AviChina

AviChina Industry & Technology Company Limited

中國航空科技工業股份有限公司

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

(Stock Code: 2357)

Annual Report

2007

AviChina

Contents

AviChina Industry & Technology Company Limited (the "Company") is a joint stock limited company promoted by AVIC II as a main promoter and was incorporated on 30th April 2003 in compliance with the Company Law of the PRC. The Company's H Shares have been listed on the Stock Exchange since 30th October 2003. The stock code of the Company is "2357". The principal shareholders of the Company's domestic shares are AVIC II, China Hua Rong Asset Management Corporation, China Cinda Asset Management Corporation and China Orient Asset Management Corporation, and the substantial shareholder of the Company's H shares is European Aeronautics Defence and Space Company (the "EADS").

The Company mostly operates through its subsidiaries. The Company and its subsidiaries (the "Group") are mainly engaged in:

- the development, manufacture and sales of mini-sized vehicles, economy sedans and automobile engines;
- the development, manufacture, sales and upgrade of aviation products such as helicopters, trainers, general-purpose aircraft and regional jets for domestic and overseas customers; and
- the co-development and manufacture of helicopters with foreign helicopter manufacturers.

PRINCIPAL PRODUCTS OF THE GROUP:

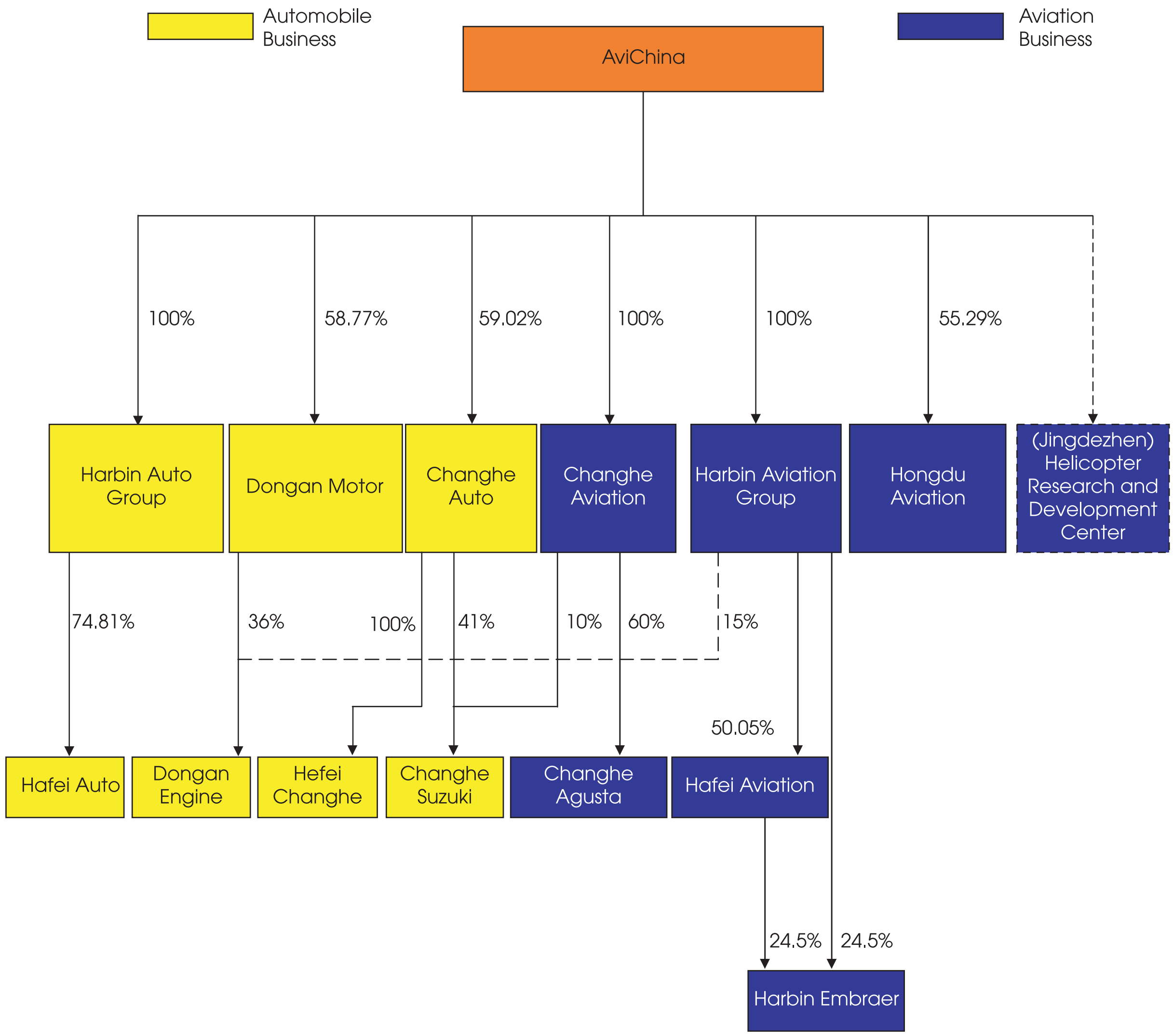
Aviation Products:

The Z-8, Z-9, Z-11 and HC-l20 series helicopters; K-8 series and CJ-6 trainers; Y-12 series multi-purpose aeroplanes and the N-5 series agricultural aeroplanes; EC-120 helicopters jointly produced by the Group and Eurocopter; CA109 helicopters jointly produced by the Group and Agusta; and ERJ-145 series regional jets jointly produced by the Group and Embraer-Empresa Brasileira de Aeronautica S.A. ("Embraer").

Automobile Products:

Hafei series and Changhe series mini-sized vehicles; low-emission economy sedans such as Lobo, Beidouxing, Saima and Ideal; sedans such as Saibao and Liana; and Dongan series auto engines (under 1.3 L); 4G1 and 4G9 series auto engines (from 1.3 L to 2.0 L) manufactured by the joint venture of the Group and Mitsubishi; K14B engines manufactured by the joint venture of the Group and Suzuki.

BUSINESS STRUCTURE OF THE GROUP (AS AT THE DATE OF THIS REPORT)



CONSOLIDATED PROFIT AND LOSS

(Prepared under International Financial Reporting Standards)
(RMB million, other than basic and diluted loss per Share)

	For the year ended 31st December		
	2007	2006	Changes
Turnover	**16,541**	17,111	(3.33%)
Loss before taxation	**(797)**	(473)	68.50%
Net loss attributable to the equity holders of the Company	**(1,026)**	(331)	209.97%
Gross profit margin	**10.64%**	11.14%	N/A
Basic and diluted loss per share for loss attributable to the equity holders of the Company (RMB)	**(0.221)**	(0.071)	211.27%

CONSOLIDATED ASSETS AND LIABILITIES

(Prepared under International Financial Reporting Standards)
(RMB million)

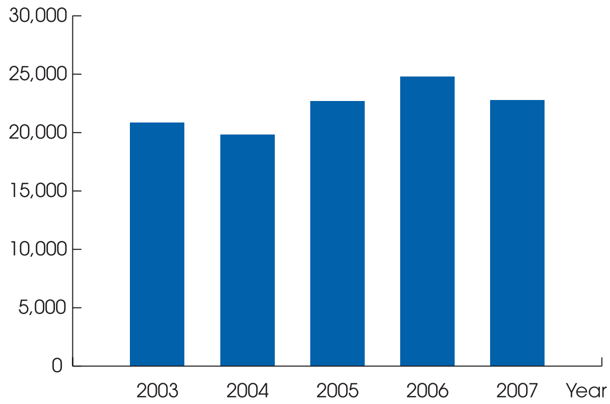
	As at 31st December		
	2007	2006	Changes
Total assets	**22,778**	24,811	(8.19%)
Total liabilities	**16,120**	16,689	(3.41%)
Minority interests	**3,170**	3,793	(16.42%)
Net assets	**3,488**	4,329	(19.43%)

The Group's financial information in the recent five years starting from 1st January 2003 is summarized as follows:
(Prepared under International Financial Reporting Standards)
(RMB million, other than basic and diluted (loss)/earnings per share)

	As at 31st December/For the year ended 31st December				
	2007	2006	2005	2004	2003
Total assets	**22,778**	24,811	22,712	19,816	20,801
Total liabilities	**16,120**	16,689	14,002	11,778	12,782
Minority interests	**3,170**	3,793	3,496	2,942	2,946
Net assets	**3,488**	4,329	5,214	5,096	5,073
Turnover	**16,541**	17,111	14,266	12,877	15,066
(Loss)/profit before taxation	**(797)**	(473)	240	224	765
Net (loss)/profit attributable to the equity holders of the Company	**(1,026)**	(331)	118	71	452
Gross profit margin	**10.64%**	11.14%	13.11%	14.98%	17.60%
Basic and diluted (loss)/ earnings per share for (loss)/profit attributable to the equity holders of the Company (RMB)	**(0.221)**	(0.071)	0.025	0.015	0.134

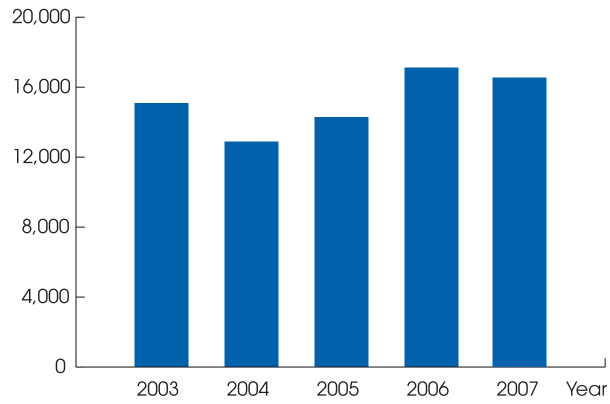
TOTAL ASSETS

(RMB million)



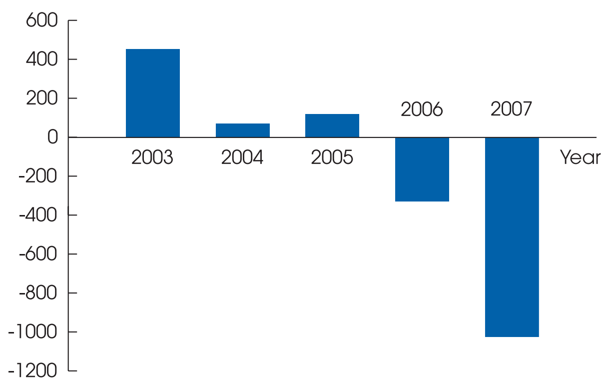
TURNOVER

(RMB million)



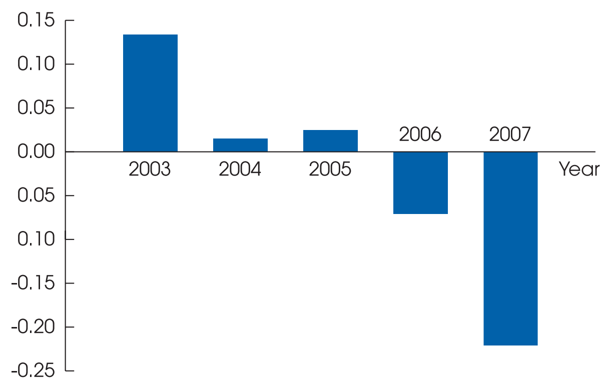
NET PROFIT/(LOSS) ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE COMPANY

(RMB million)



BASIC AND DILUTED EARNINGS/(LOSS) PER SHARE FOR PROFIT/(LOSS) ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE COMPANY

(RMB)



In 2007, the aviation business of the Group achieved a remarkable progress, with an increased turnover of aviation products, which accounted for more than 30% of the total turnover of the Group for the first time, representing a significant increase over that of 2003 when the Company was listed. In contrast, the Group recorded a significant loss in its automobile business, which was caused by unfavorable operation, the decline in sales volume of entire vehicle products and reduction of sales price, which affected the annual results of the Group and resulted in a loss of RMB1,026 million attributable to the equity holders of the Company for 2007.

In 2007, the Group had put more efforts in the market development of its aviation products. As a result, its aviation business grew steadily and recorded a sales revenue of RMB5,327 million, representing an increase of 20.31% over that of 2006. The relative proportion of the turnover attributable to the sales of aviation products to the total turnover of the Group for 2007 increased to 32.21% from 17.16% at the time of the listing of the Company in 2003.

During the reporting period, the Group's sales revenue derived from helicopters grew steadily. The test flight of L15 advanced trainer, which was primarily researched and manufactured by the Group, progressed smoothly. At present, the Group is actively exploring the domestic and international markets for L15 advanced trainer. Further, the application for type certificate ("TC") for Y-12F multi-purpose aircraft had been accepted by the Federal Aviation Administration of the United States ("FAA"). N-5A aircraft had also been granted TC by the FAA and the market outlook for it is positive.

The Group is continuously strengthening its co-operation with international partners on aviation products and expanding its subcontracting business on parts and components production. Tianjin Zhongtian Aviation Industry Investment Co., Ltd., in which Hafei Aviation and Hongdu Aviation both have equity interests, has entered into a joint venture contract with Airbus China Co., on the establishment of a joint venture company for the setting up of a final assembly line for Airbus A320 series in Tianjin. In addition, AVIC II and Airbus have entered into a framework agreement on establishment of a composite material manufacturing center. According to the framework agreement, Hafei Aviation and Airbus will set up a joint-venture manufacturing center to produce composite parts and components for A350XWB wide body aircraft. The company plans to invest RMB100 million in the joint-venture project. Hongdu Aviation entered into a sub-contracting agreement with U.S Goodrich Corporation for the production of parts and components for engines of the new Boeing 787 aircraft for the period from 2008 to 2021. The contract value is estimated to be US$57 million.

The Company has also increased its investments in the aviation business. To support the large scale industrialization of helicopter production of Changhe Aviation, the Company increased its investment in Changhe Aviation by increasing its contribution to the registered capital by RMB200 million. As part of the proposed private placing of shares by Hongdu Aviation, the Company will subscribe such number of new shares to be issued by Hongdu Aviation equivalent to RMB250 million.

With the official launch of China's self-developed large aircraft in 2008 and the growing demands for domestic helicopters and general-purpose aircraft, new opportunities have been created for the development of civil aviation products and the Group's aviation business will benefit from this project in long run. In 2008, the Group will actively participate in the development and manufacture of large aircraft, strongly promote the international technological co-operation on helicopter production as well as the development of general-purpose aircraft; continuously enhance the quality of civil aviation products and improve the quality of services; actively develop domestic and international markets for its aviation products, and strive to realize large scale helicopters export sales contracts. Meanwhile, the Group will also strengthen the co-ordination with domestic and international counterparts in production and outsourcing of parts and equipment so as to promote a balanced production and ensure the timely delivery of aviation products; and expand subcontracting business on parts and components production in order to further enhance the Group's aviation business.

In 2007, the sales volume and profit of the Group's entire vehicle products dropped. In contrast, the sales volume of the Group's automobile engine products maintained a significant growth. In 2007, the sales volume of the Group's entire vehicle products was 291,694, representing a decrease of 15.29% from that of 2006. External sales of auto engines were 283,991 units, representing an increase of 46.26% over that of 2006. In 2007, the Group continued to restructure the range of its automobile products, during which it launched a new model, Landy, and two upgraded models, Lobo Fuel-Saving π and Ideal II, and completed the development of HF9 and Furuida single/double-seat model and commenced the production of 4G15 auto engines. Development of diesel engines also achieved a remarkable progress. Further, the 4G93D engine model also received the honor of "China Top Ten Engines". Meanwhile, we actively pushed forward the international and domestic collaboration of the Group's enterprises engaging in the manufacturing of entire vehicle products and automobile engines. The Group entered into a Memorandum of Cooperation with the PSA Group of France, while its discussion with a domestic automobile group on strategic co-operation had progressed smoothly.

In 2008, the Group will further reinforce the strategy of strengthening the development of mini-vehicles and co-developing economy sedans, adhere to the marketing-oriented principle in its business operations, continue to restructure the products mix and reduce costs, put more efforts in upgrading the existing entire vehicle models and engine models and developing new models, actively promote the co-operation between the domestic and overseas manufacturers of entire vehicle, learn from past experience, overcome difficulties and further improve operational efficiency and profitability so as to boost the development of the entire vehicle segment and the engine segment simultaneously.

Finally, I would like to take this opportunity to extend my gratitude to the Group's shareholders and customers for their continued support. I also wish to express my sincere appreciation to all our highly competent and dedicated directors, management team and our employees for their great efforts and hard work.

Zhang Hongbiao
Chairman
Beijing, 11th April 2008

The following discussion and analysis should be read in conjunction with the Group's consolidated financial statements and notes thereto set out in this annual report and other sections.

SUMMARY

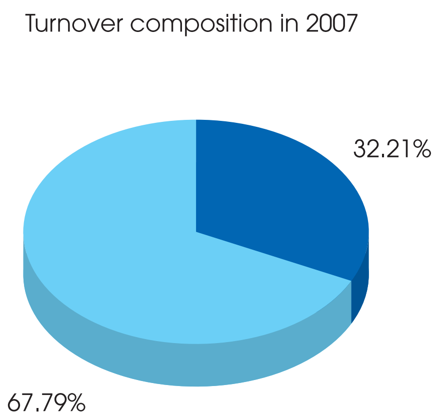
For the year ended 31st December 2007, the Group recorded a turnover of RMB16,541 million, representing a decrease of RMB570 million, or a decrease of 3.33% from the turnover of RMB17,111 million in 2006. Of the decrease, the effect of proportional consolidation for the results of Changhe Suzuki resulted in a decrease of RMB1,156 million in the turnover. If the effect was disregarded, the turnover in 2007 would have increased by RMB590 million as compared to that of 2006. The increase was mainly attributable to the growth in turnover derived from sales of aviation products and automobile engine products. As a result of unfavorable operation and a significant decline in the sales of vehicles in the automobile segment results, the share of loss by the equity holders of the Company amounted to RMB1,026 million.

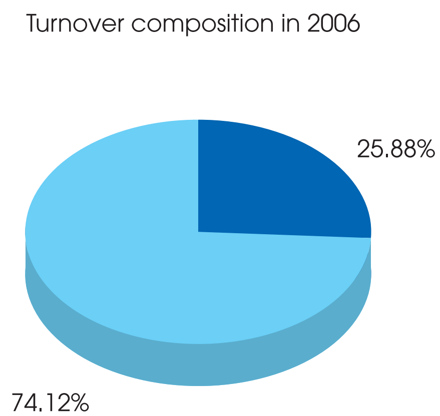
The following table sets out the comparative figures of our consolidated operating results for the years ended 31st December 2007 and 2006:

CONSOLIDATED OPERATING RESULTS

	Year ended 31st December		
RMB million	**2007**	2006	Changes
Turnover	**16,541**	17,111	(3.33%)
Of which: automobile segment	**11,214**	12,683	(11.59%)
aviation segment	**5,327**	4,428	20.31%
Cost of sales	**(14,781)**	(15,205)	(2.79%)
Of which: automobile segment	**(10,137)**	(11,443)	(11.42%)
aviation segment	**(4,644)**	(3,762)	23.45%
Other revenues	**114**	98	16.33%
Selling and distribution expenses	**(981)**	(1,157)	(15.21%)
General and administrative expenses	**(951)**	(1,065)	(10.70%)
Operating loss	**(524)**	(324)	61.73%
Financial costs, net	**(329)**	(194)	69.59%
Share of results of associates	**57**	45	26.67%
Loss before taxation	**(797)**	(473)	68.50%
Taxation	**(51)**	(13)	292.31%
Minority interests	**(178)**	155	N/A
The loss attributable to the equity holders of the Company	**(1,026)**	(331)	209.97%

1 Composition of turnover





The Group's turnover for 2007 was RMB16,541 million, representing a decrease of 3.33% from that of RMB17,111 million in 2006.

The turnover of the Group's aviation products in 2007 increased by 20.31% to RMB5,327 million, which accounted for 32.21% of the total turnover of the Group, or represented an increase of 6.33 percentage points over 25.88% in 2006. As compared to the 17.16% at the time of the listing of the Company in 2003, the proportion of aviation products to the total turnover has almost doubled. The relative proportion of turnover attributable to the sales of aviation products as compared to the total turnover of the Group is growing steadily year by year. The turnover of the Group's automobile products in 2007 decreased by 11.59% to RMB11,214 million, which accounted for 67.79% of the total turnover of the Group, or represented a decline of 6.33 percentage points from 74.12% in 2006.

The Group operates mainly in the mainland China where a majority of the turnover is generated.

2 Selling and distribution expenses

The Group's selling and distribution expenses for 2007 amounted to RMB981 million, representing a decrease of RMB176 million, or a 15.21% decrease from that of 2006. The decrease was mainly attributable to a decrease of RMB82 million in terms of selling and distribution expenses as a result of the effect of proportional consolidation for the results of Changhe Suzuki as well as the decline in the sales volume of entire vehicle products, which together resulted in a decrease of RMB150 million in the expenses on loading and freight as well as sales commissions as compared to 2006.

3 General and administrative expenses

The Group's general and administrative expenses for 2007 amounted to RMB951 million, representing a decrease of RMB114 million, or a 10.7% decrease from that of 2006. The decrease was mainly attributable to a decrease of RMB73 million resulting from the effect of proportional consolidation for the results of Changhe Suzuki.

4 Operating loss

The Group suffered an operating loss of RMB524 million for 2007, representing an increased loss of RMB200 million as compared to the loss of RMB324 million in 2006. This was mainly attributable to a widened loss in the Group's entire vehicle business as compared to that of 2006.

5 Finance costs, net

The Group's net finance costs for 2007 amounted to RMB329 million, representing an increase of RMB135 million over RMB194 million of 2006, which was mainly attributable to an increase in interest expenses resulted from a rise in the interest rate level of bank borrowings. Details are set out in note 8 to the financial statements.

6 Income taxation expenses

The Group's income tax for 2007 was RMB51 million, representing an increase of RMB38 million over the RMB13 million in 2006. Details are set out in note 9 to the financial statements.

7 Minority interests

The Group's minority interests for 2007 was a share of profit of RMB178 million, as compared to a loss of RMB155 million in 2006. The profit was mainly attributable to the growth in profits of certain non-wholly owned subsidiaries of the Group in 2007.

ASSETS, LIABILITIES AND EQUITY

	As at 31st December		
RMB million	**2007**	2006	Changes
Current assets	**14,028**	14,760	(732)
Non-current assets	**8,750**	10,051	(1,301)
Total assets	**22,778**	24,811	(2,033)
Current liabilities	**14,702**	15,659	(957)
Non-current liabilities	**1,418**	1,030	388
Total liabilities	**16,120**	16,689	(569)
Share capital	**4,644**	4,644	—
Reserves	**(1,156)**	(315)	(841)
Capital and reserves attributable to the Company's equity holders	**3,488**	4,329	(841)
Minority interests	**3,170**	3,793	(623)

As at 31st December 2007, the Group's total assets amounted to RMB22,778 million, total liabilities amounted to RMB16,120 million whereas minority interests and capital and reserves attributable to the Company's equity holders amounted to RMB3,170 million and RMB3,488 million, respectively. Among which:

1 Total assets

As at 31st December 2007, the total assets of the Group were RMB22,778 million, representing a decrease of RMB2,033 million from that of 2006. The effect of proportional consolidation for the results of Changhe Suzuki resulted in a decrease of RMB1,702 million in the total assets of the Group.

2 Liabilities

As at 31st December 2007, the total liabilities of the Group were RMB16,120 million, representing a decrease of RMB569 million from that of 2006. The effect of proportional consolidation for the results of Changhe Suzuki resulted in a decrease of RMB831 million in the total liabilities of the Group.

3 Guaranteed and secured loans

As at 31st December 2007, the Group's total borrowings amounted to RMB6,074 million, of which RMB431 million was secured by machinery, equipment and banks' acceptance bills, with a net book value of RMB602 million.

Guaranteed borrowings amounted to RMB4,233 million, of which RMB3,702 million was cross guaranteed amongst the subsidiaries of the Group, RMB50 million was guaranteed by third parties and RMB481 million was guaranteed by AVICII and its subsidiaries.

4 Capital and reserves attributable to the Company's equity holders

In 2007, the capital and reserves attributable to the Company's equity holders amounted to RMB3,488 million, representing a decrease of RMB841 million from that of 2006. Details are set out in the Consolidated Statement of Changes in Equity and note 34 and note 35 to the financial statements.

5 Exchange risks

The Group mainly operates in the PRC with most of the transactions settled in Renminbi. The Group's assets and liabilities, and transactions arising from its operations subject to foreign exchange risk are primarily associated to United States Dollar, Euro, Hong Kong Dollar and Japanese Yen.

Due to its operational needs, the Group had drawn loans denominated in Euro, United States Dollar and Japanese Yen. In addition, the Company has some deposits in Hong Kong Dollar in the amount of HK$50 million, being part of the proceeds raised from the initial public offering in October 2003. The directors are of the opinion that the exchange risks to the Group are low and will not have any material adverse impact on the Group's financial results. Details are set out in note 40(a)(i) to the financial statements.

6 Contingent liabilities and guarantees

As at 31st December 2007, the Group had not provided any guarantees in favor of any third party nor were there any significant contingent liabilities.

7 Gearing ratio

As at 31st December 2007, the Group's gearing ratio was 26.67% (31st December 2006: 26.89%), which was arrived at by dividing the total borrowings by total assets as at 31st December 2007.

CASH FLOW

1 Liquidity and capital resources

As at 31st December 2007, the Group's net cash and cash equivalents amounted to RMB2,453 million, which was mainly derived from the followings:

- cash and bank deposits at the beginning of the year;
- funds generated from its operations; and
- new bank borrowings.

The Group's cash flow for each of the years 2007 and 2006 were as follows:

Unit: RMB million (except percentage)

Main items of cash flow	**2007**	2006	Change (amount)	Change (percentage)
Net cash flows generated from operating activities	**97**	910	(813)	(89.34%)
Net cash flows used in investing activities	**(475)**	(1,551)	1,076	(69.37%)
Net cash flows generated from financing activities	**(188)**	854	(1,042)	(122.01%)
Net increase/(decrease) in cash and cash equivalents	**(566)**	213	(779)	(365.73%)

2 Operating activities

Net cash in-flows generated from operating activities for the year amounted to RMB97 million, representing a decrease of RMB813 million from that of 2006. Details are set out in note 36 to the financial statements.

3 Investing activities

Net cash out-flows used in investing activities for the year amounted to RMB475 million, representing a decrease of RMB1,076 million from that of 2006, among which term deposits with an initial term of over three months decreased by RMB359 million, while in 2006 the amount increased by RMB246 million.

4 Financing activities

Net cash flows generated from financing activities for the year was an out-flow of RMB188 million, while the financing activities in 2006 generated a net cash in-flow of RMB854 million. The net out-flow was mainly due to an increase in the repayment of bank borrowings in 2007.

As at 31st December 2007, the Group's total borrowings amounted to RMB6,074 million, of which the current borrowings, long-term borrowings due in one year and non-current portion of long-term borrowings amounted to RMB4,312 million, RMB650 million and RMB1,112 million, respectively.

The Group's long-term borrowings are repayable as follows:

Maturity	RMB million
Within one year	650
In the second year	319
In the third to fifth year	510
After the fifth year	283
Total	1,762

As at 31st December 2007, the Group's bank borrowings amounted to RMB5,914 million with an average interest rate of 6.39% per annum, representing 97.37% of the total borrowings. Other borrowings amounted to RMB160 million with an average interest rate of 0.07%, accounting for 2.63% of the total borrowings.

As at 31st December 2007, the Group's borrowings denominated in foreign currencies amounted to RMB538 million, representing 8.85% of the total borrowings, of which borrowings denominated in United States Dollar, Euro and Japanese Yen amounted to US$1 million, Euro43 million and Yen1,119 million respectively.

