

CHINA AUTOMOTIVE SYSTEMS INC
Form 10-K
April 02, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE
SECURITIES EXCHANGE ACT OF 1934.

For the fiscal year ended December 31, 2006

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF
THE SECURITIES EXCHANGE ACT OF 1934.

For the transition period from _____ to _____.

Commission File Number 000-33123

CHINA AUTOMOTIVE SYSTEMS, INC.
(Exact name of Registrant as specified in its charter)

Delaware
(State or Other Jurisdiction
of Incorporation or Organization)

33-0885775
(I.R.S. Employer
Identification No.)

No. 1 Henglong Road, Yu Qiao Development Zone
Shashi District, Jing Zhou City Hubei Province, China
(Address of Principal Executive Offices)

434000
(Zip Code)

(86) 716-8329196

(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, \$ 0.0001 par value

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The Company's revenues for its most recent fiscal year were \$95,766,439

Aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2006, based upon the closing price of the common stock as reported on the NASDAQ Stock Market under the symbol "CAAS" on such date, was approximately \$22,855,706.

23,959,702 shares of Common Stock outstanding as of February 27, 2007.

CHINA AUTOMOTIVE SYSTEMS, INC.

FORM 10-K

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Cautionary Statement

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. These statements relate to future events or the Company's future financial performance. The Company has attempted to identify forward-looking statements by terminology including "anticipates," "believes," "expects," "can," "continue," "could," "estimates," "expects," "may," "plans," "potential," "predict," "should" or "will" or the negative of these terms or other comparable terminology. Such statements are subject to certain risks and uncertainties, including the matters set forth in this report or other reports or documents the Company files with the Securities and Exchange Commission from time to time, which could cause actual results or outcomes to differ materially from those projected. Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, the Company cannot guarantee future results, levels of activity, performance or achievements. Undue reliance should not be placed on these forward-looking statements which speak only as of the date hereof. The Company's expectations are as of the date this Form 10-K is filed, and the Company does not intend to update any of the forward-looking statements after the date this Annual Report on Form 10-K is filed to confirm these statements to actual results, unless required by law.

PART I

ITEM 1. DESCRIPTION OF BUSINESS.

COMPANY HISTORY

China Automotive Systems, Inc., "China Automotive" or the "Company", was incorporated in the State of Delaware on June 29, 1999 under the name Visions-In-Glass, Inc..

On or around March 5, 2003, the Company acquired all of the issued and outstanding equity interests of Great Genesis Holding Limited, "Genesis", a corporation organized under the laws of the Hong Kong Special Administrative Region, China, by issuance of 20,914,250 shares of common stock to certain sellers. After the acquisition, the Company continued the operations of Genesis. Genesis owns all of the capital stock of Ji Long Enterprises Investment Corp. Ltd., a Hong Kong Company, "Ji Long". Ji Long in turn owns interests in seven Sino-joint ventures, which manufacture power steering systems and/or related products for different segments of the automobile industry in China.

On May 19, 2003, the Company changed its name from Visions-In-Glass, Inc. to China Automotive Systems, Inc.

Effective July 17, 2006, Hanlin Chen, Qizhou Wu, Andy Yiu Wong Tse, Robert Tung, Haimian Cai, William E. Thomson and Guangxun Xu began serving their terms as members of the Company's Board of Directors. The newly elected directors appointed Hanlin Chen as the Chief Executive Officer and Chairman of the Board of Directors, Qizhou Wu as the Chief Operating Officer and Daming Hu as Chief Financial Officer.

BUSINESS OVERVIEW

Unless the context indicates otherwise, the Company uses the terms "the Company", "we", "our" and "us" to refer to Genesis and China Automotive collectively on a consolidated basis. The Company is a holding company and has no significant business operations or assets other than its interest in Genesis. Through Genesis, the Company manufactures power steering systems and other component parts for automobiles. All operations are conducted through seven Sino-foreign joint ventures in China. Set forth below is an organizational chart as at December 31, 2006.

China Automotive Systems, Inc.

|

(100%)

Great Genesis Holdings Limited

|

(100%)

Ji Long Enterprise Investment Limited

|

44.5%	81%	70%	51%	60%	(77.33%)	(85%)
Jingzhou Henglong Automotive Parts Co., Ltd.	Shashi Jiulong Power Steering Co., Ltd.	Shenyang Jinbei Henglong Automotive Steering System Co., Ltd.	Zhejiang Henglong & VIE Pump Co., Ltd.	Universal Sensor Application, Inc.	Wuhu Henglong Automotive Steering System Co., Ltd.	Wuhan Jielong Electric Power Steering Co., Ltd.
("Henglong")	("Jiulong")	("Shenyang")	("Zhejiang")	("USAI")	("Wuhu")	("Jielong")

Jiulong was established in 1993 and mainly engaged in the production of integral power steering gears for heavy-duty vehicles.

Henglong was established in 1997 and mainly engaged in the production of rack and pinion power steering gears for cars and light duty vehicles.

Shenyang was established in 2002 and focuses on power steering parts for light duty vehicles.

Zhejiang was established in 2002 to focus on power steering pumps.

On April 12, 2005, Great Genesis, entered into a joint-venture agreement with Shanghai Hongxi Investment Inc., "Hongxi", a company controlled by Mr. Hanlin Chen, the Company's Chairman, and Sensor System Solution Inc., "Sensor", to establish a joint venture, Universal Sensor Application Inc., "USAI", in the Wuhan East Lake Development Zone. The registered capital of the Joint-venture is \$10 million. Great Genesis and Hongxi will invest \$6 million and \$1 million, respectively, including cash and land and building, which will account for 60% and 10% of the total registered capital, respectively. Sensor will invest \$3 million in technology, accounting for 30% of the total registered capital. As of December 31, 2006, Great Genesis has contributed \$900,337, the equivalent of RMB7,200,000 and Hongxi has contributed \$436,954 in cash, the equivalent of RMB3,500,000. Even though the Company had not yet contributed 60% of the total capital, all parties had agreed that the Company was a 60% owner during 2006 and on December 31, 2006. USAI reported a net loss in 2006. Pursuant to the above joint venture agreement, Sensor has failed to contribute it's sensor-related technologies and thereby failed to fulfill it's capital contribution commitment as

of March 20, 2007. As a result Sensor has withdrawn from USAI and another technology supplier is being sought.

On April 14, 2006, Great Genesis, entered into a joint-venture agreement with Hong Kong Tongda, "Tongda", to establish a joint venture, Wuhan Jielong Electric Power Steering Co., Ltd., "Jielong", in the Wuhan East Lake Development Zone. Jielong is mainly engaged in the production and sales of electric power steering, "EPS". The registered capital of the joint-venture is \$6 million, the equivalent of RMB48,000,000. Great Genesis and Tongda will invest \$5,100,000 and \$900,000, respectively, amounting to 85% and 15% of the total registered capital, respectively. As of December 31, 2006, Great Genesis and Tongda have contributed \$765,000 and \$135,034 in cash, the equivalent of RMB6,136,830 and RMB1,081,620 respectively.

