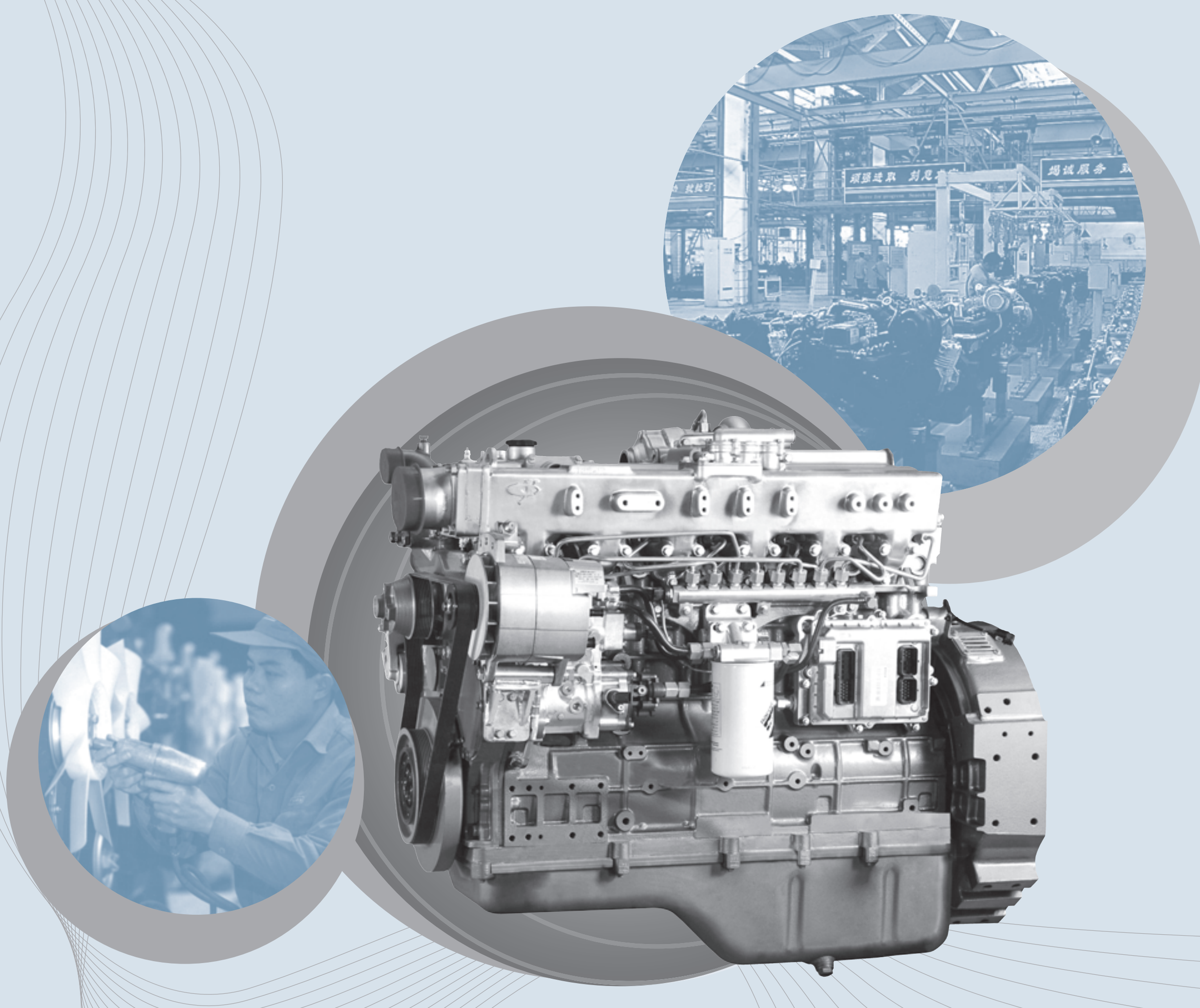
China Yuchai International Limited



Annual Report 2006

Contents

The Yuchai Spirit

玉柴动力的核心理念是绿色发展，和谐共赢、
打造玉柴世界知名品牌，
成就大型跨国企业集团的企业愿景，
建设高素质的干部队伍，打造创造性的劳动群体的人才观，
引领企业追求卓越，享有优良的社会美誉度和公众诚信度。

Yuchai's core ideals are to:

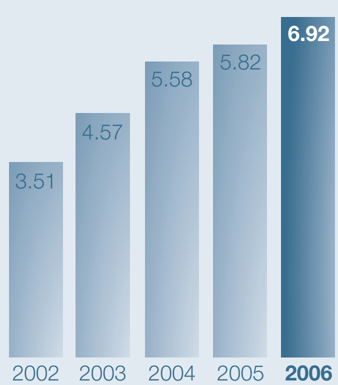
- Promote green development, harmonious partnership and mutual benefits
- Establish Yuchai as an international brand and propel Yuchai into the multinational status
- Develop caring professional workforce with technical excellence and creativity
- Lead in the pursuit of business excellence, responsible corporate citizenship and respectable public integrity


Moving into infinite growth.

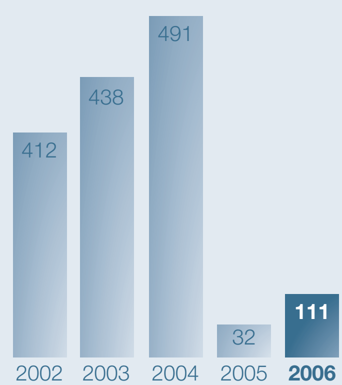
Five-Year Financial Highlights

	2006	2005	2004	2003	2002
	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000
Net revenue	**6,920,528**	5,816,740	5,582,095	4,569,950	3,513,047
Net income	**111,284**	(32,291)	491,397	438,182	412,433
Basic and diluted earnings per share	**2.99**	Rmb (0.89)	Rmb 13.90	Rmb 12.40	Rmb 11.67
Weighted average number of shares	**37,267,673**	36,459,635	35,340,000	35,340,000	35,340,000
	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000
Total assets	**7,961,387**	6,679,630	5,384,248	4,033,632	3,985,459
Stockholders' equity	**2,728,399**	2,566,263	2,483,084	1,991,687	2,161,903

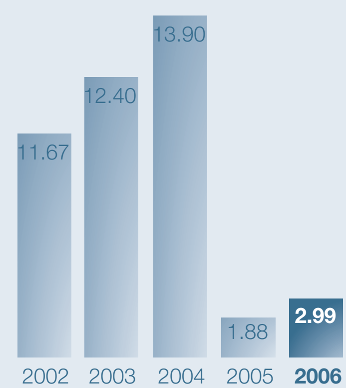
Net Revenue
(in Rmb billions)



Net Income
(in Rmb millions)



Basic and Diluted Earnings Per Share *(in Rmb)*



Corporate Background

China Yuchai International Limited ("CYI") is a Bermuda holding company established on April 29, 1993 to own a controlling interest in Guangxi Yuchai Machinery Company Limited ("Yuchai"). CYI currently own, through six of its wholly-owned subsidiaries, 76.4% of the outstanding shares of Yuchai. It operates as an exempted company limited by shares under The Companies Act 1981 of Bermuda. On March 7, 2008, CYI registered a branch office in Singapore and has its principal operating office located at 16 Raffles Quay #39-01A, Hong Leong Building, Singapore 048581.

CYI is controlled by Hong Leong Asia Ltd ("HLA") which indirectly holds 21.2% of the outstanding ordinary shares as well as one special share of CYI. The common stock of CYI is traded on the New York Stock Exchange under the symbol "CYD".

In February 2005, the Board of Directors of CYI announced its approval of the implementation of a business expansion and diversification plan. As a result, CYI acquired a 36.6% indirect interest in Thakral Corporation Ltd ("TCL") and 45.4% indirect interest in HLG Enterprise Limited ("HLGE") respectively as at 31 December 2006.

HLGE and TCL are each listed on the Singapore Exchange.

Yuchai is the principal operating subsidiary of CYI and it is one of the largest medium-duty diesel engine manufacturers in China. Yuchai is located in Yulin City, Guangxi Zhuang Autonomous Region in southern China. Yuchai produces and provides a comprehensive range of products from light-duty diesel engines to heavy-duty diesel engines, parts and diesel-powered generators to meet the needs of different sectors. Indeed, Yuchai has a strong reputation among vehicle manufacturers and customers for the performance and reliability of its products as well as its after-sales customer service.

Light-Duty Engines

Yuchai's light-duty engines are called the "4-cylinder series" which are primarily produced for light vans, minibuses and small trucks.

In 2006, Yuchai sold approximately 149,000 light duty engines, which represents a growth of 18.5% over the previous year.

Medium-Duty Engines

Yuchai's principal products are its medium-duty 6105 and 6108 diesel engines, used primarily in medium-duty vehicles weighing between five to seven tons. An approximate 113,000 units of 6105 and 6108 diesel engines were sold in 2006, a decline of approximately 5% over 2005. The sales declined in 2006 primarily due to the shift in demand by customers to the light-duty engines arising from the tightening of credit by banks in China. The medium-duty engines are more expensive than the light-duty engines.

Heavy-Duty Engines

In 2006, Yuchai sold approximately 22,330 units of the 6112 and the new super heavy-duty 6L/6M diesel engines. There is a higher level of acceptance by customers for the heavy-duty engines. However, due to the tight credit lending policies by banks in China, demand for new trucks and buses had been adversely affected. Accordingly, Yuchai had taken steps to increase marketing efforts and since then, sales of the 6L and 6M diesel engines have enjoyed steady growth due to their quality, market suitability and competitive cost.

Looking forward

The outlook is very positive for diesel engines in China, as they are not only ideal for heavy vehicles, but have growing applications for smaller vehicles as well. The demand for trucks and especially municipal buses continues as the population of many cities continues to grow. With the need for fuel efficiency and emission control, diesel engines are becoming a rising answer to these problems.

Yuchai has a strong brand name in China with an extensive sales and marketing network. As a major manufacturer of diesel engines in China with a significant market share, it is well positioned to meet the growing demand for diesel engines.

公司背景

中国玉柴国际有限公司

中国玉柴国际有限公司（“CYI”）是一家百慕达控股公司，成立于1993年4月29日，以拥有广西玉柴机器有限公司（简称“玉柴”）的控制权益。目前，CYI通过其六间全资子公司，持有玉柴76.4 %的已发行股票。在百慕达1981公司法令下，它是一间豁免股份有限公司。2008年3月7日，CYI在新加坡注册了分公司，其主要营业公司坐落于莱佛士码头16号，#39-01A，丰隆大厦，新加坡048581。

CYI是由丰隆亚洲有限公司（“HLA”）操控的，他们间接持有CYI的21.2%的已发行普通股以及一个特别股份。CYI的普通股票在纽约证券交易所上市交易，股票代号为“CYD”。

在2005年2月，CYI董事会宣布批准实施业务扩充和多元化计划。因此，截止2006年12月31日，CYI分别拥有了Thakral有限公司（“TCL”） 36.6% 的间接权益，以及HLG企业有限公司(“HLGE”) 45.4% 的间接权益

HLGE和TCL均有在新加坡交易所上市。

玉柴是CYI的主要营业子公司，也是中国中级柴油发动机最大制造商之一。玉柴位于中国南部广西壮族自治区的榆林市。它生产和提供全面的产品，从轻级柴油发动机到重级柴油发动机、零件和柴油驱动发电机，以应付不同市场的需求。因其产品高效可靠，销后服务良好，玉柴在车辆制造商和顾客当中享有良好声誉，

轻型引擎

玉柴的轻型引擎被称为“4缸系列”，主要提供给轻型货车、轻型客车和小货车。

在2006年，玉柴销售了大约149,000个轻型发动机，代表比前一年增长了18.5%。

中型引擎

玉柴的主要产品是中型6105和6108柴油发动机，主要用于重5到7吨的中型车辆中。在2006年，玉柴出售了大约113,000个单位的6105和6108柴油引擎，比2005年下降了约5%。销售量在2006年下降，主要是由于中国国内的银行收紧信贷而导致客户需求转向了小型引擎。中型引擎比轻型引擎要贵一些。

重型引擎

在2006年，玉柴销售了大约22,330个单位的6112和新的超级重型6L/6M的柴油发动。虽然客户对重型发动机的接受度更高了，不过，由于中国的银行政策信贷紧缩，对卡车和公共汽车的需求也受到了不利影响。玉柴也增加了营销方面的投资，之后，其6L和6M柴油发动机的销售额因为品质好、适合市场和成本有竞争力而增长稳定。

展望

柴油发动机在中国市场的前景非常好，因为它不仅适合重型车辆，对较小车辆也逐渐能适用。随着许多城市人口继续增加，对卡车尤其市营公共汽车的需求也持需增长。柴油发动机逐渐成为解决提高柴油效率和排放控制的方法。

玉柴在中国品牌良好，拥有广大的销售和营销网络。作为中国柴油发动机主要制造商，而且有相当大的市场占有率，它完全能应付对柴油发动机的持续增长需求。

President's Statement

The 2006 year was exciting for the Chinese auto industry as the total industry unit production and industry sales growth were 31% and 29%, respectively. Chinese commercial vehicles posted a steady 15% and 14% year-on-year growth in unit production and sales, and diesel engines outperformed the market with a strong 22% and 20% year-on-year growth in unit production and sales, respectively. Our subsidiary, Guangxi Yuchai Machinery Company Limited ("Yuchai"), for the sixth year in a row was rated No.1 in sales by the China Association of Automobile Manufacturers. It outperformed the diesel engine industry with a robust 23.2% growth in sales to approximately 284,000 units in 2006 and 16% higher unit production in 2006 compared with a year ago.

The Company's net revenues grew by 19% to RMB 6.921 billion (US$ 1.009 billion) in 2006 from RMB 5.817 billion in 2005. Net revenues grew as the Chinese economy continued to expand with both the infrastructure build out and highway network sustaining high growth, as well as the rising urban population creating more demand for trucks and buses. The central government's policies favor diesel engines for larger vehicles and the market is increasingly recognizing their stronger power output, greater fuel efficiency and high reliability. However, we are very excited to witness the rapid growth in the small- to mid-size diesel engine market, as OEMs are increasingly adopting diesel engines as a key power source.

Gross profit in 2006 was RMB 1.272 billion (US$ 185.5 million) compared with RMB 1.143 billion a year ago. Our gross margin went from 19.7% in 2005 to 18.4% in 2006. During the year, competition, elevated raw material costs and a change in the product sales mix affected Yuchai's gross profit and margin. Light-duty, medium-duty and heavy-duty diesel engine segments experienced increases in 2006 led by a 43.0% gain in our light-duty and industrial diesel engines. Our heavy-duty engines grew by 6.78% for the year. We introduced the 4F light-duty diesel engine into the commercial market in 2006 which added to our sales of light-duty diesel engines. Concerns over fuel efficiency and the government's tightening of bank credit drove purchases of the highly efficient, but relatively less expensive and less profitable light-duty models. Similar to the European market, small commercial vehicle producers in China are increasingly using diesel engines. This trend paves the way for the potential adoption of diesel engines into the passenger vehicle sector in China in the future.

We continue to invest in research and development, as we strongly believed that the future competitiveness of an independent engine producer lies in its technology leadership. Technology is one of the critical elements in developing ongoing industry leadership to enhance growth and therefore shareholder value. For that reason, our R&D expenses rose 35.4% to RMB 167.7 million (US$24.4 million) from RMB 123.8 million in 2005. The increase in R&D expenses was mainly related to Yuchai's accelerated development of diesel engines compliant with Euro III and Euro IV environmental emission standards. One of CYI's and Yuchai's strategies is to be the technology leader to meet the evolving stringent environmental standards as directed by the Chinese government. The Chinese people will benefit from reduced emissions from diesel engines even as the automotive market continues to expand. Being among the first to meet this emission initiative will provide CYI with a competitive advantage over other Chinese diesel engine manufacturers who lack the ability to quickly implement changes to meet these standards. By achieving these emission standards, new export markets that require these emission levels may open to us.

We continued to manage our selling, general and administrative expenses (SG&A) as better controlled transportation expenses and a reduced provision for doubtful accounts were experienced in 2006. SG&A of RMB 801.8 million (US$ 116.9 million) represented 11.6% of sales in 2006 compared with RMB 793.2 million, or 13.6% of sales in 2005.

Our operating income in 2006 increased significantly to RMB 304.5 million (US$44.4 million) from RMB 26.0 million in 2005. The 2005 operating income was impacted by a one-time provision for uncollectible accounts of RMB 203 million due to a debt owed by Yuchai Marketing and Logistics Company Limited (YMLC) that was deemed irrecoverable.

Interest expense rose from RMB 70.5 million in 2005 to RMB 117.5 million (US$17.1 million) in 2006. The Company utilized bank loans to accommodate the higher working capital necessary to fund its growth, and for strategic investments in both HLG Enterprise Limited (HLGE) and Thakral Corporation Ltd. (TCL). HLGE's business is in investments especially in real estate and the hospitality industries in China.

We achieved net income for 2006 of RMB 111.3 million, or RMB 2.99 per diluted share (US$ 16.2 million, or US$0.44 per diluted per share), compared with an amended net loss of RMB 32.3 million, or RMB 0.89 per diluted share in 2005.

In 2006, we expanded our diversification plan. We acquired an initial 29.13% ownership of HLG Enterprises Limited (HLGE), formerly known as LKN, through an investment of bonds, redeemable convertible preference shares and ordinary shares. Later in 2006, we further invested in HLGE to bring our ownership to 45.4% of the shares outstanding. Also, during 2006, we increased our ownership position in Thakral Corporation (TCL) to 36.6% through the investment and conversion of convertible bonds.

Net trade accounts receivable rose as sales increased and net inventories declined due to more efficient inventory controls during 2006. Bank loan balances were higher at the end of 2006 as bank debt was utilized to support our sales growth, the capital expansion of our production facilities and to further our strategic initiatives. In December 2006, CYI paid an interim cash dividend of US$0.02 per share for the 2006 year.

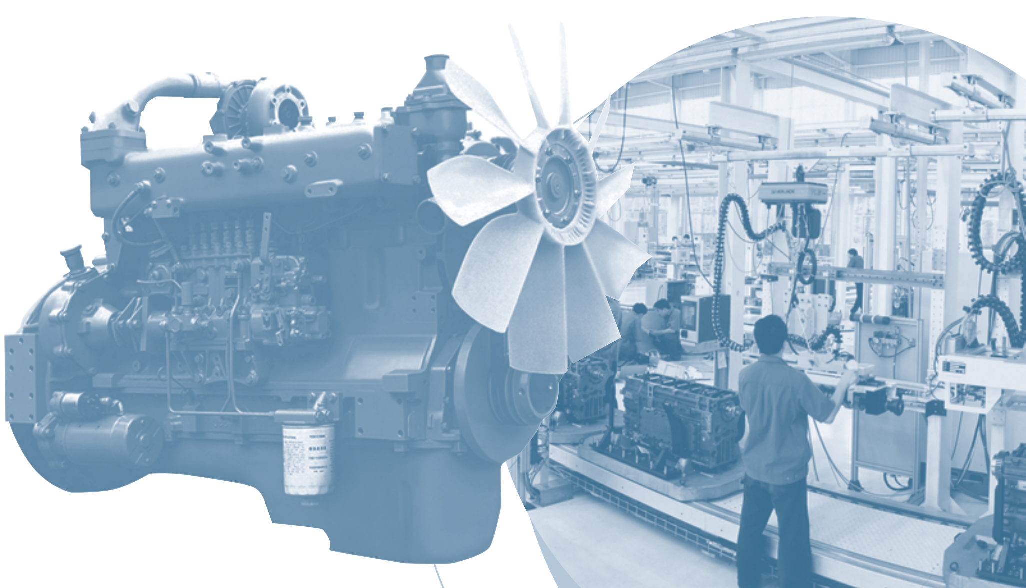
I wish to thank our shareholders for their patience in receiving this 2006 annual report, which is being presented after an inquiry and investigation into accounting errors at our subsidiary, Guangxi Yuchai Machinery Company Limited (Yuchai). The restatement to the year 2005 financial statements has also affected certain starting balances in 2006.

