# DONGFENG MOTOR GROUP COMPANY LIMITED*

# 東風汽車集團股份有限公司

*(a joint stock company incorporated in the People's Republic of China with limited liability)*

**(Stock Code: 489)**

## 2006 ANNUAL RESULTS ANNOUNCEMENT

The Board of Directors (the "Board") of Dongfeng Motor Group Company Limited (the "Company") is pleased to announce the consolidated results of the Company, its subsidiaries (the "Group") and its jointly-controlled entities (collectively with the Group, the "Dongfeng Motor Group") for the year ended 31 December 2006 together with the comparative figures in 2005.

In this announcement, unless otherwise specified, all references to revenues, profits and other financial information of the Group include those of the relevant jointly-controlled entities of the Company to the extent that such information has been proportionately consolidated or otherwise reflected in the financial information set out below. Subject to the above and unless otherwise specified, all information in this announcement relating to the Dongfeng Motor Group includes information of the Group and all companies (including jointly-controlled entities of the Company and its associates) in which the members of the Group have direct or indirect equity interests, without regard to the ownership level of, or the proportion of interest held by, the members of the Group in such companies. It should be noted that the Company and its subsidiaries only hold up to 50% of interest in the jointly-controlled entitles of the Company. Statistics of relevant production and sales volume, production capacities and sales and service points of the Dongfeng Motor Group are not calculated on the proportionately consolidation basis.

# CONDENSED CONSOLIDATED INCOME STATEMENT

| | Notes | **2006** **RMB million** | 2005 RMB million |
|---|---|---|---|
| Revenue — Sale of goods | 2, 3 | **48,264** | 41,735 |
| Cost of sales | | **(40,058)** | (35,639) |
| Gross profit | | **8,206** | 6,096 |
| Other income | 3 | **736** | 1,007 |
| Selling and distribution costs | | **(2,157)** | (1,738) |
| Administrative expenses | | **(2,219)** | (1,928) |
| Other expenses, net | | **(1,285)** | (767) |
| Finance costs | 4 | **(411)** | (478) |
| Loss on dilution of interests in jointly-controlled entities | 5 | **(252)** | — |
| Share of profits and losses of associates | | **61** | 29 |
| Profit before tax | 6 | **2,679** | 2,221 |
| Income tax expense | 7 | **(428)** | (474) |
| Profit for the year | | **2,251** | 1,747 |
| Attributable to: | | | |
| Equity holders of the parent | | **2,081** | 1,601 |
| Minority interests | | **170** | 146 |
| | | **2,251** | 1,747 |
| Dividend | 8 | **345** | 1,390 |
| Earnings per share attributable to ordinary equity holders of the parent: | 9 | | |
| Basic for the year | | **24.15 cents** | 25.86 cents |

## CONDENSED CONSOLIDATED BALANCE SHEET

| | Notes | **2006** *RMB million* | 2005 *RMB million* |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | | **15,571** | 14,414 |
| Lease prepayments | | **340** | 350 |
| Intangible assets | | **1,251** | 725 |
| Goodwill | | **434** | 434 |
| Investments in associates | | **486** | 372 |
| Available-for-sale financial assets | | **127** | 163 |
| Loan to a jointly-controlled entity | | **150** | 200 |
| Other long term assets | | **1,040** | 397 |
| Deferred tax assets | | **214** | 73 |
| Total non-current assets | | **19,613** | 17,128 |
| **Current assets** | | | |
| Inventories | | **7,128** | 6,251 |
| Trade receivables | 10 | **1,562** | 1,436 |
| Bills receivable | | **5,774** | 3,542 |
| Prepayments, deposits and other receivables | | **1,649** | 1,576 |
| Due from jointly-controlled entities | | **100** | 126 |
| Other financial assets | | **60** | 109 |
| Restricted cash | | **790** | 423 |
| Cash and cash equivalents | | **7,437** | 7,389 |
| Total current assets | | **24,500** | 20,852 |
| **TOTAL ASSETS** | | **44,113** | 37,980 |
| **EQUITY AND LIABILITIES** | | | |
| Equity attributable to the equity holders of the parent | | | |
| Issued capital | | **8,616** | 8,616 |
| Reserves | | **3,375** | 2,858 |
| Retained profits | | **1,952** | 733 |
| Proposed final dividend | | **345** | — |
| | | **14,288** | 12,207 |
| Minority interests | | **2,534** | 2,127 |
| **Total equity** | | **16,822** | 14,334 |

| | Notes | **2006** **RMB million** | 2005 RMB million |
|---|---|---|---|
| **Non-current liabilities** | | | |
| Interest-bearing borrowings | | **2,087** | 2,226 |
| Other long term liabilities | | **40** | 222 |
| Provisions | | **193** | 205 |
| Government grants | | **51** | 67 |
| Deferred tax liabilities | | **745** | 564 |
| Total non-current liabilities | | **3,116** | 3,284 |
| **Current liabilities** | | | |
| Trade payables | 11 | **7,588** | 5,757 |
| Bills payable | | **4,145** | 2,873 |
| Other payables and accruals | | **5,592** | 5,021 |
| Due to jointly-controlled entities | | **386** | 366 |
| Interest-bearing borrowings | | **5,921** | 5,931 |
| Government grants | | **28** | 18 |
| Income tax payable | | **103** | 69 |
| Provisions | | **412** | 327 |
| Total current liabilities | | **24,175** | 20,362 |
| **TOTAL LIABILITIES** | | **27,291** | 23,646 |
| **TOTAL EQUITY AND LIABILITIES** | | **44,113** | 37,980 |
| **NET CURRENT ASSETS** | | **325** | 490 |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **19,938** | 17,618 |

# NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## 1. Basis of preparation and principal accounting policies

These condensed 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 Interpretation Committee interpretations approved by the International Accounting Standards Committee that remain in effect, and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for the measurement at fair value of foreign currency forward and swap contracts, available-for-sale financial assets, derivative financial instruments and other financial assets.

The principal accounting policies used in the preparation of these financial statements are consistent with those used in the annual audited financial statements for the year ended 31 December 2005, except that the Group has adopted the following new and amended IFRSs and International Financial Reporting Interpretations Committee Interpretations ("IFRICs") during the year. Adoption of these revised standards and interpretations did not have any material effect on these financial statements of the Group. They did however give rise to additional disclosures in the financial statements.

| | |
|---|---|
| IAS 39 Amendments | Financial Instruments: Recognition and Measurement |
| IFRIC — 4 | Determining whether an Arrangement contains a Lease |

The principal effects of these changes are as follows:

**(a) *IAS 39 Financial Instruments: Recognition and Measurement***

(i) *Amendment for financial guarantee contracts*

This amendment has revised the scope of IAS 39 to require financial guarantee contracts issued that are not considered insurance contracts, to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue. The adoption of this amendment has had no material impact on these financial information.

(ii) *Amendment for the fair value option*

This amendment has changed the definition of a financial instrument classified as fair value through profit or loss and has restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through the income statement. The Group had not previously used this option, and hence the amendment has had no effect on the financial information.

(iii) *Amendment for cash flow hedge accounting of forecast intragroup transactions*

This amendment has revised IAS 39 to permit the foreign currency risk of a highly probable intragroup forecast transaction to qualify as a hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated income statement. As the Group currently has no such transactions, the amendment has had no effect on these financial information.

**(b) *IFRIC — 4 Determining whether an Arrangement contains a Lease***

The Group has adopted this interpretation as of 1 January 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial information.

***Change in segment identification***

During the year, the Group changed its identification of reportable business segments. The Group consolidated its previous four segments, namely, "Commercial vehicles", "Passenger vehicles", "Engines and other automotive parts" and "Corporate and others" into three new business segments namely, "Commercial vehicles", "Passenger vehicles" and "Corporate and others". The main change relates to the allocation of the activities pertaining to the previous "Engines and other automotive parts" segment into the respective "Passengers vehicles" segment and "Commercial vehicles" segment to the extent to which such activities are related. In the opinion of the directors, the new basis of segment identification provides a more appropriate presentation of the segment information. Prior year segment information is restated for comparative purposes.

