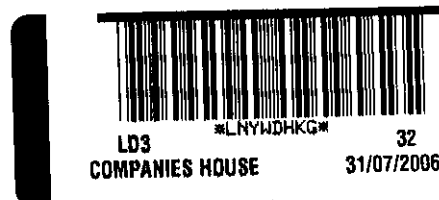


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the leading Chinese producer of lead acid batteries

China Shoto plc

2005 Annual Report



directors, secretary and advisers

→ Directors	→ Registered Number	→ Registrars
Cao Guifa (Chairman)	05448599	Capita Registrars
Yang Shanji (Chief Executive)		The Registry
Zhou Yuezhong (Finance Director)	→ Auditors	34 Beckenham Road
Zhu Shiping (Executive Director)	BDO Stoy Hayward LLP	Beckenham
Wang Zhaobin (Executive Director)	Northside House	Kent BR3 4TU
Bernard Asher (Non-executive Director)	69 Tweedy Road	
Li Shuang (Non-executive Director)	Bromley	→ Solicitors
David Thomas (Non-executive Director)	Kent BR1 3WA	Richards Butler
		Beaufort House
→ Company Secretary	→ Nominated Adviser and Broker	15 St Botolph Street
David Thomas	Seymour Pierce Limited	London EC3A 7EE
	Bucklersbury House	
→ Registered Office	3 Queen Victoria Street	
Beaufort House	London EC4N 8EL	
15 St Botolph Street		
London EC3A 7EE		

highlights

- Turnover increased by 52% to £28.4 million (2004: £18.7 million)
- Net profit, before share based payment expenses of £0.2 million, has more than doubled to £3.3 million (2004: £1.5 million)
- Basic earnings per share increased by 102% to 19.80 pence (2004: 9.79 pence)
- Trading ahead of expectations
- Acquired controlling stake in Beijing Full Three Dimension Co., Ltd after the year-end
- Employee health and safety management certificate awarded to the Group
- Granted "Environment Friendly Enterprise" title by Jiangsu provincial government
- Average time taken by customers to pay fell from 124 days in Q4 2004 to 93 days in Q4 2005
- Joined AIM December 2005

Our business

China Shoto is a leading Chinese producer of lead acid batteries. The Company has a significant market share in back up batteries for the telecommunications industry in China, and has targeted future expansion in the fast growing Chinese electric bicycle market. The Group also operates a turbine design and consultancy business through holding a 51% stake in Beijing Full Three Dimensional Power Engineering Co. Ltd. ("FTD") (increased to 51% from 30% in January 2006). FTD helps to address the ever increasing demand for electricity in China.

Objectives

China Shoto intends to become:

- the largest lead acid battery producer in Asia.
- a recognised environmentally friendly energy solution provider.
- a significant turbine technology service company in Asia.

Batteries

Product Portfolio

- AGM VRLA battery AGM
- GEL VRLA battery
- Flooded Lead Acid Battery
- Power Type VRLA Battery

Manufacturing

- factories are located 2 hours by highway from Shanghai allowing for access to convenient transportation networks
- substantial modern manufacturing facilities with six production lines, current production capacity of 800,000 units per year (before the opening of our new factory)
- products manufactured to international standards, export licenses and international certificates obtained to allow for overseas sales

Research and development

Our research and development center in Nanjing is involved in the development of new products and technologies, and is constantly seeking to upgrade our existing products

Markets & Sales

Our market sectors

Telecommunications, power generation and transmission, electric bicycle, railway and shipping, solar and wind energy storage

Our main clients

China Mobile, China Telecom, China Tietong, China Unicom, China Netcom, ZTE

Our sales, and our service and support network

30 sales and service offices across China, 141 sales and service staff, quality after-sales service
Exports more than doubled in 2005 compared to 2004

International Sales

Export levels increased by more than 100% from 2004-2005



Our main clients

Our turbine business

Our services

We are involved in both the reconstruction of old turbines under 200MW, and the design and development of a new generation 150MW turbine

Research and Development

- We have developed the turbine FTD design system, with three patents registered and one patent in application
- We employ 30 R&D staff, and our R&D is supported by the China Academy of Sciences
- We are involved in the R&D for China's National 863 Gas Turbine Project

Our strategy is to focus on growth segments in our core markets. By positioning China Shoto as an environmentally friendly energy solution provider, we are well placed to take advantage of the opportunities of strongly growing markets.

Flotation

2005 has been a successful year for China Shoto. The Group raised £6.0 million before expenses and its shares were admitted to trading on AIM on 6 December 2005. The Group has used some of the funds raised to build a new battery manufacturing plant which will significantly expand the production capacity of power type Valve Regulated Lead Acid ("VRLA") batteries.

Results and Dividend

The annual results are a head of expectations. Turnover for the year increased by 52% to £28.4 million (2004: £18.7 million). Operating profit increased by 90% to £4.4 million (2004: £2.3 million). Basic earnings per share increased by 102 % to 19.80 pence (2004 9.79 pence)

The Directors do not recommend the payment of a final dividend for 2005.

Cao Guifu
Chairman

Business Progress

Strong organic growth in the existing business reinforces our leading position in the industry. Operating results are ahead of previous years, as a result of high sales and of continuing efficiencies with regard to cost controls. Sales to China Mobile, the largest telecom service provider in China, and to ZTE Corporation ("ZTE"), one of the largest telecom equipment manufacturers in China, increased by 142% and 234% respectively over the last 12 months. Gross profit margin increased by over 4%.

The production of power type VRLA batteries used in electric bicycles is regarded as a key business for the Company in the future. Pursuant to the flotation, £3.2 million of the funds raised are being used to establish a power type VRLA battery facility within a newly built 28,000 sq. metre plant. With the new facility the Company's production capacity will be more than doubled. The use of the electric bicycle in China is showing rapid expansion, and this market is set to be a key growth and profit opportunity for the Group. In addition, the overall increase in the Company's production capacity will enable it to meet increased demand for its products which will in turn enhance its brand.

In the first half of the year the Company acquired a 30% stake in the Beijing Full Three Dimension Power Engineering Co, Ltd ("FTD") and in early 2006, completed the purchase of an additional 21%, to take its holding in FTD to 51%.

FTD is a leading turbine design and refurbishment technology service provider based in Beijing, specialising in the reconstruction of ageing turbines and the development of new turbines. For the year ending 31 December 2005, FTD's turnover and net profit were £11.5 million and £0.6 million respectively. The Board believes that with FTD as a subsidiary, the Company has a wider range of cost-effective and environmentally friendly solutions for efficient energy generation.

Global telecommunication expansion offers considerable opportunities to the Company. China Shoto is confident of the strength of its products which have already successfully challenged foreign suppliers in the Chinese domestic market. Furthermore, the Group continues to establish an international distribution network.

Social Responsibilities

The Company is committed to operating to the highest ethical standards. We are dedicated to offering our customers quality products and excellent services. China Shoto will continue to strive towards best practice standards consistent with profitability, and at the same time will seek to deliver attractive shareholder returns. The Company offers employees career development opportunities and is supportive of their family life and goals outside work.


Environmental Standards

China Shoto was the first Chinese company in the industry to receive certification to ISO14001, the international standard of Environment Management Systems. In November 2005 the Company was certified to GB/T28001 for vocation, health and safety management systems. In December 2005, the Company was awarded the title of "Environment Friendly Enterprise" by the Jiangsu environment protection bureau, which marks the government's approval of the Group's efforts.

Outlook

We believe that our expanded and improved range of products and sharply increasing output underpin the prospects for a successful 2006, and that the Company will continue to deliver impressive results and create significant long term value for shareholders. It is the Board's intention to initiate payment of dividends, commencing with an interim and final dividend for the year ending 31 December 2006. The aggregate dividend payable for the year 2006 is expected to be in the range of 25% to 30% of net earnings.

We believe that, building on the strong foundations that have been established, the Company is well positioned to achieve further substantial growth. We look forward to the future with confidence and enthusiasm.



Cao Guifa
Chairman

I am delighted to report China Shoto's results for 2005. In December 2005 we raised £6.0 million (before expenses) to enable China Shoto to undertake a significant expansion of its production facilities. This is now underway.

Market Overview

Market Sectors

In 2005, the telecommunications sector continued to be the main focus for the Group. Sales of batteries to domestic telecom service providers and system equipment manufacturers made up 68% of total sales. Sales to China Mobile and China Netcom increased by 142% and 117% respectively. Sales to ZTE, a systems equipment manufacturer, continued to grow substantially by 234%.

The Group continues to supply start-up batteries to the locomotive industry, and back-up batteries for both the power plant and broadcasting markets. In 2005, the Chinese domestic highway system started to use gel batteries which are used for backup battery power in highway speed detecting equipment. For example, China Shoto now provides 60% of gel batteries being used in a pilot project in Henan province in central China.

International

→ AGM Batteries

The 12V front-access battery which is used in the telecommunications and power industries is exported to Russia and Italy.

Yang Shanji
Chief Executive

→ Gel and flooded batteries
80% of the total exports of gel and flooded batteries are distributed to the European, American and Russian markets. These products are largely distributed through agents. 60% of the total sales of flooded batteries are to Europe and to the USA. The Company has set up an office in Malaysia which is responsible for sales and distribution to South-East Asia and as a result China Shoto's gel battery is now being tested by a key Malaysian telecom service provider. The Company has established a sales and distribution network in Thailand and Indonesia.

Key Customers

→ AGM batteries

China Shoto won two major national tenders issued by China Mobile to provide back-up batteries. In addition to this achievement the Company also won an 80% share in China Unicom's 'Headquarters' project which aims to extend telecom coverage to every village in four provinces in China. Furthermore, China Shoto was also a key supplier of 2V and 12V AGM batteries for ZTE, and accounts for over 90% of ZTE's total back-up battery purchases.

→ Gel and flooded batteries

China Shoto's gel and flooded batteries are now used by China Mobile in their central exchange stations and in China Telecom's localised mobile telephone network, marketed as the "Personal Handphone System". The Company is also the main supplier of gel batteries to ZTE.

Sales and marketing

→ Sales network

China Unicom, China Mobile, China Telecom and China Netcom are moving towards centralising nationally their procurement procedures. Accordingly, China Shoto has formed four dedicated customer account teams to service these customers. In addition, China Shoto has 30 national sales offices which work in conjunction with these account teams to service the Group's customers throughout China.

→ Power type batteries

In the second half of 2005, the Company further developed its strategy for the large scale production and sale of power-type batteries. This included setting up sales and service networks in Tianjin and in Zhejiang and Jiangsu provinces, key areas for the manufacture of electric bicycles.