The outlook remains very positive for diesel engines in China, as they are not only ideal for heavy vehicles, but have growing applications for smaller vehicles as well. The demand for trucks and especially municipal buses continues as the population of many cities continues to expand. With the mounting need for fuel efficiency and emission control, diesel engines are becoming a rising answer to these issues.

On behalf of the management team and Board of Directors, let me assure you that we are working diligently to complete the 2007 financial results and our 2008 interim financial results for public release. We look forward to continued growth in 2008, as we build value for our shareholders.

Teo Tong Kooi
President
17 July 08

US$1.00 = RMB6.8591 as on December 31, 2006



主席报告

2006年是令人兴奋的一年，在这一年里，中国汽车工业的总单位生产量和销售量分别增长了31%和29%。中国商用车辆比去年同期有稳步的增长，在单位的生产和销售量上分别增长了15%和14%。柴油引擎在单位的生产和销售量上比去年同期分别增长了22%和20%。我们的附属公司广西玉柴机器股份有限公司（玉柴）已经连续6年被中国汽车制造商协会评选为销售量第一的企业，表现远优于同行业，单位销售量以23.2%的稳健速度增长到约28.4万个单位，在2006年的单位生产量与上年相比高出16%。

公司的净营业收入从2005年的58.17亿人民币增至2006年的69.21亿人民币（10.09亿美元），增长率为19%。这与中国经济的持续扩张成长、加上基础设施建设和日益扩展的公路交通网络、以及越来越多的城市人口对卡车和公共汽车的需求是分不开的。虽然中央政府的政策鼓励大型车辆使用柴油发动机，而市场也开始意识到使用柴油发动机更有马力、更省油也更可靠，然而我们却也很高兴地见到小型到中等规模的引擎市场同时的在稳健迅速的增长，这是因为原始设备制造商也越来越多地采用柴油机作为其产品的主要源动力。

我们在2006年取得的毛利是人民币是12.72（1.855亿美元），而之前一年却只取得人民币11.43亿。然而毛利率却是从2005年的19.7%滑落到2006的18.4%。在这一年内我们面对的竞争、原材料成本的攀升及产品销售组合的变化等等都影响着玉柴的毛利润和利率。在2006年，轻型、中型和重型柴油发动机的销售都有增长。其中，轻型柴油发动机和工业发动机的销售额的增长是43.3%。重型发动机那年销售额的增长是6.78%.我们在2006年将4F轻型柴油发动机引进商业市场并因此提高了轻型柴油发动机的销售额。这是市场对燃油费用的关注及政府紧收银行信贷的政策而导致人们更偏向购买这些高效率但相对费用较低、利润也较低的轻型号产品。与欧洲市场类似的是，中国的小型商用汽车生产商也正倾向于采用柴油发动机。这对未来中国客运车采用柴油发动机的潜能性预先铺垫了道路。

我们持续投资于研究和发展。因我们坚信，未来的竞争力对一个独立的发动机制造商而言就取决于它的技术领导地位。技术是发展和保持行业领导地位的一个关键因素，它提高企业增长，也提升了股份价值。出于这个原因，我们的研发费用由2005年的1.238亿人民币（1530万美元）增加到1.677亿人民币（2440万美元），增长了35.4%。研发费用的增加主要用在玉柴加速发展符合欧盟三期及四期环境废气排放标准的柴油发动机等相关的方面。CYI和玉柴的战略之一就是要成为技术上的领先者，以满足中国政府不断变化和严格化的环境标准。哪怕汽车市场不断扩大，柴油引擎的推广也会有利于减少排放量，有益于中国人民的健康。作为能满足排放标准的前锋制造商之一的CYI，我们比其他无能力去迅速满足这些达标要求的中国柴油发动机制造商有更大的竞争优势。达标也能为我们迎来更多更新的出口市场机会。

在2006年里，我们减少了可疑帐户并更好地控制运输费用使我们能有效地持续控制我们的销售开支和一般性及行政开支。与2005年的占总销售额13.6%的7.932亿人民币相比，2006年里的销售开支和一般性及行政开支为801.8亿人民币（1.169亿美元），占总销售额的11.6%。

我们的营业收入在2006年有显著上升，由人民币2600万元升到了人民币3.045亿（4440万美元）。由于无法收回2.03亿人民币账款的一次性支出，使得2005年的营业收入受到了影响，这笔债务是由玉柴营销及物流有限公司（YMLC）欠下，并被视为不可回收的欠款。

在2006年，利息开支由人民币7050万上升至人民币1.175亿（1715万美元）。公司利用银行贷款支撑发展所需的更高的周转资金，以及在HLG企业有限公司（HLGE）和Thakral有限公司（TCL集团）上的战略性投资。HLGE的主要业务是投资，尤其是中国的房地产和宾馆行业。

2006年里，我们所取得的净收入为1.113亿人民币，相当于每股2.99元人民币（1620万美元，相当于每股0.44美元），而在2005年里，经修订后的净亏损为人民币3230万元，相当于每股0.89元人民币。

在2006年，我们扩大了我们的多元化计划。通过投资债券、可赎回可转换优先股和普通股，我们获得了HLG企业有限公司（HLGE，以前称为LKN）的29.13%所有权。之后同年，我们增加对HLGE的投资，将所有权提高到45.4%的已发行股票。同时在2006年，我们通过转换可换股债券增加了我们在Thakral公司（TCL集团）的所有权，达到36.6%。

由于在2006年销售的增加以及更有效的库存控制而产生的净库存的下降，净贸易可收账款有所增加。因为银行的债务被用作支持我们的增长和进一步落实我们的战略举措，所以银行贷款余额在2006年底较高。在2006年12月，CYI为2006年派发了每股0.02美元的中期现金股息。

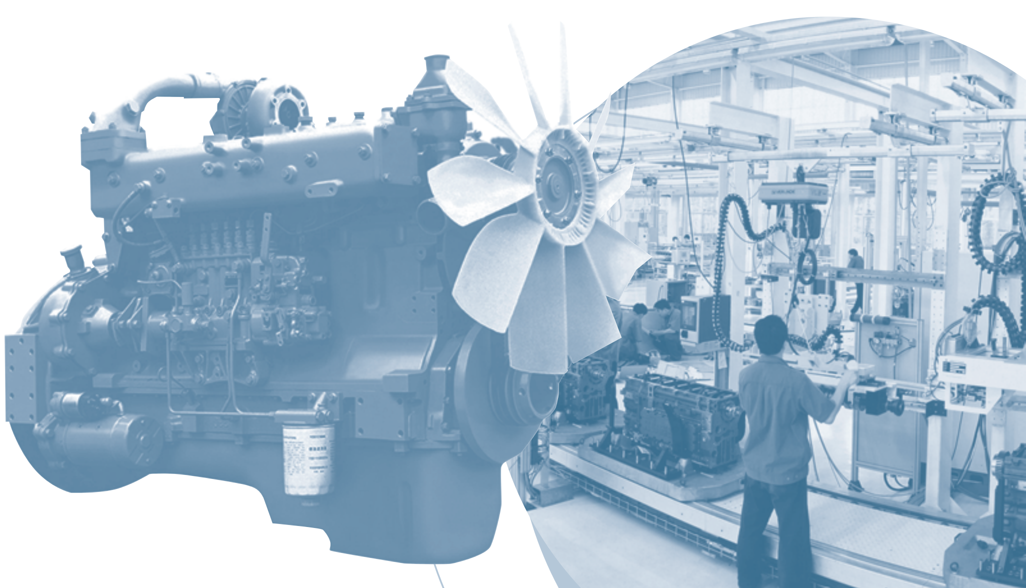
我要感谢股东们耐心的等候这份2006年度报告。经过长时间的审查和调查我们的附属公司广西玉柴机器有限公司（玉柴）里发生的会计差错之后，这份报告终于出炉了。2005年财政报表的修改也影响了2006年的某些期初余额。

柴油发动机在中国的前景仍然非常乐观，因为它不仅对重型车辆来说是理想的，而且小型车辆也越来越多地在运用柴油机。随着许多城市的人口持续增长，对卡车和尤其是巴士的需求也在持续增长。燃油效率和排放控制的需求使得柴油发动机成为解决这些问题的首选。

我仅代表整个管理团队和董事局向您们保证，我们正努力去进行完成2007年的财务报表及2008年的财务报表并会将结果早日给予公布。我们展望着2008年的持续地增长，让我们能为我们的股东们继续创造效益价值。

Teo Tong Kooi 主席
2008年7月17日

1美元=人民币6.8591于2006年12月31日



Corporate Governance

We are an exempted company incorporated in Bermuda and are subject to the laws of that jurisdiction. The legal framework in Bermuda which applies to exempted companies is flexible and allows an exempted company to comply with the corporate governance regime of the relevant jurisdiction in which the company operates or applicable listing standards. Under Bermuda law, members of a board of directors owe a fiduciary duty to the company to act in good faith in their dealings with or on behalf of the company and to exercise their powers and fulfill the duties of their office honestly. In addition, the Bermuda company legislation imposes a duty on directors and officers of an exempted company to act honestly and in good faith with a view to the best interests of the company and requires them to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. Bermuda legislation also imposes certain specific duties and obligations on companies and directors, both directly and indirectly, including duties and obligations with respect to matters such as (a) loans to directors and related persons; and (b) limits on indemnities for directors and officers. Bermuda law does not impose specific obligations in respect of corporate governance, such as those prescribed by NYSE listing standards, requiring a company to (i) appoint independent directors to their boards, (ii) hold regular meetings of non-management directors; (iii) establish audit, nominating and governance or compensation committees; (iv) have shareholders approve equity compensation plans; (v) adopt corporate governance guidelines; or (vi) adopt a code of business conduct and ethics.

We are also subject to the NYSE listing standards, although, because we are a foreign private issuer, those standards are considerably different from those applied to US companies. Under the NYSE rules, we need only (i) establish an independent audit committee that has specified responsibilities as described in the following table; (ii) provide prompt certification by our chief executive officer of any material non-compliance with any corporate governance rules; (iii) provide periodic written affirmations to the NYSE with respect to our corporate governance practices; and (iv) provide a brief description of significant differences between our corporate governance practices and those followed by US companies.

The following table compares the Company's principal corporate governance practices, which are in compliance with Bermuda law, to those required of US companies.

Standard for US Domestic Listed Companies	China Yuchai International Limited's Practice
Director Independence	
• A majority of the board must consist of independent directors.	• Three of our nine directors, Messrs. Neo Poh Kiat, Tan Aik-Leang and Matthew Richards are independent within the meaning of the NYSE standards.
Independence is defined by various criteria including the absence of a material relationship between director and the listed company. Directors who are employees, are immediate family of the chief executive officer or receive over $100,000 per year in direct compensation from the listed company are not independent. Directors who are employees of or otherwise affiliated through immediate family with the listed company's independent auditor are also not independent.	
• The non-management directors of each company must meet at regularly scheduled executive sessions without management.	• Our non-management directors do not meet periodically without management directors.
Audit Committee	
• Listed companies must have an audit committee that satisfies the requirements of Rule 10A-3 under the Exchange Act. The rule requires that the audit committee (i) be comprised entirely of independent directors; (ii) be directly responsible for the appointment, compensation, retention and oversight of the independent auditor; (iii) adopt procedures for the receipt and treatment of complaints with respect to accounting, internal accounting controls or auditing matters; (iv) be authorized to engage independent counsel and other advisors it deems necessary in performing its duties; and (v) be given sufficient funding by the company to compensate the independent auditors and other advisors as well as for the payment of ordinary administrative expenses incurred by the committee.	• Our audit committee meets the requirements of Rule 10A-3 under the Exchange Act.
• The audit committee must consist of at least three members, and each member meet the independence requirements of both the NYSE rules and Rule 10A-3 under the Exchange Act.	• Our audit committee currently consists of three members, each of whom meets the independence requirements of both the NYSE rules and Rule 10A-3 under the Exchange Act.
• The audit committee must have a written charter that addresses the committee's purpose and responsibilities.	• Our audit committee has a charter outlining the committee's purpose and responsibilities, which are similar in scope to those required of US companies.

Standard for US Domestic Listed Companies	China Yuchai International Limited's Practice
At a minimum, the committee's purpose must be to assist the board in the oversight of the integrity of the company's financial statements, the company's compliance with legal and regulatory requirements, the independent auditor's qualifications and independence and the performance of the company's internal audit function and independent auditors. The audit committee is also required to review the independent auditing firm's annual report describing the firm's internal quality control procedures, any material issues raised by the most recent internal quality control review or peer review of the firm, or by any recent governmental inquiry or investigation, and any steps taken to address such issues. The audit committee is also required to assess the auditor's independence by reviewing all relationships between the company and its auditor. It must establish the company's hiring guidelines for employees and former employees of the independent auditor. The committee must also discuss the company's annual audited financial statements and quarterly financial statements with management and the independent auditors, the company's earnings press releases, as well as financial information and earnings guidance provided to analysts and rating agencies, and policies with respect to risk assessment and risk management. It must also meet separately, periodically, with management, the internal auditors and the independent auditors.	
• Each listed company must disclose whether its board of directors has identified an Audit Committee Financial Expert, and if not the reasons why the board has not done so.	• The Board of Directors has identified Mr. Tan Aik-Leang as our Audit Committee Financial Expert.
• Each listed company must have an internal audit function.	• Our internal audit function is provided by Hong Leong Asia.
Compensation Committee	
• Listed companies must have a compensation committee composed entirely of independent board members as defined by the NYSE listing standards.	• Our compensation committee currently has three members, two of whom are independent within the meaning of the NYSE standards.
• The committee must have a written charter that addresses its purpose and responsibilities.	

Standard for US Domestic Listed Companies	China Yuchai International Limited's Practice
• These responsibilities include (i) reviewing and approving corporate goals and objectives relevant to CEO compensation; (ii) evaluating CEO performance and compensation in light of such goals and objectives for the CEO; (iii) based on such evaluation, reviewing and approving CEO compensation levels; (iv) recommending to the board non-CEO compensation, incentive compensation plans and equity-based plans; and (v) producing a report on executive compensation as required by the SEC to be included in the company's annual proxy statement or annual report. The committee must also conduct an annual performance self-evaluation.	• Our compensation committee reviews among other things the Company's general compensation structure, and reviews, recommends or approves executive appointments, compensation and benefits of directors and executive officers, subject to ratification by the Board of Directors, and supervises the administration of our employee benefit plans, if any.
Nominating/Corporate Governance Committee	
• Listed companies must have a nominating/corporate governance committee composed entirely of independent board members.	• We do not have a nominating/corporate governance committee. However, certain responsibilities of this committee are undertaken by our Compensation Committee, such as the review and approval of executive appointments and all other functions are performed by the Board of Directors.
• The committee must have a written charter that addresses its purpose and responsibilities, which include (i) identifying qualified individuals to become board member; (ii) selecting, or recommending that the board select, the director nominees for the next annual meeting of shareholders; (iii) developing and recommending to the board a set of corporate governance principles applicable to the company; (iv) overseeing the evaluation of the board and management; and (v) conducting an annual performance evaluation of the committee.	
Equity-Compensation Plans	
• Shareholders must be given the opportunity to vote on all equity-compensation plans and material revisions thereto, with limited exceptions.	• We intend to have our shareholders approve equity-compensation plans.
Corporate Governance Guidelines	
• Listed companies must adopt and disclose corporate governance guidelines.	• We have formally adopted various corporate governance guidelines, including Code of Business Conduct and Ethics (described below); Audit Committee Charter; Whistle-blowing Policy; Insider Trading Policy; and Disclosure Controls and Procedures.
Code of Business Conduct and Ethics	
• All listed companies, US and foreign, must adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers.	• We have adopted a Code of Business Conduct and Ethics Policy, a copy of which is available upon request from us. We intend to promptly disclose any waivers of the code for directors or executive officers.

Our China-Wide Presence

Guangxi Yuchai Machinery Company Limited
公司总部

Regional Sales Offices
玉柴办事处

Customer Service Stations
玉柴技术服务站

Management

Directors and Executive Officers of the Company

Our Board of Directors may consist of up to eleven members. As of May 30, 2008, there are nine members elected to and serving on our Board of Directors, with two vacancies. Pursuant to the rights afforded to the holder of the special share, Hong Leong Asia has designated Messrs. Teo Tong Kooi, Gan Khai Choon, Gao Jia Lin and Kwek Leng Peck as its nominees. Messrs. Yan Ping and Zhang Shi Yong are nominees of Coomber Investments Limited.

Our directors and executive officers are identified below.

Name(1)	Position	Year First Elected or Appointed Director or Officer
TEO Tong Kooi(2)(3)(6)	President and Director	2004
GAO Jia Lin(2)	Vice President and Director	1995
GAN Khai Choon(2)(6)	Director	1995
KWEK Leng Peck(2)(4)	Director	1994
NEO Poh Kiat(2)(4)(5)	Director	2005
TAN Aik-Leang(2)(5)	Director	2005
Matthew RICHARDS(4)(5)	Director	2006
YAN Ping(2)	Director	2007
ZHANG Shi Yong(2)	Director	2007
TAN Wan Hong(2)	Group General Manager	2008
HOH Weng Ming(3)	Chief Financial Officer	2008
FOO Shing Mei Deborah	General Counsel	2007
Ira Stuart OUTERBRIDGE III	Secretary	2001

(1) Mr. Raymond C.K. Ho ceased to be a director of CYI with effect from September 15, 2006 and resigned as a director of Yuchai on September 7, 2006. Mr. Wong Hong Ren resigned as a director of each of the Company and Yuchai with effect from July 5, 2007 and August 16, 2007, respectively. Mr. Philip Ting Sii Tien resigned as a director of each of the Company and Yuchai with effect from December 3, 2007 and March 28, 2008, respectively. Mr. Ting also resigned as the Chief Financial Officer of the Company with effect from November 15, 2007. Ms. Sheila Murugasu resigned as the General Counsel of the Company with effect from December 10, 2007. Mr. Ho Tuck Chuen was appointed as the Chief Financial Officer and Director of the Company with effect from November 15, 2007 and December 3, 2007, respectively. Mr. Ho subsequently resigned from both positions with effect from April 30, 2008.

(2) Also a Director of Yuchai.

(3) Also a Director/Alternate Director of TCL.

(4) Member of the Compensation Committee.

(5) Member of the Audit Committee.

(6) Also a Director of HLGE.

Financial Contents

Report of Independent Registered Public Accounting Firm

(Rmb and US$ amounts expressed in thousands, except per share data)

The Board of Directors and Shareholders
China Yuchai International Limited

We have audited the accompanying consolidated balance sheet of China Yuchai International Limited (the "Company") and subsidiaries as of December 31, 2006, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of China Yuchai International Limited and subsidiaries as of December 31, 2006, and the results of their operations and their cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

The accompanying consolidated financial statements as of and for the year ended December 31, 2006 have been translated into U.S. dollars for the convenience of the reader. We have audited the translation and, in our opinion, the consolidated financial statements expressed in Renminbi have been translated into U.S. dollars on the basis set forth in Note 3(i) to the consolidated financial statements.