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

| | |
|---|---|
| IAS 1 Amendment | Presentation of Financial Statements: Capital Disclosures |
| IAS 23 (Restated) | Borrowing Costs |
| IFRS 7 | Financial Instruments: Disclosures |
| IFRS 8 | Operating Segments |
| IFRIC — 7 | Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economics |
| IFRIC — 8 | Scope of IFRS 2 |
| IFRIC — 9 | Reassessment of Embedded Derivatives |
| IFRIC — 10 | Interim Financial Reporting and Impairment |
| IFRIC — 11 | IFRS 2 — Group and Treasury Share Transaction |
| IFRIC — 12 | Service Concession Arrangements |

The Group has commenced its assessment of the impact of these new and revised IFRSs and IFRICs but it is not yet in a position to state whether these IFRSs and IFRICs would have a material impact on its results of operations and financial position.

## 2. Revenue on sale of goods

Revenue on sale of goods represents the invoiced value of goods sold, net of value added tax, consumption tax and other sales taxes, after allowances for goods returns and trade discounts, and after eliminations of all significant intra-group transactions.

## 3. Segment information

Segment information is presented by way of the Group's primary segment reporting basis, by business segment. In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets. No further geographical segment information is presented as over 90% of the Group's revenue is derived from customers based in the PRC, and all of its assets are located in the PRC.

The Group's operating businesses are organised and managed separately according to the nature of the products and services provided, with each segment representing a strategic business unit that offers different products and serves different markets. As detailed in note 1 above, the Group adopted a new segment reporting basis and consolidated its businesses into three new business segments during the year. Summary details of these business segments are as follows:

| | |
|---|---|
| Commercial vehicles | Manufacture and sale of commercial vehicles, and the related engines and other automotive parts |
| Passenger vehicles | Manufacture and sale of passenger vehicles, and the related engines and other automotive parts |
| Corporate and others | Corporate operations and manufacture and sale of other automobile related products |

The following tables present revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the years ended 31 December 2006 and 2005.

*Year ended 31 December 2006*

| | Commercial vehicles *RMB million* | Passenger vehicles *RMB million* | Corporate and others *RMB million* | Total *RMB million* |
|---|---|---|---|---|
| **Segment revenue** | **13,215** | **34,219** | **830** | **48,264** |
| Sales to external customers | | | | |
| Other income | **129** | **376** | **231** | **736** |
| Total | **13,344** | **34,595** | **1,061** | **49,000** |
| **Results** | | | | |
| Segmental results | **81** | **3,814** | **(614)** | **3,281** |
| Loss on dilution of interests in jointly-controlled entities | | | | **(252)** |
| Finance costs | | | | **(411)** |
| Share of profits and losses of associates | **26** | **33** | **2** | **61** |
| Profit before tax | | | | **2,679** |
| Income tax expense | | | | **(428)** |
| Profit for the year | | | | **2,251** |
| **Assets and liabilities** | | | | |
| Segment assets | **9,542** | **23,261** | **9,633** | **42,436** |
| Investments in associates | **300** | **165** | **21** | **486** |
| Unallocated assets | | | | **1,191** |
| Total assets | | | | **44,113** |
| Segment liabilities | **5,074** | **8,885** | **4,476** | **18,435** |
| Unallocated liabilities | | | | **8,856** |
| Total liabilities | | | | **27,291** |
| **Other segment information** | | | | |
| Capital expenditure: | | | | |
| — Property, plant and equipment | **659** | **1,713** | **415** | **2,787** |
| — Intangible assets | **22** | **574** | **85** | **681** |
| Depreciation of property, plant and equipment | **427** | **985** | **67** | **1,479** |
| Amortisation of intangible assets | **20** | **109** | **26** | **155** |
| Impairment losses recognised in the income statement | **24** | **21** | **7** | **52** |

*Year ended 31 December 2005*

| | Commercial vehicles *RMB million* | Passenger vehicles *RMB million* | Corporate and others *RMB million* | Total *RMB million* |
|---|---|---|---|---|
| **Segment revenue** | | | | |
| Sales to external customers | 12,989 | 27,915 | 831 | 41,735 |
| Other income | 160 | 270 | 577 | 1,007 |
| Total | 13,149 | 28,185 | 1,408 | 42,742 |
| **Results** | | | | |
| Segmental results | 75 | 2,771 | (176) | 2,670 |
| Finance costs | | | | (478) |
| Share of profits and losses of associates | 7 | 17 | 5 | 29 |
| Profit before tax | | | | 2,221 |
| Income tax expense | | | | (474) |
| Profit for the year | | | | 1,747 |
| **Assets and liabilities** | | | | |
| Segment assets | 10,921 | 19,302 | 6,617 | 36,840 |
| Investments in associates | 290 | 38 | 44 | 372 |
| Unallocated assets | | | | 768 |
| Total assets | | | | 37,980 |
| Segment liabilities | 4,344 | 7,505 | 3,007 | 14,856 |
| Unallocated liabilities | | | | 8,790 |
| Total liabilities | | | | 23,646 |
| **Other segment information** | | | | |
| Capital expenditure: | | | | |
| — Property, plant and equipment | 701 | 2,879 | 471 | 4,051 |
| — Intangible assets | 44 | 153 | 29 | 226 |
| Depreciation of property, plant and equipment | 401 | 830 | 75 | 1,306 |
| Amortisation of intangible assets | 14 | 89 | 9 | 112 |
| Impairment losses recognised in the income statement | 34 | 16 | 1 | 51 |

Due to the change in the segment identification, certain balances and figures in the segment information for the year ended 31 December 2005 have been reclassified to confirm with the current year's presentation.

## 4. Finance Costs

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Interest on bank loans, and other borrowings wholly repayable: | | |
| — within five years | **272** | 358 |
| — beyond five years | **114** | 127 |
| Interest on discounted bills | **59** | 37 |
| Interest on short-term debentures | **7** | — |
| | **452** | 522 |
| Less: Amount capitalised in construction in progress | **(41)** | (44) |
| Net interest expense | **411** | 478 |

## 5. LOSS ON DILUTION OF INTERESTS IN JOINTLY-CONTROLLED ENTITIES

In October and December 2006, Dongfeng Automobile Co., Ltd ("DFAC") and Dongfeng Electronics Technology Co., Ltd. ("DFTC"), subsidiaries of a jointly-controlled entity of the Company with their shares listed on the Shanghai Stock Exchange, have approved in their respective shareholders' meetings to launch a share reform scheme under the requirement of the relevant PRC government authorities, respectively. Pursuant to the scheme which was completed in October and December 2006 respectively, the jointly-controlled entity of the Company was required to grant a certain portion of its shares in DFAC and DFTC to the other shareholders who held the tradeable shares in DFAC and DFTC free of consideration in order to convert the non-tradeable shares in DFAC and DFTC held by the jointly-controlled entity into tradeable shares. Accordingly, the Company's indirect equity interest in DFAC and DFTC were diluted from 35.0% to 30.1% and from 37.5% to 32.5%, respectively, and the dilution loss in aggregate of RMB252 million attributable to the decrease in the share of net assets of DFAC and DFTC was accounted for as a dilution loss in the consolidated income statement for the year ended 31 December 2006.

## 6. Profit before Tax

The Group's profit before tax is arrived at after charging:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Cost of inventories recognised as expense | **40,058** | 35,639 |
| Provision against inventories | **59** | 5 |
| Amortisation of intangible assets | **155** | 112 |
| Depreciation | **1,479** | 1,306 |
| Auditor's remuneration | **18** | 15 |
| Minimum lease payments under operating leases in respect of land and buildings | **159** | 158 |
| Staff costs (excluding directors' and supervisors' remuneration) | **2,234** | 2,022 |
| Loss on disposal of items of property, plant and equipment, net | **57** | 14 |
| Loss on disposal of intangible assets, net | **—** | 8 |
| Gain on disposal of available-for-sale financial assets | **(4)** | — |
| Impairment of property, plant and equipment | **48** | 34 |
| Impairment of available-for-sale financial assets | **8** | 24 |
| Reversal of impairment of other financial assets | **(4)** | (7) |
| Impairment/(reversal of impairment) of trade receivables | **(6)** | 16 |
| Warranty expenses | **317** | 250 |
| Research costs | **905** | 719 |
| Exchange gains, net | **(9)** | (252) |

## 7. Income tax expenses

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Current income tax | **388** | 170 |
| Deferred income tax | **40** | 304 |
| Income tax charge for the year | **428** | 474 |

(a) *Corporate income tax*

Under the relevant PRC Income Tax Law and the respective regulations, the corporate income tax for the Company, its subsidiaries and its jointly-controlled entities is calculated at rates ranging from 10% to 33%, on their estimated assessable profits for the year based on existing legislation, interpretations and practices in respect thereof. As certain of the Company's subsidiaries and its jointly-controlled entities are foreign investment enterprises, after obtaining authorisation from respective tax authorities, these subsidiaries and their jointly-controlled entities are subject to a full corporate income tax exemption for the first two years and a 50% reduction in the succeeding three years, commencing from the first profitable year.

