "Reorganisation") of CSR Zhuzhou Electric Locomotive Research Institute ("ZELRI") under the Company Law of the PRC.

Pursuant to the Reorganisation with an effective date of 30 September 2004, ZELRI, as the principal promoter of the Company, injected its assets, liabilities and businesses relating to the manufacture and sale of train-borne electrical systems and electrical components (the "Relevant Businesses") into the Company as capital contribution for subscribing approximately 94.06% of the equity interest in the Company. The Relevant Businesses at the effective date of the Reorganisation include the following:

(a) Various business divisions of ZELRI, which engaged in the manufacture and sale of train-borne electrical systems and electrical components together with their related assets and liabilities that included property, plant and equipment, cash, inventories, debtors, creditors and borrowings, except for (i) certain property, plant and equipment for basic research and development purposes, administration purposes or not related to the operations of the Relevant Businesses; (ii) certain prepayments and non-trade payable balances which were not and will not be related to the operations of the Relevant Businesses; (iii) inventories which will not be used in the operations of the Group; and (iv) certain cash balances;

(b) ZELRI's 100% equity interest in a subsidiary, Ningbo CSR Times Sensor Technology Company Ltd. ("Ningbo Company"), which is engaged in the manufacture and sale of sensors and vacuum sanitary units; and

(c) ZELRI's 90% equity interest in a subsidiary, Zhuzhou Times Electronics Technology Co., Ltd. ("Times Electronics"), which is engaged in the manufacture and sale of the electrical control systems of large railway maintenance vehicles.

The net asset value of the Relevant Businesses injected into the Company was RMB629,811,637, as appraised by a PRC valuer.

Upon its establishment, the Company issued approximately 629,811,637 ordinary shares of RMB1.00 each to ZELRI, credited as fully paid, as consideration for the Relevant Businesses injected by ZELRI into the Company. CSR Zhuzhou Electric Locomotive Company, Ltd., CSR Qishuyan Locomotive & Rolling Stock Works ("CSR Qishuyan"), New Leap Communication Equipment Invest Development Co., Ltd. ("New Leap") and China Railway Large Maintenance Machinery Co., Kunming ("Kunming China Railway"), the other promoters of the Company (collectively the "Other Promoters"), injected cash into the Company in an aggregate amount of RMB39,800,000 as consideration for the Company's paid-up capital of an aggregate of 39,800,000 shares of RMB1.00 each. As a result, 94.06% and 5.94% of the share capital of the Company were owned by ZELRI and the Other Promoters, respectively.

On 20 December 2006, the Company issued 360,560,000 new H shares to the public at a price of Hong Kong Dollars ("HK$") 5.30 per share (equivalent to approximately RMB5.330 per share), and were listed on the Main Board of The Stock Exchange of Hong Kong Limited. In addition, 36,056,000 H shares converted from certain domestic shares held by ZELRI, CSR Qishuyan and New Leap were transferred to the PRC National Council for the Social Security Fund.

1. GROUP REORGANISATION AND CORPORATE INFORMATION (Continued)

On 28 December 2006, as a result of the full exercise of the over-allotment option detailed in the Company's prospectus dated 8 December 2006 (the "Over-allotment Option"), an additional 54,084,000 new H shares were issued to the public at a price of HK$5.30 per share (equivalent to approximately RMB5.327 per share) and were listed on the Main Board of The Stock Exchange of Hong Kong Limited. In addition, 5,408,000 H shares converted from certain domestic shares held by ZELRI, CSR Qishuyan and New Leap were transferred to the PRC National Council for the Social Security Fund.

The registered office of the Company is located at Times Road, Shifeng District, Zhuzhou City, Hunan Province, PRC.

The Company and its subsidiaries are principally engaged in the sales and manufacture of train-borne electrical systems and electrical components.

In the opinion of the directors, the holding company of the Group is ZELRI and the ultimate holding company of the Group is China Southern Locomotive & Rolling Stock Industry (Group) Corporation ("CSR"), which are established in the PRC.

2.1 BASIS OF PREPARATION

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs"), which comprise standards and interpretations approved by the International Accounting Standards Board and International Accounting Standards ("IAS") and Standing Interpretations Committee interpretations ("IFRICs") approved by the International Accounting Standards Committee that remain in effect, and the disclosure requirements of the Hong Kong Companies Ordinance (the "Companies Ordinance"). They have been prepared under the historical cost convention, except for certain financial assets as further explained below.

As ZELRI controlled the Relevant Businesses before the Reorganisation and continues to have control over the Group after the Reorganisation, the Reorganisation has been accounted for as a reorganisation of entities under common control in a manner similar to a pooling of interests. As a result, the financial statements have been prepared on the basis as if the Relevant Businesses had been injected into the Company at the beginning of the comparative year ended 31 December 2005. Accordingly, the assets and liabilities comprising the Relevant Businesses injected into the Company have been stated at historical amounts.

The financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand, except when otherwise indicated.

2.1 BASIS OF PREPARATION (Continued)

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2006. The result of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which the Group had control. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries has been accounted for using the purchase method of accounting. This method involves allocating the cost of a business combination to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company's subsidiaries.

2.2 IMPACT OF ISSUED BUT NOT YET EFFECTIVE INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised IFRSs and IFRICs, that have been issued but are not yet effective, in the financial statements:

- IAS 1 Amendment — Presentation of Financial Statements: Capital Disclosures
- IAS 23 (Revised) — Borrowings Costs
- IFRS 7 — Financial Instruments: Disclosures
- IFRS 8 — Operating Segments
- IFRIC - Int 7 — Applying the Restatement Approach under IAS 29 *Financial Reporting in Hyperinflationary Economies*
- IFRIC - Int 8 — Scope of IFRS 2
- IFRIC - Int 9 — Reassessment of Embedded Derivatives
- IFRIC - Int 10 — Interim Financial Reporting and Impairment
- IFRIC - Int 11 — IFRS 2 - Group and Treasury Share Transactions
- IFRIC - Int 12 — Service Concession Agreements

The IAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

IAS 23 (Revised) shall be applied for annual periods beginning on or after 1 January 2009. The revised standard requires all borrowing costs to be capitalised if they are directly attributable to the acquisition, construction or production of a qualifying assets. The choice of immediately recognise such cost as an expense is eliminated.

IFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. The standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments.

2.2 IMPACT OF ISSUED BUT NOT YET EFFECTIVE INTERNATIONAL FINANCIAL REPORTING STANDARDS (Continued)

IFRS 8 shall be applied for annual periods beginning on or after 1 January 2009 and will replace the existing IAS 14 "*Segment Reporting*". IFRS 8 requires an entity to adopt the "management approach" to report on the financial performance of its operating segments. Generally, the information to be reported would be that used internally for the purpose of evaluating segment performance and deciding resources allocation to operating segments. Such information may be different from what is used for preparing the income statement and balance sheet. IFRS 8 therefore requires explanations of the basis on how the segment information is prepared and reconciled to the income statement and balance sheet.

IFRIC - Int 7, IFRIC - Int 8, IFRIC - Int 9, IFRIC - Int 10, IFRIC - Int 11 and IFRIC - Int 12 shall be applied for annual periods beginning on or after 1 March 2006, 1 May 2006, 1 June 2006, 1 November 2006, 1 March 2007 and 1 January 2008, respectively.

The Group has commenced its assessment of the impact of these standards and interpretation, but is not yet in a position to state whether these standards and interpretation would have a material impact on its result of operations and financial position.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated in the Company's balance sheet at cost less any impairment losses.

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long-term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. The Group's interest in an associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

The results of associates are included in the Company's income statement to the extent of dividends received and receivable. The Company's interests in associates are treated as non-current assets and are stated at cost less any impairment losses.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Goodwill

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the Group's interests in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than a segment based on either the Group's primary or the Group's secondary reporting format determined in accordance with IAS14 *Segment Reporting*.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured on the basis of the relative value of the operation disposed of and the portion of the cash-generating unit retained.

Any excess of the Group's interests in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over the cost of the acquisition of subsidiaries, after reassessment, is recognized immediately in the consolidated income statement.