/s/ KPMG

Singapore

July 17, 2008

Report of Independent Registered Public Accounting Firm

(Rmb and US$ amounts expressed in thousands, except per share data)

To the Board of Directors and Stockholders
China Yuchai International Limited

We have audited the accompanying consolidated balance sheet of China Yuchai International Limited (the "Company") and subsidiaries as of December 31, 2005, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for the years ended December 31, 2004 and 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of China Yuchai International Limited and subsidiaries as of December 31, 2005, and the results of their operations and their cash flows for the years ended December 31, 2004 and 2005, in conformity with U.S. generally accepted accounting principles.

As further described in Note 2(b) to the consolidated financial statements, the consolidated financial statements of the Company as of and for the year ended December 31, 2005 were restated for the correction of certain accounting errors.

As described in Note 5 to the consolidated financial statements, the Company recognized a provision for uncollectible loans to a related party in the amount of Rmb203 million as of December 31, 2005.

/s/ KPMG

Hong Kong

August 4, 2006, except as to Note 2(b) which is as of May 15, 2008

Consolidated Statements of Operations

for years ended December 31, 2004, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Note	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
		Years ended December 31,			
Revenues, net[(a)]	3(k), 27, 28, 33	5,582,095	5,816,740	6,920,528	1,008,956
Cost of goods sold[(a)]	4, 27	(4,006,886)	(4,673,357)	(5,648,407)	(823,491)
Gross profit		1,575,209	1,143,383	1,272,121	185,465
Research and development costs	3(m)	(136,960)	(123,793)	(167,653)	(24,442)
Selling, general and administrative expenses[(a)]	3(m), 4, 14, 27	(658,320)	(793,153)	(801,830)	(116,900)
Provision for uncollectible loans to a related party	5	—	(202,950)	—	—
Gain on transfer of land use rights to a related party	27	—	2,533	1,841	268
Operating income		779,929	26,020	304,479	44,391
Interest expense	6, 28	(31,757)	(70,527)	(117,491)	(17,129)
Equity in net losses of affiliates		—	(6,032)	(22,449)	(3,273)
Other income, net[(a)]	7, 27	5,682	25,449	38,856	5,665
Earnings/(loss) before income taxes and minority interests		753,854	(25,090)	203,395	29,654
Income taxes	8	(105,165)	(10,148)	(30,466)	(4,442)
Income/(loss) before minority interests		648,689	(35,238)	172,929	25,212
Minority interests in income/(loss) of consolidated subsidiaries		(157,292)	2,947	(61,645)	(8,987)
Net income/(loss)		491,397	(32,291)	111,284	16,225
Earnings/(loss) per common share					
Basic	3(l)	13.90	(0.89)	2.99	0.44
Diluted	3(l)	13.90	(0.89)	2.99	0.44
Weighted average number of shares					
Basic	3(l)	35,340,000	36,459,635	37,267,673	37,267,673
Diluted	3(l)	35,340,000	36,459,635	37,267,673	37,267,673

(a) Includes the following income and expenses resulting from transactions with related parties in addition to those indicated above (see Notes 5 and 27)

	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Revenues, net	4,537	7,646	86,652	12,633
Cost of goods sold	(250,549)	(417,816)	(592,535)	(86,387)
Selling, general and administrative expenses	(90,790)	(186,759)	(124,376)	(18,133)
Other income, net	—	11,922	10,512	1,533

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheets

as of December 31, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Note	As of December 31, 2005 Rmb	2006 Rmb	2006 US$
ASSETS				
Current assets				
Cash and cash equivalents	33(d)	736,195	745,933	108,751
Trade accounts receivable, net	9, 18(a)	1,178,853	1,480,918	215,906
Amounts due from related parties	10, 27	233,188	158,512	23,110
Loans to a related party, net	5	2,050	2,050	299
Loans to customers, net	11	7,904	11,486	1,675
Inventories	12	1,668,435	1,565,183	228,191
Prepaid expenses		138,322	93,977	13,700
Other receivables, net	13	135,652	140,069	20,421
Income taxes recoverable		46,054	10,750	1,567
Deferred income taxes	8	85,351	112,779	16,442
Total current assets		4,232,004	4,321,657	630,062
Property, plant and equipment, net	14	1,440,712	1,795,405	261,755
Construction in progress	15	456,752	288,559	42,070
Lease prepayments	16	69,328	124,944	18,216
Investments in affiliates	17	184,693	508,246	74,098
Other investments	17	6,355	640,192	93,335
Goodwill	3(n)	212,636	212,636	31,000
Deferred income taxes	8	77,150	69,718	10,164
Total assets		6,679,630	7,961,357	1,160,700
LIABILITIES, MINORITY INTERESTS AND STOCKHOLDERS' EQUITY				
Current liabilities				
Short-term bank loans	18(a)	812,835	1,009,134	147,123
Current installments of long-term bank loans	18(b)	100,000	—	—
Amount due to the holding company	27	4,301	3,226	470
Amounts due to related parties	10, 27	75,186	77,911	11,359
Trade accounts payable		1,800,443	2,132,798	310,944
Income taxes payable		4,208	1,789	261
Accrued expenses and other liabilities	20	611,707	639,350	93,212
Total current liabilities		3,408,680	3,864,208	563,369
Long-term bank loans, excluding current installments	18(b)	50,000	675,454	98,476
Total liabilities		3,458,680	4,539,662	661,845

Consolidated Balance Sheets

as of December 31, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Note	As of December 31, 2005 Rmb	2006 Rmb	2006 US$
Total liabilities brought forward		3,458,680	4,539,662	661,845
Minority interests		654,687	693,296	101,077
Stockholders' equity				
Common stock		31,945	31,945	4,657
Ordinary shares US$0.10 par value: authorized 100,000,000 shares; issued and outstanding 37,267,673 shares at December 31, 2006 and 2005				
Special share US$0.10 par value: authorized 1 share; issued and outstanding 1 share at December 31, 2005 and 2006		—	—	—
Contributed surplus		1,692,251	1,692,251	246,716
Statutory reserves	22	266,586	267,586	39,012
Accumulated other comprehensive income		28,851	85,643	12,486
Retained earnings		546,630	650,974	94,907
Total stockholders' equity		2,566,263	2,728,399	397,778
Commitments and contingencies	23, 24	—	—	—
Total liabilities, minority interests and stockholders' equity		6,679,630	7,961,357	1,160,700

See accompanying notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss) for years ended December 31, 2004, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Note	Common stock Rmb	Contributed surplus Rmb	Statutory reserves Rmb	Retained earnings Rmb	Accumulated other comprehensive income Rmb	Total stockholders' equity Rmb
Balance at January 1, 2004		30,349	1,486,934	229,920	244,484	—	1,991,687
2004							
Net income		—	—	—	491,397	—	491,397
Comprehensive income							491,397
Transfer to statutory reserves	22	—	—	36,309	(36,309)	—	—
Balance at December 31, 2004		30,349	1,486,934	266,229	699,572	—	2,483,084
2005							
Net loss		—	—	—	(32,291)	—	(32,291)
Net unrealized gains on investment securities held by an affiliate, net of nil tax		—	—	—	—	38,869	38,869
Foreign currency translation adjustments, net of nil tax		—	—	—	—	(10,018)	(10,018)
Comprehensive loss							(3,440)
Transfer to statutory reserves	22	—	—	357	(357)	—	—
Shares issued in connection with							
— Conversion of convertible debt into 1,927,673 common shares	19	1,596	205,317	—	—	—	206,913
Dividend declared (US$0.39 per share)		—	—	—	(120,294)	—	(120,294)
Balance at December 31, 2005		31,945	1,692,251	266,586	546,630	28,851	2,566,263
2006							
Net income		—	—	—	111,284	—	111,284
Net unrealized gains on investment securities, net of nil tax and reclassification adjustments[a]		—	—	—	—	56,840	56,840
Net unrealized gains on investment securities held by an affiliate, net of nil tax		—	—	—	—	3,201	3,201
Foreign currency translation adjustments, net of nil tax		—	—	—	—	(3,249)	(3,249)
Comprehensive income							168,076
Transfer to statutory reserves	22	—	—	1,000	(1,000)	—	—
Dividend declared (US$0.02 per share)		—	—	—	(5,940)	—	(5,940)
Balance at December 31, 2006		31,945	1,692,251	267,586	650,974	85,643	2,728,399
Balance at December 31, 2006 (in US$)		4,657	246,716	39,012	94,907	12,486	397,778

(a) Disclosure of reclassification amounts (Note 17(b)):

Unrealized holdings gains arising during 2006		97,332
Reclassification adjustments in 2006 for gains included in:	(19,550)	
— net income	(20,942)	
— investment in affiliate upon conversion	56,840	
Net unrealized gains on investment securities		

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

for years ended December 31, 2004, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Years ended December 31,			
	2004	2005	2006	2006
	Rmb	Rmb	Rmb	US$
Cash provided by operating activities				
Net income/(loss)	491,397	(32,291)	111,284	16,225
Adjustments to reconcile net income/(loss) to net cash provided by operating activities:				
— Depreciation and amortization of property, plant and equipment	129,340	141,333	142,860	20,828
— Lease prepayment charged to expense	3,449	3,339	3,328	485
— Provision for uncollectible loans to a related party	—	202,950	—	—
— Impairment of property, plant and equipment	—	—	2,346	342
— Loss on disposal of property, plant and equipment	12,998	10,474	1,598	233
— Gain on transfer of land use rights to a related party	—	(2,533)	(1,841)	(268)
— Deferred income taxes	1,116	(20,050)	(19,996)	(2,915)
— Provision for losses on guarantees	—	12,318	(7,410)	(1,080)
— Equity in losses of affiliates	—	6,032	22,449	3,272
— Dividend received from an affiliated company	—	7,815	—	—
— Minority interests	157,292	(2,947)	61,645	8,987
— Gain on redemption of investment securities	—	—	(28,457)	(4,149)
— Net loss on changes in fair value of embedded derivatives	—	—	3,617	527
— Exchange loss on financing activities	—	—	38,388	5,597
(Increase)/decrease in assets				
— Inventories	(469,211)	(321,890)	103,252	15,053
— Amounts due from related parties, net	(5,534)	(115,074)	77,401	11,284
— Trade accounts receivable, net	(25,954)	(303,288)	(302,065)	(44,039)
— Prepaid expenses	(21,069)	(79,757)	44,345	6,465
— Other receivables, net	(106,581)	(20,237)	(4,417)	(644)
— Loans to customers, net	—	(7,904)	(3,582)	(522)
— Income taxes recoverable	(21,842)	(67,232)	32,885	4,794
Increase/(decrease) in liabilities				
— Trade accounts payable	357,751	710,726	332,355	48,455
— Accrued expenses and other liabilities	88,521	112,828	25,236	3,679
— Amount due to holding company	(2,065)	158	(1,075)	(157)
Net cash provided by operating activities	589,608	234,770	634,146	92,452

Consolidated Statements of Cash Flows

for years ended December 31, 2004, 2005 and 2006

(Rmb and US$ amounts expressed in thousands, except per share data)

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Cash flow from investing activities				
Purchase of property, plant and equipment and construction in progress (includes interest capitalized)	(552,902)	(515,359)	(323,781)	(47,205)
Proceeds from disposal of property, plant and equipment	5,883	3,826	2,134	311
Proceeds from disposal of land use rights	—	3,580	2,394	349
Repayment of loans by a related party	—	205,000	—	—
Loans to a related party	(205,000)	(205,000)	—	—
Purchase of investments	(1,348)	(161,358)	(923,101)	(134,580)
Prepayments for land use right	—	—	(59,497)	(8,674)
Proceeds from redemption of investment securities	—	—	11,907	1,736
Net cash used in investing activities	(753,367)	(669,311)	(1,289,944)	(188,063)
Cash flow from financing activities				
Proceeds from short-term bank loans	330,000	1,188,178	974,978	142,144
Proceeds from long-term bank loans	100,000	50,000	687,473	100,228
Proceeds from issuance of convertible debt	—	206,913	—	—
Repayments of short-term and long term bank loans	(190,000)	(805,343)	(962,835)	(140,373)
Repayment of short-term borrowing from a related party	(8,000)	—	—	—
Capital contribution from minority stockholders	31,000	—	—	—
Dividends paid by subsidiaries to minority stockholders	(8,507)	(66,677)	(23,036)	(3,358)
Dividends paid to stockholders	—	(120,294)	(5,940)	(866)
Net cash provided by financing activities	254,493	452,777	670,640	97,775
Effect of foreign currency exchange on cash and cash equivalents	—	(4,713)	(5,104)	(744)
Net increase in cash and cash equivalents	90,734	13,523	9,738	1,420
Cash and cash equivalents at beginning of year	631,938	722,672	736,195	107,331
Cash and cash equivalents at end of year	722,672	736,195	745,933	108,751
Supplemental disclosures of cash flow information				
Cash paid during the year for:				
— Interest, net of amount capitalized	31,757	70,527	117,491	17,129
— Income taxes	125,891	97,431	21,012	3,063

Significant non-cash investing transactions

During 2005, the convertible debt issued was converted to 1,927,673 ordinary shares of the Company (see Note 19).

During 2006, the Company settled the amounts payable for the acquisitions of certain new debt and equity securities issued by an affiliated company and the amounts receivable from redemption of its existing investment in debt securities of the same affiliated company with a net cash payment of S$5.3 million by the Company (see Note 17(b)(ii)).

See accompanying notes to consolidated financial statements.

1 Background and principal activities

China Yuchai International Limited (the "Company") was incorporated under the laws of Bermuda on April 29, 1993. The Company was established to acquire a controlling financial interest in Guangxi Yuchai Machinery Company Limited ("Yuchai"), a Sino-foreign joint stock company which manufactures, assembles and sells diesel engines in the People's Republic of China (the "PRC"). The principal markets for Yuchai's diesel engines are truck manufacturers in the PRC.

The Company owns, through six wholly-owned subsidiaries, 361,420,150 shares or 76.41% of the issued share capital of Yuchai ("Foreign Shares of Yuchai"). Guangxi Yuchai Machinery Group Company Limited ("State Holding Company"), a state-owned enterprise, owns 22.09% of the issued share capital of Yuchai ("State Shares of Yuchai").

In December 1994, the Company issued a special share (the "Special Share") at par value of US$0.10 to Diesel Machinery (BVI) Limited ("DML"), a company controlled by Hong Leong Corporation Limited, now known as Hong Leong (China) Limited ("HLC"). The Special Share entitles its holder to designate the majority of the Company's Board of Directors (six of eleven). The Special Share is not transferable except to Hong Leong Asia Ltd. ("HLA"), the holding company of HLC, or any of its affiliates. During 2002, DML transferred the Special Share to HL Technology Systems Pte Ltd ("HLT"), a subsidiary of HLC.

Yuchai established three direct subsidiaries, Yuchai Machinery Monopoly Company Limited ("YMMC"), Guangxi Yulin Yuchai Machinery Spare Parts Manufacturing Company Limited ("GYSPM") and Yuchai Express Guarantee Company Limited ("YEGCL"). YMMC and GYSPM were established in 2000, and are involved in the manufacture and sale of spare parts and components for diesel engines in the PRC. YEGCL, was established in 2004, and is involved in the provision of financial guarantees to mortgage loan applicants in favor of banks in connection with the applicants' purchase of automobiles equipped with diesel engines produced by Yuchai. In 2006, YEGCL ceased granting new guarantees with the aim of servicing the remaining outstanding guarantee commitments to completion, expected to be in 2009. As at December 31, 2006, Yuchai held an equity interest of 71.83%, 97.14% and 76.92% respectively in these companies. As at December 31, 2005 and 2006, YMMC had direct controlling interests in twenty-one subsidiaries, which are involved in the trading and distribution of spare parts of diesel engines and automobiles, all of which are established in the PRC.

In March 2005, the Company acquired 14.99% of the ordinary shares of Thakral Corporation Limited ("TCL"). TCL is a company listed on the main board of the Singapore Exchange Securities Trading Limited (the "Singapore Exchange") and is involved in the manufacture, assembly and distribution of high-end consumer electronic products and home entertainment products in the PRC. Three directors out of ten directors on the board of TCL are appointed by the Company. Based on the Company's shareholdings and representation in the board of directors of TCL, management has concluded that the Company has the ability to exercise significant influence over the operating and financial policies of TCL. Consequently, the Company's consolidated financial statements include the Company's share of the results of TCL, accounted for under the equity method. The Company acquired an additional 1.00% of the ordinary shares of TCL in September 2005. As a result of the rights issue of 87,260,288 rights shares on February 16, 2006, the Company's equity interest in TCL increased to 19.36%. On August 15, 2006, the Company exercised its right to convert all of its 52,933,440 convertible bonds into 529,334,400 new ordinary shares in the capital of TCL. Upon the issue of the new shares, the Company's interest in TCL has increased to 36.61% of the total issued and outstanding ordinary shares. (See Note 17(b)(i)).

(Rmb and US$ amounts expressed in thousands, except per share data)

1 Background and principal activities (continued)

On February 7, 2006, the Company acquired 29.13% of the ordinary shares of HLG Enterprise Limited ("HLGE"). HLGE is a public company listed on the main board of the Singapore Exchange. HLGE is primarily engaged in investment holding, and through its group companies, invests in rental property, hospitality and property developments in Asia. On November 15, 2006, the Company exercised its right to convert all of its 196,201,374 non-redeemable convertible cumulative preference shares into 196,201,374 new ordinary shares in the capital of HLGE, (see Note 17(b)(ii)). Upon the issue of the new shares, the Company's equity interest in HLGE has increased to 45.42% of the enlarged total number of ordinary shares in issue. Three directors out of six directors on the board of HLGE are appointed by the Company. Based on the Company's shareholdings and representation in the board of directors of HLGE, management has concluded that the Company has the ability to exercise significant influence over the operating and financial policies of HLGE. Consequently, the Company's consolidated financial statements include the Company's share of the results of TCL, accounted for under the equity method.

2 General

(a) Basis of presentation

The accompanying consolidated financial statements are prepared in accordance with United States of America generally accepted accounting principles ("U.S. GAAP").

(b) Restatement of 2005 consolidated financial statements

The Company's consolidated financial statements as of and for the year ended December 31, 2005 were previously restated on May 30, 2008 to reflect certain adjustments to correct accounting error for such period. The most significant adjustment was to correct accounting errors for the understatement of accounts payable of Rmb167.8 million by Yuchai at December 31, 2005. The accompanying 2005 consolidated financial statements reflect those previously restated financial statements of the Company and its subsidiaries.

3 Summary of significant accounting policies and practices

(a) Principles of consolidation

The consolidated financial statements include the financial statements of the Company, its majority-owned subsidiaries and those entities that the Company has determined that it has a direct or indirect controlling financial interest in (collectively, referred to as the 'Group'). All significant intercompany balances and transactions have been eliminated in consolidation. In addition, the Company evaluates the Group's relationships with other entities to identify whether they are variable interest entities as defined by the Financial Accounting Standard Board (the "FASB") Interpretation ("FIN") No. 46 (R), "Consolidation of Variable Interest Entities" ("FIN 46(R)") and to assess whether it is the primary beneficiary of such entities. If the determination is made that the Group is the primary beneficiary, then that entity is included in the consolidated financial statements in accordance with FIN 46(R). The Group was not the primary beneficiary of any variable interest entities during the three years ended December 31, 2006.

