CHINA AUTOMOTIVE SYSTEMS INC
Form 10-Q
November 13, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

x **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2006

o **TRANSITION REPORT UNDER 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	**33-0885775**
(State or other jurisdiction of incorporation or organization)	(IRS employer identification number)

No. 1 Henglong Road, Yu Qiao Development Zone Shashi District,
Jing Zhou City, Hubei Province, People's Republic of China
(Address of principal executive offices)
Issuer's telephone number: (86) 716- 832- 9196
Issuer's fax number: (86) 716- 832-9298

Not Applicable
(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 x No o

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 o Accelerated filer o Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of September 30, 2006, the Company had 23,289,495 shares of common stock issued and outstanding.

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PART 1 — FINANCIAL INFORMATION

Item 1. Financial Statements

China Automotive Systems, Inc.
Condensed Consolidated Statements of Operations (Unaudited)

	Three Months Ended September 30, 2006	2005
Operating revenue:		
Net product sales, including $1,100,320 and $360,433 to related parties at September 30, 2006 and 2005, respectively	$ 22,399,673	$ 14,262,933
Net other sales (See Note 15)	341,225	525,167
	22,740,898	14,788,100
Operating cost:		
Cost of product sales, including $602,127 and $337,108 purchased from related parties at September 30, 2006 and 2005, respectively	14,266,514	8,754,017
Cost of other sales (See Note 15)	284,991	373,010
	14,551,505	9,127,027
Gross profit	8,189,393	5,661,073
Operating expenses:		
Selling expenses (See Note 15)	1,540,030	1,151,638
General and administrative expenses (See Note 15)	2,139,440	846,238
R&D expenses (See Note 15)	206,732	261,711
Depreciation and amortization (See Note 15)	904,622	607,392
	4,790,824	2,866,979
Income from operations	3,398,569	2,794,094
Non-operating income (See Note 15)	93,632	18,518
Financial (expenses)	(295,121)	(333,885)
Income before income taxes	3,197,080	2,478,727
Income taxes	470,617	597,427
Income before minority interests	2,726,463	1,881,300
Minority interests	1,194,340	804,388
Net income	$ 1,532,123	$ 1,076,912
Basic	$ 0.07	$ 0.05
Diluted	$ 0.07	$ 0.05
Weighted average number of common shares outstanding -		
Basic	23,287,049	22,574,542
Diluted	23,287,782	22,574,207

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Operations (Unaudited)

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Operating revenue:		
Net product sales, including $2,478,059 and $1,360,293 to related parties at September 30, 2006 and 2005, respectively	$ 68,112,037	$ 45,002,692
Net other sales (See Note 15)	1,154,242	1,248,758
	69,266,279	46,251,450
Operating cost:		
Cost of product sales, including $1,932,329 and $1,232,897 purchased from related parties at September 30, 2006 and 2005, respectively	43,762,536	28,496,684
Cost of other sales (See Note 15)	897,406	1,048,245
	44,659,942	29,544,929
Gross profit	24,606,337	16,706,521
Operating expenses:		
Selling expenses (See Note 15)	5,419,420	3,818,669
General and administrative expenses (See Note 15)	6,529,130	4,010,754
R&D expenses (See Note 15)	647,873	757,660
Depreciation and amortization (See Note 15)	2,846,716	1,992,163
	15,443,139	10,579,246
Income from operations	9,163,198	6,127,275
Non-operating income (See Note 15)	94,257	27,183
Financial (expenses)	(806,984)	(941,486)
Income before income taxes	8,450,471	5,212,972
Income taxes	1,522,067	1,150,750
Income before minority interests	6,928,404	4,062,222
Minority interests	3,550,247	1,617,073
Net income	$ 3,378,157	$ 2,445,149
Basic	$ 0.15	$ 0.11
Diluted	$ 0.15	$ 0.11
Weighted average number of common shares outstanding -		
Basic	23,076,215	22,574,542
Diluted	23,084,675	22,585,732

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended September 30,	
	2006	**2005**
Net income	$ 1,532,123	$ 1,076,912
Other comprehensive income:		
Foreign currency translation gain	—	1,329,624
Comprehensive income	$ 1,532,123	$ 2,406,536

	Nine Months Ended September 30,	
	2006	**2005**
Net income	$ 3,378,157	$ 2,445,149
Other comprehensive income:		
Foreign currency translation gain	601,399	1,329,624
Comprehensive income	$ 3,979,556	$ 3,774,773

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Balance Sheets

		September 30, 2006 (Unaudited)		December 31, 2005
ASSETS				
Current assets:				
Cash and cash equivalents	$	18,424,513	$	12,374,944
Pledged cash deposits		3,533,732		1,185,660
Accounts and notes receivable, net, including $3,583,158 and $1,829,075 from related parties at September 30, 2006 and December 31, 2005, respectively, net of an allowance for doubtful accounts of $3,677,533 and $2,856,025 at September 30, 2006 and December 31, 2005, respectively		50,702,026		41,580,320
Advance payments and other, including $342,135 and $312,036 to related parties at September 30, 2006 and December 31, 2005, respectively (See note 15)		1,475,131		1,029,892
Inventories		17,514,260		12,385,833
Total current assets		91,649,662		68,556,649
Long-term Assets:				
Property, plant and equipment, net		38,349,268		39,796,033
Intangible assets, net		3,111,854		3,503,217
Other receivables, net, including $4,274,201 and $3,570,461 from related parties at September 30, 2006 and December 31, 2005, respectively, net of an allowance for doubtful accounts of $2,123,525 and $1,040,169 at September 30, 2006 and December 31, 2005, respectively		5,104,002		6,503,629
Advance payment for property, plant and equipment, including $705,388 and $599,729 to related parties at September 30, 2006 and December 31, 2005, respectively (See note 15)		3,040,858		1,096,121
Long-term investments		67,832		74,074
Total assets	$	141,323,476	$	119,529,723
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Bank loans	$	16,229,713	$	14,814,815
Accounts and notes payable, including $541,233 and $383,578 to related parties at September 30, 2006 and December 31, 2005, respectively		35,103,991		31,375,599
Customer deposits		288,564		157,919
Accrued payroll and related costs		1,504,462		1,418,093
Accrued expenses and other payables		6,119,563		5,191,617
Accrued pension costs		2,900,333		2,653,064

Taxes payable		5,206,614		4,172,212
Amounts due to shareholders/directors		259,525		766,642
Total current liabilities		67,612,765		60,549,961
Long-term liabilities:				
Advances payable		301,552		301,614
Total liabilities	$	67,914,317	$	60,851,575
Minority interests		27,343,634		21,751,043
Stockholders' equity:				
Preferred stock, $0.0001 par value-				
Authorized - 20,000,000 shares				
Issued and outstanding - None				
Common stock, $0.0001 par value-				
Authorized - 80,000,000 shares				
Issued and outstanding-				
23,289,495 and 22,574,543 shares at September 30, 2006 and December 31, 2005, respectively				
Common stock, $0.0001 par value-		2,329		2,257
Additional paid-in capital		23,305,514		18,146,721
Retained earnings-				
Appropriated		5,078,584		4,923,262
Unappropriated		15,745,015		12,522,181
Accumulated other comprehensive income		1,934,083		1,332,684
Total stockholders' equity		46,065,525		36,927,105
Total liabilities and stockholders' equity	$	141,323,476	$	119,529,723