(b) *Hong Kong profits tax*

No provision for Hong Kong profits tax has been made as the Group had no assessable profits arising in Hong Kong during the years ended 31 December 2005 and 2006.

(c) *Deferred income tax*

Deferred tax assets have been recognised at the end of each year in respect of temporary differences relating to certain future deductible expenses for the purpose of corporate income tax arising from the impairment of various assets.

Deferred tax liabilities were mainly recognised for taxes that would be payable on the unremitted earnings of certain of the Company's subsidiaries, jointly-controlled entities or associates.

## 8. Dividend

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Special dividend — Nil (2005: RMB23.09 cents) per ordinary share | **—** | 1,390 |
| Proposed final — RMB0.04 (2005: Nil) per ordinary share | **345** | — |
| | **345** | 1,390 |

The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

On 29 October 2005, the directors proposed to declare a dividend of RMB23.09 cents per share amounting to RMB1,390 million to its then sole shareholder, DFM, which was approved in the shareholder's meeting on the same date.

## 9. Earnings Per Share Attributable to Equity Holders of the Parent

The calculation of basic earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the parent, and the weighted average number of ordinary shares in issue during the year.

The weighted average number of ordinary shares used in the calculation is the number of ordinary shares in issue during the year.

The calculation of basic earnings per share is based on:

| | 2006 | 2005 |
|---|---|---|
| | *RMB million* | *RMB million* |
| Earnings: | | |
| Profit for the year attributable to ordinary equity holders of the parent | **2,081** | 1,601 |

| | *Number of shares* | |
|---|---|---|
| | ***million*** | *million* |
| Shares: | | |
| Weighted average number of shares in issue during the year | **8,616** | 6,192 |

No diluted earnings per share amount has been disclosed as no diluting events existed during the year.

## 10. Trade Receivables

Sales of the Group's and its jointly-controlled entities' commercial and passenger vehicles are normally settled on an advance receipt basis, whereby the dealers are required to pay in advance either in cash or by bank acceptance drafts. However, in the case of long-standing customers with bulk purchases and a good repayment history, the Group and its jointly-controlled entities may offer these customers credit terms that are generally between 30 and 180 days. For sales of engines and other automotive parts, the Group and its jointly-controlled entities generally offer their customers credit terms that are generally between 30 and 180 days. Trade receivables are non-interest-bearing.

An aged analysis of the trade receivables, net of impairment, of the Group, based on the due date, is as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Within three months | **1,361** | 1,171 |
| More than three months but within one year | **157** | 208 |
| More than one year | **44** | 57 |
| | **1,562** | 1,436 |

## 11. Trade Payables

An aged analysis of the trade payables of the Group, based on the due date, is as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Within three months | **6,804** | 5,098 |
| More than three months but within one year | **589** | 514 |
| More than one year | **195** | 145 |
| | **7,588** | 5,757 |

## 12. Commitments

(a) *Operating lease commitments as lessee*

The Group's future minimum rental payables under non-cancellable operating leases are as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Within one year or on demand | **2** | — |
| After one year but not more than five years | **67** | 50 |
| More than five years | **789** | 835 |
| | **858** | 885 |

In addition, the Group's share of future minimum rental payables under non-cancellable operating leases of its jointly-controlled entities, which are not included in the above are as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Within one year or on demand | **95** | 83 |
| After one year but not more than five years | **359** | 328 |
| More than five years | **569** | 485 |
| | **1,023** | 896 |

(b) *Commitments*

In addition to the operating lease commitments detailed in note 12(a) above, the Group had the following commitments at the balance sheet date:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Contracted, but not provided for: | | |
| Property, plant and equipment | **9** | 86 |
| Capital contribution to an associate | **175** | — |
| | **184** | 86 |
| Authorised, but not contracted for: | | |
| Property, plant and equipment | **—** | 3 |

In addition, the Group's share of the capital commitments of its jointly-controlled entities, which are not included in the above, is as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Contracted, but not provided for: | | |
| Property, plant and equipment | **1,785** | 1,675 |
| Authorised, but not contracted for: | | |
| Property, plant and equipment | **1,355** | 1,210 |

## 13. Contingent Liabilities

At the balance sheet date, contingent liabilities not provided for in the financial statements were as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Guarantees given to banks in connection with facilities granted to jointly-controlled entities at nil consideration: | **742** | 844 |

In addition, the Group's share of the contingent liabilities of its jointly-controlled entities not provided for in the financial statements, which are not included in the above, is as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Guarantees given to banks in connection with facilities granted to the following parties at nil consideration: | | |
| — Associates | **53** | 10 |
| — Others | **85** | 111 |
| Pending litigation | **32** | — |
| | **170** | 121 |

No financial liabilities were recorded for the above guarantees given to banks as, in the opinion of the directors, the fair values of the financial guarantee contracts were not material as at 31 December 2005 and 2006.

## 14. Post Balance Sheet Events

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.

# CHAIRMAN'S STATEMENT

Dear shareholders,

I am pleased to submit the annual report for the year ended 31 December 2006 of Dongfeng Motor Group Company Limited for your review.

With the dynamic progress and healthy development in the PRC economy, its automotive industry continued to grow rapidly in 2006. On the basis of statistics published by the China Association of Automobile Manufactures, the whole automotive manufacturing sector produced approximately 7.28 million vehicles and sold approximately 7.22 million vehicles in 2006, representing an increase of approximately 27% and 25% respectively compared to last year.

The year 2006 was a significant one in the development of the Dongfeng Motor Group. Besides its overall production and sales growth in line with other players, the performance of its passenger vehicle business excelled in the market and all of the joint ventures' operations were back on a rising track. During the year, the Dongfeng Motor Group manufactured approximately 756,000 vehicles, and realized sales of approximately 751,000 vehicles, representing a growth of 26.4% and 26.3% on the previous year, and the sales took up approximately 10.4% of the market share according to the China Association of Automobile Manufacturers. Hence, the combined sales achieved was RMB48,264 million and profit attributable to equity holders of the parent amounted to RMB2,081 million. Dongfeng Peugeot Citroën Automobiles Company Ltd, the joint venture between the Company, Peugeot Citroën Automobiles, Automobiles Citroën and Automobiles Peugeot was profitable for the year, laying a solid groundwork for its continuous development.

During 2006, the Dongfeng Motor Group moved steadily and proactively in the expansion of production capacity, Research and Development, product launches and construction of the after-sales service network. The aggregate production capacity reached 945,000 vehicles as at 31 December 2006 with reasonable utilization rate attained. The Dongfeng Motor Group had made progress in various major Research and Development projects. In particular, 36 vehicle models with over 100 varieties including 東風天龍, 大力神, which signified a new generation of medium and heavy commercial vehicles were launched on the market. With regard to passenger vehicles, 7 new models were launched. These innovations have ensured the continuity of technological and product development and have provided greate depth to cater for the needs of the market. During the year, the composition of the after-sales service network was fine-tuned and its market coverage was further enlarged. Meanwhile, the Dongfeng Motor Group also continued to emphasize the importance of safety conditions and environmental protection. The Dongfeng Motor Group also continued to pay particular attention to the protection of our staff's legal rights and to corporate social responsibility. These are pivotal to the Dongfeng Motor Group's harmonious working environment and the continuous and stable growth.