3 Summary of significant accounting policies and practices (continued)

(b) Cash and cash equivalents

Cash includes cash on hand and demand deposits with banks. For purposes of the consolidated statement of cash flows, management considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. None of the Group's cash is restricted as to withdrawal. See Note 29 for discussion of restrictions on the Renminbi.

(c) Trade accounts receivable and bills receivable , net

Trade accounts receivable are recorded at the invoiced value of goods sold after deduction of trade discounts and allowances, if any. The allowance for doubtful accounts is management's best estimate of the amount of probable credit losses in the Group's accounts receivable. Management determines the allowance based on specific account identification and historical write-off experience by industry and national economic data.

Management reviews the Group's allowance for doubtful accounts monthly. Past due balances over 90 days and over a specified amount are reviewed individually for collectability. All other balances are reviewed on a pooled basis by aging of such balances. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Group does not have any off-balance-sheet credit exposure related to its customers, except for outstanding bills discounted with banks (see Note 24(e)) and off-balance-sheet credit exposure of YEGCL (see Note 24(d)), that are subject to recourse for non-payment.

The Group sells trade accounts and bills receivable to banks on an ongoing basis. The buyer is responsible for servicing the receivables upon maturity of the trade accounts receivable. Sales of the trade accounts receivable are accounted for under Statement of Financial Accounting Standards ("SFAS") No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". Accordingly, trade accounts and bills receivable are derecognized, and a discount equal to the difference between the carrying value of the trade accounts and bills receivable and cash received is recorded. The Group received proceeds from the sales of the trade accounts and bills receivable of Rmb2,380,569, Rmb3,423,296 and Rmb4,485,221 (US$653,908), for the years ended December 31, 2004, 2005 and 2006, respectively. The Group has recorded discounts totaling of Rmb31,709, Rmb44,362 and Rmb54,720 (US$7,978) in respect of sold trade accounts and bills receivable for the years ended December 31, 2004, 2005 and 2006, respectively, which has been included in interest expense.

(d) Inventories

Inventories are stated at the lower of cost and market. Cost is determined using the weighted average cost method. Cost of work in progress and finished goods comprises direct materials, direct labor and an attributable portion of production overheads. Management routinely reviews its inventory for salability and indications of obsolescence to determine if inventory carrying values are higher than market values. If market conditions or future product enhancements and developments change, inventories would be written down to reflect the estimated realizable value.

3 Summary of significant accounting policies and practices (continued)

(e) Property, plant and equipment, net

Property, plant and equipment, including leasehold improvements, are stated at cost. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, taking into account the estimated residual value. The estimated useful lives are as follows:

Buildings	30 to 40 years
Machinery and equipment	5 to 15 years
Office and computer equipment	4 to 5 years
Leasehold improvements	shorter of estimated useful life or remaining lease terms

The Group capitalizes interest with respect to major assets under installation or construction based on the average cost of the Group's borrowings. Repairs and maintenance of a routine nature are expensed while those that extend the life of assets are capitalized. Upon retirement or disposal of assets, the cost and related accumulated depreciation are removed from the consolidated balance sheets and any gain or loss is included in the consolidated statements of operations.

Construction in progress represents factories under construction and machinery and equipment pending installation. All direct costs relating to the acquisition or construction of buildings and machinery and equipment, including interest charges on borrowings, are capitalized as construction in progress. No depreciation is provided in respect of construction in progress. Construction of plant is considered to be completed on the date when the plant is substantially ready for its intended use notwithstanding whether the plant is capable of producing saleable output in commercial quantities.

(f) Lease prepayments

Lease prepayments represent payments to the PRC land bureau for land use rights, which are charged to expense on a straight-line basis over the respective periods of the rights which are in the range of 15 to 50 years.

(g) Guarantees

The fair value of a guarantee provided by the Group for the obligation of others is recognized at fair value at inception as a liability in accordance with FIN No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees". If the guarantee was issued in a stand-alone transaction for a fee, the fair value of the liability recognized generally would offset the cash received by the Group, which is included in "Accrued expenses and other liabilities" and amortized to revenue over the period of guarantee.

After initial measurement and recognition of the liability for obligations under the guarantee, management periodically evaluates outstanding guarantees and accounts for potential loss contingencies associated with the guarantees based on estimated losses from default in accordance with SFAS No. 5, "Accounting for Contingencies," under which the liability is adjusted for further loss that is probable and when the amount of the loss can be reasonably estimated.

3 Summary of significant accounting policies and practices (continued)

(h) Investments

Affiliates

An affiliated company is an entity in which the Company or the Group has the ability to exercise significant influence in its financial and operating policy decisions, but does not have a controlling financial interest. Investments in affiliates are accounted for using the equity method. The Group's share of earnings and losses of affiliated companies, adjusted to eliminate intercompany gains and losses and to account for the difference between the cost of investment and underlying equity in net assets of the affiliates, is included in the consolidated results.

Management assesses impairment of its investments in affiliates when adverse events or changes in circumstances indicate that the carrying amounts may not be recoverable. A loss in value of investments in affiliated companies which is considered other than a temporary decline is recognized as an impairment charge.

Other investments

Investment in available-for-sale debt securities, including convertible preference shares of an affiliate, that are mandatorily redeemable, are carried at fair value. Unrealized holding gains and losses, net of related tax effect, on available-for-sale securities are included in accumulated other comprehensive income/(loss), a separate component of stockholders' equity, until realized. Realized gains and losses from the disposal of available-for-sale equity securities are determined on a specific-identification basis.

Investment in convertible preference shares of an affiliate that are neither mandatorily redeemable by the issuer nor redeemable at the option of the investor, and that do not have a readily determinable fair value are accounted for under the cost method.

The Group recognizes an impairment loss when the decline in fair value below the carrying value of an available-for-sale or cost method investment is considered other than temporary. In determining whether a decline in fair value is other than temporary, management considers various factors including market price of underlying holdings when available, investment ratings, the financial conditions and near term prospect of the investees, the length of time and the extent to which the fair value has been less than cost and the Group's intent and ability to hold the investment for a reasonable period of time sufficient to allow for any anticipated recovery of the fair value.

Equity derivatives embedded in the available-for-sale debt securities are recorded at fair values through income.

(i) Foreign currency transactions and translation

The Company's functional currency is the US dollar. The functional currency of the Company's subsidiaries and certain of its affiliated companies located in the PRC is the Renminbi. Transactions denominated in currencies other than Renminbi are recorded based on exchange rates at the time such transactions arise, such as the Renminbi exchange rates quoted by the People's Bank of China (the "PBOC") prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using the applicable exchange rates at the balance sheet dates. The resulting exchange differences are recorded in the consolidated statements of operations as part of "Other income, net".

3 Summary of significant accounting policies and practices (continued)

(i) Foreign currency transactions and translation (continued)

The Company's reporting currency is the Renminbi. Assets and liabilities of the Company and its subsidiaries whose functional currency is not the Renminbi are translated into Renminbi using the exchange rate on the balance sheet date. Revenues and expenses are translated at average rates prevailing during the year. The gains and losses resulting from translation of financial statements are recorded in accumulated other comprehensive income / (loss), a separate component within stockholders' equity. Cumulative translation adjustments are recognized as income or expenses upon disposal or liquidation of a foreign subsidiary and affiliates.

For the US dollar convenience translation amounts included in the accompanying consolidated financial statements, the Renminbi equivalent amounts have been translated into U.S. dollars at the rate of Rmb 6.8591 = US$1.00, the rate quoted by the PBOC at the close of business on June 30, 2008. No representation is made that the Renminbi amounts could have been, or could be, converted into U.S. dollars at that rate or at any other rate prevailing on June 30, 2008 or any other date.

(j) Income taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets are reduced by a valuation allowance to the extent management concludes it is more likely than not that the assets will not be realized. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates, if any, is recognized in the statements of operations in the financial year that includes the enactment date.

(k) Revenue recognition

(i) Product sales

Revenue is recognized in accordance with the Securities and Exchange Commission ("SEC") Staff Accounting Bulletin No. 104, "Revenue Recognition" ("SAB 104"). SAB 104 requires that, among other conditions, four basic criteria be met before revenue can be recognized: (i) persuasive evidence of an arrangement exists; (ii) the price is fixed or determinable; (iii) collectability is reasonably assured; and (iv) product delivery has occurred. For the Group, these criteria are generally considered to be met upon delivery and acceptance of products at the customer site.

Product sales represent the invoiced value of goods, net of value added taxes ("VAT"), sales returns, trade discounts and allowances. Yuchai and its subsidiaries are subject to VAT which is levied on the majority of their products at the rate of 17% of the invoiced value of sales. Output VAT is borne by customers in addition to the invoiced value of sales. VAT paid by Yuchai and its subsidiaries on its purchases of materials and supplies is recoverable out of VAT collected from sales to their customers.

(Rmb and US$ amounts expressed in thousands, except per share data)

3 Summary of significant accounting policies and practices (continued)

(ii) Guarantee fee income

Guarantee fees received or receivable for a guarantee issued are recorded in "Accrued expenses and other liabilities" based upon the estimated fair value at the inception of such guarantee obligations, and are recognized as revenue on a straight line basis over the respective terms of the guarantees.

(l) Earnings/(loss) per share

Basic earnings/(loss) per share is computed by dividing income/ (loss) attributable to common shares by the weighted average number of common shares outstanding for the period. Diluted earnings/ (loss) per share is calculated by dividing net earnings/(loss) by the weighted average number of common shares outstanding and the number of additional common shares that would have been outstanding if the potential common shares that were dilutive had been issued related to the period in 2005 during which convertible debt issued by the Company was outstanding. No adjustment has been made as the effect would have been anti-dilutive.

The Company's basis and diluted earnings/(loss) per share are as follows:

	Years ended December 31,			
	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Net income/ (loss) attributable to common shares	491,397	(32,291)	111,284	16,225
Earnings/ (loss) per share				
— Weighted average common shares outstanding during the year				
Basic	35,340,000	36,459,635	37,267,673	37,267,673
Diluted	35,340,000	36,459,635	37,267,673	37,267,673
— Basic earnings (loss) per share of common shares				
Basic	13.90	(0.89)	2.99	0.44
Diluted	13.90	(0.89)	2.99	0.44

There were no potentially dilutive common shares during the years ended December 31, 2004 and 2006.

(m) Advertising, research and development costs

Advertising, research and development costs are expensed as incurred. Advertising cost included in "Selling, general and administrative expenses", amounted to Rmb48,725, Rmb45,291 and Rmb42,636 (US$6,216) respectively, for the years ended December 31, 2004, 2005 and 2006.

Research and development expenses are shown net of government subsidies of Rmb nil, Rmb5,915 and Rmb7,858 (U$1,146) for the years ended December 31, 2004, 2005 and 2006.

3 Summary of significant accounting policies and practices (continued)

(n) Goodwill

Goodwill represents the excess of costs over fair value of net assets of businesses acquired. Goodwill is not amortized, but instead is tested for impairment at least annually or whenever certain circumstances indicate a possible impairment may exist. Management evaluates the recoverability of goodwill using a two-step impairment test approach at the reporting unit level at the end of each year. In the first step, the fair value of the reporting unit is compared to its carrying value including goodwill. The fair value of the reporting unit is determined based upon discounted future cash flows. In the case that the fair value of the reporting unit is less than its carrying value, a second step is performed which compares the implied fair value of the reporting unit's goodwill to the book value of the goodwill. In determining the implied fair value of the reporting unit goodwill, the fair values of the tangible net assets and recognized and unrecognized intangible assets is deducted from the fair value of the reporting unit. If the implied fair value of reporting unit goodwill is lower than its carrying amount, goodwill is considered impaired and is written down to its implied fair value. The results of the impairment testing in 2004, 2005 and 2006 did not result in any impairment of goodwill.

(o) Product warranty

The Group recognizes a liability at the time the product is sold, for the estimated future costs to be incurred under the lower of a warranty period or warranty mileage on various engine models, on which the Group provides free repair and replacement. Warranties generally extend for a duration (12 months to 18 months) or mileage (80,000 kilometers to 180,000 kilometers), whichever is the lower. Provisions for warranty are primarily determined based on historical warranty cost per unit of engines sold adjusted for specific conditions that may arise and the number of engines under warranty at each financial year. In previous years, warranty claims have typically not been higher than the relevant provisions made in our consolidated balance sheet. If the nature, frequency and average cost of warranty claims change, the accrued liability for product warranty will be adjusted accordingly.

(p) Use of estimates

The preparation of the consolidated financial statements in accordance with U.S. GAAP requires management of the Group to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the recoverability of the carrying amount of long-lived assets including goodwill, estimated fair value of investments and other financial instruments, realizable values for inventories, valuation allowances for receivables, obligations for warranty costs, and probable losses on loan guarantees of YECGL. Actual results could differ from those estimates.

3 Summary of significant accounting policies and practices (continued)

(q) Impairment of long-lived assets, other than goodwill

Long-lived assets to be held and used, such as property, plant and equipment and construction in progress are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the consolidated balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

(r) Commitments and contingencies

Liabilities for loss contingencies, arising from claims, assessments, litigation, fines and penalties and other sources are recorded when it is probable that an obligation has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

(s) Defined Contribution Plans

The Group participates in the national pension schemes as defined by the laws of the countries in which it has operations. Yuchai and its subsidiaries make contributions to the defined contribution retirement plans, organized by the Guangxi Regional Government and Beijing City Government, at a fixed proportion of the basic salary of the staff. Contributions are recognized as compensation expense in the period in which the related services are performed.

(t) Recently issued accounting standards

In September 2006, the US Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 108 ("SAB 108"). "Considering the Effect of Prior Year Misstatement when Quantifying Misstatements in Current Year Financial Statements" which requires companies to evaluate the materiality of identified unadjusted errors on each financial statement and related financial statement disclosure using both the rollover approach and the iron curtain approach ("dual approach"). The rollover approach quantifies misstatements based on the amount of the error originating in the current year statement of operations whereas the iron curtain approach quantifies misstatements based on the effects of correcting the misstatements existing in the balance sheet at the end of the current year, irrespective of the misstatements year(s) of origin. Financial statements would require adjustment when either approach results in quantifying a misstatement that is material. The Group adopted SAB No. 108 effective January 1, 2006.

3 Summary of significant accounting policies and practices (continued)

(t) Recently issued accounting standards (continued)

As a transition accommodation, SAB No. 108 permits accumulative effect adjustments, without restatement of previously issued financial statements, to be used for errors that are determined to be immaterial pursuant to the Group's previous method of quantification of unadjusted errors but are determined to be material under dual approach. Prior to the adoption of SAB No. 108, the Group had quantified unadjusted errors under the rollover approach and has assessed these unadjusted errors to be immaterial – individually and in the aggregate. Upon initial adoption of SAB No. 108 for the fiscal year 2006, the management quantified unadjusted errors under the dual approach and assessed that these unadjusted errors are not material. As such, the initial adoption of SAB No. 108, had no impact on the Company's consolidated financial statements.

In December 2004, the FASB issued SFAS No.123 (revised 2004), "Share-Based Payment", which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. This statement is a revision to SFAS No. 123 and supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees", and its related implementation guidance. This statement will require measurement of the cost of employee services received in exchange for stock compensation based on the grant-date fair value of the employee stock options. Incremental compensation costs arising from subsequent modifications of awards after the grant date must be recognized. The Company adopted this statement on January 1, 2006 under the modified prospective method of application. Under that method, the Company will recognize compensation costs for new grants of share-based awards, awards modified after the effect date, and the remaining portion of the fair value of the unvested awards at the adoption date. The initial adoption of this statement did not have any effect on the Company's 2006 consolidated financial statements.

In December 2004, the FASB issued SFAS No. 151, "Inventory Costs", which clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Under this statement, such items will be recognized as current-period charges. In addition, the statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement was effective and adopted by the Company for inventory costs incurred on or after January 1, 2006. The initial adoption of this statement had no effect on the Company's 2006 consolidated financial statements.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets", which eliminates an exception in APB Opinion No. 29, "Accounting for Nonmonetary Transactions", for recognizing nonmonetary exchanges of similar productive assets at fair value and replaces it with an exception for recognizing exchanges of nonmonetary assets at fair value that do not have commercial substance. This statement was effective and adopted by the Company for nonmonetary asset exchanges occurring on or after January 1, 2006. The adoption of this statement had no effect on the Company's 2006 consolidated financial statements.

3 Summary of significant accounting policies and practices (continued)

(t) Recently issued accounting standards (continued)

In September 2005, the EITF issued EITF 04-13, "Accounting for Purchases and Sales of Inventory with the Same Counterparty". EITF 04-13 provides guidance as to when purchases and sales of inventory with the same counterparty should be accounted for as a single exchange transaction. EITF 04-13 also provides guidance as to when a nonmonetary exchange of inventory should be accounted for at fair value. EITF 04-13 was applied to new arrangements entered into, and modifications or renewals of existing arrangements beginning in the first interim or annual reporting periods beginning after March 15, 2006. The application of EITF 04-13 did not have any impact on the Company's consolidated financial statements.

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments — an amendment of FASB Statements No. 133 and 140". This statement amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". This statement resolves issues addressed in SFAS No. 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets". This statement will be effective for the fiscal years beginning after September 15, 2006. Management does not believe there will be any material impact of initial adoption of this statement to the Company's consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets — an amendment of FASB Statement No. 140". This statement amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and servicing liabilities. The statement requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in certain situations and requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable. The statement also provides guidelines to classification, disclosure and subsequent measurement of servicing assets and servicing liabilities. This statement will be effective for the fiscal years beginning after September 15, 2006. Management is currently evaluating the impact of the statement to the Company's consolidated financial statements.

In June 2006, the FASB issued FIN No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in the Company's financial statements in accordance with SFAS No. 109. FIN 48 prescribes a recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The provisions of FIN 48 are effective for the fiscal years beginning after December 15, 2006. Management is currently evaluating the impact of the provisions of FIN 48 to the Company's consolidated financial statements.

3 Summary of significant accounting policies and practices (continued)

(t) Recently issued accounting standards (continued)

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expenses disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements and eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS No. 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. In February 2008, the FASB Staff Position, or FSP, SFAS No. 157-1, "Application of FASB SFAS No. 157 to SFAS No. 13 and its Related Interpretive Accounting Pronouncements That Address Leasing Transactions," and FSP SFAS No. 157-2, "Effective Date of SFAS No. 157." FSP SFAS No. 157-1 excludes from the scope of SFAS No.157 certain leasing transactions accounted for under SFAS No. 13, "Accounting for Leases". FSP SFAS No. 157-2 delays the effective date of SFAS No. 157 from 2008 to 2009 for all non financial assets and non financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The provisions of SFAS No. 157 will be applied prospectively to fair value measurements and disclosures for financial assets and financial liabilities and non financial assets and non financial liabilities recognized or disclosed at fair value in the financial statements on at least an annual basis beginning in the first quarter of 2008. Management does not believe the adoption of SFAS No. 157 will have a material impact on the consolidated financial statements at this time and will monitor any additional implementation guidance that may be issued.

In February 2007, the FASB issued SFAS No. 159, "Fair Value Option for Financial Assets and Financial Liabilities". Under SFAS No. 159, entities will be permitted to measure various financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis (the fair value option). SFAS No. 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company has elected not to adopt the fair value option for the eligible items as of January 1, 2008.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), or SFAS No. 141R, "Business Combination" which replaces FAS Statement No. 141. SFAS No. 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non controlling interest in the acquiree and the goodwill acquired. The statement also establishes disclosure requirements which will enable users to evaluate the nature and financial effects of the business combination. This statement is effective as of the beginning of an entity's first fiscal year beginning after December 15, 2008. The impact of the adoption of SFAS No. 141R on the Company's consolidated financial position and consolidated results of operations is dependent upon the specific terms of any applicable future business combinations.