→ Technical exchange, training and seminars

The Group has further strengthened its reputation as a leading brand in China through attending industry seminars and by providing technical training to our customers. In June 2005, the Group was invited to attend the "3rd China Telecom Power Supply Seminar" held by the Ministry of Information Industry, which provided exposure to major domestic and international telecom service providers.

Operating Overview

AGM batteries

AGM batteries continue to be the highest contributors to the Group's turnover and gross profit.

→ Manufacturing

The acceptance rate on the first testing of products reached 99.5%, achieved through controlled monitoring of the manufacturing process and detailed checks and procedures at the end of the manufacturing cycle. Production capacity has also increased through the use of new equipment and the recruitment of additional labour.

→ Technical advances

2005 saw the addition of five new battery designs to the product range. Changes to the manufacturing process for these batteries are expected to create a reduction in production costs of around 10%.

→ Logistics management

The Group continues to implement measures to reduce transportation costs, for example, by introducing competitive tendering and reducing single journey transportation.

Gel and flooded batteries

Sales of gel and flooded batteries have continued to increase.

→ Localised sourcing of material

The Group has reduced purchase costs by localising the sourcing of parts and components of eleven types of gel batteries and eight types of flooded batteries.

→ Exports

Rising international demand in the UPS market provides the opportunity for China Shoto to increase the export of 12V and 6V flooded batteries.

→ Quality Control

China Shoto manufactures batteries according to German DIN standards and has the highest quality control using advanced manufacturing equipment and production procedures. The acceptance rate on the first testing of products reached 99.8%.

Research and development

The Group continues to place considerable emphasis on remaining at the forefront of technological innovation. The Company holds over 80 patents, 18 of which were granted during the course of 2005. These patents cover the Group's existing technologies and research projects in such fields as supercapacitors, lithium ion batteries and direct methanol fuel cells.

In addition a 2V/2.5Ah spiral wound battery has also been successfully developed. This project passed our stringent appraisal system for efficient manufacture in December 2005. We have now started pilot production. These batteries are used in, inter alia, medical instruments, sports equipment and traffic management applications.

China Shoto successfully designed several new models extending the power type VRLA battery range: 12V7AH, 12V14AH, 12V16AH and 12V20AH.

Beijing Full Three Dimension Co., Ltd ("FTD")

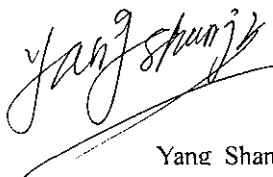
As previously announced the Group now has a controlling stake in FTD, after increasing its shareholding from 30% to 51%. In 2005 sales generated by FTD were £11.5 million and its net profit was £0.6 million.

FTD has continued the successful introduction of its 150 MW turbine. Four have been delivered of which two are installed and in operation. In 2005 orders were taken for the refurbishment of two turbines; one has already been refurbished and is operating, the other one will be completed in the first half of 2006.

FTD was awarded certificate ISO-9001, which is the international standard of quality management systems, in 2005.

Prospects

China Shoto has established a strong reputation as a provider of high quality products and services in its markets. The Group has clearly demonstrated its ability to grow in the domestic market and is now developing its strategy for overseas expansion. The Company views the future with optimism.



Yang Shanji
Chief Executive
8 May 2006

Finance director's review

Results

- Group sales have increased by 52% to £28.41 million (2004: £18.69 million).
- The operating profit of the Group is £4.56 million*, an increase of 96% (2004: £2.32 million).
- The pre-tax profit of the Group is £3.77 million*, an increase of 112% (2004: £1.78 million).
- The net profit of the Group is £3.25 million*, an increase of 116% (2004: £1.51 million).

* These figures are stated before share based payment expenses of £145,000 pursuant to IFRS 2

Taxation

China Shoto's subsidiaries were subject to different tax treatments in 2005 based on the enterprise, technology and location rules.

- Shuangdeng Group Co., Limited
Since it was incorporated as a foreign enterprise on 10 May 2005 the Company has been entitled to exemptions from PRC income tax for the first two years (2005 to 2006) and it is entitled to a 50% relief from PRC income tax for another three years thereafter (2007 to 2009).
- Longyuan Shuangdeng Power Supply
Located in an area designated as an Economic Development Coastal Region in accordance with PRC tax regulations, the Company is entitled to an applicable tax rate of 24%. Meanwhile as a industry enterprise with foreign investment it is entitled to a 50% relief from PRC income tax in 2005.
- Fuste Power Supply
Located in an area designated as an Economic Development Coastal Region in accordance with PRC tax regulations and is entitled to an applicable tax rate of 24%; meanwhile as a industry enterprise with foreign investment enterprises it was entitled to exemptions from PRC income tax for the year of 2005.
- Shuangdeng Power Supply
The company is recognised as a "technology and knowledge concentrated enterprise" and has been and continues to be entitled to a 15% PRC income tax rate.
- Nanjing R&D
In 2005 the Nanjing operations were reregistered as both a foreign investment enterprise and a industry enterprise located in a development zone in accordance with the PRC income tax legislation; therefore it is entitled to exemptions from PRC income tax for the two years commencing from their first profit-making year of operation and thereafter FTD benefits from a reduced rate of corporate of 15% on net profits because of its status as a high tech business.

Zhou Yuezhang
Finance Director

Earnings and Dividends

Basic earnings per share in 2005 are 19.80 pence. The Directors do not recommend the payment of a final dividend for 2005.

Acquisition

The Group purchased a 30% stake in FTD during the year at cost of £425,000. In January 2006 the Group purchased a further 21% stake in FTD at cost of £260,000.

FTD's turnover for the year ended 31 December 2005 was £11.5 million and its net profit was £0.6 million.

Equity shareholders' funds

Shareholders' funds have increased to £16.1 million (2004: £7.5 million). The retained earnings were £3.8 million (2004: £1.7 million).

Cash Flow

The Group has achieved significant improvement in its cash flow from operating activities from negative £833,000 in 2004 to positive £3,185,000 in 2005. Debt management improved significantly in 2005. Effective control over raw materials, production in progress and finished products improved inventory turnover to 5 times (2004: 3 times).

Interest paid was £864,000 (2004: £587,000) and tax payments were £496,000 (2004: £337,000).

Debtor days

Average debtor days in the fourth quarter of 2005 were 93 days compared to 124 days for the same period of 2004.

Borrowing

The Group entered into credit agreements with Bank of China, China Construction Bank, Agricultural Bank of China and Shenzhen Development Bank.

At 31 December 2005, the Group had outstanding bank loans of £12.1 million (2004: £10.0 million)

Currency risks

The Group has limited exposure to currency risk. Raw materials are purchased in Chinese Renminbi ("RMB") and export sales are currently relatively small. In developing an international market, the Group will need to take account of the negative effect of any appreciation of the RMB.

Interest rate risks

The interest rate risk is the fluctuation of interest rates both at the present time and in the future. The interest rates payable under the Group's bank facilities are generally variable with the fluctuation of the Central Bank's base interest rate. Changes in this rate have been modest. For certain bank borrowing arrangements, the interest rate is fixed.



Zhou Yuezhong
Finance Director
8 May 2006

board of directors

Zhou Yuezhang

Cao Guifa

Bernard Asher

Zhu Shiping

Cao Guifa

Executive Chairman (aged 52)

Cao Guifa became the chairman of the former holding company of what is now the China Shoto group in 2002 and he is a substantial shareholder of the Group. From 1979 to 1993 he served as a research fellow and then doctoral supervisor in the Chinese Academy of Sciences ("CAS"), which is a leading Chinese academic institution and comprehensive research and development centre for science and technology. Between 1988 and 1995 Mr Cao held several positions as a local consultant to the World Bank on development projects in China. He has more than 10 years of investment banking experience gained at a subsidiary of CAS, where he was general manager.

Yang Shanji

Chief Executive (aged 53)

Yang Shanji became the general manager of JS Power in 1995 before becoming the general manager of the former holding company of what is now the China Shoto group in 2002. He is a substantial shareholder of the Group. He first became involved in the rechargeable battery industry in 1990 and he has more than 25 years of management experience, in a number of manufacturing enterprises. He also has a master's degree in administration.

Bernard Asher

Non-executive Director (aged 70)

Bernard Asher, who resides in London, was an Executive Director of HSBC Holdings from 1986 to 1998 and Chairman of HSBC Investment Bank. In 1998 Bernard became Non-executive Vice Chairman of Legal & General Group, Chairman of Lonrho Africa, and a Non-executive director of Morgan Sindall, IMH (formerly Seymour Pierce Group plc) and TIR Capital Protection Fund. Mr. Asher is the chairman of Liontrust, a UK based equity investment fund.

Zhou Yuezhang

Finance Director (aged 48)

From 1990 to 1995 Zhou Yuezhang was the factory deputy director of the Jiangyan Sealed Storage Battery Factory. Mr. Zhou is also one of the founders of the Shuangdeng Group. He joined JS Power as deputy general manager in 1995 when it was set up. He has been the deputy general manager of the Shuangdeng Group since September 2002 when the Shuangdeng Group formally came into existence. Mr. Zhou has nearly 15 years of management experience in the storage battery industry. Mr. Zhou holds a master degree.

Wang Zhaobin

Executive Director (aged 43)

Wang Zhaobin is a graduate of Suzhou University. He served as a civil servant from 1989 to 2003. In September 2003 Mr. Wang joined the group, and has been appointed as deputy general manager since March 2004.

Yang Shanji

Wang Zhaobin

Li Shuang

David Thomas

Zhu Shiping

Executive Director (aged 65)

Zhu Shiping is a graduate of Anhui University and has been a senior engineer since 1989. From 1963 to 1987, Mr. Zhu worked in the fourteenth research institute of the government's former Electronic Department. Having worked for Shenzhen Huada Power Supply Co., Ltd. from 1987 to 1993, Mr Zhu became the chief engineer of the Jiangyan Sealed Storage Battery Factory. He has served as deputy general manager of JS Power and Shuangdeng Group and as a director of Shuangdeng Group since September 2003.

Li Shuang

Non-executive Director (aged 62)

Li Shuang is a professor in the Central University of Finance and Economics. Professor Li was appointed as the deputy secretary-general of the Chinese Institute of Certified Public Accountants (CICPA) from 1999 to 2002, and then an advisor to CICPA from 2002-2004. Now he is the director and member of Academic Committee of Accounting Society of China (ASC), and China Audit Society, and director of CICPA. He is also an independent non-executive director of three companies listed in China.