However, the Board was aware that the development of commercial vehicle business of the Dongfeng Motor Group was unstable, especially for heavy and medium trucks. The outcome of marketing efforts for the new products was not meeting the expectation in full. There were signs of improvement in the second half of the year and with the implementation of adjustment of product mix, there is considerable room to enhance the Group's profitability.

The Board considers that the business segments of the Dongfeng Motor Group as a whole contributed to encouraging results in 2006. On the other hand, the Dongfeng Motor Group has been facing long-term challenges. Our honorable shareholders, please be assured that we always uphold the philosophy of adding value for you regardless of setbacks or accomplishments. The Board is committed to enhancing and strengthening the Company's profitability and position in the industry in order to push forward its lasting development in 2007 and the years to come.

**Xu Ping**
*Chairman*

Wuhan, the PRC
18 April 2007

## BUSINESS REVIEW AND OUTLOOK

### Business Overview

**I** ***Major Businesses of the Dongfeng Motor Group***

The principal products of the Dongfeng Motor Group include commercial vehicles, which comprise trucks and buses, and passenger vehicles (which comprise basic passenger cars, MPVs and SUVs) and engines and other auto parts. The trucks comprise heavy trucks, medium trucks and light trucks. The Dongfeng Motor Group is also engaged in other automotive-related businesses such as the import/export of vehicles and vehicle manufacturing equipment, auto finance businesses, insurance agency businesses and used car businesses.

The commercial vehicle business of the Dongfeng Motor Group, which was established in 1969, has commanded a leading position in the PRC commercial vehicle industry for many years. Currently, the Dongfeng Motor Group's whole commercial whole vehicle and engines and auto parts businesses are principally operated by Dongfeng Motor Co., Ltd., the joint venture between the Company and Nissan Motor Co., Ltd (through Nissan (China) Investment Co., Ltd).

The Dongfeng Motor Group's passenger vehicle business is principally operated by the following companies: Dongfeng Motor Co., Ltd, Dongfeng Peugeot Citroën Automobiles Company Ltd (the joint venture between the Company, Peugeot Citroën Automobiles, Automobiles Citroën and Automobiles Peugeot) and Dongfeng Honda Automobile Co., Ltd (the joint venture between the Company and Honda Motor Co., Ltd (partly through Honda Motor (China) Investment Co., Ltd, a wholly-owned subsidiary of Honda Motor Co., Ltd.)). At present, the Dongfeng Motor Group's engines and auto parts business for passenger vehicles is principally operated by Dongfeng Motor Co., Ltd, Dongfeng Peugeot Citroën Automobiles Company Ltd, Dongfeng Honda Engine Co., Ltd, Dongfeng Honda Auto Parts Co., Ltd and Dongfeng Honda Automobile Co., Ltd.

The Dongfeng Motor Group's vehicle manufacturing equipment business is in conducted primarily through Dongfeng Motor Co., Ltd.

1. *Commercial vehicles*

   As of 31 December 2006, the members of the Dongfeng Motor Group produced 33 principal basic series of whole commercial vehicles, including 27 principal basic series of trucks and 6 principal basic series of buses. Most of the whole commercial vehicles manufactured by the Dongfeng

Motor Group are manufactured by Dongfeng Motor Co., Ltd. Commercial vehicles manufactured by the Dongfeng Motor Group are currently sold mainly through three major after-sales services networks devoted exclusively to the provision of sales and services for the whole commercial vehicles manufactured by the Dongfeng Motor Group, which form one of the most extensive commercial vehicle sales and services networks in the PRC.

Members of the Dongfeng Motor Group manufacture commercial vehicle engines mainly for their internal use and also for external sales. The members of the Dongfeng Motor Group which manufacture engines are mainly Dongfeng Motor Co., Ltd, which mainly manufactures Dongfeng series and Cummins series diesel and petrol commercial vehicle engines. In addition to the manufacture of engines, members of the Dongfeng Motor Group also manufacture a range of auto parts for commercial vehicles, including power transmission systems (mainly comprised of gear box, clutch, and transmission shaft), vehicle bodies (mainly comprised of pressed products) and chassis (mainly comprised of axles, car frames and chassis parts), electronic parts and other parts.

2. *Passenger vehicles*

As of 31 December 2006, the members of the Dongfeng Motor Group produced 18 series of passenger vehicles, including 14 series of passenger cars, 2 series of MPV and 2 series of SUV. The passenger vehicles manufactured by the Dongfeng Motor Group are currently sold together with after-sales services through 5 independently managed after-sales services networks throughout the PRC. Each of these networks sells one brand of passenger vehicle with after-sales services, and is managed by the relevant Joint Venture Company and Dongfeng Motor Group.

Members of the Dongfeng Motor Group manufacture passenger and commercial vehicle engines mainly for their internal use and also for external sales. The members of the Dongfeng Motor Group which manufacture engines are Dongfeng Motor Co., Ltd, Dongfeng Peugeot Citroën Automobile Company Ltd, Dongfeng Honda Engine Co., Ltd and Dongfeng Honda Automobile Co., Ltd. Dongfeng Motor Co., Ltd mainly manufactures Nissan series sedan engines; Dongfeng Honda Engine Co., Ltd and Dongfeng Honda Automobile Co., Ltd manufacture Honda series sedan engines; Dongfeng Peugeot Citroën Automobile Company Ltd manufactures Citroën series and Peugeot series sedan engines. In addition to the manufacture of engines, members of the Dongfeng Motor Group also manufacture a range of auto parts for commercial vehicles, including power transmission systems (mainly comprised of gear box, clutch, and transmission shaft), vehicle bodies (mainly comprised of pressed products) and chassis (mainly comprised of axles, car frames and chassis parts), electronic parts and other parts.

3. *Other businesses*

The Dongfeng Motor Group is also engaged in the manufacture of vehicle manufacturing equipment through Dongfeng Motor Co., Ltd. Vehicle manufacturing equipment manufactured by Dongfeng Motor Co., Ltd includes machine tools, coating equipment, pressing and forging moulds, and measuring and cutting tools. In addition, Dongfeng Motor Co., Ltd provides various equipment maintenance services.

In addition to the products described above, the Dongfeng Motor Group is engaged in various other automotive-related businesses, including vehicle and vehicle manufacturing equipment import/export, auto finance, insurance agency and used car sales businesses.

## II ***Business Operations during the year under review***

1. *Sales and production volume and market share for whole vehicles of the Dongfeng Motor Group*

As of 31 December 2006, the production volume and sales volume for whole vehicles of the Dongfeng Motor Group was 756,319 and 751,088 units respectively. According to the statistics published by the China Association of Automobile Manufacturers, the Dongfeng Motor Group held a domestic market share of approximately 10.4% in terms of the total domestic sales of commercial and passenger vehicles in 2006. The following table sets out the sales and production volume of the Dongfeng Motor Group for commercial and passenger vehicles, as well as its market share in terms of sales volume in 2006 (on the basis of statistics published by the China Association of Automobile Manufactures):

| | | **No. of units produced** *(units)* | | **No. of units sold** *(units)* | **Market share in terms of sales volume** *(%)* |
|---|---|---|---|---|---|
| Commercial Vehicles | | 260,240 | | 256,242 | 12.6 |
| Trucks | 221,501 | | 217,965 | | 12.4 |
| Buses | 38,739 | | 38,277 | | 13.2 |
| Passenger Vehicles | | 496,079 | | 494,846 | 9.6 |
| Basic passenger cars | 436,379 | | 438,103 | | 11.4 |
| MPVs | 24,572 | | 23,450 | | 12.3 |
| SUVs | 35,128 | | 33,293 | | 14.0 |
| Total | | 756,319 | | 751,088 | 10.4 |

2. *Ranking of the Dongfeng Motor Group's major vehicle lines in the domestic market in 2006 (on the basis of statistics published by the China Association of Automobile Manufactures):*

| | **Number of units sold by the Dongfeng Motor Group** *(units)* | **Ranking in the domestic market** |
|---|---|---|
| Heavy trucks | 66,778 | 1 |
| Medium trucks | 50,426 | 2 |
| Light trucks | 100,761 | 2 |
| Basic passenger cars | 438,103 | 3 |
| MPVs | 23,450 | 4 |
| SUVs | 33,293 | 3 |

3. *Sales Revenue*

As of 31 December, 2006, the sales revenue of the Group was RMB48,264 million.

| | Sales revenue *(RMB millions)* | | Contribution to the Group's sales revenue *(%)* | |
|---|---|---|---|---|
| Commercial vehicles | | 13,215 | | 27.4 |
| Whole vehicles | 11,471 | | 23.8 | |
| External sales of engines and auto parts | 1,744 | | 3.6 | |
| Passenger vehicles | | 34,219 | | 70.9 |
| Whole vehicles | 27,014 | | 56.0 | |
| External sales of engines and auto parts | 7,205 | | 14.9 | |
| Others | | 830 | | 1.7 |
| Total | | 48,264 | | 100.0 |

## III *Production Capacity, Production Capacity Distribution and Future Expansion Plans*

As at 31 December 2006, the total motor vehicle production capacity of the Dongfeng Motor Group was 945,000 units, among which the production capacity of commercial vehicles was 320,000 units and the production capacity of passenger vehicles was 625,000 units. The total production capacity of engines was 1,180,000 units.