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005
Cash flows from operating activities:		
Net income from continuing operations	$ 1,532,123	$ 1,076,912
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Minority interests	1,194,340	804,388
Stock-based compensation	131,625	—
Depreciation and amortization	1,542,239	1,369,361
Allowance for doubtful accounts (Recovered)	597,562	(200,064)
Provision for long-term investment	6,242	—
Changes in operating assets and liabilities:		
Increase (decrease) in:		
Pledged deposits	(1,686,315)	351,506
Accounts and notes receivable	1,906,905	(210,405)
Advance payments and others (See Note 15)	(491,501)	(190,466)
Inventories	(2,761,466)	(582,850)
Increase (decrease) in:		
Accounts and notes payable	(392,539)	(506,416)
Customer deposits	(478,404)	(30,844)
Accrued payroll and related costs	37,869	98,878
Accrued expenses and other payables	130,925	490,683
Accrued pension costs	66,395	46,947
Taxes payable	(41,763)	548,184
Advances payable		4,845
Net cash provided by (used in) operating activities (See Note 15)	1,294,237	3,070,659
Cash flows from investing activities:		
(Increase) decrease in other receivables	181,408	(244,453)
Cash paid to acquire property, plant and equipment (See Note 15)	(2,723,803)	(3,003,243)
Cash paid to acquire intangible assets	(1,437)	(4,794)
Cash received from other investing activities	(3,920)	—
Net cash provided by (used in) investing activities (See Note 15)	(2,547,752)	(3,252,490)
Cash flows from financing activities:		
Increase (decrease) in proceeds from bank loans	—	1,802,767
Dividends be paid to the minority interest holders of Joint-venture companies	(124,844)	—
Increase (decrease) in amounts due to shareholders/directors	(55,979)	23,712
Proceeds from issuance of common stock	67,500	—
Capital Contribution from the minority interest holders of Joint-venture companies	(1,149)	—
Net cash provided by (used in) financing activities (See Note 15)	(114,472)	1,826,479
Cash and cash equivalents effected by foreign currency (See Note 15)	—	1,327,839
Increase (decrease) in cash and cash equivalents	(1,367,987)	2,972,487
Cash and cash equivalents at the beginning of period	19,792,500	11,055,235
Cash and cash equivalents at the end of period	$ 18,424,513	$ 14,027,722

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China Automotive Systems, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited) (continued)

	Three Months Ended September 30,	
	2006	**2005**
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	$ 154,787	$ 268,141
Cash paid for income taxes	$ 556,212	$ 116,192

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc.
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Nine months Ended September 30, 2006	2005
Cash flows from operating activities:		
Net income	$ 3,378,157	$ 2,445,149
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Minority interests	3,550,247	1,617,073
Stock-based compensation	131,625	68,850
Depreciation and amortization	4,876,558	3,661,800
Allowance for doubtful accounts (Recovered)	1,861,107	(2,743)
Provision for long-term investment	6,242	—
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Pledged deposits	(2,348,072)	(671,834)
Accounts and notes receivable	(9,911,144)	3,663,852
Advance payments and others (See Note 15)	(445,239)	72,155
Inventories	(5,128,427)	(2,611,827)
Increase (decrease) in:		
Accounts and notes payable	3,728,392	1,264,891
Customer deposits	130,645	(105,194)
Accrued payroll and related costs	86,369	120,371
Accrued expenses and other payables	2,413,794	178,328
Accrued pension costs	247,269	701,083
Taxes payable	1,034,402	347,760
Advances payable	(62)	4,689
Net cash provided by (used in) operating activities (See Note 15)	3,611,863	10,754,403
Cash flows from investing activities:		
(Increase) decrease in other receivables	275,791	(1,510,417)
Cash paid to acquire property, plant and equipment (See Note 15)	(4,790,102)	(8,001,096)
Cash paid to acquire intangible assets	(140,899)	(198,939)
Net cash provided by (used in) investing activities (See Note 15)	(4,655,210)	(9,710,452)
Cash flows from financing activities:		
Increase (decrease) in proceeds from bank loans	1,414,898	1,200,357
Dividends be paid to the minority interest holders of Joint-venture companies	(864,430)	(787,321)
Increase (decrease) in amounts due to shareholders/directors	(507,117)	78,257
Proceeds from issuance of common stock	5,027,240	—
Capital Contribution from the minority interest holders of Joint-venture companies	1,420,926	—
Net cash provided by (used in) financing activities (See Note 15)	6,491,517	491,293
Effect of exchange rate fluctuations on cash and cash equivalents (See Note 15)	601,399	1,327,839
Increase (decrease) in cash and cash equivalents	6,049,569	2,863,083
Cash and cash equivalents at the beginning of period	12,374,944	11,164,639

Cash and cash equivalents at the end of period	$	18,424,513	$	14,027,722

China Automotive Systems, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited) (continued)

	Nine months Ended September 30,			
		2006		**2005**
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:				
Cash paid for interest	$	596,871	$	649,424
Cash paid for income taxes	$	958,507	$	789,537
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:				
Issuance of common shares on a non-cash basis	$	4	$	—
Financing services fee related to issuance of common shares	$	(4)	$	—
Increase in capital by minority shareholders of Joint-venture Companies	$	921,785	$	—
Dividends payable to minority shareholders of Joint-venture Companies being converted into capital	$	(921,785)	$	—

The accompanying notes are an integral part of these condensed consolidated financial statements.

China Automotive Systems, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
September 30, 2006

1. ORGANIZATION AND BASIS OF PRESENTATION

Organization - Effective March 5, 2003, Visions-In-Glass, Inc., a United States company incorporated in the State of Delaware, “Visions”, entered into a Share Exchange Agreement to acquire 100% of the shareholder interest in Great Genesis Holding Limited, a company incorporated on January 3, 2003 under the Companies Ordinance in Hong Kong as a limited liability company, “Great Genesis”, as a result of which Great Genesis became a wholly-owned subsidiary of Visions. At the closing, the former directors and officers of Visions resigned, and new directors and officers were appointed. Visions subsequently changed its name to China Automotive Systems, Inc.

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 described below, is engaged in the manufacture and sale of automotive systems and components in the People’s Republic of China, the “PRC” or “China”, as described below.

As of September 30, 2006 and 2005, Great Genesis owns the following aggregate net interests in seven Sino-foreign Joint-ventures organized in the PRC:

	Percentage Interest September 30,	
Name of Entity	**2006**	**2005**
Shashi Jiulong Power Steering Co. Limited ("Jiulong")	81.0%	81.0%
Jingzhou Henglong Automotive Parts Co. Limited ("Henglong")	44.5%	44.5%
Shenyang Jinbei Henglong Automotive Steering System Co. Limited ("Shenyang")	70.0%	70.0%
Zhejiang Henglong & Vie Pump-Manu Co. Limited ("Zhejiang")	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 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, the wholly-owned subsidiary of the company, 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 September 30, 2006, Great Genesis has contributed $900,337, the equivalent of RMB7,200,000, Sensor has contributed $3,000,000, and Hongxi has contributed $436,954 in cash, the equivalent of RMB3,500,000.

On April 14, 2006, the wholly-owned subsidiary of the company, 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 September 30, 2006, Great Genesis and Tongda have contributed $766,146 and $135,034 in cash, the equivalent of RMB6,120,000 and RMB1,080,000 respectively.

On March 31, 2006, as amended on May 2, 2006, Great Genesis, the wholly-owned subsidiary of the Company, 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 and $850,087, respectively, which will account for 77.33% and 22.67% of the total registered capital, respectively. As of September 30, 2006, the capital of $3,750,387, the equivalent of RMB30,000,000, has been totally contributed in Wuhu.

Basis of Presentation - For the three months and nine months ended September 30, 2006 and 2005, the accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. The subsidiaries include the seven Sino-foreign Joint-ventures mentioned in Note 1. Significant inter-company balances and transactions have been eliminated upon consolidation. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America.

Foreign Currencies - The Company maintains its books and records in Renminbi, “RMB”, the currency of the PRC, its functional currency. Foreign currency transactions in RMB are reflected using the temporal method. Under this method, all monetary items are translated into the functional currency at the rate of exchange prevailing at the balance sheet date. Non-monetary items are translated at historical rates. Income and expenses are translated at the rate in effect on the transaction dates. Transaction gains and losses, if any, are included in the determination of net income (loss) for the period.

In translating the financial statements of the Company from its functional currency into its reporting currency in United States dollars, balance sheet accounts are translated using the closing exchange rate in effect at the balance sheet date and income and expense accounts are translated using an average exchange rate prevailing during the reporting period. Adjustments resulting from the translation, if any, are included in cumulative other comprehensive income (loss) in stockholders’ equity.