David Thomas

Non-executive Director (aged 52)

Mr. Thomas, who resides in London, has a degree in Law from Oxford University. He is an English solicitor and has more than 20 years working experience in the fields of international enterprise financing, law, and quoted companies. Between 1985 and 2000, he was a partner in several major law firms specialising in corporate finance and finance law. Between 2000 and 2002 he was involved in the management of a London investment bank, and was also involved in the financing of enterprises whilst with the bank. Mr. Thomas is also an independent non-executive director of three other public companies whose shares are traded on AIM and whose businesses are based in China.

directors' report

The Directors have pleasure in submitting the first annual report and financial statements of China Shoto plc, for the year ended 31 December 2005.

→ Principal Activities

The principal activity of the Company is acting as a holding company. The principal activities of the Group are the design, development, manufacture and sale of industrial lead acid batteries, and the operation of a turbine design and consultancy business.

→ Business Review

The Group has performed satisfactorily during the year and the trading performance is in line with the directors' expectations. The directors expect the Group's activity levels to be sustained through the foreseeable future. A detailed review of the Group's performance, financial results and future development are contained within the chairman's statement, chief executive's review and finance director's review.

→ Proposed Dividend

The directors do not recommend the payment of a final dividend in respect of the year ended 31 December 2005.

→ Substantial Shareholders

As at 27 April 2006 the Company has been notified of no beneficial interests, other than those of the directors, in 3% or more of the issued capital of the company.

→ Directors and Directors' Interests

The names of the current directors, along with their brief biographical details are given on pages 12 and 13.

The interests of the directors in the shares of the Company were as follows:

Name	Date of appointment		31 December 2005	
	Number of Ordinary Shares	Percentage of issued share capital	Number of Ordinary Shares	Percentage of issued share capital
Cao Guifa	1,107,693	7.2%	1,107,693	5.5%
Yang Shanji	10,984,614	71.4%	10,984,614	54.9%
Zhou Yuezhang	523,077	3.4%	523,077	2.6%
Zhu Shiping	523,077	3.4%	523,077	2.6%
Wang Zhaobin	-	-	-	-
David Thomas	-	-	-	-
Li Shuang	-	-	-	-
Bernard Asher	-	-	-	-

All the directors above (other than David Thomas and Li Shuang) were appointed on 3 October 2005. David Thomas and Li Shuang were appointed on 6 December 2005.

RB Directors One Limited was appointed as a director on 10 May 2005 (the date of incorporation) and resigned on 3 October 2005.

All directors' interests in shares are beneficially held. There has been no change in the interests set out above since the balance sheet date to one month before the notice of AGM.

Options over the Company's ordinary shares granted to directors are disclosed in the Remuneration Report on page 18.

→ Employee policy

The motivation and commitment of our people is extremely important to the Group's performance. The Group's policy is that training, career development and promotion opportunities will be available to all employees.

The Group is committed to being an equal opportunities employer regardless of gender, age, religious and other forms of discrimination. Personnel are selected on the basis of merit and capability.

→ Environmental policy

As an environment friendly energy supplier, the Group always takes account of environmental protection when formulating and implementing its business strategy. This concern manifests itself, for instance, in the construction of our new manufacturing facility, the purchase of equipment and materials, recycling, and reducing our waste emissions. The Group has also invested in improvements to the environment surrounding its facilities, and improvements in local transportation.

The Group is the first company in the industry in China certified by ISO14001 in the year 2000, and was also awarded GB/T18001 vocational health and safety management system in November 2005. In December 2005, the Group was awarded the title of "Environment Friendly Enterprise" by the Jiangsu environment protection bureau, which marks the approval of the Group's efforts.

→ Creditor payment policy

The Group pays for the main raw material consumed (lead ingot) against delivery. The Group's payments for other raw materials are usually made on 50 to 90 days credit through long term co-operation agreements with suppliers. The Company has no trade creditors.

→ Financial instruments

Details of financial instruments, including financial risk management objectives and policies, details of the Group's exposure to credit risk, interest rate risk, foreign currency risk and liquidity risk are set out in note 26 to the financial statements.

→ Communication with shareholders and the market

The annual report and accounts and interim statement at each half year are the primary vehicles for communication with shareholders. Meetings with significant shareholders are arranged through our nominated advisor, and will take place after the final and interim financial statements are published. Such meetings may also take place after other significant announcements are made to the market.

Reports published by the Company's brokers are another means of communication with shareholders and the market. General information about the Company and its business is also available on the Company's website: www.chinashoto.com.

→ Annual general meeting

The annual general meeting (AGM) of the Company will take place at 100 Cannon Street, London EC4N6EU on 20 June 2006 at 10.00 am. Full details of the resolutions to be put to the meeting are given in the notice of the AGM to be found at pages 47 and 48 of this annual report.

→ Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of BDO Stoy Hayward LLP as auditor of the Company is to be proposed at the AGM.



By order of the board

David Thomas

Company Secretary

8 May 2006

Introduction

The board of directors is accountable to the Company's shareholders for good corporate governance. Although the Company's shares are traded on AIM, the directors plan to comply with the Combined Code where practicable and appropriate.

Below is a brief description of the role of the Board and its committees, followed by a statement regarding the Group's system of internal financial control.

The Board and its committees

→ The Board

The board comprises eight directors, five of whom are executive directors and three of whom are non-executive directors. It is responsible to shareholders for the proper management of the Group and it meets not less than four times a year, reviewing trading performance, ensuring adequate funding, setting and monitoring strategy, examining acquisition opportunities and capital expenditure projects, and reports to shareholders.

→ Audit Committee

The Audit Committee, which is chaired by Li Shuang, comprises non-executive directors only. It meets not less than once annually.

The Audit Committee receives and reviews reports from management and the Group's auditors relating to the interim and annual financial statements, and the accounting and internal control systems in use throughout the Group. The Audit Committee will have unrestricted access to the Group's auditors.

The audit committee advises the Board on the appointment of external auditors and on their remuneration, and discusses the nature and scope of the audit with the external auditors.

A formal statement of independence is received from the external auditors each year.

→ Remuneration Committee

The Remuneration Committee is chaired by David Thomas and includes Li Shuang and Wang Zhaobin. It meets at least once annually.

It is responsible for reviewing the scale and structure of the executive directors' and senior employees' remuneration and the terms of their service or employment contracts, including share option schemes and bonus arrangements. The remuneration and terms and conditions of the non-executive directors will be set by the entire Board.

→ Investment Committee

The Investment Committee is chaired by Zhu Shiping, and includes Bernard Asher and Cao Guifa. It meets at least once annually.

The responsibility of the Committee is assisting the Board in the implementation of the Company's strategy by preparing a feasibility study concerning each significant investment project before a decision is taken by the Board. Such a report will seek to improve profitability from the use of capital and minimise risks and monitor progress of such projects as are approved by the Board.

Internal Control and Risk Management

The board is responsible for establishing and maintaining the Group's system of internal control. The key procedures, which the directors have established with a view to providing effective internal controls, are as follows:

→ Management structure

The Board has overall responsibility for the Group. Executive directors together with key senior executives at the Group level meet monthly to discuss sales and day to day operational matters. The subsidiary undertakings of the Group also hold monthly management meetings to summarize operating activities, as well as additional meetings on matters such as quality analysis and control, and financial cost analysis.

→ Identification of business risks

The Board is responsible for identifying the major business risks faced by the Company and for determining the appropriate course of action to manage those risks.

→ Budgetary process

Each year the Board approves the annual budget, and key risk areas are identified. Performance is monitored and relevant action taken throughout the year through the monthly reporting to the Board of variances from the budget, updated forecasts for the year and information on the key risk areas.

→ Investment appraisal

As stated above the Investment Committee assists the Board in the implementation of the Company's strategy by preparing a feasibility study concerning each significant investment project before a decision is taken by the Board.

statement of directors' responsibilities

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of financial statements which comply with the requirements of the Companies Act 1985.

The directors have elected to prepare the financial statements for the Group and the company in accordance with International Financial Reporting Standards (IFRSs).

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Group's and the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards. A fair presentation also requires the directors to:

- select and apply appropriate accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- *provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.*

remuneration report

Remuneration policy

The aim of the Company's remuneration policy is to reward performance and to enhance shareholder value. Executive remuneration is designed to provide competitive rewards that will attract and retain high quality executives capable of achieving the Group's performance targets on both an annual and a longer-term basis.

The Remuneration Committee

The principal functions of the Remuneration Committee are to decide upon, on behalf of the Board and the shareholders, the remuneration packages of the executive directors, and the remuneration of senior executives of the Company.

The Committee also considers the approval of all service contracts between the Company and its Directors, or between the company and any such senior executive.

The Board (excluding the non-executive directors) determines the remuneration of non-executive directors.

Director's Remuneration

→ Executive directors

The main components of executive directors' remuneration are:

Salary

The basic salary of each director is determined by taking into account of the director's experience, responsibility and value to the organisation.

Bonus awards

In addition to salary, all executive directors were eligible for a performance-related bonus. The bonus was linked to achieving and exceeding certain clearly defined financial targets for the year ended 31 December 2005. The targets were designed to ensure that the total remuneration varies in line with corporate performance.

Benefits

Benefits include car subsidy, medical insurance, and contribution to State Pension Scheme (which is subject to stipulations of the State).

→ Non-executive directors

Non-executive directors' fees reflect the time that they are required to commit to their duties.

→ Remuneration

The remuneration of the directors during the year ended 31 December 2005 is set out in note 5 to the financial statements.

→ Share Options

The following directors had interests in options to subscribe for ordinary shares as follows:

Name	As at 31 Dec 2005	% of Issued Capital	Exercise price	Date of grant	Exercise period
Cao Guifa	300,000	1.5%	£1.30	30 Nov 2005	Dec 2008-Dec 2015
Yang Shanji	500,000	2.5%	£1.30	30 Nov 2005	Dec 2008-Dec 2015
Zhou Yue Zhang	200,000	1.0%	£1.30	30 Nov 2005	Dec 2008-Dec 2015
Wang Zhaobin	80,000	0.4%	£1.30	30 Nov 2005	Dec 2008-Dec 2015

Contracts of Service

The service agreements with each of the executive directors are terminable on 12 months notice by either party.

The non-executive directors all have letters of appointment with an initial fixed term of 12 months. The appointment may be terminated at any time thereafter by six months' written notice.

independent auditors' report to the members of china shoto plc

We have audited the group and parent company financial statements (the 'financial statements') of China Shoto plc for the year ended 31 December 2005 which comprise the Consolidated Income Statement, the Consolidated and Parent Company Balance Sheets, the Consolidated and Parent Company Statements of Changes in Equity, the Consolidated and Parent Company Cash Flow Statements, and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with those financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report, the Chairman's Statement, the Chief Executive's Review, the Financial Director's Review, the Highlights, the Company Overview, the Remuneration Report, the Corporate Governance statement and the Statement of Directors' Responsibilities. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 December 2005 and of its profit for the year then ended;
- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2005; and
- the financial statements have been properly prepared in accordance with the Companies Act 1985.