SEGMENT INFORMATION

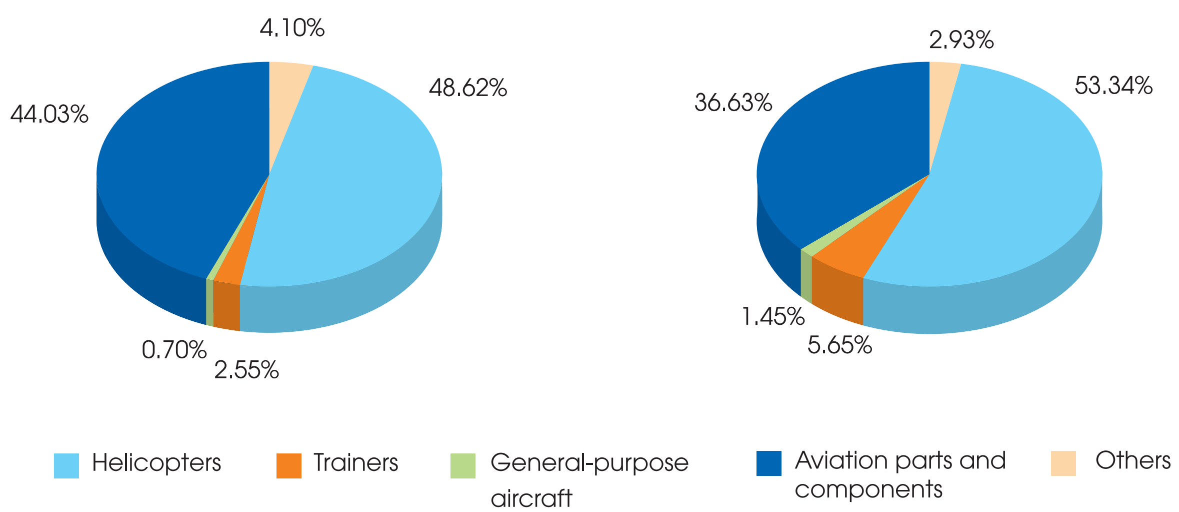
The Group's principal operations comprise two segments, namely, the aviation segment and the automobile segment.

AVIATION SEGMENT

Sales Revenue

Sales Revenue of Aviation Segment in 2007

Sales Revenue of Aviation Segment in 2006



The Group's sales revenue derived from aviation products for 2007 was RMB5,327 million, representing an increase of RMB899 million, or a 20.31% increase over that of 2006. The increase was mainly attributable to the increase in sales volume of helicopters and aviation parts and components during the year.

Cost of Sales

Cost of sales of the Group's aviation products for 2007 was RMB4,644 million, representing an increase of RMB882 million, or a 23.45% increase over that of 2006.

Gross Margin

Gross margin of the Group's aviation products for 2007 was 12.83%, representing a decrease of 2.2 percentage points from that of 2006. The decrease was mainly attributable to the increase in domestic raw materials prices not matched with increases in the selling prices of the Group's aviation products which remained at the same level.

Review and Outlook

In 2007, the Group had put more efforts in the market development of its aviation products. Through participating in the 2007 Asian Aerospace International Expo and Congress in Hong Kong, the reputation of the Group's aviation products has been further enhanced.

During the reporting period, the Group sold 120 helicopters in total, representing 24 units more than that of 2006, which was mainly attributable to an increase in the delivery of fuselages for EC-120 helicopter. The sales volume of Z-9 helicopter also increased, marking the entry into a steadily growing stage of market demands for this product. Changhe Agusta delivered two CA109 helicopters in 2007, and signed a sales contract with the China Central Television in May 2007 for the sale of one CA109 helicopter to be used for Olympic aerial shooting and is expected to be delivered in May 2008.

Apart from continuing to perform the export and production contract on K8 trainers entered into with China National Aero-Technology Import & Export Corporation, co-production of K8E trainers project with Egyptian partners also progressed smoothly. The test flight of L15 advanced trainer, which was primarily researched and manufactured by the Group, has progressed smoothly. At present, the Group is actively exploring the domestic and international markets for L15 advanced trainer.

The sales of the Group's Y-12 series aircraft remained steady. The application for type certificate ("TC") for Y-12F multi-purpose aircraft had been accepted by the Federal Aviation Administration of the United States ("FAA"). It will perform its maiden flight in 2008. N-5A aircraft had been granted TC by the FAA and the market outlook for it is positive. The Group is currently engaging in the research, development, upgrading and improving of its agricultural and forestry planes in accordance with the demands of the domestic and international markets. The research and development of N-5B plane is progressing well and has achieved milestone development.

The Group is continuously strengthening its co-operation with international partners on aviation products and expanding its subcontracting business on parts and components production. Tianjin Zhongtian Aviation Industry Investment Co., Ltd., in which Hafei Aviation and Hongdu Aviation both have interests, has entered into a joint venture contract with Airbus China on the establishment of a joint venture company for the setting up of a final assembly line for Airbus A320 series in Tianjin. In addition, AVIC II and Airbus have entered into a framework agreement on establishment of a composite material manufacturing center. According to the framework agreement, Hafei Aviation and Airbus will set up a joint-venture manufacturing center to produce composite parts and components for A350XWB wide body aircraft. The Company plans to invest RMB100 million in the joint-venture project. Hongdu Aviation entered into a sub-contracting agreement with U.S. Goodrich Corporation for the production of parts and components for engines of the new Boeing 787 aircraft for the period from 2008 to 2021. The contract value is estimated to be US$57 million.

The Company has also increased its investments in the aviation business. To support the large scale industrialization of helicopter production of Changhe Aviation and upon the approval by the Board at the sixth board meeting of the second Board in 2007, the Company increased its investment in Changhe Aviation by increasing its contribution to the registered capital by RMB200 million. As part of the proposed private placing of shares by Hongdu Aviation, the Company will subscribe such number of new shares to be issued by Hongdu Aviation equivalent to RMB250 million.

With the official launch of China's self-developed large aircraft and the growing demands for domestic helicopters and general-purpose aircraft, new opportunities have been created for the development of civil aviation products and the Group's aviation business will benefit from this in long run. In 2007, the Group made satisfactory progress in the market development of its aviation products. However, the profitability of its aviation business is yet to improve. In 2008, the Group will adopt the following strategies to improve its aviation business:

1. Accelerate and expand its efforts in research and development of aviation products, invest in more funds in this area, actively participate in the development and manufacture of large aircraft, and strongly promote the international technological co-operation on helicopter production as well as the development of general-purpose aircraft;

2. Strengthen co-operation with overseas partners, actively develop domestic and international markets for its aviation products, strive to realize large scale helicopters export sales contracts and expand sub-contracting production;

3. Strengthen the co-ordination with domestic and international counterparts in production and outsourcing of parts and equipment so as to promote a balanced production and improve large scale production capability; and

4. Based on lean management, the Group will continuously enhance the quality of civil aviation products, improve quality of services and endeavor to reduce production costs so as to improve the operational effectiveness of aviation business.

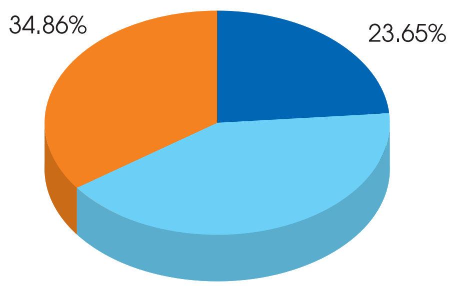
Orders for Aviation Products

As at the date of this report, the Group's confirmed orders for aviation products are as follows: 115 helicopters, 118 trainers, 7 general-purpose aircraft and 43 regional aircraft. The Group endeavors to obtain more orders for its aviation products.

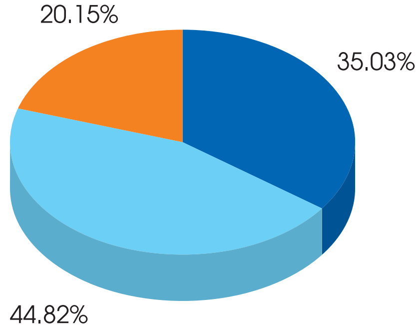
AUTOMOBILE SEGMENT

Sales Revenue

Sales Revenue of Automobile Segment in 2007



Sales Revenue of Automobile Segment in 2006



Sedans   Mini-vans and mini-trucks   Other automobile products

The Group's turnover of automobile products for 2007 amounted to RMB11,214 million, representing a decrease of RMB1,469 million from that of 2006. The effect of proportional consolidation for the results of Changhe Suzuki resulted in a decrease of sales revenue of RMB1,156 million. If the effect was disregarded, the turnover would have represented a decrease of RMB313 million from that of 2006. Of the 2007 turnover, the sales revenue of entire vehicle products was RMB7,305 million, representing a decrease of RMB2,822 million, or a 27.87% decrease from that of 2006; and external sales of automobile engine products and auto parts and components amounted to RMB3,909 million, representing an increase of 52.93% over that of 2006.

Cost of Sales

Cost of sales of the Group's automobile products for 2007 amounted to RMB10,137 million, representing a decrease of RMB1,306 million from that of 2006. The effect of proportional consolidation for the results of Change Suzuki resulted in a decrease of RMB1,150 million in the cost of sales. If the effect was disregarded, the cost of sales would have represented a decrease of RMB156 million as compared to that of 2006. Of the total cost of sales, the cost of sales of entire vehicle products was RMB7,243 million, representing a decrease of RMB2,206 million, or a 23.35% decrease from that of 2006; the cost of external sales of automobile engines and auto parts and components amounted to RMB2,894 million, representing an increase of 45.14% over that of 2006.

Gross Margin

Gross margin of the Group's automobile products for 2007 was 9.60%, representing a decrease of approximately 0.18 percentage points from that of 2006. During the year of 2007, despite a series of price-cutting measures to promote sales, the sales volume of the Group's entire vehicle products had not reached the expected level, this resulted in a low utilization rate of the production capacity, increased provision for depreciation of production lines over that of 2006, which contributed to a drop in the gross margin of the Group's entire vehicle products. Nevertheless, the sales volume of auto engine products rose and the gross margin of the auto engine products remained steady. Overall, the gross margin of the Group's automobile products dropped slightly in 2007.

Review and Outlook

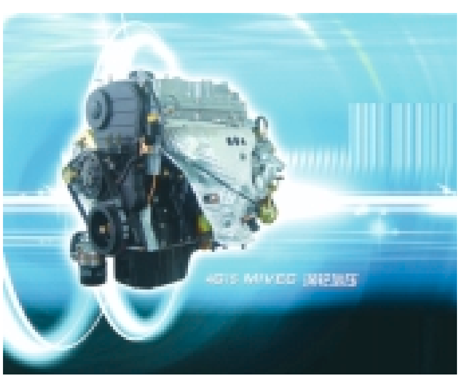
In 2007, the PRC automobile industry maintained its rapid growth as a whole. According to the statistics published by China Automobile Industry Association, a total of approximately 8,882,400 and 8,791,500 vehicles were produced and sold, respectively in the PRC in 2007, representing an increase of 22.02% and 21.84% as compared to that of 2006, respectively.

In 2007, due to certain negative factors, such as unfavorable operation and decline in the competitiveness of the Company's automobile products, the sales volume of the Group's entire vehicle products dropped. In contrast, the sales volume of automobile engine products maintained a significant growth. The Group sold 291,694 vehicles in 2007, representing a decrease of 15.29% as compared to that of 2006, among which the sales volume of mini-vans and trucks was 196,052, representing a decrease of 17.16% from that of 2006; and the sales volume of sedans was 95,642, representing a decrease of 11.20% from that of 2006. External sales of auto engines was 283,991 units, representing an increase of 46.26% over that of 2006.

In 2007, the Group continued to restructure the range of its automobile products, during which it launched a new model, Landy, and two upgraded models, Lobo Fuel-Saving π and Ideal II. The Group also escalated its promotional efforts in the upgraded model, Beidouxing (1.4L), which recorded a sales volume of 41,940 units, representing an increase of 23.56% over that of 2006.The Group completed the development of HF9 and Furuida single/double-seat model and commenced the production of 4G15 auto engines. Development of diesel engines also achieved a remarkable progress. The 4G93D engine model received the honor of "China Top Ten Engines".

In 2007, the Group strengthened international and domestic co-operation by actively pushing forward the international and domestic collaborations of the Group's enterprises engaging in the manufacturing of entire vehicle products and automobile engines. During the reporting period, the Group entered into a Memorandum of Cooperation with the PSA Group of France, while its discussion with a domestic automobile group on strategic co-operation had progressed smoothly. The partnerships with Suzuki, Mitsubishi, AVL and BOSCH had also been reinforced.

The Group always emphasizes the development of overseas markets for its entire vehicle products as well as the markets for external sales of its automobile engines. The export of entire vehicle products to the markets in Russia and South America achieved a significant breakthrough while the assembly line set up in Vietnam for auto model, namely, Ideal, has commenced production. In the meantime, the export volume of mini-trucks continued to increase. The Group's enterprises engaging in automobile engine manufacturing had endeavored to develop the market for sales to domestic proprietary automobile manufacturers. The rapid growth in external sales of automobile engines has boosted the rapid development of the Group's auto engine business.



In 2008, the Group will further reinforce the strategy of strengthening the development of mini-vehicles and co-developing economy sedans, adhere to the marketing-oriented principle in its business operations and improve its operational efficiency and profitability in order to enhance the development of the entire vehicle segment and the engine segment simultaneously.

1. With emphasis on marketing strategies, the Group will refine its sales and marketing practices, enhance the level of marketing network and endeavor to explore second and third-tier markets so as to boost the sales volume of mini-sedans and mini-vans and trucks;

2. Based on market positioning, the Group will restructure its product mix, make appropriate adjustments to the prices and accessories of each model based on the Cost-Volume-Profit Analysis. Models with higher profit margin will be promoted in priority. At the same time, the Group seeks to reduce outsourcing costs and administrative expenses through optimal production means, and minimize the impact caused by the inflationary prices of raw materials such as steel, metals and plastics;

3. The Group will continue to upgrade the existing entire vehicle models and engine models and develop new models, launch new model HF9 and Furuida single/double-seat model and steadily promote the introduction and development of other successive new automobile models, upgraded models and engine products; and

4. Further promote the co-operation between the domestic and overseas manufacturers of entire vehicle in order to better integrate with the mainstream PRC automobile industry and enjoy complementary advantages through co-operation and thereby promote development.

USE OF PROCEEDS

According to the plan for use of proceeds, the proceeds used up to 31st December 2007 amounted to RMB925 million in total, out of which RMB700 million was used for the research and development of new vehicle models and new automobile engines; RMB225 million was used for the research and development of new advanced trainers and helicopters; and the remaining balance was deposited with banks in the PRC as short term deposits which would also be used by the Company as planned.

EMPLOYEES

As of 31st December 2007, the Group had 27,849 employees. The Group has provided appropriate emoluments, benefits and training to its employees.

Employees breakdown by functions

	Number of employees	Percentage to total employees (%)
Vehicles and engines	17,068	61.29%
Aviation	10,169	36.51%
Other activities	612	2.2%
Total	27,849	100%

For the year ended 31st December 2007, total staff costs of RMB945 million were incurred by the Group in connection with its employees, representing a decrease of RMB52 million as compared to RMB997 million in 2006.

REMUNERATION OF EMPLOYEES

The Group's remuneration scheme is determined on fair and reasonable principles which are similar to those available in the market. Remuneration of employees comprises basic salary, contribution to a housing fund, and contributions to pension plans. The Group will also, in its discretion, pay year-end bonus to employees according to their respective performance.

TRAINING FOR EMPLOYEES

The Group expects a high level of knowledge and skill in respect of the automobile manufacturing industry and the aviation manufacturing industry from its employees. Therefore, implementation of comprehensive employee training is the key to the Group's continuous development. Accordingly, the Group will continuously review its existing employee training scheme in order to provide comprehensive and systematic training to its employees.

In 2007, the Group provided a series of training on optimization management ideas to its senior management, and provided more special training courses, seminars and field survey on strategic management, human resources management, and financial management. Training relating to all kinds of professional skills and management techniques are also provided to all professional departments of the Group's headquarters and the business departments of its subsidiaries. On-the-job training covering corporate culture, management concept and management standardization are also provided to new employees.

The Group also provides overseas training to the management officers and technicians through co-operation with international partners. The employees, through training, are able to continuously acquire new knowledge to improve their capabilities. This will in turn enhance the Group's competitiveness in the ever-changing market.

DIRECTORS

Executive Directors

Mr. Zhang Hongbiao （張洪飈）

62, chairman of the Board of Directors. He is a researcher level senior engineer. He has been the president of AVIC II since December 2003. Mr. Zhang graduated from Beijing University of Aeronautics and Astronautics in Aircraft Design in 1968 and received his master degree from Chongqing University in 1981. He commenced his career in aviation industry in September 1968 and used to be the head of technology department, workshop supervisor, assistant to the chief engineer, deputy general manager and general manager of Harbin Dongan Engine Manufacturing Company. He was appointed as the deputy chief engineer in May 1990 and subsequently the chief engineer of the Ministry of Aero-Space, the vice president of China Aviation Industry Corporation in 1993 and the vice chairman of the Commission of Science Technology and Industry for National Defence in 1998. Mr. Zhang has been appointed as the chairman of the Board since June 2004.

Mr. Wu Xiandong （吳獻東）

43, vice chairman of the Board of Directors and the president of the Company. He is a researcher level senior engineer. He graduated from Beijing University of Aeronautics and Astronautics majoring in electro-mechanical control in manufacturing engineering and received his Ph.D. degree from the Moscow Aircraft Institute of Russia majoring in production organization in the aviation industry. He has been engaged in the aviation field since July 1987, joined AVIC in 1996, and joined AVIC II in 1999. He used to be an assistant engineer in Harbin Dongan Engine Manufacturing Company, the general manager of Harbin Aviation Elec-Mec Company, the director of assets and enterprises management department of AVIC II and an assistant to the president of AVIC II and a vice president of AVIC II. Mr. Wu has been appointed as the vice chairman of the Board and the president of the Company since April 2003.

Mr. Tan Ruisong （譚瑞松） (Chairman of Automobile Business Development and Strategy Committee)

46, vice chairman of the Board and a researcher level senior engineer. Mr. Tan also serves as the vice president of AVIC II. He graduated from Beijing University of Aeronautics and Astronautics in 1983 with a bachelor degree majoring in manufacture and design of engines, and received his master degree in shipping and ocean engineering and Ph.D. degree in management science and engineering from Harbin Engineering University in 2002 and 2006, respectively. Mr. Tan commenced his career in aviation in July 1983, and used to be a technician, technical supervisor and workshop supervisor of National Dongan Machinery Factory. He had been the deputy chief engineer and deputy general manager of Harbin Dongan Engine Company, the general manager of Harbin Dongan Auto Engine Co., Ltd., member of the board, vice chairman and the general manager of Harbin Dongan Engine (Group) Co., Ltd., and the chairman of Harbin Aviation Industry (Group) Co., Ltd. Mr. Tan has been appointed as a director of the Company since June 2005 and as the vice chairman of the Board since June 2006.

Non-executive Directors

Mr. Liang Zhenhe （梁振河） (Chairman of Aviation Business Development and Strategy Committee and member of Audit Committee)

61, a researcher level senior engineer. He also serves as a special consultant of AVIC II. Mr. Liang graduated from the Northwestern Polytechnical University in Aircraft Design Profession in August 1970 and commenced his career in aviation industry from then on. He used to be the deputy section chief, section chief, deputy general manager and general manager of Hanzhong 141 Plant（漢中一四一廠）in Shaanxi. He was appointed as the deputy general manager and general manager of Hanzhong Tianda Aviation Industry Corporation（漢中天達航空工業總公司）in Shaanxi in November 1990. He was deployed to China Aviation Industry Corporation in 1996 and used to be the deputy director of the corporate governance department and the deputy head of corporate governance office. He was appointed as a vice president of AVIC II in 1999. He was awarded the "Model Worker" by the Ministry of Aero Space in April 1991. Mr. Liang has been appointed as a director of the Company since June 2004.

Mr. Song Jingang（宋金剛）(Chairman of Remuneration Committee and member of Automobile Business Development and Strategy Committee)

63, a researcher level senior engineer. Mr. Song also serves as a special consultant of AVIC II. He graduated from the Harbin Military Engineering Institute, majoring in aero-engines. He commenced his career in the aviation industry in August 1970 and used to be the head of technology department, workshop supervisor, a deputy director and the director of Harbin Dongan Mechanic Factory, a deputy general manager and the general manager of Harbin Dongan Engine Manufacturing Company, the general manager, the chairman of AVIC Mini-sized Vehicle (Group) Co., Ltd.（中航微型汽車（集團）有限責任公司）and the vice president of AVIC II. Mr. Song has been appointed as a director of the Company since April 2003.

Mr. Tian Min（田民）(Member of Remuneration Committee)

51, a class one senior accountant. He also serves as the chief accountant of AVIC II. Mr. Tian graduated from Zhengzhou Aviation Industry Management Institute in the Department of Organisational Management in July 1982. After graduation, he used to be the deputy section chief, deputy director and director of financial and accounting division and deputy chief accountant, chief accountant and deputy general manager, general manager, and chairman of Hongdu Aviation Industry (Group) Co., Ltd.. Mr. Tian also received his master degree in Engineering from Central China University of Science and Technology. He was elected as a representative of the 10th National People's Congress of Jiangxi Province in 2002. Mr. Tian received the honour from AVIC II and the Commission of Science Technology and Industry for National Defence as the Youth with Excellent Contributions; the incentive award to the general managers from AVIC II. He was elected the candidate (senior management expert) of "511 Experts Work" of the Commission of Science Technology and Industry for National Defence in 2002. Mr. Tian has been appointed as a director of the Company since June 2004.

Mr. Wang Bin（王斌）

48, a researcher level senior engineer. Mr. Wang also serves as the deputy chief engineer of AVIC II. He has been appointed as an executive director and the general manager of Jiangxi Changhe Aviation Industry Co. Ltd. since November 2004. Mr. Wang graduated from Shenyang Institute of Aeronautical Engineering in 1982 with a bachelor degree majoring in aircraft manufacture. He commenced his career in aviation in August 1982 and had been a technician of assembly section, vice team head, team head, deputy manager, deputy supervisor of workshop, deputy general technologist and general technologist. He was appointed as a deputy chief engineer, chief of general engineer office, and deputy general manager of Harbin Aircraft Manufacturing Corporation in 1997, member of the board, the general manager and chairman of Harbin Aviation Industry Co. Ltd., and the general manager and vice chairman of Harbin Aircraft Industry (Group) Co., Ltd. Mr. Wang served as member of board of Harbin Embraer Aircraft Industry Co., Ltd. from July 2002 to December 2004. He serves as the chairman of Changhe Agusta and the chairman of Shanghai Sikorsky Aircraft Co., Ltd.. Mr. Wang has been appointed as a director of the Company since June 2005.

Mr. Chen Huaiqiu（陳淮秋）(Member of Aviation Business Development and Strategy Committee)

62, a researcher level senior engineer. He graduated from Beijing University of Aeronautics and Astronautics in 1969 majoring in aeronautic engineering dynamics. He commenced his career in the aviation industry in September 1970 and used to be a technician of Guizhou Base of the Third Ministry of Machine Building, a lecturer at Metal Technology Institute of Beijing Aeronautics College, a deputy division director, a division director, a deputy director and the director of the planning bureau of AVIC and the director-general of the planning and development department of AVIC II. Mr. Chen has been appointed as a director of the Company since April 2003.

Mr. Wang Yong （王勇）

51, a senior economist. He was appointed as the deputy general manager of China Hua Rong Asset Management Corporation Changchun Office in April 2000. He has been appointed as the deputy general manager of China Hua Rong Asset Management Corporation Harbin Office since December 2001. He graduated from Harbin Normal University in 1997 with a bachelor degree majoring in economy administration. Mr. Wang commenced his career in the People's Bank of China, Lanxi County branch. He had been the manager of the credit and loan department and a vice president of Industrial and Commercial Bank of China, Suihua branch, the department head of credit and loan department of Industrial and Commercial Bank of China, Heilongjiang branch, the president of Industrial and Commercial Bank of China, Qiqihar branch. At present, Mr. Wang serves as a vice chairman of China First Heavy Industries (Group) Co., Ltd., a vice chairman of Harbin Huaer Chemical Industry Co., Ltd. and a vice chairman of Harbin Turbine Co., Ltd.. Mr. Wang has been appointed as a director of the Company since June 2005.

Mr. Maurice Savart (Member of Aviation Business Development and Strategy Committee)

49, Chairman of Airbus Asia Advisory Council. Mr. Maurice commenced his career in science and technology for national defence in 1982 when he worked at the Training and Cooperation Department of the Ministry of Defence of France. He used to be the area sales manager (Asia) of the Thomson-CSF/Aerospace Group, the business development director (Asia Pacific), vice president (North Asia) of the Lagardere Group, the managing director (North Asia) of Aerospatiale Lagardere International and the senior vice president of EADS in charge of business in north Asia. He has been the Chairman of Airbus Asia Advisory Council from late 2007. Mr. Maurice graduated from the School of Engineering of Ecole Nationale Supérieure de Physique in France in 1980 and received his master degree in Science from the University of California in the USA in 1981 and a MBA degree from the School of Business Administration of Institut Supérieure des Affaires in France in 1982. Mr. Savart has been appointed as a director of the Company since June 2004.

Independent Non-executive Directors

Mr. Guo Chongqing（郭重慶）(Member of Audit Committee, Remuneration Committee and Automobile Business Development and Strategy Committee)

75, an academician of the Chinese Academy of Engineering and a professor of Tongji University, a professor of Shanghai Jiao Tong University, the consulting dean of the Mechanical Engineering Institute and Economics and Management Institute, the head of management and science department of the National Committee of Natural Science Funds and a member of the specialist committee of Chinese Association of Machine Building. He graduated from Harbin Polytechnical University in 1957 majoring in machinery manufacturing and was an assistant professor in the university. He had been the chief designer of a number of major national construction projects, and was awarded the "Chinese Master of Engineering Design". Mr. Guo has been appointed as an independent non-executive director of the Company since May 2003.

Mr. Li Xianzong （李現宗）(Chairman of Audit Committee and member of Remuneration Committee)

51, a professor and supervisor for master degree students. He graduated from Zhengzhou Institute of Aeronautical Industry Management in 1982. He then graduated from Tianjin Finance and Economics Academy in 1996 with a master degree majoring in accounting. Mr. Li was the deputy chairman and subsequently the chairman of the Accounting Department of Zhengzhou Institute of Aeronautical Industry Management. He is the deputy dean of Zhengzhou Institute of Aeronautical Industry Management. Mr. Li was an independent non-executive director of Guizhou Guihang Automobile Parts Joint Stock Company Limited. Mr. Li is also a member of the Association of Accounting in the PRC, non-practicing member of the Chinese Institute of Certified Public Accountants in the PRC, an asset appraiser, member of the Institute of International Internal Auditors, and a member of the third Council of the Chief Accountants' Association in the PRC. Mr. Li has been appointed as an independent non-executive director of the Company since August 2004.

Mr. Lau Chung Man, Louis （劉仲文） (Member of Audit Committee and Remuneration Committee)

49, executive director and CFO of Sing Tao News Corporation ("Sing Tao", a company listed on the main board of the Stock Exchange). Mr. Lau joined Sing Tao on 23rd May 2005. Mr. Lau is a Chartered Accountant and has been granted the Master of Business and Administration in Victoria University of Wellington, New Zealand. Mr. Lau is also a member of New Zealand Institute of Chartered Accountants (NZICA) and an associate member of Hong Kong Institute of Certified Public Accountants (HKICPA). He has experience in accounting and finance for more than 21 years. Before he joined the Sing Tao, he had been an executive director of China Everbright Ltd. (a company listed on the main board of the Stock Exchange) since 1st September 2002. Mr. Lau has been appointed as an independent non-executive director of the Company since August 2006.

Supervisors

Mr. Tang Jianguo（湯建國）

56, a research professor and a vice president of AVIC II. He graduated from Beijing University of Aeronautics and Astronautics majoring in metallic materials and welding engineering. He commenced his career in the aviation industry in December 1971 and used to serve at Factory No.550 under the Ministry of Aviation Industry, Beijing University of Aeronautics and Astronautics, AVIC and vice director and the director of the human resources department of AVIC II. He is the chief director of China Aviation Industry and Technology Research Institute, a research fellow of China Engineering Academy, a research fellow of Beijing University of Aeronautics and Astronautics Advanced Education Study Centre, a research fellow of China Labour Scientific Institute（中國勞動科學院）and vice chairman of the remuneration committee of China Labour's Society. Mr. Tang has been appointed as a supervisor of the Company since April 2003 and as the chairman of the Supervisory Committee since August 2006.