On March 31, 2006, as amended on May 2, 2006, Great Genesis, entered into a joint-venture agreement with Wuhu Chery Technology Co., Ltd., "Chery Technology", to establish a Joint-venture, Wuhu Henglong Automotive Steering System Co., Ltd in the Wuhu Technological Development Zone. Wuhu is mainly engaged in the production and sales of automobile steering system. The registered capital of the Joint-venture is \$3,750,387, the equivalent of RMB30,000,000. Great Genesis and Chery Technology will invest \$2,900,300, the equivalent of RMB23,200,000 and \$848,938, the equivalent of RMB6,800,000 respectively, which will account for 77.33% and 22.67% of the total registered capital, respectively. As of December 31, 2006, the capital of \$3,750,387, the equivalent of RMB30,000,000, has been totally contributed in Wuhu.

The Company has business relations with more than sixty vehicle manufacturers, including FAW Group and Dongfeng Auto Group, two of the five largest automobile manufacturers in China; Shenyang Brilliance Jinbei Co., Ltd., the largest van manufacturers in China; Cherry Automobile Co., Ltd, the largest state owned car manufacturer in China, and Zhejiang Geely Automobile Co., Ltd., the largest private owned car manufacturer. In 2005 and 2006, the Company has supplied the power steering pumps for SAIC GM Wuling Co., one of the Sino-Foreign joint ventures established by General Motors (GM).

The Company currently owns two trademarks covering automobile parts and twelve Chinese patents covering power steering technology. The Company is in the process of integrating new advanced technologies such as electronic chips in power steering systems into its current production line and is pursuing aggressive strategies in technology to maintain a competitive edge within the automobile industry. In 2001, the Company signed a Ten-Year Licensing Agreement with Bishop Steering Technology Limited, a leader in automotive steering gear technology innovation which is expected to offer advanced technology for steering valves within the contract period. In 2003, the Company signed a Technology Transfer Agreement with Nanyang Ind. Co. Ltd., a leading steering column maker, for the technology necessary for electronic power steering (EPS) systems. In addition, the Company established with Tsinghua University a steering systems research institute designed to develop Electronic Power Steering (EPS) and Electronic Hydraulic Steering Systems (EHPS).

STRATEGIC PLAN

The Company's short to medium term strategic plan is to focus on both domestic and international market expansion. To achieve this goal and higher profitability, the Company focuses on brand recognition, quality control, decreasing costs, research and development and strategic acquisitions. Set forth below are the Company's programs:

- Brand Recognition. Under the Henglong and Jiulong brands, the Company offers four separate series of power steering sets and 310 models of power steering sets, steering columns, steering oil pumps and steering hoses.
- Quality Control. The Henglong and Jiulong manufacturing facilities passed the ISO/TS 16949 System Certification in January 2004, a well-recognized quality control system in the auto industry developed by TUV Rheinland of Germany.
- Decrease Cost. By improving the Company's production ability and enhancing equipment management, optimizing the process and products structure, perfecting the supplier system and cutting production cost, the Company's goal is to achieve a more competitive profit margin.
- Research and Development. By partnering with Bishop Steering Technology Limited, Nanyang Ind. Co. Ltd. and Tsinghua University for the development of advanced steering systems, the Company's objective is to gain increased market share in China.
- International Expansion. The Company has entered into agreements with several international vehicle manufacturers and auto parts modules suppliers and carried on preliminary negotiations regarding future development projects.

- Acquisitions. The Company is exploring opportunities to create long-term growth through new ventures or acquisitions of other auto component manufacturers. The Company will seek acquisition targets that fulfill the following criteria:

- companies that can be easily integrated into product manufacturing and corporate management;
- companies that have strong joint venture partners that would become major customers; and
- companies involved with power steering systems, oil pump or engine-cooling systems.

CUSTOMERS

The Company's ten largest customers represent 72.6% of the Company's total sales for the year ended December 31, 2006. The following table sets forth information regarding the Company's ten largest customers.

Name of Major Customers	Percentage of Total Revenue in 2006
Chery Automobile Co., Ltd	16.4%
Brilliance China Automotive Holdings Limited	13.3%
Beiqi Foton Motor Co., Ltd.	11.1%
Zhejiang Geely Holding Co., Ltd	10.3%
Xi'an BYD Electric Car Co., Ltd	7.2%
Dongfeng Auto Group Co., Ltd	4.6%
China FAW Group Corporation	3.2%
Shanxi Heavy Auto Co., Ltd	2.5%
Shenyang Zhongshun Auto Co., Ltd	2.1%
Great Wall Motor Company Limited	1.9%
Total	72.6%

We primarily sell our products to the above-mentioned customers; we also have excellent relationships with them, including as their first-ranking supplier and developer for new product development for new models. While we intend to continue to focus on retaining and winning this business, we cannot ensure that we will succeed in doing so. It is difficult to keep these contracts as a result of severe price competition and customers' diversification of their supply base. The Company's business would be materially and adversely affected if it loses one or more of these major customers.

SALES AND MARKETING

The Company's sales and marketing team has 102 sales persons, which are divided into an original equipment manufacturing, (OEM), team, a sales service team and a working group dedicated to international business. These sales and marketing teams provide a constant interface with the Company's key customers. They are located in all major vehicle producing regions to more effectively represent the Company's customers' interests within the Company's organization, to promote their programs and to coordinate their strategies with the goal of enhancing overall service and satisfaction. The Company's ability to support its customers is further enhanced by its broad presence in terms of sales offices, manufacturing facilities, engineering technology centers and joint ventures.

The Company's sales and marketing organization and activities are designed to create overall awareness and consideration of, and therefore to increase sales of, the Company's modular systems and components. To achieve that objective, the Company organized delegations to visit the United States, Korea, India and Japan and met with potential customers. Through these activities, the Company has generated potential business interests as a strong base for future development.

DISTRIBUTION

The Company's distribution system covers all of China. The Company has established sales and service offices with certain significant customers to deal with matters related to such customers in a timely fashion. The Company also established distribution warehouses close to major customers to ensure timely deliveries. The Company maintains strict control over inventories. Each of these sales and service offices sends back to the Company through e-mail or fax information related to the inventory and customers' needs. The Company guarantees product delivery in 8 hours for those customers who are located within 200 km from the Company's distribution warehouses, and 24 hours for customers who are located outside of 200 km from the Company's distribution warehouses. Delivery time is a very important competitive factor in terms of customer decision making, together with quality, pricing and long-term relationships.

EMPLOYEES AND FACILITIES

As of December 31, 2006, the Company employed approximately 2,042 persons, including approximately 1,452 by Henglong and Jiulong, approximately 217 by Shengyan, approximately 264 by Zhejiang, approximately 43 by USAI and approximately 66 by Wuhu.