Exchange rate used in translating the financial statements of the Company from its functional currency, “Renminbi”, into its reporting currency, “US Dollars”:

Reporting Period		**Renminbi**		**US Dollars**
Prior to July 1, 2005	$	1	$	0.1205
From July 1, 2005 to December 31, 2005	$	1	$	0.1233
From January 1, 2006 to September 30, 2006	$	1	$	0.1248

Comments - The accompanying interim condensed consolidated financial statements are unaudited, but in the opinion of management of the Company, contain all adjustments, which include normal recurring adjustments, necessary to present fairly the financial position, the results of operations and cash flows for the three months and nine months ended September 30, 2006.

The consolidated balance sheet as of December 31, 2005 is derived from the Company’s audited financial statements.

Certain information and footnote disclosures normally included in financial statements that have been prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, although the Company’s management believes that the disclosures contained in these financial statements are adequate to make the information presented therein not misleading. For further information, refer to the financial statements and the notes thereto included in the Company’s 2005 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The results of operations for the three months and nine months ended September 30, 2006 are not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2006.

Income Per Share - Basic income per share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted income per share is calculated assuming the issuance of common shares, if dilutive, resulting from the exercise of warrants.

Actual weighted average shares outstanding used in calculating basic and diluted earnings (loss) per share were:

	Three Months Ended September 30,	
	2006	**2005**
Weighted average shares outstanding	23,287,049	22,574,542
Effect of dilutive securities	733	665
Diluted shares outstanding	23,287,782	22,575,207

	Nine months Ended September 30,	
	2006	**2005**
Weighted average shares outstanding	23,076,215	22,574,542
Effect of dilutive securities	8,460	11,190
Diluted shares outstanding	23,084,675	22,585,732

The 156,250 shares underlying warrants issued to Cornell Capital Partners, LP on March 20, 2006 and 22,500 shares options issued to three independent directors on July 6, 2006 have not been included in the computation of diluted earnings (loss) per share because such inclusion would have had an anti-dilutive effect:

	Three Months Ended September 30,	
	2006	**2005**
Anti-dilutive securities	200,819	—

	Nine months Ended September 30,	
	2006	**2005**
Anti-dilutive securities	131,719	—

Stock-Based Compensation - The Company may issue stock options to employees and stock options or warrants to non-employees in non-capital raising transactions for services and for financing costs.

On March 20, 2006, the Company issued 37,863 shares of common stock to Cornell Capital Partners, LP and a placement agent in non-capital raising transactions, collectively at an exercise price of $11.885 per share as a commitment fee and a placement agent fee of $450,000 in connection with the establishment of a $15,000,000 equity line of credit under a Standby Equity Distribution Agreement with Cornell Capital Partners, LP. The exercise value of $450,000 by issuing 37,863 shares of common stock were regarded as financing expenses and has been debited to additional paid-in capital. The excess of exercise value over par value, $449,996 has been credited to additional paid-in capital.

The Company has adopted Statement of Financial Accounting Standards (“SFAS”) No. 123R, “Accounting for Stock-Based Compensation”, which establishes a fair value method of accounting for stock-based compensation plans. In accordance with SFAS No. 123R, the cost of stock options and warrants issued to employees and non-employees is measured at the grant date based on the fair value. The fair value is determined using the Black-Scholes option pricing model. The resulting amount is charged to expense on the straight-line basis over the period in which the Company expects to receive benefit, which is generally the vesting period.

The weighted-average fair value of options granted during the periods 2006, 2005 and 2004 was $5.85, $3.06 and $2.45, respectively. The fair value of each option grant was estimated on the date of grant using option valuation model and assumptions noted in the table:

	2006	2005	2004
Expected volatility	93.19%	46.0%	121.6%
Risk-free rate	4.75%	3.6%	4.0%
Expected term (years)	5	5	2
Dividend yield	0.0%	0.0%	0.0%

The weighted average fair value of warranties issued during the periods 2006 was $5.33. The fair value of warrant grant was estimated on the date of grant using option valuation model and assumptions noted in the table:

Expected volatility	Risk-free rate	Expected term (years)	Dividend yield
82.20%	4.66%	3	0%

On March 20, 2006, the Company raised a gross amount of $5,000,000 in a private placement (PIPE) to Cornell Capital Partners, LP, "Investor" by issuing 625,000 shares of common stock. As part of the financing cost, the Company issued a warrant to purchase 86,806 shares of common stock, exercisable for three years at an exercise price of $14.40 per share, and a warrant to purchase 69,444 shares of common stock, exercisable for three years at an exercise price of $18.00 per share, to Cornell Capital Partners, LP. The fair value of above-mentioned warrant at the grant date is $832,639, which was measured based on Black-Scholes option pricing model. This amount was recorded as financing expenses and debited to additional paid-in capital. Additionally, the same amount was credited to additional paid-in capital, resulting in zero effect on additional paid-in capital and the Consolidated Financial Statements.

On July 6, 2006, the Company issued options to purchase 7,500 shares of common stock to each of its three independent directors. Such stock options vest immediately upon grant and are exercisable at $7.94 per share over a period of five years. The fair value of the options at the grant date being $131,625 which was measured based on Black-Scholes option pricing model. The fair value was recorded as compensation expenses. This amount has been debited to operating expenses and credited to additional paid-in capital.

A summary of option activities under the plans to September 30, 2006 was as follows:

	Shares	Weighted-Average Exercise Price	Weighted-Average Contractual Term (years)
Outstanding - January 1, 2005	22,500	$ 4.50	2
Granted	22,500	6.83	5
Exercised	—	—	—
Cancelled	—	—	—
Outstanding - December 31, 2005	45,000	5.67	3.5
Granted	178,750	14.99	3.3
Exercised	(22,500)	4.50	—
Cancelled	—	—	—
Outstanding - September 30, 2006	201,250	14.07	3.4
Exercisable options-September 30, 2006	22,500	$ 6.83	5

The following is a summary of the range of exercise prices for stock options that are outstanding and exercisable at September 30, 2006:

Range of Exercise Prices	Outstanding Stock Options	Weighted Average Remaining Life	Weighted Average Exercise Price	Number of Stock Options Exercisable	Weighted Average Exercise Price
\$4.50 - \$10.00	45,000	4.26	\$ 7.39	22,500	\$ 6.83
\$10.01 - \$20.00	156,250	2.47	16.00	—	—
	201,250		\$ 14.07	22,500	\$ 6.83

Product Warranties - The Company provided for the estimated cost of product warranties when the products were sold. Such estimates of product warranties were based on, among other things, historical experience, product changes, material expenses, service and transportation expenses arising from the changed product. Our estimates will be adjusted on the basis of actual claims and circumstances.

For the year ended December 31, 2005 and nine months ended September 30, 2006, the warranties activities were as follows:

	September 30, 2006	December 31, 2005
Balance at the beginning of year	\$ 1,787,869	\$ 548,390
Additions during the reporting period	2,346,672	1,787,870
Previous record for warranty, including estimation change	433,359	—
Settlement within reporting period, by cash or actual material	(1,500,220)	(561,931)
Foreign currency translation	20,088	13,540
Balance at the end of period	\$ 3,087,768	\$ 1,787,869

The Company has recorded \$ 3,087,768 and \$1,787,869 product warranty reserves for the periods ended September 30, 2006 and December 31, 2005, which were included in the accrued liabilities in the accompanying consolidated financial statements.

Comprehensive Income - The Company has adopted the provisions of Statement of Financial Accounting Standards No. 130, “Reporting Comprehensive Income” (“SFAS No. 130”). SFAS No. 130 which establishes standards for the reporting and disclosure of comprehensive income, its components and accumulated balances in a full set of general purpose financial statements. SFAS No. 130 defines comprehensive income to include all changes in equity except those resulting from investments by owners and distributions to owners, including adjustments to minimum pension liabilities, accumulated foreign currency translation, and unrealized gains or losses on marketable securities.

For the three months and nine months ended September 30, 2006, the Company’s only component of other comprehensive income is foreign currency translation gain of \$0 and \$601,399. These amounts have been recorded as a separate component of stockholders’ equity. For the three months and nine months ended September 30, 2005, the Company’s only component of other comprehensive income is foreign currency translation gain of \$1,329,624 and \$1,329,624.