Mr. Wang Shouxin（王守信）

65, a professional adviser of AVIC II and a researcher level senior engineer. He graduated from Peking University in 1967 majoring in mathematics mechanics. He commenced his career in aviation industry in August 1968 and used to be a deputy director and the director of the specialist division of the personnel department of the Ministry of Aviation Industry, an assistant to the director of the science and technology research institute of the Ministry of Aero-Space Industry, a deputy director and the director of the exploration and design institute of AVIC, the director of the security department of AVIC, the director of the human resources department and the supervision department and the vice president of AVIC II. Mr. Wang has been appointed as a supervisor of the Company since April 2003.

Mr. Li Shentian（李申田）

61, a researcher level senior engineer, the general counsel of AVIC II and a qualified PRC practicing lawyer and enterprise legal adviser. He graduated from Beijing Aeronautics College and Nanjing Huadong Engineering Institute, majoring in exterior ballistics, and from Beijing Renwen Correspondence University majoring in law. He also took the examination in legal professional in the National Tertiary Self Study Education Examination. He commenced his career in aviation industry in 1970 and used to be a technician in Harbin Aircraft Manufacturing Company, a secretary of the general office and a deputy director of the legal division of the Ministry of Aviation Industry, the director of the legal division of the policy and legal department, an inspector, a deputy director of the supervision department and a legal counsel of the Ministry of Aero-Space Industry, a deputy director of the general office and the director of the legal centre of AVIC and the director of the general office of AVIC II. Mr. Li has been appointed as a supervisor of the Company since April 2003.

Ms. Bai Ping（白萍）

53, a class one senior accountant, a certified public accountant and a deputy chief accountant of AVIC II. She graduated from Zhengzhou Aviation Industry Management Institute majoring in financial management. She also took the business administration diploma course in the faculty of economics, management and human resources training center in Beijing University of Aeronautics and Astronautics and an MBA course sponsored by the University of California, USA. She commenced her career in aviation industry in 1970 and served as a staff in the management office of electronic component division of Shaanxi Xingping Qinling Company, an auditor of the audit department of the Ministry of Aero-Space Industry, a deputy director and the director of the audit office under the finance department of AVIC, and the director-general of the finance and audit department of AVIC II. Ms. Bai has been appointed as a supervisor of the Company since April 2003.

Mr. Han Xiaoyang （韓曉暘）

38, a senior economist. He is also the director-general of the supervision and audit department of AVIC II. Mr. Han graduated from Renmin University of China with a bachelor degree in 1991, majoring in national economy administration and obtained a master degree in engineering from Beijing University of Aeronautics and Astronautics in 2001. He commenced his career in aviation industry since July 1991 and served as a staff in the department for employees' affairs, the deputy director of human resources department, the general manager of Harbin branch, the general manager of International Project Company of China National Aero-Technology Import & Export Co., Ltd. and the deputy director-general of the supervision and audit department of AVIC II. Mr. Han has been appointed as a supervisor of the Company since June 2006.

Mr. Yu Yan （于岩）

45, a senior economist. Mr. Yu also serves as an assistant manager of the assets management department of China Orient Asset Management Corporation, Harbin Office responsible for assets and stock management. From 1989, he worked in the Bank of China, Heilongjiang branch's finance research institute, trust and investment corporation and corporate department engaged in research, investment management, investment fund and credit and loan operations. He joined China Orient Asset Management Corporation Harbin Office since 2000. Mr. Yu has been appointed as a supervisor of the Company since April 2003.

Mr. Li Deqing（李德慶）

39, a senior economist. He is also the vice general manager of the assets preservation department of China Construction Bank Corporation, Heilongjiang branch. Mr. Li graduated from the Economy and Trade Institute of Northeast Agricultural University with a master degree in 1992, majoring in economy administration. He commenced his career in China Construction Bank Corporation, Heilongjiang branch since 1998 and served as a secretary in the office for managers, the head of secretaries, an assistant to directors and the vice manager of the investment department. Mr. Li has been appointed as a supervisor of the Company since June 2006.

Independent Supervisors

Ms. Zheng Li（鄭力）

72, a senior economist, a registered accountant and an international registered internal auditor. She graduated from Moscow Finance and Economics Institute in January 1959. She then worked in the former State Development and Planning Commission and held the position of deputy division head, division head and deputy department head of the general department of national economy of the State Development and Planning Commission; she was a full-time committee member of the State Development and Planning Commission; the deputy auditors-general of the Auditing Administration, a special inspector of the State Council and member of the supervisory board of China Development Bank and the chairman of China Internal Audit Committee. She was a deputy to the 9th China People's Political Consultative Committee, member of the executive board of the 5th, 6th and 7th All-China Women's Federation and was awarded the National "Eighth of March" Red Flag Bearer. Ms. Zheng has been appointed as an independent supervisor of the Company since September 2003.

Mr. Xie Zhihua (謝志華)

48, a professor and a vice chancellor at the Beijing Business University, a Ph.D. degree holder, a certified public accountant, a vice chairman of China Commerce and Economy Academy, a vice chairman of China Commerce and Accounting Academy, a standing director of China Audit Academy, a director of China Accounting Academy, a director of China Financial Academy, a director of China Cost Academy and a vice chairman of the Guidance Committee of Industrial and Commercial Subjects of Education Ministry. He also serves as visiting professor in twenty universities and institutes, such as the Science and Research Institute under the Financial Ministry. He is a special research fellow at the Chinese Study Centre of University of Cardiff in the United Kingdom and a visiting professor at the King's College in Canada. He is awarded ministry-level young specialist in management and special subsidy by the State Council as a specialist. Mr. Xie has been appointed as an independent supervisor of the Company since May 2003.

Senior Management

Mr. Li Hui (李慧)

52, a vice president of the Company. He is also a researcher level senior engineer and holds a post-graduate degree. He graduated from Beijing University of Aeronautics and Astronautics majoring in computer programme system design and economics and management. He commenced his career in the aviation industry in September 1978 and used to be a technician at the electrical equipment division of the ancillary machine department of the Third Ministry of the Machine-Building Industry and general office secretary, an assistant engineer at the Third Ministry of the Machine-Building Industry, secretary and engineer at general office of the Ministry of the Aviation Industry, a deputy director and the director of the trading division of China Aviation Industry Science and Technology Corporation, a deputy general manager of China Aviation Industry Science and Technology Corporation, a deputy director, the general deputy director and the director of the general office of AVIC II, and the director of China Aviation Industry Economy Technology Research Centre and the director of development and research department. Mr. Li has been appointed as the vice president of the Company since April 2003.

Mr. Li Yao (李耀)

43, a vice president and the chief financial officer of the Company and a senior accountant. He is also a director of Hafei Aviation. He graduated from Zhengzhou Aviation Industry Management Institute majoring in finance and accounting and studied in the Beijing University of Aeronautics and Astronautics majoring in corporate management and industrial economics. He commenced his career in the aviation industry in July 1986 and served as a staff official in the finance department of the Ministry of Aviation Industry and the Ministry of Aero-Space Industry, a deputy director of the enterprise division of the finance department of AVIC and a deputy director of the finance and audit department of AVIC II. He has been the chairman of Changhe Auto since August 2007. Mr. Li has been appointed as the vice president of the Company since April 2003.

Mr. Liu Tao （劉濤）

54, a vice president and a class one senior economist. Mr. Liu graduated from Hafei Industry Institute majoring in enterprise administration. He commenced his career in the aviation industry in August 1969 and used to be the chief supervisor of workshop and vice director of the production department of Harbin Aircraft Manufacturing Co., Ltd., a deputy general manager and the general manager of Hafei Auto Co., Ltd., a deputy general manager and a member of the board of Harbin Aircraft Industry (Group) Co., Ltd., a deputy general manager and a member of the board of Harbin Aviation Industry (Group) Co., Ltd. and the chairman of Hafei Automobile Industry Group Co., Ltd.. Mr. Liu has been appointed as the vice president of the Company since August 2007.

Company Secretary

Mr. Yan Lingxi（閆靈喜）

38, a senior engineer. He is also a director of Hongdu Aviation, a director of Dongan Motor and a supervisor of Hafei Aviation. He graduated from the Beijing University of Aeronautics and Astronautics with a bachelor degree in engineering (majoring in management information system) in 1991 and with a master degree in management in 1999. He commenced his career in the aviation industry in July 1991 and worked in the reform bureau of the Ministry of Aero-Space Industry, the corporate management office of Nanjing Jincheng Machinery Factory, the corporate management department and the asset and business management department of AVIC. He was appointed as a deputy division director and a division director of the corporate assets management department of AVIC II, and is also the director in the security and legal department of the Company. Mr. Yan has been appointed as the Company Secretary of the Company since April 2003.

Mr. Ip Kun Wan, Kiril（葉冠寰）

47, also a managing director of China Everbright Investments Management Limited, a wholly owned subsidiary of China Everbright Limited (a company listed on the Stock Exchange). Mr. Ip was the company secretary and legal counsel of China Everbright Limited. He started his career as marine engineer and subsequently changed his career to becoming a solicitor of the High Court of Hong Kong. Mr. Ip graduated from the University of Hong Kong with a bachelor degree in mechanical engineering and from the University of Sydney with a master degree in transport management. Mr. Ip has been appointed as the Company Secretary of the Company since September 2003.

The Board presents its annual report of the directors together with the audited financial statements of the Group for the year ended 31st December 2007.

BUSINESS OF THE GROUP

The Group is principally engaged in the research, development, manufacture and sale of automobiles and civil aviation products.

RESULTS AND DIVIDEND

The results of the Group for 2007 are set out in the Consolidated Income Statement on page 52 of the Annual Report.

The Board recommended no distribution of final dividend for the year ended 31st December 2007.

SHARE CAPITAL

In 2007, there were no changes in the share capital of the Company.

The Company's capital structure as at 31st December 2007 was as follows:

Class of shares	**Number of shares as at 31st December 2007**	**Percentage of total number of shares in issue as at 31st December 2007** (%)
Domestic shares	2,963,808,000	63.83
Overseas listed foreign invested shares (H shares)	1,679,800,500	36.17
Total	4,643,608,500	100

SHAREHOLDINGS OF SUBSTANTIAL SHAREHOLDERS

As at 31st December 2007, pursuant to the register kept under Section 336 of the Securities and Futures Ordinance (the "SFO"), shareholders holding more than 5% equity interests in the Company and associated corporations were as follows:

Name of Shareholders	Class of shares	Number of shares	Percentage of shareholdings in the same class of shares	Percentage of shareholdings out of share capital in issue	Nature of shares held
AVIC II	Domestic shares	2,835,305,636	95.66%	61.06%	Long position
EADS	H shares	232,180,425	13.82%	5%	Long position
The Hamon Investment Group Pte Limited	H shares	204,580,000	12.18%	4.41%	Long position
Montpelier Asset Management Limited	H shares	105,420,000	6.28%	2.27%	Long position
The Bank of New York Mellon Corporation	H shares	101,412,000	6.04%	2.18%	Long position
Mellon Financial Corporation	H shares	85,706,000	5.10%	1.85%	Long position

Save as disclosed above, as at 31st December 2007, the Company had not been notified of any interests and short positions in 5% or more than 5% of shares and underlying shares of the Company which had been recorded in the register kept under section 336 of the SFO.

PURCHASE, SALE AND REDEMPTION OF SHARES

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares for the year ended 31st December 2007.

PRE-EMPTIVE RIGHTS

There are no provisions in respect of pre-emptive rights under the Articles of Association and the laws of the PRC.

DESIGNATED DEPOSITS AND OVERDUE FIXED DEPOSITS

As at 31st December 2007, there was no designated deposit or overdue fixed deposit placed by the Group that could not be collected by the Group upon maturity.

FIXED ASSETS

Details of fixed assets of the Company are set out in note 14 to the financial statements.

RESERVES

Details of movement in reserves of the Group for the year ended 31st December 2007 are set out in the Consolidated Statement of Changes in Equity and note 35 to the financial statements.

DISTRIBUTABLE RETAINED EARNINGS

As at 31st December 2007, the Company had no distributable retained earnings.

MAJOR CUSTOMERS AND SUPPLIERS

During the reporting period, the Group's total purchases from the five largest suppliers accounted for 7.28% of the Group's total purchases, of which purchases from the largest supplier accounted for approximately 2.81% of the Group's total purchases. The Group's sales to the five largest customers accounted for 36.98% of the Group's total sales, of which, sales to the largest customer accounted for 10.86% of the Group's total sales.

Purchases of aviation segment from the five largest suppliers accounted for 15.93% of the total purchases in the Group's aviation segment, of which, purchases from the largest supplier accounted for 8.36% of the total purchases in the Group's aviation segment. Sales in the aviation segment to the five largest customers accounted for 72.21% of the total sales in the Group's aviation segment, of which, sales to the largest customer accounted for 33.71% of the total sales in the Group's aviation segment.

Purchases of automobile segment from the five largest suppliers accounted for 7.93% of the total purchases in the Group's automobile segment, of which, purchases from the largest supplier accounted for 2.51% of the total purchases in the Group's automobile segment. Sales in the automobile segment to the five largest customers accounted for 30.05% of the total sales in the Group's automobile segment, of which, sales to the largest customer accounted for 11.03% of the total sales in the Group's automobile segment.

During the reporting period, save for the connected transactions with AVIC II Group, as disclosed in the section of Connected Transactions in the Annual Report, none of the directors, their associates or any shareholder holding more than 5% in the share capital of the Company has any interest in the above major suppliers and customers.

SUBSIDIARIES AND ASSOCIATES

Details of subsidiaries and associates are set out in note 42 to the financial statements.

CONNECTED TRANSACTIONS

Continuing Connected Transactions

The Group has engaged in several continuing connected transactions with AVIC II Group (AVIC II and its subsidiaries, together referring to as AVIC II Group, is a connected person of the Company as AVIC II is the controlling shareholder of the Company), joint venture partners (who are connected persons of the Company as they hold at least 10% interests in the subsidiaries of the Company) and non-wholly owned subsidiaries of the Company (who are connected persons of the Company as AVIC II or its associates hold 10% or more interests in them).

In 2007, the approved continuing connected transactions of the Company are as follows:

1. On 26th August 2005, the Company entered into a supplemental agreement with AVIC II to renew the terms of the product and ancillary services mutual supply agreement ("Mutual Supply Agreement") for a further term of three years expiring on 31st December 2008, whereby the AVIC II Group has agreed to provide certain products and services to the Group and the Group has agreed to provide certain products and services to AVIC II Group.

2. On 26th August 2005, the Company entered into a supplemental agreement with AVIC II to renew the terms of the comprehensive services agreement ("Comprehensive Services Agreement") for a further term of three years expiring on 31st December 2008, whereby AVIC II Group has agreed to provide certain social welfare and logistics services to the Group.

3. On 2nd October 2003, the Company entered into a land use rights leasing agreement ("Land Use Rights Leasing Agreement") with AVIC II whereby the AVIC II Group has agreed to lease to the Group 48 pieces of land, with an aggregate area of approximately 2.9 million square metres at the annual rent of approximately RMB37.6 million. The land is used by the Group as workshops, warehouses, an administrative office and ancillary facilities. The term of the lease is 20 years.

4. On 26th August 2005, the Company entered into a supplementary agreement for the properties leasing agreement ("Properties Leasing Agreement") with AVIC II whereby the AVIC II Group has agreed to lease to the Group certain properties with an aggregate gross floor area of approximately 111,000 square metres ("Rented Properties") at an annual rent of approximately RMB24 million. Similarly, the Group has agreed to lease to the AVIC II Group certain properties with an aggregate gross floor area of approximately 36,000 square meters ("Leased Properties") at an annual rent of approximately RMB1.1 million. The Rented Properties are built on leased lands and used by the Group as workshops, warehouses and ancillary facilities. The Leased Properties are used by AVIC II as workshops, warehouses and ancillary facilities.

5. On 26th August 2005, the Company entered into a supplementary agreement with AVIC II to renew the terms of the technology cooperation framework agreement ("Technology Cooperation Agreement") for a further term of three years expiring on 31st December 2008, whereby the AVIC II Group has agreed to transfer or grant a licence to the Group to use certain existing technologies required for the Group's business in connection with the production of aviation products and automobiles. The agreement has also provided for future co-operation between the AVIC II Group and the Group in respect of development of new technology.

6. On 30th June 1999, Dongan Engine entered into a technology transfer agreement ("Mitsubishi Technology Transfer Agreement") with Mitsubishi, a connected person by virtue of it being a substantial shareholder of Dongan Engine, whereby Mitsubishi has agreed to grant to Dongan Engine a licence to use the industrial properties rights, patent and technology documents relating to engines, gearboxes and the respective assemblies, parts and components.

7. As part of the joint venture establishment agreement of Dongan Engine dated 16th June 1998, the CKD spare parts supply agreement between Dongan Engine and Mitsubishi ("Mitsubishi CKD Agreement") states that Dongan Engine agrees to purchase CKD spare parts and components from Mitsubishi.

8. On 26th August 2005, the Company and its subsidiaries entered into a supplementary agreement to renew the term of the internal connected transaction agreement ("Internal CT Agreement") for a further term of three years expiring on 31st December 2008, which set out the general principles of the transactions between the Company (or its wholly-owned subsidiaries) and the non-wholly owned subsidiaries of the Company and transactions between the non-wholly owned subsidiaries of the Company. Dongan Engine and Hafei Auto are the two parties engaging in transactions according to the Internal CT Agreement.

9. On 2nd June 2005, the Group entered into the Agusta Agreement with Agusta, a connected person by virtue of it being a substantial shareholder of Changhe Agusta (a joint venture established by the Group and Agusta, whereby Agusta agrees to provide to Changhe Agusta parts and components for manufacturing helicopters and assistance in manufacturing, assembling and selling helicopters.

10. On 24th December 2003, 21st March 2005 and 24th December 2003, Changhe Suzuki entered into three licence agreements ("Suzuki Licence Agreement") with Suzuki, a connected person by virtue of it being a substantial shareholder of Changhe Suzuki, namely Liana Licence Agreement, New Model Technology Transfer Agreement and K Series Licence Agreement, whereby Suzuki agrees to grant Changhe Suzuki licence to use Suzuki's technologies in manufacturing, assembling and selling Lianas, new models, K series engines, gear boxes and relevant parts and components and to use relevant patents, brands and technologies, provide technical assistance, and supply relevant parts and components.

11. Hafei Auto entered into Mitsubishi Joint Development Agreement with Mitsubishi, whereby Mitsubishi agrees to provide assistance to Hafei Auto in developing automobile products with Mitsubishi's technologies and grant Hafei Auto licence to use certain Mitsubishi's automobile technologies, information and patents.

12. Hafei Auto entered into Mitsubishi Hafei Parts and Components Contract with Mitsubishi, whereby Hafei Auto agrees to purchase CKD spares and parts from Mitsubishi so as to use Mitsubishi's technologies in manufacturing automobiles.

Proposed annual caps for financial years 2006, 2007 and 2008 of respective continuing connected transactions are set out as follows:

		Proposed Annual Caps RMB million		
		Financial year ended 31st December		
Agreements		**2006**	2007	2008
1	**Mutual Supply Agreement**			
	(a) Annual expenditures of the Group	**3,000**	3,500	4,000
	(b) Annual revenues of the Group	**5,400**	7,000	8,500
2	**Comprehensive Services Agreement**			
	Annual expenditures of the Group	**180**	200	220
3	**Land Use Rights Leasing Agreement**			
	Annual expenditures of the Group	**38**	38	38
	Properties Leasing Agreement			
	(a) Annual expenditures of the Group	**24**	24	24
	(b) Annual revenues of the Group	**1.1**	1.1	1.1
4	**Technology Co-operation Agreement**			
	(a) Annual expenditures of the Group	**33**	36	40
	(b) Annual revenues of the Group	**22**	24	27
5	**Mitsubishi Technology Transfer Agreement**			
	Annual expenditures of the Group	**8**	120	150
	Mitsubishi CKD Agreement			
	Annual expenditures of the Group	**36**	400	450
6	**Internal CT Agreement**			
	(i) Annual expenditures of Dongan Engine and Hafei Auto	**2,700**	3,200	3,800
	(ii) Annual revenues of Dongan Engine and Hafei Auto	**500**	550	600
	(iii) Annual guarantees provided by subsidiaries of the Group to Hafei Auto	**2,000**	2,000	2,000
7	**Agusta Agreement**			
	Annual expenditures of the Group	**78**	117	117
8	**Liana Licence Agreement, New Model Technology Transfer Agreement and K Series Licence Agreement**			
	Annual expenditures of the Group	**1,105**	2,070	2,121
9	**Mitsubishi Joint Development Agreement**			
	Annual expenditures of the Group	**41**	38	53
	Mitsubishi Hafei Parts and Components Contract			
	Annual expenditures of the Group	**30**	95	135

The Board (including independent non-executive directors) has reviewed the above continuing connected transactions and confirmed that they had been entered into under the following conditions:

(a) The transactions were entered into in the ordinary and usual course of business of the Group;

(b) The transactions were entered into: i) on normal commercial terms; or ii) in accordance with the relevant agreements governing such transactions, on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; and iii) where there is no appropriate comparison for the purposes of determing whether the above (i) or (ii) is satisfied, on terms that are no less favourable to the Company than terms available to or from (as appropriate) independent third parties; and

(c) The aggregate amounts of the transactions have not exceeded the respective caps as set out above.

The Company's auditors have reviewed the relevant transactions, and have confirmed in a letter to the Directors stating that:

(a) The transactions have received the approval of the Board;

(b) The transactions have been entered into in accordance with the pricing policies as stated in the relevant agreements, or if no such policies or agreements are available, on terms no less favourable than those available from/to (as appropriate) independent third parties;

(c) The transactions have been entered into in accordance with the terms of the respective agreements and documents governing the transactions, or if no such agreements or documents are available, on terms no less favorable than those available from/to (as appropriate) independent third parties; and

(d) The aggregate amounts of the transactions have not exceeded the respective annual caps as set out above.

ONE-OFF CONNECTED TRANSACTIONS

1. Hongdu Aviation, a 55.29% owned subsidiary of the Company entered into an agreement with Hongdu Group on 24th September 2007, pursuant to which Hongdu Aviation would acquire Hongdu Group's property rights in a science building from Hongdu Group with a total consideration of RMB10,618,000 (equivalent to approximately HK$11,061,000). This consideration was paid by internal resources of Hongdu Aviation. This agreement constitutes a connected transaction of the Company under Chapter 14A of the Listing Rules. As each of the percentage ratios (as defined in the Listing Rules), other than the profits ratios (as defined in the Listing Rules), for the transaction is below 2.5%, the agreement is only subject to the reporting and announcement requirements under Rule 14A.45 to Rule 14A.47 of the Listing Rules. Details of the transaction have been disclosed in an announcement issued by the Company on 27th September 2007.

2. The Company entered into a joint venture agreement with AVIC II and its associates and other non-connected persons on 19th October 2007 to establish a joint venture to invest in the manufacture and sale of wind power generation equipment in China (the "Joint Venture Agreement"). The Joint Venture Agreement constitutes a connected transaction of the Company under the Listing Rules. As each of the percentage ratios (as defined in the Listing Rules), other than the profits ratios (as defined in the Listing Rules), for the transaction is below 2.5%, the Joint Venture Agreement is only subject to the reporting and announcement requirements under Rule 14A.45 to Rule 14A.47 of the Listing Rules. Details of the transaction have been disclosed in an announcement issued by the Company on 22nd October 2007.

3. The board of Hongdu Aviation resolved on 30th December 2007 the proposed issue and placing of new Hongdu Shares for subscription by not more than 10 qualified investors, including the Company and Hongdu Group. After taking into account of Hongdu Aviation 2007 dividend policy, the minimum placing price of each new share of Hongdu Group ("Hongdu Share") would be not less than RMB25.4, and the total number of new Hongdu Shares to be issued would be not more than 98,000,000, both of which will be determined by the bidding process according to the requirements of relevant PRC authorities. Hongdu Aviation entered into the subscription agreements and supplemental agreements with the Company and Hongdu Group on 29th December 2007 and 22nd February 2008, respectively. Pursuant to the agreements, the Company undertakes, subject to conditions and completion, to subscribe approximately 9,842,520 new Hongdu Shares, subject to adjustment, among the new Hongdu Shares to be issued by Hongdu Aviation with a consideration to be satisfied by the Company's internal resources; and Hongdu Group undertakes, subject to conditions and completion, to subscribe approximately 13,779,527 new Hongdu Shares, subject to adjustment, among the new Hongdu Shares to be issued by Hongdu Aviation with a consideration to be satisfied by Hongdu Group transferring to Hongdu Aviation certain assets. The subscription of Hongdu Shares by Hongdu Group and the transfer of assets to Hongdu Aviation by Hongdu Group constitute a connected transaction of the Company under the Listing Rules and will be subject to approval by independent shareholders of the Company. Upon completion of the subscription, the aggregate shareholding of Hongdu Aviation held by the Company will be diluted from 55.29% to approximately 46.09%. The dilution constitutes a deemed disposal and material dilution of the interest held by the Company in Hongdu Aviation pursuant to Rules 14.29 and Rule 13.36(1)(a)(ii) as well as a major transaction under the Listing Rules, which will be subject to approval by the independent shareholders of the Company. To ensure that Hongdu Aviation will remain as a subsidiary of the Company, the Company and Hongdu Group entered into an agreement on 29th December 2007 whereby after the completion of the transaction, Hongdu Group undertakes to vote its voting rights in Hongdu Aviation in accordance with the instructions of the Company. Accordingly, upon the completion of the transaction, Hongdu Aviation will continue to be consolidated in the group accounts of the Company. Details of the transaction have been disclosed in the announcements issued by the Company on 9th January 2008 and 22nd February 2008 as well as the circular despatched to the shareholders of the Company on 25th February 2008. The transaction mentioned above had been approved at the first extraordinary general meeting of the Company in 2008 held on 31st March 2008.

4. Hongdu Aviation, a 55.29% owned subsidiary of the Company, entered into an agreement with AVIC II and its associates, China Huarong Assets Management Corporation ("China Huarong"), AviChina Undercarriage Limited Liability Company ("AviChina Undercarriage") and an independent third party on 26th March 2008 (the "AviChina Undercarriage Capital Injection Agreement"), according to which Hongdu Aviation would inject RMB100 million (equivalent to approximately HK$110.18 million) as capital into AviChina Undercarriage. AVIC II is the controlling shareholder of the Company, holding 61.06% equity interests in the Company. China Huarong is one of the promoters of the Company, holding 2.14% equity interests in the Company. As AVIC II is a substantial shareholder of AviChina Undercarriage, the proposed injection of capital by Hongdu Aviation into AviChina Undercarriage pursuant to the AviChina Undercarriage Capital Injection Agreement would constitute a connected transaction of the Company under the Listing Rules. On the same day, Hongdu Aviation, Hongdu Group and Jiangxi Changjiang General Aviation Co., Ltd. ("Changjiang General Aviation") entered into an agreement, according to which Hongdu Aviation would inject RMB49.96 million (equivalent to approximately HK$55.05 million) as capital into Changjiang General Aviation ("Changjiang General Aviation Capital Injection Agreement"). Hongdu Group is a subsidiary of AVIC II, therefore, an associate of AVIC II and a connected person of the Company. As Hongdu Group is a substantial shareholder of Changjiang General Aviation, the proposed capital injection by Hongdu Aviation into Changjiang General Aviation pursuant to Changjiang General Aviation Capital Injection Agreement would constitute a connected transaction of the Company under the Listing Rules. The capital injections mentioned above would be paid by Hongdu Aviation out of the proceeds to be raised in the proposed placing of new shares by Hongdu Aviation (for details, please refer to items (g) and (j) of the "Use of Proceeds" section as disclosed in the circular despatched to the shareholders of the Company on 25th February 2008). The AviChina Undercarriage Capital Injection and Changjiang General Aviation Capital Injection were not inter-conditional. As each of the percentage ratios (as defined in the Listing Rules), other than the profits ratio (as defined in the Listing Rules), for the aggregate of the proposed capital injections was below 2.5%, the proposed capital injections were only subject to the reporting and announcement requirements under Rule 14A.45 to Rule 14A.47 of the Listing Rules. Details of the transactions have been disclosed in an announcement published by the Company on 27th March 2008.

OTHER SIGNIFICANT ISSUES

1. During the period from September 2007 to January 2008, the Company had sold an aggregate of 13,800,000 shares of the listed A shares in Changhe Auto, accounting for 3.37% in the total share capital of Changhe Auto; and 3,434,000 shares of the listed A shares in Dongan Motor, accounting for 0.74% of the total share capital of Dongan Motor.