For the acquisitions of additional interests in subsidiaries, the excess of the Group's additional interests in the carrying value of the acquiree's identifiable net assets over the cost of acquisition of such additional interests in subsidiaries is recognised immediately in the consolidated income statement.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign currencies

The financial statements are presented in RMB, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

On consolidation, the financial statements of overseas subsidiaries are translated into RMB. As at the balance sheet date, the assets and liabilities of these entities are translated into the presentation currency of the Company at the exchange rates ruling at the balance sheet date and, their income statements are translated into RMB at the weighted average exchange rates for the year. The resulting exchange differences are included in the exchange fluctuation reserve. No such exchange differences arose during the years ended 31 December 2005 and 2006.

For the purpose of the consolidated cash flow statement, the cash flows of overseas subsidiaries are translated into RMB at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arose throughout the year are translated into RMB at the weighted average exchange rates for the year.

Property, plant and equipment and depreciation

Property, plant and equipment, which consist of buildings, plant, machinery and equipment, computer equipment and others, and construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the consolidated income statements in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset.

Depreciation is calculated on the straight-line basis to write off the cost of each asset over its estimated useful life, after taking into account their estimated residual value. The estimated useful lives of property, plant and equipment are as follows:

	Useful life
Buildings	20 years
Plant, machinery and equipment	10 years
Computer equipment and others	5 years

The gain or loss on disposal or retirement of an item of property, plant and equipment recognised in the consolidated income statement is the difference between the net sales proceeds and the carrying amount of the relevant asset at the time of disposal.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Construction in progress

Construction in progress represents buildings, plant, machinery and equipment under construction and pending installation, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises direct costs of construction and interest charges on related borrowed funds during the period of construction, installation and testing. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Prepaid land lease payments

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms ranging from 40 to 50 years.

Prepaid land lease payments represent the cost of land use rights paid to the PRC government authorities. Land use rights are stated at cost less accumulated amortisation and any impairment losses. The land use rights are amortised on the straight-line basis over the terms of the rights ranging from 40 to 50 years.

Intangible assets

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset are reviewed at least at each balance sheet date.

Technical know-how

Purchased royalty, patents and licences

Expenditure on acquired royalty, patents and licences is capitalised as intangible assets and amortised using the straight-line method over their useful lives of 10 years. Royalty, patents and licences are not revalued as there is no active market for these assets.

Computer software

Acquired computer softwares is capitalised on the basis of the costs incurred to acquire and bring to use the specific softwares. These costs are amortised using the straight-line method over their estimated useful lives of 5 to 10 years.

Research and development costs

Research costs are expensed as incurred. Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products, commencing from the date when the products are put into commercial production.

The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use, or otherwise when events or changes in circumstances indicate that the carrying value may not be recoverable.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment of assets

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognised in the consolidated income statements in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount, that increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the consolidated income statements unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Investments and other financial assets

Financial assets in the scope of IAS39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the trade date, i.e., the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category "financial assets at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on investments held for trading are recognized in the consolidated income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has the positive intention and ability to hold to maturity. Investments intended to be held for an undefined period are not included in this classification. Other long-term investments that are intended to be held to maturity, such as bonds, are subsequently measured at amortised cost. Amortised cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount. This calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. For investments carried at amortised cost, gains and losses are recognised in the consolidated income statements when the investments are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in listed and unlisted equity securities that are designated as available for sale or are not classified in any of the other three categories. After initial recognition, available-for-sale financial assets are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the consolidated income statements. When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and option pricing models.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of manufacturing overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Trade and other receivables

Trade and other receivables are recognised and carried at invoice amounts less allowances for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off as incurred.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and cash equivalents

For the purpose of the consolidated cash flow statements, cash and cash equivalents comprise cash on hand and demand deposits, and short-term highly liquid investments that are readily convertible into known amounts of cash and that are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are repayable on demand and form an integral part of the Group's cash management.

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the consolidated income statements.

Provision for product warranties granted by the Group for its products is recognised based on the sales volume and past experience of the level of repairs, discounted to its present value as appropriate.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the amortisation process.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e., assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised as expenses in the consolidated income statements in the period in which they are incurred.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the consolidated income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the consolidated income statement on the straight-line basis over the lease terms.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the consolidated income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

PRC corporate income tax is provided at rates applicable to enterprises in the PRC on the Group's income for financial reporting purposes, as adjusted for income and expense items which are not assessable or deductible for income tax purposes.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries and interests in associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries and interests in associates, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income tax (Continued)

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) rental income, on a time proportion basis over the lease terms;

(c) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset; and

(d) dividend income, when the shareholders' right to receive payment has been established.

Retirement benefits

The Company and its subsidiaries established in the PRC are required to participate in a central pension scheme operated by relevant government authorities in the PRC. The Group contributes on a monthly basis to the relevant defined contribution retirement benefit plans, the PRC government undertakes to assume the retirement benefit obligations payable to all existing and future retired employees under these plans and the Group has no further obligation for post-retirement benefits beyond the contributions made. The contributions are charged to the consolidated income statement as they become payable, in accordance with the rules of the central pension scheme.

In 2006, the Group implemented a new pension annuity plan pursuant to which the Group is required to regularly contribute a fixed percentage of salaries to the plan and the Group has no further obligation thereto once the required contribution has been made. The contributions are recognised as an employee benefit expense when incurred.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Related parties

A party is considered to be related to the Group if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d); or

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e).

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Provision for obsolete inventories

Management reviews the condition of inventories of the Group at each balance sheet date and makes provision for obsolete and slow-moving inventory items identified that are no longer suitable for sale. Management estimates the net realisable value for such inventories based primarily on the latest sales invoice prices and current market conditions. Management reassesses the estimation at each balance sheet date.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated.

Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Impairment of receivables

The policy for impairment of receivables of the Group is based on the evaluation of collectability and the aging analysis of trade receivables and on the judgement of the management. A considerable amount of judgement is required in assessing the ultimate realisation of these receivables, including the current creditworthiness and the past collection history of the customers. Management reassesses the estimation on each of the balance sheet dates.

Useful lives and impairment of property, plant and equipment

The Group's management determines the estimated useful lives of its property, plant and equipment based on the historical experience of the actual useful lives of property, plant and equipment of similar nature and functions. Management will increase the depreciation charge where useful lives are less than previously estimated lives. The impairment loss for property, plant and equipment is recognised for the amount by which the carrying amount exceeds its recoverable amount.

4. SEGMENT INFORMATION

Segment information is required by IAS 14 *Segment Reporting* to be presented by way of two segment formats: (i) on a primary segment reporting basis, which the Group has determined to be by business segment; and (ii) on a secondary segment reporting basis, which the Group has determined to be by geographical segment.

The Group is principally engaged in the manufacture and sale of electrical systems and components relating to locomotive and rolling stock. All of the Group's products are of a similar nature and subject to similar risks and returns. Accordingly, the Group's operating activities are attributable to a single business segment. In addition, the Group's revenue, expenses, profit, assets and liabilities and capital expenditures are principally attributable to a single geographical region, which is the PRC. Therefore, no analysis in business or geographical segment is presented.

5. REVENUE, OTHER REVENUE AND GAINS

Revenue on sale of goods

Revenue represents the net invoiced value of goods sold, net of discounts and returns.

An analysis of the Group's revenue, other revenue and gains is as follows:

	Notes	**2006** **RMB'000**	2005 RMB'000
Revenue:			
Sale of goods		**1,266,909**	1,005,780
Less: Sales tax and surcharge		**(10,983)**	(7,804)
		1,255,926	997,976
Other revenue and gains:			
Interest income		**25,048**	1,238
Profit from sale of raw materials		**2,246**	3,345
Gross rental income		**2,359**	—
Exchange gains, net		**—**	4,212
Excess of the acquirers' additional interests in the carrying value of the acquirees' net assets over the cost of acquisition of additional interests in subsidiaries	(i)	**7,952**	—
Value-added tax refund	(ii)	**15,499**	6,969
Technical service income		**2,780**	1,320
Others		**8,589**	1,446
Total		**64,473**	18,530

5. REVENUE, OTHER REVENUE AND GAINS (Continued)

(i) Acquisition of additional interests in subsidiaries

In June 2006, the Company acquired a further 10% equity interest in Times Electronics, a then 90%-owned subsidiary, at a consideration of RMB9,150,000. In addition, the Company agreed that the seller should be entitled to a 10% of the net profit of Times Electronics for the six months ended 30 June 2006, which amounted to RMB4,005,000. The Group's additional interest in the carrying value of the net assets of Times Electronics arising from such acquisition of 10% equity interest from Times Electronics' minority shareholder amounted to RMB20,569,000 and the excess of such carrying value over the cost of acquisition attributable to the Group (includes net profit of Times Electronics entitled by the seller) of RMB7,414,000 was credited to the Group's consolidated income statement for the year ended 31 December 2006. The cash flows used in such investment activities for the year ended 31 December 2006 amounted to RMB13,155,000.