Reclassifications - Certain reclassifications have been made to the Consolidated Statements of OperationsôConsolidated Statements of Cash Flows and Consolidated Balance Sheets for the three months and nine months ended September 30, 2005 to conform to the current year presentation. (See Note 15)

2. CERTAIN SIGNIFICANT RISKS AND UNCERTAINTIES

The Company is subject to the consideration and risks of operating in the PRC. These include risks associated with the political and economic environment, foreign currency exchange and the legal system in the PRC.

The economy of the PRC differs significantly from the economies of the "western" industrialized nations in structure, level of development, gross national product, growth rate, capital investment, resource allocation, self-sufficiency, rate of inflation and balance of payments position, among others. Only recently has the PRC government encouraged substantial private economic activities. The Chinese economy has experienced significant growth in the past several years, but such growth has been uneven among various sectors of the economy and geographic regions. Actions by the PRC government to control inflation have significantly restrained economic expansion in the recent past. Similar actions by the PRC government in the future could have a significant adverse effect on economic conditions in the PRC.

Many laws and regulations dealing with economic matters in general and foreign investment in particular have been enacted in the PRC. However, the PRC still does not have a comprehensive system of laws, and enforcement of existing laws may be uncertain and sporadic.

The Company's operating assets and primary sources of income and cash flows are the interests of its subsidiaries in Sino-foreign Joint-ventures in the PRC. The PRC economy has been, for many years, a centrally-planned economy, operating on the basis of annual, five-year and ten-year state plans adopted by central PRC governmental authorities, which set out national production and development targets. The PRC government has been pursuing economic reforms since it first adopted its "open-door" policy in 1978. There is no assurance that the PRC government will continue to pursue economic reforms or that there will not be any significant change in its economic or other policies, particularly in the event of any change in the political leadership of, or the political, economic or social conditions in the PRC. There is also no assurance that the Company will not be adversely affected by any such change in governmental policies or any unfavorable change in the political, economic or social conditions, the laws or regulations, or the rate or method of taxation in the PRC.

As many of the economic reforms, which have been or are being implemented by the PRC government, are unprecedented or experimental, they may be subject to adjustment or refinement, which may have adverse effects on the Company. Further, through state plans and other economic and fiscal measures such as the level of exchange rate, it remains possible for the PRC government to exert significant influence on the PRC economy.

The Company's financial instruments that are exposed to concentration of credit risk consist primarily of cash and cash equivalents, and accounts receivable from customers. Cash and cash equivalents are maintained with major banks in the PRC. The Company's business activity is with customers in the PRC. The Company periodically performs credit analysis and monitors the financial condition of its clients in order to minimize credit risk.

Any devaluation of the RMB against the United States dollar would have adverse effects on the Company's financial performance and asset values when measured in terms of the United States dollar. Should the RMB significantly devalue against the United States dollar, such devaluation could have a material adverse effect on the Company's earnings and the foreign currency equivalent of such earnings. The Company does not hedge its RMB - United States dollar exchange rate exposure.

On July 21, 2005, the People's Bank of China changed its exchange rate system from its previous fixed exchange rate announced on January 1, 1994 to a unitary and well-managed floating exchange rate based on market supply and demand. No representation is made that the RMB amounts could be freely converted into other foreign currencies. All foreign exchange transactions continue to take place either through the Bank of China or other banks authorized to buy and sell foreign currencies at the exchange rate quoted by the People's Bank of China. Approval of foreign currency payments by the People's Bank of China or other institutions requires submission of a payment application form together with suppliers' invoices, shipping documents and signed contracts.

3. RECENT ACCOUNTING PRONOUNCEMENTS

In 2003, the FASB issued SFAS No. 132R, "Employers' Disclosures about Pensions and Other Postretirement Benefits (Revised in December 2003)" - an amendment of FASB Statements No. 87, 88, and 106 (Issued 12/03). This Statement revises employers' disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans required by FASB Statements No. 87, Employers' Accounting for Pensions, No. 88, Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits, and No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions. SFAS 132R is effective for fiscal years beginning after December 15, 2003. The adoption of SFAS No. 132R did not have a significant effect on the Company's financial statement presentation or disclosures.

In November 2004, the FASB issued SFAS No. 151, “Inventory Costs — An Amendment of Accounting Research Bulletin No. 43, Chapter 4” (SFAS 151). SFAS 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and spoilage should be expensed as incurred and not included in overhead as an inventory cost. The new statement also requires that allocation of fixed production overhead costs to conversion costs should be based on normal capacity of the production facilities. The provisions in SFAS 151 must be applied prospectively and became effective for the Company beginning January 1, 2006. The Company adopted this statement beginning in the first quarter of 2006.

In December 2004, the FASB issued SFAS No. 152 “Accounting for Real Estate Time-Sharing Transactions - an amendment of FASB Statements No. 66 and 67” (“SFAS 152”). This statement amends FASB Statement No. 66 “Accounting for Sales of Real Estate” to reference the financial accounting and reporting guidance for real estate time-sharing transactions that is provided in AICPA Statement of Position 04-2 “Accounting for Real Estate Time-Sharing Transactions” (“SOP 04-2”). SFAS 152 also amends FASB Statement No. 67 “Accounting for Costs and Initial Rental operations of Real Estate Projects” to state that the guidance for incidental operations and costs incurred to sell real estate projects does not apply to real estate time-sharing transactions, with the accounting for those operations and costs being subject to the guidance in SOP 04-2. The provisions of SFAS 152 are effective in fiscal years beginning after June 15, 2005. The Company adopted this statement beginning in the first quarter of 2006.

In December 2004, the FASB issued SFAS No. 123 (Revised 2004), “Share-Based Payment” (SFAS 123R). This statement requires financial statement recognition of compensation cost related to share-based payment transactions. Share-based payment transactions within the scope of SFAS 123R include stock options, restricted stock plans, performance-based awards, stock appreciation rights, and employee share purchase plans. The provisions of SFAS 123R are effective for the first fiscal year beginning after June 15, 2005. However, in April 2005, the SEC deferred the effective date of SFAS 123R for SEC registrants to the first interim period beginning after June 15, 2005. Accordingly, the Company adopted this statement beginning in the first quarter of 2006.

In December 2004, the FASB issued SFAS No. 153 “Exchanges of Nonmonetary Assets, an amendment of Accounting Principles Board Opinion No. 29” (SFAS 153). This statement amends Accounting Principles Board Opinion (APB) No. 29, “Accounting for Nonmonetary Transactions” to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that have no commercial substance. Under SFAS 153, if a nonmonetary exchange of similar productive assets meets a commercial-substance criterion and fair value is determinable, the transaction must be accounted for at fair value resulting in recognition of any gain or loss. SFAS 153 was effective for nonmonetary transactions in fiscal periods beginning after June 15, 2005. The Company adopted this statement beginning in the first quarter of 2006.

In March 2005, the FASB issued Interpretation No. 47, “Accounting for Conditional Asset Retirement Obligations, an Interpretation of FASB Statement No. 143” (FIN 47). Under FIN 47, we are required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. Any uncertainty about the amount and/or timing of future settlement should be factored into the measurement of the liability when sufficient information exists. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value. The provisions of FIN 47 were required to be applied no later than the end of fiscal years ending after December 15, 2005. The Company adopted this statement beginning in the first quarter of 2006.

In May 2005, the FASB issued SFAS No. 154, “Accounting Changes and Error Corrections — a replacement of APB Opinion No. 20 and FASB Statement No. 3” (SFAS 154). This statement changes the requirements for the accounting for and reporting of a change in accounting principle and applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. APB No. 20 required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. This statement requires retrospective application to prior period financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. The provisions of SFAS 154 are effective for fiscal years beginning after December 15, 2005. The Company adopted this statement beginning in the first quarter of 2006.

In February 2006, the FASB issued SFAS No. 155, “Accounting for Certain Hybrid Financial Instruments”. This Statement amends FASB Statements No. 133, Accounting for Derivative Instruments and Hedging Activities, and No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. This Statement resolves issues addressed in Statement 133 Implementation Issue No. D1, “Application of Statement 133 to

Beneficial Interests in Securitized Financial Assets." SFAS No. 155 permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement 133, and establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation. It also clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives and amends Statement 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company has not yet determined the impact of the adoption of SFAS No. 155 on its financial statements, if any.