2. On 3rd March 2008, Dongan Motor published an announcement on the Shanghai Stock Exchange, which stated that: the Company intended to contribute its equity interest which is subject to trading restrictions in Dongan Motor as capital contribuition, Hafei Auto, a subsidiary of the Company, intended to contribute some of its automobile business assets as capital contribution and Dongfeng Motor Corporation intended to contribute cash for co-operation and the formation of a joint venture. The transaction was under negotiation and no agreement in this regard had been reached.

CORPORATE GOVERNANCE

Details of corporate governance practices adopted by the Company are set out in the section of "Corporate Governance Report" of the Annual Report.

PUBLIC FLOAT

Based on the information that is available to the Company and to the knowledge of the Board, as at the date of this report, there is sufficient public float of more than 25% of the Company's issued shares as required under the Listing Rules.

AUDITORS

The financial statements for the year have been audited by PricewaterhouseCoopers. In the forthcoming annual general meeting, a resolution for the re-appointment of PricewaterhouseCoopers as the international auditor of the Company for the financial year of 2008 will be presented.

CHANGES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Mr. Liu Tao and Mr. Liu Hongde were appointed as vice presidents of the Company at a board meeting of the Company held on 27th August 2007. Mr. Liu Hongde subsequently resigned from his position as the vice president of the Company on 11th April 2008 due to change of work position. Save as disclosed herein, there were no changes to the directors, supervisors and senior management of the Company for the year ended 31st December 2007.

SERVICE CONTRACTS OF DIRECTORS AND SUPERVISORS

Each of the Directors (except the independent non-executive directors) and Supervisors has entered into a service contract with the Company. None of the Directors and Supervisors has entered into service contracts which are not terminable by the Company within one year without payment of compensation (other than statutory compensation).

DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS

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

THE INTERESTS OF DIRECTORS, SUPERVISORS AND CHIEF EXECUTIVE IN THE SECURITIES OF THE COMPANY

As at 31st December 2007, none of the Directors, Supervisors and Chief Executive of the Company had interests or held short positions in the shares of the Company and/or shares, relevant shares and/or securities of its associated corporations (within the meaning of Part XV of the SFO), which are required to be recorded and kept in the register pursuant to section 352 of the SFO and be notified to the Company and the Stock Exchange pursuant to Part XV, Part 7 and Part 8 of the SFO.

REMUNERATION OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Details of remuneration of the existing Directors, Supervisors and senior management are set out in note 13 to the financial statements.

RIGHTS OF DIRECTORS AND SUPERVISORS TO ACQUIRE SHARES OR DEBENTURES

As at 31st December 2007, none of the Directors or Supervisors was entitled to acquire shares or debentures of the Company.

MANAGEMENT CONTRACTS

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

To all shareholders:

During the year of 2007, the Supervisory Committee strictly complied with the PRC Company Law, the Articles of Association and Procedural Rules for Meetings of Supervisory Committee and duly adhered to the principles of honesty and integrity in performing the supervisory duties and exercising the rights conferred on it by the Articles of Association, and also in good faith safeguarded the shareholders' interests in a diligent, pragmatic and serious manner.

The Supervisory Committee convened two meetings in 2007, at which 8 resolutions were considered and approved. The Supervisory Committee fulfilled its tasks on reviewing the 2006 Annual Report, 2007 Interim Report, plans on distribution of profits for 2006 and the first six months of 2007 respectively and budgets for 2007 of the Company. The Supervisory Committee had also attended the Board meetings and the general meetings held in 2007 to monitor the validity of procedures undertaken leading to the convening of and decisions made during the board meetings and general meetings. Through convening supervisory committee meetings and attending board meetings and general meetings, the Supervisory Committee performed its duties of supervising the major operating activities of the Group, as well as the performance of directors and senior management officers in discharging their duties and provided advice to the Board.

The Supervisory Committee has reviewed the Report of the Board which the Board submitted to the general meeting, and considered that the report has fairly reflected the current position of the Company. In 2007, the Board and the senior management of the Company had duly exercised various powers conferred by the shareholders pursuant to the laws, performed various obligations, and used their best endeavors to make important contributions to the development of the Company.

The Supervisory Committee has also reviewed the financial statements as audited by PricewaterhouseCoopers, and considered that the statements had fairly reflected the financial position and operating results of the Company. The Company's financial statements are prepared accurately with clear records and complete information.

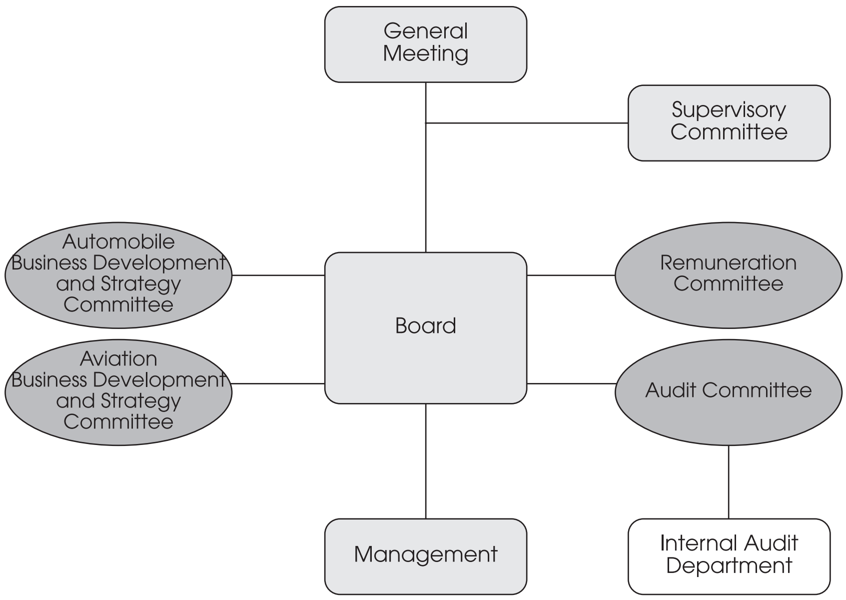
The Supervisory Committee is fully confident in the prospect of the Company. In 2008, the Supervisory Committee will continue to strictly perform its duties in accordance with the Articles of Association and the relevant requirements to safeguard shareholders' interests.

By Order of the Supervisory Committee

Tang Jianguo
Chairman of the Supervisory Committee
Beijing, the PRC, 11th April 2008

The Company strictly complies with various applicable laws, rules and regulations as well as the Articles of Association to standardize its operation. In 2007, under the framework guidance of the Articles of Association, Procedural Rules for General Meetings, Procedural Rules for Board Meetings, Procedural Rules for Meetings of Supervisory Committee, Working Guidelines for the Management, Working Guidelines for the Audit Committee, Terms of Reference of the Remuneration Committee and Rules on Information Disclosure, the Company continuously enhanced its corporate governance standard through the co-ordination of general meetings, the Board and the relevant special committees of the Board, Supervisory Committee and the management.

Governance structure of the Company is set out as follows:



CODE ON CORPORATE GOVERNANCE PRACTICES

The Board reviewed the corporate governance practices adopted by the Company and is of the view that the Company has complied with the principles and code provisions set out in the Code on Corporate Governance Practices (the "Code") in Appendix 14 to the Listing Rules.

THE BOARD

The Board is responsible for the leadership and supervision of the Company. The Board assumes the role to promote the business of the Company through directing and supervising the affairs of the Company.

DIRECTORS

The Board comprises thirteen Directors, including three executive Directors, namely, Mr. Zhang Hongbiao (Chairman), Mr. Wu Xiandong and Mr. Tan Ruisong, seven non-executive directors, namely, Mr. Liang Zhenhe, Mr. Song Jingang, Mr. Tian Min, Mr. Wang Bin, Mr. Chen Huaiqiu, Mr. Wang Yong and Mr. Maurice Savart and three independent non-executive directors, namely, Mr. Guo Chongqing, Mr. Li Xianzong and Mr. Lau Chung Man, Louis. The Directors have contributed their comprehensive knowledge, skills and experience for the effective management of the Group. With extensive professional knowledge and experience, the independent non-executive directors have assumed the supervisory and balancing roles in order to protect the interests of shareholders of the Company and the Company as a whole. The Board believes that the independent non-executive directors are capable of making judgments independently and comply with the guidelines on the independence of independent non-executive directors as set out in Rule 3.13 of the Listing Rules. In addition, the Company had received a written confirmation from each independent non-executive director on their independency, based on which the Company considers that the independent non-executive directors are independent.

The Company adopts the formal procedures in the appointment of new directors. The Company has not established any nomination committee. The Board will consider referrals from the shareholders and nominate new directors pursuant to certain standards. These standards include relevant professional knowledge and industry experience, personal ethics, integrity and skills of directors, as well as their time commitment to the affairs of the Company.

Each director (including non-executive director) holds office for a period of three years, and is eligible for re-election upon the expiration of the term of office. A list of directors, their respective profiles and roles in the Board and special committees of the Board are set out in page 21 to page 29 of the Annual Report. Relevant information will also be published on the website of the Company.

The Company has arranged for appropriate insurance coverage in respect of any legal actions which may be instituted against its directors and senior management in relation to their services.

RESPONSIBILITIES OF THE BOARD

The Board manages and supervises the Group on behalf of the shareholders of the Company. Each director is deemed to act in the best interest of the Company with prudence and honesty.

The Board regularly reviews the Group's overall strategy, its business targets and operational results. The Board exercises its power to formulate the objectives and strategies of the Group, and to monitor operational and financial performance of the Group.

The Board will ensure the completeness of the financial information and the effectiveness of internal control and risk management procedures of the Group. The Board is also responsible for preparing the financial statements of the Group. All Group policies, material transactions or transactions leading to conflicts of interest are decided by the Board. On the other hand, the chief executive officer is responsible for attaining the business targets of the Company and managing the daily operations. Duties reserved to the Board and those delegated to management are clearly set out in the Procedural Rules for Board Meetings and Working Guidelines for the Management. The Board regularly reviews the duties and powers delegated to the chief executive officer to ensure such arrangements are appropriate.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The roles of the chairman and the chief executive officer have been clearly segregated to ensure a balance of power and authority. The current chairman of the Company, Mr. Zhang Hongbiao, is responsible for leading the Board to ensure the effective operation of the Board. The chief executive officer, Mr. Wu Xiandong, is responsible for business operations of the Company. The roles and duties of the chief executive officer are clearly set out in the Working Guidelines for the Management.

BOARD MEETINGS

The Board has four scheduled meetings every year in April, June, August and December respectively. Matters to be considered at these regular board meetings are put into writing. Further, additional board meetings are held as and when required, and reasonable notices are sent to the Directors before the convening of such meetings.

The company secretaries assist the chairman in preparing the agenda for each board meeting and consider the matters proposed by other directors for inclusion in the agenda. The agenda and relevant materials are usually delivered to the directors at least three days before the relevant board meeting date. The chairman should ensure that all directors are properly briefed on issues to be discussed at the board meeting and provided with relevant documents which contain analysis and background information.

The management has provided the directors and committee members with adequate and sufficient information on a timely basis. This will ensure that the directors and committee members are well-informed of the Company's latest development so that they may discharge their duties effectively. Every director has received comprehensive induction training upon his appointment. Directors are encouraged to constantly update their skills, knowledge and understanding of the business of the Group through the induction training, regular attendance to board meetings and committee meetings, and meetings with key personnel of the head office and various departments of the Group. In June 2007, the Company invited the independent non-executive directors of the Company to make visits to its subsidiaries and discuss with the management of those subsidiaries on production and operation problems, through which the directors had learned more about the business of the Company.

All directors have access to the services of the company secretaries. The company secretaries are responsible for ensuring that board procedures are followed and advising the Board accordingly. The company secretaries regularly update the Reference Guide for Directors and Supervisors to ensure that the Board is well-informed of the latest information on corporate governance and supervision as well as the development of the Group. Directors, the audit committee and the remuneration committee may seek independent professional advice at the Company's expenses in discharging their duties.

Directors are encouraged to discuss issues of the Group openly and frankly at board meetings and every executive director is available for inquires raised by non-executive directors. Independent non-executive directors may convene meetings amongst themselves if necessary to discuss issues related to the Group. Board minutes as well as any materials related to the board meetings are kept by the company secretaries and made available for inspection by any member of the Board.

The Board has established an audit committee and a remuneration committee to ensure good corporate governance. Duties of these committees are set out in accordance with the principles of the Code. In addition, the Company has established Aviation Business Development & Strategy Committee and Automobile Business Development & Strategy Committee to formulate long-term development strategies and to decide on substantial investments. Each committee reports directly to the Board. Minutes of committee meetings are kept by the company secretaries. In 2007, the Company convened no meeting of the Remuneration Committee, one meeting of the Aviation Business Development & Strategy Committee and two meetings of the Automobile Business Development & Strategy Committee, at which resolutions in respect of enlarging the registered capital of Changhe Aviation and making investments to automobile business had been considered and reviewed.

Seven meetings were held by the Board during 2007. The chief executive officer and vice presidents, including the chief financial officer, attended these meetings to brief the Board or reply to issues relating to resolutions discussed at those meetings. The attendance of every director (including the circumstance of appointing another director on his behalf) in the board meetings and the audit committee meetings in 2007 is set out below:

	Times of presence/Times of meetings should present	
Directors	**The Board**	**Audit Committee**
Executive directors		
Mr. Zhang Hongbiao	7/7	
Mr. Wu Xiandong	7/7	
Mr. Tan Ruisong	7/7	
Non-executive directors		
Mr. Liang Zhenhe	7/7	2/2
Mr. Song Jingang	7/7	
Mr. Tian Min	7/7	
Mr. Wang Bin	7/7	
Mr. Chen Huaiqiu	7/7	
Mr. Wang Yong	6/7	
Mr. Maurice Savart	7/7	
Independent non-executive directors		
Mr. Guo Chongqing	7/7	2/2
Mr. Li Xianzong	7/7	2/2
Mr. Lau Chung Man, Louis	7/7	2/2

INTERESTS HELD AND SECURITIES TRANSACTIONS BY DIRECTORS

All Directors should declare to the Board whether they hold offices or positions in other companies or entities upon their appointments as directors and they are required to update the Board annually in respect of their relevant interests. If the Board considers that a director has conflict of interest in any motion or transaction, the director shall declare his interests and abstain from voting. If required, the director should be excused from the meeting.

Interests of the Company held by the Directors as at 31st December 2007 have been disclosed on page 39 of the Report of the Board of the Annual Report. The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") set out in Appendix 10 to the Listing Rules as its own guidelines for securities transactions by Directors and employees of the Company. All directors and supervisors have been provided with a copy of the Model Code upon appointments. The Directors and supervisors of the Company, will receive written reminders of the restrictions on dealing in any securities or derivatives of the Company. The written reminders will be provided one month prior to the board meeting of the Company for approving annual or interim results. All Directors and supervisors of the Company have confirmed their compliance with the Model Code in 2007 upon specific enquiries with them.

Employees who may likely possess unpublished price sensitive information of the Group are also required to comply with the Model Code. The Company is not aware of any breach in this regard in 2007.

REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

The Board has established a remuneration committee which comprises one non-executive director Mr. Song Jingang, as the chairman and three independent non-executive directors, Mr. Guo Chongqing, Mr. Li Xianzong and Mr. Lau Chung Man, Louis. The remuneration committee is responsible for approving policies on remuneration of all directors, supervisors and senior management, as well as making recommendations to the Board on revising policies and structure for remuneration. The remuneration committee reports to the Board after every meeting. Terms of reference of the remuneration committee are published on the website of the Company.

Details of the remunerations of the directors, supervisors and senior management of the Company for the year ended 31st December 2007 are set out in note 13 to the financial statement.

ACCOUNTABILITY AND AUDIT

FINANCIAL REPORTS

The Board is responsible for monitoring the preparation of the financial statements for every financial period and ensuring those financial statements provide a true and fair view on the results of operations, financial position and cash flow of the Group in the relevant financial period. In preparing the financial statements for the year ended 31st December 2007, the directors have:

— selected appropriate accounting policies and applied them consistently;

— adopted all the relevant standards in the International Financial Reporting Standards; and

— made a prudent and reasonable judgment and estimation and prepared financial statements on a going concern basis.

In accordance with the requirements of the Listing Rules, the Company has timely announced its annual and interim results within four and two months respectively after the end of the relevant financial periods.

INTERNAL CONTROL

The Board is responsible for maintaining a steady, appropriate and efficient internal control system of the Group to safeguard the Group's assets. The Board reviews the effectiveness of the internal control system annually through the audit committee.

The Company has established an Internal Audit Department which acts as a daily operation office of the audit committee of the Board to monitor how the Company and its subsidiaries establish and improve their respective internal control systems and give guidance in this respect, to supervise and review the implementation of regulations on internal control systems at proper times. In 2007, the Internal Audit Department prepared an annual assessment list on the internal control system and carried out a questionnaire, based on which the department evaluates the internal control system of the Group as a whole. The department also requested the senior management of each subsidiary to provide statements on the healthiness, reasonableness and effective implementation of their respective internal control procedures. The Internal Audit Department then conducted an evaluation based on the activities mentioned above and reported the results of such evaluation to the audit committee and the Board.

In the 2006 Annual Report of the Company, it is disclosed that two continuing connected transactions of the Group had exceeded their respective annual caps for the year 2006. The Company convened an annual general meeting on 15th June 2007 to approve the revised annual caps for those two continuing connected transactions. The Company has also taken certain measures to strengthen the scrutiny on the Group's continuing connected transactions, such as preparing a manual on connected transactions, requesting each subsidiary to provide reports on connected transactions per month and regularly evaluating the relevant financial effect.

The audit committee and the Board confirmed that the internal control system of the Group is effective in implementing the measures required in monitoring and controlling material aspects of the Group, preventing critical mistakes or severe damages to the Group, securing the safety of the Group's assets, ensuring proper maintenance of accounting records and compliance with laws and regulations as well as in accordance with the requirements on the internal control system set out in the Code as a whole.

However, due to inherent limits of the internal control system, the establishment of the Group's internal control system could manage potential risks but not be able to eliminate risks completely. Therefore, the internal control system could only provide a reasonable means, rather than an absolute means for the Group to achieve its operational targets. Likewise, the internal control system will not completely eliminate all material inaccurate statements made or damages done to the Group.

AUDIT COMMITTEE

The Board has established an audit committee and set out the terms of reference of the audit committee in accordance with the Guide for the Effective Audit Committee issued by the Hong Kong Institute of Certified Public Accountants.

The audit committee is responsible for monitoring the financial operation and audit procedures of the Company, assessing effectiveness of the internal control system and risk control system of the Company, maintaining effective communication with the management, internal audit department and external auditors of the Company, as well as performing other duties and responsibilities assigned by the Board. The majority of the audit committee members are independent non-executive directors, with Mr. Li Xianzong, an independent non-executive director, as the chairman of the committee. The chairman and most committee members have appropriate professional qualifications in accounting or related financial management expertise as required by the Listing Rules.

The terms of reference of the audit committee are published on the website of the Company.

The audit committee held two meetings during 2007 with the presence of management, chief financial officer and external auditors of the Company. In 2007, the audit committee reviewed and evaluated the audit results of the Company's external auditors, the accounting principles and standards applied by the Group and the internal control system and the financial statements of the Company. The audit committee reported to the Board its scope of work, discussion results and advice after every meeting. During 2007, the audit committee:

— reviewed the audited financial statements and the relevant annual results announcement of the Group for the year ended 31st December 2006;

— reviewed the interim financial information and the relevant interim results announcement of the Group for the six months ended 30th June 2007;

— reviewed resolution relating to appointments of international and PRC auditors of the Company for the financial year 2007 and determination of their respective remunerations;

— considered the resolution in relation to the proportionate consolidation of the results of Changhe Suzuki; and

— reviewed the self-assessment report on the internal control of the Company and the brief on the surveillance of connected transactions of the Company and provided recommendations to the management of the Company.

The audit committee had reviewed the Group's annual results and consolidated financial statements for the year ended 31st December 2007.

SUPERVISORY COMMITTEE

The Supervisory Committee is accountable to the general meetings of the Company. The committee comprises four supervisors selected from representatives of the Company's shareholders, three supervisors selected from employees of the Company and two independent supervisors. In 2007, the Supervisory Committee held two meetings and considered and approved eight resolutions. It supervised, on behalf of shareholders of the Company, the financial position of the Group, the legality of directors and senior management of the Company during the performance of their duties, attended the board meetings and general meetings and fulfilled its duties diligently.

EXTERNAL AUDITORS

In 2007, the payment to the Company's external auditors in relation to auditing services amounted to RMB5.5 million. The payments mentioned above had been approved at the general meeting.

The Board has resolved to propose at the forthcoming annual general meeting to re-appoint PricewaterhouseCoopers and PricewaterhouseCoopers Zhong Tian CPAs Limited Company as the international and PRC auditors of the Company to assume statutory audit work of the Company for the financial year 2008. The resolution is subject to the approval of shareholders at the annual general meeting of the Company for the year 2007.

INFORMATION DISCLOSURE AND INVESTOR RELATIONS

The company secretaries are responsible for information disclosure of the Company. The Company has established Rules on Information Disclosure to ensure information disclosed by the Company is accurate, complete and timely made. During the reporting period, the Company published its annual report, interim report and relevant announcements (including the overseas regulatory announcements which covered the announcements published by the subsidiaries of the Company whose shares are listed on other stock exchanges) in accordance with the Listing Rules and made detailed disclosures on material information and reported the progress of any significant issues relating to the Company.

General meetings of the Company have absolute power to perform its functions according to laws and regulations and make decisions on significant issues. The annual general meeting and extraordinary general meetings of the Company provide an open platform for shareholders to exchange opinions with the Board. In 2007, the Company convened one annual general meeting, at which seven resolutions were considered and approved, including resolutions relating to the revision of the existing annual caps of certain continuing connected transactions. Directors and management of the Company endeavored to attend the general meetings.

At the annual general meeting, each resolution such as the appointment of directors would be dealt with and resolved separately. Details about the procedures for voting by poll at the general meeting and the right of the shareholders to require a voting by poll are set out in the circular despatched to the shareholders. The circular will also contain details of the proposed resolutions. Results of voting by poll are published on the websites of the Company and the Stock Exchange respectively.

The Company has assigned specific employees to assume the role of contacting and communicating with investors. During the reporting period, due to the change of information disclosure methods required by the Stock Exchange, the Company had put more efforts in the maintenance of its websites to ensure that information is disclosed accurately and in a timely manner. The Company not only renews and modifies its Chinese and English websites continuously, but also regularly publishes and updates business news and information contained in its website to help investors understand the up-to-date situation of the Company clearly and timely. Details on the businesses of the Group and announcements such as interim results and annual results could also be downloaded from the Company's websites.

The Company also emphasized the mutual communication with its investors. During 2007, the Company communicated effectively with its investors through receiving investors during their visits or holding telephone conferences and effectively exchanged opinions with them.

PRICEWATERHOUSECOOPERS

羅兵咸永道會計師事務所

PricewaterhouseCoopers
22nd Floor Prince's Building
Central, Hong Kong

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF
AVICHINA INDUSTRY & TECHNOLOGY COMPANY LIMITED
(A joint stock company incorporated in the People's Republic of China with limited liability)

We have audited the consolidated financial statements of AviChina Industry & Technology Company Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 52 to 141, which comprise the consolidated and company balance sheets as of 31st December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

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

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

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

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Company and of the Group as of 31st December 2007, and of the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

OTHER MATTERS

This report, including the opinion, has been prepared for and only for you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 11th April 2008

Consolidated Income Statement

For the year ended 31st December 2007

	Note	2007 RMB'000	2006 RMB'000
Revenue	5	**16,540,645**	17,110,508
Cost of sales		**(14,780,935)**	(15,204,907)
Gross profit		**1,759,710**	1,905,601
Other income	6	**113,796**	98,411
Selling and distribution expenses		**(980,648)**	(1,156,994)
General and administrative expenses	7	**(950,741)**	(1,065,352)
Other operating expenses, net	7	**(466,112)**	(105,954)
Operating loss	7	**(523,995)**	(324,288)
Finance income	8	**57,966**	78,256
Finance costs	8	**(387,391)**	(272,282)
Finance costs, net		**(329,425)**	(194,026)
Share of results of associates	18	**56,711**	45,051
Loss before income tax		**(796,709)**	(473,263)
Income tax expense	9	**(51,635)**	(13,399)
Loss for the year		**(848,344)**	(486,662)
Attributable to:			
Equity holders of the Company	10	**(1,026,226)**	(331,079)
Minority interests		**177,882**	(155,583)
		(848,344)	(486,662)
Loss per share for loss attributable to equity holders of the Company during the year		**RMB**	RMB
– Basic and diluted	11	**(0.221)**	(0.071)

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

As at 31st December 2007

	Note	Group 2007 RMB'000	Group 2006 RMB'000	Company 2007 RMB'000	Company 2006 RMB'000
ASSETS					
Non-current assets					
Property, plant and equipment	14	**7,325,989**	9,049,538	**7,413**	8,205
Land use rights	15	**81,375**	96,331	**—**	—
Intangible assets	16	**331,614**	450,654	**—**	—
Interests in subsidiaries	17	**—**	—	**3,544,134**	4,019,964
Interests in associates	18	**297,921**	247,967	**30,000**	—
Other non-current financial assets	19	**587,417**	131,247	**—**	—
Deferred income tax assets	20	**126,241**	75,305	**—**	—
		8,750,557	10,051,042	**3,581,547**	4,028,169
Current assets					
Accounts receivable	21	**3,237,673**	3,716,924	**—**	—
Advances to suppliers	22	**519,014**	628,383	**—**	—
Other receivables and prepayments	23	**1,203,537**	708,218	**151,358**	137,267
Inventories	24	**5,277,527**	4,804,913	**—**	—
Financial assets at fair value through profit or loss		**7,414**	—	**—**	—
Pledged deposits	26	**638,350**	694,391	**—**	—
Term deposits with initial term of over three months	27	**691,820**	1,051,128	**661,820**	765,470
Cash and cash equivalents	36(e)	**2,452,706**	3,155,527	**143,266**	91,592
		14,028,041	14,759,484	**956,444**	994,329
Total assets		**22,778,598**	24,810,526	**4,537,991**	5,022,498

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

Balance Sheets

As at 31st December 2007

	Note	Group 2007 RMB'000	Group 2006 RMB'000	Company 2007 RMB'000	Company 2006 RMB'000
EQUITY					
Capital and reserves attributable to equity holders of the Company					
Share capital	34	**4,643,609**	4,643,609	**4,643,609**	4,643,609
Reserves	35	**(1,155,536)**	(314,710)	**(601,370)**	(138,782)
		3,488,073	4,328,899	**4,042,239**	4,504,827
Minority interests		**3,170,322**	3,793,213	**—**	—
Total equity		**6,658,395**	8,122,112	**4,042,239**	4,504,827
LIABILITIES					
Non-current liabilities					
Long-term borrowings	33	**1,111,540**	836,704	**—**	—
Deferred income from government grants		**149,886**	157,002	**—**	—
Deferred income tax liabilities	20	**156,332**	35,872	**—**	—
		1,417,758	1,029,578	**—**	—
Current liabilities					
Accounts payable	28	**6,761,213**	7,037,244	**—**	—
Advances from customers	29	**884,568**	460,470	**—**	—
Other payables and accruals	30	**1,324,343**	1,667,884	**31,454**	53,373
Amounts payable to ultimate holding company	31	**520,524**	520,524	**464,298**	464,298
Provisions	32	**174,431**	103,284	**—**	—
Current portion of long-term borrowings	33	**650,457**	433,695	**—**	—
Short-term borrowings	33	**4,312,163**	5,401,598	**—**	—
Current income tax liabilities		**74,746**	34,137	**—**	—
		14,702,445	15,658,836	**495,752**	517,671
Total liabilities		**16,120,203**	16,688,414	**495,752**	517,671
Total equity and liabilities		**22,778,598**	24,810,526	**4,537,991**	5,022,498
Net current (liabilities)/assets		**(674,404)**	(899,352)	**460,692**	476,658
Total assets less current liabilities		**8,076,153**	9,151,690	**4,042,239**	4,504,827