BDO Stoy Hayward LLP

BDO Stoy Hayward LLP
Chartered Accountants and Registered Auditors
Northside House
69 Tweedy Road
Bromley
BR1 3WA
8 May 2006

consolidated income statement

For the year ended 31 December 2005

	Notes	Year ended 31 December 2005 £000	Year ended 31 December 2004 £000
Revenue	3	28,413	18,688
Cost of sales		(18,161)	(12,750)
Gross profit		10,252	5,938
Other operating income	3	689	569
Selling and distribution expenses		(3,879)	(3,003)
Administrative expenses		(2,681)	(1,147)
Other operating expenses		(20)	(37)
Share of results of associate		56	—
Profit from operations	4	4,417	2,320
Finance income	3	72	45
Finance costs	6	(864)	(590)
Profit before tax		3,625	1,775
Tax	7	(514)	(269)
Net profit for the year attributable to equity holders		3,111	1,506
Earnings per share in pence:			
Basic	9	19.80p	9.79p
Diluted	9	19.74p	9.76p

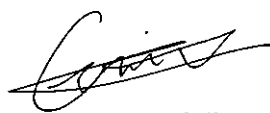
All amounts relate to continuing operations.

consolidated balance sheet

As at 31 December 2005

	Notes	31 December 2005 £000	31 December 2004 £000
Assets			
Non-current assets			
Property, plant and equipment	10	8,559	7,811
Investment in associate	12	512	—
Land use right	13	1,393	1,208
Other intangible assets	14	17	18
Deferred tax assets	7	36	20
		10,517	9,057
Current assets			
Inventories	15	3,547	4,164
Trade receivables	16	11,953	7,213
Other receivables and prepayments	17	3,480	2,976
Due from related parties	23	1,963	1,623
Short-term investments	18	2,350	31
Cash and cash equivalents	19	8,300	3,845
		31,593	19,852
Total assets		42,110	28,909
Liabilities			
Current liabilities			
Bank borrowings	20	12,083	9,950
Trade payables		3,919	3,061
Notes payable	21	4,126	2,960
Other payables and accruals	22	5,058	4,741
Due to related parties	23	765	669
Income tax payable		97	73
		26,048	21,454
Total liabilities		26,048	21,454
Capital and reserves			
Share capital	24	2,000	—
Share premium	25	3,875	—
Other reserves	25	2,916	4,454
Statutory reserves	25	4,024	3,206
Retained earnings	25	3,837	1,744
Foreign currency translation reserve	25	(590)	(1,949)
Total equity		16,062	7,455
Total equity and liabilities		42,110	28,909

The financial statements were approved and authorised for issue by the Board of Directors on 8 May 2006 and signed on its behalf by:


Cao Guifa
Chairman


Yang Shanji
Chief Executive

consolidated statement of changes in equity

For the year ended 31 December 2005

	Share capital Note 24 £000	Share premium Note 25 £000	Other reserves Note 25 £000	Statutory reserves Note 25 £000	Retained earnings Note 25 £000	Currency translation reserve Note 25 £000	Total £000
Balance as at 31 December 2003	–	–	4,454	2,622	2,947	(1,394)	8,629
Net profit for the financial year	–	–	–	–	1,506	–	1,506
Transfer to statutory reserves	–	–	–	584	(584)	–	–
Dividends paid to external shareholders	–	–	–	–	(2,125)	–	(2,125)
Foreign currency translation	–	–	–	–	–	(555)	(555)
Balance as at 31 December 2004	–	–	4,454	3,206	1,744	(1,949)	7,455
Issue of ordinary shares to the vendors							
of Leadstar Enterprises Ltd	1,538	–	(1,538)	–	–	–	–
Issue of ordinary shares on placing	462	5,538	–	–	–	–	6,000
Share issue costs	–	(1,663)	–	–	–	–	(1,663)
Net profit for the financial year	–	–	–	–	3,111	–	3,111
Transfer to statutory reserves	–	–	–	818	(818)	–	–
Share based payment expense							
- Employee share options	–	–	–	–	27	–	27
- Expenses of flotation	–	–	–	–	118	–	118
Dividends paid to external shareholders	–	–	–	–	(345)	–	(345)
Foreign currency translation	–	–	–	–	–	1,359	1,359
Balance as at 31 December 2005	2,000	3,875	2,916	4,024	3,837	(590)	16,062

consolidated cash flow statements

For the year ended 31 December 2005

	Notes	Year ended 31 December 2005 £000	Year ended 31 December 2004 £000
Net cash from operating activities	a	3,185	(833)
Cash flows from investing activities			
Purchase of trade mark		—	(20)
Purchase of associate		(425)	—
Purchase of land use right		(60)	(1,218)
Purchase of property, plant and equipment		(954)	(2,009)
Purchase of short-term investment		(2,336)	(20)
Proceeds from disposal of property, plant and equipment		93	133
Proceeds from disposal of short-term investment		21	1,451
Cash flows used in investing activities		(3,661)	(1,683)
Cash flows from financing activities			
Net cash inflow from share placing		4,337	—
Increase in short-term bank borrowings		674	6,401
Interest paid		(864)	(587)
Dividends paid to external shareholders		—	(2,125)
Cash flows from financing activities		4,147	3,689
Net increase in cash and cash equivalents		3,671	1,173
Cash and cash equivalents at beginning of year		3,845	2,923
Foreign exchange differences		784	(251)
Cash and cash equivalents at end of year		8,300	3,845

notes to the consolidated cash flow statements

(a) Cash flows from operating activities

	Year ended 31 December 2005 £000	Year ended 31 December 2004 £000
Profit before tax	3,625	1,775
Adjustments for:		
Amortisation of trade mark	1	1
Amortisation of land use right	28	24
Allowance for doubtful trade debts	27	(182)
Allowance for doubtful non-trade debts	27	(32)
Depreciation of property, plant and equipment	855	709
Losses on disposal of property, plant and equipment	20	18
Gain on disposal of short-term investment	(56)	(13)
Share based payment expense	145	—
Financial income	(72)	(30)
Financial expense	864	587
Operating profit before working capital changes	5,464	2,857
Working capital changes:		
(Increase)/decrease in:		
Inventories	1,134	(2,056)
Trade receivables	(3,615)	2,897
Other receivables, deposits and prepayments	(237)	810
Due from related parties	(102)	1,148
Increase/(decrease) in:		
Trade payables	397	1,433
Other payable and accruals	(130)	(2,067)
Notes payables	698	130
Due to related parties	—	(5,678)
Cash generated from/(used in) operations	3,609	(526)
Interest received	72	30
Income tax paid	(496)	(337)
Net cash from operating activities	3,185	(833)

(b) Non-cash flow transactions

On 30 November 2005, the shareholders of Leadstar Enterprises Limited and China Shoto plc entered into a share exchange agreement. China Shoto plc issued 15,384,615 10p ordinary shares at 130p each to the shareholders of Leadstar Enterprises Limited in exchange for the entire share capital of Leadstar Enterprises Limited.

(c) Dividend


A subsidiary undertaking, Hong Kong Wealth Source Development Co. Ltd, declared a dividend of £34.50 per ordinary share amounting to £345,000 on 30 June 2005 to its shareholders at that date. All the dividend was set against the debt due from those shareholders.

company balance sheet

As 31 December 2005

	Notes	31 December 2005 £000
Assets		
Non-current assets		
Investment in subsidiaries	11	20,000
		20,000
Current assets		
Other receivables	17	6
Due from related parties	23	4,928
Cash and cash equivalents	19	67
		5,001
Total assets		25,001
Liabilities		
Current liabilities		
Due to related parties	23	667
Total liabilities		667
Capital and reserves		
Share capital	24	2,000
Share premium	25	3,875
Other reserve	25	18,462
Retained earnings	25	(3)
Total equity		24,334
Total equity and liabilities		25,001

The financial statements were approved and authorised for issue by the Board of Directors on 8 May 2006 and signed on its behalf by:



Cao Guifa
Chairman



Yang Shanji
Chief Executive

company statement of changes in equity

For the period ended 31 December 2005

	Share capital Note 24 £000	Share premium Note 25 £000	Other reserves Note 25 £000	Retained earnings Note 25 £000	Total £000
Incorporation (10 May 2005)	—	—	—	—	—
Issue of ordinary shares to the vendors of Leadstar Enterprises Limited	1,538	—	18,462	—	20,000
Issue of ordinary shares on placing	462	5,538	—	—	6,000
Share issue costs	—	(1,663)	—	—	(1,663)
Net loss for the financial period	—	—	—	(148)	(148)
Share based payment expense	—	—	—	—	—
- Employee share options	—	—	—	27	27
- Expenses of flotation	—	—	—	118	118
Balance as at 31 December 2005	2,000	3,875	18,462	(3)	24,334

company cash flow statement

For the period ended 31 December 2005

	Notes	Year ended 31 December 2005 £000
Net cash from operating activities	a	(4,937)
Cash flows from financing activities		
Net cash inflow from share placing		5,004
Net increase/(decrease) in cash and cash equivalents		67
Cash and cash equivalents at end of year		67

notes to the company cash flow statements

For the period ended 31 December 2005

(a) Cash flows from operating activities

	Year ended 31 December 2005 £000
Loss before income tax	(148)
Adjustment for share based payment expense	145
Operating loss before working capital changes	(3)
Working capital changes:	
Amounts due from subsidiary undertakings	(4,928)
Other receivables	
Cash generated from (used in) operations	(4,937)
Net cash used in operating activities	(4,937)

notes to the financial statements

For the year ended 31 December 2005

1 General information

China Shoto plc is a company incorporated in the United Kingdom on 10 May 2005 under the Companies Act 1985. The address of the registered office is given on page 1, and the principal place of business is Shuangdeng Science and Industrial Zone, Liangxu Town, Jiangyan City, Jiangsu Province, China. Details of the Group's reporting and functional currencies are disclosed in note 2 below.

These financial statements present information about the Company on a stand alone basis and as a consolidated group of companies. The nature of the Group's operations and its principal activities are set out in the Directors' report on page 14.

These financial statements are the Group's and the Company's first financial statements.