In 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets". This Statement amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities. This Statement requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in indicated situations; requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable; permits an entity to choose relevant subsequent measurement methods for each class of separately recognized servicing assets and servicing liabilities; at its initial adoption, permits a one-time reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights, without calling into question the treatment of other available-for-sale securities under Statement 115, provided that the available-for-sale securities are identified in some manner as offsetting the entity's exposure to changes in fair value of servicing assets or servicing liabilities that a servicer elects to subsequently measure at fair value; and requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional disclosures for all separately recognized servicing assets and servicing liabilities. The adoption of SFAS No. 156 did not have a material impact on our Consolidated Financial Statements.

4. ACCOUNTS AND NOTES RECEIVABLE

The Company's accounts and notes receivable at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	September 30, 2006	**December 31, 2005**
Accounts receivable	$ 36,769,824	$ 31,866,156
Notes receivable	17,609,755	12,570,189
	54,379,579	44,436,345
Less: allowance for doubtful accounts	(3,677,553)	(2,856,025)
	$ 50,702,026	$ 41,580,320

Notes receivable represent accounts receivable in the form of bills of exchange whose acceptances and settlements are handled by banks.

5. OTHER RECEIVABLES

The Company's other receivable at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	September 30, 2006	**December 31, 2005**
Other receivable	$ 7,227,527	$ 7,543,798
Less: allowance for doubtful accounts	(2,123,525)	(1,040,169)
	$ 5,104,002	$ 6,503,629

Other receivables consist of amounts advanced to both related and unrelated parties, primarily as unsecured demand loans, with no stated interest rate or due date.

Loan amounts receivable from related parties: As of September 30, 2006 (unaudited) and December 31, 2005, the loan amounts receivable from related parties are as follows:

Description	**September 30, 2006**	**December 31, 2005**

Amounts loaded to related parties controlled by Mr. Hanlin Chen, the Company's Chairman*	$	3,182,244	$	3,570,461
Amounts loaned to minority shareholders of Joint-venture Companies**		1,091,957		—
	$	4,274,201	$	3,570,461

* This balance is interest bearing and will be due on demand or before December 31, 2006.

** This balance is non-interest bearing and will be due on demand or before December 31, 2006.

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6. INVENTORIES

Inventories at September 30, 2006 (Unaudited) and December 31, 2005 consisted of the following:

	September 30, 2006	December 31, 2005
Raw materials	$ 5,354,736	$ 3,025,467
Work-in-process	3,391,663	2,559,626
Finished goods	9,263,056	7,295,082
	18,009,455	12,880,175
Less: provision for loss	(495,195)	(494,342)
	$ 17,514,260	$ 12,385,833

The Company intends to increase the inventory to meet the demands of production and sales, resulting from the significant increase of sales.

7. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	September 30, 2006	December 31, 2005
Land	$ 6,081,581	$ 5,043,046
Buildings	11,962,441	11,782,552
Machinery and equipment	32,000,252	30,980,053
Electronic equipment	2,176,909	2,023,457
Motor vehicles	2,129,799	2,179,161
Construction in progress	436,647	73,400
	54,787,629	52,081,669
Less: Accumulated depreciation	(16,438,361)	(12,285,636)
	$ 38,349,268	$ 39,796,033

8. INTANGIBLE ASSETS

The activities in the Company’s intangible asset account at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	September 30, 2006	December 31, 2005
Balance at the beginning of year	$ 3,503,217	$ 392,552
Add: Additions during the period -		
Management software license	61,798	3,147,867
Mapping design software license	39,739	93,827
Foreign currency translation gain	39,362	9,693
	3,644,116	3,643,939
Less: Amortization during the period	(532,262)	(140,722)
Balance at the end of the period	$ 3,111,854	$ 3,503,217

9. ACCOUNTS AND NOTES PAYABLE

Accounts and notes payable at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	September 30, 2006	December 31, 2005
Accounts payable	$ 22,415,955	$ 15,615,402
Notes payable	12,688,036	15,760,197
	$ 35,103,991	$ 31,375,599

Notes payable represent accounts payable in the form of bills of exchange whose acceptances and settlements are handled by banks.

The Company has pledged cash deposits, notes receivable and certain plant and machinery to secure trade financing granted by banks.

10. BANK LOANS

At September 30, 2006, the Company through its Sino-foreign Joint-ventures had outstanding fixed-rate short-term bank loans of $16,229,713. The weighted average interest rate for the nine months ended September 30, 2006 was 5.88% per annum. Henglong, one of the Company's joint ventures, provided Jiulong, another of the Company's Joint-ventures, with loan guarantees covering bank loans of $6,242,197. The remaining bank loan of $9,987,516 was secured by mortgages on certain plant and equipment of the Company. There were no charges for these guarantee.

At December 31, 2005, the Company through its Sino-foreign Joint-ventures had outstanding fixed-rate short-term bank loans of $14,814,815. The weighted average interest rate for the year ended December 31, 2005 was 5.92% per annum. Jiulong, one of the Company's Joint-ventures, provided Henglong, another of the Company's Joint-ventures, with loan guarantees covering bank loans of $3,086,420. Henglong provided Jiulong with loan guarantees covering bank loans of $4,938,272. The remaining bank loan of $6,790,123 was secured by mortgages on certain plant and equipment of the Company. There were no charges for these guarantee.

11. AMOUNTS DUE TO SHAREHOLDERS/DIRECTORS

The activities in the amounts due to shareholders/directors at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

Balance, December 31, 2004	$ 589,594
Cash advances from shareholders	177,048
Balance, December 31, 2005	766,642
Cash repaid to shareholder	(507,117)
Balance, September 30, 2006	$ 259,525

As of September 30, 2006 and December 31, 2005, the amounts due to shareholders/directors were unsecured, interest-free and repayable on demand.

12. MINORITY INTERESTS

The activities in respect of the amounts of the minority interests' equity at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

Balance, December 31, 2005	$ 21,751,043
Add: contribution by minority shareholders	2,342,710
Minority interests' income	3,550,247

Less: dividends paid to the minority stockholders' equity of Joint-venture companies	(300,367)
Balance, September 30, 2006	$ 27,343,633

On February 25, 2006, Jiulong, one of the Joint-ventures of the Company, held a meeting of the board and approved an increase in its capital stock of $1,897,628, the equivalent of RMB15,200,000, of which the Company subscribed $1,537,079, the equivalent of RMB12,312,000, and capital stock of $360,549, the equivalent of RMB2,888,000, subscribed by the minority shareholder was deducted from dividends payable.

On February 25, 2006, Henglong, one of the Joint-ventures of the Company, held a meeting of the board and approved an increase in its capital stock of $1,011,236, the equivalent of RMB8,100,000, of which the Company subscribed $450,000, the equivalent of RMB3,604,500, and the capital stock of $561,236, the equivalent of RMB4,495,500 subscribed by the minority shareholder was deducted from dividends payable.

On February 20, 2006, Shengyang, one of the Joint-ventures of the Company, held a meeting of the board and approved distribution of dividends of $1,001,223, the equivalent of RMB 8,019,803, of which $700,856, the equivalent of RMB4,900,599, was distributed to the Company and $300,367, the equivalent of RMB3,119,204, was distributed to the minority shareholder.

On April 6, 2006, USAI, one of the Joint-ventures of the Company, its minority stockholders distributed capital stock of $436,954 in cash, the equivalent of RMB3,500,000.

On April 14, 2006, the wholly-owned subsidiary of the company, 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. As of September 30, 2006, Great Genesis and Tongda have contributed $766,146 and $135,034 in cash, the equivalent of RMB 6,120,000 and RMB 1,080,000 respectively.

On March 31, 2006, as amended on May 2, 2006, Great Genesis, the wholly-owned subsidiary of the Company, 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. As of September 30, 2006, Great Genesis and minority stockholders have contributed $2,900,300 and $848,936 in cash, the equivalent of RMB23,200,000 and RMB6,800,000 respectively.