In December 2006, Times Electronics acquired a further 15% equity interest in Zhuzhou Times Guangchuang Converter Technology Co., Ltd. ("Times Guangchuang"), a then 70%-owned subsidiary of Times Electronics, at a consideration of RMB892,000 in cash. Thereafter, its equity interest in Times Guangchuang increased from 70% to 85%. Times Electronics's additional interest in the carrying value of the net assets of Times Guangchuang arising from the acquisition of 15% equity interest from Times Guangchuang' minority shareholders amounted to RMB1,430,000, and the excess of the carrying value over the cost of acquisition attributable to Times Electronics of RMB538,000 was recognised in the Group' consolidated income statement for the year ended 31 December 2006.

(ii) Value-added tax refund

Sales of goods are generally subject to value-added tax ("VAT") at a rate of 17%. Pursuant to the "Notice on the Taxation Policy Issues relating to Encouraging the Development of the Software Industry and Integrated Circuit Industry" issued by State Administration of Taxation and General Administration of Custom, the Group is entitled to a refund of VAT paid in excess of 3% in respect of sale of certain products during the years ended 31 December 2005 and 2006.

6. PROFIT BEFORE TAX

The Group's profit before tax from operating activities is arrived at after charging/(crediting):

	Notes	2006 RMB'000	2005 RMB'000
Cost of inventories sold		**640,377**	542,314
Staff costs (including directors' and supervisors' emoluments)	(i)	**139,462**	117,888
Auditors' remuneration		**3,600**	159
Depreciation of items of property, plant and equipment		**33,764**	25,335
Amortisation of lease prepayments		**556**	564
Amortisation of intangible assets		**2,192**	2,345
Minimum lease payments under operating leases in respect of:			
Land and buildings		**457**	127
Plant and equipment		**9,115**	9,000
Provision for obsolete inventories		**12,297**	11,883
Exchange losses/(gains), net		**1,442**	(4,212)
Research and development costs		**95,982**	52,388
Less: staff cost included above		**(39,259)**	(25,904)
depreciation and amortisation included above		**(3,133)**	(4,675)
Research and development costs net of staff cost, depreciation and amortisation		**53,590**	21,809
Losses/(gains) on disposal of items of property, plant and equipment, net		**(53)**	199
Provision for impairment of trade and other receivables, net		**17,520**	4,318
Write-off of an available-for-sale financial asset		**306**	—
Loss on disposal of an associate		**277**	—
Provision for warranties		**33,273**	32,403
Interest income		**(25,048)**	(1,238)
Gross rental income		**(2,359)**	—

6. PROFIT BEFORE TAX (Continued)

(i) Staff cost

	2006	2005
	RMB'000	RMB'000
Wages, salaries and bonuses	**104,728**	93,872
Contribution to government-operated pension schemes	**8,862**	6,734
Contribution to a pension annuity plan	**3,713**	—
Welfare and other expenses	**22,159**	17,282
Total	**139,462**	117,888

In 2006, the Group implemented a new pension annuity plan. Pursuant to the new pension annuity plan, the Group is required to contribute a fixed percentage of salaries to the annuity plan and has no further payment obligation to the pension annuity plan once the contributions have been made.

7. FINANCE COSTS

	2006	2005
	RMB'000	RMB'000
Interest paid on bank and other borrowings		
repayable within one year	**14,352**	13,819

8. DIRECTORS' AND SUPERVISORS' EMOLUMENTS

Details of the directors' and supervisors' remuneration for the year, disclosed pursuant to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and Section 161 of the Companies Ordinance, are as follows:

	2006	2005
	RMB'000	RMB'000
Fees	**—**	—
Other emoluments:		
Salaries, allowances and benefits in kind	**1,403**	682
Bonuses	**1,690**	1,617
Pension scheme contributions	**62**	30
Total	**3,155**	2,329

8. DIRECTORS' AND SUPERVISORS' EMOLUMENTS (Continued)

The names of the directors and supervisors of the Company and their remuneration for the year ended 31 December 2006 are as follows:

	Fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Bonuses RMB'000	Pension scheme contributions RMB'000	Total RMB'000
Executive directors:					
Liao Bin	—	177	417	10	604
Tian Lei	—	157	417	10	584
Ding Rongjun	—	135	408	12	555
Lu Penghu	—	27	28	2	57
Non-executive directors:					
Liao Bin	—	35	83	2	120
Tian Lei	—	31	83	2	116
Ma Yunkun	—	56	—	—	56
Independent non-executive directors:					
Zhou Heliang	—	5	—	—	5
Gao Yucai	—	5	—	—	5
Chan Kam Wing, Clement	—	138	—	—	138
Pao Ping Wing	—	138	—	—	138
Tan Xiao'ao	—	33	—	—	33
	—	937	1,436	38	2,411
Supervisors:					
Jiang Yi	—	162	100	12	274
Pang Yiming	—	126	154	12	292
Zhang Liqiang	—	44	—	—	44
He Hongqu	—	67	—	—	67
Liu Chunru	—	67	—	—	67
	—	466	254	24	744
Total	—	1,403	1,690	62	3,155

8. DIRECTORS' AND SUPERVISORS' EMOLUMENTS (Continued)

The names of the directors and supervisors of the Company and their remuneration for the year ended 31 December 2005 are as follows:

	Fees	Salaries, allowances and benefits in kind	Bonuses	Pension scheme contributions	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Executive directors:					
Liao Bin	—	122	501	6	629
Tian Lei	—	116	475	6	597
Ding Rongjun	—	91	339	6	436
Non-executive director:					
Ma Yunkun	—	14	—	—	14
Independent non-executive directors:					
Chan Kam Wing, Clement	—	35	—	—	35
Pao Ping Wing	—	33	—	—	33
Tan Xiao'ao	—	—	—	—	—
	—	411	1,315	18	1,744
Supervisors:					
Jiang Yi	—	104	153	6	263
Pang Yiming	—	122	149	6	277
Zhang Liqiang	—	11	—	—	11
He Hongqu	—	17	—	—	17
Liu Chunru	—	17	—	—	17
	—	271	302	12	585
Total	—	682	1,617	30	2,329

In November 2006, Liao Bin and Tian Lei became non-executive directors of the Company. Further, in November 2006, Lu Penghu was appointed as an executive director of the Company, and Gao Yucai and Zhou Heliang were appointed as non-executive directors of the Company. The remuneration of Lu Penghu, Gao Yucai and Zhou Heliang have not been disclosed in the above tables relating to the year ended 31 December 2005.

8. DIRECTORS' AND SUPERVISORS' EMOLUMENTS (Continued)

The five highest paid employees of the Group during the year were as follows:

	The Group	
	2006	2005
Directors and supervisors	**3**	3
Non-director and non-supervisor employees	**2**	2
	5	5

The remuneration paid to the above non-director, non-supervisor, highest paid employees is as follows:

	The Group	
	2006	2005
	RMB'000	RMB'000
Salaries, allowances and benefits in kind	**312**	198
Bonuses	**372**	506
Pension scheme contributions	**23**	13
	707	717

The number of these non-director, non-supervisor, highest paid employees whose remuneration fell within the following band is as follows:

	2006	2005
Nil to HK$1,000,000	**2**	2

During the year, no emoluments were paid by the Group to any of the persons who are directors of the Company, or the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

There was no arrangement under which a director waived or agreed to waive any remuneration nor during the year.

9. INCOME TAX EXPENSE

The Group is subject to income tax on an entity basis on the profits arising in or derived from jurisdictions in which members of the Group are domiciled and operate.