The following table shows the production capacity distribution of vehicles and engines of the Dongfeng Motor Group as at 31 December 2006:

1. *Production capacity of commercial vehicles*

| **Company** | **Production capacity** *('000 units)* |
|---|---|
| Dongfeng Motor Co., Ltd | 315 |
| Dongfeng Nissan Diesel Motor Co., Ltd | 5 |

2. *Production capacity of passenger vehicles*

| **Company** | **Production capacity** *('000 units)* |
|---|---|
| Dongfeng Motor Co., Ltd | 285 |
| Dongfeng Peugeot Citroën Automobiles Company Ltd | 220 |
| Dongfeng Honda Automobile Co., Ltd | 120 |

3. *Production capacity of engines*

| **Company** | **Production capacity** *('000 units)* |
|---|---|
| Dongfeng Motor Co., Ltd | 500 |
| Dongfeng Peugeot Citroën Automobiles Company Ltd | 200 |
| Dongfeng Honda Automobile Co., Ltd | 120 |
| Dongfeng Honda Engine Co., Ltd | 360 |

**IV** ***Production safety and environmental protection***

In 2006, management and production officers of all levels of the Dongfeng Motor Group adhered to the concept of safety development and complied with the national laws and regulations, and policies of production safety. They handled safety and development properly by continuing to enhance the corporate culture for safety, strengthening the basic safety management, improving the safety production responsibility system and establishing a healthy long term effective safety management mechanism and accident precaution mechanism. Production safety and economic benefits were developed to ensure the safety and health of the staff of the Dongfeng Motor Group, as well as the stable and sustainable development of the Dongfeng Motor Group.

In 2006, the Dongfeng Motor Group achieved the goal of "five eliminations" — namely minimizing any serious accidents of occupational injuries and deaths, fire disasters, explosions of boilers, pressure vessels and pipes, emissions of hazardous chemicals and explosions, and occupational poisonings. During the year, there were 92 occupational injuries in total, of which 12 were serious and 80 were minor. The frequency of accidents was 1.07 % and frequency of serious injuries was 0.14%. Occupational injuries of all kind were below the control standard.

For environment protection, the Dongfeng Motor Group strictly complied with the national laws and regulations and developed the concepts of scientific development, clean development and sustainable growth, and put an emphasis on "precaution and treatment, with precaution as priority" with the aim for reducing the emission of pollutants and their concentration, to ensure that no occurrence of material pollution during the year. The Dongfeng Motor Group implemented the environment protection assessment for all projects, and the achievement rate for monitoring the emission of key pollution was approximately 99.8%, disposal rate for solid wastes achieved 100% and the discharge of industrial waste water for 100 million production value reduced by approximately 0.93% as compared to that in 2005.

The Dongfeng Motor Group sees environment protection as an integral part of its production and operation, and formulates, develops and implements its production and operation plan in line with its environment protection measures, aiming to realize production and environment protection at the same time. The Dongfeng Motor Group managed to (i) implement its environment protection measures in its entire value chain of production, with continuous improvement and adaptability development, and striving to develop the core technology for energy saving and environmental protection, (ii) to allocate funds for the improvement of material, technical procedures and environment protection facilities to reduce the amount of pollutants and their concentration from the sources, and devoting to the development of cycle economy to increase the utility rate of the energy and raw material, and (iii) to focus on the management of environment protection during the production processes to maximize the utilization of the environment protection facilities to ensure the permitted level of emission, and implementation of ISO14001 environment protection system for the management of important environment factors and finding out problems and hidden danger in advance to ensure a much stricter environment protection management standard, and (iv) to establish an environmentally friendly automobile manufacturer by further implementing the three "environmentally clean chains", i.e. the reduction of pollutants, recycling of resources in the production process and the reduction of the discharge of wastes to realize energy saving, reduction of consumption and pollution and increase of efficiency.

**V** ***Sales and Service Networks***

The motor vehicles manufactured by the Dongfeng Motor Group are sold together with after-sales services in the PRC through 8 major sales and service networks. Each of these 8 sales and service networks sells vehicles manufactured by a particular Joint Venture Company with after-sales services, and is managed by the relevant Joint Venture Company independently of the other members of the

Dongfeng Motor Group. The sales outlets which comprise each network are generally owned and operated by independent third parties. The Dongfeng Motor Group provides after-sales services through these distribution and services networks.

The commercial vehicles are mainly distributed with after-sales services through 3 major sales and service networks, which are devoted to the distribution of, and after-sales services for, the commercial vehicles manufactured by Dongfeng Motor Co., Ltd.

The passenger vehicles are mainly sold together with after-sales services through 5 sales and service networks. Each of these networks sells one brand of passenger vehicle with after-sales services, and is operated by the relevant Joint Venture Company independently of the Dongfeng Motor Group.

1. *Sales and service networks for commercial vehicles*

The Dongfeng Motor Group is currently one of the commercial vehicle manufacturers in the PRC operating one of the most extensive after-sales service networks. The following table sets out the details of the major domestic after-sales service networks for commercial vehicles of the Dongfeng Motor Group as at 31 December 2006.

| | **No. of after-sales services outlets** | **No. of first-level outlets** | **No. of second-level outlets** | **No. of provinces/ cities covered** |
|---|---|---|---|---|
| Dongfeng Motor Co., Ltd (commercial vehicle company) | 565 | 328 | 237 | 31/323 |
| Dongfeng Automobile Co., Ltd | 580 | 580 | — | 31/303 |
| Dongfeng Liuzhou Motor Co., Ltd | 406 | 406 | — | 28/318 |

2. *Sales and service networks for passenger vehicles*

The passenger vehicle sales and service networks operated by the Dongfeng Motor Group, which comprises passenger vehicle sales and service networks mainly operated by Dongfeng Motor Co., Ltd, Dongfeng Peugeot Citroën Automobiles Company Ltd and Dongfeng Honda Automobile Co., Ltd, is currently one of the most extensive sales and service networks for passenger vehicles in the PRC automotive market.

The following table sets out the details of the different major domestic after-sales service networks for passenger vehicles of the Dongfeng Motor Group as at 31 December 2006.

| | **No. of after-sales services outlets** | **No. of first-level outlets** | **No. of second level outlets** | **No. of provinces/ cities covered** | **Product type serviced** |
|---|---|---|---|---|---|
| Dongfeng Nissan Passenger Vehicle Company | 280 | 244 | 36 | 31/172 | Nissan passenger vehicles |
| Dongfeng Peugeot Citroën Automobiles Company Ltd | 321 | 321 | | 31/171 | Citroën passenger vehicles |
| | 202 | 110 | 92 | 30/143 | Peugeot passenger vehicles |
| Dongfeng Honda Automobile Co., Ltd | 119 | 119 | | 29/82 | Honda passenger vehicles |
| Dongfeng Liuzhou Motor Co., Ltd | 185 | 181 | 4 | 29/136 | Dongfeng Future passenger vehicles |
| Zhengzhou Nissan Automobile Co., Ltd | 293 | 257 | 36 | 31/248 | Nissan passenger vehicles |

## VI *Investment in 2006 and Future Investment Plan for the next two years*

The Dongfeng Motor Group has managed to invest by adhering to the principle of rational and profitable investment. The actual total investment in 2006 was RMB5,515 million. According to the Dongfeng Motor Group's future plan for products and business plan, the total investment in the next two years will still remain at a high level. The total investment in 2007 is expected to be approximately RMB9,830 million, while the total investment in 2008 is expected to be approximately RMB9,695 million.