Director
Wu Xiandong

Director
Chen Huaiqiu

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

	Attributable to equity holders of the Company							
	Share Capital RMB'000	Capital reserve RMB'000	Available-for-sale financial assets reserve RMB'000	Statutory surplus reserve RMB'000	Accumulated losses RMB'000	Subtotal RMB'000	Minority interests RMB'000	Total RMB'000
	(Note 34)	(Note35(b))		(Note35(c))	(Note35(e))			
For the year ended 31st December 2007								
Balance at 1st January 2007, as previously stated	4,643,609	77,585	–	188,493	(580,788)	4,328,899	3,793,213	8,122,112
Adjustment on reserve appropriation (Note35(c))	–	–	–	(161,781)	161,781	–	–	–
Balance at 1st January 2007	4,643,609	77,585	–	26,712	(419,007)	4,328,899	3,793,213	8,122,112
Transfer to statutory reserve	–	–	–	4,466	(4,466)	–	–	–
Change in fair value of available-for-sale financial assets								
- gross	–	–	251,845	–	–	251,845	203,653	455,498
- deferred taxation	–	–	(66,335)	–	–	(66,335)	(53,280)	(119,615)
Others	–	(110)	–	–	–	(110)	(2,281)	(2,391)
Net (expense)/income recognised directly in equity	–	(110)	185,510	4,466	(4,466)	185,400	148,092	333,492
(Loss)/profit for the year	–	–	–	–	(1,026,226)	(1,026,226)	177,882	(848,344)
Total recognised (expense)/income for the year	–	(110)	185,510	4,466	(1,030,692)	(840,826)	325,974	(514,852)
Contributions from minority shareholders of subsidiaries	–	–	–	–	–	–	2,000	2,000
Purchase of additional interests in a subsidiary	–	–	–	–	–	–	(2,909)	(2,909)
Disposal of certain interests in subsidiaries	–	–	–	–	–	–	14,973	14,973
Disposal of a subsidiary	–	–	–	–	–	–	(2,203)	(2,203)
Dividend to minority shareholders of subsidiaries	–	–	–	–	–	–	(37,230)	(37,230)
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	–	–	–	–	–	–	(923,496)	(923,496)
Balance at 31st December 2007	4,643,609	77,475	185,510	31,178	(1,449,699)	3,488,073	3,170,322	6,658,395

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31st December 2007

	Attributable to equity holders of the Company							
	Share capital RMB'000	Capital reserve RMB'000	Statutory surplus reserve RMB'000	Statutory public welfare fund RMB'000	Retained earnings/ (accumulated losses) RMB'000	Subtotal RMB'000	Minority interests RMB'000	Total RMB'000
	(Note 34)	(Note35(b))	(Note35(c))	(Note35(d))	(Note35(e))			
For the year ended 31st December 2006								
Balance at 1st January 2006, as previously stated	4,643,609	74,898	95,651	79,275	320,362	5,213,795	3,495,411	8,709,206
Adjustment on reserve appropriation (Note35(c))	—	—	(68,939)	(79,275)	148,214	—	—	—
Balance at 1st January 2006	4,643,609	74,898	26,712	—	468,576	5,213,795	3,495,411	8,709,206
Additional contribution in an associate	—	2,687	—	—	—	2,687	—	2,687
2005 dividend	—	—	—	—	(48,758)	(48,758)	—	(48,758)
Share reform (Note 35(f))	—	—	—	—	(507,746)	(507,746)	386,633	(121,113)
Net income/(expense) recognised directly in equity	—	2,687	—	—	(556,504)	(553,817)	386,633	(167,184)
Loss for the year	—	—	—	—	(331,079)	(331,079)	(155,583)	(486,662)
Total recognised income/ (expense) for the year	—	2,687	—	—	(887,583)	(884,896)	231,050	(653,846)
Contributions from minority shareholders of subsidiaries	—	—	—	—	—	—	136,193	136,193
Acquisition of a subsidiary	—	—	—	—	—	—	11	11
Disposal of a subsidiary	—	—	—	—	—	—	(1,424)	(1,424)
Dividend to minority shareholders of subsidiaries	—	—	—	—	—	—	(68,028)	(68,028)
Balance at 31st December 2006	4,643,609	77,585	26,712	—	(419,007)	4,328,899	3,793,213	8,122,112

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

For the year ended 31st December 2007

	Note	2007 RMB'000	2006 RMB'000
Cash flows from operating activities			
Net cash generated from operations	36(a)	**503,390**	1,193,167
Interest received		**57,966**	76,219
Interest paid		**(398,171)**	(332,714)
Enterprise income tax paid		**(65,911)**	(27,141)
Net cash generated from operating activities		**97,274**	909,531
Cash flows from investing activities			
Purchase of property, plant and equipment		**(894,643)**	(1,250,581)
Payments for intangible assets		**(6,392)**	(80,035)
Addition of other non-current financial assets		**—**	(12,567)
Disposal of other non-current financial assets		**380**	—
Decrease/(increase) in term deposits with initial term of over three months		**359,308**	(245,911)
Proceeds from sale of property, plant and equipment	36(b)	**14,819**	21,087
Net cash outflow from disposal of a subsidiary	36(c)	**(1,559)**	(886)
Proceeds from disposal of certain interests in subsidiaries		**47,413**	—
Additional investments in associates		**(30,000)**	(15,000)
Disposal of interests in associates		**99**	10,000
Dividends received from associates		**33,256**	31,777
Dividends received from other non-current financial assets		**4,870**	—
Purchase of additional interests in a subsidiary		**(2,909)**	—
Net cash outflow from acquisition of a subsidiary	36(d)	**—**	(8,396)
Net cash used in investing activities		**(475,358)**	(1,550,512)
Cash flows from financing activities			
Decrease/(increase) in pledged deposits		**56,041**	(288,817)
Proceeds from borrowings		**7,896,298**	6,525,514
Repayments of borrowings		**(8,077,298)**	(5,382,811)
Contributions from minority shareholders of subsidiaries		**2,000**	136,193
Dividend paid to minority shareholders of subsidiaries		**(37,451)**	(90,383)
Dividend paid to holding company		**(28,070)**	(20,466)
Payments in respect of share reform		**—**	(25,084)
Net cash (used in)/generated from financing activities		**(188,480)**	854,146
Net (decrease)/increase in cash and cash equivalents		**(566,564)**	213,165
Cash and cash equivalents at 1st January		**3,155,527**	2,942,362
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))		**(136,257)**	—
Cash and cash equivalents at 31st December	36(e)	**2,452,706**	3,155,527

The notes on pages 58 to 141 are an integral part of these consolidated financial statements.

1 ORGANISATION AND PRINCIPAL ACTIVITIES

AviChina Industry & Technology Company Limited (the "Company") was established in the People's Republic of China (the "PRC") on 30th April 2003 as a joint stock company with limited liability under the PRC laws as a result of a group reorganisation (the "Reorganisation") of China Aviation Industry Corporation II ("AVIC II"). The Company's H shares were listed on the Main Board of The Stock Exchange of Hong Kong Limited on 30th October 2003.

The Company and its subsidiaries are collectively referred to as the "Group". The Group is principally engaged in the research, development, manufacture and sale of automobile and aviation products.

The Company's directors regard AVIC II, a company established in the PRC, as being the ultimate holding company of the Company.

These consolidated financial statements are presented in Renminbi ("RMB"), unless otherwise stated, and have been approved for issue by the Board of Directors on 11th April 2008.

2 BASIS OF PREPARATION

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, and financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss, as appropriate.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 4.

In preparing these financial statements, the directors have taken into account all information that could reasonably be expected to be available and have ascertained that the Group has obtained adequate financial resources to support the Group to continue in operational existence for the foreseeable future. Under these circumstances, the directors consider that it is proper to prepare the financial statements on a going concern basis notwithstanding that at 31st December 2007, the Group's current liabilities exceeded its current assets by RMB674,404,000.

2 BASIS OF PREPARATION (continued)

The following new standard, amendment to standard and interpretations are mandatory for financial year ended 31st December 2007:

IAS 1 (Amendment)	Capital Disclosures
IFRS 7	Financial Instruments: Disclosures
IFRIC-Int 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies
IFRIC-Int 8	Scope of IFRS 2
IFRIC-Int 9	Reassessment of Embedded Derivatives
IFRIC-Int 10	Interim Financial Reporting and Impairment

The adoption of the above standard, amendment to standard and interpretations did not have any significant financial impact to the Group.

The Group has not early adopted the following new/revised standards or interpretations that have been issued but are not yet effective. The directors are currently assessing the impact on their adoption.

IAS 1 (Revised)	Presentation of Financial Statements
IAS 23 (Revised)	Borrowing Costs
IAS 27 (Revised)	Consolidated and Separate Financial Statements
IAS 32 and IAS 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation
IFRS 2 (Amendments)	Share-Based Payment – Vesting Conditions and Cancellations
IFRS 3 (Revised)	Business Combinations
IFRS 8	Operating Segments
IFRIC-Int 11	IFRS 2 – Group and Treasury Share Transactions
IFRIC-Int 12	Service Concession Arrangements
IFRIC-Int 13	Customer Loyalty Programmes
IFRIC-Int 14	IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

3 PRINCIPAL ACCOUNTING POLICIES

(a) Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiaries made up to 31st December.

(i) *Subsidiaries*

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interests. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, including any contingent liabilities assumed, the difference is recognised directly in the consolidated income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet, interests in subsidiaries are stated at cost less provision for impairment losses. The results of the subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

(ii) *Transactions and minority interests*

The Group applies a policy of treating transactions with minority interests as transactions with equity owners of the Group. For purchases from minority interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is deducted from equity. Gains or losses on disposals to minority interests are also recorded in equity. For disposals to minority interests, differences between any proceeds received and the relevant share of minority interests are also recorded in equity.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(a) Consolidation (continued)

(iii) *Jointly ventures*

A jointly controlled entity is a joint venture in respect of which a contractual arrangement is established between the participating ventures and whereby the Group together with the other venturers undertake an economic activity which is subject to joint control and none of the venturers has unilateral control over the economic activity.

The Group's interest in a jointly controlled entity is accounted for by proportionate consolidation. The Group combines its share of the jointly controlled entity's individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in the Group's consolidated financial statements. The Group recognises the portion of gains or losses on the sale of assets by the Group to the jointly controlled entity that it is attributable to the other venturers. The Group does not recognise its share of profits or losses from the jointly controlled entity that result from the Group's purchase of assets from the jointly controlled entity until it resells the assets to an independent party. However, a loss on the transaction is recognised immediately if the loss provides evidence of a reduction in the net realisable value of current assets, or an impairment loss. As a result of a change in management roles and responsibilities in Jiangxi Changhe Suzuki Automobile Co., Ltd. ("JCSA"), a former subsidiary indirectly held by the Group, the directors of the Company consider that the Group no longer controls JCSA as a subsidiary and therefore have reclassified JCSA as a jointly controlled entity of the Group during the year and accounted for JCSA using proportionate consolidation from the date when the Group's control over JCSA ceased.

Certain of the Group's activities are conducted through joint ventures where the venturers have a direct ownership interest in and jointly control the assets of the venture. The income, expenses, assets and liabilities of these jointly controlled assets are included in the consolidated financial statements in proportion to the Group's interest.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(a) Consolidation (continued)

(iv) *Associates*

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in associates are carried at cost less provision for impairment losses. The results of associates are accounted for by the Company on the basis of dividends received and receivable.

(b) Property, plant and equipment

Property, plant and equipment other than construction-in-progress are stated at historical cost less accumulated depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(b) Property, plant and equipment (continued)

Depreciation is calculated on a straight-line basis to write off the cost less accumulated impairment losses of each asset to their residual values over their estimated useful lives as follows:

Buildings	5 - 45 years
Plant and equipment	3 - 16 years
Furniture and fixtures, other equipment and motor vehicles	5 - 12 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 3 (f)).

Gains and losses on disposals are determined by comparing net sales proceeds and the carrying amount of the relevant assets, and are included in the income statement.

(c) Construction-in-progress

Construction-in-progress represents buildings, plant and machinery under construction and pending installation and is stated at cost less accumulated impairment losses, if any. Cost includes the costs of construction of buildings, the costs of plant and machinery, and interest charges arising from borrowings used to finance these assets during the period of construction or installation and testing. All other borrowing costs are expensed. No provision for depreciation is made on construction-in-progress until such time as the relevant assets are completed and ready for intended use. When the assets concerned are brought to use, the costs are transferred to property, plant and equipment and depreciated in accordance with the policy as stated in Note 3(b) to the financial statements.

(d) Land use rights

Land use rights are stated at cost less accumulated amortisation and accumulated impairment losses. Cost represents consideration paid for the rights to use the land on which various plants and buildings are situated for periods varying from 30 to 50 years.

Amortisation of land use rights is calculated on a straight-line basis over the period of the land use rights.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(e) Intangible assets

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technical feasibility and its costs can be measured reliably. Other development expenditures that do not meet their criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use on a straight-line basis over its expected useful life, not exceeding five years; and tested for impairment according to Note 3(f) below.

Where the research phase and the development phase of an internal project cannot be clearly distinguished, all expenditure incurred on the project is charged to the income statement.

Technology know-how is initially recognised at cost. Technology know-how that has a definite useful life is carried at cost less accumulated amortisation and accumulated impairment losses, if any. Amortisation is calculated using the straight-line method to allocate the cost of technology know-how over their estimated useful lives of 6 years.

(f) Impairment of investments in subsidiaries, associates and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation/depreciation and are at least tested annually for impairment. Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date. Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in the income statement.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(g) Financial assets

The Group classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, held-to-maturity and available-for-sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(i) *Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives are classified as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.

(ii) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables include accounts and other receivables.

(iii) *Held-to-maturity investments*

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. During the year, the Group did not hold any financial asset in this category.

(iv) *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are classified under "Other non-current financial assets" and included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Regular purchases and sales of financial assets are recognised on the trade-date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(g) Financial assets (continued)

Gains or losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are presented in the income statement in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognised in the income statement when the Group's right to receive payments is established.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale are analysed between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognised in profit or loss; translation differences on non-monetary securities are recognised in equity. Changes in the fair value of monetary and non-monetary securities classified as available for sale are recognised in equity.

When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as gains and losses from investment securities.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the Group's right to receive payments is established.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted investments), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs. However, if the range of reasonable fair value estimate is significant and the probabilities of the various estimate cannot be reasonably assessed, such financial assets are carried at cost less accumulated impairment losses.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of receivables is described in Note 3(j).

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(h) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined by the weighted average method. The cost of finished goods and work in progress comprises raw materials, direct labor, other direct costs and related production overheads (based on normal operating capacity). Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

(i) Contracts in progress

Contracts in progress in connection with the manufacturing of aircraft are accounted for under construction contracts.

When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred and that it is probable to be recoverable; and contract costs are recognised when incurred.

When the outcome of a construction contract can be estimated reliably and it is probable that the contract will be profitable, contract revenue is recognised over the period of the contract. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

The Group uses the percentage of completion method to determine the appropriate amount to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract. Costs incurred in the year in connection with future activity on a contract are excluded from contract costs in determining the stage of completion. They are presented as inventories, prepayments or other assets, depending on their nature.

The Group presents as an asset the gross amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceed progress billings. Progress billings not yet paid by customers and retention are included within "accounts receivable".

The Group presents as a liability the gross amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses).

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(j) Receivables

Receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original term of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement within "general and administrative expenses". When a receivable is uncollectible, it is written off against the allowance account for receivables. Subsequent recoveries of amounts previously written off are credited against general and administrative expenses in the income statement.

(k) Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks and term deposit with initial terms of less than three months.

(l) Financial liabilities and equity

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. Financial liabilities (including accounts payables) are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest method. An equity instrument is any contract that does not meet the definition of financial liability and evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Equity shares are classified as equity. Incremental costs, net of tax, directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds.

(m) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

(n) Borrowings costs

Borrowing costs incurred for the construction of qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed as incurred.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(o) Current and deferred income tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Group operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the relevant tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference can be controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

(p) Employee benefits

(i) *Pension obligations*

The Group contributes on a monthly basis to various defined contribution retirement benefit plans organised by relevant municipal and provincial governments in the PRC. The municipal and provincial governments undertake to assume the retirement benefit obligations payable to all existing and future retired employees under these plans and the Group has no further obligation for post-retirement benefits beyond the contributions made. Contributions to these plans are expensed as incurred.

(ii) *Early retirement benefits*

Early retirement benefits are recognised as expense in the period the Group reaches agreements with the relevant employees for the early retirement.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(p) Employee benefits (continued)

(iii) *Housing benefits*

The Group sold staff quarters to its employees, subject to a number of eligibility requirements, at preferential prices. When staff quarters are identified as being subject to sale under these arrangements, the carrying value of the staff quarters is written down to the net recoverable amount. Upon sale, any difference between sales proceeds and the carrying amount of the staff quarters is charged to the income statement.

The above discounted quarters allocation plans were phased out in accordance with the policies of the PRC government. In 1998, the State Council of the PRC issued a circular which stipulated that the sale of quarters to employees at preferential prices should be withdrawn. In 2000, the State Council further issued a circular stating that cash subsidies should be made to the employees following the withdrawal of allocation of staff quarters. However, the specific timetable and procedures of implementation of these policies are to be determined by individual provincial or municipal government based on the particular situation of the province or municipality.

Based on the relevant detailed local government regulations promulgated, certain entities within the Group have adopted cash housing subsidy plans. In accordance with these plans, for those eligible employees who have not been allocated with quarters at all or who have not been allocated with quarters up to the prescribed standards before the discounted quarters sale plans were terminated, the Group is required to pay them one-off cash housing subsidies based on their years of service, positions and other criteria. These cash housing subsidies are charged to the income statement in the year in which it was determined that the payment of such subsidies is probable and the amounts can be reasonably estimated. Based on the available information and its best estimate, the Group estimated the required provision for these cash housing subsidies which was charged to the income statement in the year ended 31st December 2000 when the State Council circular in respect of cash subsidies was issued.

Pursuant to the Reorganisation, AVIC II would bear any further one-off cash housing subsidies in excess of the amount provided for in the consolidated balance sheet of the Group. Employees joining the Group after the incorporation of the Company would not be entitled to any one-off cash housing subsidies.

In addition, all full-time employees of the Group are entitled to participate in various government-sponsored housing funds. The Group contributes on a monthly basis to these funds based on certain percentages of the salaries of the employees. The Group's liability in respect of these funds is limited to the contributions payable in each period.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(q) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Warranty obligations are accrued at the time the sales are recognised, based on the estimated amounts of fulfilling the total obligations, including handling and transportation costs. The assumptions used to estimate warranty expenses are evaluated periodically and based on historical experience.

(r) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Assets leased out under operating leases are included in property, plant and equipment in the balance sheet. They are depreciated over their expected useful lives on a basis consistent with similar owned property, plant and equipment. Rental income is recognised on a straight-line basis over the lease term.

(s) Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of (i) the amount initially recognised less, where appropriate, cumulative amortisation recognised in the income statement over the period of the relevant liabilities and (ii) the amount of which the Group is obliged to reimburse the recipient under the financial guarantee contracts.

(t) Foreign currency translation

(i) *Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "Functional Currency"). The financial statements are presented in Renminbi ("RMB"), which is the Company's functional and presentation currency.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(t) Foreign currency translation(continued)

(ii) *Transactions and balances*

Foreign currency transactions are translated into the Functional Currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Translation differences on non-monetary financial assets and liabilities such as equity instruments held at fair value through profit or loss are recognised in profit or loss as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale are included in the fair value reserve in equity.

(iii) *Group companies*

The results and financial position of all the group entities (none of which has the currency of a hyperinflationary economy) that have a Functional Currency different from the presentation currency are translated into the presentation currency as follows:

(a) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

(b) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

(c) all resulting exchange differences are recognised as a separate component of equity.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(u) Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sales of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts after eliminated sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured and it is probable that future economic benefits will flow to the Group. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement. Revenue and income are recognised as follows:

Turnover represents revenues recognised on sales of automobiles and aviation products. Sales of goods are recognised when a group entity has delivered products to the customer, the customer has accepted the products and collectibility of the related receivables is reasonably assured.

The Group combines its proportionate share of the jointly controlled entity's turnover as described in Note 3(a)(iii) with similar recognition policies mentioned above.

Recognition policy of revenue relating to long-term construction contracts is disclosed in Note 3(i) above.

Dividend income and income from investments are recognised when the right to receive payment is established.

Revenue from the provision of services is recognised when the services are rendered.

Rental income under operating leases is recognised on a straight-line basis over the lease periods.

Interest income from bank deposits is recognised on a time proportion basis using the effective interest method.

(v) Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs they are intended to compensate.

Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred income from government grants and are credited to the income statement on a straight-line basis over the expected lives of the related assets.

(w) Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders or directors, where appropriate.

3 PRINCIPAL ACCOUNTING POLICIES (continued)

(x) Derivative financial instruments

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. During the year, the Group did not enter into any derivative financial instruments.

(y) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements used in preparing the financial statements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) Depreciation and amortisation

The Group's management determines the estimated useful lives and related deprecation/amortisation charges for the property, plant and equipment and intangible assets with reference to the estimated periods that the Group intends to derive future economic benefits from the use of these assets. Management will revise the depreciation and amortisation charge where useful lives are different to previously estimated, or it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold.

(ii) Development costs

The Group's management determines the capitalisation of development costs when it is probable that the project will be a success considering its commercial and technology feasibility. It could change significantly as a result of technological innovations and the changes of estimated projections. Management will write-off or write-down development costs when there are adverse changes in technological innovations or estimated projections.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(iii) Impairment of non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset exceeds its recoverable amount in accordance with the accounting policy stated in Note 3(f). The recoverable amount of an asset or a cash-generating unit is determined based on value-in-use calculations. The value-in-use calculation requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value, which has been prepared on the basis of management's assumptions and estimates.

At 31st December 2007, if the budgeted gross margin used in the value-in-use calculation had been 10% lower/higher than management's estimates and the pre-tax discount rate applied to the discounted cash flows had been 1% higher/lower, with all other variables held constant, the impairment charges on property, plant and equipment and intangible assets would, in aggregate, increase/decrease by RMB128,612,000 and RMB131,770,000 respectively.

(iv) Impairment of account and other receivables

Provision for impairment of account and other receivables is determined based on the evaluation of collectibility of account and other receivables. A considerable amount of judgment is required in assessing the ultimate realisation of these receivables, including the current creditworthiness, the past collection history of each customer and the current market condition.

(v) Inventories

Management estimates the net realisable value for finished goods and work-in progress based primarily on the latest invoice prices and current market conditions. The Group carries out an inventory review on a product-by-product basis at each balance sheet date and will make provision for impairment on obsolete and slow-moving items or will write-off or write-down inventories to net realisable value.

(vi) Revenue recognition

The Group uses the percentage of completion method in accounting for its contract revenues. Use of the percentage of completion method requires the Group to estimate the contract costs incurred up to the balance sheet date as a proportion of the total estimated cost for each contract. Based on the Group's experience and nature of the construction contracts undertaken by the Group, the Group makes estimates of the point at which it considers the work is sufficiently advanced such that costs to complete and revenue can be reliably estimated. Management is confident that the actual outcome will not materially differ from the estimates made at the balance sheet date.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(vii) Income taxes

The Group is subject to income taxes in the PRC. There are certain transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(viii)Provisions

The Group gives warranties on certain automobile and aviation products and undertakes to repair or replace items that fail to perform satisfactorily based on certain pre-determined conditions. Management estimates the related warranty claims based on historical warranty claim information including level of repairs and returns as well as recent trends that might suggest that past cost information may differ from future claims.

Factors that could impact the estimated claim information include the success of the Group's product quality initiatives, as well as parts and labor costs. Any increase or decrease in the provision would affect profit or loss in future years.

5 SEGMENT INFORMATION

The Group is principally engaged in the manufacturing, assembly, sales and servicing of automobiles and civilian aircrafts. In accordance with the Group's internal financial reporting system, the Group has determined business segments be presented as the primary reporting format.

(a) Primary reporting format – business segments

The Group is organised into two main business segments:

- Aviation – manufacturing, assembly, sales and servicing of helicopters, trainers and other aircrafts.
- Automobiles – manufacturing, assembly, sales and servicing of automobiles.

All segment revenues were made to external parties.

Operating expenses of a functional unit are allocated to the relevant segment which is the predominant user of the services provided by the unit. Operating expenses of other shared services which cannot be allocated to a specific segment are included as unallocated costs. Unallocated costs mainly represent corporate expenses.

Segment assets consist primarily of property, plant and equipment, land use rights, intangible assets, deferred income tax assets, investments in associates, inventories, operating receivables, prepayments, deposits and cash and cash equivalents, and mainly exclude corporate assets. Segment liabilities comprise operating liabilities, deferred income tax liabilities, and exclude corporate liabilities. Capital expenditures mainly comprise additions to property, plant and equipment, land use rights and intangible assets.

5 SEGMENT INFORMATION (continued)

Primary reporting format – business segments

	As at and for the year ended 31st December 2007		
	Aviation RMB'000	Automobiles RMB'000	Total RMB'000
Operating results			
Segment revenue	5,327,408	11,213,237	16,540,645
Segment results	306,241	(852,840)	(546,599)
Unallocated income			48,745
Unallocated costs			(26,141)
Operating loss			(523,995)
Finance costs, net	(73,707)	(255,718)	(329,425)
Share of results of associates	53,389	3,322	56,711
Loss before income tax			(796,709)
Income tax expense			(51,635)
Loss for the year			(848,344)
Assets			
Segment assets	8,855,603	12,812,702	21,668,305
Interests in associates	240,552	57,369	297,921
Unallocated assets			812,372
Total assets			22,778,598
Liabilities			
Segment liabilities	6,107,254	9,517,197	15,624,451
Unallocated liabilities			495,752
Total liabilities			16,120,203
Other segment information			
Capital expenditures	217,461	702,851	920,312
Depreciation	89,145	936,147	1,025,292
Amortisation	2,309	62,795	65,104
Provisions for impairments	24,549	359,772	384,321
Write off of intangible assets	—	83,117	83,117

5 SEGMENT INFORMATION (continued)

	As at and for the year ended 31st December 2006		
	Aviation	Automobiles	Total
	RMB'000	RMB'000	RMB'000
Operating results			
Segment revenue	4,427,598	12,682,910	17,110,508
Segment results	375,063	(650,755)	(275,692)
Unallocated income			6,591
Unallocated costs			(55,187)
Operating loss			(324,288)
Finance costs, net	(34,462)	(159,564)	(194,026)
Share of results of associates	42,540	2,511	45,051
Loss before income tax			(473,263)
Income tax expense			(13,399)
Loss for the year			(486,662)
Assets			
Segment assets	7,720,276	15,976,945	23,697,221
Interests in associates	192,339	55,628	247,967
Unallocated assets			865,338
Total assets			24,810,526
Liabilities			
Segment liabilities	5,119,222	11,051,521	16,170,743
Unallocated liabilities			517,671
Total liabilities			16,688,414
Other segment information			
Capital expenditures	157,655	1,045,909	1,203,564
Depreciation	70,266	857,847	928,113
Amortisation	1,277	125,572	126,849
Provisions for impairments	30,248	75,706	105,954

5 SEGMENT INFORMATION (continued)

(b) Secondary reporting format – geographical segments

All assets and operations of the Group for the year were located in the PRC, which is considered as one geographical location in an economic environment with similar risk and returns.

No geographical segments analysis is presented as less than 10% of the Group's revenue and assets are attributable to markets not located in the PRC.