PRC corporate income tax ("CIT") has been provided based on the taxable income as reported in the statutory accounts of the relevant companies comprising the Group, which are prepared in accordance with Accounting Standards for Business Enterprises and the Accounting System for Business Enterprises ("PRC GAAP") as adjusted for income and expense items which are not assessable or deductible for income tax purpose. The income tax rates for the Company and its subsidiaries are as follows:

(i) Pursuant to the approvals of relevant tax authorities, ZELRI, as a scientific research organisation enterprise, is exempt from CIT from 1 October 2000 to 30 September 2007. Therefore, no CIT was provided for the profits arising from the Relevant Businesses operated by ZELRI which is included in those financial statements for the period prior to the establishment of the Company on 26 September 2005.

 Pursuant to the Reorganisation, the Company was established to take over the Relevant Businesses from ZELRI, and in accordance with relevant tax regulations and an approval from the local tax authorities, the Company is exempt from CIT for two years starting from 1 October 2005. Accordingly, no CIT has been provided for by the Company during the year.

(ii) Times Electronics and Times Guangchuang are enterprises established in Zhuzhou Hi-technology Development Zone and are subject to CIT at a rate of 15%. As approved by the local tax authorities, Times Electronics is entitled to an exemption from CIT from 1 April 2005 to 31 December 2006. Times Electronics is subject to a tax rate of 15% for the three month period ended 31 March 2005, and no provision for income tax of Times Electronics was made after 1 April 2005.

 As approved by the local tax authorities, Times Guangchuang, as a software development enterprise, is entitled to a 50% reduction of CIT for the three years starting from 1 January 2004. Accordingly, CIT of Times Guangchuang for the years ended 31 December 2005 and 2006 were provided at a reduced rate of 7.5%.

(iii) As approved by the relevant tax authorities, Ningbo Company, as a scientific research organisation enterprise, is exempt from CIT from 2002 to 2005. In addition, pursuant to relevant tax regulations and the approval from the relevant tax authorities, the CIT exemption granted to Ningbo Company is further extended to the years ended 31 December 2006 and year ending 31 December 2007. Therefore, no provision for CIT of Ningbo Company was made during the year.

9. INCOME TAX EXPENSE (Continued)

Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the PRC, based on the existing legislation, interpretations and practices in respect thereof.

	2006	2005
	RMB'000	RMB'000
Current taxation - PRC corporate income tax	**313**	639

A reconciliation of income tax exposure applicable to profit before tax at the statutory income tax rate in the PRC to income tax exposure at the Group's effective income tax rate are as follows:

	2006		2005	
	RMB'000	**%**	RMB'000	%
Profit before tax	**302,581**		218,556	
Standard tax rate applied to profit before tax	**99,852**	**33.0**	72,123	33.0
Reconciling items:				
Expenses not deductible for income tax purposes	**3,984**	**1.3**	1,640	0.7
Income not subject to income tax	**(7,769)**	**(2.6)**	(1,110)	(0.5)
Effect of tax incentive	**(1,235)**	**(0.4)**	(78)	(0.0)
Tax exemptions	**(94,519)**	**(31.2)**	(71,936)	(32.9)
Total tax charge for the year	**313**	**0.1**	639	0.3

10. DIVIDENDS

	2006	2005
	RMB'000	RMB'000
Pre-incorporation profit distribution (i)	**—**	119,852
Special dividend (ii)	**167,538**	—
Proposed final – RMB0.034 per ordinary share (iii)	**36,865**	—
	204,403	119,852

10. DIVIDENDS (Continued)

(i) In accordance with the "Provisional Regulation Relating to Corporate Reorganisation of Enterprises and Related Management of state-owned Capital and Financial Treatment" notice issued by the Ministry of Finance (財政部關於印發《企業公司制改建有關國有資本管理與財務處理的暫行規定》的通知), the Company is required to make a distribution to ZELRI which represents an amount equal to the net profit attributable to shareholders, as determined based on PRC GAAP, generated during the period from 30 September 2004 (effective date of the Reorganisation) to 26 September 2005 (the date of incorporation of the Company) by the Relevant Businesses of ZELRI. Accordingly, pre-incorporation profits of RMB51,476,000 and RMB119,852,000 were distributable to ZELRI during the year ended 31 December 2004 and the year ended 31 December 2005, respectively. Further details are set out in note 31.

(ii) In November 2006, as approved at the shareholders' meeting of the Company, a special dividend of RMB167,538,000 which represents an amount equal to the net profit earned during the period from 26 September 2005 to 30 June 2006, as determined based on the lower of the Company's PRC GAAP and IFRS after-tax profits after allowance for the transfer to the statutory common reserve fund of an amount of RMB14,278,000, was declared to be payable to the shareholders of the Company before the issue of H shares.

(iii) The proposed final dividend for the year ended 31 December 2006 is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

11. PROFIT ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE PARENT

The consolidated profit attributable to the equity holders of the parent for the year ended 31 December 2006 includes a profit of RMB268,673,000 (2005: RMB126,379,000), which has been dealt with in the financial statements of the Company (note 30).

12. EARNINGS PER SHARE

The calculation of basic earnings per share is based on:

	2006	2005
	RMB'000	RMB'000
Earnings:		
Profit attributable to ordinary equity holders of the parent	**296,771**	211,733
Shares:		
Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation	**682,058,366**	640,388,623

The Company's weighted average number of domestic shares in issue used in the basic earning per share calculation for the year ended 31 December 2005 is determined on the assumption that the 629,811,637 domestic shares of RMB1.00 each issued as a result of the Reorganisation had been in issue during the year and was adjusted to add the 39,800,000 domestic shares of RMB1.00 each issued to the Other Promoters upon the establishment of the Company on 26 September 2005. Further details of the Reorganisation are set out in note 1.

No diluted earnings per share have been disclosed as no diluting events existed during the years ended 31 December 2005 and 2006.

13. PROPERTY, PLANT AND EQUIPMENT

The Group

	Buildings RMB'000	Plant, machinery and equipment RMB'000	Computer equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2006					
At 31 December 2005 and at 1 January 2006:					
Cost	200,122	151,712	36,025	35,981	423,840
Accumulated depreciation and impairment	(45,808)	(60,756)	(14,273)	—	(120,837)
Net carrying amount	154,314	90,956	21,752	35,981	303,003
At 1 January 2006, net of accumulated depreciation and impairment	154,314	90,956	21,752	35,981	303,003
Reclassification	(4)	(2,886)	2,890	—	—
Additions	1,100	20,206	27,052	54,250	102,608
Disposals	(1,096)	(315)	(1,832)	(720)	(3,963)
Depreciation provided during the year	(10,483)	(13,846)	(9,435)	—	(33,764)
Transfers	22,857	1,453	—	(24,310)	—
At 31 December 2006, net of accumulated depreciation and impairment	166,688	95,568	40,427	65,201	367,884
At 31 December 2006:					
Cost	222,020	162,891	69,169	65,201	519,281
Accumulated depreciation and impairment	(55,332)	(67,323)	(28,742)	—	(151,397)
Net carrying amount	166,688	95,568	40,427	65,201	367,884

13. PROPERTY, PLANT AND EQUIPMENT (Continued)

The Group (Continued)

	Buildings RMB'000	Plant, machinery and equipment RMB'000	Computer equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005					
At 1 January 2005:					
Cost	124,536	137,238	23,745	43,131	328,650
Accumulated depreciation and impairment	(38,979)	(46,907)	(10,946)	—	(96,832)
Net carrying amount	85,557	90,331	12,799	43,131	231,818
At 1 January 2005, net of accumulated depreciation and impairment	85,557	90,331	12,799	43,131	231,818
Additions	11,690	12,304	15,080	61,322	100,396
Disposals	(344)	(919)	(2,109)	(504)	(3,876)
Depreciation provided during the year	(7,000)	(14,095)	(4,240)	—	(25,335)
Transfers	64,411	3,335	222	(67,968)	—
At 31 December 2005, net of accumulated depreciation and impairment	154,314	90,956	21,752	35,981	303,003
At 31 December 2005:					
Cost	200,122	151,712	36,025	35,981	423,840
Accumulated depreciation and impairment	(45,808)	(60,756)	(14,273)	—	(120,837)
Net carrying amount	154,314	90,956	21,752	35,981	303,003