13. STOCKHOLDERS’ EQUITY

The activities in respect of the amounts of the stockholders’ equity at September 30, 2006 (unaudited) and December 31, 2005 are summarized as follows:

	Common Stock		**Preferred Stock**		
	Shares	**Par Value**	**Shares**	**Par Value**	**Additional Paid- in Capital**
Balance, December 31, 2005	22,574,543	$ 2,257	—	$ —	$ 18,146,720
Sale of common stock	677,089	68	—	—	5,027,173
Issuance of common shares related to financing services	37,863	4	—	—	(4)
Issuance of options for independent directors	—	—	—	—	131,625
Foreign currency translation gain	—	—	—	—	—
Net income for the period ended September 30, 2006	—	—	—	—	—
Balance, September 30, 2006	23,289,495	$ 2,329	—	$ —	$ 23,305,514

	Retained Earnings			
	Appropriated	**Unappropriated**	**Accumulated Other Comprehensive**	**Total**

			Income (Loss)	
Balance, December 31, 2005	$ 4,923,262	$ 12,522,180	$ 1,332,684	$ 36,927,103
Sale of common stock	—	—	—	5,027,241
Issuance of common shares related to financing services	—	—	—	—
Issuance of options for independent directors				131,625
Foreign currency translation gain	—	—	601,399	601,399
Net income for the period ended September 30, 2006	—	3,378,157	—	3,378,157
Appropriation of retained earnings	155,322	(155,322)	—	—
Balance, September 30, 2006	$ 5,078,584	$ 15,745,015	$ 1,934,083	$ 46,065,525

14. INCOME TAXES

The Company’s Sino-foreign Joint-ventures are subject to PRC state and local income taxes at the applicable tax rate on the taxable income as reported in their PRC statutory financial statements in accordance with the relevant income tax laws applicable to foreign invested enterprises. In accordance with the Income Tax Law of the PRC for Enterprises with Foreign Investments and Foreign Enterprises, enterprises with foreign investments and foreign enterprises meeting certain criteria are entitled to full exemption from income tax for the first two years and a 50% reduction for the next three years, commencing from the first profit-making year after offsetting all tax losses carried forward from the previous five years.

Two of the Company’s Sino-foreign Joint-ventures, Henglong and Jiulong, were subject to a tax rate of 15% during 2005 and 2006. Shenyang was entitled to and was certified for a two-year tax holiday commencing in 2003, the first profit-making year. Therefore, Shenyang was income tax exempted in 2004 and is subject to a tax rate of 7.5% in 2005 and 2006. The tax rate for Zhejiang has not yet been approved by tax authorities, but in accordance with the relevant income tax laws as mentioned above, Zhejiang is also entitled to two-year tax exemption in 2004 and 2005, and is subject to a tax rate of 16.5% in 2006. USAI, Jielong and Wuhu did not have any operating income in 2006.

No provision for Hong Kong profits tax has been made as Ji Long and Great Genesis are investment holding companies and did not have any assessable profits in Hong Kong during three months and nine months ended September 30, 2006 and 2005.

No provision for US income taxes has been made as the Company did not have any assessable profits in United States during three months and nine months ended September 30, 2006 and 2005.

15. RECLASSIFICATIONS

Certain reclassifications have been made to the Consolidated Statements of OperationsôConsolidated Statements of Cash Flows and Consolidated Balance Sheets for the three months and nine months ended September 30, 2005 to conform to the current year presentation.

Reclassification of Consolidated Statements of Operations:

	Three months ended September 30, 2005		**Nine months ended September 30, 2005**	
Item	**Original**	**Present**	**Original**	**Present**
Revenues (costs and expenses):				
General and administrative expenses - warranty	(128,366)	—	(405,024)	—
Operating expenses - “3-R Guarantees” service charge	—	(128,366)	—	(405,024)
General and administrative expenses - Depreciation and amortization expenses	(364,933)	—	(1,396,414)	—
Depreciation and amortization	—	(364,933)	—	(1,396,414)
General and administrative expenses - R & D expenses	(261,711)	—	(757,660)	—
R & D expenses	—	(261,711)	—	(757,660)
Stock-based compensation	—	—	(68,850)	—
General and administrative expenses - Compensation	—	—	—	(68,850)
Non-operating income	152,157	—	200,513	—
Net other sales	—	525,167	—	1,248,758
Cost of other sales	—	(373,010)	—	(1,048,245)

Total	(602,853)	(602,853)	(2,427,435)	(2,427,435)

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Reclassification of Consolidated Balance Sheets:

	December 31, 2005	
Item	**Original**	**Present**
Advances to suppliers	2,126,013	—
Prepayment of property and equipment	—	1,096,121
Prepaid expenses and other	—	1,029,892
Total	2,126,013	2,126,013

Reclassification of Statements of Cash Flows

	Three months ended September 30, 2005		Nine months ended September 30, 2005	
Item	**Original**	**Present**	**Original**	**Present**
Net cash provided by (used in) operating activities	2,807,989	3,070,659	7,720,812	10,754,403
Net cash provided by (used in) investing activities	(1,311,264)	(3,252,490)	(4,998,305)	(9,710,452)
Net cash provided by (used in) financing activities	1,475,762	1,826,479	140,576	491,293
Effect of exchange rate fluctuations on cash and cash equivalents	—	1,327,839	—	1,327,839
Total	2,972,487	2,972,487	2,863,083	2,863,083

16. SIGNIFICANT CONCENTRATIONS

The Company grants credit to its customers, generally on an open account basis. The Company's customers are all located in the PRC.

During the three months ended September 30, 2006, the Company's ten largest customers accounted for 58.7% of the Company's consolidated net sales, with each of two customers individually accounting for more than 10% of consolidated net sales, i.e. 14.4% and 13.5% individually, or an aggregate of 27.9%. At September 30, 2006, approximately 19.1% of accounts receivable were from trade transactions with the aforementioned two customers.

During the nine months ended September 30, 2006, the Company's ten largest customers accounted for 65.5% of the Company's consolidated net sales, with each of four customers individually accounting for more than 10% of consolidated net sales, i.e. 15.6%, 13.9%, 11.0% and 10.5% individually, or an aggregate of 51.0%. At September 30, 2006, approximately 34.1% of accounts receivable were from trade transactions with the aforementioned four customers.

During the three months ended September 30, 2005, the Company's ten largest customers accounted for 68.3% of the Company's consolidated net sales, with three customers individually accounting for more than 10% of consolidated net sales, i.e. 16.3%, 14.9% and 10.6% individually, or an aggregate of 41.8%. At September 30, 2005, approximately 26.0% of accounts receivable were from trade transactions with the aforementioned three customers.

During the nine months ended September 30, 2005, the Company's ten largest customers accounted for an aggregate of 72.4% of its consolidated net sales, with four customers individually accounting for more than 10% of consolidated net sales, i.e. 15%, 11.3%, 10.9% and 10.7% individually, or an aggregate of 47.9%. At September 30, 2005, approximately 26% of accounts receivable were from trade transactions with the aforementioned four customers.

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17. RELATED PARTY TRANSACTIONS

Henglong, one of the Joint-ventures of the Company, has constructed seven buildings dedicated to research and administration for its operations in Wuhan. Due to the unified building guidance and planning on floor and building areas by the government of Wuhan, the actual building areas were greater than the areas the Company needed. The Company decided to dispose of two of its seven buildings to WuHan Geological University Information S&T Development Co., Ltd. "WuHan Information", a Chinese company controlled by Mr. Hanlin Chen, the Chairman of the Company, at fair market value of $2,636,444, which was determined by an independent appraisal firm. The amount is secured by a mortgage in favor of the Company to assure payment of the receivable. As of September 30, 2006, this amount has not been repaid, but WuHan Information has paid the interest of $95,000 at an agreed conventional bank rate on November 10, 2006.

Related sales and purchases: During the three months and nine months ended September 30, 2006 and 2005, the Joint-ventures entered into related party transactions with companies with common directors as shown below:

	Three Months Ended September 30,			
		2006		2005
Sales	$	1,100,320	$	360,433
Purchases	$	602,127	$	337,108

	Nine months Ended September 30,			
		2006		2005
Sales	$	2,478,059	$	1,360,293
Purchases	$	1,932,329	$	1,232,897

These transactions were consummated under similar terms as those with the Company's customers and suppliers.