6 OTHER INCOME

	2007	2006
	RMB'000	RMB'000
Profit from sale of scrap materials	**22,312**	19,699
Income from government grants	**70,000**	66,223
Refund of value-added tax and real estate tax	**3,683**	1,878
Rental income from plant and equipment, net	**1,074**	2,012
Income from rendering of other services, net	**11,857**	8,599
Dividend income from other non-current financial assets	**4,870**	—
	113,796	98,411

7 OPERATING LOSS

Operating loss is stated after charging/(crediting):

	2007 RMB'000	2006 RMB'000
Auditors' remuneration	**7,190**	7,780
Amortisation		
– Land use rights (Note 15)	**6,229**	2,983
– Intangible assets (Note 16)	**58,875**	123,866
Costs of inventories sold	**14,780,935**	15,204,907
Depreciation on property, plant and equipment (Note 14)	**1,025,292**	928,113
Operating lease rentals		
– Land and buildings	**45,548**	41,029
– Property, plant and equipment	**216**	—
Repairs and maintenance expense on property, plant and equipment	**50,996**	24,301
Research expenditures and development costs	**244,539**	230,712
Staff costs, including directors' emoluments (Note 12)	**945,478**	997,118
Warranty expenses (Note 32)	**246,903**	154,841
Other operating expenses, net		
Write off of intangible assets (Note 16)	**83,117**	—
Provision/(reversal of provision) for impairment		
– Property, plant and equipment (Note 14)	**243,421**	642
– Intangible assets (Note 16)	**5,958**	70,710
– Other non-current financial assets	**(1,326)**	12,355
– Receivables	**13,067**	22,126
– Inventories	**121,875**	121
	466,112	105,954

7 OPERATING LOSS (continued)

	2007 RMB'000	2006 RMB'000
Other gains *		
Amortisation of deferred income relating to government grants	**(33,161)**	(18,396)
Fair value gain on financial assets at fair value through profit or loss	**(338)**	—
Gain on disposal of		
– Property, plant and equipment	**(16,838)**	(12,780)
– Certain interests in subsidiaries	**(32,440)**	—
– Financial assets at fair value through profit or loss	**(16,305)**	(6,591)
	(99,082)	(37,767)

* *Other gains are included in general and administrative expenses as it is considered that the amount is relatively immaterial to present as an additional line item on the face of consolidated income statement.*

8 FINANCE COSTS, NET

	2007 RMB'000	2006 RMB'000
Finance income:		
Interest income on bank balances and deposits	**57,966**	78,256
Finance costs:		
Interest expense on bank borrowings		
– Wholly repayable within 5 years	**381,010**	313,986
– Not wholly repayable within 5 years	**17,054**	15,618
Interest expense on other borrowings		
– Wholly repayable within 5 years	**—**	9,707
– Not wholly repayable within 5 years	**107**	121
	398,171	339,432
Less: Amount capitalised in property, plant and equipment (note)	**(26,111)**	(59,252)
Government interest subsidies	**(33,245)**	(27,119)
	338,815	253,061
Exchange losses	**35,183**	14,487
Other finance costs	**13,393**	4,734
	387,391	272,282
	329,425	194,026

Note: Interest expenses capitalised are borrowing costs related to funds borrowed specifically for the purpose of obtaining a qualifying asset. Interest rates on such capitalised borrowings are as follows:

	2007	2006
Interest rates per annum at which finance costs were capitalised	**5.49% -6.57%**	3.74% - 5.81%

9 INCOME TAX EXPENSE

	2007 RMB'000	2006 RMB'000
PRC enterprise income tax	**106,520**	52,686
Deferred income taxes	**(54,885)**	(39,287)
	51,635	13,399

Notes:

(a) Except for certain subsidiaries which are taxed at preferential rates ranging from 7.5% to 15% (2006: 7.5% to 15%), in accordance with the relevant PRC enterprise income tax rules and regulations, provision for PRC enterprise income tax is calculated based on the statutory income tax rate of 33% on the assessable income of the Group (2006: 33%).

(b) The reconciliation between the Group's actual tax charge and the amount which is calculated based on the statutory tax rate of 33% in the PRC is as follows:

	2007 RMB'000	2006 RMB'000
Loss before income tax	**(796,709)**	(473,263)
Tax calculated at the statutory tax rate of 33% (2006: 33%)	**(262,914)**	(156,177)
Preferential tax rates on the income of certain subsidiaries	**(214,523)**	(91,449)
Non-taxable income	**(61,811)**	(63,662)
Expenses not deductible for tax purposes	**124,669**	26,951
Tax losses for which no deferred income tax asset was recognised	**483,181**	314,119
Utilisation of previously unrecognised tax losses	**(6,769)**	—
Effect of changes in future tax rates	**(18,297)**	—
Write off of previously recognised deferred tax assets	**15,347**	—
Others	**(7,248)**	(16,383)
Tax charge	**51,635**	13,399

(c) Share of taxation attributable to associates for the year ended 31st December 2007 of RMB4,686,000 (2006: RMB772,000) is included in the consolidated income statement as share of results of associates.

On 16th March 2007, the National People's Congress approved the Corporate Income Tax Law of the PRC (the "new CIT Law"). The new CIT Law reduces (increases) the corporate income tax rate for domestic enterprises (foreign invested enterprises) from 33% (15% or 24%) to 25% with effect from 1st January 2008. As a result of the new CIT Law, the carrying value of the net deferred tax assets has been increased by RMB18,297,000 in the year ended 31st December 2007.

10 LOSS ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The loss attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of RMB462,588,000 (2006: RMB166,985,000).

11 LOSS PER SHARE

The calculation of basic loss per share is based on the Group's loss attributable to equity holders of the Company of RMB1,026,226,000 (2006: RMB331,079,000) and based on the weighted average number of 4,643,608,500 (2006: 4,643,608,500) shares in issue during the year.

There was no dilution effect on the basic loss per share for the years ended 31st December 2007 and 2006 as there were no potential dilutive shares outstanding during the years ended 31st December 2007 and 2006.

12 STAFF COSTS, INCLUDING DIRECTORS' EMOLUMENTS

	2007	2006
	RMB'000	RMB'000
Wages, salaries and bonuses	**605,951**	690,103
Housing benefits	**62,626**	55,305
Contributions to pension plans	**160,080**	128,072
Welfare and other expenses	**116,821**	123,638
	945,478	997,118

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) Directors' emoluments

The emoluments of each of the directors of the Company for the years ended 31st December 2007 and 2006 are set out below.

	Year ended 31st December 2007				
Name of director	Fees	Basic salaries, housing allowance, other allowances and benefits in kind	Bonuses	Employer's contributions to retirement schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Executive directors					
Zhang Hongbiao	—	180	—	—	180
Wu Xiandong	—	160	—	—	160
Tan Ruisong	—	160	—	—	160
Non-executive directors					
Liang Zhenhe	120	—	—	—	120
Song Jingang	120	—	—	—	120
Tian Min	120	—	—	—	120
Chen Huaiqiu	120	—	—	—	120
Wang Bin	120	—	—	—	120
Wang Yong	35	—	—	—	35
Maurice Savart	—	—	—	—	—
Independent non -executive directors					
Lau Chungman	119	—	—	—	119
Guo Chongqing	60	—	—	—	60
Li Xianzong	60	—	—	—	60
	874	500	—	—	1,374

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

(a) Directors' emoluments (continued)

	Year ended 31st December 2006				
Name of director	Fees	Basic salaries, housing allowance, other allowances and benefits in kind	Bonuses	Employer's contributions to retirement schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Executive directors					
Zhang Hongbiao	—	180	—	—	180
Wu Xiandong	—	160	—	—	160
Tan Ruisong	—	140	—	—	140
Non-executive directors					
Liang Zhenhe	120	—	—	—	120
Song Jingang	120	—	—	—	120
Tian Min	120	—	—	—	120
Chen Huaiqiu	120	—	—	—	120
Wang Bin	120	—	—	—	120
Wang Yong	35	—	—	—	35
Maurice Savart	—	—	—	——	
Independent non -executive directors					
Dr. The Hon. Li Kwok -Po, David (note (i))	64	—	—	—	64
Guo Chongqing	62	—	—	—	62
Li Xianzong	62	—	—	—	62
Lau Chungman (note (ii))	63	—	—	—	63
	886	480	—	—	1,366

Notes:

(i) Dr. The Hon. Li Kwok-Po, David resigned on 16th June 2006.

(ii) Mr Lau Chungman was appointed on 28th August 2006.

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

(b) Supervisors' emoluments

The emoluments of each of the supervisors of the Company for the years ended 31st December 2007 and 2006 are set out below.

	Year ended 31st December 2007				
Name of supervisor	Fees	Basic salaries, housing allowance, other allowances and benefits in kind	Bonuses	Employer's contributions to retirement schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Supervisors					
Tang Jianguo	160	—	—	—	160
Wang Shouxin	120	—	—	—	120
Li Shentian	120	—	—	—	120
Bai Ping	120	—	—	—	120
Han Xiaoyang	120	—	—	—	120
Li Deqing	25	—	—	—	25
Yu Yan	—	—	—	—	—
Independent supervisors					
Zheng Li	35	—	—	—	35
Xie Zhihua	35	—	—	—	35
	735	—	—	—	735

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

(b) Supervisors' emoluments (continued)

	Year ended 31st December 2006				
Name of supervisor	Fees	Basic salaries, housing allowance, other allowances and benefits in kind	Bonuses	Employer's contributions to retirement schemes	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Supervisors					
Tang Jianguo	140	—	—	—	140
Wang Shouxin	140	—	—	—	140
Li Shentian	120	—	—	—	120
Bai Ping	120	—	—	—	120
Han Xiaoyang (note (i))	60	—	—	—	60
Lu Liubao (note (ii))	60	—	—	—	60
Liu Xianping (note (ii))	11	—	—	—	11
Yu Yan	24	—	—	—	24
Li Deqing (note (i))	13	—	—	—	13
Independent supervisors					
Zheng Li	35	—	—	—	35
Xie Zhihua	35	—	—	—	35
	758	—	—	—	758

Notes:

(i) These supervisors were appointed on 16th June 2006.

(ii) These supervisors resigned on 16th June 2006.

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

(c) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year are as follows:

	Number of individuals	
	2007	2006
In the capacity as:		
Director	**3**	3
Supervisor	**1**	1
Senior management	**1**	1
	5	5

The five individuals whose emoluments were highest in the Group for the year included three (2006: three) directors and one (2006: one) supervisor whose emoluments are reflected in the analyses presented above. The emoluments payable to the remaining individual during the years ended 31st December 2007 and 2006 are as follows:

	2007	2006
	RMB'000	RMB'000
Basic salaries, housing allowance, other allowances and benefits in kind	**140**	241
Contributions to retirement schemes	**—**	—
	140	241

The emoluments fell within the following band:

	Number of individual	
	2007	2006
Nil – RMB936,400 (equivalent to HKD 1,000,000)	**1**	1

13 DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

(d) No directors or supervisors of the Company waived any emoluments during the years ended 31st December 2006 and 2007. During the year, no emoluments have been paid by the Group to the directors or supervisors of the Company or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office (2006: Nil).

14 PROPERTY, PLANT AND EQUIPMENT

	Group				
	Construction in progress RMB'000	Buildings RMB'000	Plant and equipment RMB'000	Furniture and fixtures, other equipment and motor vehicles RMB'000	Total RMB'000
Cost					
As at 1st January 2007	737,969	2,194,278	9,822,664	735,264	13,490,175
Additions	507,430	136,975	27,849	199,773	872,027
Transfer upon completion	(602,388)	84,227	496,943	21,218	—
Disposals/write off	—	(138,705)	(358,999)	(35,393)	(533,097)
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	(116,337)	(194,655)	(793,204)	(139,358)	(1,243,554)
As at 31st December 2007	526,674	2,082,120	9,195,253	781,504	12,585,551
Accumulated depreciation and impairment					
As at 1st January 2007	—	638,964	3,464,096	337,577	4,440,637
Depreciation	—	48,374	888,726	88,192	1,025,292
Impairment charge(note (c))	—	—	243,421	—	243,421
Disposals/write off	—	(45,263)	(205,675)	(20,460)	(271,398)
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	—	(14,995)	(123,490)	(39,905)	(178,390)
As at 31st December 2007	—	627,080	4,267,078	365,404	5,259,562
Net book value					
As at 31st December 2007	526,674	1,455,040	4,928,175	416,100	7,325,989

14 PROPERTY, PLANT AND EQUIPMENT (continued)

	Group				
	Construction in progress RMB'000	Buildings RMB'000	Plant and equipment RMB'000	Furniture and fixtures, other equipment and motor vehicles RMB'000	Total RMB'000
Cost					
As at 1st January 2006	1,629,663	2,103,442	8,255,149	639,642	12,627,896
Additions	931,725	15,439	113,992	50,056	1,111,212
Transfer upon completion	(1,822,114)	104,886	1,638,230	78,998	—
Disposals/write off	(1,305)	(29,489)	(184,707)	(33,432)	(248,933)
As at 31st December 2006	737,969	2,194,278	9,822,664	735,264	13,490,175
Accumulated depreciation and impairment					
As at 1st January 2006	1,305	573,489	2,793,784	286,240	3,654,818
Depreciation	—	79,437	771,605	77,071	928,113
Impairment charge	—	—	642	—	642
Disposals/write off	(1,305)	(13,962)	(101,935)	(25,734)	(142,936)
As at 31st December 2006	—	638,964	3,464,096	337,577	4,440,637
Net book value					
As at 31st December 2006	737,969	1,555,314	6,358,568	397,687	9,049,538

14 PROPERTY, PLANT AND EQUIPMENT (continued)

	Company		
	Plant and equipment RMB'000	Furniture and fixtures, other equipment and motor vehicles RMB'000	Total RMB'000
Cost			
As at 1st January 2007	**6,637**	**8,654**	**15,291**
Additions	**—**	**180**	**180**
Disposals	**—**	**(250)**	**(250)**
As at 31st December 2007	**6,637**	**8,584**	**15,221**
Accumulated depreciation and impairment			
As at 1st January 2007	**3,340**	**3,746**	**7,086**
Depreciation	**290**	**607**	**897**
Disposals	**—**	**(175)**	**(175)**
As at 31st December 2007	**3,630**	**4,178**	**7,808**
Net book value			
As at 31st December 2007	**3,007**	**4,406**	**7,413**
Cost			
As at 1st January 2006	6,637	8,364	15,001
Additions	—	290	290
As at 31st December 2006	6,637	8,654	15,291
Accumulated depreciation and impairment			
As at 1st January 2006	3,094	2,991	6,085
Depreciation	246	755	1,001
As at 31st December 2006	3,340	3,746	7,086
Net book value			
As at 31st December 2006	3,297	4,908	8,205

14 PROPERTY, PLANT AND EQUIPMENT (continued)

Notes:

(a) Carrying value of the Group's property, plant and equipment pledged as securities for bank borrowings were set out as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Property, plant and equipment pledged (Note 33(h))	**542,303**	209,539

(b) As at 31st December 2007,certain of the Group's property, plant and equipment with carrying value of approximately RMB700,993,000 (2006: RMB900,034,000) were situated on leasehold land in the PRC which are granted by AVIC II for the Group's use at no cost or have been leased from certain fellow subsidiaries under long-term leases. The remaining period of the Group's rights on the leasehold land at 31st December 2007 ranged from 15 to 42 years (2006: 16 to 43 years).

(c) During the year, the Group reviewed the recoverable amount of its property, plant and equipment, taking into account the product lines of the Group and the market conditions, which consequently led to the recognition of an impairment loss of RMB243,421,000 mainly in relation to its automobile segment. The recoverable amount of the relevant assets has been determined on the basis of their value in use. The pre-tax discount rate used in measuring value in use was 9.7% per annum, the basis of which is generally consistant with those used in prior years.

15 LAND USE RIGHTS

	Group	
	2007	2006
	RMB'000	RMB'000
Cost		
As at 1st January	**125,286**	125,286
Disposal	**(2,093)**	—
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	**(7,322)**	—
As at 31st December	**115,871**	125,286
Accumulated amortisation		
As at 1st January	**28,955**	25,972
Amortisation	**6,229**	2,983
Disposal	**(311)**	—
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	**(377)**	—
As at 31st December	**34,496**	28,955
Net book amount		
As at 31st December	**81,375**	96,331

16 INTANGIBLE ASSETS

	Group			
	Development costs RMB'000 (note (i))	Technology know-how RMB'000 (note (ii))	Electricity use rights RMB'000	Total RMB'000
Cost				
As at 1st January 2007	**848,951**	**41,710**	**—**	**890,661**
Additions	**36,574**	**11,711**	**—**	**48,285**
Written off	**(103,896)**	**—**	**—**	**(103,896)**
Effect on proportionate consolidation of a jointly controlled entity (note 3(a)(iii))	**—**	**(20,438)**	**—**	**(20,438)**
As at 31st December 2007	**781,629**	**32,983**	**—**	**814,612**
Accumulated amortisation and impairment				
As at 1st January 2007	**437,838**	**2,169**	**—**	**440,007**
Impairment charge (note (iii))	**5,958**	**—**	**—**	**5,958**
Amortisation	**54,626**	**4,249**	**—**	**58,875**
Written off	**(20,779)**	**—**	**—**	**(20,779)**
Effect on proportionate consolidation of a jointly controlled entity (note 3(a)(iii))	**—**	**(1,063)**	**—**	**(1,063)**
As at 31st December 2007	**477,643**	**5,355**	**—**	**482,998**
Net book amount				
As at 31st December 2007	**303,986**	**27,628**	**—**	**331,614**
Cost				
As at 1st January 2006	865,847	—	37,760	903,607
Additions	50,642	41,710	—	92,352
Written off	(67,538)	—	(37,760)	(105,298)
As at 31st December 2006	848,951	41,710	—	890,661
Accumulated amortisation and impairment				
As at 1st January 2006	312,969	—	37,760	350,729
Impairment charge (note (iii))	70,710	—	—	70,710
Amortisation	121,697	2,169	—	123,866
Written off	(67,538)	—	(37,760)	(105,298)
As at 31st December 2006	437,838	2,169	—	440,007
Net book amount				
As at 31st December 2006	411,113	39,541	—	450,654

16 INTANGIBLE ASSETS (continued)

Notes:

(i) In 2005, the Group entered into a jointly controlled asset arrangement with a fellow subsidiary to develop a new model of aircraft in which the Group has 60.56% participating interests. As at 31st December 2007, the aggregate amounts of development costs incurred by the Group amounted to RMB201,486,000 (2006: RMB175,957,000).

(ii) Technology know-how represents upfront license fees paid for acquiring technical details in connection with certain new automobile and engine models.

(iii) During the year, management has determined to write-off certain development costs for automobile segment as a result of a change in production plan based on the latest market conditions. Impairment losses on intangible assets are mainly in relation to certain development costs of automobile segment for which management estimated that the carrying amounts of these assets have exceeded their recoverable amounts as determined based on value-in-use calculations. The key assumptions and discount rate used in determining the recoverable amounts are consistent to those applied for reviewing other assets impairment.

17 INTERESTS IN SUBSIDIARIES

	Company	
	2007	2006
	RMB'000	RMB'000
Investments, at cost		
– Shares listed in the PRC	**2,205,757**	2,219,793
– Unlisted investments	**1,295,171**	1,295,171
	3,500,928	3,514,964
Less: Provision for impairment losses	**(491,794)**	—
	3,009,134	3,514,964
Loans to subsidiaries (note)	**535,000**	505,000
	3,544,134	4,019,964
Market value of listed shares (also see Note 35(f))	**10,538,842**	4,865,390

Particulars of the principal subsidiaries of the Group as at 31st December 2007 are set out in Note 42.

Note: Loans to subsidiaries are unsecured and non-interest bearing. These loans have no fixed terms of repayment and are regarded as equity contributions to the subsidiaries.

18 SHARE OF RESULTS OF/INTERESTS IN ASSOCIATES

	Group	
	2007	2006
	RMB'000	RMB'000
Share of net assets, as at 1st January	**247,967**	252,863
Share of results of associates		
– Profit before income tax	**61,397**	45,823
– Income tax expense	**(4,686)**	(772)
	56,711	45,051
	304,678	297,914
Dividends received from associates	**(33,256)**	(31,777)
New investments	**30,000**	—
Acquisition	**—**	15,000
Disposals	**(3,501)**	(23,375)
Acquired as a subsidiary	**—**	(9,795)
Share of net assets, as at 31st December	**297,921**	247,967

	Company	
	2007	2006
	RMB'000	RMB'000
Unlisted investment, at cost	**30,000**	—

Particulars of the principal associates of the Group as at 31st December 2007 are set out in Note 42.

19 OTHER NON-CURRENT FINANCIAL ASSETS

	Group	
	2007	2006
	RMB'000	RMB'000
Available-for-sale financial assets		
Listed equity securities, at fair value	**528,719**	—
Investment in promoter shares, unlisted (note)	**—**	62,177
Other investments, unlisted (note)	**69,727**	81,425
Less: Provision for impairment	**(11,029)**	(12,355)
	58,698	69,070
	587,417	131,247

Note: These assets principally represent investments in promoter shares of certain companies listed in the PRC which are only transferable subject to approval from relevant regulatory authorities, and interests in certain unlisted companies; all of which do not have a quoted market price in an active market and for which the range of other methods of reasonably estimating fair value is significant and the probabilities of the various estimates cannot be reasonably assessed. Accordingly, these investments are carried at cost less accumulated impairment losses.

20 DEFERRED INCOME TAXES

Deferred income taxes are calculated in respect of temporary differences under the liability method using the tax rates enacted or substantively enacted by the balance sheet date.

The movement on the deferred income tax accounts is as follows:

Deferred income tax assets:

	Group	
	2007	2006
	RMB'000	RMB'000
As at 1st January	**75,305**	49,489
Credited to consolidated income statement	**55,730**	25,816
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	**(4,794)**	—
As at 31st December	**126,241**	75,305

Deferred income tax liabilities:

	Group	
	2007	2006
	RMB'000	RMB'000
As at 1st January	**(35,872)**	(49,343)
(Charged)/credited to consolidated income statement	**(845)**	13,471
Charged to available-for-sale financial assets reserve	**(119,615)**	—
As at 31st December	**(156,332)**	(35,872)

20 DEFERRED INCOME TAXES (continued)

The deferred income taxes are provided for, prior to offsetting of balances within the same tax jurisdiction, in respect of:

	Group	
	2007	2006
	RMB'000	RMB'000
Deferred income tax assets:		
Provision for impairment of receivables	**64,765**	54,672
Provision for impairment of inventories	**18,437**	14,417
Provision for impairment of investments	**2,545**	1,853
Provision for impairment of property, plant and equipment	**4,667**	2,812
Provision for warranty expense	**43,443**	30,926
Other temporary differences	**20,710**	12,433
	154,567	117,113
Deferred income tax liabilities:		
Development costs	**59,341**	72,590
Fair value changes on available-for-sale financial assets	**119,615**	—
Other temporary differences	**5,702**	5,090
	184,658	77,680
Total deferred income tax assets less total deferred income tax liabilities	**(30,091)**	39,433

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes related to the same fiscal authority. The following amounts, determined after appropriate offsetting, are shown in the consolidated balance sheet:

	Group	
	2007	2006
	RMB'000	RMB'000
Representing:		
Deferred income tax assets	**126,241**	75,305
Deferred income tax liabilities	**(156,332)**	(35,872)
Total deferred income tax assets less total deferred income tax liabilities	**(30,091)**	39,433

20 DEFERRED INCOME TAXES (continued)

Deferred income tax assets are recognised for tax losses carried forward to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group did not recognise deferred income tax assets of approximately RMB323 million (2006: RMB404 million) in respect of tax losses amounting to approximately RMB1,465 million (2006: RMB1,222 million) that can be carried forward against future taxable income. These unrecognised tax losses are expiring within 5 years.

21 ACCOUNTS RECEIVABLE

	Group	
	2007	2006
	RMB'000	RMB'000
Trade receivables, gross (note (a))		
– Fellow subsidiaries (note (b))	**992,205**	1,701,901
– A jointly controlled entity (note (b))	**109,007**	—
– Other related parties (note (b))	**949**	152,778
– Others	**1,329,744**	1,206,085
	2,431,905	3,060,764
Less: Provision for impairment of receivables	**(234,264)**	(222,108)
	2,197,641	2,838,656
Notes receivable (note (c))		
– Fellow subsidiaries	**209,000**	37,263
– Others	**831,032**	841,005
	1,040,032	878,268
	3,237,673	3,716,924

21 ACCOUNTS RECEIVABLE (continued)

Notes:

(a) Certain of the Group's sales were on advance payment or documents against payment. Sales to small, new or short-term customers are normally expected to be settled shortly after delivery. A credit period of up to six months may be granted in respect of sales to customers with good credit history and long-established relationship with the Group. Terms offered to related parties are similar to those offered to third parties. Ageing analysis of trade receivables is as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Current to 1 year	**2,109,716**	2,820,467
1 year to 2 years	**87,174**	63,532
2 years to 3 years	**58,255**	5,449
Over 3 years	**176,760**	171,316
	2,431,905	3,060,764

The credit quality of accounts receivable that are neither past due nor impaired can be assessed by reference to the historical information about counterparty default rates. The existing counterparties do not have significant default in the past.

As of 31st December 2007, trade receivables of RMB176,228,000 (2006: RMB109,820,000) were past due but not impaired. These relate mainly to a number of customers in the aviation segment for whom there is no recent history of default. The ageing analysis of these past due but not impaired receivables is as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Up to 1 year	**64,666**	69,402
1 year to 2 years	**61,920**	32,790
2 years to 3 years	**47,336**	3,800
Over 3 years	**2,306**	3,828
	176,228	109,820

As of 31st December 2007, trade receivables of RMB234,264,000 (2006: RMB222,108,000) were impaired. The individually impaired receivables mainly relate to smaller customers which are in financial difficulties. The ageing of these impaired receivables is as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Current to 1 year	**23,637**	22,228
1 year to 2 years	**25,254**	30,742
2 years to 3 years	**10,919**	1,649
Over 3 years	**174,454**	167,489
	234,264	222,108

21 ACCOUNTS RECEIVABLE (continued)

Movements on the provision for impairment of accounts receivable are as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
At 1st January	**222,108**	252,719
Provision for accounts receivable impairment	**16,734**	25,173
Unused amounts reversed	**(4,578)**	(26,563)
Write off	**—**	(29,221)
At 31st December	**234,264**	222,108

(b) Trade receivables from fellow subsidiaries, a jointly controlled entity and other related parties are unsecured, non-interest bearing and are repayable in accordance with the relevant trading terms.

(c) Substantially all of the notes receivable are bank acceptance notes with average maturity period of within six months.

(d) Substantially all of the accounts receivable are denominated in RMB and the carrying amounts of accounts receivable approximate their fair values.

(e) Certain notes receivable were pledged as security for bank loans (Note 33(h)).

22 ADVANCES TO SUPPLIERS

	Group	
	2007	2006
	RMB'000	RMB'000
Advances to suppliers		
– Fellow subsidiaries	**76,718**	38,824
– Other related parties	**6,242**	2,254
– Others	**436,054**	587,305
	519,014	628,383

In the ordinary course of business, the Group is required to make advance payments to certain suppliers according to the terms of respective agreements. The advance payments made to these parties are unsecured, non-interest bearing and will be settled or utilised in accordance with the terms of relevant agreements.

23 OTHER RECEIVABLES AND PREPAYMENTS

	Group		Company	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Advances for purchase of property, plant and equipment	**4,788**	30,386	**—**	—
Amounts due from customers for contract work (Note 25)	**422,596**	—	**—**	—
Dividends receivable from subsidiaries	**—**	—	**151,128**	137,195
Other advances (note)				
– Ultimate holding company	**6,011**	57,293	**—**	—
– Fellow subsidiaries	**181,181**	38,696	**—**	—
– A jointly controlled entity	**43,051**	—	**—**	—
– Other related parties	**20,258**	16,058	**—**	—
Other receivables	**379,869**	390,526	**—**	—
Prepayments and deposits	**56,000**	101,652	**—**	72
Other current assets	**89,783**	73,607	**230**	—
	1,203,537	708,218	**151,358**	137,267

Note: Other advances mainly represent current account balances with the respective related parties which are unsecured, non-interest bearing and are repayable on demand.

24 INVENTORIES

	Group	
	2007	2006
	RMB'000	RMB'000
Raw materials	**2,272,486**	2,081,314
Work in progress	**924,117**	673,204
Finished goods	**2,163,933**	1,990,662
Consumables	**105,212**	138,385
	5,465,748	4,883,565
Less: Provision for impairment losses	**(188,221)**	(78,652)
	5,277,527	4,804,913

25 CONTRACTS IN PROGRESS

	Group	
	2007	2006
	RMB'000	RMB'000
Contracts in progress at balance sheet date:		
Amounts due from customers for contract work (Note 23)	**422,596**	—
Amounts due to customers for contract work (Note 30)	**—**	(40,409)
	422,596	(40,409)
Contract costs incurred and recognised profits to date	**3,031,092**	4,408,458

At 31st December 2007, no retentions were held by customers for contract work (2006: Nil). Receivables of RMB75,448,000 were recognised on construction contracts and were included in accounts receivable (Note 21) (2006: advances of RMB83,088,000 were received on construction contracts and were included in advances from customers (Note 29)) .

26 PLEDGED DEPOSITS

	Group	
	2007	2006
	RMB'000	RMB'000
Renminbi denominated deposits	**638,350**	694,391

As at 31st December 2007, trade finance facilities utilised by the Group for issuing notes payable to its suppliers amounting to RMB1,487,488,000 (2006: RMB1,365,285,000) were secured by these pledged deposits.

Pledged deposits earn interest at rates ranging from 0.72 % to 3.78% (2006: 0.72% to 1.98%). The conversion of Renminbi denominated balances into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC Government.