As of December 31, 2006, each of Henglong and Jiulong, Shenyang, Zhejiang and Wuhu has a manufacturing and administration area of 448,612 square meters, 35,354 square meters, 27,756 square meters, and 83,705 square meters, respectively.

Hubei Province, which is home to Dongfeng, one of the largest automakers in China, provides an ample supply of inexpensive but skilled labor to automotive-related industries. The annual production of the Company's main product, power steering gears, was approximately 450,000 units, 510,000 units and 800,000 units in 2004, 2005 and 2006 respectively. Although the production process continues to rely heavily on manual labor, the Company has invested substantially in high-level production machinery to improve capacity and production quality. Approximately \$21.5 million was spent over the last three years on professional-grade equipment -- approximately 88% of which is already in place and in use as of December 31, 2006.

RAW MATERIALS

The Company purchases various manufactured components and raw materials for use in its manufacturing processes. The principal components and raw materials the Company purchases include castings, electronic parts, molded plastic parts, finished sub-components, fabricated metal, aluminum and steel. The most important raw material is steel. The Company enters into purchase agreements with local suppliers. The annual purchase plans are determined at the beginning of the calendar year but are subject to revision every three months as a result of customers' orders. A purchase order is made according to monthly production plans. This protects the Company from building up inventory when the orders from customers change.

The Company's purchases from its ten largest suppliers represent in the aggregate 21.9% of all components and raw materials it purchased for the year ended December 31, 2006, with no single supplier providing more than 10% of total purchases.

All components and raw materials are available from numerous sources. The Company has not, in recent years, experienced any significant shortages of manufactured components or raw materials and normally does not carry inventories of these items in excess of what is reasonably required to meet its production and shipping schedules.

RESEARCH AND DEVELOPMENT

The Company has a ten-year consulting and licensing agreement with Bishop Steering Technology Ltd, one of the leading design firms in power steering systems. Bishop's technology in power steering systems is currently used by carmakers such as BMW and Mercedes Benz. Pursuant to the agreement, the Company has implemented the Bishop steering valve technology into the Henglong brand R&P power steering gear.

Henglong owns a Hubei Provincial-Level Technical Center, which is approved by the Hubei Economic Commission. The center has a staff of 122, including 12 senior engineers, 2 foreign experts and 68 engineers, primarily focused on steering system R&D, tests, production process improvement and new material and production methodology application.

In addition, the Company has partnered with Tsinghua University to establish a steering system research center, called Tsinghua Henglong Automobile Steering Research Institute, for the purposes of R&D and experimentation for Electronic-controlled Power Steering (EPS).

We believe that our engineering and technical expertise, together with our emphasis on continuing research and development, allow us to use the latest technologies, materials and processes to solve problems for our customers and to bring new, innovative products to market. We believe that continued research and development activities, including engineering, are critical to maintaining our pipeline of technologically advanced products. We have aggressively managed costs in other portions of our business in order to maintain our total expenditures for research and development activities, including engineering, at approximately \$1,100,000, \$1,000,000 and \$1,500,000 for the years ended December 31, 2006, 2005 and 2004, respectively. In 2006, the sales of newly developed products accounted for about 9.6% of total sales.

COMPETITION

The automotive components industry is extremely competitive. Criteria for the Company's customers include quality, price/cost competitiveness, system and product performance, reliability and timeliness of delivery, new product and technology development capability, excellence and flexibility in operations, degree of global and local presence, effectiveness of customer service and overall management capability. The power steering system market is fragmented in China, and the Company has seven major competitors. Of these competitors, two are Sino-foreign joint ventures while the other five are state-owned. Like many competitive industries, there is downward pressure on selling prices. For the year ended December 31, 2006, the selling price of the Company's principal products was reduced by an average of 9.5% compared with 2005.

The Company's major competitors, including Shanghai ZF and FKS, are component suppliers to specific automobile manufacturers. Shanghai ZF is the joint venture of SAIC and ZF Germany, which is an exclusive supplier to SAIC-Volkswagen and SAIC-GM. First Auto FKS is a joint venture between First Auto Group and Japan's Koyo Company and its main customer is FAW-Volkswagen Company.

While the Chinese Government limits foreign ownership of auto assemblers to 50%, there is no analogous limitation in the automotive components industry. Thus opportunities exist for foreign component suppliers to set up factories in China. These overseas competitors employ technology that may be more advanced and may have existing relationships with global automobile assemblers, but they are generally not as competitive as the Company in China in terms of production cost and flexibility in meeting client requirements.

CHINESE AUTOMOBILE INDUSTRY

The Company is a supplier of automotive parts and all of its operations are located in China. An increase or decrease in output and sales of Chinese vehicles could result in an increase or decrease of the Company's results of operations. According to the latest statistics from the China Association of Automobile Manufacturers, CAAM, in 2006, the output and sales volume of domestic made vehicles has reached 5,233,100 and 5,176,000 units respectively, with an increase of 32.76% and 30.02% compared with the same period of last year. The sales volume of national brand vehicles had reached 982,800 units, representing 25.67% of total passenger vehicles sales, an increase of 4.13% as compared with 21.54% market share in 2005. The output and sales volume of commercial vehicles has reached 2,050,000 and 2,040,000 units respectively with an increase of 15.0% and 14.0% over last year. National brand vehicles maintained a lead in the commercial vehicle market obtaining more than 96% thereof.

In 2006, due to the increased sales volume of Chinese vehicles, the Company's sales of steering gear and steering pumps for passenger vehicles increased by 50.5% and 70.6%, respectively, as compared with the corresponding period in 2005, however, the Company's sales of steering gears for commercial vehicles increased by 43.3% as compared with the corresponding period in 2005.

The Company expects that in 2007, China's automobile market will develop steadily.

Lei Jiang, the Secretary General of the China Association of Automotive Manufacturers and Chairman of the Automobile Industry of the China Council for the promotion of International Trade, predicted that in 2007, there will be healthy development for the Chinese auto market, and the output and sales of vehicles will increase by approximately 15%. Based on this prediction, management believes that the Company's net sales would increase by 15%-20%.

CHINESE ECONOMY

Management believes that the most important factor in understanding the Chinese automobile industry is the country's rapid economic growth. Chinese economic growth maintained high levels in 2006. According to data from State Statistical Bureau, the Chinese economic growth reached 10.7% in 2006. Because of the growth of the Chinese economy and the increased income level of its residents, the investment by Chinese enterprises and consumption by Chinese residents will continue to increase rapidly.

Management believes that the continued investment and consumption growth will have a favorable effect on the sales of commercial vehicles and passenger vehicles.

HIGHWAY DEVELOPMENT

Management believes that the continuing development of the highway system will have a significant positive impact on the manufacture and sale of private automobiles. Statistics from the Ministry of Communications show that 94,000 kilometers of highway and 4,300 kilometers of expressway were developed in 2006. Total highways and expressways now amount to 2,014,000 kilometers and 44,000 kilometers, respectively.