13. PROPERTY, PLANT AND EQUIPMENT (Continued)

The Company

	Buildings RMB'000	Plant, machinery and equipment RMB'000	Computer equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2006					
At 31 December 2005 and at 1 January 2006:					
Cost	154,132	132,618	28,799	14,798	330,347
Accumulated depreciation and impairment	(31,757)	(56,269)	(11,287)	—	(99,313)
Net carrying amount	122,375	76,349	17,512	14,798	231,034
At 1 January 2006, net of accumulated depreciation and impairment	122,375	76,349	17,512	14,798	231,034
Reclassification	—	(236)	236	—	—
Additions	200	16,991	22,244	24,218	63,653
Disposals	(6)	(113)	(1,039)	(650)	(1,808)
Depreciation provided during the year	(8,039)	(12,650)	(6,964)	—	(27,653)
Transfers	22,857	1,203	—	(24,060)	—
At 31 December 2006, net of accumulated depreciation and impairment	137,387	81,544	31,989	14,306	265,226
At 31 December 2006:					
Cost	177,167	147,365	52,369	14,306	391,207
Accumulated depreciation and impairment	(39,780)	(65,821)	(20,380)	—	(125,981)
Net carrying amount	137,387	81,544	31,989	14,306	265,226

13. PROPERTY, PLANT AND EQUIPMENT (Continued)

The Company (Continued)

	Buildings RMB'000	Plant, machinery and equipment RMB'000	Computer equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005					
Transferred from ZELRI in connection with the Reorganisation	51,956	76,270	6,482	41,613	176,321
Additions	10,907	8,915	15,080	41,153	76,055
Disposals	—	(780)	(685)	—	(1,465)
Depreciation provided during the year	(4,899)	(11,391)	(3,587)	—	(19,877)
Transfers	64,411	3,335	222	(67,968)	—
At 31 December 2005, net of accumulated depreciation and impairment	122,375	76,349	17,512	14,798	231,034
At 31 December 2005:					
Cost	154,132	132,618	28,799	14,798	330,347
Accumulated depreciation and impairment	(31,757)	(56,269)	(11,287)	—	(99,313)
Net carrying amount	122,375	76,349	17,512	14,798	231,034

14. PREPAID LAND LEASE PAYMENTS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Carrying amount at beginning of year	**21,840**	22,098	**8,970**	—
Additions	**11,508**	306	**—**	306
Transferred from ZELRI in connection with the Reorganisation	**—**	—	**—**	8,841
Amortisation provided during the year	**(556)**	(564)	**(182)**	(177)
Carrying amount at end of year	**32,792**	21,840	**8,788**	8,970

15. INTANGIBLE ASSETS

The Group

	Patents and technical know-how RMB'000	Computer software RMB'000	Total RMB'000
At 1 January 2005:			
Cost	16,100	2,903	19,003
Accumulated amortisation	(2,904)	(350)	(3,254)
Net carrying amount	13,196	2,553	15,749
Cost at 1 January 2005, net of accumulated amortisation	13,196	2,553	15,749
Additions	—	724	724
Amortisation provided during the year	(2,013)	(332)	(2,345)
At 31 December 2005	11,183	2,945	14,128
At 31 December 2005 and at 1 January 2006:			
Cost	16,100	3,627	19,727
Accumulated amortisation	(4,917)	(682)	(5,599)
Net carrying amount	11,183	2,945	14,128
Cost at 1 January 2006, net of accumulated amortisation	11,183	2,945	14,128
Additions	—	2,994	2,994
Amortisation provided during the year	(1,410)	(782)	(2,192)
At 31 December 2006	9,773	5,157	14,930
At 31 December 2006:			
Cost	16,100	6,621	22,721
Accumulated amortisation	(6,327)	(1,464)	(7,791)
Net carrying amount	9,773	5,157	14,930

15. INTANGIBLE ASSETS (Continued)

The Company

	Patents and technical know-how RMB'000	Computer software RMB'000	Total RMB'000
Transferred from ZELRI in connection with the Reorganisation	13,196	2,553	15,749
Additions	—	220	220
Amortisation provided during the year	(2,013)	(318)	(2,331)
At 31 December 2005	11,183	2,455	13,638
At 31 December 2005 and at 1 January 2006:			
Cost	16,100	3,123	19,223
Accumulated amortisation	(4,917)	(668)	(5,585)
Net carrying amount	11,183	2,455	13,638
Cost at 1 January 2006, net of accumulated amortisation	11,183	2,455	13,638
Additions	—	2,438	2,438
Amortisation provided during the year	(1,410)	(524)	(1,934)
At 31 December 2006	9,773	4,369	14,142
At 31 December 2006:			
Cost	16,100	5,561	21,661
Accumulated amortisation	(6,327)	(1,192)	(7,519)
Net carrying amount	9,773	4,369	14,142

16. INVESTMENTS IN SUBSIDIARIES

	The Company	
	2006	2005
	RMB'000	RMB'000
Unlisted investments, at cost	**127,067**	112,298

Particulars of the subsidiaries as at 31 December 2006 are as follows:

Name	Notes	Place of incorporation/ establishment and operations	Paid-up/ registered capital	Percentage of equity interests attributable to the Company		Principal activities
				Direct	Indirect	
Ningbo Company		PRC	RMB48,826,200	100	—	Manufacture and sale of sensors and vacuum sanitary units
Times Electronics	(i)	PRC	RMB80,000,000	100	—	Manufacture and sale of electrical control systems for large railway maintenance vehicles
Times Guangchuang	(ii)	PRC	RMB3,000,000	—	85	Manufacture and sale of power supply equipment for air conditioners of locomotives
Times Electric, USA LLC		United States of America	US$200,000	100	—	Sale of electric, electronic and mechanical products

(i) As mentioned in note 1, pursuant to the Reorganisation, ZELRI injected its 90% equity interest in Times Electronics into the Company. In June 2006, the Company acquired a further 10% equity interest in Times Electronics. Thereafter, Times Electronics became a wholly-owned subsidiary of the Company (note 5(i)).

(ii) As mentioned in note 5(i), in December 2006, Times Electronics acquired a further15% equity interest in Times Guangchuang, a then 70%-owned subsidiary of Times Electronics. Thereafter, its equity interest in Times Guangchuang increased from 70% to 85%.

17. INTEREST IN AN ASSOCIATE

	The Group	
	2006	2005
	RMB'000	RMB'000
Share of net assets	**1,920**	980

Particulars of the associate as at 31 December 2006 are as follows:

Name	Particulars of issued shares held	Place of incorporation/ registration	Percentage of ownership interest attributable to the Group	Principal activities
Zhuzhou Times Zhuoyue Automotive Electronics Co., Ltd.	RMB5,000,000	PRC	40	Manufacture and sale of automotive electronics products and computer control software

18. AVAILABLE –FOR-SALE FINANCIAL ASSETS

	The Group	
	2006	2005
	RMB'000	RMB'000
At cost:		
Unlisted equity investments	**1,200**	1,606

19. INVENTORIES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Raw materials	**201,099**	140,983	**125,269**	68,320
Work in progress	**51,194**	43,144	**36,292**	28,812
Finished goods	**155,939**	79,966	**144,267**	74,285
Consumables and packing materials	**750**	160	**750**	160
	408,982	264,253	**306,578**	171,577
Less: Provision for obsolete inventories	**(51,825)**	(40,375)	**(39,374)**	(31,765)
	357,157	223,878	**267,204**	139,812

20. TRADE RECEIVABLES

The Group generally stipulates payment upon delivery in sales contracts entered into with customers. However, in the opinion of the directors, the Group has effectively granted an average credit period of around six months to its customers after taking into account the practice of the industry in which the Group conducts its business.