(Rmb and US$ amounts expressed in thousands, except per share data)

3 Summary of significant accounting policies and practices (continued)

(t) Recently issued accounting standards (continued)

In December 2007, the FASB issued SFAS No. 160, "Non Controlling Interests in Consolidated Financial Statements-Amendments of ARB No. 51". SFAS No. 160 states that accounting and reporting for minority interests will be recharacterised as non controlling interests and classified as a component of equity. The statement also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non controlling owners. FAS No. 160 applies to all entities that prepare consolidated financial statements, except non-for-profit organizations, but will affect only those entities that have an outstanding non controlling interest in one or more subsidiaries or that deconsolidate a subsidiary. The Company is required to adopt this statement in the first quarter of fiscal year 2009 and management is currently assessing the impact of adopting SFAS No. 160.

4 Depreciation and amortization, sales commissions, and shipping and handling expenses

Depreciation and amortization of property, plant and equipment, are included in the following captions:

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Cost of goods sold	84,907	90,354	94,215	13,736
Selling, general and administrative expenses	44,433	50,979	48,645	7,092
	129,340	141,333	142,860	20,828

Sales commissions to sales agents are included in the following caption:

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Selling, general and administrative expenses	11,564	39,372	32,172	4,690

Sales related shipping and handling expenses not separately billed to customers are included in the following caption:

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Selling, general and administrative expenses	86,163	126,813	116,570	16,995

(Rmb and US$ amounts expressed in thousands, except per share data)

5 Provision for uncollectible loans to a related party

The amount represents the recognition of specific doubtful debt provisions totaling Rmb202,950 on the loans with an aggregate principal amount of Rmb205,000 due from Yuchai Marketing and Logistic Company Limited ("YMLC") as of December 31, 2005. YMLC is wholly owned by Coomber Investment Limited ("Coomber"), a shareholder of the Company and State Holding Company (collectively, the "Chinese Shareholders").

In March and May 2004, Yuchai granted interest-free advances to YMLC at the request of Yuchai's PRC directors to provide YMLC with initial working capital for its start-up activities. YMLC was set up with the intention of offering a complementary range of services including spare parts distribution, insurance, vehicle financing and warranty servicing. These advances were provided with the approval of the previous Chairman of Yuchai but without prior approval by the majority of the shareholders of Yuchai.

On December 2, 2004, these advances were converted into formal loans and written agreements and were executed between Yuchai and YMLC through an authorized financial institution in the PRC. Under the terms of the loan agreements, the loans were payable in their entirety on December 2, 2005 and interest, at the rate of 5.58% per annum, was payable on a monthly basis. Further, the loans were secured by guarantees given by the Chinese Shareholders. The Company's policy with regard to interest earned on impaired loan is to recognize interest income on the cash basis, as management believes there is no assurance that future interest due relative to the loan's terms will be collected. Interest income of Rmb11,922 and Rmb10,512 (US$1,533) was received and recognized in 2005 and 2006, respectively (see Note 7).

Because the loans had already been disbursed, the Chinese Shareholders had issued guarantees for these loans, and the Company's relationship with the Chinese Shareholders was improving, the Directors of Yuchai believed that it was in the Company's and Yuchai's best interest to ratify the loans. Consequently, the loans were ratified by the Board of Directors of Yuchai in April 2005.

In 2005, the Company discussed with the Chinese Shareholders the possibility of converting the loans into an equity investment in YMLC, subject to the Yuchai board's approval. This potential alternative was incorporated within the terms of the reorganization agreement entered into by the Company with Yuchai and Coomber on April 7, 2005 ("Reorganization Agreement").

When the loans became due in December 2005, Yuchai was requested to extend the maturity date for the loans. However, the Company and Yuchai had been unable to access the financial statements of YMLC. Consequently, the Directors from the Company's and Yuchai's boards had doubts about YMLC's ability to repay the loans. However, the Company's and Yuchai's board of directors considered the request to extend the loans based on representations received from the Chinese Shareholders and management of YMLC concerning their respective abilities and intentions to repay the loans and honor their guarantees, and therefore agreed to extend the repayment date of the loans for an additional year. The extension of the loans was approved by the Board of Directors of Yuchai on December 2, 2005. An agency bank was appointed under PRC requirements to administer the Rmb205,000 loans and the legal method requires such loans to be repaid and the funds re-disbursed. The new loans carry the same terms, including scheduled maturity on December 1, 2006. New guarantees were also granted by the Chinese Shareholders for these loans.

(Rmb and US$ amounts expressed in thousands, except per share data)

5 Provision for uncollectible loans to a related party (continued)

The Company discussed this matter with the Chinese Shareholders and management of YMLC and also considered the financial position and financial resources of the State Holding Company and Coomber. CYI management made an assessment of the future cash flows of the State Holding Company and Coomber and concluded that it was likely they will not be able to honor their respective guarantees in the event YMLC is unable to repay the loans when they become due.

Consequently, at that time, CYI management identified a number of possible courses of action in the event YMLC is unable to repay the loans when they become due. These actions included:

- Taking actions to force YMLC to liquidate;
- Retaining portions of future dividends declared by Yuchai and payable to State Holding Company until the guarantee obligations are fulfilled; and
- Commencing legal action against YMLC and possibly the Chinese Shareholders.

The Company's management ruled out any form of legal or other enforcement action against the Chinese Shareholders as management believed that Yuchai may not be the first preferred creditor entitled to receive payment of the judgment debt. Moreover, management believed that the process for enforcement of a judgment in China is complex and not as effective when compared with other jurisdictions. In addition, management believed that the commencement of legal or other enforcement actions will likely lead to a deterioration in relations with the Chinese Shareholders which could have a materially adverse impact on the Company's investment in Yuchai and could lead to the impairment of shareholder value of the Company. Consequently, management believed that it was beneficial to the Company's shareholders for management to continue their dialogue and seek other possible arrangements with YMLC, Coomber and State Holding Company to resolve the repayment of the Rmb205,000 (US$29,887) loans rather than for it to resort to legal and enforcement actions described above.

The Company will recognize any subsequent recoveries of the amount due from YMLC in its consolidated financial statements in the periods in which any such recoveries are realized (see Note 34(b)).

6 Interest cost

The Group capitalizes interest charges as a component of the cost of construction in progress. The following is a summary of interest cost incurred during 2004, 2005 and 2006:

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Interest cost capitalized	19,701	20,991	18,057	2,633
Interest cost charged to consolidated statements of operations	31,757	70,527	117,491	17,129
Total interest cost incurred	51,458	91,518	135,548	19,762

(Rmb and US$ amounts expressed in thousands, except per share data)

7 Other income, net

Other income, net consists of:

	Years ended December 31,			
	2004 Rmb	*2005* Rmb	*2006* Rmb	*2006* US$
Interest income (see Note 5)	3,286	21,744	47,124	6,871
Foreign exchange (loss)/gain, net	(38)	607	(41,940)	(6,115)
Dividend income from other investments	4,591	—	—	—
Rental income	—	6,078	1,766	257
Gain on redemption of investment securities (Note 17(b)(ii))	—	—	28,457	4,149
Net loss on changes in fair value of embedded derivatives (Note 17(b))	—	—	(3,617)	(527)
Others, net	(2,157)	(2,980)	7,066	1,030
	5,682	25,449	38,856	5,665

8 Income taxes

Bermuda tax

The Company is incorporated under the laws of Bermuda and, under the current Bermuda laws, is not subject to tax on income or capital gains.

The Company has received an undertaking from the Minister of Finance in Bermuda pursuant to the provisions of the Exempted Undertakings Tax Protection Act, 1966, which exempts the Company and its stockholders, other than stockholders ordinarily resident in Bermuda, from any Bermuda taxes computed on profit, income or any capital assets, gain or appreciation, or any tax in the nature of estate duty or inheritance tax at least until the year 2016.

PRC income tax

As Yuchai is a sino-foreign enterprise in the Western Region of the PRC that is engaged in an encouraged industry, its PRC statutory income tax rate is 15% in 2004, 2005 and 2006 under the relevant PRC income tax laws.

The PRC income tax rates of Yuchai's subsidiaries under the relevant PRC income tax laws are 15% to 33% in 2004, 2005 and 2006.

Pursuant to the income tax law of the PRC concerning foreign investment and foreign enterprises (the "FEIT Law"), the applicable income tax rate through December 31, 2006 of Yuchai was 15%. Since January 1, 2002, Yuchai is subject to tax at a rate of 15.0% so long as it continues to qualify as a foreign-invested enterprise eligible for tax reductions under PRC income tax law. In 2008, Yuchai has fulfilled the requirements to qualify for the reduced tax rate of 15%, although pending approval of the tax authority, which management has assessed to be more than probable. In the event that this is not approved, Yuchai will be subject to tax at a rate of 18%. Some of Yuchai's subsidiaries that were subject to tax at a rate of 33% has been lowered to 25% following the Corporate Income Tax Law (the "CIT Law") which became effective January 1, 2008. The CIT Law adopts a uniform tax rate of 25% for all enterprises, including foreign-invested enterprises.

(Rmb and US$ amounts expressed in thousands, except per share data)

8 Income taxes (continued)

Income tax expense in the consolidated statements of operations consists of:

	Years ended December 31,			
	2004	**2005**	**2006**	**2006**
	Rmb	**Rmb**	**Rmb**	**US$**
Current tax expense	104,049	30,198	50,462	7,357
Deferred tax expense/(benefit)	1,116	(20,050)	(19,996)	(2,915)
	105,165	10,148	30,466	4,442

Income tax expense reported in the consolidated statements of operations differs from the amount computed by applying the PRC income tax rate of 15% for the three years ended December 31, 2006 for the following reasons:

	Years ended December 31,			
	2004	**2005**	**2006**	**2006**
	Rmb	**Rmb**	**Rmb**	**US$**
Computed "expected" tax expense (benefit)	113,078	(3,764)	30,509	4,448
Adjustments resulting from:				
— Non-deductible expenses related to errors correction (see Note (iii))	—	10,623	7,795	1,136
— Other non-deductible expenses	471	5,703	4,053	591
— Tax credits (see Note (i))	(16,184)	(43,535)	(17,281)	(2,519)
— Change in valuation allowance	—	45,231	(6,492)	(946)
— Rate differential of subsidiaries	7,800	(4,110)	11,882	1,732
Actual tax expense	105,165	10,148	30,466	4,442

Notes:

(i) Amounts mainly represent tax credits relating to the purchase of domestic equipment for technological improvement and for approved research and development costs.

(ii) All pre-tax booked income and income tax expense (benefit) are from PRC sources.

(iii) Amount relates to non-deductible permanent differences from the restatement of the Company's 2005 financial statements as at May 15, 2008 as such expenses are not expected to be deductible in accordance with PRC regulations.

(Rmb and US$ amounts expressed in thousands, except per share data)

8 Income taxes (continued)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets at December 31, 2005 and 2006 are presented below:

	December 31,		
	2005 Rmb	2006 Rmb	2006 US$
Trade accounts receivable	23,810	36,806	5,366
Inventories	8,336	23,251	3,390
Property, plant and equipment	50,734	26,982	3,933
Accrued expenses and other liabilities	39,259	49,384	7,200
Tax losses carried forward	11,615	5,075	740
Tax credits	43,535	50,434	7,353
Loans to a related party	30,443	29,304	4,272
Total gross deferred tax assets	207,732	221,236	32,254
Less: Valuation allowance	45,231	38,739	5,648
Net deferred tax assets	162,501	182,497	26,606

The following table represents the classification of the Group's net deferred tax assets:

	December 31,		
	2005 Rmb	2006 Rmb	2006 US$
Net deferred tax assets comprise:			
Current portion	85,351	112,779	16,442
Non-current portion	77,150	69,718	10,164
	162,501	182,497	26,606

As of December 31, 2006, Yuchai was granted tax credits amounting to Rmb10,382 (US$1,514) in relation to approved research and development costs which were fully utilized against current income taxes. In addition, Yuchai was granted tax credits of Rmb6,899 (US$1,006) in 2006 relating to the purchase of certain domestic equipment. According to the relevant laws and regulations in the PRC, the amount of these credits entitled for deduction each year is limited to the incremental current income tax expense of the subsidiary for the year compared to the income tax expense of the subsidiary in the year immediately prior to the year the credit was approved. The Company also has Rmb43,535 of available credits relating to the purchase of certain domestic equipment carried over from prior years

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets of the Group will not be realized. Management considered that it is more likely than not that available tax credits totaling Rmb27,102 (US$3,951) relating to the purchase of domestic equipment cannot be fully utilized as the amount entitled for deduction each year is limited to the incremental current income tax expense of the subsidiary compared to the income tax expense of the subsidiary in the year prior to the year the credit was approved. Based on management's forecast of future taxable income and of related tax to be paid for each of the years through 2010, management believes that it is more likely than not that credits approved in 2005 of Rmb27,102 will expire unused.

(Rmb and US$ amounts expressed in thousands, except per share data)

8 Income taxes (continued)

As at December 31, 2006, Yuchai has credits for PRC tax purposes of Rmb50,434 (US$7,353) which are available to offset future taxable income, if any. Tax credits of Rmb7,711, Rmb27,102 and Rmb15,621 expire in 2008, 2009 and 2010, respectively if not utilized.

As at December 31, 2006 certain subsidiaries of the Company had net operating loss carry forwards for PRC income tax purposes of Rmb26,727 (US$3,897), which are available to offset future taxable income, if any. Net operating loss carry forwards Rmb20,155, Rmb4,824 and Rmb1,748 will expire if unused in 2009, 2010 and 2011, respectively. One of the subsidiaries has been loss making since its commencement of operations in 2004 and management deems it more likely than not that the deferred tax asset relating to the net operating loss of this entity in the amount of Rmb1,954 will not be realizable. In addition, management has concluded that all other deferred tax assets of this subsidiary in the amount of Rmb9,683 are also not likely to be realized. A total valuation allowance of Rmb11,637 has been provided for the above net operating loss carry over and other deferred tax assets as at December 31, 2006.

9 Trade accounts receivable, net

Trade accounts receivable, net comprise:

	December 31,		
	2005	***2006***	***2006***
	Rmb	**Rmb**	**US$**
Trade accounts receivable	606,644	517,130	75,393
Less: Allowance for doubtful accounts	69,047	90,365	13,174
	537,597	426,765	62,219
Bills receivable	641,256	1,054,153	153,687
	1,178,853	1,480,918	215,906

An analysis of the allowance for doubtful accounts for 2004, 2005 and 2006 is as follows:

	December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Balance at beginning of year	94,423	107,457	69,047	10,066
Add:				
Charge to consolidated statements of operations	13,034	25,587	21,582	3,146
Less:				
Written off	—	63,997	264	38
Balance at end of year	107,457	69,047	90,365	13,174

(Rmb and US$ amounts expressed in thousands, except per share data)

9 Trade accounts receivable, net (continued)

At December 31, 2005 and 2006, gross trade accounts receivable due from a major customer, Dongfeng Automobile Company and its affiliates ("the Dongfeng companies"), were Rmb161,930 and Rmb121,336 (US$17,690), respectively. See Note 33 for further discussion of business concentration risk.

As of December 31, 2006, no trade accounts receivable was pledged as security under loan arrangements (see Note 18(a)).

10 Amounts due from/to related parties

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
Amounts due from:			
GYMEC	146,222	—	—
SHC & subsidiaries	19,764	54,987	8,017
YMLC & subsidiaries	—	96,547	14,076
Others	67,202	6,978	1,017
Due within one year	233,188	158,512	23,110

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
Amounts due to:			
SHC & subsidiaries	—	64,761	9,442
YMLC & subsidiaries	—	3,863	563
HLMS	—	9,287	1,354
Others	75,186	—	—
Due within one year	75,186	77,911	11,359

Related parties include Guangxi Yuchai Mechanical and Electronics Company ("GYMEC"), Hong Leong Management Services Pte Limited ("HLMS"), TCL, HLGE, YMLC, State Holding Company ("SHC") and their subsidiaries and affiliates. At December 31, 2006, the amounts due from/to related parties are unsecured, interest free and arose principally from transactions as disclosed in Note 27. All amounts due from/to related parties are payable on demand.

In June 2006, YMLC and State Holding Company entered into an agreement with Yuchai to enable Yuchai and its subsidiaries to settle the amounts due from/to YMLC, State Holding Company and their subsidiaries on a net basis, i.e. the balance due from/to YMLC, State Holding Company, their subsidiaries and affiliates as of December 31, 2005 and in 2006 were offset for settlement purposes only.

(Rmb and US$ amounts expressed in thousands, except per share data)

11 Loans to customers, net

Loans to customers, net refers to the designated loans lent by YEGCL through financial institutions to customers. The terms of the loan agreements were designated by the Group. The financial institutions assist the Group to release the principal to the borrowers and collect the repayment on behalf of the Group without bearing the risk of default by customers, if any. The loans carried interest rates ranged from 5.31% to 7.49% and are repayable in installments within one year. The loans are secured and guaranteed by independent third parties.

12 Inventories

Inventories are comprised of:

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
Raw materials	1,029,023	1,058,619	154,338
Work in progress	66,326	24,251	3,536
Finished goods	573,086	482,313	70,317
	1,668,435	1,565,183	228,191

13 Other receivables, net

Other receivables, net comprise:

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
VAT recoverable	87,891	66,005	9,623
Staff loans	18,075	6,602	963
Staff advances	5,434	4,803	700
Amounts due under guarantee contracts, net (see (Note 24(d))	2,004	15,189	2,214
Land deposit	5,000	5,000	729
Interest receivable	—	19,658	2,866
Others	17,248	22,812	3,326
	135,652	140,069	20,421

(Rmb and US$ amounts expressed in thousands, except per share data)

14 Property, plant and equipment, net

Property, plant and equipment, net comprise:

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
Buildings, including leasehold improvements	709,643	854,241	124,541
Machinery and equipment	1,800,640	2,119,912	309,066
Office furniture, fittings and equipment	36,309	97,342	14,192
	2,546,592	3,071,495	447,799
Less: Accumulated depreciation and amortization	1,105,880	1,276,090	186,044
Property, plant and equipment, net	1,440,712	1,795,405	261,755

Loss on disposal of property, plant and equipment for the years ended December 31, 2004, 2005 and 2006 is included in "Selling, general and administrative expenses" as follows:

	December 31,			
	2004	2005	2006	2006
	Rmb	Rmb	Rmb	US$
Loss on disposal of property, plant and equipment	12,998	10,474	1,598	233

15 Construction in progress

Construction in progress comprises capital expenditures and capitalized interest charges relating to the following construction of facilities and assembly lines projects as follows:

	December 31,		
	2005	2006	2006
	Rmb	Rmb	US$
Diesel engine production line and facilities projects	282,900	172,278	25,117
Factories auxiliary facilities	95,230	47,680	6,951
Second foundry	26,047	8,704	1,269
Others	52,575	59,897	8,733
	456,752	288,559	42,070

(Rmb and US$ amounts expressed in thousands, except per share data)

16 Lease prepayments

Summary of lease prepayments follows:

	December 31,		
	2005	*2006*	*2006*
	Rmb	**Rmb**	**US$**
Gross payments for land use rights	96,877	155,596	22,685
Less: amounts charged to expense	27,549	30,652	4,469
Lease prepayments	69,328	124,944	18,216

The land on which the Group's buildings are erected is owned by the PRC Government. Yuchai and its subsidiaries are granted the land use rights of 15 to 50 years in respect of such land. Lease prepayment represents those amounts paid for land use rights to the PRC government. The prepayments are are charged ratably to expense over the term of the land use agreement. In the event that land use rights are sold or transferred, the remaining balance of the prepayment is derecognized and any resulting gain or loss is recorded. Lease prepayments charged to expense were Rmb3,449, Rmb3,339 and Rmb3,328 (US$485) for the years ended December 31, 2004, 2005 and 2006, respectively.