27 TERM DEPOSITS WITH INITIAL TERM OF OVER THREE MONTHS

Term deposits with initial term of over three months are denominated in the following currencies:

	Group		Company	
	2007	2006	**2007**	2006
Currency	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Renminbi *	**645,000**	950,658	**615,000**	665,000
Hong Kong Dollar	**46,820**	100,470	**46,820**	100,470
	691,820	1,051,128	**661,820**	765,470

The weighted average effective interest rates of the Group and the Company on term deposits with initial term of over three months were 2.36% (2006: 2.31%) and 2.41% (2006: 2.47%) per annum respectively.

* *The conversion of Renminbi denominated balances into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC Government.*

28 ACCOUNTS PAYABLE

	Group	
	2007	2006
	RMB'000	RMB'000
Trade payables (note (a))		
– Ultimate holding company (note (b))	**—**	6,487
– Fellow subsidiaries (note (b))	**529,067**	336,891
– A jointly controlled entity (note (b))	**2,774**	—
– Other related parties (note (b))	**8,372**	300,957
– Others	**4,389,974**	4,587,023
	4,930,187	5,231,358
Notes payable (note (c))		
– Fellow subsidiaries	**366,881**	176,131
– Other related parties	**—**	756
– Others	**1,464,145**	1,628,999
	1,831,026	1,805,886
	6,761,213	7,037,244

28 ACCOUNTS PAYABLE (continued)

Notes:

(a) The normal credit period for trade payables generally ranges from 0 to 6 months. Ageing analysis of trade payables is as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Current to 1 year	**4,287,572**	4,953,475
1 year to 2 years	**489,816**	215,827
2 years to 3 years	**116,883**	46,806
Over 3 years	**35,916**	15,250
	4,930,187	5,231,358

(b) Trade payables to ultimate holding company, fellow subsidiaries, a jointly controlled entity and other related parties are unsecured, non-interest bearing and will be settled in accordance with the relevant trading terms.

(c) Substantially all of the notes payable are bank acceptance notes with average maturity period of within six months.

(d) The carrying amounts of accounts payable approximate their fair values.

29 ADVANCES FROM CUSTOMERS

	Group	
	2007	2006
	RMB'000	RMB'000
Advances from customers		
– Fellow subsidiaries	**405,917**	21,381
– Other related parties	**—**	43,664
– Others	**478,651**	395,425
	884,568	460,470

In the ordinary course of the Group's business, certain of the Group's customers are required to pay advance deposits according to terms of the respective agreements. The advances from fellow subsidiaries and other related parties are unsecured, non-interest bearing and will be settled or utilised in accordance with the terms of relevant agreements.

30 OTHER PAYABLES AND ACCRUALS

	Group		Company	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Payable for property, plant and equipment				
– Fellow subsidiaries (note (i))	**6,767**	55	**—**	—
– Others	**130,583**	212,886	**—**	—
Wages, salaries and bonuses payables	**308,234**	382,860	**137**	156
Accrued expenses	**356,613**	385,901	**4,705**	3,546
Deferred income from government grants	**17,755**	43,441	**—**	—
Consumption tax, business tax and other taxes payable	**31,253**	60,212	**50**	3
Amounts due to customers for contract work (Note 25)	**—**	40,409	**—**	—
Other advances (note (ii))				
– Ultimate holding company	**13,680**	45,997	**12,240**	37,431
– Fellow subsidiaries	**161,971**	205,674	**14,322**	12,237
– A jointly controlled entity	**192**	—	**—**	—
– Other related parties	**—**	22,362	**—**	—
Payable relating to share reform	**96,029**	96,029	**—**	—
Other current liabilities	**201,266**	172,058	**—**	—
	1,324,343	1,667,884	**31,454**	53,373

Notes:

(i) Payable for property, plant and equipment is unsecured, non-interest bearing and will be settled in accordance with the relevant trading terms.

(ii) Other advances mainly represent current account balances with the respective related parties which are unsecured, non-interest bearing and are repayable on demand.

31 AMOUNTS PAYABLE TO ULTIMATE HOLDING COMPANY

	Group		Company	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Supplementary pension subsidies (note (a))	**464,298**	464,298	**464,298**	464,298
One-off housing benefit (note (b))	**56,226**	56,226	**—**	—
	520,524	520,524	**464,298**	464,298

Notes:

(a) Prior to the Reorganisation, the Group paid supplementary pension subsidies to its retired employees who retired prior to the Reorganisation. In addition, the Group was committed to make periodic benefits payments to certain former employees who retired early in accordance with various rationalisation programmes adopted by the Group prior to the Reorganisation. Pursuant to the Reorganisation, the Group and AVIC II agreed that, upon establishment of the Company, the Group's obligations to make these supplementary pension benefits and early retirement payments as at 30th June 2002 were assumed by AVIC II and the actual payments of these obligations will be made by AVIC II. The Group is not obliged to any further liabilities in respect of these supplementary pension benefits and early retirement payments to these former employees after 30th June 2002. The above obligations were actuarially determined by a PRC insurance company using the projected unit credit method and are repayable to AVIC II with no fixed repayment terms under the Reorganisation. The balance is unsecured and non-interest bearing.

(b) This represents provision made by a subsidiary in connection with one-off housing subsidies for its eligible employees as at 31st December 2000 as detailed in Note 3(p)(iii). AVIC II has undertaken to bear any final actual cash settlement to those eligible employees in excess of RMB56,226,000. During 2006, it was agreed that such one-off housing subsidies and future settlements shall be handled by AVIC II and accordingly the balance payable was transferred to AVIC II.

32 PROVISIONS

	Group		
	One-off housing subsidies RMB'000	**Warranty RMB'000 (note)**	**Total RMB'000**
As at 1st January 2007	**—**	**103,284**	**103,284**
Additional provisions	**—**	**246,903**	**246,903**
Utilised during the year	**—**	**(171,364)**	**(171,364)**
Effect on proportionate consolidation of a jointly controlled entity (Note 3(a)(iii))	**—**	**(4,392)**	**(4,392)**
As at 31st December 2007	**—**	**174,431**	**174,431**
As at 1st January 2006	56,226	81,636	137,862
Additional provisions	—	154,841	154,841
Utilised during the year	—	(133,193)	(133,193)
Transfer (Note 31(b))	(56,226)	—	(56,226)
As at 31st December 2006	—	103,284	103,284

Note: The Group provides warranties to its customers on certain automobile and aviation products and undertakes to repair or replace items that fail to perform up to certain specified standard. Provision for expected warranty claims has been determined based on historical warranty information after taking into account of the Group's recent claim experience.

33 BORROWINGS

	Group 2007 RMB'000	Group 2006 RMB'000
Short-term borrowings		
Bank borrowings		
– Secured (note (h))	**2,664,794**	3,608,111
– Unsecured	**1,637,369**	1,398,689
	4,302,163	5,006,800
Other short-term borrowings, unsecured (note (c))	**10,000**	394,798
	4,312,163	5,401,598
Current portion of long-term borrowings	**650,457**	433,695
	4,962,620	5,835,293
Long-term borrowings		
Bank borrowings		
– Secured (note (h))	**1,611,890**	1,032,760
– Unsecured	**—**	59,800
	1,611,890	1,092,560
Other borrowings		
– Secured (note (h))	**10,650**	12,067
– Unsecured (note (d))	**139,457**	165,772
	150,107	177,839
	1,761,997	1,270,399
Less: Current portion of long-term borrowings	**(650,457)**	(433,695)
	1,111,540	836,704
Total borrowings	**6,074,160**	6,671,997

33 BORROWINGS (continued)

Notes:

(a) The long-term borrowings are analysed as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Wholly repayable within five years		
– Bank borrowings	**1,340,000**	820,670
– Other borrowings	**139,457**	165,772
	1,479,457	986,442
Not wholly repayable within five years		
– Bank borrowings	**271,890**	271,890
– Other borrowings	**10,650**	12,067
	282,540	283,957
	1,761,997	1,270,399

(b) The long-term borrowings are repayable as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Bank borrowings:		
– Within one year	**511,000**	400,670
– In the second year	**319,000**	100,000
– In the third to fifth year	**510,000**	366,000
– After the fifth year	**271,890**	225,890
	1,611,890	1,092,560
Other borrowings:		
– Within one year	**139,457**	33,025
– In the third to fifth year	**—**	132,747
– After the fifth year	**10,650**	12,067
	150,107	177,839
	1,761,997	1,270,399

33 BORROWINGS (continued)

Notes: (continued)

(c) As at 31st December 2007, other short-term borrowings represented a loan granted by Shenzhen Finance Bureau to a subsidiary of the Group. The loan is unsecured, non-interest bearing and is repayable in full in 2008.

As at 31st December 2006, other short-term borrowings represented a zero coupon debenture issued by a subsidiary of the Group with an aggregate face value of RMB400,000,000 for a term of one year. The debenture was issued at RMB96.68 for par value of RMB100 each. The debenture was initially recognised at fair value and subsequently carried at amortised cost. The debenture was fully redeemed during the year.

(d) Other long-term borrowings

Included in unsecured other long-term borrowings was a loan granted by Shenzhen Finance Bureau to a subsidiary of the Group with a face value of RMB150,000,000. The loan is unsecured, non-interest bearing and is repayable in full in 2008.

(e) The exposure of the total borrowings of the Group to interest rate changes is as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Bank borrowings		
– Fixed rates	**2,830,963**	5,889,470
– Floating rates	**3,083,090**	209,890
	5,914,053	6,099,360
Other borrowings		
– Fixed rates	**160,107**	572,637
– Floating rates	**—**	—
	160,107	572,637
	6,074,160	6,671,997

The annual effective interest rates of long-term and short-term borrowings at balance sheet date were as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Weighted average effective interest rates		
– Bank borrowings	**6.39%**	5.29%
– Other borrowings	**0.07%**	1.42%

33 BORROWINGS (continued)

Notes: (continued)

(f) The carrying amounts of long-term and short-term borrowings are denominated in the following currencies:

	Group	
	2007	2006
Currency	**RMB'000**	RMB'000
Renminbi	**5,536,316**	5,867,581
United States Dollar	**10,650**	470,755
Euro	**455,500**	333,661
Others	**71,694**	—
	6,074,160	6,671,997

(g) The carrying amount and fair value of non-current portion of long-term borrowings are as follows:

	Group			
	Carrying amount		Fair value	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Bank borrowings	**1,100,890**	691,890	**1,027,450**	661,237
Other borrowings	**10,650**	144,814	**4,359**	137,656
	1,111,540	836,704	**1,031,809**	798,893

The fair values are based on discounted cash flows using applicable discount rates based upon the prevailing market rates of interest available to the Group for financial instruments with substantially the same terms and characteristic as at the balance sheet dates. Such discount rates ranged from 7.56 % to 7.83% as at 31st December 2007 (2006: 6.30% to 6.84%), depending on the type of the debt. The carrying amounts of current borrowings approximate their fair values.

33 BORROWINGS (continued)

Notes: (continued)

(h) The Group's long-term and short-term borrowings are secured as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Securities over the Group's assets, at carrying value		
– Property, plant and equipment, at net book value (Note 14(a))	**542,303**	209,539
– Notes receivable (Note 21(e))	**59,866**	33,561
– Pledged deposits (Note 26)	**638,350**	694,391
Guarantees provided by		
– Ultimate holding company (Note 39(d))	**389,890**	289,890
– Fellow subsidiaries (Note 39(d))	**90,650**	540,729
– Subsidiaries within the Group (cross guarantees)	**3,702,094**	3,567,320
– Third parties	**50,000**	145,000

(i) As at 31st December 2007, the Group had the following undrawn committed borrowing facilities.

	Group	
	2007	2006
	RMB'000	RMB'000
Expiring beyond one year at floating rates	**1,476,567**	824,000

34 SHARE CAPITAL

	Company	
	2007	2006
	RMB'000	RMB'000
Registered:	**4,643,609**	4,643,609
Issued and fully paid:		
2,963,808,000 Domestic Shares of RMB1 each	**2,963,808**	2,963,808
1,679,800,500 H Shares of RMB1 each	**1,679,801**	1,679,801
	4,643,609	4,643,609

During 2003, the Company completed its initial public offering (the "Offering") and placing of 1,679,800,500 H Shares with a par value of RMB1.00 each at a price of HK$1.21 (equivalent to RMB1.28) per H Share in cash for an aggregate consideration of HK$2,033 million (equivalent to approximately RMB2,167 million), which comprised 1,527,090,000 new H Shares issued by the Company and 152,710,500 shares offered by the Promoters pursuant to an approval from the State-owned Assets Supervision and Administration Commission of the State Council to convert such relevant Domestic Shares owned by the Promoters into H Shares as part of the Offering. As a result, the issued share capital of the Company increased to 4,643,608,500 shares, comprising 2,963,808,000 Domestic Shares and 1,679,800,500 H Shares, representing 63.83% and 36.17% of the issued capital respectively.

The H Shares rank pari passu in all respects with the Domestic Shares and rank equally for all dividends or distributions declared, paid or made except that all dividends in respect of H Shares are to be paid by the Company in Hong Kong dollars and H Shares may only be subscribed for by, and traded in Hong Kong dollars between legal or natural persons of Hong Kong, Macau, Taiwan or any other country other than the PRC. The transfer of the Domestic Shares is subject to such restrictions as the PRC laws may impose from time to time.

35 RESERVES

	Company				
	Capital reserve RMB'000 (Note (b))	Statutory surplus reserve RMB'000 (Note (c))	Statutory public welfare fund RMB'000 (Note (d))	(Accumulated losses)/ retained earnings RMB'000 (Note (e))	Total RMB'000
Balance at 1st January 2007	**(2,073)**	**26,712**	**—**	**(163,421)**	**(138,782)**
Loss for the year	**—**	**—**	**—**	**(462,588)**	**(462,588)**
Transfer to statutory reserve	**—**	**4,466**	**—**	**(4,466)**	**—**
As at 31st December 2007	**(2,073)**	**31,178**	**—**	**(630,475)**	**(601,370)**
Balance at 1st January 2006	(2,073)	17,809	8,903	52,322	76,961
Loss for the year	—	—	—	(166,985)	(166,985)
2005 dividend	—	—	—	(48,758)	(48,758)
Transfer to statutory reserve	—	8,903	(8,903)	—	—
Balance at 31st December 2006	(2,073)	26,712	—	(163,421)	(138,782)

35 RESERVES (continued)

Notes:

(a) Movements in the reserves of the Group are set out in the consolidated statement of changes in equity on pages 55 to 56.

(b) Capital reserve

Capital reserve of the Company represents the difference between the amount of share capital issued by the Company and the historical net value of the assets, liabilities and interests transferred to the Company upon its establishment, set off by net premium on issue of shares upon listing of the Company. Capital reserves of the Group also included reserves arising from the issuance of additional shares by a subsidiary or capital contributions in associates.

(c) Statutory surplus reserve

In accordance with the relevant PRC laws and financial regulations, every year the Company is required to transfer 10% of the profit after taxation determined in accordance with the PRC accounting standards to the statutory surplus reserve until the balance reaches 50% of the paid-up share capital. Such reserve can be used to reduce any losses incurred and to increase share capital. Except for the reduction of losses incurred, any other usage should not result in this reserve balance falling below 25% of the registered capital.

In prior years, the Group reported its share of statutory surplus reserve appropriations made by the entities consolidated in the Group's consolidated financial statements based on the respective equity interests held by the Group in these entities. Effective from 1st January 2007, the Group did not make such reserve appropriations upon the preparation of its consolidated financial statements, and the corresponding changes to the reserves have been adjusted retrospectively. There are no impact on net loss and loss per share of the Group as a result of the changes. The opening retained earnings of the Group at 1st January 2006 increased by RMB148,214,000.

(d) Statutory public welfare fund

In prior years, the Company was required to transfer between 5% and 10% of the profit after taxation determined in accordance with the PRC accounting standards to a statutory public welfare fund every year pursuant to the relevant PRC regulations and the Articles of Association of the Company. The use of this fund was restricted to capital expenditure for employees' collective welfare facilities, the ownership in respect of which belonged to the Group. The statutory public welfare fund was not available for distribution to shareholders except under liquidation. Once the capital expenditure on staff welfare facilities had been made, an equivalent amount must be transferred from the statutory public welfare fund to the discretionary surplus reserve, a reserve which could be used to reduce any losses incurred or to increase share capital.

During the year ended 31st December 2006, as a result of the issuance of certain revised PRC regulations which was effective from 1st January 2006, the Company was no longer required to provide for statutory public welfare fund. Consequently, the balance of statutory public welfare fund as at 31st December 2005 was transferred into statutory surplus reserve.

(e) Retained earnings available for distribution

In accordance with the relevant PRC regulations and Articles of Association of the Company, retained earnings available for distribution by the Company will be deemed to be the lower of the amounts determined in accordance with the PRC GAAP and the amount determined in accordance with IFRS. As at 31st December 2006 and 2007, there were no retained earnings available for distribution under both PRC GAAP and IFRS.

35 RESERVES (continued)

Notes: (continued)

(f) Share reform

In 2006, the Group's four subsidiaries whose A shares are listed on the Shanghai Stock Exchange have completed their respective share reform schemes (collectively "Share Reform"). Consequently, the Group's interests in the domestic shares ("Domestic Shares") in each of Harbin Dongan Auto Engine Co., Ltd ("Dongan"), Jiangxi Changhe Automobile Co., Ltd ("Changhe"), Jiangxi Hongdu Aviation Industry Co., Ltd. ("Hongdu") and Hafei Aviation Industry Co., Ltd. ("Hafei") have been converted into A shares and become tradable on the Shanghai Stock Exchange subject to certain specified conditions.

As a result of the Share Reform, the Group's equity interests in Dongan, Changhe, Hongdu and Hafei have been reduced from 70.01%, 72.53% (among which 0.96% was held by Dongan), 54.75% and 55.73% to 59.51%, 63.22% (among which 0.83% was held by Dongan), 55.29% and 50.05% respectively.

In accordance with the Group's accounting policy, transactions with minority shareholders are dealt with in reserves. Accordingly, the aggregate effect on the reduction of equity interests in these subsidiaries of approximately RMB507,746,000 was accounted for as a reduction of the Group's reserves in the consolidated financial statements for the year ended 31st December 2006.

In the Company's financial statements, the effect of reduction in the equity interest in the Company's directly owned subsidiaries, namely, Dongan, Changhe and Hongdu totalling RMB328,993,000 was charged directly to the Company's income statement for the year ended 31st December 2006.

36 CONSOLIDATED CASH FLOW STATEMENT

(a) Cash generated from operations

	Group	
	2007	2006
	RMB'000	RMB'000
Loss before taxation	**(796,709)**	(473,263)
Adjustments for:		
Share of results of associates	**(56,711)**	(45,051)
(Gain)/loss on disposal of		
– Property, plant and equipment	**(16,838)**	(12,780)
– A subsidiary	**—**	3
– Certain interests in subsidiaries	**(32,440)**	—
– Associates	**—**	9,811
Amortisation		
– Land use rights	**6,229**	2,983
– Intangible assets	**58,875**	123,866
Amortisation of deferred income relating to government grants	**(33,161)**	(18,396)
Depreciation on property, plant and equipment	**1,025,292**	928,113
Write off of intangible assets	**83,117**	—
Provision/(reversal of provision) for impairment		
– Property, plant and equipment	**243,421**	642
– Intangible assets	**5,958**	70,710
– Other non-current financial assets	**(1,326)**	12,355
– Receivables	**13,067**	22,126
– Inventories	**121,875**	121
Dividend income from other non-current financial assets	**(4,870)**	—
Interest income	**(57,966)**	(78,256)
Interest expense	**338,815**	253,061
	896,628	796,045

36 CONSOLIDATED CASH FLOW STATEMENT (continued)

(a) Cash generated from operations (continued)

	Group	
	2007	2006
	RMB'000	RMB'000
Changes in working capital (excluding the effects of acquisitions and disposals of subsidiaries):		
– Decrease/(increase) in accounts receivable	**289,938**	(817,032)
– (Increase)/decrease in advances to suppliers, other receivables and prepayments	**(284,615)**	178,710
– Increase in inventories	**(851,867)**	(680,764)
– (Increase)/decrease in financial assets at fair value through profit or loss	**(7,414)**	41,027
– Increase in accounts payable	**57,108**	1,223,373
– Increase in advance from customers, other payables and accruals	**328,073**	383,081
– Increase/(decrease) in provisions	**75,539**	(34,578)
– Decrease in amounts payable to ultimate holding company	**—**	(11,774)
– Increase in deferred income from government grants	**—**	115,079
Net cash generated from operations	**503,390**	1,193,167

36 CONSOLIDATED CASH FLOW STATEMENT (continued)

(b) In the cash flow statement, proceeds from sale of property, plant and equipment comprise:

	Group	
	2007	2006
	RMB'000	RMB'000
Net book amount (Note 14)	**261,699**	105,997
Gain on sale of property, plant and equipment	**16,838**	12,780
Receivables from sale of property, plant and equipment	**(263,718)**	(97,690)
Proceeds from sale of property, plant and equipment	**14,819**	21,087

(c) Disposal of a subsidiary

	Group	
	2007	2006
	RMB'000	RMB'000
Property, plant and equipment	**516**	233
Current assets	**43,588**	12,102
Total assets	**44,104**	12,335
Total liabilities	**(51)**	(9,429)
Minority interests	**(2,203)**	(1,424)
Net assets sold	**41,850**	1,482
Total consideration	**41,850**	1,479
Loss on disposal of a subsidiary	**—**	3
Net cash outflow from disposal is determined as follows:		
Proceeds received from disposal of a subsidiary	**41,850**	1,479
Less: Cash and cash equivalents in a subsidiary disposed	**(43,409)**	(2,365)
Net cash outflow from disposal of a subsidiary	**(1,559)**	(886)

36 CONSOLIDATED CASH FLOW STATEMENT (continued)

(d) Acquisition of a subsidiary

Details of net assets acquired are as follows:

	As at 1st January 2006 RMB'000
Purchase consideration:	
– cash paid	11,994
Fair value of net assets acquired (shown as below)	(11,994)

The assets and liabilities arising from the acquisition are as follows:

	Fair value RMB'000	Acquiree's carrying amount RMB'000
Property, plant and equipment	9,734	9,734
Receivables	19,198	19,198
Cash and cash equivalents	3,598	3,598
Payables	(10,730)	(10,730)
Net assets	21,800	21,800
Interests held as an associate (Note 18)	(9,795)	
Minority interests	(11)	
Net assets acquired	11,994	
Purchase consideration settled in cash		11,994
Cash and cash equivalents in a subsidiary acquired		(3,598)
Cash outflow on acquisition		8,396

The acquired subsidiary's contributions to the Group's revenue and operating results for the period from the date of acquisition to 31st December 2006 were not material.

36 CONSOLIDATED CASH FLOW STATEMENT (continued)

(e) Analysis of cash and cash equivalents

	Group		Company	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Bank balances and cash	**2,375,706**	3,155,527	**98,266**	91,592
Term deposits with initial term of less than three months	**77,000**	—	**45,000**	—
	2,452,706	3,155,527	**143,266**	91,592

The cash and cash equivalents are denominated in the following currencies:

	Group		Company	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Renminbi*	**2,384,976**	3,030,648	**140,916**	87,181
Other currencies	**67,730**	124,879	**2,350**	4,411
	2,452,706	3,155,527	**143,266**	91,592

The weighted average effective interest rate of the Group and the Company on term deposits with initial term of less than three months was 1.71% per annum. Bank balances earn interest at floating rates based on daily bank deposit rates.

* *The conversion of these RMB denominated balances into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC Government.*

37 COMMITMENTS

(a) Capital commitments

The Group has the following capital commitments not provided for as at 31st December 2007:

	Group 2007 RMB'000	Group 2006 RMB'000
Acquisition of property, plant and equipment		
– Authorised but not contracted for	**48,557**	161,012
– Contracted but not provided for	**228,001**	148,446
	276,558	309,458
Construction commitments		
– Authorised but not contracted for	**14,070**	—
– Contracted but not provided for	**57,846**	6,050
	71,916	6,050
Investment in a jointly controlled asset		
– Contracted but not provided for	**40,764**	66,292
Investments in an associate		
– Contracted but not provided for	**88,175**	48,000
	477,413	429,800

37 COMMITMENTS (continued)

(b) Operating lease commitments

The Group has commitments to make the following future minimum lease payments under non-cancellable operating leases as at 31st December 2007:

	Group	
	2007	2006
	RMB'000	RMB'000
Land and buildings		
– Not later than one year	**17,406**	26,132
– Later than one year and not later than five years	**47,170**	66,904
– Later than five years	**21,426**	101,004
	86,002	194,040

Generally, the Group's operating leases are for terms of 1 to 20 years.

(c) The Company did not have any significant commitment as at 31st December 2007 (2006: Nil).

38 INTEREST IN A JOINTLY CONTROLLED ENTITY

Particulars of the jointly controlled entity of the Group as at 31st December 2007 are set out in Note 42.

The following amounts represent the Group's share of the jointly controlled entity's assets and liabilities as at 31st December 2007, and the Group's share of its income and results since the date when it was reclassified as a jointly controlled entity, which are included in the Group's consolidated balance sheet and consolidated income statement:

	2007 RMB'000
Assets:	
Non-current assets	1,097,546
Current assets	609,947
	1,707,493
Liabilities:	
Non-current liabilities	—
Current liabilities	1,033,513
	1,033,513
Net assets	673,980
Income	1,263,021
Expenses	(1,685,139)
Net loss	(422,118)
Proportionate interest in the jointly controlled entity's capital commitments	92,729

38 INTEREST IN A JOINTLY CONTROLLED ENTITY (continued)

The jointly controlled entity did not have any material operating lease commitments as at 31st December 2007.

There are no contingent liabilities relating to the Group's interest in the jointly controlled entity and the jointly controlled entity did not have any material contingent liabilities as at 31st December 2007.

39 SIGNIFICANT RELATED PARTY TRANSACTIONS

The Group is controlled by AVIC II, which owns 61.06% of the Company's shares as at 31st December 2007. The remaining 38.94% of the shares are widely held.

Related parties refer to entities in which AVIC II has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions; or directors or officers of the Company and of its ultimate holding company, associates or jointly controlled entity. Given that the PRC government still owns a significant portion of the productive assets in the PRC despite the continuous reform of the government structure, a majority of the Group's business activities had been conducted with enterprises directly or indirectly owned or controlled by the PRC government ("state-owned enterprises"), including AVIC II, its subsidiaries, associated companies and jointly controlled entities in the ordinary course of business.

In accordance with IAS 24, "Related Party Disclosures", state-owned enterprises and their subsidiaries, other than entities under AVIC II (also a state-owned enterprise), directly or indirectly controlled by the PRC government are also defined as related parties of the Group. Neither AVIC II nor the PRC government publishes financial statements for public use. In the normal course of the Group's business, it may either enter into various transactions with one or more of such state-owned enterprises and their subsidiaries.

39 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

The following is a summary of significant related party transactions entered into in the ordinary course of business between the Group and its related parties and the balances arising from related party transactions in addition to the related party information shown elsewhere in the financial statements. Management of the Group are of the opinion that meaningful information relating to related party disclosures has been adequately disclosed.