DOING BUSINESS IN CHINA

CHINESE LEGAL SYSTEM

The practical effect of the Chinese legal system on the Company's business operations in China can be viewed from two separate but intertwined considerations. First, as a matter of substantive law, the Foreign Invested Enterprise Laws provide significant protection from government interference. In addition, these laws guarantee the full enjoyment of the benefits of corporate articles and contracts to Foreign Invested Enterprise participants. These laws, however, do impose standards concerning corporate formation and governance, which are not qualitatively different from the general corporation laws of other provinces. Similarly, the Chinese accounting laws mandate accounting practices, which are not consistent with US Generally Accepted Accounting Principles. The Chinese accounting laws require that an annual "statutory audit" be performed in accordance with Chinese accounting standards and that the books of account of Foreign Invested Enterprises be maintained in accordance with Chinese accounting laws. Article 14 of the People's Republic of China Wholly Foreign-Owned Enterprise Law requires a Wholly Foreign-Owned Enterprise to submit certain periodic fiscal reports and statements to designated financial and tax authorities. Otherwise, there is risk that its business license will be revoked.

Second, while the enforcement of substantive rights may appear less clear than those in the United States, the Foreign Invested Enterprises and Wholly Foreign-Owned Enterprises are Chinese registered companies which enjoy the same status as other Chinese registered companies in business dispute resolution. Because the terms of the Company's various Articles of Association provide that all business disputes pertaining to Foreign Invested Enterprises will be resolved by the Arbitration Institute of the Stockholm Chamber of Commerce in Stockholm, Sweden applying Chinese substantive law, the Chinese minority partner in the Company's joint venture companies will not assume any advantageous position regarding such disputes. Any award rendered by this arbitration tribunal is, by the express terms of the various Articles of Association, enforceable in accordance with the "United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958)." Therefore, as a practical matter, although no assurances can be given, the Chinese legal infrastructure, while different from its United States counterpart, should not present any significant impediment to the operation of Foreign Invested Enterprises.

ECONOMIC REFORM ISSUES

Although the Chinese Government owns the majority of productive assets in China, in the past several years the Government has implemented economic reform measures that emphasize decentralization and encourage private economic activity. Because these economic reform measures may be inconsistent or ineffectual, there is no assurance that:

- The Company will be able to capitalize on economic reforms;
- The Chinese Government will continue its pursuit of economic reform policies;
- The economic policies, even if pursued, will be successful;
- Economic policies will not be significantly altered from time to time; and
- Business operations in China will not become subject to the risk of nationalization.

Negative impact resulting from economic reform policies or nationalization could result in a total investment loss in the Company's common stock.

Since 1979, the Chinese Government has reformed its economic system. Because many reforms are unprecedented or experimental, they are expected to be refined and readjusted. Other political, economic and social factors, such as political changes, changes in the rates of economic growth, unemployment or inflation, or disparities in per capita wealth between regions within China, could lead to further readjustment of the reform measures. This refining and readjustment process may negatively affect the Company's operations.

Over the last few years, China's economy has registered a high growth rate. Recently, there have been indications that the rate of inflation has increased. In response, the Chinese Government recently has taken measures to curb the excessively expansive economy. These measures included implementation of a unitary and well-managed floating exchange rate system based on market supply and demand for the exchange rates of Renminbi, restrictions on the availability of domestic credit, reduction of the purchasing capability of its citizens, and centralization of the approval process for purchases of certain limited foreign products. These austerity measures alone may not succeed in slowing down the economy's excessive expansion or control inflation, and may result in severe dislocations in the Chinese economy. The Chinese Government may adopt additional measures to further combat inflation, including the establishment of freezes or restraints on certain projects or markets.

To date reforms to China's economic system have not adversely affected the Company's operations and are not expected to adversely affect the Company's operations in the foreseeable future; however, there can be no assurance that reforms to China's economic system will continue or that the Company will not be adversely affected by changes in China's political, economic, and social conditions and by changes in policies of the Chinese Government, such as changes in laws and regulations, measures which may be introduced to control inflation, changes in the rate or method of taxation, imposition of additional restrictions on currency conversion and remittance abroad, reduction in tariff protection and other import restrictions.

ITEM 1A. RISK FACTORS.

The Company's business, financial conditions and results of operations could be materially and adversely affected by many risk factors. Because of these risk factors, actual results might differ significantly from those projected in the forward-looking statements. Factors that might cause such differences include, among others, the following:

Risks Related to the Company's Business and Industry

Because the Company is a holding company with substantially all of its operations conducted through its subsidiaries, its performance will be affected by the performance of its subsidiaries.

The Company has no operations independent of those of Great Genesis and its subsidiaries, and its principal assets are its investments in Great Genesis and its subsidiaries. As a result, the Company is dependent upon the performance of Great Genesis and its subsidiaries and will be subject to the financial, business and other factors affecting Great Genesis as well as general economic and financial conditions. As substantially all of the Company's operations are and will be conducted through its subsidiaries, it will be dependent on the cash flow of its subsidiaries to meet its obligations.

Because virtually all of the Company's assets are and will be held by operating subsidiaries, the claims of its stockholders will be structurally subordinate to all existing and future liabilities and obligations, and trade payables of such subsidiaries. In the event of the Company's bankruptcy, liquidation or reorganization, the Company's assets and those of its subsidiaries will be available to satisfy the claims of its stockholders only after all of the Company's and its subsidiaries' liabilities and obligations have been paid in full.

With the automobile parts markets being highly competitive and many of the Company's competitors having greater resources than it does, the Company may not be able to compete successfully.

The automobile parts industry is a highly competitive business. Criteria for the Company's customers include:

- Quality;
- Price/cost competitiveness;
- System and product performance;
- Reliability and timeliness of delivery;
- New product and technology development capability;
- Excellence and flexibility in operations;
- Degree of global and local presence;
- Effectiveness of customer service; and
- Overall management capability.

The Company's competitors include independent suppliers of parts, as well as suppliers formed by spin-offs from its customers, who are becoming more aggressive in selling parts to other vehicle manufacturers. Depending on the particular product, the number of the Company's competitors varies significantly. Many of the Company's competitors have substantially greater revenues and financial resources than it does, as well as stronger brand names, consumer recognition, business relationships with vehicle manufacturers, and geographic presence than it has. The Company may not be able to compete favorably and increased competition may substantially harm its business, business prospects and results of operations.

Internationally, the Company faces different market dynamics and competition. The Company may not be as successful as its competitors in generating revenues in international markets due to the lack of recognition of its products or other factors. Developing product recognition overseas is expensive and time-consuming and the Company's international expansion efforts may be more costly and less profitable than it expects. If the Company is not successful in its target markets, its sales could decline, its margins could be negatively impacted and the Company could lose market share, any of which could materially harm the Company's business, results of operations and profitability.

The cyclical nature of automotive production and sales could result in a reduction in automotive sales, which could adversely affect the Company's business and results of operations.