17 Investments

(a) Investments as of December 31, 2005 and 2006 are summarized as follows:

	December 31,		
	2005	*2006*	*2006*
	Rmb	**Rmb**	**US$**
Investments in affiliated companies under the equity method	184,693	508,246	74,098
Other investments in debt and equity securities of affiliated companies (see Note 17 (e))	6,355	640,192	93,335
	191,048	1,148,438	167,433

(b) Investments in affiliated companies accounted for using the equity method as of December 31, 2005 and 2006 are as follows:

	December 31,		
	2005	*2006*	*2006*
	Rmb	**Rmb**	**US$**
Listed:			
TCL (see Note (i))	184,095	385,583	56,215
HLGE (see Note (ii))	—	117,360	17,110
Unlisted:			
Others (see Note (iii))	598	5,303	773
	184,693	508,246	74,098

17 Investments (continued)

(b) Investments in affiliated companies accounted for using the equity method as of December 31, 2005 and 2006 are as follows: (continued)

Notes:

(i) The Company acquired 264,000,000 shares and 17,795,664 shares of TCL's ordinary shares on March 23, 2005 and September 5, 2005, representing 14.99% and 1.00% interests of the enlarged share capital of TCL at a consideration of Singapore dollars ("S$") 30,880,000 (Rmb152,133) and S$1,400,000 (Rmb6,890) respectively. As a result, the Company held a 15.99% equity interest in TCL as of December 31, 2005. Among the 17,795,664 ordinary shares purchased in September 2005, 6,715,196 ordinary shares held by the Company as of December 31, 2005 are subject to a call option which is exercisable by certain members of the Thakral family ("Thakral Family Members"), who are stockholders of TCL.

The option was granted only to Thakral Family Members by the participating creditors in connection with a scheme of arrangement dated October 24, 2001 in relation to TCL sanctioned by the High Court of Singapore on November 2, 2001 ("the Scheme"). The option price payable per TCL share under the call option is S$0.25 plus an interest of Singapore Interbank offer rate plus 0.5% from March 27, 2002 until the completion of the sale and purchase of the shares pursuant to an exercise of the call option. Management assessed the value of the options and determined that it was insignificant. The Thakral Family Members did not exercise the call option, which expired on March 26, 2006.

In February 2006, the Company acquired an additional 3.37% interest in TCL and S$52,933,440 principal amount of convertible bonds of TCL pursuant to a rights issue by TCL for an aggregate cash consideration of S$49.4 million (Rmb243,230). The total purchase consideration has been allocated to the ordinary shares, the bond host instrument and the embedded conversion option based on their respective fair values of S$7 million (Rmb34,626), S$33.3 million (Rmb163,924) and S$9.1 million (Rmb44,680). The Company has separately accounted for the conversion option as an embedded derivative instrument subject to fair value adjustment through earnings. The remaining host instrument of the convertible bonds has been accounted for as an available-for-sale debt security through August 2006, at which time the Company exercised its option and converted the bonds into 529,334,400 ordinary shares of TCL.

Immediately prior to the conversion, the fair value of the bond host instrument had increased by S$3.3 million (Rmb20,942), which was reclassified from "Accumulated other comprehensive income/(loss)" and included as a part of the cost of the additional equity interest in TCL acquired as a result of the conversion. The decrease in fair value of the embedded conversion option of S$1.2 million (Rmb5,662) has been recorded as a charge to the consolidated statement of operations. The fair value of the embedded conversion option immediately prior to the conversion of S$7.9 million (Rmb39,984) has also been included in the cost of the additional interest in TCL. The conversion resulted in CYI increasing its interest in TCL by a further 17.25%. As of December 31, 2006, the Company's equity interest in TCL was 36.61%.

17 Investments (continued)

(b) Investments in affiliated companies accounted for using the equity method as of December 31, 2005 and 2006 are as follows: **(continued)**

Notes: (continued)

As of December 31, 2005 and 2006, the Company's carrying value of its equity method investments in TCL exceeded its underlying equity in TCL's net assets by S$0.2 million (Rmb926) and S$12.8 million (Rmb64,897), respectively, primarily related to the differences between the fair value and book value of certain assets of TCL, which are being amortized over the remaining useful lives of the underlying assets (average of 21 years).

The fair value, based on the quoted market price, of the TCL shares held by the Company was S$80.9 million (Rmb427,489) as of December 31, 2006.

(ii) On February 3, 2006, the Company acquired a portfolio of debt and equity securities of HLGE for an aggregate purchase consideration of approximately S$132 million (Rmb653,178) from several unrelated parties. The portfolio consisted of:

- 191,413,465 ordinary shares, representing 29.13% of the total issued and outstanding ordinary shares of HLGE;
- S$129,428,256 in principal amount of secured bonds ("the Secured Bonds");
- 15,376,318 Series A mandatorily redeemable convertible preference shares of par value S$0.01 each ("RCPS A"); and
- 107,634,237 Series B redeemable convertible preference shares of par value S$0.01 each (RCPS B).

With the investments in the ordinary shares of HLGE, the Company is able to exercise significant influence over the operating and financing policies of HLGE. The investment in the ordinary shares of HLGE has been accounted for under the equity method.

The Secured Bonds have been accounted for as available-for-sale securities.

The Secured Bonds mature in March 2010, and the interest payable on the bonds is calculated based on the actual net cashflows derived from the assets on which the bonds are secured by.

The RCPS A are mandatorily redeemable by HLGE and are more akin to a debt instrument. As such, the conversion option is not clearly and closely related to the host instrument and is therefore accounted for separately as an embedded derivative instrument, subject to the fair value adjustment through earnings. The RCPS A host instrument, other than the embedded conversion option, has been accounted for as an available-for-sale debt security.

(Rmb and US$ amounts expressed in thousands, except per share data)

17 Investments (continued)

(b) *Investments in affiliated companies accounted for using the equity method as of December 31, 2005 and 2006 are as follows:* (continued)

Notes: (continued)

RCPS A is redeemable upon the disposal of certain properties and upon any new issue of HLGE ordinary shares with the purpose of raising funds for the redemption of RCPS A. Any outstanding RCPS A will be mandatorily redeemed in March 2015. RCPS A can also be converted into ordinary shares at the conversion ratio of 1:1 upon the passing of a special resolution at a meeting of the holders of the RCPS A any time prior to March 2015.

The RCPS B are neither mandatorily redeemable nor redeemable at the option of the Company and are akin to an equity instrument. The embedded conversion option is deemed to be clearly and closely related to the host instrument and as the RCPS B's fair value is not readily determinable, the instrument in its entirety has been accounted for under the cost method.

RCPS B is redeemable upon the disposal of certain properties and upon any new issue of HLGE ordinary shares with the purpose of raising funds for the redemption of RCPS B. RCPS B which are not redeemed prior to March 2010, shall be mandatorily converted to ordinary share at the conversion ratio of 1:1 in March 2010. RCPS B can also be converted into ordinary shares at the conversion ratio of 1:1 upon the passing of a special resolution at a meeting of the holders of the RCPS B any time prior to March 2010.

The aggregate purchase consideration of S$132 million was allocated to the above instruments based on their respective fair values as follows:

	Fair value
	S$'000
Secured bonds	109,543
RCPS A	1,948
RCPS A-Embedded equity derivatives	137
RCPS B	7,221
Ordinary shares	12,766
	131,615

In June and December of 2006, HLGE partially redeemed a portion of RCPS A and RCPS B as required by the terms of the preference share agreement as a result of the disposals of certain assets. The proceeds from the partial redemptions amounted to S$2.4 million (Rmb11,907), resulting in a gain of S$1.7 million (Rmb8,907).

17 Investments (continued)

***(b) Investments in affiliated companies accounted for using the equity method as of December 31, 2005 and 2006 are as follows:* (continued)**

Notes: (continued)

On February 28, 2006, HLGE announced a proposed renounceable rights issue of zero coupon unsecured non-convertible bonds due 2009 (the "New Bonds") and non-redeemable convertible cumulative preference shares in the capital of HLGE (the "NCCPS") to raise funds for the purpose of redeeming existing Secured Bonds and for working capital purposes. On July 4, 2006, in connection with the rights issue, the Company was allotted 196,201,374 of NCCPS and S$130,800,917 in principal amount of the New Bonds at a total consideration of S$135 million (Rmb677,010). In conjunction with the allotment, the Secured Bonds were redeemed at their principal value of S$129.4 million.

At the date of settlement, the fair value of the newly acquired NCCPS and New Bonds was S$8 million and S$109.3 million, respectively, the sum of which exceeded the aggregate of the S$5.3 million cash payment by the Company and the fair value of the Secured Bonds of S$109 million, resulting in a net gain of approximately S$3 million. The gain primarily related to an unrealized gain of S$2.3 million (Rmb19,550) immediately prior to the redemption of the Secured Bonds, which had been included in "Accumulated other comprehensive income/ (loss)" and was reclassified and included in "Other income, net" upon redemption.

The New Bonds have been accounted for as available-for-sale debt securities. The investment in NCCPS, which does not have a readily determinable fair value, was accounted for using the cost method. On November 15, 2006, the Company exercised its right to convert all of its 196,201,374 NCCPS into 196,201,374 new ordinary shares of HLGE. As a result of the conversion of the NCCPS, the Company's interest in HLGE has increased to 45.42% of the total issued and outstanding ordinary shares of HLGE.

As of December 31, 2006, the Company's carrying value of its equity method investments in HLGE exceeded its underlying equity in HLGE's net assets by S$29.3 million (Rmb148,043), primarily related to the differences between the fair value and book value of the certain assets and liabilities of HLGE, which will be amortized over the respective periods consistent with the manner in which the underlying assets and liabilities are depreciated or otherwise accreted to HLGE's earnings, as adjustments to the Company's share of earnings and loss of HLGE.

The fair value, based on the quoted market price, of the HLGE ordinary shares held by the Company was S$32.9 million (Rmb166,400) as of December 31, 2006.

(iii) Represents the Company's interests in certain entities in the PRC in which the Company has the ability to exercise significant influence in its financial and operating policy decisions, but do not have the controlling financial interests.

(Rmb and US$ amounts expressed in thousands, except per share data)

17 Investments (continued)

(c) Summarized consolidated financial information regarding TCL as of December 31, 2005 and 2006, and for the period from March 23, 2005 to December 31, 2005, and the year ended December 31, 2006, is as follows:

	December 31,		
	2005	**2006**	**2006**
	Rmb	**Rmb**	**US$**
Financial position			
Current assets	932,008	979,767	142,842
Property, plant and equipment, net	173,266	113,457	16,541
Other assets	453,327	369,498	53,870
Total assets	1,558,601	1,462,722	213,253
Current liabilities	337,971	139,208	20,295
Long term debt	32,076	65,497	9,549
Other non-current liabilities	1,034	—	—
Total liabilities	371,081	204,705	29,844
Minority interests	30,416	27,256	3,974
Stockholders' equity	1,157,104	1,230,761	179,435
Total liabilities, minority interests and stockholders' equity	1,558,601	1,462,722	213,253

(c) Summarized consolidated financial information regarding TCL for the year ended December 31, 2006 and for the period from March 23, 2005 to December 31, 2005 is as follows:

	Period from March 23, 2005 to December 31, 2005	Year ended December 31,2006	
	Rmb	**Rmb**	**US$**
Statement of operations			
Net Sales	1,641,439	1,225,028	178,599
Gross profit	133,192	62,796	9,155
Operating loss	(57,969)	(93,064)	(13,568)
Income tax credit/(expense)	(6,086)	9,089	1,325
Loss before minority interest	(38,206)	(88,337)	(12,879)
Minority interests in income of consolidated subsidiaries	6,232	4,997	729
Net loss	(31,974)	(83,340)	(12,150)
The Company's equity in loss of TCL	(5,982)	(23,923)	(3,488)

The Company's equity in losses of TCL, net of nil tax, is determined as follows:

(Rmb and US$ amounts expressed in thousands, except per share data)

17 Investments (continued)

(c) *Summarized consolidated financial information regarding TCL for the year ended December 31, 2006 and for the period from March 23, 2005 to December 31, 2005 is as follows:* (continued)

	Year ended December 31, 2006
	Rmb
— Based on the respective equity interest during different periods of the year	(24,448)
— Adjustment to account for the basis difference	525
	(23,923)

(d) *Summarized consolidated financial information regarding HLGE as of December 31, 2006, and for the period from February 3, 2006 to December 31, 2006, is as follows:*

	December 31, 2006	
	Rmb	US$
Financial position		
Current assets	390,522	56,935
Property, plant and equipment, net	376,901	54,949
Other assets	127,863	18,641
Total assets	895,286	130,525
Current liabilities	112,372	16,383
Non-current liabilities	850,692	124,024
Total liabilities	963,064	140,407
Stockholders' deficit	(67,778)	(9,882)
Total liabilities and stockholders' deficit	895,286	130,525

	Period from February 3, 2006 to December 31, 2006	Period from February 3, 2006 to December 31, 2006
	Rmb	US$
Statement of operations		
Net Sales	163,968	23,905
Gross profit	91,928	13,402
Operating profit	16,542	2,412
Income tax expense	(6,215)	(906)
Income before minority interest	10,327	1,506
Loss from continuing operations	(21,674)	(3,160)
Income from discontinued operations	44,213	6,446
Net Income	22,539	3,286
The Company's equity in income of HLGE	1,395	203

(Rmb and US$ amounts expressed in thousands, except per share data)

17 Investments (continued)

(d) Summarized consolidated financial information regarding HLGE as of December 31, 2006, and for the period from February 3, 2006 to December 31, 2006, is as follows: **(continued)**

The Company's equity in income of HLGE, net of nil tax, is determined as follows:

	Period from February 3, 2006 to December 31, 2006
	Rmb
— Based on the respective equity interest during the different periods of the year	6,865
— Adjustment to amount for the basis difference	(5,470)
	1,395

(e) Other investments as of December 31, 2006 described above are summarized as follows:

	2005	2006	2006
	Rmb	Rmb	US$
Available for sale securities, at fair value:			
Unsecured bonds	—	589,637	85,964
RCPS A	—	10,646	1,552
Embedded derivatives	—	1,505	219
Investment securities, at cost:			
Unquoted equity securities	6,355	6,355	927
RCPS B	—	32,049	4,673
	6,355	640,192	93,335

Initial fair value, gross unrealized holding gain, gross unrealized holding losses, and period-end fair value of available-for-sale securities as of December 31, 2006, were as follows:

	Initial fair value	Gross unrealized holding gains	Gross unrealized holding (losses)	Carrying value (Fair value)
	RMB	RMB	RMB	RMB
Unsecured bonds of HLGE	534,930	54,707	—	589,637
RCPS A of HLGE	8,513	2,133	—	10,646
	543,443	56,840	—	600,283

The fair values of available-for-sale securities are estimated using the discounted cash flow methodology.

(Rmb and US$ amounts expressed in thousands, except per share data)

17 Investments (continued)

***(e) Other investments as of December 31, 2006 described above are summarized as follows:* (continued)**

Maturities of securities classified as available-for-sale were as follows as of December 31, 2006:

	Initial fair value	***Carrying value (Fair value)***
	Rmb	**Rmb**
Due after one year through five years	534,930	589,637
Due after five years through ten years	8,513	10,646

18 Bank debt

(a) Short-term bank loans

Short-term bank loans are denominated in Renminbi as follows:

	December 31,		
	2005	***2006***	***2006***
	Rmb	**Rmb**	**US$**
Renminbi denominated loans	812,835	806,506	117,581
Singapore dollars denominated loans	—	202,628	29,542
	812,835	1,009,134	147,123

The weighted average interest rate of short-term bank loans at December 31, 2005 and 2006 was 5.52% and 4.05% per annum, respectively.

As of December 31, 2005, short-term bank loans of Rmb42,835, were secured by the pledge of certain Yuchai's trade accounts receivable (see Note 9). The amount was fully repaid in 2006.

As of December 31, 2006, short-term bank loans consist of unsecured loans of Rmb512,628 (US$74,737) and unsecured bonds of Rmb496,506 (US$72,386).

(Rmb and US$ amounts expressed in thousands, except per share data)

18 Bank debt (continued)

(b) Long-term bank loans

Long-term bank loans comprise:

	Interest rate at December 31, 2006	December 31, 2005	December 31, 2006	December 31, 2006
	(per annum)	Rmb	Rmb	US$
Renminbi denominated loans (unless stated):				
— due in 2006	4.94% - 5.49%	100,000	—	—
— due in 2007	5.85%	50,000	—	—
— due in 2008 (US$ denominated loans; multi-currency)	3.83% - 4.01%	—	575,454	83,897
— due in 2010	5.85%	—	100,000	14,579
Total long-term bank loans outstanding		150,000	675,454	98,476
Less: Amounts due within one year included under current liabilities		100,000	—	—
Amounts due after one year		50,000	675,454	98,476

All long-term bank loans are unsecured and have carrying values that approximate their fair values as of December 31, 2005 and 2006.

Notes:

(a) Total bank facilities of Rmb585,653 (US$75,000) and Rmb305,376 (S$60 million) based on historical PBOC exchange rate of 7.8087 and 5.0896 respectively as at 29 December 2006).

(b) US$50.0m credit facility with Sumitomo Mitsui Banking Corporation, Singapore Branch ("Sumitomo"):

On September 7, 2005, in order to fund its business expansion plans, the Company entered into a revolving credit facility agreement with Sumitomo with a committed aggregate value of US$50.0 million for a three years duration. Among other things, the terms of the facility require that Hong Leong Asia Ltd. ("HLA") retains ownership of the Company's special share and that the Company remains a consolidated subsidiary of HLA. The terms of the facility also include certain financial covenants with respect to the Company's tangible net worth (as defined in the agreement) as at June 30 and December 31 of each year not being less than US$120,000 and the ratio of the Company's total net debt (as defined in the agreement) to tangible net worth as at June 30 and December 31 of each year not exceeding 2.0 times, as well as negative pledge provisions and customary drawdown requirements. At all times during the year ended December 31, 2006, the Company was in compliance with these financial covenants. The Company has also undertaken to make available to Sumitomo, within 180 days after the end of its financial year (beginning with financial year 2005), copies of its audited consolidated accounts as at the end of and for that financial year. A waiver from compliance with this undertaking in relation to the production of the 2006 and 2007 audited consolidated accounts has been received from Sumitomo granting an extension of time until July 18, 2008 and September 30, 2008 respectively.