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18. OFF-BALANCE SHEET ARRANGEMENTS
At September 30, 2006 and December 31, 2005, the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

19. COMMITMENTS AND CONTINGENCIES:
The following table summarizes our major contractual payment obligations and commitments as of September 30, 2006:

Payment Obligations by Period

	2006 (a)	**2007**	**2008**	**2009**	**2010**	**Thereafter**	**Total**
Obligations for service agreement	$ —	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 550,000
Obligations for purchasing agreement	$ 510,990	$ 565,109	$ —	$ —	$ —	$ —	$ 1,076,099
Total	$ 510,990	$ 675,109	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 1,626,099

(a) Remaining 3 months in 2006.

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20. OPERATING INFORMATION OF THE COMPANY'S SINO-FOREIGN JOINT-VENTURES

The Company has no operations independent of those of Great Genesis and its subsidiaries, and the principal assets are its investments in Great Genesis and its subsidiaries. The operational results of Company's Sino-foreign Joint-ventures for the three months and nine months ended September 30, 2006 and 2005 were summarized as follows:

	Parent Company		**Henglong**	
	Three Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	100%	100%	44.5%	44.5%
Net sales	3,826	593	12,906,647	8,919,345
Cost of sales and operating expenses	304,401	138,464	11,329,738	7,328,219
Operating earnings (losses)	(300,575)	(137,871)	1,576,909	1,591,126
Other income (expenses), net	312	(9)	(101,084)	(220,109)
Pretax earnings	(300,263)	(137,880)	1,475,825	1,371,017
Income tax	0	0	382,608	492,397
Income (expenses) before minority interest	(300,263)	(137,880)	1,093,217	878,620
Minority interest income (expenses)	0	0	624,020	475,708
Net earnings (expenses)	(300,263)	(137,880)	469,197	402,912

	Jiulong		**Shenyang**	
	Three Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	81%	81%	70%	70%
Net sales	7,616,711	4,086,869	3,736,832	2,803,932
Cost of sales and operating expenses	6,631,839	3,666,296	2,753,573	2,377,898
Operating earnings (losses)	984,872	420,573	983,259	426,034
Other income (expenses), net	(119,145)	(91,699)	5,988	830
Pretax earnings	865,727	328,874	989,247	426,864
Income tax	101,150	69,205	(120,368)	35,825
Income (expenses) before minority interest	764,577	259,669	1,109,615	391,039
Minority interest income (expenses)	126,295	105,404	330,652	117,312
Net earnings (expenses)	638,282	154,265	778,963	273,727

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	Zhejiang		USAI	
	Three Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	51%	51%	60%	0%
Net sales	2,247,682	1,553,594	36,648	—
Cost of sales and operating expenses	1,708,596	1,332,959	233,427	—
Operating earnings (losses)	539,086	220,635	(196,779)	—
Other income (expenses), net	1,642	(4,380)	1,377	—
Pretax earnings	540,728	216,255	(195,402)	—
Income tax	107,227	—	—	—
Income (expenses) before minority interest	433,501	216,965	(195,402)	—
Minority interest income (expenses)	212,228	105,965	(78,161)	—
Net earnings (expenses)	221,273	110,290	(117,241)	—

	Wuhu		Jielong	
	Three Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	77.33%	0%	85.0%	0%
Net sales	—	—	—	—
Cost of sales and operating expenses	70,273	—	44,803	—
Operating earnings (losses)	(70,273)	—	(44,803)	—
Other income (expenses), net	7,092	—	2,329	—
Pretax earnings	(63,181)	—	(42,474)	—
Income tax	—	—	—	—
Income (expenses) before minority interest	(63,181)	—	(42,474)	—
Minority interest income (expenses)	(14,323)	—	(6,371)	—
Net earnings (expenses)	(48,858)	—	(36,103)	—

	Elimination		Total	
	Three Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year				
Net sales	3,807,448	2,576,233	22,740,898	14,788,100

Cost of sales and operating expenses	3,734,321	2,849,830	19,342,329	11,994,006
Operating earnings (losses)	73,127	(273,597)	3,398,569	2,794,094
Other income (expenses), net	—	—	(201,489)	(315,367)
Pretax earnings	73,127	(273,597)	3,197,080	2,478,727
Income tax	—	—	470,617	597,427
Income (expenses) before minority interest	73,127	(273,597)	2,726,463	1,881,300
Minority interest income (expenses)	—	—	1,194,340	804,388
Net earnings (expenses)	73,127	(273,597)	1,532,123	1,076,912

	Parent Company		Henglong	
	Nine months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	100%	100%	44.5%	44.5%
Net sales	9,895	1,581	38,738,619	25,543,625
Cost of sales and operating expenses	1,281,287	496,897	32,866,236	22,664,913
Operating earnings (losses)	(1,271,392)	(495,316)	5,872,383	2,878,712
Other income (expenses), net	702,733	4,425	(399,837)	(568,924)
Pretax earnings	(568,659)	(490,891)	5,472,546	2,309,788
Income tax	—	—	1,167,734	731,362
Income (expenses) before minority interest	(568,659)	(490,891)	4,304,812	1,578,426
Minority interest income (expenses)	—	—	2,436,098	855,644
Net earnings (expenses)	(568,659)	(490,891)	1,868,714	722,784

	Jiulong		Shenyang	
	Nine months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	81%	81%	70%	70%
Net sales	20,898,496	16,371,451	11,723,350	8,762,249
Cost of sales and operating expenses	19,046,561	14,956,000	9,923,915	7,337,385
Operating earnings (losses)	1,851,935	1,775,451	1,790,435	1,424,864
Other income (expenses), net	(334,679)	(336,383)	10,494	2,858
Pretax earnings	1,517,256	1,439,068	1,800,929	1,427,722
Income tax	54,300	302,035	(36,791)	117,353
Income (expenses) before minority interest	1,462,956	1,137,033	1,837,720	1,310,369
Minority interest income (expenses)	280,263	205,346	549,084	393,111
Net earnings (expenses)	1,182,693	931,687	1,288,636	917,258

	Zhejiang		USAI	
	Nine months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
	51%	51%	60%	0%

Proportionate ownership interest at the end of year				
Net sales	7,238,942	4,014,362	146,567	—
Cost of sales and operating expenses	5,707,147	3,665,484	846,320	—
Operating earnings (losses)	1,531,795	348,878	(699,753)	—
Other income (expenses), net	(1,535)	(16,279)	1,533	—
Pretax earnings	1,530,260	332,599	(698,220)	—
Income tax	336,824	—	—	—
Income (expenses) before minority interest	1,193,436	332,599	(698,220)	—
Minority interest income (expenses)	587,784	162,973	(279,288)	—
Net earnings (expenses)	608,652	169,626	(418,932)	—

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	Wuhu		Jielong	
	Nine Months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	2005	2006	2005
Proportionate ownership interest at the end of year	77.33%	0%	85.0%	0%
Net sales	—	—	—	—
Cost of sales and operating expenses	70,273	—	44,803	—
Operating earnings (losses)	(70,273)	—	(44,803)	—
Other income (expenses), net	7,092	—	2,329	—
Pretax earnings	(63,181)	—	(42,474)	—
Income tax	—	—	—	—
Income (expenses) before minority interest	(63,181)	—	(42,474)	—
Minority interest income (expenses)	(14,323)	—	(6,371)	—
Net earnings (expenses)	(48,858)	—	(36,103)	—

	Elimination		Total	
	Nine months Ended September 30, (Unit: US Dollars, except ownership percentage)			
	2006	**2005**	**2006**	**2005**
Proportionate ownership interest at the end of year				
Net sales	9,489,590	8,801,818	69,266,279	46,251,450
Cost of sales and operating expenses	9,692,461	8,996,504	60,103,081	40,124,175
Operating earnings (losses)	(202,871)	(194,686)	9,163,198	6,127,275
Other income (expenses), net	700,857	—	(712,727)	(914,303)
Pretax earnings	497,986	(194,686)	8,450,471	5,212,972
Income tax	—	—	1,522,067	1,150,750
Income (expenses) before minority interest	497,986	(194,686)	6,928,404	4,062,222
Minority interest income (expenses)	—	—	3,550,247	1,617,073
Net earnings (expenses)	497,986	(194,696)	3,378,157	2,445,149

21. SUBSEQUENT EVENTS
None

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

This Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. Generally, the words "believes", "anticipates," "may," "will," "should," "expect "intend," "estimate," "continue," and similar expressions or the negative thereof or comparable terminology are intended to identify forward-looking statements which include, but are not limited to, statements concerning the Company's expectations regarding its working capital requirements, financing requirements, business prospects, and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. Such statements are subject to certain risks and uncertainties, including the matters set forth in this Quarterly 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. 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. In addition, the forward-looking statements in this Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 involve known and unknown risks, uncertainties and other factors that could cause the actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein. Please see the discussion on risk factors in Item 1A of Part II of this quarterly report on Form 10-Q.