## VII *Research & Development*

In the year 2006, the Dongfeng Motor Group's development of new models of the third-generation 1.5 ton highly flexible off-road vehicle series was completed and the development of the second-generation 3.5 ton off-road vehicle series was also completed.

The development of mixed power passenger buses/cars made new advances, with whole vehicles and certain core components for development having promising industrial prospects. The Dongfeng Motor Group also received two national 863 projects in the "11th five-year plan" after successfully passing the government's inspection for the national 863 project in the "10th five-year plan".

For heavy medium commercial vehicles, the Dongfeng Motor Group launched brand-new products such as Dongfeng "Kinland" and 東風大力神, with 36 models and 100 brands in total, to equip with the newly-developed D310 driving cab.

For light vehicles, the enhanced models of Dongfeng Xiaobawang and Dongfeng Duolika entered into the market during 2006.

Research developments on new technology for commercial vehicles was as follows: the preliminary development of electrically controlled common trail injection technology for engines, whole vehicle electronic control technology, "AMT控制器開發", "混合動力整車控制器開發", "越野車用差速器總成台架試驗方法研究" and power train integration technology made significant progress, which served as technological exploration and reserves in the areas of automotive advance technology. Reliability design, simulation analysis technology, system matching technology and trial verification technology were further strengthened and applied. The development of products thus became more efficient and of higher technical level.

In relation to passenger vehicles, 7 new vehicles were launched to create new a growth point for sales. The vehicles launched included new Teana, Bluebird Sylphy, Geniss, Dongfeng Peugeot 206, 東風雪鐵龍凱旋, C2 and CIVIC, Dongfeng Honda's first attempt in passenger cars.

## VIII Business Outlook

*Position in the industry*

It is expected that the sales and production volume of the Dongfeng Motor Group will continue to grow at a fast pace in order to strengthen and raise its position in the PRC automotive industry by enlarging its market share.

*Increase in production capacity*

According to the automotive market forecast and the business plan of the Dongfeng Motor Group, production capacity will rise gradually so as to meet the needs of manufacturing products, while capacity utilization will continue to increase. By the year 2008, the production capacity of motor vehicles is expected to reach approximately 1,280,000 units and to approximately 1,630,000 units by 2010.

*New products to the market*

There are 4 to 8 new models of passenger vehicles being put into the market by the Dongfeng Motor Group every year. After the new generation of heavy trucks, represented by Dongfeng "Kinland", entered into the market in 2006, the Dongfeng Motor Group, to cater for the market need, will continue to work on the research and development of a new generation of long head medium vehicles and new engine products for commercial medium vehicles.

*Profitability*

To maintain or improve the profitability and the profit level, the Dongfeng Motor Group will further implement measures that would raise the rate of localization, improve technology which would lower costs and reduce expenses, etc.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE RESULTS

### Financial Results Overview

During the year, revenue of the Group amounted to approximately RMB48,264 million, representing an increase of approximately RMB6,529 million, or 15.6%, when compared with approximately RMB41,735 million of 2005. The profit of the Group attributable to shareholders amounted to approximately RMB2,081 million for the year, representing an increase of approximately RMB480 million, or 30.0%, when compared with of approximately RMB1,601 million of 2005. Earnings per share of the Group was approximately RMB24.15 cents.

In 2006, after excluding the one-time expenses of approximately RMB252 million arising from the share reform schemes for Dongfeng Automobile Co., Ltd and Dongfeng Electronics Technology Co., Ltd., whose shares are listed on the A-share market in Mainland China, the adjusted net profit of the Group amounted to approximately RMB2,333 million, representing an increase of approximately RMB732 million, or 45.7%, over the net profit in 2005. In 2006, the adjusted earnings per share of the Group was RMB27.07 cents.

### Revenue

During the year, the total revenue of the Group amounted to approximately RMB48,264 million, representing an increase of approximately RMB6,529 million, or 15.6%, when compared with the figure in 2005 of approximately RMB41,735 million.

| | **2006 Revenue from sales** *RMB million* | | ***Units sold*** | 2005 Revenue from sales *RMB million* | | *Units sold* |
|---|---|---|---|---|---|---|
| **Passenger vehicles:** | | **34,219** | **N/A** | | 27,915 | N/A |
| Whole vehicles | **27,014** | | **494,846** | 21,798 | | 351,219 |
| External sales of engines and parts | **7,205** | | **N/A** | 6,117 | | N/A |
| **Commercial vehicles:** | | **13,215** | **N/A** | | 1,2989 | N/A |
| Whole vehicles | **11,471** | | **256,242** | 11,193 | | 243,582 |
| External sales of engines and parts | **1,744** | | **N/A** | 1,796 | | N/A |
| Others | | **830** | **N/A** | | 831 | N/A |
| Total | | **48,264** | **751,088** | | 41,735 | 594,801 |

*Note:* It should be noted that the revenue figures in the above table reflected the proportionate consolidated revenue of the Group. However, the related figures of the units of vehicles sold by the Group in the above table represented the actual units sold by the Dongfeng Motor Group, not adjusted on a proportionate consolidation basis, for the indicated periods.

During the year, revenue of the Group from sales of passenger vehicles increased by approximately RMB6,304 million, or 22.6%, from approximately RMB27,915 million in 2005 to approximately RMB34,219 million. Of which, revenue from sales of whole passenger vehicles increased by approximately RMB5,216 million, or 23.9%, from approximately RMB21,798 million in 2005 to approximately RMB27,014 million. Despite oil price hikes, increase in consumption tax and auto price decline for intensifying market competition during the year, the revenue from sales of passenger vehicles recorded a significant increase of 23.9%. That was mainly attributable to a significant increase in the sales volume of vehicles. During the year, the total sales volume of whole passenger vehicles increased by 40.9% to 494,846 units from 351,219 units in 2005, higher than the industry growth rate of 30.0% for passenger vehicles. The market share in terms of sales volume of the Dongfeng Motor Group for the year increased to approximately 9.6% from approximately 8.8% in 2005. The newly released Peugeot 206, C-Triomphe, Civic, Sylphy, Geniss and C2 in 2006 gained wide acceptance in the market with encouraging sales performance. Meanwhile, the sales of various existing passenger vehicle series had not been affected by the above new model launches and remained encouraging during the year. During the year, because of the diversification of the product mix, the whole passenger vehicles of the Dongfeng Motor Group successfully extended its market share in high and medium as well as small passenger vehicles. The change of the product mix of the whole passenger vehicles (with gross profit margin of the Group increased to 17.9% from 14.5% in 2005) drove the revenue of the Group from sales of whole passenger vehicles to increase by approximately 23.9%.

Revenue of the Group from the sale of passenger vehicle engines and other auto parts increased by approximately 17.8% to RMB7,205 million for the year from RMB6,117 million in 2005. This overall increase in revenue of passenger vehicle engines and other auto parts was primarily due to the steady growth trend in the sales volume brought about by the enhancement in the engines of Dongfeng Honda Engine Co., Ltd.