(a) The directors of the Company has identified the following principal related parties, which had significant related party transactions or balances with the Group during the year:

Principal related parties	**Relationship with the Group**
Ultimate holding company	
– AVIC II	Ultimate holding company of the Company
Fellow subsidiaries	
– Jiangxi Hongdu Aviation Industrial Group Corporation ("Hongdu Group")	A wholly-owned subsidiary of AVIC II
– Changhe Aircraft Industries (Group) Ltd.	A wholly-owned subsidiary of AVIC II
– Harbin Dongan Engine (Group) Co., Ltd.	A wholly-owned subsidiary of AVIC II
– Harbin Aircraft Industry (Group) Co., Ltd.	A wholly-owned subsidiary of AVIC II
– Hefei Changhe Industry Co., Ltd.	A wholly-owned subsidiary of AVIC II
– China National Aero-Technology Import & Export Corporation	A subsidiary of AVIC II
– CATIC International Industry and Trade Company	A subsidiary of AVIC II
Other related parties	
– Shenzhen Shenhang Avionics Co., Ltd.	An associate of Group
– Mitsubishi Motor Corporation	A shareholder of Harbin Dongan Automotive Engine Manufacturing Co., Ltd., a subsidiary of the Group
– Jiangxi Changhe Suzuki Automobile Co., Ltd.	A jointly controlled entity
Other state-owned enterprises	Related parties as defined under IAS 24

39 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

(b) Significant transactions with related parties:

	Group	
	2007	2006
	RMB'000	RMB'000
Revenues		
Revenue from sale of goods and materials		
– Fellow subsidiaries	**4,685,494**	3,599,256
– A jointly controlled entity	**163,066**	—
– Other related parties	**14,948**	235,875
– Other state-owned enterprises	**1,115,196**	1,237,965
Revenue from rendering of service		
– Fellow subsidiaries	**71,427**	159,689
Expenses		
Purchases of goods and raw materials		
– Fellow subsidiaries	**2,553,654**	1,666,825
– A jointly controlled entity	**34,445**	—
– Other related parties	**248,272**	1,012,790
– Other state-owned enterprises	**1,206,301**	2,440,136
Service fees payable		
– Fellow subsidiaries (note (ii))	**166,988**	423,203
– Other related parties	**14,067**	30,743
– Other state-owned enterprises	**63,654**	76,221
Rental expenses for property, plant and equipment		
– Fellow subsidiaries	**41,892**	37,841
Interest expense		
– Other state-owned enterprises	**355,140**	259,926
Key management compensations		
– Salaries, bonuses and other welfares	**2,648**	2,814

Notes:

(i) In the opinion of the directors of the Company, the above transactions were carried out in the ordinary course of the Group's business and were determined based on mutually agreed terms.

(ii) Included in service fees to fellow subsidiaries for the year ended 31st December 2006 was an amount of RMB80,095,000 representing compensation paid to a fellow subsidiary of the Group in connection with its logistic services provided to the Group for the years ended 31st December 2004 and 2005. The amount was determined bases on mutually agreed terms.

39 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

(c) Significant balances with related parties:

	Group	
	2007	2006
	RMB'000	RMB'000
Assets		
Accounts receivable		
– Fellow subsidiaries	**992,205**	1,701,901
– A jointly controlled entity	**109,007**	—
– Other related parties	**949**	152,778
– Other state-owned enterprises	**63,330**	86,849
Notes receivable		
– Fellow subsidiaries	**209,000**	37,263
Advance to suppliers		
– Fellow subsidiaries	**76,718**	38,824
– Other related parties	**6,242**	2,254
– Other state-owned enterprises	**93,591**	134,045
Other receivables and prepayments		
– Ultimate holding company	**6,011**	57,293
– Fellow subsidiaries	**181,181**	38,696
– A jointly controlled entity	**43,051**	—
– Other related parties	**20,258**	16,058
– Other state-owned enterprises	**384**	69,902
Pledged deposits		
– Other state-owned enterprises	**638,350**	656,643
Term deposits with initial term of over three months		
– Other state-owned enterprises	**691,820**	1,051,128
Cash and cash equivalents deposited with		
– Other state-owned enterprises	**2,126,852**	3,005,885

39 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

(c) Significant balances with related parties: (continued)

	Group	
	2007	2006
	RMB'000	RMB'000
Liabilities		
Accounts payable		
– Ultimate holding company	**—**	6,487
– Fellow subsidiaries	**529,067**	336,891
– A jointly controlled entity	**2,774**	—
– Other related parties	**8,372**	300,957
– Other state-owned enterprises	**267,643**	1,035,050
Notes payable		
– Fellow subsidiaries	**366,881**	176,131
– Other related parties	**—**	756
– Other state-owned enterprises	**479,413**	—
Advance from customers		
– Fellow subsidiaries	**405,917**	21,381
– Other related parties	**—**	43,664
– Other state-owned enterprises	**60,540**	77,468
Other payables and accruals		
– Ultimate holding company	**13,680**	45,997
– Fellow subsidiaries	**168,738**	205,729
– A jointly controlled entity	**192**	—
– Other related parties	**—**	22,362
– Other state-owned enterprises	**1,603**	19,104
Bank borrowings		
– Other state-owned enterprises	**5,161,985**	6,099,360

Details of the balances with ultimate holding company, fellow subsidiaries, a jointly controlled entity and other related parties are disclosed in Notes 21, 22, 23, 28, 29, 30 and 31 to the financial statements.

39 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

(d) Other items:

	Group	
	2007	2006
	RMB'000	RMB'000
Guarantees on bank loans granted to the Group from		
– Ultimate holding company	**389,890**	289,890
– Fellow subsidiaries	**90,650**	540,729

In addition, AVIC II granted certain leasehold land for the Group's use at no cost, details of which are disclosed in Note 14(b).

(e) Whilst other state-owned enterprises are related parties of the Group as defined under IAS 24, the directors are of the opinion that each party is operating independently; and the above balances are arising in the ordinary course of the Group's businesses. Details of these balances are included under Notes 26, 27, 33 and 36(e) to the financial statements.

40 FINANCIAL RISK MANAGEMENT

(a) Financial risk factors

The Group's activities expose it to a variety of financial risks: market risks (including: foreign exchange risk, interest-rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The use of financial derivatives to hedge certain risk exposures is governed by the Group's policies approved by the board of directors. The Group does not use derivative financial instruments for speculative purposes.

(i) *Foreign exchange risk*

The Group mainly operates in the PRC with most of the transactions settled in RMB. Foreign exchange rate risk arises when future commercial translation or recognised assets and liabilities are denominated in a currency that is not the entity's functional currency. The Group is exposed to foreign exchange risk primarily with respect to the United States Dollar ("USD"), Euro and Hong Kong Dollar ("HKD").

The Group's assets and liabilities, and transactions arising from its operations primarily do not expose to material foreign exchange risk. Other than certain term deposits, bank balances and borrowings, the Group's assets and liabilities are primarily denominated in RMB. The Group generates RMB from sales in the PRC to meet its liabilities denominated in RMB. The Group has not used any forward contracts to hedge its exposure as the cost-benefit is considered not effective.

40 FINANCIAL RISK MANAGEMENT (continued)

(a) Financial risk factors (continued)

(i) *Foreign exchange risk (continued)*

As at 31st December 2006 and 2007, certain of the Group's borrowings (Note 33), term deposits and bank balances (Notes 27 and 36(e)) were denominated in foreign currencies. RMB experienced certain appreciation in recent years which is the major reason for the exchange differences recognised by the Group for the years ended 31 December 2006 and 2007. Further appreciation or depreciation of RMB against these currencies will affect the Group's financial position and results of operations.

However, as foreign currency denominated assets and liabilities are relatively insignificant to the Group, management considers that the Group's volatility against changes in exchange rates of foreign currencies would not be significant. Accordingly, no sensitivity analysis is presented for foreign exchange risk.

(ii) *Cash flow and fair value interest-rate risk*

The Group's income and operating cash flows are substantially independent of changes in market interest rates and the Group has no significant interest-bearing assets except for the bank deposits and cash and cash equivalents, details of which have been disclosed in Notes 26, 27 and 36(e). The Group's exposure to changes in interest rates is mainly attributable to its borrowings, details of which have been disclosed in Note 33. Borrowings carried at floating rates expose the Group to cash flow interest-rate risk whereas those carried at fixed rates expose the Group to fair value interest-rate risk. As of 31st December 2007, 49% (2006: 97%) of the Group's borrowings were at fixed rates. The Group has not used any interest rate swaps to hedge its exposure to interest rate risk.

At 31st December 2007, if the interest rates on bank borrowings' deposits and cash and cash equivalents had been 50 basis points higher/lower than the prevailing rate announced by People's Bank of China, with all other variables held constant, loss for the year would have been RMB2,250,000 (2006: RMB15,715,000) lower/higher.

(iii) *Price risk*

The Group is exposed to equity securities price risk in respect of investments held by the Group which are classified as available-for-sale financial assets and financial assets at fair value through profit or loss. Some of these financial assets are publicly traded in recognised stock exchanges. At 31st December 2007, if the quoted market price of these equity investments held by the Group had increased/decreased by 10%, with all other variables held constant, loss for the year would have been RMB556,000 (2006: Nil) lower/higher and equity would have been RMB39,654,000 (2006: Nil) higher/lower as a result of the changes in fair value of financial assets at fair value through profit or loss and available-for-sale financial assets.

40 FINANCIAL RISK MANAGEMENT (continued)

(a) Financial risk factors (continued)

(iv) *Credit risk*

The carrying amounts of bank deposits and balances, receivables, available-for-sale financial assets and financial assets at fair value through profit or loss included in the consolidated balance sheet represent the Group's maximum exposure to credit risk in relation to its financial assets.

Substantially all of the Group's bank deposits and balances are held in major financial institutions, which management believes are of high credit quality. Most of the Group's available-for-sale financial assets and financial assets at fair value through profit or loss are also publicly traded in recognised stock exchanges. Management does not expect any losses from non-performance by these counterparties.

The Group has no significant concentrations of credit risk. The carrying amount of receivables included in the consolidated balance sheet represents the Group's maximum exposure to credit risk in relation to these financial assets. Ageing analysis of the Group's accounts receivable is disclosed in Note 21. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history and the Group performs periodic credit evaluations of its customers. Normally, the Group does not require collaterals from trade debtors. Management makes periodic collective assessment as well as individual assessment on the recoverability of account and other receivables based on historical payment records, the length of the overdue period, the financial strength of the debtors and whether there are any disputes with the relevant debtors. The Group's historical experience in collection of trade and other receivables falls within the recorded allowances and the directors are of the opinion that adequate provision for uncollectible receivables has been made in the financial statements.

(v) *Liquidity risk*

Prudent liquidity risk management implies maintaining sufficient cash and cash equivalents and the availability of funding through an adequate amount of committed credit facilities.

The Group's primary cash requirements have been for additions of and upgrades on property, plant and equipment, payment on related debts and payment for purchases and operating expenses. The Group finances its working capital requirements through a combination of internal resources and long-term and short-term bank borrowings.

As at 31st December 2007, the net current liabilities of the Group amounted to RMB674,404,000. Management monitors regularly the Group's current and expected liquidity requirements to ensure it maintains sufficient cash and cash equivalents and has available funding through adequate amount of committed banking facilities to meet its working capital requirements. The amount of undrawn credit facilities at the balance sheet date are disclosed in Note 33 to the financial statements. The directors believe that the Group's current operating cash flows and credit facilities from PRC banks are sufficient for financing its capital commitments in the near future and for working capital purposes.

40 FINANCIAL RISK MANAGEMENT (continued)

(a) Financial risk factors (continued)

(v) *Liquidity risk* (continued)

The table below analyses the Group's and the Company's financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

	Less than 1 year RMB'000	Between 1 and 2 years RMB'000	Between 2 and 5 years RMB'000	Over 5 years RMB'000
Group				
At 31st December 2007				
Bank and other borrowings	**5,295,282**	**337,024**	**534,143**	**299,700**
Accounts and other payables	**8,085,556**	**—**	**—**	**—**
Amounts due to ultimate holding company	**520,524**	**—**	**—**	**—**
At 31st December 2006				
Bank and other borrowings	6,147,790	105,985	515,443	251,021
Accounts and other payables	8,705,128	—	—	—
Amounts due to ultimate holding company	520,524	—	—	—
Company				
At 31st December 2007				
Other payables	**31,454**	**—**	**—**	**—**
Amounts due to ultimate holding company	**464,298**	**—**	**—**	**—**
At 31st December 2006				
Other payables	53,373	—	—	—
Amounts due to ultimate holding company	464,298	—	—	—

40 FINANCIAL RISK MANAGEMENT (continued)

(b) Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may consider the macro economic conditions, prevailing borrowing rates in the market and adequacy of cash flows generating from operations and may raise funding through capital market or bank borrowings as necessary.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings as shown in the consolidated balance sheet less cash and cash equivalents. Total capital is calculated as equity, as shown in the consolidated balance sheet, plus net debt.

During 2007, the Group's strategy, which was unchanged from 2006, was to maintain a stable gearing ratio. The gearing ratios at 31st December 2007 and at 31st December 2006 were as follows:

	Group	
	2007	2006
	RMB'000	RMB'000
Total borrowings	**6,074,160**	6,671,997
Less: Cash and cash equivalents (Note 36(e))	**(2,452,706)**	(3,155,527)
Net debt	**3,621,454**	3,516,470
Total equity	**6,658,395**	8,122,112
Total capital	**10,279,849**	11,638,582
Gearing ratio	**35%**	30%

The increase in the gearing ratio during 2007 resulted primarily from the decrease in total equity as a result of the loss for the year.

40 FINANCIAL RISK MANAGEMENT (continued)

(c) Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group is the current bid price.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. As detailed in Note 19 to the financial statements, there are no quoted market price in an active market for certain of the Group's other non-current financial assets in the PRC and for which the range of other methods of reasonably estimating fair value is significant and the probabilities of the various estimates cannot be reasonably assessed without incurring excessive costs. Accordingly, these investments are carried at cost less accumulated impairment losses.

The carrying amounts of the Group's current financial assets, including cash and cash equivalents, deposits, trade receivables, notes receivable and other receivables, and the Group's current financial liabilities, including trade and other payables and current borrowings, approximate their fair values. The fair value of non-current portion of borrowings are disclosed in Note 33 to the financial statements.

The face values less any estimated credit adjustments for financial assets and liabilities with a maturity of less than one year are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments.

41 SUBSEQUENT EVENTS

(a) Pursuant to a resolution passed in the Extraordinary General Meeting of the Company held on 31st March 2008, the Company will subscribe for certain new shares of Hongdu, an existing subsidiary of the Company whose shares are listed on the Shanghai Stock Exchange, as a result of a proposed placement of not more than 98,000,000 new shares of Hongdu to the Company, Hongdu Group and certain other independent third parties (the "Placement"). Upon completion of the Placement and subject to the approval from the relevant authorities, the Company's interest in Hongdu will be reduced to 46.09%. The Group will continue to control Hongdu subsequent to the Placement pursuant to the relevant terms and conditions of the Placement.

(b) In January 2008, the Group disposed of an aggregate 16,140,000 A shares of Changhe, representing 3.94% of its total share capital, at market price with a gain on disposal.

42 PARTICULARS OF PRINCIPAL SUBSIDIARIES, ASSOCIATES AND A JOINTLY CONTROLLED ENTITY

Name	Registered and paid up capital	Attributable equity interest	Type of legal entity	Principal activities
Subsidiaries				
Directly held				
Harbin Aviation Industry Group Co., Ltd. (哈爾濱航空工業（集團）有限責任公司)	RMB616,102	100%	Limited liability company	Manufacture and sale of general-purpose aeroplane and automobile
Jiangxi Changhe Aviation Industry Co., Ltd. (江西昌河航空工業有限公司)	RMB421,037,974	100%	Limited liability company	Manufacture and sale of general-purpose aeroplane, automobile and automobile parts and components
Jiangxi Hongdu Aviation Industry Co., Ltd. (江西洪都航空工業股份有限公司)	RMB228,768,039	55.29%	Joint stock company (listed on the Shanghai Stock Exchange)	Design, development, manufacture and sale of basic trainers, general-purpose aeroplane and other aero products, including parts and components
Harbin Dongan Auto Engine Co., Ltd. (哈爾濱東安汽車動力股份有限公司)	RMB462,080,000	58.77%	Joint stock company (listed on the Shanghai Stock Exchange)	Manufacture and sale of automobile engine
Jiangxi Changhe Automobile Co., Ltd. (江西昌河汽車股份有限公司)	RMB410,000,000	62.12%	Joint stock company (listed on the Shanghai Stock Exchange)	Design, development, manufacture and sale of mini-sized vehicles
Harbin Hafei Automobile Industry Group Co., Ltd. (哈爾濱哈飛汽車工業集團有限公司)	RMB758,035,000	100%	Joint stock company	Manufacture and sale of automobile products
Indirectly held				
Hafei Aviation Industry Co., Ltd. (哈飛航空工業股份有限公司)	RMB300,393,899	50.05%	Joint stock company (listed on the Shanghai Stock Exchange)	Research, development, design, manufacture and sale of aero products, including parts and components

42 PARTICULARS OF PRINCIPAL SUBSIDIARIES, ASSOCIATES AND A JOINTLY CONTROLLED ENTITY (continued)

Name	Registered and paid up capital	Attributable equity interest	Type of legal entity	Principal activities
Indirectly held (continued)				
Jiujiang Changhe Automobile Co., Ltd. (九江昌河汽車有限責任公司)	RMB161,250,000	72.89%	Limited liability company	Development, manufacture and sale of parts and components for mini-sized vehicles
Harbin Dongan Automotive Engine Manufacturing Co., Ltd. (哈爾濱東安汽車發動機製造有限公司)	RMB450,888,750	36.16%	Equity joint venture	Manufacture and sale of automobile engines
Hafei Motor Co., Ltd. (哈飛汽車股份有限公司)	RMB804,322,000	74.81%	Joint stock company	Manufacture and sale of automobile products
Associates				
Directly held				
Baoding Huide Wind Power Engineering Co., Ltd. (保定惠德風電工程有限公司)	RMB150,000,000	20.00%	Equity joint venture	Development, manufacture and sale of large-scale wind power generation equipments
Indirectly held				
Harbin Wanxiang Hafei Motor Chassis System Co., Ltd. (哈爾濱萬向汽車底盤系統有限公司)	RMB60,000,000	35.00%	Limited liability company	Manufacture and sales of motor chassis system
Harbin Embraer Aircraft Industry Co., Ltd. (哈爾濱安博飛機工業有限公司)	USD25,000,000	36.76%	Limited liability company	Production of regional jets and provision of relevant sales and after-sale services
Jointly controlled entity				
Indirectly held				
Jiangxi Changhe Suzuki Automobile Co., Ltd. (江西昌河鈴木汽車有限責任公司)	USD311,800,000	35.47%	Equity joint venture	Manufacture and sale of mini-sized vehicles

Notes:

(i) All the above subsidiaries, associates and the jointly controlled entity are established and operating in the PRC.

(ii) The English names of certain subsidiaries, associates and the jointly controlled entity referred to herein represent management's best effort at translating the Chinese names of these companies as no English names have been registered.

In this Annual Report, unless the context otherwise requires, the following terms shall have the meanings indicated.

"Agusta"	Agusta S. p. A.
"Articles of Association"	Articles and Association of the Company (as amended from time to time)
"A Shares"	Renminbi-denominated Domestic Shares traded on the Shanghai Stock Exchange by PRC legal persons or individuals
"A Share listed subsidiaries"	Changhe Auto, Dongan Motor, Hafei Aviation and Hongdu Aviation, whose A shares are listed on Shanghai Stock Exchange
"AVIC"	中國航空工業總公司 (Aviation Industry of China Corporation), the predecessor of China Aviation Industry Corporation I and AVIC II.
"AVIC II"	中國航空工業第二集團公司 (China Aviation Industry Corporation II), a controlling shareholder of the Company holding 61.06% equity interests of the Company
"AVIC II Group"	AVIC II and its subsidiaries and associates (excluding the Group)
"AviChina", "the Company"	中國航空科技工業股份有限公司 (AviChina Industry & Technology Company Limited), a joint stock limited company established in the PRC with limited liability on 30th April 2003
"Board" or "Board of Directors"	the board of directors of the Company
"Changhe Agusta"	江西昌河阿古斯特直升機有限責任公司 (Jiangxi Changhe-Agusta Helicopter Co., Ltd.), a sino-foreign joint venture held as to 60% by Changhe Aviation and 40% by Agusta
"Changhe Auto"	江西昌河汽車股份有限公司 (Jiangxi Changhe Automobile Co., Ltd.), a joint stock limited company whose shares are listed on the Shanghai Stock Exchange with 59.02% of its interests being directly held by the Company
"Changhe Suzuki"	江西昌河鈴木汽車有限公司 (Jiangxi Changhe Suzuki Automobile Co., Ltd.), a joint venture with 41%, 10%, 25.1%, 20.9% and 3% of its interests being held by Changhe Auto, Changhe Aviation, Suzuki, Suzuki (China) Investment Co., Ltd. and OKAYA & Co., Ltd. respectively
"Changhe Aviation"	江西昌河航空工業有限公司 (Jiangxi Changhe Aviation Industry Co., Ltd.), a wholly-owned subsidiary at the Company
"Directors"	the director(s) of the Company
"Domestic Shares"	ordinary shares of the Company, with a nominal value of RMB1.00 each, which are subscribed for or credited as fully paid in Renminbi by PRC corporate entities
"Dongan Motor"	哈爾濱東安汽車動力股份有限公司 (Harbin Dongan Auto Engine Co., Ltd.), a joint stock limited company whose shares are listed on the Shanghai Stock Exchange with 58.77% of its interests being held by the Company

"Dongan Engine"	哈爾濱東安汽車發動機製造有限公司 (Harbin Dongan Automotive Engine Manufacturing Co., Ltd.), a sino-foreign joint venture with 36% and 15% of its interests being held by Dongan Motor and Harbin Aviation Group
"economy sedan"	sedans with a total engine capacity below 1.6 litres (excluding 1.6 litres) and basic sales price below RMB100,000
"Eurocopter"	a subsidiary of European Aeronautic Defence and Space Company ("EADS")
"H Shares"	overseas listed foreign invested shares in the share capital of the Company, with a nominal value of RMB1.00 each, which are traded in Hong Kong dollars and listed on the Stock Exchange
"Hafei Auto"	哈飛汽車股份有限公司 (Hafei Motor Co., Ltd.), a joint stock limited liability company with foreign investment which is held as to 74.81% by Harbin Automobile Group, a wholly-owned subsidiary of the Company
"Hafei Aviation"	哈飛航空工業股份有限公司 (Hafei Aviation Industry Co., Ltd.), a joint stock limited company whose shares are listed on the Shanghai Stock Exchange with 50.05% of its interests being held by Harbin Aviation Group
"Harbin Automobile Group"	哈爾濱哈飛汽車工業集團有限公司 (Harbin Hafei Automobile Industry Group Co., Ltd.), a wholly-owned subsidiary of the Company
"Harbin Aviation Group"	哈爾濱航空工業(集團)有限公司 (Harbin Aviation Industry (Group) Co., Ltd.), a wholly-owned subsidiary of the Company
"Harbin Embraer"	哈爾濱安博威飛機工業有限公司 (Harbin Embraer Aircraft Industry Co., Ltd.), a joint venture established in the PRC held as to 24.5% by Harbin Aviation Group, 24.5% by Hafei Aviation and 51% by Embraer-Empresa Brasileira de Aeronautica S.A. (Embraer)
"Hefei Changhe"	合肥昌河汽車有限責任公司 (Hefei Changhe Automobile Co., Ltd.), a wholly-owned subsidiary of Changhe Auto transferred from a former branch of Changhe Auto in May 2007
"Hongdu Aviation"	江西洪都航空工業股份有限公司 (Jiangxi Hongdu Aviation Industry Co., Ltd.), a joint stock limited company whose shares are listed on the Shanghai Stock Exchange with 55.29% of its interests being held by the Company
"Hongdu Group"	江西洪都航空工業(集團)有限責任公司 (Jiangxi Hongdu Aviation Industry Group Corporation), a wholly-owned subsidiary of AVIC II
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange (as amended from time to time)
"mini-sized vehicles"	generally refers to mini-vans and mini-trucks with lengths not exceeding 3.5 metres, with engine capacity below 1.0 litre and total loading capability below 600 kilogrammes, according to "Motor Vehicles and Semi-trailer Types Terms and Definitions" (reference No.GB/T 3730-1-1998) issued by the China Association of Automobile Manufacturers. In recent years, the length of mini-sized vehicles was extended to 3.7 metres as a result of the implementation of the new anti-crash regulations

"Mitsubishi"	Mitsubishi Motor Corporation (三菱自動車工業株式會社), a substantial shareholder of Dongan Engine
"Promoters"	AVIC II, China Hua Rong Asset Management Corporation, China Cinda Asset Management Corporation and China Orient Asset Management Corporation
"Shares"	Domestic Shares and H Shares
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Supervisors"	the members of the Supervisory Committee of AviChina
"Suzuki"	Suzuki Motor Corporation (日本國鈴木株式會社), a partner to a joint venture of the Company with 25.1% equity interests in Changhe Suzuki
"the Group"	AviChina and all or any of its subsidiaries
"the PRC"	People's Republic of China
"Trainer"	aeroplanes designed and used for pilot training purposes

BOARD OF DIRECTORS

Chairman	Zhang Hongbiao
Vice Chairman	Wu Xiandong
	Tan Ruisong
Directors	Liang Zhenhe
	Song Jingang
	Tian Min
	Wang Bin
	Chen Huaiqiu
	Wang Yong
	Maurice Savart
	Guo Chongqing*
	Li Xianzong*
	Lau Chung Man, Louis*

* *Independent Non-executive Directors*

SUPERVISORY COMMITTEE

Chairman	Tang Jianguo
Supervisors	Wang Shouxin
	Li Shentian
	Bai Ping
	Han Xiaoyang
	Yu Yan
	Li Deqing
	Zheng Li
	Xie Zhihua

SENIOR MANAGEMENT

President	Wu Xiandong
Vice President	Li Hui
	Li Yao
	Liu Tao
Company Secretaries	Yan Lingxi
	Ip Kun Wan, Kiril

THE LEGAL NAME OF THE COMPANY

中國航空科技工業股份有限公司
AviChina Industry & Technology Company Limited

Abbreviation name in Chinese:	中航科工
Abbreviation name in English:	AVICHINA
Legal representative:	Zhang Hongbiao

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Unit B, 15/F, United Center, Queensway 95, Hong Kong

AUTHORISED REPRESENTATIVES

Wu Xiandong   Yan Lingxi

PRINCIPAL BANKERS

Industrial and Commercial Bank of China
No.55 Fuxingmen nei Street, Xicheng District,
Beijing, the PRC

Bank of China
No.1 Fuxingmen nei Street, Xicheng District,
Beijing, the PRC

China Construction Bank
No.25, Finance Street, Xicheng District,
Beijing, the PRC

Shanghai Pudong Development Bank Ltd.
No.500, Pudong South Road, Pudong New District,
Shanghai

PLACE OF LISTING, STOCK NAME AND STOCK CODE

Main Board of The Stock Exchange of Hong Kong Limited
(H Shares), AVICHINA, 2357

REGISTERED ADDRESS

No.16, Hong Da Bei Lu, Beijing Economic-Technological
Development Area, Beijing, the PRC

WEBSITE

www.avichina.com

CORRESPONDENCE ADDRESS

Postal Code: 100009
P.O. Box 1655, Beijing, the PRC

Telephone: 86-10-64094832
Facsimile: 86-10-64094826/36
E-mail Box: avichina@avichina.com

SHARE REGISTRAR

Computershare Hong Kong Investor Services Limited
Room 1712-1716, 17th Floor, Hopewell Centre,
183 Queen's Road East, Hong Kong

ANNUAL GENERAL MEETING

The annual general meeting of the Company for the year 2007 will be held on Friday, 13th June 2008 at 9:00 a.m. at Beijing Jinjiang Fuyuan Hotel, No. 11 Ronghua Road, Beijing Economic & Technological Development Area, Beijing, the People's Republic of China. As to the procedures for demanding a poll, the existing Articles of Association provide that:

Subject to the rules prescribed by the Stock Exchange or any relevant stock exchanges (as amended from time to time), at any shareholders' general meeting a resolution shall be decided on a show of hands unless a poll is (before or after any vote by show of hands) demanded by:

i) the chairman of the meeting;

ii) at least two shareholders or proxies entitled to vote; or

iii) one or more shareholders (including proxy of shareholder) alone or jointly representing 10 percent or more (inclusive) of all Shares carrying the right to vote at such meeting.

Unless a poll is demanded, the chairman's declaration of the results of the voting by show of hands and the record of the same in the minutes of the meeting shall be conclusive evidence of the results of voting. There is no need to provide evidence as to the number of votes for and against the resolution or the proportion of votes for and against in respect thereof:

The request for voting by poll can be withdrawn by the person proposing the same.

AUDITORS

International Auditors
PricewaterhouseCoopers
22nd Floor, Prince's Building
Central, Hong Kong

Auditors in the PRC
PricewaterhouseCoopers Zhong Tian CPAs Limited Company
11/F, PricewaterhouseCoopers Center,
No. 202 Hu Bin Road,
Shanghai 200021, the PRC

LEGAL ADVISERS

As to Hong Kong law
Baker & McKenzie
14th Floor, Hutchison House,
10 Harcourt Road, Central,
Hong Kong

As to PRC law
Beijing Jiayuan Law Firm
F407, Ocean Plaza,
158 Fuxingmennei Street,
Xicheng District,
Beijing, the PRC