2 Accounting policies

The consolidated financial statements of China Shoto plc and its subsidiary undertakings (the 'Group') and the individual financial statements of China Shoto plc (the 'Company') have been prepared in accordance with those International Financial Reporting Standards and Interpretations in force ('IFRS'), as adopted by the European Union, and those parts of the Companies Act 1985 applicable to companies preparing financial statements under IFRS.

The Company has taken advantage of the exemption allowed under section 230 of the Companies Act 1985 and has not presented its income statement in these financial statements. The Group profit for the year includes a loss after tax of £148,000 which is dealt with in the financial statements of the Company.

The preparation of financial statements in conformity with IFRSs requires management to make assumptions that affects the application of accounting policies and the amounts of assets, liabilities, income and expenditure. The estimates and associated assumptions are based on historical experience and other relevant factors, the results of which form the basis for the judgements that underlie the carrying value of the assets and liabilities. Actual results may differ from these estimates. The most significant areas in which judgements are required relate to the evaluation of fair values in the application of acquisition accounting, the estimate of useful economic lives and residual values of non-current assets and the recoverable amount of current and non-current assets. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised if the revision affects only that period, or in the period of revision and future period if the revision affects both the current and future periods. For the years ended 31 December 2005 and 2004 the Group comprised only one business and geographic segment.

The following principal accounting policies have been applied consistently in dealing with items which are considered material to the financial statements.

→ Basis of consolidation

The consolidated financial statements include the financial statements of China Shoto plc and all of its subsidiary undertakings as at 31 December 2005 using the acquisition method of accounting. The results of subsidiary undertakings are included from the date of acquisition.

The acquisition of Leadstar Enterprises Limited by China Shoto plc on 30 November 2005 has been accounted for as a reverse acquisition, in accordance with IFRS 3 'Business Combinations', on the basis that the management, who are the former majority shareholders of Leadstar Enterprises Limited, retained effective control of the Group. The fair value of the assets of China Shoto plc at the date of the business combination were equivalent to the fair value of the Company and the fair value of the notional number of equity instruments which would have been issued by Leadstar Enterprises Limited to acquire China Shoto plc, and therefore no goodwill arises in respect of this business combination. The comparative financial statements and the results up to the date of the business combination represent those of the Leadstar Enterprises Limited group.

→ Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary or associated undertaking at the date of acquisition.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement, through administrative expenses, and is not subsequently reversed.

notes to the financial statements (continued)

For the year ended 31 December 2005

→ Associated undertakings

An entity is treated as an associated undertaking where the Group has a participating interest and exercises significant influence over its operating and financial policy decisions. In the consolidated financial statements, interests in associated undertakings are accounted for using the equity method of accounting. The consolidated income statement includes the Group's share of the associate's net profit, based on audited financial statements and/or management accounts. In the consolidated balance sheet, the investment in associated undertakings is shown as the Group's share of the net assets of the associated undertakings.

→ Foreign currencies

The functional currency of the subsidiary undertakings is Renminbi ("RMB"), and the audited financial statements of the subsidiary undertakings have been drawn up in RMB. As sales and purchases are denominated primarily in RMB and receipts from operations are usually retained in RMB, the directors are of the opinion that RMB reflects the economic substance of the underlying events and circumstances relevant to the Group. Monetary assets and liabilities maintained in currencies other than RMB are translated into RMB at the approximate rates of exchange ruling at the balance sheet date. Transactions in currencies other than RMB are translated at rates ruling on the transaction dates. All resulting exchange differences are dealt with in the income statements.

The presentation currency of the Group is pounds sterling and therefore the financial statements have been translated from RMB to pounds sterling at the following exchange rates:

	Year-end rates	Average rates
31 December 2004	£1 = RMB 15.8901	£1 = RMB 15.1651
31 December 2005	£1 = RMB 13.9122	£1 = RMB 14.8270

Assets and liabilities are translated into sterling at the closing rate, and all income and expenses are translated at the average rate during the financial period, being an approximation for the actual rates at the date of the transactions. All resulting exchange differences are taken to the Exchange reserve within equity.

The functional currency and the presentation currency of the Company is pounds sterling. Monetary assets and liabilities maintained in currencies other than pounds sterling are translated into pounds sterling at the rates of exchange ruling at the balance sheet date. Transactions in currencies other than pounds sterling are translated at rates ruling on the transaction dates. All resulting exchange differences are dealt with in the income statement.

→ Revenue recognition

Revenue from the sale of goods is recognised when significant risks and rewards of ownership of the goods are transferred to the customer, when the companies neither retain continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, when it is probable that the economic benefits associated with the transaction will flow to the companies and when the relevant amount of revenue and costs can be measured reliably.

Interest income is recognised on a time apportioned basis, taking account of the principal outstanding and the effective rate over the period to maturity, when it is determined that such income will accrue to the companies within the Group.

Government grants in respect of revenue items are recognised when received, dependent upon the revenue item cost having been booked or incurred.

Management charges are recognised monthly relating to the income received from the related parties for providing management services.

→ Employee benefits

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statements as incurred.

→ Share-based payments

The Group has applied the requirements of IFRS2 Share-based payments in these financial statements.

The Group has issued equity-settled share-based payments to certain directors and employees, and to its advisors for services provided in respect of the flotation. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled, share-based payments is expensed to the income statement on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest.

Fair value is measured by use of the Black-Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

→ Borrowings costs

All borrowings costs are recognised in the income statement in the period in which they are incurred.

→ Income tax

Income tax for the financial year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case such tax is recognised in equity.

Current tax is the expected tax payable on the taxable income for the financial year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous financial years.

Deferred tax is provided using the liability method, providing for temporary differences as at the balance sheet date between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, except for differences arising on the initial recognition of goodwill and goodwill for which amortisation is not deductible. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

→ Dividends

Equity dividends are recognised when they become legally payable. In respect of interim dividends to equity shareholders, this is when they are declared and paid. In respect of final dividends to equity shareholders, this is when they are approved by the Annual General Meeting.

→ Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Depreciation is calculated on the straight-line method so as to write off the cost of property, plant and equipment reduced by the estimated residual value of the assets over their estimated useful lives. The estimated residual value and annual depreciation rates used for this purpose are as follows:

Item	Estimated residual value	Useful life	Annual depreciation rates
Building	10%	20	4.5%
Machinery	10%	10	9%
Motor vehicles	10%	5	18%
Office equipment	10%	5	18%

Fully depreciated plant and equipment are retained in the financial statements until such time that they are no longer in use. Construction in progress represents property, plant and equipment under construction and is stated at cost. No provision for depreciation is made on construction in progress until such time as the relevant assets are completed and put into use.

→ Land use rights

Land use rights are measured initially at fair value, including the fair value of government grants, as deemed cost. Government grants relating to land use rights, being the difference between the fair value and the cost to the Group are deducted from the fair value of the asset, and the net cost amortised through the income statement on a straight line basis over the life of the asset. The life of the land use right is taken to be the length of time for which the right has been granted (42 to 50 years). The carrying values of land use rights are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

notes to the financial statements (continued)

For the year ended 31 December 2005

→ Other intangible assets

Other intangible assets are stated at cost less any impairment losses. Intangible assets are amortised through administrative expenses using the straight-line basis over the following estimated useful lives:

Trademark 10 years

The carrying values of intangible assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

→ Investment in subsidiary undertakings

Investments in subsidiaries are stated at cost less provision for any permanent impairment in value.

→ Impairment of assets

The carrying amounts of non-current assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of the asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised through administrative expenses in the income statement.

The recoverable amount is the higher of an asset's net selling price and value in use. The net selling price is the amount obtainable from the sale of an asset in an arm's length transaction. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. Recoverable amounts are estimated for individual assets or, if it is not possible, for the cash generating unit.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised. Reversals of impairment losses are recognised in the income statement.

→ Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average cost method. The cost of finished goods comprises raw materials, direct labour, other direct costs and related production overheads but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less the costs of completion and selling expenses.

→ Financial assets

Financial assets are cash and bank balances, trade and other receivables, amounts due from related parties, notes receivable and investments.

Trade and other receivables, amounts due from related parties, notes receivable and short-term investments are stated at cost as reduced by appropriate allowances for estimated irrecoverable amounts.

Known bad receivables are written off as incurred when collection for the full amount is no longer probable, and an estimate for doubtful debts made based on past experience.

→ Cash and cash equivalents

Cash comprises cash in hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

→ Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. Financial liabilities include trade and other payables, amounts due to related parties and shareholders, bank borrowings and notes payable.

Trade and other payables are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Group.

Bank borrowings and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges are charged to the income statement on an accruals basis.

Equity instruments are recorded at the fair value of the consideration received, net of direct issue costs.

For the year ended 31 December 2005

→ Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing and subsequently measured at amortised cost using the effective interest rate method.

→ Government grants

Government grants received on capital expenditure are generally deducted in arriving at the carrying amount of the asset purchased. *Grants for revenue expenditure are netted against the cost incurred by the Group.*

Where retention of the government grant is dependent on the Group satisfying certain criteria it is initially recognised as deferred income. When the criteria for retention have been satisfied, the deferred income balance is released to the income statement or netted against the asset purchased as appropriate.

→ Related parties

Parties are considered to be related if one party 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. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

→ Research and development expenditure

Development expenditure not satisfying the capitalisation criteria set out in IAS 38 Intangible Assets and expenditure on the research phase of internal projects are recognised in the income statement as incurred.

3 Revenue

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
Sale of goods	28,413	18,688
Other operating income		
Waste disposal and sale of by-products	30	126
Management fee	385	310
Government grant income	266	104
Other	8	29
	689	569
Finance income		
Interest income	67	30
Gain on disposal of investment	—	13
Exchange gain	5	2
	72	45
Total income	29,174	19,302

Sale of goods represents the invoiced amount of delivered goods net of discounts, returns and valued added tax. All intra-group transactions are excluded from the revenue of the Consolidated Group.

notes to the financial statements (continued)

For the year ended 31 December 2005

4 Profit from operations

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
After charging / (crediting):		
Cost of inventories recognised as an expense	18,161	12,750
Allowance for obsolete inventories / (no longer required)	-	(2)
Remuneration of auditors		
- Audit services	49	25
- Non-audit services	-	-
Amortisation of land use right	28	24
Amortisation of intangible assets	1	1
Depreciation of property, plant and equipment	855	709
Loss/(gain) on disposal of property, plant and equipment	20	18
Allowance for doubtful trade debts/(no longer required)	27	(183)
Allowance for doubtful non-trade debts / (no longer required)	27	(32)
Research and development expenditure	224	382
(Gain) on disposal of short-term investments	-	(13)
Share based payment expense:		
Employee share options	27	-
Expenses of flotation	118	-

Audit fees include an amount of £22,000 in respect of the Company (2004: £nil).