During the year, the sales volume of commercial vehicles of the Dongfeng Motor Group increased by approximately 5.2%, maintaining its leading position in the domestic commercial vehicles market; revenue of the Group increased by approximately RMB226 million, or 1.7%, from approximately RMB12,989 million in 2005 to approximately RMB13,215 million. Of which, revenue of the Group from sales of whole commercial vehicles increased by approximately RMB278 million from approximately RMB11,193 million in 2005 to approximately RMB11,471 million, increased by approximately 2.5% for the whole year, representing a turnaround from the approximately 15.2% drop in sales volume in the first half of the year. The increase was mainly resulted from a series of promotion activities launched by the Dongfeng Motor Group, bringing about the approximately 24.3% increase in sales volume of whole commercial vehicles of the Dongfeng Motor Group for the second half of the year as compared with the corresponding period in 2005. During the year, sales volume of the Dongfeng Motor Group's heavy trucks decreased from 71,652 units in 2005 to 66,778 units, while the sales volume increased by approximately 12.3% for the second half of the year as compared with the corresponding period in 2005. As the newly launched "Kinland" heavy trucks by the Dongfeng Motor Group was going through the adjustment process, its sales volume failed to meet the expected target. During the year, sales volume of medium trucks decreased from 55,883 units in 2005 to 50,426 units, while the sales volume increased by approximately 18.3% for the second half of the year as compared with the corresponding period in 2005. The Dongfeng Motor Group's sales volume of light trucks during the year increased from 82,569 units in 2005 to 100,761 units, the growth in sales volume for the second half of the year was approximately 34.2% compared with the corresponding period in 2005.

## COST OF SALES AND GROSS PROFIT MARGIN

During the year, the total cost of sales of the Group was approximately RMB40,058 million, representing an increase of approximately RMB4,419 million when compared with approximately RMB35,639 million in 2005. The gross profit margin of the Group increased to 17.0% from 14.6% in 2005, primarily because the Group maintained the selling price at a reasonable level through launching various competitive new vehicle models to avoid price decrease, and on the other hand adopted cost reduction measures. The measures included increasing the localization ratio, controlling expenses in the sourcing, technical and management areas, and involving all the staff to cut expenses for the whole production process and the entire value chain, resulting in drop in the unit cost for various vehicle models to different extent. During the year, the gross profit margin of passenger vehicles increased to approximately 18.9% from approximately 15.8% in 2005, and the gross profit margin of whole passenger vehicles increased to approximately 17.9% from approximately 14.5% in 2005.

During the year, the gross profit margin of passenger vehicle engines and other auto parts increased to approximately 22.6% from approximately 20.4% in 2005. The rise in the price of key raw materials such as fuel and aluminum in the PRC during the year led to the increase of material costs to some extent. However, the cost savings resulting from RMB appreciation against Japanese Yen offset the effect of price increase of domestic raw materials. Coupled with the adoption of measures such as increasing the localisation ratio, optimising work processes and reducing costs, the gross profit margin of passenger vehicle engines and other auto parts increased during the year.

During the year, the gross profit margin of the Group's commercial vehicles increased to approximately 12.0% from approximately 11.3% in 2005, and the gross profit margin of whole commercial vehicles increased to approximately 11.5% from approximately 10.5% in 2005. Under the unfavourable business environment for whole commercial vehicles, the Dongfeng Motor Group adopted a number of measures to boost sales and managed to get the Dongfeng Motor Group's whole commercial vehicles business back on the track of growth.

## OTHER INCOME

During the year, the total other income of the Group was approximately RMB736 million, representing a decrease of approximately RMB271 million when compared with approximately RMB1,007 million in 2005. The decrease in other income was mainly attributable to a decrease in grants by RMB293 million received from the government for the purpose of supporting the development of automotive technologies and automobile projects.

## SELLING AND DISTRIBUTION COSTS

During the year, the selling and distribution costs of the Group amounted to approximately RMB2,157 million, representing an increase of approximately RMB419 million when compared with approximately RMB1,738 million in 2005. This was due to higher transportation costs resulting from increased sales volume of vehicles of the Dongfeng Motor Group as well as higher advertising and exhibition costs and market expansion expenses arising from the marketing of several new models.

During the year, the sales and distribution costs of the Group as a percentage of sales revenue increased slightly by approximately 0.3% points to approximately 4.5%, up from approximately 4.2% in 2005, reflecting an effective control over the sales and distribution costs of the Dongfeng Motor Group in spite of an increase in the sale volume of vehicles and the marketing of a number of new models.

## ADMINISTRATIVE EXPENSES

During the year, the total administrative expenses of the Group amounted to approximately RMB2,219 million, representing an increase of approximately RMB291 million when compared with approximately RMB1,928 million in 2005. This was due to the increased business volume. During the year, the administrative expenses of the Group as a percentage of sales revenue remained at the 2005 level of approximately 4.6%, reflecting administrative expenses of the Group under control.

## OTHER EXPENSES

During the year, other expenses of the Group was approximately RMB1,285 million, representing an increase of approximately RMB518 million when compared with approximately RMB767 million in 2005. This was mainly due to (1) research and development costs increased by approximately RMB186 million or 25.9% to approximately RMB905 million from approximately RMB719 million in 2005, as the Dongfeng Motor Group made greater investments in research and development; and (2) the Group recorded an exchange gain of approximately RMB9 million during the year while there was an exchange gain of approximately RMB252 million in 2005. Hence, an increase of RMB243 million of other expenses was recorded for the year. The exchange gain recorded in 2005 was due to the weakening of EURO, which was beneficial to the EURO loans of a jointly-controlled entity of the Company.

## LOSS ON DILUTION OF INTERESTS IN JOINTLY-CONTROLLED ENTITIES

During the year, the Group completed share reform schemes for two subsidiaries of a jointly-controlled entity, incurring one-time expenses of approximately RMB252 million. The shareholdings of these two listed companies indirectly held by the Company obtained the tradable right. The details are set out below:

(1) Dongfeng Automobile Co., Ltd ("DFAC"), a subsidiary of Dongfeng Motor Co., Ltd., a jointly-controlled entity of the Company, approved a share reform scheme in its shareholders' meeting on 30 October 2006. With the aggregate number of share capital of DFAC (2,000,000,000 shares) remained unchanged, Dongfeng Motor Co., Ltd granted shares to all tradeable shareholders whose names appeared on the register of members at a registration date specified by the share reform scheme according to their respective shareholdings on the basis of offering 3.3 shares for every 10 tradeable shares held. A total of 198,000,000 shares were transferred. The net book value of the consideration shares amounting to approximately RMB234 million attributable to the Group was recorded as an one-time expense.

(2) Dongfeng Electronics Technology Co., Ltd. ("DFTC"), a subsidiary of Dongfeng Motor Co., Ltd., approved a share reform scheme in its shareholders' meeting on 20 December 2006. With the aggregate number of share capital of DFTC (313,560,000 shares) remained unchanged, Dongfeng Motor Co., Ltd granted shares to all tradeable shareholders whose names appeared on the register of members at a registration date specified by the share reform scheme according to their respective shareholdings on the basis offering 4 shares for every 10 tradeable shares held. A total of 31,356,000 shares were transferred. The net book value of the consideration shares amounting to approximately RMB18 million attributable to the Group was recorded as an one-time expense.

## STAFF COSTS

During the year, the staff costs of the Group amounted to approximately RMB2,234 million, representing an increase of approximately RMB212 million when compared with approximately RMB2,022 million in 2005. It was because the increase in the sales volume of vehicles brought about a higher demand for labour and a general rise in salaries. In addition, the Group adopted a plan of stock appreciation rights as incentives to its senior management, and the amortised expenses during the year were RMB36 million.

## DEPRECIATION CHARGES

With a view to expanding its business, the Group made greater investments in properties, plant and equipment. During the year, the Group's depreciation charges amounted to approximately RMB1,479 million, representing an increase of approximately RMB173 million when compared with approximately RMB1,306 million in 2005.

## FINANCE COSTS

During the year, the finance costs of the Group amounted to approximately RMB411 million, representing a decrease of approximately RMB67 million when compared with approximately RMB478 million in 2005. Such a decrease is mainly attributable to the bank loans obtained in 2005 for financing the repurchase of shareholdings held by asset management companies being fully repaid within a month after the listing with the proceeds therefrom.

## INCOME TAX

The income tax expenses of the Group during the year amounted to approximately RMB428 million, representing a decrease of approximately RMB46 million when compared with approximately RMB474 million in 2005. The effective tax rate decreased to 16.0% from 21.3% in 2005. The decrease in income tax expenses was mainly due to the prior year's tax losses of the Company and one of jointly-controlled entities of the Company, which partly offseted the income tax payable and the decrease in deferred taxation due to the receipt of dividends from subsidiaries of the Dongfeng Motor Group during the year.