The Company's business relies on automotive vehicle production and sales by its customers, which are highly cyclical and depend on general economic conditions and other factors, including consumer spending and preferences. They also can be affected by labor relations issues, regulatory requirements, and other factors. In addition, in the last two years, the price of automobiles in China has generally declined. As a result, the volume of automotive production in China has fluctuated from year to year, which give rise to fluctuations in the demand for the Company's products. Any significant economic decline that results in a reduction in automotive production and sales by the Company's customers would have a material adverse effect on its results of operations. Moreover, if the prices of automobiles do not remain low, then demand for automobile parts could fall and result in lower revenues and profitability.

Increasing costs for manufactured components and raw materials may adversely affect the Company's profitability.

The Company uses a broad range of manufactured components and raw materials in its products, including castings, electronic components, finished sub-components, moulded plastic parts, fabricated metal, aluminum and steel, and resins. Because it may be difficult to pass increased prices for these items on to the Company's customers, a significant increase in the prices of the Company's components and materials could materially increase its operating costs and adversely affect its profit margins and profitability.

Pricing pressure by automobile manufacturers on their suppliers may adversely affect the Company's business and results of operations.

Recently, pricing pressure from automobile manufacturers has been prevalent in the automotive parts industry in China. Virtually all vehicle manufacturers seek price reductions each year, including requiring suppliers to pay a "3-R Guarantees" service charge for repair, replacement and refund in an amount equal to one percent of the total amount of parts supplied. Although the Company has tried to reduce costs and resist price reductions, these reductions have impacted the Company's sales and profit margins. If the Company cannot offset continued price reductions through improved operating efficiencies and reduced expenditures, price reductions will have a material adverse effect on the Company's results of operations.

The Company's business, revenues and profitability would be materially and adversely affected if it loses any of its large customers.

For the year ended December 31, 2006, approximately 16.4% of the Company's sales were to Chery Automobile Co., Ltd, approximately 13.3% were to Brilliance China Automotive Holdings Limited, approximately 11.1% were to Beiqi Foton Motor Co., Ltd, and approximately 10.3% were to Zhejiang Geely Holding Co., Ltd, the Company's four largest customers. The loss of, or significant reduction in purchases by, one or more of these major customers could adversely affect the Company's business.

The Company may be subject to product liability and warranty and recall claims, which may increase the costs of doing business and adversely affect the Company's financial condition and liquidity.

The Company may be exposed to product liability and warranty claims if its products actually or allegedly fail to perform as expected or the use of its products results, or is alleged to result, in bodily injury and/or property damage. The Company started to pay to its customers' increased after-sales service expenses due to consumer rights protection policies of "recall" issued by the Chinese Government in 2004, such as the recalling flawed vehicles policy. Beginning in 2004, automobile manufacturers unilaterally required their suppliers to pay a "3-R Guarantees" service charge (for repair, replacement and refund) in an amount equal to one percent of the total amount of parts supplied. Accordingly, the Company has experienced and shall continue to experience higher after sales service expenses. Product liability, warranty and recall costs may have a material adverse effect on the Company's financial condition.

The Company is subject to environmental and safety regulations, which may increase the Company's compliance costs and may adversely affect the Company's results of operation.

The Company is subject to the requirements of environmental and occupational safety and health laws and regulations in China. The Company cannot provide assurance that it has been or will be at all times in full compliance with all of these requirements, or that it will not incur material costs or liabilities in connection with these requirements. Additionally, these regulations may change in a manner that could have a material adverse effect on the Company's business, results of operations and financial condition. The capital requirements and other expenditures that may be necessary to comply with environmental requirements could increase and become a material expense of doing business.

Non-performance by the Company's suppliers may adversely affect its operations by delaying delivery or causing delivery failures, which may negatively affect demand, sales and profitability.

The Company purchases various types of equipment, raw materials and manufactured component parts from its suppliers. The Company would be materially and adversely affected by the failure of its suppliers to perform as expected. The Company could experience delivery delays or failures caused by production issues or delivery of non-conforming products if its suppliers failed to perform, and the Company also faces these risks in the event any of its suppliers becomes insolvent or bankrupt.

The Company's business and growth may suffer if it fails to attract and retain key personnel.

The Company's ability to operate its business and implement its strategies effectively depends on the efforts of its executive officers and other key employees. The Company depends on the continued contributions of its senior management and other key personnel. The Company's future success also depends on its ability to identify, attract and retain highly skilled technical staff, particularly engineers and other employees with electronics expertise, together with managerial, finance and marketing personnel. The Company does not maintain a key person life insurance policy on Mr. Hanlin Chen. The loss of the services of any of the Company's key employees or the failure to attract or retain other qualified personnel could substantially harm the Company's business.

The Company's management controls approximately 83.8% of its outstanding common stock and may have conflicts of interest with its minority stockholders.

Members of the Company's management beneficially own approximately 83.8% of the outstanding shares of the Company's common stock. As a result, these majority stockholders have control over decisions to enter into any corporate transaction and have the ability to prevent any transaction that requires the approval of stockholders, which could result in the approval of transactions that might not maximize stockholders' value. Additionally, these stockholders control the election of members of the Company's board, have the ability to appoint new members to the Company's management team and control the outcome of matters submitted to a vote of the holders of the Company's common stock. The interests of these majority stockholders may at times conflict with the interests of the Company's other stockholders.

There is a limited public float of the Company's common stock, which can result in its stock price being volatile and prevent the realization of a profit on resale of the Company's common stock

There is a limited public float of the Company's common stock. Of the Company's outstanding common stock, approximately 16.2% is considered part of the public float. The term "public float" refers to shares freely and actively tradable on the NASDAQ SmallCap Market and not owned by officers, directors or affiliates, as such term is defined under the Securities Act. Due to the Company's relatively small public float and the limited trading volume of its common stock, purchases and sales of relatively small amounts of the Company's common stock can have a disproportionate effect on the market price for the Company's common stock. As a result, the market price of the Company's common stock can be volatile. This stock price volatility could prevent a stockholder seeking to sell Company common stock from being able to sell it at or above the price at which the stock was bought.

Provisions in the Company's certificate of incorporation and bylaws and the General Corporation Law of Delaware may discourage a takeover attempt.

Provisions in the Company's certificate of incorporation and bylaws and the General Corporation Law of Delaware, the state in which the Company is organized, could make it difficult for a third party to acquire the Company, even if doing so might be beneficial to the Company's stockholders. Provisions of the Company's certificate of incorporation and bylaws impose various procedural and other requirements, which could make it difficult for stockholders to effect certain corporate actions and possibly prevent transactions that would maximize stockholders' value.

Risks Related to Doing Business in China and other International Countries

Because the Company's operations are all located outside of the United States and are subject to Chinese laws, any change of Chinese laws may adversely affect the Company's business.

All of the Company's operations are outside the United States and in China, which exposes it to risks, such as exchange controls and currency restrictions, currency fluctuations and devaluations, changes in local economic conditions, changes in Chinese laws and regulations, exposure to possible expropriation or other Chinese government actions, and unsettled political conditions. These factors may have a material adverse effect on the Company's operations or on the Company's business, results of operations and financial condition.

