

## Chairman's Statement

I am pleased to present to shareholders the annual report of Cosmos Machinery Enterprises Limited (the "Company") and its subsidiaries (the "Group") for the year ended 31st December, 2006.

### RESULTS

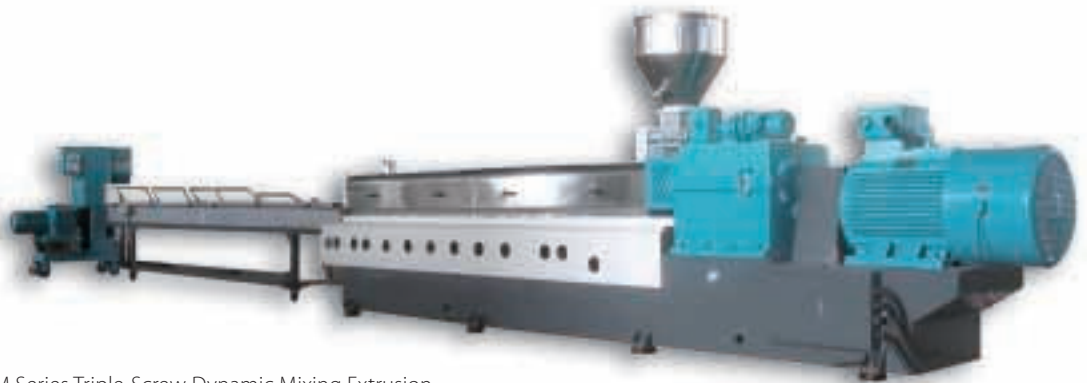
The Group's consolidated turnover for the year 2006 was in the region of approximately HK\$2,022,632,000, representing an increase of about 23% over the approximate figure of HK\$1,650,729,000 for 2005. Our profit after taxation stood at about HK\$88,616,000, or some 21% higher than the approximate figure of HK\$73,102,000 for the previous year. For the year ended 31st December, 2006, the profit attributable to shareholders was about HK\$65,143,000, increasing by 20% when compared with last year.

### CHAIRMAN'S STATEMENT

Driven by the Eleventh Five-Year Plan of China, high-performance, hi-tech and professional products in China's domestic market have attracted much attention during the year under review. In open overseas markets with keen competition, better quality products with a higher performance-price ratio are having more room for expansion. Despite of such a booming market environment, the consistently high raw material prices and pressure for wage increase on the Mainland remain as challenges to all businesses to different extents.

The Group's business strategy is always to, based on a suitable production scale, give emphasis on resources for technology research and development capability, as well as introduce high quality, hi-tech products to meet the changes in market demand, so as to counterbalance the pressure for higher costs, free itself from the unregulated price competition, and strive for better returns in the fields of technology and service provision.

During the period, the high-performance, professional plastic injection moulding machine series in the machinery manufacturing business recorded satisfactory sales. The growth in sales of other new products, such as rubber injection machines and CNC sheet-metal working machines, was also remarkable, making them the new impetus for growth in sales and gains of the business.



TDM Series Triple-Screw Dynamic Mixing Extrusion

## Chairman's Statement

As quality control was improved, injection moulding products and the processing business recorded desirable results during the period. The business expanded into markets with more stringent requirements and developed a series of new products with innovative injection moulding technology, which have received positive feedback from existing and new customers and driven the business toward a new milestone.

In the past year, the printed circuit board processing business underwent improvement in its production process. It also deployed new, state-of-the-art equipment for higher competency in markets that emphasizes quality products. With optimisation measures implemented on various aspects, the results for the period were again record-breaking and drove the business even further.

As for the trading business, the Group continued to consolidate its foundation on a customer market stressing quality and performance, and achieved satisfactory results.

To encounter challenges in a complex, rigid environment, it is essential that the Group gather resources for its core businesses. After careful analysis and consideration, last year the Group's management decided to sell out the audio and electronic products business, which consistently incurred losses in recent years, so as to prevent its impact on our overall earnings performance.