## NET PROFIT

Based on the above reasons, the net profit of the Group increased by approximately RMB480 million or 30.0% to approximately RMB2,081 million from approximately RMB1,601 million in 2005.

In 2006, after excluding the one-time expenses of approximately RMB252 million arising from the share reform schemes for DFAC and DFTC, which their respective shares listed in A share market in Mainland China, the adjusted net profit of the Group amounted to approximately RMB2,333 million, representing an increase of approximately 45.7% over the net profit in 2005.

## DIVIDENDS

The board of directors recommends to distribute a dividend of RMB4 cents per share in respect of the earnings in 2006.

## LIQUIDITY AND SOURCES OF CAPITAL

The Group raises funds through operations, bank loans and listing of shares to meet its working capital requirements. The funds raised by the Group are mainly used for operating activities, capital expenditure and repayment of short and long term loans.

| | **2006** | 2005 |
|---|---|---|
| | ***RMB million*** | *RMB million* |
| Net increase in cash flows generated from operating activities | **4,561** | 4,322 |
| Net decrease in cash flows generated from investing activities | **(3,930)** | (4,269) |
| Net increase/(decrease) in cash flows generated from financing activities | **(558)** | 1,055 |
| Net increase in cash and cash equivalents | **73** | 1,108 |

During the year, net cash inflows of the Group from operating activities amounted to approximately RMB4,561 million. This principally represents: (1) profit before tax amounting to approximately RMB2,679 million; (2) an increase of approximately RMB2,488 million in trade receivables, bills receivable and prepayments, deposits and other receivables; (3) an increase of approximately RMB4,077 million in trade, bills and other payables and accrued liabilities; (4) depreciation and impairment of approximately RMB1,531 million; and (5) a decrease of approximately RMB877 million in inventories.

During the year, net cash used in investing activities of the Group amounted to approximately RMB3,930 million. This is mainly attributable to the purchase of property, plant and equipment to the value of approximately RMB2,787 million, generally relating to the expansion of capacity and development of new products. During the year, the above outlays together with an increase of approximately RMB25 million in unsecured time deposits was partly offset by proceeds of approximately RMB87 million from the disposal of obsolete property, plant and equipment.

During the year, net cash outflow from financing activities of the Group amounted to approximately RMB558 million, mainly reflecting the offsetting of borrowings of approximately RMB11,894 million by repayment of borrowings of approximately RMB12,039 million.

During the year, the increase in cash and cash equivalents (excluding the time deposits with original maturity of three months or more) of the Group amounted to approximately RMB73 million. As at 31 December 2006, cash and cash equivalents of the Group amounted to approximately RMB5,659 million, and cash and bank balances (including the time deposits with original maturity of three months or more) amounted to approximately RMB7,437 million.

As at 31 December 2006, the Group's gearing ratio, measured on the basis of total borrowings as a percentage of total shareholders' equity is approximately 56.0%, representing an improvement form the 2005 level of 66.8%. On 12 December 2006, the Group completed the issue of the first tranche of its short term debentures with an aggregate face value of RMB1,900 million, and the term of maturity was one year. All the proceeds were used to repay the short-term bank borrowings. The successful issue of the short term debentures ear-marked a more diversified capital structure of the Group.

In 2006, the Group's turnover days of inventory was 54 days, which was almost equivalent to 55 days in 2005, reflecting the Dongfeng Motor Group's prudent inventory management.

The Group's turnover days of account receivable (including bills receivable) increased to 56 days from 44 days in 2005, and the turnover days of account receivable (excluding bills receivable) decreased slightly to 12 days from 13 days in 2005, which was mainly due to the Dongfeng Motor Group's strengthening its collection management of account receivable in 2006. The turnover days of bills receivable increased to 44 days from 31 days in 2005, as a result of the Dongfeng Motor Group using promissory notes from trustworthy banks for facilitating transactions. The Dongfeng Motor Group adopts stringent polices for the management of bills receivable and only accepts applications by clients with credibility, while the credit risks related to bank promissory notes are assumed by the clients' banks.

## MAJOR ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES, JOINTLY-CONTROLLED ENTITIES AND ASSOCIATES

There were no major acquisitions or disposals of subsidiaries, jointly-controlled entities and associates by the Company for the year ended 31 December 2006.

## EMPLOYEES AND REMUNERATION POLICIES

As at 31 December 2006, the Dongfeng Motor Group had a total of 88,530 full-time employees. The numbers of employees in various divisions and their percentage of the total number of employees are as follows:

| Division | Employees | Percentage of total |
|---|---|---|
| Manufacturing | 54,260 | 61.29% |
| Engineering and technology | 10,392 | 11.74% |
| Management | 17,020 | 19.22% |
| Services | 6,858 | 7.75% |
| Total | 88,530 | 100.00% |

The remuneration package of the Group's employees includes salary, bonuses and allowances. The Group has joined the social insurance payment programme organised by the Dongfeng Automobile Social Insurance Association. In accordance with the relevant national and local laws and regulations on labour and social welfare, each member of the Group is required to pay in respect of each of its relevant employees a monthly social insurance premium covering pension insurance, medical insurance, unemployment insurance, occupational injury insurance and insurance for maternity leave.

The Group endeavours to provide trainings for its employees. The scope of the completed and on-going training programs includes management skills and technology training, overseas exchange programs and other courses. The Group also encourages its employees to engage in self-learning programs by awarding scholarships.

The Stock Appreciation Rights ("SARs") are granted to members of the Board of Directors and the supervisory committee (excluding independent non-executive directors and independent supervisors), senior management, heads of business departments of the Company, directors and senior management of the JCEs appointed by the Company, as well as other key employees. The Board of Directors or its remuneration committee is authorized to determine which other key employees are eligible for the SARs.

## PURCHASE, SALE OR REDEMPTION OF THE LISTED SECURITIES OF THE COMPANY

Neither the Company, its subsidiaries nor its jointly-controlled entities has purchased, sold or redeemed any of the Company's listed securities during the year ended 31 December 2006.

## CORPORATE GOVERNANCE

The Company has throughout the year ended 31 December 2006 fully complied with the Code Provisions of the Code of Corporate Governance Practices as set out in Appendix 14 of the Rules Governing the Listing of Securities of The Stock Exchange Hong Kong Limited.

## REVIEW OF THE ACCOUNTS

The audit committee of the Company has reviewed with the management of the Company, the accounting principles and practices accepted by the Group and has discussed with the Directors matters concerning internal Controls and financial reporting of the Company, including a review of the results of the Group for the year ended 31 December 2006.

## CLOSURE OF REGISTER OF MEMBERS

In order to determine the name list of shareholders who are entitled to attend the annual general meeting, the register of members of the Company will be closed from Friday, 18 May 2007 to Monday, 18 June 2007, both days inclusive, during which period, no registration of shareholders and no transfers of shares will be effected. In order to qualify to attend and vote at the annual general meeting, holders of H shares whose transfers have not been registered shall deposit the transfer documents together with the relevant share certificates at the H share registrar of the Company, Computershare Hong Kong Investor Services Limited, at Room 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong at or before 4:00 pm on Thursday, 17 May 2007.

## BOARD OF DIRECTORS

As at the date of this announcement, the directors of the Company are Mr. Xu Ping, Mr. Liu Zhangmin, Mr. Zhou Wenjie, Mr. Li Shaozhu, Mr. Fan Zhong as executive directors, Mr. Tong Dongcheng, Mr. Ouyang Jie, Mr. Liu Weidong, Mr. Zhu Fushou as non-executive directors, and Mr. Sun Shuyi, Mr. Ng Lin-fung, Mr. Yang Xianzu as independent non-executive directors.

## SUPERVISORY COMMITTEE

As at the date of this announcement, the supervisors of the Company are Mr. Ye Huicheng, Mr. Zhou Qiang, Mr. Ren Yong, Mr. Liu Yuhe, Mr. Li Chunrong and Mr. Kang Li as supervisors, and Mr. Wen Shiyang and Mr. Deng Mingran as independent supervisors.

By order of the Board
**Xu Ping**
*Chairman*

Wuhan, the PRC
18 April 2007

* *For identification purposes only*

*Please also refer to the published version of this announcement in* ***South China Morning Post.***