18 Bank debt (continued)

(b) Long-term bank loans (continued)

Notes: (continued)

(c) US$25.0 million credit facility with Bank of Tokyo-Mitsubishi:

On March 23, 2005, in furtherance of its business expansion plans, the Company entered into a revolving credit facility agreement with the Bank of Tokyo-Mitsubishi with a committed aggregate value of US$25.0 million for a three years duration. Among other things, the terms of the facility require that Hong Leong Asia Ltd. ("HLA") retains ownership of the Company's special share and that the Company remains a consolidated subsidiary of HLA. The terms of the facility also include certain financial covenants with respect to the Company's tangible net worth (as defined in the agreement) as at June 30 and December 31 of each year not being less than US$120,000 and the ratio of the Company's total net debt (as defined in the agreement) to tangible net worth as at June 30 and December 31 of each year not exceeding 2.0 times, as well as negative pledge provisions and customary drawdown requirements. At all times during the year ended December 31, 2006, the Company was in compliance with these financial covenants.

(d) S$60.0 million credit facility with Oversea-Chinese Banking Corporation Limited ("OCBC"):

On January 26, 2006, in furtherance of its acquisitions and business expansion plans, the Company entered into a revolving credit facility agreement with OCBC with a committed aggregate value of S$60.0 million for a period of 18 months. Among other terms, the terms of the facility require that Hong Leong Asia Ltd. ("HLA") retains ownership of the Company's special share and that the Company remains a consolidated subsidiary of HLA. The terms of the facility also include certain financial covenants with respect to the Company's tangible net worth (as defined in the agreement) as at 30 June and 31 December of each year not being less than US$120,000, and the ratio of the Company's total net debt (as defined in the agreement) to tangible net worth as at 30 June and 31 December of each year not exceeding 2.0 times, as well as negative pledge provisions and customary drawdown requirements. At all times during the year ended December 31, 2006, the Company was in compliance with these financial covenants."

19 Convertible debt

On February 23, 2005, the Company issued US$25,000 (Rmb206,913) in principal amount of convertible debt on a private placement basis. The convertible debt bears an interest rate of 2% per annum and mature in 2012, unless redeemed earlier in accordance with the terms of the convertible debt. The convertible debt was converted to 1,927,673 ordinary shares on June 3, 2005, thereby increasing the Company's issued and outstanding shares from 35,340,000 ordinary shares to 37,267,673 ordinary shares.

(Rmb and US$ amounts expressed in thousands, except per share data)

20 Accrued expenses and other liabilities

Accrued expenses and other liabilities comprise:

	December 31,		
	2005 Rmb	2006 Rmb	2006 US$
Deposits from customers	96,936	57,577	8,394
Staff welfare payable (see Note (i))	15,041	15,041	2,193
Accrued product warranty (see Note 21)	142,126	163,701	23,866
Wages payable	107,130	127,382	18,571
Management bonus payable	8,158	15,035	2,192
Payable for construction in progress	39,330	49,147	7,165
Accrued research and development expenses	24,952	26,947	3,929
Accrued advertising expense	3,817	4,165	607
Accrued legal fee and other professional fees	5,050	3,421	499
Accrued expenses for litigation and guarantees (see Notes 24(c) and (d))	18,921	7,849	1,144
Individual income tax withholding	10,250	3,890	567
Accrued sales discount	45,741	59,769	8,714
Accrued interest	—	2,749	401
Other payables	8,014	20,764	3,027
Accrued retirement benefits	5,747	5,747	838
Other accruals and liabilities	80,494	76,166	11,105
	611,707	639,350	93,212

Note (i): Staff welfare payable is determined by Yuchai's Board of Directors. The payable can be applied towards the payment of special bonuses or collective welfare benefits to staff and workers of Yuchai, such as staff dormitories and staff welfare facilities.

21 Accrued product warranty

An analysis of the accrued product warranty for 2004, 2005 and 2006 is as follows:

	December 31,			
	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Balance at beginning of year	101,215	126,114	142,126	20,721
Allowance charged to consolidated statements of operations	190,205	179,184	200,892	29,288
Less: Amounts utilized	(165,306)	(163,172)	(179,317)	(26,143)
Balance at end of year	126,114	142,126	163,701	23,866

(Rmb and US$ amounts expressed in thousands, except per share data)

22 Statutory reserves

The Company's attributable share in the statutory reserves of Yuchai and its subsidiaries for the three years ended December 31, 2006 is as follows:

	December 31,			
	2004	**2005**	**2006**	**2006**
	Rmb	**Rmb**	**Rmb**	**US$**
Statutory general reserve (see Note (ii))				
Balance at January 1	156,111	170,041	170,280	24,825
Transfer from retained earnings	13,930	239	1,000	146
Balance at December 31	170,041	170,280	171,280	24,971
Statutory public welfare fund (see Note (iii))				
Balance at January 1	48,103	70,482	70,600	10,293
Transfer from retained earnings	22,379	118	—	—
Balance at December 31	70,482	70,600	70,600	10,293
General surplus reserve				
Balance at January 1 and December 31	25,706	25,706	25,706	3,748
Total	266,229	266,586	267,586	39,012

Notes:

(i) In accordance with the relevant regulations in the PRC, Yuchai and its subsidiaries are required to provide certain statutory reserves which are designated for specific purposes based on the net income reported in the PRC GAAP financial statements. The reserves are not distributable in the form of cash dividends (see Note 30).

(ii) In accordance with the relevant regulations in the PRC, a 10% appropriation to the statutory general reserve based on the net income reported in the PRC financial statements is required until the balance reaches 50% of the authorized share capital of Yuchai and its subsidiaries. Statutory general reserve can be used to make good previous years' losses, if any, and may be converted into share capital by the issue of new shares to stockholders in proportion to their existing shareholdings, or by increasing the par value of the shares currently held by them, provided that the reserve balance after such issue is not less than 25% of the authorized share capital.

(iii) Yuchai and its subsidiaries shall determine to transfer 5% to 10% of its net income reported in the PRC financial statements to the statutory public welfare fund. There is no limit on the amount that may be allocated to this fund. This fund can only be utilized on capital expenditure for the collective welfare of Yuchai and its subsidiaries' employees, such as the construction of dormitories, canteen and other welfare facilities, and cannot be utilized to pay staff welfare expenses. The transfer to this fund must be made before the distribution of a dividend to stockholders. Since January 1, 2006, in accordance with the amended Company's policy, the contribution to the fund ceased. The fund balance as at December 31, 2005 was carried forward to the statutory reserves in 2006.

(Rmb and US$ amounts expressed in thousands, except per share data)

23 Commitments

At December 31, 2006, Yuchai had the following commitments:

	December 31,	
	2006	***2006***
	Rmb	**US$**
Authorized and contracted for:		
Improvement to existing production facilities	126,961	18,510

The Group has several non-cancellable operating leases, primarily for offices and warehouses that expire over the next four years. These leases generally contain renewal options for periods ranging from one year to four years.

Future minimum lease payments under non-cancellable operating leases (with initial or remaining lease terms in excess of one year) as of December 31, 2006 are:

	Rmb	**US$**
2007	4,355	635
2008	2,106	307
2009	1,157	169
2010	480	70
2011	—	—
	8,098	1,181

Rental expense for operating leases is included in “Selling, general and administrative expenses” as follows:

	December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Rental expense	9,232	8,726	10,113	1,474

24 Contingencies

(a) Product liability

The General Principles of the Civil Law of China and the Industrial Product Quality Liability Regulations imposes that manufacturers and sellers are liable for loss and injury caused by defective products. Yuchai and its subsidiaries do not carry product liability insurance. Yuchai and its subsidiaries have not had any significant product liability claims brought against them.

24 Contingencies (continued)

(b) Environmental liability

China adopted its Environmental Protection Law in 1989, and the State Council and the State Environmental Protection Agency promulgate regulations as required from time to time. The Environmental Protection Law addresses issues relating to environmental quality, waste disposal and emissions, including air, water and noise emissions. Environmental regulations have not had a material impact on Yuchai's results of operations. Yuchai delivers, on a regular basis, burned sand and certain other waste products to a waste disposal site approved by the local government and makes payments in respect thereof. Yuchai expects that environmental standards and their enforcement in China will, as in many other countries, become more stringent over time, especially as technical advances make achievement of higher standards more feasible. Yuchai has built an air filter system to reduce the level of dust and fumes resulting from its production of diesel engines. The PRC emission standard equivalent to Euro III is expected to be implemented progressively throughout China from 2008. Yuchai believes it will be able to comply with the new standard.

In addition, the manufacture and sales of EURO 0 and Euro I engines in major urban area became unlawful after August 31, 2004. After that date, the engines equipped with EURO 0 and Euro I engines cannot be sold and used in major urban area.

Yuchai is subject to Chinese national and local environmental protection regulations which currently impose fees for the discharge of waste substances, require the payment of fines for pollution, and provide for the closure by the Chinese government of any facility that fails to comply with orders requiring Yuchai to cease or improve upon certain activities causing environmental damage. Due to the nature of its business, Yuchai produces certain amounts of waste water, gas, and solid waste materials during the course of our production. Yuchai believes its environmental protection facilities and systems are adequate for it to comply with the existing national, provincial and local environmental protection regulations. However, Chinese national, provincial or local authorities may impose additional or more stringent regulations which would require additional expenditure on environmental matters or changes in our processes or systems.

(c) Dispute with Bank of China

In 2003, the Yulin Branch of Bank of China ("BOC") initiated legal proceedings to recover Rmb6,603 (US$963) from Yuchai based on an irrevocable letter of guarantee issued by Yuchai to the BOC in 1993 to secure a loan of US$550 to Great Wall Machinery Plant ("Great Wall"). At trial, a Yulin court ruled that if Great Wall could not pay the loan, Yuchai would be liable to pay the guaranteed sum to the BOC. Yuchai appealed unsuccessfully.

In January 2004, the State Holding Company issued a letter of commitment confirming that it would reimburse Yuchai in the event that Yuchai was required to pay on this guarantee.

Based on the advice from the Company's Legal Counsel, the Company has recorded a loss contingency equal to the amount of the claim. The amounts due to the BOC and from the State Holding Company have been recorded in "Accrued expenses and other liabilities" and "Amounts due from related parties", respectively.

In 2005 and 2006, there were no new developments in this case.

24 Contingencies (continued)

(d) Guarantees

YEGCL provides guarantees of loans granted by commercial banks in the PRC to unrelated third-party individuals who have obtained the loans to purchase automobiles equipped with diesel engines produced by Yuchai. During the years ended December 31, 2004, 2005 and 2006, YEGCL guaranteed borrowings of Rmb7,422, Rmb153,538 and Rmb88,991 (US$12,974), respectively. YEGCL did not issue any such guarantees prior to 2004. The guarantees cover the entire principal amount of the loan, which generally has a term of one to two years with equal monthly or quarterly installment payments by the borrower. The guarantees are secured by cash deposits from the individual to YEGCL and by the automobile. In the event of defaults on payment, YEGCL would be required under its guarantee to make payments to the banks on behalf of the borrowers.

In return for issuing the guarantee, YEGCL receives a premium fee ranging from 2% to 8% of the loan amount for the years ending December 31, 2005 and 2006, respectively, which is considered to be the fair value of YEGCL's guarantee at its inception and is recorded as a liability in accordance with the provisions of FIN 45. The Group received Rmb239, Rmb4,268 and Rmb4,250 (US$620) of premium fees in 2004, 2005 and 2006, respectively, which are included in "Accrued expenses and other liabilities" and recognized as revenue on a straight line basis over the terms of the respective guarantee. Guarantee fee recognized as revenue in 2004, 2005 and 2006 amounted to Rmb14, Rmb1,167 and Rmb4,718 (US$688), respectively. As of December 31, 2004, 2005 and 2006, deferred guarantee fee revenue amounted to Rmb224, Rmb3,326 and Rmb2,858 (US$417), respectively.

Subsequent to initial measurement and recognition of the liability for YEGCL's obligations under with these loan guarantees, management evaluates YEGCL's guarantee portfolio and accounts for potential loss contingencies associated with the guarantees based on the estimated losses resulting from known and expected defaults. Each guarantee is secured by a cash deposit from the borrower and a security interest in the automobile purchased by the borrower. As of December 31, 2005 and 2006, YEGCL had gross receivables of Rmb3,257 and Rmb26,896 (US$3,921), respectively, relating to payments made by YEGCL to the banks in conjunction with loans that had been defaulted and to be recovered from the individual borrowers. YEGCL recorded a bad debt allowance in the amount of Rmb1,253 and Rmb12,467 (US$1,818) at December 31, 2005 and 2006 respectively. The net receivable amount of Rmb2,004 (US$249) and Rmb15,189 (US$2,214), is included in "Other receivables" in the accompanying consolidated balance sheets (See Note 13).

As of December 31, 2005 and 2006, the maximum potential amount future undiscounted payments YEGCL could be required to make under the guarantees was Rmb134,235 and Rmb132,345 (US$19,295), respectively. YEGCL held cash deposits of Rmb6,904 and Rmb12,389 as of December 31, 2005 and 2006 and security interests in automobiles with an aggregate initial purchase value of Rmb242,216 and Rmb431,781 as of December 31, 2005 and 2006, respectively. If, in the event of default the cash deposits and the amount of recoveries, if any, from repossession of the automobiles may not entirely mitigate YEGCL's losses then, YEGCL accumulates the total expected risk against the total expected recoverable amount and provides for any expected shortfall. Accordingly, management recorded an accrual for potential losses associated with the guarantees in the amount of Rmb12,318 and Rmb2,611 (US$381) as of December 31, 2005 and 2006, respectively, included in "Accrued expenses and other liabilities".

(Rmb and US$ amounts expressed in thousands, except per share data)

24 Contingencies (continued)

An analysis of reserves for potential losses associated with the guarantees including amounts paid to banks in connection with guarantees issued by YEGCL is as follows:

	December 31		
	2005 Rmb	2006 Rmb	2006 US$
Balance at beginning of year	—	13,571	1,979
Charged to consolidated statements of operations	13,571	1,507	220
Balance at end of year	13,571	15,078	2,199
Balance allocated to:			
Allowance for uncollectible other receivables	1,253	12,467	1,818
Potential losses associated with the guarantees	12,318	2,611	381
	13,571	15,078	2,199

(e) Outstanding bank bills discounted

As of December 31, 2006, outstanding bills receivable discounted with banks for which the Group has retained a recourse obligation totaled Rmb1,848,438 (US$269,487). Management has assessed the fair value of the recourse obligation arising from these discounted bank bills to be immaterial based on the Company's default experience and the credit status of the issuing banks.

(f) Outstanding letters of credit

As of December 31, 2006, the Group issued irrevocable letters of credit totaled Rmb34,769 (US$5,069).

(g) Other outstanding litigation

In addition to the matters disclosed in Note 24(c), the Group is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations, or liquidity.

25 Dispute with State Holding Company

The Company has from time to time in the period up to 2006 encountered difficulties in obtaining the cooperation of the State Holding Company, and its former Chairman, Mr. Wang Jianming, in the daily management and operation of Yuchai, including obtaining payments of the Company's share of the final 2001 dividend declared in August 2002. Mr. Wang Jianming ceased to serve as the Chairman, legal representative and chief executive officer of Yuchai, as well as the Chairman and legal representative of the State Holding Company, the principal Chinese shareholder of Yuchai with effect from October 28, 2005. The new Chairman and legal representative of these companies is Mr. Yan Ping whose appointment was confirmed on December 2, 2005.

25 Dispute with State Holding Company (continued)

The Chinese stakeholders had previously asserted that the transfer of ownership of shares with respect to Yuchai in November 1994, in connection with the Company's initial public offering ("IPO"), was not validly approved by the Chinese authorities, and that as a result the Company's exercise of control over Yuchai has been improper.

As a result of a number of meetings between the parties, the Company and Yuchai entered into an agreement in July 2003 (the "July 2003 Agreement") to work together in trying to jointly promote mutual plans to enhance the Company's shareholder value.

On April 7, 2005, the Company entered into a Reorganization Agreement ("Reorganization Agreement") with Yuchai and Coomber in furtherance of the terms of the July 2003 Agreement, and the terms of this agreement were acknowledged and agreed to by the State Holding Company. The Reorganization Agreement was extended to December 31, 2006 by way of the Reorganization Agreement Amendment No.1 dated December 2, 2005 and then extended to June 30, 2007 by way of the Reorganization Agreement Amendment No.2 dated November 30, 2006. The Reorganization Agreement Amendments No.1 and No.2 were similarly acknowledged and agreed to by the State Holding Company.

On June 30, 2007, the Company entered into the Cooperation Agreement with Yuchai, Coomber and the State Holding Company. The Cooperation Agreement amends certain terms of the Reorganization Agreement, as amended, among CYI, Yuchai and Coomber, and as so amended, incorporates the terms of the Reorganization Agreement. The Reorganization Agreement was terminated on June 30, 2007. The Cooperation Agreement provides that the parties will explore new business opportunities and ventures for the growth and expansion of Yuchai's existing businesses. Although the parties to the Cooperation Agreement expect to work towards its implementation as expeditiously as possible, no assurance can be given as to when the transactions contemplated therein will be consummated.

The principal terms contained in the Reorganization Agreement Amendments No.1 and No.2 and the Co-operation Agreement relating to governance related issues are being adhered to by Yuchai.

26 Retirement and other postretirement benefits

As stipulated by the regulations of the PRC, Yuchai and its subsidiaries participate in defined contribution retirement plans organized by the Guangxi Regional Government and Beijing City Government for its staff. All staff are entitled to an annual pension equal to a fixed proportion of their final basic salary amount at their retirement date. For the years ended December 31, 2004, 2005 and 2006, Yuchai and its subsidiaries were required to make contributions to the retirement plan at a rate of 20.0% of the basic salary of their staff. The Guangxi Regional Government and Beijing City Government are responsible for the entire obligations of all Yuchai and its subsidiaries' retirees. Expenses incurred in connection with the plan were Rmb29,868, Rmb33,299 and Rmb42,254 (US$6,160), respectively, for the years ended December 31, 2004, 2005 and 2006.

Yuchai and its subsidiaries have no obligation for the payment of pension benefits or any other postretirement benefits beyond the annual contributions described above.

(Rmb and US$ amounts expressed in thousands, except per share data)

27 Other related party transactions

In addition to the loans to YMLC and interest income from (as discussed in Note 5), the Group has undertaken other significant business transactions with related parties during the three years ended December 31, 2006. The following is a summary of these transactions:

	Years ended December 31,			
	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Sales of trucks from customers to Guangxi Yuchai Mechanical and Electronics Company ("GYMEC") (see Note (i))	753	—	—	—
Sales of diesel engines to State Holding Company, its subsidiaries and affiliates (see Note (ii))	3,784	7,646	20,923	3,050
Sales of raw materials to YMLC (see Note (ii))	—	—	65,729	9,583
Purchase of raw materials and supplies from subsidiaries and affiliates of State Holding Company (see Note (ii))	(142,829)	(235,329)	(377,129)	(54,982)
Purchase of raw materials and supplies from YMLC (see Note (iii))	—	(60,756)	(201,802)	(29,421)
Purchase of trucks from YMLC (see Note (iii))	(95,391)	(77,324)	—	—
Processing fee to YMLC (see Note (iv))	(12,329)	(44,407)	(13,604)	(1,983)
Delivery expense charged by a subsidiary of YMLC (see Note (iv))	(65,468)	(126,028)	(90,840)	(13,244)
General and administrative expenses				
— charged by State Holding Company (see Note (v))	(21,180)	(25,931)	(19,821)	(2,890)
— charged by HLA	(4,142)	(4,035)	(4,061)	(592)
— charged by an affiliate of HLA (see Note (vi))	—	(30,765)	(9,654)	(1,408)

	Years ended December 31,			
	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Gain on disposal of land use rights to a subsidiary of State Holding Company (See Note (vii))	—	2,533	1,841	268

Notes:

(i) Sales of diesel trucks to GYMEC

GYMEC was formerly a subsidiary of State Holding Company. It became a subsidiary of YMLC following a share transfer from State Holding Company to YMLC in 2004. During 2003 and 2004, Yuchai received diesel trucks from certain customers as part of the settlement of their trade accounts receivable. Pursuant to an agreement between Yuchai and GYMEC, Yuchai sold such diesel trucks at cost to GYMEC, which owns a business license for selling diesel trucks in the PRC. Yuchai recorded a receivable from GYMEC in connection with the truck sales. The amount due from GYMEC is unsecured, interest free and repayable on demand.