The Company's international expansion plans subject it to risks inherent in doing business internationally.

The Company's long-term business strategy relies on the expansion of the Company's international sales outside China by targeting markets, such as the United States. Risks affecting the Company's international expansion include challenges caused by distance, language and cultural differences, conflicting and changing laws and regulations, foreign laws, international import and export legislation, trading and investment policies, foreign currency

fluctuations, the burdens of complying with a wide variety of laws and regulations, protectionist laws and business practices that favor local businesses in some countries, foreign tax consequences, higher costs associated with doing business internationally, restrictions on the export or import of technology, difficulties in staffing and managing international operations, trade and tariff restrictions, and variations in tariffs, quotas, taxes and other market barriers. These risks could harm the Company's international expansion efforts, which could in turn materially and adversely affect the Company's business, operating results and financial condition.

The Company faces risks associated with currency exchange rate fluctuations, any adverse fluctuation may adversely affect the Company's operating margins.

Although the Company is incorporated in the United States, the majority of its current revenues is in Chinese currency. Conducting business in currencies other than US dollars subjects the Company to fluctuations in currency exchange rates that could have a negative impact on the Company's reported operating results. Fluctuations in the value of the US dollar relative to other currencies impact the Company's revenues, cost of revenues and operating margins and result in foreign currency translation gains and losses. Historically, the Company has not engaged in exchange rate hedging activities. Although the Company may implement hedging strategies to mitigate this risk, these strategies may not eliminate the Company's exposure to foreign exchange rate fluctuations and involve costs and risks of their own, such as ongoing management time and expertise, external costs to implement the strategy and potential accounting implications.

If relations between the United States and China worsen, the Company's stock price may decrease and the Company may have difficulty accessing the U.S. capital markets.

At various times during recent years, the United States and China have had disagreements over political and economic issues. Controversies may arise in the future between these two countries. Any political or trade controversies between the United States and China could adversely affect the market price of the Company's common stock and the Company's ability to access US capital markets.

The Chinese Government could change its policies toward private enterprise, which could adversely affect the Company's business.

The Company's business is subject to political and economic uncertainties in China and may be adversely affected by its political, economic and social developments. Over the past several years, the Chinese Government has pursued economic reform policies including the encouragement of private economic activity and greater economic decentralization. The Chinese Government may not continue to pursue these policies or may alter them to the Company's detriment from time to time. Changes in policies, laws and regulations, or in their interpretation or the imposition of confiscatory taxation, restrictions on currency conversion, restrictions or prohibitions on dividend payments to stockholders, devaluations of currency or the nationalization or other expropriation of private enterprises could have a material adverse effect on the Company's business. Nationalization or expropriation could result in the total loss of the Company's investment in China.

The economic, political and social conditions in China could affect the Company's business.

All of the Company's business, assets and operations are located in China. The economy of China differs from the economies of most developed countries in many respects, including government involvement, level of development, growth rate, control of foreign exchange, and allocation of resources. The economy of China has been transitioning from a planned economy to a more market-oriented economy. Although the Chinese Government has implemented measures recently emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets and the establishment of sound corporate governance in business enterprises, a substantial portion of productive assets in China is still owned by the Chinese Government. In addition, the Chinese Government continues to play a significant role in regulating industry by imposing industrial policies. It also exercises significant control over China's economic growth through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. Therefore, the Chinese Government's involvement in the economy could adversely affect the Company's business operations, results of operations and/or the financial condition.

The significant but uneven growth in the economy of China in the past 20 years could have an adverse effect on the Company's business and results of operations.

The Chinese Government has implemented various measures from time to time to control the rate of economic growth. Some of these measures benefit the overall economy of China, but may have a negative effect on the Company.

Government control of currency conversion and future movements in exchange rates may adversely affect the Company's operations and financial results.

The Company receives substantially all of its revenues in Renminbi, the currency of China. A portion of such revenues will be converted into other currencies to meet the Company's foreign currency obligations. Foreign exchange transactions under the Company's capital account, including principal payments in respect of foreign currency-denominated obligations, continue to be subject to significant foreign exchange controls and require the approval of the State Administration of Foreign Exchange in China. These limitations could affect the Company's ability to obtain foreign exchange through debt or equity financing, or to obtain foreign exchange for capital expenditures.

The Chinese Government controls its foreign currency reserves through restrictions on imports and conversion of Renminbi into foreign currency. Although the exchange rate of the Renminbi to the US dollar has been stable since January 1, 1994, and the Chinese Government has stated its intention to maintain the stability of the value of Renminbi, there can be no assurance that exchange rates will remain stable. The Renminbi could devalue against the US dollar. The Company's financial condition and results of operations may also be affected by changes in the value of certain currencies other than the Renminbi in which the Company's earnings and obligations are denominated. In particular, a devaluation of the Renminbi is likely to increase the portion of the Company's cash flow required to satisfy the Company's foreign currency-denominated obligations.

Because the Chinese legal system is not fully developed, the Company's legal protections may be limited.

The Chinese legal system is based on written statutes and their interpretation by the Supreme People's Court. Although the Chinese government introduced new laws and regulations to modernize its business, securities and tax systems on January 1, 1994, China does not yet possess a comprehensive body of business law. Because Chinese laws and regulations are relatively new, interpretation, implementation and enforcement of these laws and regulations involve uncertainties and inconsistencies and it may be difficult to enforce contracts. In addition, as the Chinese legal system develops, changes in such laws and regulations, their interpretation or their enforcement may have a material adverse effect on the Company's business operations. Moreover, interpretative case law does not have the same precedential value in China as in the United States, so legal compliance in China may be more difficult or expensive.

It may be difficult to serve the Company with legal process or enforce judgments against the Company's management or the Company.

All of the Company's assets are located in China and three out of the Company's directors and officers are non-residents of the United States, and all or substantial portions of the assets of such non-residents are located outside the United States. As a result, it may not be possible to effect service of process within the United States upon such persons to originate an action in the United States. Moreover, there is uncertainty that the courts of China would enforce judgments of U.S. courts against the Company, its directors or officers based on the civil liability provisions of the securities laws of the United States or any state, or an original action brought in China based upon the securities laws of the United States or any state.

Risks Related to the Standby Equity Distribution Agreement (“SEDA”)

Future sales by the Company’s stockholders may adversely affect its stock price and its ability to raise funds in new stock offerings.

Sales of the Company’s common stock in the public market following the SEDA could lower the market price of its common stock. Sales may also make it more difficult for the Company to sell equity securities or equity-related securities in the future at a time and price that management deems acceptable, or at all. Of the 23,959,702 shares of common stock outstanding as of February 27, 2007, all such shares are, or will be, freely tradable without restriction, unless held by our “affiliates.” Some of these shares may be resold under Rule 144.

Existing stockholders could experience significant dilution from the Company’s sale of shares under the SEDA.