5 Information regarding directors and employees

	Group Year ended 31 December 2005 Number	Group Year ended 31 December 2004 Number
Average number of employees of the Group		
Management and administration	186	150
Sales	141	141
Manufacturing	450	401
	777	692

	£000	£000
The aggregate payroll costs of these employees was as follows:		
Wages and salaries	1,956	1,391
Social security costs	139	63
Retirement benefits	27	88
Share-based payment expense	27	-
	2,149	1,542

For the year ended 31 December 2005

Directors remuneration was as follows:

	Year ended 31 Dec2005	Year ended 31 Dec2005	Year ended 31 Dec2005	Year ended 31 Dec2005 Total emoluments	Year ended 31 Dec2004 Total emoluments
	Salary £000	Benefits £000	Bonus £000	£000	£000
Cao Guifa	20	—	16	36	19
Yang Shanji	20	—	47	67	97
Zhou Yuezhang	16	3	16	35	35
Wang Zhaobin	16	2	16	34	12
Zhu Shiping	8	3	16	27	27
Li Shuang	5	—	—	5	—
Bernard Asher	1	—	—	1	—
David Thomas	1	—	—	1	—
Total	87	8	111	206	190

One director (Zhou Yuezhang) is a member of the Group's pension scheme. Total contributions to the pension scheme in respect of Zhou Yuezhang were £175 (2004: £171).

6 Finance costs

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
Interest expense on bank and other loans	864	590

notes to the financial statements (continued)

For the year ended 31 December 2005

7 Income tax

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
Income tax expense is as follows		
Current income tax	527	243
Deferred income tax	(13)	26
	514	269
Deferred tax assets		
At beginning of the financial period	20	48
Transfer to/(from) income statement	13	(26)
Exchange differences	3	(2)
At end of the financial period	36	20
Tax effect of temporary difference arising from:		
Allowance for bad and doubtful debts	31	20
Potential gain on share options	5	—
	36	20
Reconciliation of effective tax rates		
Profit before tax	3,770	1,775
Tax at respective companies' domestic income tax rate	519	259
Tax effect of non-deductible expenses	—	10
Tax effect of share-based payment expenses	(5)	—
	514	269

The company and the significant subsidiary undertakings are subject to income tax on the following bases and at the following rates:

- China Shoto plc
The Company is subject to UK corporation tax at the standard rate of 30%.
- Jiangsu Shuangdeng Group Co. Ltd
In 2005 the company reregistered as a foreign enterprise and is entitled to exemptions from PRC income tax for the first two years (2005 and 2006) and to a 50% relief from PRC income tax for another three years thereafter. Its standard applicable tax rate is 33%.
- Jiangsu Shuangdeng Longyuan Power Supply Co. Ltd and Jiangsu Fuste Power Supply Co. Ltd
The companies are located in an area designated as an Economic Development Coastal Region in accordance with PRC tax regulations and are entitled to an applicable tax rate of 24%; meanwhile as a production enterprise in accordance with the PRC tax legislation applicable to foreign investment enterprises each company is entitled to exemptions from PRC income tax for the two years commencing from their first profit-making year of operation (2001 for Jiangsu Shuangdeng Longyuan Power Supply Co. Ltd and 2004 for Jiangsu Fuste Power Supply Co. Ltd) and for another three years thereafter they are entitled to a 50% relief from PRC income tax.

→ Jiangsu Shuangdeng Power Supply Co. Ltd

The company is recognised as a 'technology and knowledge concentrated enterprise' and entitled to a 15% PRC income tax rate because it is a production enterprise and also located in an area designated as an Economic Development Coastal Region in accordance with PRC tax regulations.

→ Nanjing Shuangdeng Science and Technology Research and Development Institute Co. Ltd

In 2005 the company reregistered as a foreign investment enterprise and meanwhile it is a production enterprise located in a development zone in accordance with the PRC income tax legislation so it is entitled to exemptions from PRC income tax for the two years commencing from its first profit-making year of operation and thereafter it is entitled to a 50% relief from PRC income tax for the next three years. Its applicable tax rate is 24%.

8 Dividends

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
Interim dividends paid	345	2,125

A subsidiary undertaking, Hong Kong Wealth Source Development Ltd. declared a dividend of £34.50 per ordinary share amounting to £345,000 on 30 June 2005 to its shareholders at that date. All the dividend was set against the debt due from those shareholders. The interim dividends paid in 2004 relate to dividends paid by various subsidiary undertakings to former shareholders following the establishment of the Group.

The Directors do not propose a final dividend (2004: £nil).

9 Earnings per share

Earnings for the purpose of basic and diluted earnings per share are the net profit for the financial year of £3,111,000 (2004: £1,506,000).

The weighted average number of ordinary shares used in the calculation of earnings per share has been derived as follows:

	Group Year ended 31 December 2005 Number	Group Year ended 31 December 2004 Number
Weighted average number of ordinary shares - basic		
15,384,615 10p ordinary shares issued to the vendors of Leadstar Enterprises Limited	15,384,615	15,384,615
2 £1 ordinary shares issued on incorporation, and subsequently split into 20 10p ordinary shares	13	—
4,615,385 10p ordinary shares issued on placing	328,767	—
	15,713,395	15,384,615
Weighted average number of ordinary shares - diluted		
Weighted average number of ordinary shares - basic	15,713,395	15,384,615
Dilutive effect of share options	48,600	48,600
	15,761,955	15,433,215

notes to the financial statements (continued)

For the year ended 31 December 2005

10 Property, plant and equipment

Group	Buildings £000	Machinery £000	Motor vehicles £000	Office equipment £000	Construction in progress £000	Total £000
Cost						
At 1 January 2004	3,793	4,520	131	936	751	10,131
Additions	44	423	15	49	875	1,406
Reclassifications	12	506	—	(518)	—	—
Transfers	1,430	107	—	1	(1,538)	—
Disposals	(121)	(30)	(58)	(40)	—	(249)
Exchange adjustments	(319)	(351)	(7)	(40)	(20)	(737)
At 31 December 2004	4,839	5,175	81	388	68	10,551
Additions	222	236	180	174	35	847
Reclassifications	62	13	—	2	(77)	—
Disposals	(15)	(85)	(44)	(88)	—	(232)
Exchange adjustments	588	594	9	46	8	1,245
At 31 December 2005	5,696	5,933	226	522	34	12,411
Accumulated depreciation						
At 1 January 2004	644	965	56	647	—	2,312
Charge for the year	201	438	12	58	—	709
Reclassifications	10	428	—	(438)	—	—
Disposals	(25)	(26)	(28)	(18)	—	(97)
Exchange adjustments	(52)	(103)	(3)	(26)	—	(184)
At 31 December 2004	778	1,702	37	223	—	2,740
Charge for the period	262	464	14	115	—	855
Disposals	(2)	(6)	(22)	(19)	—	(49)
Exchange adjustments	87	192	2	25	—	306
At 31 December 2005	1,125	2,352	31	344	—	3,852
Net book value						
At 31 December 2004	4,061	3,473	44	165	68	7,811
At 31 December 2005	4,571	3,581	195	178	34	8,559

For the year ended 31 December 2005

11 Investment in subsidiary undertaking

	2005 £000
Cost:	
At the beginning of financial period	—
Additions	20,000
At 31 December 2005	20,000

The Company issued 15,384,615 10p ordinary shares at 130p each to the shareholders of Leadstar Enterprises Limited on 30 November 2005 in return for the entire issued share capital of that company.

12 Investment in associates

	31 December 2005 £000	31 December 2004 £000
Cost of investment in associates	425	—
Group's share of the associate's profits for period	56	—
Exchange adjustments	31	—
	512	—
Cost of investment in associates	425	—
Share of net assets on acquisition date	(270)	—
Goodwill on investment in associates	155	—

The carrying value of goodwill has been tested for impairment at the end of the year. No impairment is considered necessary as the associate's value in use is considered to exceed the carrying value.

Details of the Group's associated undertaking at 31 December 2005 are as follows:

Name of the associate	Place of incorporation and operation	Proportion of ownership interest	Principal activity
Beijing Full Three Dimension Power Engineering Co. Limited	Beijing China	30%	Design and reconstruction of turbines

Beijing Full Three Dimension Engineering Co. Ltd became an associated undertaking of the Consolidated Group on 23 June 2005.

notes to the financial statements (continued)

For the year ended 31 December 2005

	6 January 2006 (see note 28) £000	23 June 2005 £000
Non-current assets	101	112
Current assets		
Trade and other receivables	8,376	11,316
Cash and cash equivalents	1,430	1,946
Total assets	9,907	13,374
Creditors due within one year	(8,751)	(12,474)
Net assets	1,156	900
Group's share of the associate's net assets		270

Summarised financial information in respect of the Group's associate is set out below:

	Period from 23 June 2005 to 31 December 2005 £000	Period ended 23 June 2005 £000
Revenue	4,917	6,627
Profit for the period	185	457
Group's share of the associate's net profit for the period	56	—

13 Land use rights

	31 December 2005 £000	31 December 2004 £000
Cost:		
At the beginning of financial year	1,232	75
Additions	60	1,218
Exchange adjustments	154	(61)
At the end of financial year	1,446	1,232
Accumulated amortisation:		
At beginning of financial year	24	1
Amortisation for the financial year	28	24
Exchange adjustments	1	(1)
At the end of financial year	53	24
Net book value	1,393	1,208

The Group's land use rights have a remaining amortisation period of 40 or 48 years.

For the year ended 31 December 2005

14 Other intangible assets

	31 December 2005 £000	31 December 2004 £000
Trademark		
Cost:		
At the beginning of financial year	19	—
Additions	—	20
Exchange adjustments	—	(1)
At the end of financial year	19	19
Accumulated amortisation:		
At beginning of financial year	1	—
Amortisation for the financial year	1	1
At the end of financial year	2	1
Net book value	17	18

15 Inventories

	Group 31 December 2005 £000	Group 31 December 2004 £000
Raw materials	704	640
Work in progress	1,009	924
Finished goods	1,834	2,600
	3,547	4,164

16 Trade receivables

	Group 31 December 2005 £000	Group 31 December 2004 £000
Trade receivables	12,117	7,332
Allowance for doubtful receivables	(164)	(119)
	11,953	7,213

17 Other receivables and prepayments

	Group 31 December 2005 £000	Group 31 December 2004 £000	Company 31 December 2005 £000
Notes receivable	145	—	—
Advances to suppliers	2,500	1,634	—
Advances to employees	816	887	—
Other advances	17	432	—
Other receivables	55	48	6
	3,533	3,001	6
Allowance for doubtful other receivables	(53)	(25)	—
	3,480	2,976	6

notes to the financial statements (continued)

For the year ended 31 December 2005

18 Short term investments

	Group 31 December 2005 £000	Group 31 December 2004 £000
Cost:		
Deposits with an initial maturity of more than 23 months		
- Short term deposits secured for notes payable	755	19
- Other short term deposits	1,581	-
Investment in shares	14	12
	2,350	31

The short term deposits are invested for the period from 29 December 2005 to 29 June 2006 with a fixed annual interest rate of 2.07%.