27 Other related party transactions (continued)

Notes: (continued)

(ii) Sale and purchase of raw materials, supplies, scraps and diesel engines to/from State Holding Company, its subsidiaries and affiliates.

Certain subsidiaries and affiliates of State Holding Company have acted as suppliers of raw materials and supplies to the Company and certain subsidiaries of State Holding Company have acted as sales agents of the Group. The State Holding Company also purchased scraps from the Group. Management considers that these transactions were entered into in the normal course of business and expects that these transactions will continue on normal commercial terms.

(iii) Purchase of raw materials, supplies and trucks from YMLC

From July 2004 to April 2006, subsidiaries of YMMC engaged in the sale of trucks which were mainly supplied by and purchased from YMLC. YMLC has also become a supplier of raw materials and supplies to the Group since 2005. Management considers that these transactions were entered into in the normal course of business. In April 2006, the above procurement and distribution arrangement between GYMCL and YMLC was stopped and YMLC sold the remaining inventory and some ancillary fixed assets back to YMMC.

(iv) Processing fee and delivery expense charged by YMLC and its subsidiaries

The fee is for the packaging and delivery of spare parts charged by YMLC, which were recorded in "Cost of goods sold" and "Selling, general and administrative expenses" respectively. Management considers that these transactions were entered into in the normal course of business and these transactions continued on normal commercial terms until April 2006 when YMLC ceased operation.

(v) General and administrative expenses

State Holding Company charges Yuchai for certain general and administrative expenses in respect of rental of certain office premises, property management services rendered by State Holding Company. The expenses are charged to Yuchai and its subsidiaries by State Holding Company on an actual incurred basis. Management believes that the expenses charged to Yuchai by State Holding Company would not have been materially different on a stand-alone basis because Yuchai could provide these services for itself at approximately the same amount.

(vi) Service fee to an affiliate of HLA

The fee was paid to Hong Leong Management Services Pte Ltd., an affiliate of HLA. Service fee includes Rmb9,654 (US$1,211) in relation to the consultancy services performed for the acquisition of interests in TCL during 2005 and HLGE in 2006 . The remaining amounts were mainly in relation to securing additional credit facilities and entering into the Reorganization Agreement. The transactions were approved by the Board of Directors. Management considers that the transactions were entered into in the normal course of business.

27 Other related party transactions (continued)

Notes: (continued)

(vii) Gain on disposal of land use rights to a subsidiary of State Holding Company

The Group has disposed of certain land use rights with net book value of Rmb1,047 and Rmb552 (US$81) to a subsidiary of SHC for a consideration of Rmb3,580 and Rmb2,393 (US$349) in the years ended December 31, 2005 and 2006 respectively.

(viii) Amounts due from/to related parties

Amounts due from/to related parties arise mainly from the transactions as stated above.

In addition to the above, Yuchai also entered into transactions with other PRC Government owned enterprises. Management considers that these transactions were entered into in the normal course of business and expects that these transactions will continue on normal commercial terms. Balances with other PRC entities are excluded from this caption.

(ix) Amounts due to the holding company

Amounts due to the holding company comprise mainly general and administrative expenses charged by the holding company in relation to the management, financial planning and control and other services provided to Yuchai. The balance is unsecured, interest free and repayable on demand.

28 Segment information

SFAS No. 131, “Disclosures about Segments of an Enterprise and Related Information”, establishes standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance.

The Company’s operating segments are Yuchai, HLGE and TCL for the year ended December 31, 2006. The Company’s operating segments were Yuchai, HLGE and TCL for the year ended December 31, 2005. Prior to the purchase of TCL, the Company’s only operating segment was Yuchai.

The segment result for Yuchai is based on income before income taxes and minority interests. The segment result for TCL is the Company’s equity in the net income or losses or TCL. Segment assets for Yuchai are based on total assets of Yuchai. Segment assets for TCL are based on the Company’s net investment in TCL. Substantially all of the Company’s operations including TCL are in the PRC. Consequentially no geographic information is presented. Further segment information about TCL is included in Note 17(c).

(Rmb and US$ amounts expressed in thousands, except per share data)

28 Segment information (continued)

Following is the segment information for the years ended December 31, 2005 and 2006:

	2004	2005		2006		
	Yuchai	Yuchai	TCL	Yuchai	TCL	HLGE
	Rmb	Rmb	Rmb	Rmb	Rmb	Rmb
Segment revenue from external customers	5,582,095	5,816,740	—	6,920,528	—	—
Interest revenue	3,286	21,744	—	47,124	—	—
Interest expense	31,757	70,527	—	117,491	—	—
Depreciation and amortization	132,789	144,672	—	146,188	—	—
Equity in losses of affiliates		50	—	80	—	—
Segment profit / (loss)	753,854	30,179	(5,982)	294,782	(23,923)	1,395
Significant non-cash items:						
— Provision for uncollectible loans to a related party	—	202,950	—	—	—	—
— Bad debt expense	13,034	25,587	—	16,358	—	—
— Provision for inventory write-down	9,546	15,990	—	89,404	—	—
— Provision / (write back) for losses on guarantees	—	12,318	—	(7,410)	—	—
Segment assets	5,268,660	6,235,585	184,095	6,479,886	385,583	117,360
Total expenditures for additions to long-lived assets	552,902	515,359	—	323,781	—	—

Reconciliation of segment information to the consolidated financial statements for the years ended December 2004, 2005 and 2006.

	2004	2005	2006
	Rmb	Rmb	Rmb
Total segment profit	773, 571	24,197	272,254
Service fee to an affiliate of HLA (see Note 27)	—	(30,765)	(9,654)
Other corporate general and administrative expenses	(19,717)	(18,522)	(59,205)
Consolidated income/(loss) before income taxes and minority interests	753,854	(25,090)	203,395
Total segment assets	5,268,660	6,419,680	6,982,828
Corporate cash and cash equivalents	108,514	247,332	100,990
Other corporate assets	7,074	12,618	877,539
Consolidated total assets	5,384,248	6,679,630	7,961,357

(Rmb and US$ amounts expressed in thousands, except per share data)

28 Segment information (continued)

Revenues from external customers by product category are summarized as follows:

	Years ended December 31,			
	2004	***2005***	***2006***	***2006***
	Rmb	**Rmb**	**Rmb**	**US$**
Revenues, net				
4F Light-Duty Diesel Engines	—	—	264,335	38,538
4108 Light-Duty Diesel Engines	325,242	634,532	941,657	137,286
4110 Light-Duty Diesel Engines	544,297	595,239	644,116	93,907
4112 Light-Duty Diesel Engines	314,453	321,548	372,423	54,296
6105 Medium-Duty Diesel Engines	1,143,535	1,744,953	1,705,399	248,633
6108 Medium-Duty Diesel Engines	1,372,073	809,054	991,190	144,507
6112 Heavy-Duty Diesel Engines	1,203,558	785,236	725,288	105,741
6113 Heavy-Duty Diesel Engines	97,368	192,850	365,717	53,319
Diesel Engine Parts	446,135	488,414	875,453	127,634
Others *	135,434	244,914	34,950	5,095
	5,582,095	5,816,740	6,920,528	1,008,956

* Others mainly represent the revenues earned through sales of motor vehicle chassis and power generators, and from guarantee fees.

29 Foreign currency exchange

The Renminbi is not fully convertible into foreign currencies. All foreign exchange transactions involving Renminbi must take place either through the PBOC or other institutions authorized to buy and sell foreign exchange. The exchange rate adopted for the foreign exchange transactions is the rate of exchange quoted by the PBOC which are determined largely by supply and demand.

Foreign currency payments, including the remittance of earnings outside of the PRC, must be arranged through banks authorized to conduct foreign exchange business.

30 Distribution of profits

The Group's sources of cash flow are its share of the dividends, if any, paid by Yuchai, HLGE and TCL to the Company. With respect to dividends by Yuchai, applicable PRC laws and regulations require that, before it can distribute profit to its stockholders it must satisfy all tax liabilities, recover losses in previous years and make contributions to certain statutory reserves as discussed in Note 22. Such dividends may be paid partly in Renminbi and partly in foreign currency. In the event that dividends are distributed in Renminbi, the dividends may be converted into foreign currency and remitted in accordance with relevant PRC laws, regulations and policies and to the extent permitted by PRC market conditions. Dividends of Yuchai are determined based on distributable profits reported in its PRC GAAP financial statements, after appropriation to statutory reserves. Such distributable profits differ from the amounts reported under U.S. GAAP. No similar provisions were imposed with respect to dividends by TCL and HLGE.

Under the Companies Act of 1981 of Bermuda (as amended), the Company's contributed surplus is available for distribution to stockholders.

31 Derivative instrument and hedging activities

For the periods presented, the Company and its subsidiaries did not enter into transactions with respect to derivative instruments. The Company and its subsidiaries do not hedge risk exposures or speculate using derivative instruments.

32 Fair value of financial instruments

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties. The carrying amount of cash and cash equivalents, trade accounts receivable, bills receivable, short term amounts due from related parties, prepaid expenses, other receivables, short-term bank loans, current instalments of long-term bank loans, trade accounts payable, amount due to the holding company and amounts due to related parties approximates their fair value because of the short maturity of these instruments. It was not practicable for management to estimate the fair value of its equity investments for which a quoted market price is not available because it has not yet obtained or developed the valuation model necessary to make the estimate, and the cost of obtaining an independent valuation is considered excessive in relation to the significance of the equity investments to the Group. Management does not believe the carrying value of the equity investments will be significantly different from its fair value. Management estimated the fair value of its equity investments by obtaining an independent valuation of the investments by a professional valuer.

The carrying amount of long-term bank loans approximates their fair value based on the borrowing rates currently available for bank loans with similar terms and average maturities.

(Rmb and US$ amounts expressed in thousands, except per share data)

33 Significant concentrations and risks

(a) Customer concentration

Substantially all of the Group's customers are located in the PRC. The following are the customers that individually comprise 10% or more of gross revenue in any of the relevant periods:

	Years ended December 31,			
	2004 Rmb	2005 Rmb	2006 Rmb	2006 US$
Liuzhou Dongfeng Automobile (see Note (i))	830,018	385,049	453,090	66,057
Hubei Dongfeng Automobile (see Note (ii))	344,910	333,452	238,400	34,757

Notes:

(i) Sales to Liuzhou Dongfeng Automobile for the year ended December 31, 2004, 2005 and 2006 was approximately 14.9%, 6.6% and 6.5% of total sales.

(ii) Sales to Hubei Dongfeng Automobile for the year ended December 31, 2004, 2005 and 2006 was approximately 6.2%, 5.7% and 3.4% of total sales.

All the above customers are controlled by or affiliated with Dongfeng Automobile Company. At December 31, 2005 and 2006, approximately 13% and 22% of gross trade accounts receivable, respectively, were due from these customers. Management considers its relationships with these major customers to be good; however, the loss of one or more of the Group's major customers would have a material adverse effect on the Company's consolidated financial position, results of operations and cash flows.

(b) Nature of operations

During periods of economic expansion, the demand of trucks, construction machinery and other application of diesel engines generally increases. Conversely, during economic slowdowns the diesel engine industry is generally adversely affected by a decline in demand. As a result, the performance of Chinese economy will affect the Group's business and prospects by a significant degree.

(Rmb and US$ amounts expressed in thousands, except per share data)

33 Significant concentrations and risks (continued)

(c) Transactions involving Yuchai's Chinese shareholders

Although the Company has proper legal ownership over and a controlling financial interest of 76.41% interest in Yuchai, the Company has from time to time encountered difficulties in obtaining the cooperation of the State Holding Company and Coomber. As part of the terms of the Reorganization Agreement as described in Note 25, Yuchai and State Holding Company acknowledged and reaffirmed the Company's continued rights as majority shareholder to direct the management and policies of Yuchai through Yuchai's board of directors. However, no assurance can be given that disagreements or difficulties with Yuchai's management of State Holding Company and Coomber will not recur. In addition, as described in Note 5, Yuchai has entered into transactions that involved the Chinese Shareholders that have resulted in losses. No assurance can be given that future transactions involving the State Holding Company, Coomber and their related parties will be conducted on an arm-length basis or otherwise be beneficial to the Company. Consequently, such disagreements, or difficulties and transactions involving State Holding Company, Coomber and their related parties could have a material adverse impact on the Company's consolidated financial position, operating results and cash flows.

On June 30, 2007, we entered into the Cooperation Agreement with Yuchai, Coomber and the State Holding Company. The Cooperation Agreement amends certain terms of the Reorganization Agreement, as amended, among CYI, Yuchai and Coomber, and as so amended, incorporates the terms of the Reorganization Agreement. The Reorganization Agreement was scheduled to terminate on June 30, 2007.

The Cooperation Agreement provides that the parties will explore new business opportunities and ventures for the growth and expansion of Yuchai's existing businesses. Although the parties to the Cooperation Agreement expect to work towards its implementation as expeditiously as possible, no assurance can be given as to when the transactions contemplated therein will be consummated.

(d) Cash and cash equivalents

Cash and cash equivalents denominated in various currencies are held in bank accounts in the following countries:

	December 31			
	2005 Rmb PRC	2005 Rmb Singapore	2006 Rmb PRC	2006 Rmb Singapore
Rmb	488,863	—	644,944	—
USD	—	245,814	—	99,506
SGD	—	1,518	—	1,483
	488,863	247,332	644,944	100,989

34 Subsequent events

(a) New joint ventures

On April 10, 2007, Yuchai signed a Cooperation Framework Agreement with Zhejiang Geely Holding Group Co., Ltd ("Geely") and Zhejiang Yinlun Machinery Co., Limited ("Yinlun") to consider establishing a proposed joint venture company to develop diesel engines for passenger cars in China. The location of the proposed joint venture was to be at Tiantai, Zhejiang Province in China. Yuchai was to be the largest shareholder followed by Geely as the second largest shareholder. In December 2007, further to the Cooperation Framework Agreement, Yuchai entered into an Equity Joint Venture Agreement with Geely and Yinlun, to form two joint venture companies in Tiantai, Zhejiang Province and Jining, Shandong Province. The joint venture companies ("JV Cos") will be primarily engaged in the development, production and sales of a proprietary diesel engine and its parts for passenger vehicles. The main product is a 4D2.0L diesel engine and the technology for this new diesel engine will be purchased by the JV Cos from Geely subject to certain specified design technology standards being met. The total design production capacity of both JV Cos will be 300,000 diesel units, with each JV Co starting with a capacity for 50,000 diesel engine units and then adding capacity to reach 150,000 units annually. Yuchai will be the controlling shareholder with 52% with Geely and Yinlun holding 30% and 18% shareholding respectively in both JV Cos.

(b) Purchase of Guangxi Yulin Hotel Company Ltd

During 2004, Yuchai granted loans of Rmb 205 million to YMLC, a subsidiary of Coomber, with an interest rate of 5.58% for one year. The loans were guaranteed by Coomber and the State Holding Company as guarantors (together, the "Guarantors"). The loans were repaid in 2005 and were subsequently re-loaned with a maturity date of June 1, 2007 and further extended to May 30, 2008. In July 2007, Yuchai's Board of Director's agreed in principle to a proposal by the State Holding Company to settle the amount due from YMLC, along with various other amounts receivable from YMLC (collectively, the "receivables"), by forgiving the receivables in exchange for the transfer of ownership of a hotel in Yulin, PRC and YMLC's central office building in Guilin, PRC. Yuchai has, pursuant to a share transfer contract acquired all the outstanding share capital of Guangxi Yulin Hotel Company Ltd ("Yulin Hotel Company") for Rmb 245.6 million in repayment of the Rmb 205 million loan. The balance of the consideration payable for the purchase of Yulin Hotel Company will be offset against certain trade receivables due from YMLC, the Guarantors and other related parties. The acquisition by Yuchai of Yulin Hotel Company was ratified by the Board of Directors of Yuchai and its shareholders subject to the original shareholders of Yulin Hotel Company obtaining approval for the transaction from the regulatory agency in China by November 30, 2008. If such approval from the regulatory agency in China is not obtained by November 30, 2008, Yuchai has the right to sell to the State Holding Company, who shall be obligated to buy, 100% of the equity in Yulin Hotel Company at the original purchase price of Rmb 245.6 million as set out in the share transfer contract. In the event that Yuchai elects to exercise this option and should the State Holding Company be unable to pay the entire purchase price of Rmb 245.6 million, whether in cash or in kind, the Company may have to make a provision for such amount as necessary. This condition is contained in the guarantee letter provided by the original shareholders of Yulin Hotel Company. As a result of the acquisition of 100% equity of Yulin Hotel Company, the loan agreements with YMLC have been terminated and the guarantees provided by the Guarantors have been discharged.

34 Subsequent events (continued)

(c) Co-operation Agreement

On June 30, 2007, the Company entered into the Cooperation Agreement with Yuchai, Coomber and the State Holding Company. The Cooperation Agreement amended certain terms of the Reorganization Agreement, as amended, and as so amended, incorporated the terms of the Reorganization Agreement. The Reorganization Agreement was scheduled to terminate on June 30, 2007.

The Cooperation Agreement provides that the parties will explore new business opportunities and ventures for the growth and expansion of Yuchai's existing businesses. Pursuant to the amendments to the Reorganization Agreement, the Company agreed that the restructuring and spin-off of Yuchai would not be pursued, recognizing the understandings that were reached between the Company and the State Holding Company to jointly undertake efforts to expand the business of Yuchai, the Company would not seek to recover the anti-dilution fee of US$20 million from Yuchai.

(d) Multi-currency Revolving Credit Facility

On March 20, 2008, the Company entered into a new facility agreement with the Bank of Tokyo-Mitsubishi, UFJ Ltd, Singapore branch to re-finance the existing revolving credit facility. The new unsecured, multi-currency revolving credit facility has a committed aggregated value of S$21.5 million with a one year duration. The new facility will be used to finance the Company's long-term general working capital requirements. Among other things, the terms of the facility require that Hong Leong Asia Ltd. ("HLA") retains ownership of the Company's special share and that the Company remains a consolidated subsidiary of HLA. The terms of the facility also include certain financial covenants with respect to the Company's tangible net worth (as defined in the agreement) as at June 30 and December 31 of each year not being less than US$120,000,000 and the ratio of the Company's total net debt (as defined in the agreement) to tangible net worth as at June 30 and December 31 of each year not exceeding 2.0 times, as well as negative pledge provisions and customary drawdown requirements.

(e) Issuance of Bonds

The Yuchai bonds amounting to Rmb497,000 (US$72,500) matured on March 9, 2007 and have since been refinanced with short-term loans from three local banks which are interest bearing at 5.022% per annum and are repayable on demand. On April 18, 2007, Yuchai issued the second tranche of short term bonds of Rmb650.0 million (US$94.8 million) under approval given by PBOC on May 30, 2006 and the funds were used to pay off the short term loans from three local banks. The bonds were issued at discount and an amount totaling Rmb637.0 million was received by Yuchai. The bonds matured on January 18, 2008.

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