The Company’s financial needs will be partially provided from the SEDA. The issuance of shares of the Company’s common stock under the SEDA, at below-market prices, will have a dilutive impact on its other stockholders and the issuance or even potential issuance of such shares could have a negative effect on the market price of its common stock. As a result, the Company’s net income per share could decrease in future periods, and the market price of the Company’s common stock could decline. In addition, the lower the Company’s stock price, the more shares of common stock it will have to issue under the SEDA to draw down the full amount. If the Company’s stock price is lower, then its existing stockholders would experience greater dilution.

Under the SEDA, Cornell Capital Partners will pay less than the then-prevailing market price of the Company’s common stock.

The common stock to be issued under the SEDA will be issued at a 1.5% discount to the lowest daily Volume Weighted Average Price, VWAP, of the Company’s common stock during the five consecutive trading day period immediately following the date the Company notifies Cornell Capital Partners that it desires to access the SEDA; provided, that the price per share paid by Cornell Capital Partners will in no event be less than a minimum of 90% of the closing bid price for the Company’s common stock on the trading day immediately preceding the date that it delivers an advance request. Further, Cornell Capital Partners will retain 4.5% of each advance under the SEDA. Based on this discount, Cornell Capital Partners will have an incentive to sell immediately to realize the gain on the 1.5% discount. These sales could cause the price of the Company’s common stock to decline, based on increased selling of its common stock.

The sale of the Company’s stock under the SEDA could encourage short sales by third parties, which could contribute to the future decline of the Company’s stock price.

In many circumstances, the provisions of a SEDA have the potential to cause a significant downward pressure on the price of a company’s common stock. This is especially the case if the shares being placed into the market exceed the market’s ability to take up the increased stock or if the Company has not performed in such a manner to show that the equity funds raised will be used for growth. Such an event could place further downward pressure on the price of the Company’s common stock. The Company may request numerous drawdowns pursuant to the terms of the SEDA. Even if the Company uses the SEDA to invest in ways that are materially beneficial to it, the opportunity exists for short sellers and others to contribute to the future decline of the Company’s stock price. If there are significant short sales of stock, the price decline that would result from this activity in turn may cause long holders of the stock to sell their shares thereby contributing to sales of stock in the market. If there is an imbalance on the sell side of the market for the Company’s common stock, the price will decline.

It is not possible to predict those circumstances whereby short sales could materialize or the extent to which the stock price could drop. In some companies that have been subjected to short sales the stock price has dropped significantly.

This could happen to the Company's stock price.

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Cornell Capital Partners may sell shares of the Company's common stock after it delivers an advance notice during the pricing period, which could cause the Company's stock price to decline.

Cornell Capital Partners is deemed to beneficially own the shares of common stock corresponding to a particular advance on the date that the Company delivers an advance notice to Cornell Capital Partners, which is prior to the date the stock is delivered to Cornell Capital Partners. Cornell Capital Partners may sell such shares any time after the Company delivers an advance notice. Accordingly, Cornell Capital Partners may sell such shares during the pricing period. Such sales may cause the Company's stock price to decline and if so would result in a lower VWAP during the pricing period, which would result in the Company having to issue a larger number of shares of common stock to Cornell Capital Partners in respect of the advance.

The Company may not be able to obtain a cash advance under the SEDA if Cornell Capital Partners holds more than 9.9% of the Company's common stock.

In the event Cornell Capital Partners holds more than 9.9% of our then-outstanding common stock, the Company will be unable to obtain a cash advance under the SEDA. A possibility exists that Cornell Capital Partners may own more than 9.9% of the Company's outstanding common stock at a time when it would otherwise plan to request an advance under the SEDA. In that event, if the Company is unable to obtain additional external funding, it could fail to achieve the corporate objectives that it had hoped to use the cash to achieve.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not Applicable.

ITEM 2. DESCRIPTION OF PROPERTY.

The Company's headquarters are located at No. 1 Henglong Road, Yu Qiao Development Zone Shashi District, Jing Zhou City Hubei Province, PRC. Set forth below are the manufacturing facilities operated by each joint venture. The Company has long-term rights, forty to fifty years, to use the land and owns all of the land improvements.

Name of Entity	Product	Total Area (M ²)	Building Area (M ²)	Original Cost of Equipment	Site
Henglong	Automotive Parts	395,741	20,226	\$ 17,383,308	Jingzhou City, Hubei Province
		13,393	13,707	-	Wuhan City, Hubei Province
Jiulong	Power Steering Gears	39,478	23,728	9,851,256	Jingzhou City, Hubei Province
Shenyang	Automotive Steering Gears	35,354	16,369	1,958,812	Shenyang City, Liaoning Province
Zhejiang	Steering Pumps	27,756	7,262	3,369,420	Zhuji City, Zhejiang Province
USAI	Sensor Modular	—	—	368,205	Wuhan City, Hubei Province

Wuhu	Automotive Steering Gears	83,705	15,197	8,472	Wuhu City, Anhue Province
Jielong	Electric Power Steering	—	—	33,000	Wuhan City, Hubei Province
Total		595,427	96,489	\$ 32,972,473	

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The Company is not involved in investments in (i) real estate or interests in real estate, (ii) real estate mortgages, and (iii) securities of or interests in persons primarily engaged in real estate activities, as all of its land rights are used for production purposes.

ITEM 3. LEGAL PROCEEDINGS.

The Company is not a party to any pending or to the best of the Company's knowledge, any threatened legal proceedings. No director, officer or affiliate of the Company, or owner of record of more than five percent (5%) of the securities of the Company, or any associate of any such director, officer or security holder is a party adverse to the Company or has a material interest adverse to the Company in reference to pending litigation.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

During the fiscal year 2006, we held a shareholder meeting, elected directors and approved the engagement of Schwartz Levitsky Feldman LLP as independent auditor.

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

(a) MARKET PRICES OF COMMON STOCK

The Company's common stock has been traded on the NASDAQ Small Cap market under the symbol "CAAS". The high and low bid intra-day prices of the common stock in 2006 and 2005 were reported on NASDAQ for the time periods indicated on the table below. Accordingly, the table below contains the high and low bid closing prices of the common stock as reported on the NASDAQ for the time periods indicated.

	Price Range			
	2006		2005	
	High	Low	High	Low
First Quarter	\$ 14.04	\$ 6.57	\$ 12.46	\$ 8.53
Second Quarter	11.19	6.41	9.8	6.14
Third Quarter	8.14	6.52	7.85	4.1
Fourth Quarter	\$ 12.49	\$ 6.68	\$ 10.00	\$ 4.27

The above quotations reflect inter-dealer prices, without retail mark-up, markdown or commission, and may not represent actual transactions.

(b) STOCKHOLDERS

The Company's common shares are issued in registered form. Securities Transfer Corporation in Frisco, Texas is the registrar and transfer agent for the Company's common stock. As of February 27, 2007, there were 23,959,702 shares of the Company's common stock outstanding and the Company had approximately 76 stockholders of record.