19 Cash and cash equivalents

	Group 31 December 2005 £000	Group 31 December 2004 £000	Company 31 December 2005 £000
Cash-floating rate	6,884	1,403	67
Deposits-secured for Notes Payables with an initial maturity of 3 months	1,416	2,442	-
	8,300	3,845	67

The short term deposits are invested at an annual interest rate of 2.07%. Cash earns interest at variable rates, averaging 0.72%.

20 Bank borrowings

	31 December 2005 £000	31 December 2004 £000
Short-term bank borrowings	12,083	9,950

Short-term bank borrowings are all at fixed rates and are secured by a first mortgage over the Group's main property, plant and equipment and land use right, guaranteed by the Group's credit and secured by the Group's notes receivables.

Short-term bank borrowings have an average maturity of 7 months from the end of the financial year (2004: 7 months) and an interest rate ranging from 5.58% to 5.74% (2004: 5.04% to 5.74%). The weighted average interest rate is 5.62% (2004: 5.41%).

21 Notes payables

	Group 31 December 2005 £000	Group 31 December 2004 £000
Notes payable	4,126	2,960

Notes payable are secured by fixed deposits (notes 18 and 19), are interest free and have an average maturity of 6 months.

22 Trade and other payables and accruals

	Group 31 December 2005 £000	Group 31 December 2004 £000
Other payables and accruals comprise:		
Advances from customers	292	579
Staff costs	1,048	395
Other tax payable	465	253
Loan from third parties	—	118
Amount due to employees	1,540	1,567
Staff housing fund	974	726
Other payables	739	1,103
	5,058	4,741

Trade payables comprise amounts outstanding for trade purchases and ongoing costs. The Group pays for the main raw material (lead ingot) against delivery of the goods. The Group's payments for other raw materials are usually made on 50 to 90 days credit.

The directors consider that the carrying amount of trade and other payables and accruals approximate to their fair values.

23 Related parties

The group companies set out in note 27, the associated undertaking identified in note 12, the directors and the following related parties have been identified:

Related parties	Relationship
Shenyang Shuangdeng Sci-tech Development Co. Ltd	Common legal representative
Nanjing Wo Bang Sci-tech Co. Ltd	Common legal representative
Jiangsu Shuangdeng Electric Appliance and Cable Co. Ltd	Managed by Jiangsu Shuangdeng Group Co. Ltd

Directors' remuneration is disclosed in note 5. Amounts due from and to related parties are as follows:

	Group 31 December 2005 £000	Group 31 December 2004 £000	Company 31 December 2005 £000
Due from related parties - Trade	757	490	—
Due from related parties - Non-trade	1,206	1,133	—
Due from subsidiary undertakings - Non-trade	—	—	4,928
	1,963	1,623	4,928
Due to related parties - Trade	—	3	—
Due to related parties - Non-trade			
- due to Chief Executive Yang Shanji	746	664	—
- due to other shareholders	19	2	—
Due to subsidiary undertakings - non-trade	—	—	667
	765	669	667

notes to the financial statements (continued)

For the year ended 31 December 2005

In addition to the related party information disclosed elsewhere in the financial statements, significant transactions during the financial year with related parties, all of which were negotiated at arms length, were as follows:

	Group Year ended 31 December 2005 £000	Group Year ended 31 December 2004 £000
Sale of goods:		
Jiangsu Shuangdeng Electric Appliance and Cable Co. Ltd	643	977
Shenyang Shuangdeng Sci-tech Development Co. Ltd	2,146	939
Nanjing Wo Bang Sci-tech Co, Ltd	-	860
	2,789	2,776
Other operating income:		
Yangzhou Hua Fu Industrial Co., Ltd	-	26
Jiangsu Shuangdeng Electric Appliance and Cable Co., Ltd	386	353
	386	379
Purchases:		
Yangzhou Hua Fu Industrial Co. Ltd	-	(224)
Jiangsu Shuangdeng Electric Appliance and Cable Co. Ltd	(49)	(645)
	(49)	(869)
Debt factoring:		
Huazi Property Management Co. Ltd	-	1,242
Shenyang Shuangdeng Sci-tech Development Co. Ltd	-	152
	-	1,394

Amounts due to the Company from subsidiary undertakings represents net proceeds from the flotation which have been advanced to the trading subsidiaries to invest in new plant. Amounts due to subsidiary undertakings represent share issue costs paid on the Company's behalf by subsidiary undertakings.

In the opinion of the directors, the Group is controlled by Mr. Yang Shanji, General Manager and Director, who owned 54.9% percentage of issued share capital of China Shoto plc at 31 December 2005.

For the year ended 31 December 2005

24 Share capital

	31 December 2005 £000	31 December 2004 £000
Authorised		
100,000,000 Ordinary shares of 10p each	10,000	—
Allotted, called up and fully paid:		
20,000,020 Ordinary shares of 10p each	2,000	—
	Number	£000
Issued on incorporation - 2 £1 ordinary shares	2	—
Sub-division into 10 ordinary shares	18	—
30 November 2005:		
Issue of 10p ordinary shares on reverse acquisition of Leadstar Enterprises Ltd	15,384,615	1,538
6 December 2005: Issue of 10p ordinary shares on placing	4,615,385	462
At 31 December 2005	20,000,020	2,000

The Company was incorporated on 10 May 2005 with authorised share capital of £1,000 divided into 1,000 ordinary shares of £1 each. On incorporation, 2 ordinary shares of £1 each were issued for cash at £1 per share.

On 30 November 2005 the authorised share capital was sub-divided into 10,000 ordinary shares of 10p each, and the authorised share capital was increased to £10,000,000 by the creation of a further 99,990,000 ordinary shares of 10p each, and 15,384,615 shares were issued in consideration for the entire issued share capital of Leadstar Enterprises Limited.

On 5 December 2005, 4,615,385 10p ordinary shares were issued in connection with the placing.

Details of share options are given in note 29.

25 Reserves

→ Share premium account

	31 December 2005 £000	31 December 2004 £000
Arising on issue of ordinary shares		
Premium of £1.20 per share arising on placing	5,538	—
Less: expenses of issue	(1,663)	—
	3,875	—

In accordance with s131 Companies Act 1985, no share premium has been created in respect of the shares issued in consideration for the acquisition of Leadstar Enterprises Limited. The difference between the fair value of the consideration paid and the nominal value of the 10p ordinary shares issued to the vendors of Leadstar Enterprises Limited has been credited to other reserves in the Company's books.

notes to the financial statements (continued)

For the year ended 31 December 2005

→ Other reserves

In accordance with IFRS 3, the principles of reverse acquisition accounting have been applied in the consolidated financial statements in respect of the business combination of the Company and Leadstar Enterprises Limited. The fair value of the Company's net assets and business were assessed at £2, being the book value of its assets, and therefore no goodwill arose on this transaction. The difference between the net book value of Leadstar Enterprises Limited's net assets and the nominal value of the ordinary shares issued by the Company has been credited to other reserves.

In the Company's financial statements, the difference between the fair value of the consideration paid and the nominal value of the 10p ordinary shares issued to the vendors of Leadstar Enterprises Limited has been credited to other reserves.

→ Statutory reserves

Statutory reserves comprise the following:

Statutory surplus reserve

Under People's Republic of China ("PRC") regulations and the Articles of Association of the relevant companies, companies within the Group registered in the PRC are required to transfer 10% of their profit after income tax, as determined under PRC GAAP, to the statutory surplus reserve until the reserve balance reaches 50% of its registered capital. The transfer to this reserve must be made before the distribution of dividends to equity owners. The statutory surplus reserve can be used to make up previous years' losses, if any, and may be converted into paid-in capital in proportion to the existing interests of equity owners, provided that the balance after such conversion is not less than 25% of the registered capital.

Statutory public welfare fund

According to the relevant PRC regulations and the Articles of Association of the relevant companies, companies within the Group registered in PRC are required to transfer 10% of their profit after income tax, as determined under PRC GAAP, to the statutory public welfare fund. The statutory public welfare fund is established for the purpose of providing employee facilities and other collective benefits.

→ Retained earnings

The retained earnings reserve comprises the cumulative net gains and losses recognised in the consolidated income statement.

→ Foreign currency translation reserve

The foreign currency translation reserve comprises the gains and losses arising on translating the net assets of overseas operations into pounds sterling.

26 Financial instruments

The Group is exposed to interest rate and other market risks arising in the normal course of business. The Group does not hold or issue derivative financial instruments for trading purposes or to hedge against fluctuations, if any, in interest rates and foreign exchange rates.

→ (a) Credit risk

Credit risk refers to the risk that a counter party will default on its contractual obligations resulting in a loss to the Group. The Group has adopted the policy of only dealing with creditworthy counter parties and monitors their balances.

The Group's credit risk is primarily attributable to its trade and other receivables. Cash is placed with creditworthy financial institutions. The trade and other receivables presented in the balance sheet are net of an allowance for doubtful receivables, estimated by management based on current economic conditions.

The carrying amount of financial assets recorded in the financial statements net of any allowance for doubtful receivables, represents the Group's maximum exposure to credit risk.

→ (b) Interest rate risk

Interest rate risk arises from the potential changes in interest rates that may have an adverse effect on the Group in the current reporting period and in future years.

The Group is exposed to interest rate risk through the impact of change in interest rates on interest bearing debts and interest-bearing cash. All of the Group's interest bearing debts and interest-bearing cash are at fixed rates and in RMB. The Group does not enter into any derivative instruments to hedge this risk.

→ (c) Foreign currency risk

Foreign exchange risk refers to the risk that movement in foreign currency exchange rates against the Group's functional or reporting currency will affect the Group's financial results and cash flows. Substantially all the Group's transactions are in RMB, and all of the Group's interest bearing financial assets and liabilities are in RMB.

→ (d) Liquidity risk

Liquidity risk arises from the possibility that the Group is unable to meet its obligations towards other counter parties.

The Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows.

→ (e) Fair values

The carrying amounts of the financial assets and financial liabilities in the financial statements approximate their fair values.

27 Group companies

The companies comprising the Group are as follows:

Name of the companies	Place and date of incorporation	Principal activities	Proportion of voting rights and ordinary share capital attributable to the Group at 31 December 2005
Leadstar Enterprises Limited	British Virgin Islands 18 March 2005	Investment holding	100%
Jiangsu Shuangdeng Group Co. Ltd	China, 16 September 2003	Investment holding	100%
Hong Kong Wealth Source Development Co. Ltd	Hong Kong, China, 24 September 1997	Investment holding	100%
Jiangsu Shuangdeng Power Supply Co. Ltd	China, 9 December 1995	Manufacturing, sales and development of AGM batteries	100%
Jiangsu Longyuan Shuangdeng Power Supply Co. Ltd	China, 2 August 1999	Manufacturing AGM batteries	100%
Jiangsu Fuste Power Supply Co. Ltd	China, 23 October 2001	Manufacturing and sales of GEL and GFX batteries	100%
Nanjing Shuangdeng Science and Technology R&D Institute Co. Ltd	China, 18 June 2001	Technology research and development, manufacture and sales of UPS	100%

For the year ended 31 December 2005

28 Subsequent events

On 6 January 2006, the Group acquired a further 21% interest in Beijing Full Three Dimension Power Engineering Co. Limited ("FTD") for £260,000. FTD will be accounted for as a subsidiary undertaking from that date. Further details in respect of FTD are given in note 12.

In January 2006, the Company invested £2,000,000 to form Jiangsu Best Power Supply Co. Ltd in Jiangsu Province, China. Jiangsu Best Power Supply Co. Ltd specialises in manufacturing power-aided bicycle batteries and recharging systems, power supplies and electronic equipment.

Options in respect of 100,000 new Ordinary shares of 10p each were exercised on 10 April 2006. The exercise price was 130p per share and the closing mid-market price of shares on the date of exercise was 177.5p. There was a further exercise of options in respect of a further 100,000 shares at 130p per share on 4 May.

29 Share-based payments

Equity-settled share options

1,480,000 share options were granted to certain directors and employees on flotation of the Company, and a total of 320,000 share options were granted to Seymour Pierce Limited and FT International Corporate Advisory Limited for services provided in respect of the flotation. The options granted to the directors and employees are exercisable in the period December 2008 to December 2015 and lapse thereafter or if the employee leaves the Group. The options granted to Seymour Pierce Limited and FT International Corporate Advisory Limited are exercisable at any time up to 2 years from the date of listing on AIM, and were exercisable at 31 December 2005. All the options were granted at the placing price of £1.30 per share.

	2005	
		Exercise price (£)
Granted during the period	1,800,000	1.30
Outstanding at the end of the period	1,800,000	1.30
Exercisable at the end of the period	—	—

No share options were exercised during the year. The options outstanding at 31 December 2005 had a weighted average exercise price of £1.30, and a weighted average remaining contractual life of 8.6 years.

The inputs into the Black-Scholes model are as follows:

	2005
Weighted average share price	£1.30
Weighted average exercise price	£1.30
Expected volatility	46.6%
Expected life	5.3 years
Risk free rate	4.31%

Expected volatility was determined by reference to the average volatility of comparable publicly traded companies. The expected life used in the model has been adjusted, based on the management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

The Group recognised total expenses of £145,000 related to equity-settled share-based payment transaction during the year (2004: £nil).

notice of annual general meeting

NOTICE IS HEREBY GIVEN that the first Annual General Meeting of the China Shoto plc ("the Company") will be held at 100 Cannon Street, London EC4N6EU on 20 June 2006 at 10.00am to transact the following:

Ordinary business

- 1 To receive and adopt the Company's annual report and financial statements for the financial year ended 31 December 2005, together with directors' report and the auditors' report on those financial statements.
- 2 To re-appoint BDO Stoy Hayward LLP as auditors to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting of the Company at which financial statements are laid and to authorise the directors to fix their remuneration.
- 3 To reappoint Cao Guifa, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 4 To reappoint Yang Shanji, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 5 To reappoint Zhu Shiping, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 6 To reappoint Zhou Yuezhong, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 7 To reappoint Wang Zhaobin, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 8 To reappoint Bernard Asher, who retires by rotation pursuant to Article 79 of the Company's Articles of Association and who, being eligible, offers himself for reappointment, as a Director.
- 9 To reappoint David Thomas, who has been appointed by the Board since the adoption of the Articles of Association of the Company pursuant to Article 83 of the Articles of Association of the Company, as a Director.
- 10 To reappoint Li Shuang, who has been appointed by the Board since the adoption of the Articles of Association of the Company pursuant to Article 83 of the Articles of Association of the Company, as a Director.

Special business

- 11 That for the purposes of Section 80 of the Companies Act 1985 ('the Act') the Directors be and they are generally and unconditionally authorised to exercise all the powers of the Company to allot, grant options over, offer or otherwise deal with or dispose of any relevant securities (as defined in Section 80(2) of the Act) in the capital of the Company, in substitution of all previous authorities up to a maximum amount of 8 million shares, nominal value of £800,000 to such persons and at such times and on such terms as the Directors think proper, such authority to expire on the day falling 15 months after the date of the passing of this resolution or, if earlier, at the conclusion of the Annual General Meeting of the Company to be held in 2007 unless and to the extent that such authority is renewed or extended prior to such date, provided that the Company may make an offer or agreement before the expiry of this authority which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities pursuant to such an offer or agreement as if the authority conferred hereby had not expired.

notice of annual general meeting (continued)

12 That, subject to passing of resolution 11 above, the Directors are empowered, in substitution for all previous authorities and pursuant to Section 95 of the Act to allot, grant options over, offer or otherwise deal with or dispose of equity securities (as defined in Section 94(2) of the Act) for cash as if Section 89(1) of the Act did not apply to any such allotment, grant of options, offer, dealing or disposal provided that this power shall be limited to the allotment of equity securities as follows -

(a) the allotment of equity securities in connection with any issue by way of rights or other offering where the number of equity securities to be allotted to holders of Ordinary Shares of the Company on a fixed record date is proportionate (as nearly as may be) to the number of Ordinary Shares then held by such shareholders, subject to such exclusions or other arrangements as the Directors may deem necessary or expedient to deal with legal or practical problems under the laws of, or the requirements of, any regulatory or stock exchange authority in any jurisdiction or in relation to fractional entitlements; and

(b) otherwise than pursuant to sub-paragraph (a) above, up to 8 million shares, an aggregate nominal amount of £800,000,

provided that this power shall, unless it is (prior to its expiry) duly revoked or varied or renewed by the Company in general meeting, expire on the day falling 15 months after the date of the passing of this resolution of, if earlier, at the conclusion of the Annual General Meeting of the Company to be held in 2007, save that the Company may make an offer or agreement before the expiry of this power which would or might require equity securities to be allotted after such expiry and the Directors may allot equity securities pursuant to such an offer or agreement.



By Order of the Board

David Thomas

Company Secretary

8 May 2006

NOTES

- 1 A member entitled to attend and vote at the meeting may appoint one or more proxies to attend and on a poll vote instead of him. A proxy need not be a member of the Company.
- 2 To be effective, the instrument appointing a proxy and any authority under which it is executed (or a notarially certified copy of such authority) must be deposited with the Company's registrars, Capita Registrars, not less than 48 hours before the time of the holding of the meeting or any adjournment thereof. Completion and return of the form of proxy will not preclude shareholders from attending and voting in person at the meetings.
- 3 In accordance with Regulation 41 of the Uncertificated Securities Regulations 2001, only those members entered on the register of members of the Company as at 10.00 am on 18 June 2006 shall be entitled to attend or vote at the meeting in respect of the number of shares registered in their name at that time. Or if the meeting is adjourned, such time being not more than 48 hours prior to the time fixed for the adjourned meeting. Changes to entries on the register of members after 10.00 am on 18 June 2006 shall be disregarded in determining the rights of any person to attend or vote at the meeting.
- 4 The register of interests of directors and their families in the Company's shares and copies of all directors' service contracts will be available for inspection at the registered office of the Company during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted) from the date of this Notice until the conclusion of the meeting.

Form of proxy

I/We (name in full) _____

of _____

being (a) shareholder/(s) of China Shoto plc hereby appoint the Chairman of the Meeting

or _____

as my/our proxy to vote for me/us on my/our behalf at the Annual General Meeting of the Meeting of the Company to be held at 100 Cannon Street, London EC4N6EU on 20 June 2006 at 10.00am

Please indicate with an 'X' in the space below how you wish your vote to be cast. In the absence of any specific direction, and on any other resolution or motion put to the Meeting, the proxy will, vote or abstain as the proxy thinks fit.

RESOLUTION	FOR	AGAINST
1 To receive the Annual Report and audited financial statements for the year ended 31 December 2005.		
2 To re-appoint BDO Stoy Hayward LLP as Auditors		
3 To re-elect Mr Cao Guifa as a Director		
4 To re-elect Mr Yang Shanji as a Director		
5 To re-elect Mr Zhu Shiping as a Director		
6 To re-elect Mr Zhou Yuezhang as a Director		
7 To re-elect Mr Wang Zhaobin as a Director		
8 To re-elect Mr Bernard Asher as a Director		
9 To re-elect Mr David Thomas as a Director		
10 To re-elect Mr Li Shuang as a Director		
11 To authorise the Directors to allot relevant securities in the Company pursuant to section 80 of the Companies Act 1985.		
12 To disapply the provisions of section 89 of the Companies Act 1985 in respect of the allotment of equity securities in the Company.		

Signature(s) _____

Date _____

2006

NOTES

- 1 To be valid, this Form of Proxy, duly completed, must be deposited with the Company's Registrars at, Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU, not less than 48 hours before the time appointed for the Meeting.
- 2 In the case of joint holders, only one signature is required.
- 3 In the case of a corporation, this Form of Proxy must be executed under its common seal or signed on its behalf by an attorney or officer duly authorised.
- 4 Any alteration made to this Form or Proxy must be initialled.
- 5 Completion and return of a Form of Proxy will not preclude shareholders from attending and voting in person should they subsequently decide to do so.
- 6 Any shareholder entitled to attend and vote at the above Meeting may appoint one or more proxies of his/her own choice to attend and, on a poll, to vote instead of him/her. A proxy need not be a shareholder of the Company. A shareholder completing a Form of Proxy will not thereby be precluded from attending in person instead of by proxy.

ChinaShoto plc

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