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade receivables from:				
CSR and its subsidiaries (other than the Group)	**89,208**	133,555	**67,450**	118,705
Subsidiaries	**—**	—	**23,874**	2,417
Third parties	**453,983**	394,160	**368,608**	279,982
	543,191	527,715	**459,932**	401,104
Less: Provision for impairment of receivables	**(35,038)**	(18,296)	**(26,702)**	(14,112)
	508,153	509,419	**433,230**	386,992

20. TRADE RECEIVABLES (Continued)

An aging analysis of the trade receivables, net of provision for impairment of receivables, is as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 1 year	**477,330**	480,199	**412,909**	367,367
Over 1 year but within 2 years	**31,899**	30,485	**19,423**	21,086
Over 2 years but within 3 years	**17,728**	12,111	**15,345**	8,947
Over 3 years	**16,234**	4,920	**12,255**	3,704
	543,191	527,715	**459,932**	401,104
Less: Provision for impairment of receivables	**(35,038)**	(18,296)	**(26,702)**	(14,112)
	508,153	509,419	**433,230**	386,992

The amounts due from CSR and its subsidiaries included in the Group's and the Company's trade receivables, and the amounts due from subsidiaries included in the Company's trade receivables are unsecured, interest-free and repayable on demand.

21. NOTES RECEIVABLE

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 3 months	**70,779**	20,425	**24,918**	18,001
Over 3 months but within 6 months	**73,074**	38,612	**61,954**	16,192
	143,853	59,037	**86,872**	34,193

22. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Prepayments, deposits and other receivables:				
CSR and its subsidiaries (other than the Group)	**4,531**	149,139	**4,517**	148,573
Subsidiaries	**—**	—	**96,004**	11,724
Third parties	**92,452**	33,381	**83,557**	25,272
	96,983	182,520	**184,078**	185,569
Less: Provision for impairment of receivables	**(895)**	(140)	**(195)**	—
	96,088	182,380	**183,883**	185,569

The amounts due from CSR and its subsidiaries included in the Group's and the Company's prepayments, deposits and other receivables, and the amounts due from subsidiaries included in the Company's prepayments, deposits and other receivables are unsecured, interest-free and repayable on demand.

23. CASH AND CASH EQUIVALENTS AND PLEDGED DEPOSITS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash and bank balances	**2,264,279**	165,126	**2,233,470**	122,486
Less: Pledged deposits against trade finance facilities	**(2,969)**	—	**(704)**	—
Cash and cash equivalents	**2,261,310**	165,126	**2,232,766**	122,486

Cash at banks earn interest at floating rates based on daily bank deposit rates. Short-term time deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Group, and earn interest at the respective short-term time deposit rates. The carrying amounts of cash and cash equivalents and pledged or restricted deposits approximate to their fair values.

24. TRADE PAYABLES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade payables to:				
CSR and its subsidiaries				
(other than the Group)	**57,562**	23,481	**56,170**	8,293
Subsidiaries	**—**	—	**56,210**	30,198
Third parties	**172,750**	167,414	**140,938**	126,090
	230,312	190,895	**253,318**	164,581

The amounts due to CSR and its subsidiaries included in the Group's and the Company's trade payables, and the amounts due to subsidiaries included in the Company's trade payables are unsecured, interest-free and repayable on demand. The normal credit period for trade payables is three months.

An aging analysis of the trade payables is as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 3 months	**170,674**	153,039	**195,646**	135,653
Over 3 months but within 1 year	**43,475**	33,875	**42,348**	26,064
Over 1 year but within 2 years	**15,142**	3,199	**14,534**	2,728
Over 2 years but within 3 years	**657**	203	**692**	136
Over 3 years	**364**	579	**98**	—
	230,312	190,895	**253,318**	164,581

25. NOTES PAYABLE

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 3 months	**36,475**	14,580	**30,145**	14,580
Over 3 months but				
within 6 months	**62,197**	2,700	**62,197**	2,700
	98,672	17,280	**92,342**	17,280

26. OTHER PAYABLES AND ACCRUALS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Receipts in advance	**62,980**	56,500	**60,449**	36,016
Other payables	**45,591**	67,839	**31,428**	42,811
Accruals	**56,430**	6,079	**44,815**	4,891
Amounts due to CSR and its subsidiaries (other than the Group)	**44,697**	30,831	**43,920**	23,351
Subsidiaries	**—**	—	**4,558**	—
	209,698	161,249	**185,170**	107,069

The amounts due to CSR and its subsidiaries included in the Group's and the Company's other payables and accruals, and the amounts due to subsidiaries included in the Company's other payables and accruals are unsecured, interest-free and repayable on demand.

27. PROVISION FOR WARRANTIES

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
At beginning of year	**31,898**	23,377	**22,115**	14,694
Provision made during the year	**33,273**	32,403	**30,588**	24,488
Amounts utilised	**(28,273)**	(23,882)	**(26,608)**	(17,067)
At end of year	**36,898**	31,898	**26,095**	22,115

The Group generally provides one to three year warranties to its customers on certain of its products, under which faulty products are repaired or replaced. The amount of provision is estimated based on sales volume and past experience of the level of repairs and returns. The estimation basis is reviewed on an ongoing basis and revised where appropriate.

28. INTEREST-BEARING BANK AND OTHER BORROWINGS

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Bank loans:				
Secured	**—**	10,000	**—**	10,000
Unsecured	**364,537**	239,541	**364,537**	229,541
	364,537	249,541	**364,537**	239,541
Other borrowings -				
Unsecured	**—**	2,980	**—**	2,980
	364,537	252,521	**364,537**	242,521
Represented by:				
Repayable within one year or on demand:				
Bank loans	**364,537**	249,541	**364,537**	239,541
Other borrowings	**—**	2,980	**—**	2,980
	364,537	252,521	**364,537**	242,521

As at 31 December 2005, the Group's bank loans of approximately RMB229,541,000 and RMB10,000,000 were guaranteed by a subsidiary of CSR and ZELRI, respectively. The Group's other bank loan of RMB10,000,000 as at 31 December 2005 was secured by the Company's notes receivable.

The Group's and the Company's bank loans of approximately RMB364,537,000 as at 31 December 2006 were due within one year and were under open credit terms.

The Group's and the Company's bank loans as at 31 December 2006 bore interest at effective rates ranging from 5.022% to 7.500% per annum during the year ended 31 December 2006.

29. SHARE CAPITAL

	2006	2005
	RMB'000	RMB'000
Registered, issued and fully paid		
- domestic shares of RMB1.00 each	**628,148**	669,612
- H shares of RMB1.00 each	**456,108**	—
	1,084,256	669,612

29. SHARE CAPITAL (Continued)

A summary of the movements in the issued share capital is as follows:

	Notes	Domestic shares of RMB1.00 each RMB'000	H Shares of RMB1.00 each RMB'000	Total RMB'000
At 1 January 2005		—	—	—
Capitalisation as a result of the Reorganisation	(i)	629,812	—	629,812
Capital contribution from the other promoters (note 1)		39,800	—	39,800
At 31 December 2005 and 1 January 2006		669,612	—	669,612
Issuance of new H shares upon listing	(ii)	—	360,560	360,560
Domestic shares converted into H shares upon listing	(ii)	(36,056)	36,056	—
Issuance of new H shares upon full exercise of the Over-allotment Option	(iii)	—	54,084	54,084
Domestic shares converted into H shares upon full exercise of the Over-allotment Option	(iii)	(5,408)	5,408	—
At 31 December 2006		628,148	456,108	1,084,256

Notes

(i) Upon the incorporation of the Company on 26 September 2005, the historical net asset value of the Relevant Businesses was converted into the Company's share capital of RMB629,811,637, comprising 629,811,637 ordinary shares of RMB1.00 each, with all the then existing reserves eliminated and the difference between the amount of share capital issued and the historical net asset value of the Relevant Businesses transferred to the Company as at 30 September 2004 was presented in the reserves of both the Group and the Company. Separate classes of reserves, including retained profits of the Group prior to incorporation of the Company were not separately disclosed as all of these reserves had been capitalised and established in the capital reserves of the Group and the Company pursuant to the Reorganisation.

(ii) On 20 December 2006, the Company issued 360,560,000 new H shares with a par value of RMB1.00 each to the public by way of placement and offer at a price of HK$5.30 per share (equivalent to approximately RMB5.330). In addition, 36,056,000 domestic shares held by ZELRI, CSR Qishuyan and New Leap were converted into 36,056,000 H shares and transferred to the PRC National Council for the Social Security Fund.