(c) DIVIDENDS

The Company has never declared or paid any cash dividends on its common stock and it does not anticipate paying any cash dividends in the foreseeable future. The Company currently intends to retain future earnings, if any, to finance operations and the expansion of its business. Any future determination to pay cash dividends will be at the discretion of the Board of Directors and will be based upon the Company's financial condition, operating results, capital requirements, plans for expansion, restrictions imposed by any financing arrangements and any other factors that the Board of Directors deems relevant.

(d) SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

The securities authorized for issuance under equity compensation plans at December 31, 2006 are as follows:

Plan category	Number of securities to be issued upon exercise of outstanding options	Weighted average exercise price of outstanding options	Number of securities remaining available for future issuance
Equity compensation plans approved by security holders	2,200,000	\$ 6.42	2,132,500

The stock options plan was approved in the 2004 Annual Meeting of Stockholders, and the maximum common shares for issuance under this plan are 2,200,000 with a period of 10 years.

ITEM 6. SELECTED FINANCIAL DATA.

The following selected financial data reflects the results of operations and balance sheet data for the years ended 2002 to 2006. The data below should be read in conjunction with, and is qualified by reference to, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and notes thereto included elsewhere in this report. The financial information presented may not be indicative of our future performance.

	Years Ended December 31,				
	2006	2005	2004	2003	2002(1)
Statement of Operations Data:					
Net sales	\$ 95,766,439	\$ 63,572,301	\$ 58,185,845	\$ 53,624,868	\$ —
Net income	4,811,704	3,315,478	6,867,337	3,871,269	4,159,000
Basic & Diluted earnings per share	0.21	0.15	0.30	0.18	0.20
Balance Sheet Data:					
Total assets	152,108,538	119,529,723	105,486,645	95,846,750	19,427,000
Total liabilities	75,615,581	60,851,575	55,776,357	51,145,176	13,330,000
Minority interests	23,112,667	21,751,043	17,571,838	18,686,712	—
Shareholders equity	\$ 53,380,290	\$ 36,927,105	\$ 32,138,450	\$ 26,014,862	\$ 6,097,000

(1). The minority joint venture partners have the right to participate in management before January 1, 2003. Pursuant to EITF 96-16, the Company accounted for its interest in these joint ventures under the equity method for the years ended December 31, 2002 and 2001. During early 2003, the directors of the Company and the other joint ventures in the Company's Sino-foreign joint ventures executed "Act in Concert" agreements, accordingly, the Company has accounted for the above joint ventures on a consolidated basis since January 1, 2003 because the Company has exercised sufficient control over their management and operations.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION.

The following is management's discussion and analysis of certain significant factors which have affected the Company's financial position and operating results during the periods included in the accompanying consolidated financial statements, as well as information relating to the plans of its current management. This report includes forward-looking statements. These statements relate to future events or the Company's future financial performance. The Company has attempted to identify forward-looking statements by terminology including "anticipates," "believes," "expects," "can," "continue," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predict," "should" or "will" or other comparable terminology. Such statements are subject to certain risks and uncertainties, including the matters set forth in this report or other reports or documents the Company files with the Securities and Exchange Commission from time to time, which could cause actual results or outcomes to differ materially from those projected. Although the Company believes that the expectations reflected in the forward-looking statements are reasonable, the Company cannot guarantee future results, levels of activity, performance or achievements. Undue reliance should not be placed on these forward-looking statements which speak only as of the date hereof. The Company undertakes no obligation to update these forward-looking statements. The Company's expectations are as of the date this Form 10-K is filed, and the Company does not intend to update any of the forward-looking statements after the date this Annual Report on Form 10-K is filed to confirm these statements to actual results, unless required by law.

The following discussion and analysis should be read in conjunction with the Company's consolidated financial statements and the related notes thereto and other financial information contained elsewhere in this Form 10-K.

GENERAL OVERVIEW:

China Automotive Systems, Inc., including, when the context so requires, its subsidiaries and the subsidiaries' interests in the Sino-foreign joint ventures described below, is referred to herein as the "Company". The Company, through its Sino-foreign joint ventures, engaged in the manufacture and sales of automotive systems and components in the People's Republic of China, the "PRC" or "China", as described below.

The Company owns the following aggregate net interests in seven Sino-foreign joint ventures organized in the PRC as of December 31, 2006.

Name of Entity	Percentage Interest		
	2006	2005	2004
Jingzhou Henglong Automotive Parts Co., Ltd."Henglong"	44.5%	44.5%	44.5%
Shashi Jiulong Power Steering Gears Co., Ltd."Jiulong"	81.0%	81.0%	81.0%
Shenyang Jinbei Henglong Automotive Steering System Co., Ltd."Shenyang"	70.0%	70.0%	70.0%
Zhejiang Henglong & Vie Pump-Manu Co., Ltd."Zhejiang"	51.0%	51.0%	51.0%
Universal Sensor Application Inc."USAI"	60.0%	60.0%	—
Wuhan Jielong Electric Power Steering Co., Ltd. ("Jielong")	85.0%	—	—
Wuhu HengLong Auto Steering System Co., Ltd. ("Wuhu")	77.33%	—	—

Jiulong and Henglong were formed in 1993 and 1997 respectively, and they are mainly engaged in the production of rack and pinion power steering gear and integral power steering gear for cars and light and heavy-duty vehicles. Shenyang and Zhejiang were established in 2002 for the production of power steering parts and power steering pumps, respectively. USAI was established in 2005 and mainly engaged in the production and sales of sensor modular. Jielong and Wuhu were established in 2006, and they are mainly engaged in the production of rack and pinion power steering gear for cars and light vehicles and electric power steering, "EPS". During 2006, USAI has entered into small batch production, Jielong and Wuhu were in the early technology and production preparation stage, and expected to start its small batch production in 2007.

Jingzhou Henglong Fulida Textile Co., Ltd. ("Jingzhou") was formed in February 2003 to produce environmental textiles and raw materials, and was owned 51% by the Company. Effective August 31, 2004, in order to concentrate on its main products, namely steering and automotive parts, the Company disposed of its 51% interest in Jingzhou by entering into an equity exchange agreement with Hubei Wanlong Investment Co., Ltd., for its 2.5% equity interest in Henglong.

The divested non-core business of Jingzhou has been treated as a discontinued operation under SFAS No. 144. Jingzhou's results of operation and related charges have been reclassified as discontinued operations in the Company's consolidated statements of operations in 2004.

RESULTS OF OPERATIONS

The following table sets forth for the periods indicated certain items from the Company's Consolidated Statements of Income expressed as a percentage of net sales and the percentage change in the dollar amount of each such item from that in the indicated previous year.

	Percentage on net sales December 31,			Change in percentage	
	2006	2005	2004	2005 to 2006	2004 to 2005
Income from continued operations:					
Net sales	100.0%	100.0%	100.0%	50.6%	9.3%
Cost of sales					