The Group's established development policy was also deployed last year. With a strong foundation on collaboration and through active and practical discussions, the Group signed an agreement with South China University of Technology, Guangdong Province, on 14th December, 2006 for the establishment of a strategic partnership for closer co-operation on three aspects, namely "manufacture, learning and research". On 23rd March this year, a contract was signed between the Group and UBE Machinery (Shanghai) Ltd., a subsidiary of Japan UBE Machinery Corporation Ltd. in Shanghai for the set-up of a joint venture for producing UBE ST and PZIII plastic injection moulding machines series. It is anticipated that the joint venture, named 無錫宇部大同機械有限公司 (Wuxi UBE Cosmos Machinery Ltd.), will commence its operations in May this year. At the same time, the Group co-operated with REP International S.A. in February this year on the development of high-performance rubber injection machines. Such collaboration with the above companies has enabled the Group to establish a strategic platform for technology development and human resources investment, thus fortifying the Group's operating conditions for technology research and development, talents training, blending of the best people, further expansion into overseas and local markets, management enhancement, and so on. We believe that all businesses will be able to benefit from synergy within the Group.



RC-750Y High Speed Injection Moulding Machine

## Chairman's Statement

Looking forward to the coming year, the political environment in the PRC will remain stable and political and economic reforms dense and meticulous, accompanied by the ongoing implementation of new policies and greater incentives for innovative technologies. Meanwhile, driven by internal demands, the market is believed to continue to boom and flourish. Nevertheless, the persistently high raw material prices, the gradual increase in labour wage on the Mainland, as well as the impact of other market changes triggered by concerns over the emerging uncertainties in the US market, are presenting huge challenges to the Group's ability to cope with changes. Despite the above, in view of our pragmatic operational strategy, adequate deployment of human resources, and devotion to technology research and development, we believe that our management can be enhanced, more advanced products with higher performance/price ratios produced, as well as better quality services offered to meet the market demands for products and services.

In the coming year, we will implement and consolidate our strategic co-operation project which was established in the previous year. Under the synergy effect, it is expected that the Group's results will achieve even higher returns for our shareholders and stakeholders.

On behalf of the Group, I would like to extend my deepest gratitude to all staff members for their devoted efforts. I would also like to express my acknowledgement of their improved performance, and am looking forward to even better achievements in the coming year.

### TANG To

*Chairman*

Hong Kong, 24th April 2007



CNC Brake Press

# Management Discussion and Analysis

## BUSINESS REVIEW

### Manufacturing Business

#### Machinery

Although affected by the continued macro-economic control policy on the Mainland and oversupply of general purpose plastic injection moulding machines in 2006, the Group benefited from such favourable factors as the continually stable, booming economy on the Mainland and the increasing overseas demand for domestic equipment, with turnover rising by 19% as compared to that of last year to reach approximately HK\$685,684,000, which amounted to 34% of the Group's consolidated turnover. During the year, like other manufacturers who have established facilities in China, the Group's machinery business was consistently impacted by such unfavourable factors as the increase in minimum wage and surge in the cost of raw materials, which together resulted in a higher cost of production. In addition, the release and sale of a series of new machinery equipment in the year, whose operational cost was relatively high at the initial stage of development, offset part of the profit. In spite of that, the operating profit for the year was approximately HK\$33,134,000, up by 14% as compared to that of the previous financial year.

The overall turnover improved during the year under review. This was attributable to the upward trend of the economy on the Mainland, a stronger intention of customers to invest in plastic and rubber machineries, and the Group's strategic control of its core injection moulding machine product portfolio, which

together resulted in an increase in overall sales. Sales of general purpose plastic injection moulding machines were comparable to last year, with high performance and export-oriented plastic injection moulding machines being the main source of sales growth.