(iii) On 28 December 2006, the Company issued an additional 54,084,000 H shares with a par value of RMB 1.00 each, to the public by way of placement at a price of HK$5.30 per share (equivalent to approximately RMB5.327 per share) as a result of the full exercise of the Over-allotment Option. In addition, 5,408,000 domestic shares held by ZELRI, CSR Qishuyan and New Leap were converted into 5,408,000 H shares and transferred to the PRC National Council for the Social Security Fund.

The proceeds received from the issue of the 360,560,000 new H shares and the additional 54,084,000 H shares amounted to RMB2,209,968,000. Part of the proceeds of RMB414,644,000 was recorded as the share capital, and the remaining balance of the proceeds of RMB1,795,324,000 was recorded as capital reserve.

30. RESERVES

The Group

The amount of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity in these consolidated financial statements.

The Company

	Notes	Capital reserve RMB'000	Statutory reserve RMB'000	Proposed final dividend RMB'000	Owners' equity/ retained profits RMB'000	Total RMB'000
At 1 January 2005		—	—	—	463,771	463,771
Profit for the year		—	—	—	126,379	126,379
Total income and expense for the year		—	—	—	126,379	126,379
Capitalisation as a result of the Reorganisation	29(i)	(186,195)	—	—	(443,617)	(629,812)
Appropriation to statutory reserves	(i)	—	13,134	—	(13,134)	—
Distribution of pre-incorporation profit	10	—	—	—	(119,852)	(119,852)
At 31 December 2005 and 1 January 2006		(186,195)*	13,134*	—	13,547*	(159,514)
Profit for the year		—	—	—	268,673	268,673
Total income and expense for the year		—	—	—	268,673	268,673
Issuance of new H shares	29(ii)&(iii)	1,795,324	—	—	—	1,795,324
Share issuing expenses	(ii)	(122,781)	—	—	—	(122,781)
Appropriation to statutory reserves	(i)	—	25,383	—	(25,383)	—
Special dividends	10(ii)	—	—	—	(167,538)	(167,538)
Proposed final dividend	10(iii)	—	—	36,865	(36,865)	—
At 31 December 2006		1,486,348*	38,517*	36,865	52,434*	1,614,164

* These reserve accounts comprise the reserves of RMB1,577,299,000 (2005: RMB(159,514,000)) in the Company's balance sheet.

30. RESERVES (Continued)

Notes:

In accordance with the articles of association of the Company, which is applicable from 1 January 2006, the net profit after tax of the Company for the purpose of profit distribution will be deemed to be the lesser of (i) the net profit determined in accordance with PRC GAAP and (ii) the net profit determined in accordance with IFRS.

Under PRC Company Law and the Company's articles of association, net profit after tax can only be distributed as dividends after allowances have been made for the following:

(a) Making up prior years' cumulative losses, if any.

(b) Allocations to the statutory common reserve fund of at least 10% of after-tax profit, until the fund aggregates to 50% of the Company's issued share capital. For the purpose of calculating the transfer to reserves, the profit after tax shall be the amount determined under PRC GAAP. The transfer to this reserve must be made before any distribution of dividends to shareholders.

The statutory common reserve fund can be used to offset previous years' losses, if any, and part of the statutory common reserve fund can be capitalised as the Company's share capital provided that the amount of this reserve remaining after the capitalisation shall not be less than 25% of the share capital of the Company before the capitalisation.

(c) Allocations to the discretionary common reserve, if approved by the shareholders.

The statutory common reserve fund and discretionary common reserve cannot be used for the purposes other than those for which they are created and are not distributable as cash dividends.

Following the establishment of the Company, the Company appropriated RMB6,567,000 to each of the statutory common reserve and the statutory public welfare fund for the year ended 31 December 2005, which represented 10% of the net profit after tax of the Company for the period from establishment date (26 September 2005) to 31 December 2005, as determined under PRC GAAP.

During the year, the directors of the Company approved the appropriation of RMB25,383,000 to the statutory common reserve fund, which represented 10% of the net profit of the Company for the year ended 31 December 2006, as determined under PRC GAAP.

For dividend purposes, the amount which the Company's PRC subsidiaries can legally distribute by way of a dividend is determined with reference to their profits available for distribution, as reflected in their respective financial statements that are prepared in accordance with PRC GAAP. These profits differ from those dealt with in the financial statements which are prepared in accordance with IFRS.

31. MAJOR NON-CASH TRANSACTION

As mentioned in note 10(i), during the year ended 31 December 2006, the Group settled the pre-incorporation profit distribution of RMB171,328,000 to ZELRI through a set-off against an outstanding receivable from ZELRI.

32. CONTINGENT LIABILITIES

As at 31 December 2006, neither the Group nor the Company had any significant contingent liabilities.

33. OPERATING LEASE ARRANGEMENTS

(i) As lessor

The Group leases its items of property, plant and machinery under operating lease arrangements, with leases negotiated for terms of two years.

As at 31 December 2006, the Group and the Company had total future minimum lease receivables under non-cancellable operating leases with its tenants falling due as follows:

	The Group and the Company	
	2006	2005
	RMB'000	RMB'000
Within one year	**1,867**	—
In the second year	**1,867**	—
	3,734	—

(ii) As lessee

The Group leases certain of its property, plant and machinery under operating lease arrangements, with leases negotiated for terms ranging from approximately one to four years.

As at 31 December 2006, the Group and the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	The Group and the Company	
	2006	2005
	RMB'000	RMB'000
Within one year	**9,578**	127
In the second to fourth years, inclusive	**9,390**	127
	18,968	254

34. COMMITMENTS

The Group and the Company had the following capital commitments at the balance sheet date:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Contracted, but not provided for:				
Acquisition of items of property, plant and equipment	**38,232**	35,487	**29,607**	20,219

In July 2006, the Company entered into an agreement to acquire a 17% equity interest in Siemens Traction Equipment Ltd., Zhuzhou ("Siemens Zhuzhou") from ZELRI at a consideration of 17% of the sum of a base price and an adjustment. The base price is the higher amount of (i) Siemens Zhuzhou's net assets as at 31 December 2005, as valued by a valuation agency designated by both parties and (ii) Siemens Zhuzhou's net assets on its accounts as at 31 December 2005. The adjustment is equal to the difference of Siemens Zhuzhou's net assets on its accounts between 31 December 2005 and the last day of the month immediately preceding the completion of the business registration of the share transfer, as reviewed by an auditor approved by both ZELRI and the Company. The acquisition has not yet been completed at the date of the financial statements.

In April 2006, the Company entered into an agreement to acquire a 50% equity interest in Zhuzhou Shiling Transportation Equipment, Ltd. ("Shiling") from ZELRI at a consideration of 50% of the sum of a base price and an adjustment. The base price is the higher amount of (i) Shiling's net assets as at 31 December 2005, as valued by a valuation agency designated by both parties and (ii) Shiling's net assets on its accounts as at 31 December 2005. The adjustment is equal to the difference between Shiling's net assets on its accounts as at 31 December 2005 and on the last day of the month immediately preceding the completion of the business registration of the share transfer, as reviewed by an auditor approved by ZELRI and the Company. The acquisition was completed in March 2007 at a consideration of RMB63,515,000 in cash, which equals to 50% of the net asset value of Shiling as at 31 December 2006. Thereafter, Shiling became a jointly-controlled entity of the Company.

35. RELATED PARTY TRANSACTIONS

(i) In addition to those disclosed in elsewhere in the financial statements, the Group had the following material transactions with related parties:

	The Group	
	2006	2005
	RMB'000	RMB'000
Transactions with CSR and its subsidiaries:		
Sales of goods	**296,258**	255,651
Purchases of materials and components	**162,404**	91,300
Sales of property, plant and machinery	**673**	—
Purchases of property, plant and machinery	**2,142**	—
Sales of electricity	**762**	—
Purchases of electricity	**—**	4,771
Fees paid for usage of property, plant and machinery	**9,152**	9,127
Supporting service fee	**6,781**	6,478
Rental income from items of property, plant and machinery	**2,221**	—

In the opinion of the directors, the above transactions arise from the ordinary course of the Group's business and were conducted in accordance with mutually agreed terms.