ST3150 Injection Moulding Machine



Double Conical Twin-Screw Extruder

## Management Discussion and Analysis

The consistent optimisation of the multi-product and multi-region production operation mode further consolidated the development trend of product individualization. In terms of new products, sales of CNC sheet-metal working machines, rubber injection machines and plastic pipe extrusion lines recorded a healthy growth of 80% as compared to that of last year. On 14th December, 2006, the Group signed a strategic alliance agreement with South China University of Technology, a research partner for years, to fully collaborate on research development and talent training; to strengthen the optimal design of machinery, mould design and analysis, alongside new product research and development; whilst in line with talent training on plastic processing, control engineering as well as machine manufacturing.

As for prospects in 2007, in view of the stable political and economic environments on the Mainland, and emphasis has been put on industrial transformation, particularly on technology improvement in the Eleventh Five-Year Plan of China, it is anticipated that the growth in investments and domestic demand will continue, together with a higher gross demand for high performance plastic processing machinery. As China has become the third largest automobile producer and distributor, a relatively higher growth in demand for large-scale, high performance plastic injection moulding machines is expected from certain industries, for example, the auto-parts industry. This year the Group will further collaborate with world renowned rubber and plastics machinery plants, including the set-up of a joint venture with UBE Machinery (Shanghai) Ltd. in the first half of 2007 for producing and distributing high-end plastic injection moulding machines, as well as co-operating with REP International S. A. in the production of high-end rubber injection machines on the Mainland. In terms of export business, with the Group's adamant efforts in establishing foundation for sustainable development, together with the increasing recognition of domestic machinery by overseas customers, it is anticipated that the rapid growth of sales from export-oriented plastic injection moulding machines will continue. To complement the change in product portfolio as mentioned above, last year the Group integrated the production bases in South China and East China, producing synergy in the use of resources for both regions. At the same time, the sales system on the Mainland was adjusted and strengthened to meet market needs. In conclusion, with the launched products entering the growth stage and overseas markets the maturity stage, the Group remains cautiously optimistic about the sales of and growth in the machine manufacturing business.



Electric Punch



Plastic Food Containers

### Plastic Products and Processing

During the year under review, sales of the Group's plastic products and processing business steadily rose by approximately 22% as compared to that of the previous year to reach HK\$425,166,000, accounting for 21% of the Group's turnover. Operating profit for the year was approximately HK\$28,590,000, up by 29% when compared to that of last year and making positive contributions to the Group.

## Management Discussion and Analysis

The production cost of the plastic processing plant in Dongguan for the year under review continued to increase due to soaring prices of plastics, diesel and metalware, and the increase in labour wage. Fortunately, the desirable growth in sales for the year, which produced economies of scale, and the substantial efforts by the employees, together with optimised management, helped to reduce wastage and facilitate cost control for reasonable returns. The growth in turnover was mainly attributable to the increase in orders from core customers as well as the establishment of new customers.

The plant in Zhuhai, which specializes in plastic injection products such as professional sanitary plastic tableware and food packaging, was impaired by a lower negotiating power with customers and providers for the year under review. This was caused by the increase in oil and plastics prices, minimum wage in China and other operational costs, as well as the unregulated competition in the local plastic products market. As a result, operating profit of the business dropped and the results turned out not so satisfactory. In the coming year the Group will focus on producing manufacturing products with higher marginal profit, reducing costs and enhancing the efficiency in production and processing processes. Apart from the food industry, the Group will also expand its customer base whose sanitary demands are stringent, as an initiative to improve the performance of the plant.

The optic products business also encountered a severe problem of operational cost increase for the year under review. Despite that, the business adopted several measures to meet the challenges in the market: in terms of marketing and sales, increasing promotional channels for direct sales, e-commerce and exhibitions; in terms of products development, fully improving product design and diversifying product portfolio; and, in terms of management, improving production processes and reducing production costs. With such measures, the business yielded growth in both turnover and profit.



4" dia Illuminated Magnifier 2x 4x

### Audio and Electronic Products

The audio and electronic products business has incurred losses for years. In view of the current economic environment, the Group decided to sell out the business so as to cease further losses and to transform resources to other core businesses. On 31st December, 2006, the Group sold out the business for HK\$3. As at 31st December, 2006, the total loss of the business, including the related expenses involved in the write down of asset value to net realizable value and redundancy, was HK\$7,943,000.