(ii) Compensation of key management personnel of the Company:

	The Group	
	2006	2005
	RMB'000	RMB'000
Short term employee benefits	**3,093**	2,299
Post-employment benefits	**62**	30
Total compensation paid to key management personnel	**3,155**	2,329

Further details of directors' and supervisors' emoluments are included in note 8 to the financial statements.

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

Financial instrument

The financial assets of the Group mainly include cash and cash equivalents, trade and notes receivables, other receivables and other financial assets. The financial liabilities of the Group mainly include other payables and accruals, trade and notes payables, bank loans and other borrowings. The Group did not enter into any derivative activities during the years ended 31 December 2005 and 2006.

Fair value estimates are made at a specific point in time and based on relevant market information and information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The main risks arising from the Group's financial instruments are credit risk, liquidity risk, interest rate risk and foreign currency risk. The directors review and agree policies for managing each of these risks and they are summarised below.

Credit risk

Most of the Group's cash and cash equivalents are held in major financial institutions located in the PRC, which management believe are of high credit quality.

The Group has no significant credit risk with major customers since the Group maintains long-term and stable business relationships with these major customers. The Group performs ongoing credit evaluations of its customers' financial conditions and generally does not require collateral on trade receivables. The Group maintains an allowance for doubtful accounts and actual losses have been within management's expectations.

The Group's notes receivable are mainly guaranteed by banks and the risk of default in payment is minimal.

The Group's trade and notes receivable, and other receivables represent the Group's maximum exposure to credit risk attributable to its financial assets.

Other than the aforesaid, the Group has no significant concentration of credit risk with any single counterparty.

Liquidity risk

The Group policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed credit facilities from banks to meet its commitment over the foreseeable future, in accordance with its strategic plan.

Interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of the changes in market interest rates.

The Group's interest rate risk arises from borrowings. All the borrowings of the Group are negotiated at fixed rates and borrowings issued at fixed rates expose the Group to fair value interest rate risk. The directors of the Company and its subsidiaries believe that the exposure to fair value interest rate risk of financial assets and liabilities was minimum since their deviation from their respective fair values is not significant.

36. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Foreign currency risk

The businesses of the Group are principally conducted in the PRC. While most of the transactions of the Group are principally conducted in RMB, certain of their purchases, sales and borrowings are denominated in other currencies including, among others, United States dollar, European currency units and the Hong Kong dollar. Fluctuation of exchange rates of RMB against foreign currencies can affect the Group's results of operations.

37. EVENTS AFTER THE BALANCE SHEET DATE

(i) During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law ("the New Corporate Income Tax Law") was approved and will become effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. Since the detailed implementation and administrative rules and regulations have not yet been announced, the financial impact of the New Corporate Income Tax Law to the Group cannot be reasonably estimated at this stage.

(ii) In January 2007, the Company, as the single investor, established a subsidiary, (Beijing CSR Times Information Technology Co., Ltd.) and has made a capital contribution of RMB29,000,000 for 100% equity interest therein.

(iii) In March 2007, the acquisition of a 50% equity interest in Shiling by the Company had been completed, further details are set out in note 34 to the financial statements.

38. THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 23 April 2007.

Glossary

"Board" or "Board of Directors"	the board of directors of the Company
"Company"	株洲南車時代電氣股份有限公司 (Zhuzhou CSR Times Electric Co., Ltd.)
"CSR"	中國南方機車車輛工業集團公司 (China Southern Locomotive & Rolling Stock Industry (Group) Corporation), the controlling shareholder of the Parent Company
"CSR Group"	CSR and its subsidiaries, excluding the Parent Group
"CSR Qishuyan"	中國南車集團戚墅堰機車車輛廠 (CSR Qishuyuan Locomotive & Rolling Stock Works), a wholly-owned subsidiary of CSR and one of the Promoters of the Company
"Group"	the Company and its subsidiaries
"Kunming China Railway"	昆明中鐵大型養路機械集團有限公司 (China Railway Large Maintenance Machinery Co., Kunming), held as to 55.56% by 中國鐵道建築總公司 (China Railway Construction Corporation), as to 41.68% by the Staff Committee (聯工持股會) of Kunming China Railway, as to 0.27% by 鐵道科學研究院 (China Academy of Railway Sciences), as to 1.06% by CSR Qishuyan, as to 1.06% by the Parent Company, one of the Promoters and as to 0.27% by 鐵道專業設計院 (China Academy of Railway Designs); one of the Promoters of the Company
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong
"NERCC"	株洲變流技術國家工程研究中心 (Zhuzhou National Engineering Research Center of Converters), a company wholly-owned by the Parent Company

"New Leap"	新力搏交通裝備投資發展有限公司 (New Leap Communication Equipment Invest Development Co., Ltd.), held as to 98% by CSR and as to 1% each by 中國南車集團資陽機車廠 (CSR Ziyang Locomotive Works) and 中國南車集團南京浦鎮車輛廠 (CSR Nanjing Puzhen Rolling Stock Works); one of the Promoters of the Company
"Ningbo Company"	寧波南車時代傳感技術有限公司 (Ningbo CSR Times Sensor Technology Company, Ltd.), a wholly-owned subsidiary of the Company
"Parent Company" or "ZELRI"	中國南車集團株洲電力機車研究所 (CSR Zhuzhou Electric Locomotive Research Institute), a company held as to 51% by CSR and as to 49% by CNR; one of the Promoters and also the controlling shareholder of the Company
"Parent Group"	the Parent Company and its subsidiaries (excluding the Group)
"Promoters"	Promoters of the Company, being ZELRI, ZELC, New Leap, CSR Qishuyan and Kunming China Railway
"Shiling"	株洲時菱交通設備有限公司 (Zhuzhou Shiling Transportation Equipment Company, Ltd.), held as to 50% by the Parent Company, as to 40% by Mitsubishi Electric Corporation and as to 10% Mitsubishi Electric (China) Ltd.
"the year" or "the reporting period"	the year ended 31 December 2006
"Times Electronics"	株洲時代電子技術有限公司 (Zhuzhou Times Electronics Technology Co., Ltd.), a wholly-owned subsidiary of the Company
"Times Guangchuang"	株洲時代廣創變流技術有限公司 (Zhuzhou Times Guangchuang Converter Technology Co., Ltd.), owned as to 85% by Times Electronics

"ZELC"	中國南車集團株洲電力機車有限公司 (CSR Zhuzhou Electric Locomotive Company, Ltd.), held as to 76.05% by CSR, as to 12.61% by the Parent Company, as to 10.08% by New Leap and as to 1.26% by 株洲聯誠集團有限責任公司 (Zhuzhou Lince Group Co., Ltd.); one of the Promoters of the Company
"Zhuzhou CSR Electric"	株洲南車電機股份有限公司 (Zhuzhou CSR Electric Co., Ltd.), the holding company of which is ZELC

Basic Corporate Information

1	Name in Chinese	株洲南車時代電氣股份有限公司
	Name in English	Zhuzhou CSR Times Electric Co., Ltd.
2	Authorized representatives	Liao Bin Tang Tuong Hock, Gabriel
3	Joint company secretaries	Lu Penghu Tang Tuong Hock, Gabriel
	Qualified accountant	Tang Tuong Hock, Gabriel
	Registered office	Times Road, Shifeng District, Zhuzhou, Hunan Province, PRC, 412001
	Telephone	+ 86 733 849 8028
	Fax	+ 86 733 849 3447
	Website	http://www.timeselectric.cn
	Principal place of business in Hong Kong	Unit 1106, 11th Floor, Jubilee Centre, 18 Fenwick Street, Wanchai, Hong Kong,
4	Listing information	H Share The Stock Exchange of Hong Kong Limited Stock Code : 3898 Short Name of Stock : CSR Times Electric
5	H share registrar	Computershare Hong Kong Investor Services Limited Shops 1712-16, 17/F., Hopewell Centre 183 Queen's Road East Wanchai Hong Kong
6	Legal advisers	Jones Day Grandall Legal Group
7	Auditors	Ernst & Young
8	Compliance advisers	Macquarie Securities Limited Polaris Securities (Hong Kong) Limited

株洲南車時代電氣股份有限公司
ZHUZHOU CSR TIMES ELECTRIC CO., LTD.
Times Road, Shifeng District, Zhuzhou
Hunan Province, 412001, PRC