GENERAL OVERVIEW:

Organization - Effective March 5, 2003, Visions-In-Glass, Inc., a United States company incorporated in the State of Delaware, “Visions”, entered into a Share Exchange Agreement to acquire 100% of the shareholder interest in Great Genesis Holding Limited, a company incorporated on January 3, 2003 under the Companies Ordinance in Hong Kong as a limited liability company, “Great Genesis”, as a result of which Great Genesis became a wholly-owned subsidiary of Visions. At the closing, the old directors and officers of Visions resigned, and new directors and officers were appointed. Visions subsequently changed its name to China Automotive Systems, Inc.

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 described below, is engaged in the manufacture and sale of automotive systems and components in the People’s Republic of China, the “PRC” or “China”, as described below.

As of September 30, 2006 and 2005, Great Genesis owns the following aggregate net interests in seven Sino-foreign Joint-ventures organized in the PRC:

Name of Entity	Percentage Interest September 30, 2006	2005
Shashi Jiulong Power Steering Co. Limited ("Jiulong")	81.0%	81.0%
Jingzhou Henglong Automotive Parts Co. Limited ("Henglong")	44.5%	44.5%
Shenyang Jinbei Henglong Automotive Steering System Co. Limited ("Shenyang")	70.0%	70.0%
Zhejiang Henglong & Vie Pump-Manu Co. Limited ("Zhejiang")	51.0%	51.0%
Universal Sensor Application, Inc. (“USAI”)	60.0%	60%
Wuhan Jielong Electric Power Steering Co., Ltd. (“Jielong”)	85.0%	—
Wuhu HengLong Auto Steering System Co., Ltd. (“Wuhu”)	77.33%	—

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, 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, the wholly-owned subsidiary of the company, 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 September 30, 2006, Great Genesis has contributed $900,337, the equivalent of RMB7,200,000, Sensor has contributed $3,000,000, and Hongxi has contributed $436,954 in cash, the equivalent of RMB3,500,000.

On April 14, 2006, the wholly-owned subsidiary of the company, 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 September 30, 2006, Great Genesis and Tongda have contributed $766,146 and $135,034 in cash, the equivalent of RMB6,120,000 and RMB1,080,000 respectively.

On March 31, 2006, as amended on May 2, 2006, Great Genesis, the wholly-owned subsidiary of the Company, 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 and $850,087, respectively, which will account for 77.33% and 22.67% of the total registered capital, respectively. As of September 30, 2006, the capital of $3,750,387, the equivalent of RMB30,000,000, has been totally contributed in Wuhu.

CRITICAL ACCOUNTING POLICIES:
The Company prepares its condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions. The following critical accounting policies affect the more significant judgments and estimates used in the preparation of the Company’s condensed consolidated financial statements.

MINORITY INTERESTS:
Minority interests refer to the percentage of the owner’s equity of a subsidiary owned by those investors other than the parent company. Minority interests in the condensed consolidated financial statements means the percentage of the Company’s net assets owned by shareholders of the Company’s Sino-foreign Joint-ventures other than the Company, according to their respective investment ratios.

SALES: Sales is mainly derived from automobile parts while the other sales are generated from the sales of raw materials and the non-recurring sales of used and unused equipment, as well as the automobiles balanced against the payment of goods by customers.

PRODUCT SALES:
The Company recognizes product sales revenue when the significant risks and rewards of ownership have been transferred to the customer pursuant to PRC law, including factors such as when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, sales and value added tax laws have been complied with, and collectibility is probable. The Company recognizes product sales generally at the time the product is shipped. Concurrent with the recognition of revenue, the Company reduces revenue for estimated product returns. Shipping and handling costs are included in cost of goods sold. Revenue is presented net of any sales tax and value added tax.

OTHER SALES:
Other sales are recognized when the products are shipped to the customer and when persuasive evidence of an arrangement exists, which means the significant risks and rewards of ownership have been transferred to the customer, the price is fixed or determinable and collectibility is reasonably assured. The sales revenue of materials is presented net of any sales tax and value added tax.

ACCOUNTS RECEIVABLE
In order to determine the value of the Company’s accounts receivable, the Company records an allowance for doubtful accounts to cover estimated credit losses. Management reviews and adjusts this allowance periodically based on historical experience and its evaluation of the collectibility of outstanding accounts receivable. The Company evaluates the credit risk of its customers utilizing historical data and estimates of future performance.

INVENTORIES
Inventories are stated at the lower of cost or net realizable value. Cost is calculated on the moving-average basis and includes all costs to acquire and other costs incurred in bringing the inventories to their present location and condition. The Company evaluates the net realizable value of its inventories on a regular basis and records a provision for loss to reduce the computed moving-average cost if it exceeds the net realizable value.

INCOME TAXES
The Company records a tax provision to reflect the expected tax payable on taxable income for the period, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous periods.

IMPAIRMENT OF LONG-LIVED ASSETS
The Company's long-lived assets consist of property and equipment and certain intangible assets. In assessing the impairment of such assets, the Company periodically makes assumptions regarding the estimated future cash flows and other factors to determine the fair value of the respective assets. If these estimates or the related assumptions indicate that the carrying amount may not be recoverable, the Company records impairment charges for these assets at such time.

RESULTS OF OPERATIONS — THREE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005:

TOTAL REVENUES
Total sales revenues consist of product sales and net revenue from other sales. Total sales revenues for the three months ended September 30, 2006 increased by $7,952,798, representing a 53.8% increase, to $22,740,898 as compared to $14,788,100 for the same period of the prior year. Other sales were $341,225 for the three months ended September 30, 2006, as compared to $525,167 for the same period of 2005, a decrease of $183,942 or 35.0%, mainly due to a significant drop of sales of automobiles to customers under barter trade with no cash payment.

NET PRODUCT SALES
Net sales were $22,399,673 for the three months ended September 30, 2006, as compared to $14,262,933 for the three months ended September 30, 2005, an increase of $8,136,740 or 57.0%. The increase in net sales in 2006 as compared to 2005 was a result of the following factors:

(1) Primarily, the increase in sales was due to an increase in sales of domestic passenger vehicles. As a result of increased demands for domestic passenger vehicles, demand for steering gear and steering pumps for domestic passenger vehicles were stimulated, which led to increased sales for steering gear and pumps for the three months ended September 30, 2006 by 49.1% and 63.6% over the same period of 2005, respectively.

(2) In the third quarter of 2006, sales of steering gear and accessories for commercial vehicles increased by 73.0% as compared to the same period of 2005. Sales for the three months ended September 30, 2005 were affected adversely by state macro-controls and were reduced to $3,717,623 as compared to past sales, an historical low. Sales of steering gear and accessories for commercial vehicles were $6,430,791 and recovered to normal sales of $6,000,000 during the three months ended September 30, 2006.

GROSS PROFIT
For the three months ended September 30, 2006, gross profit was $8,189,393, as compared to $5,661,073 for the three months ended September 30, 2005, an increase of $2,528,320 or 44.7%. The gross profit from other sales for the three months ended September 30, 2006, decreased by $95,924, representing a 63.0% decrease, to $56,234 as compared to $152,158 for the same period of the prior year, primarily due to a decrease in sales volume.

PRODUCT GROSS PROFIT

For the three months ended September 30, 2006, gross profit was $8,133,159, as compared to $5,508,917 for the three months ended September 30, 2005, an increase of $2,624,242 or 47.6%. The increase in sales volume contributed to an increase of $3,303,408 in gross profit, a decrease in unit cost resulted in an increase of $67,928 in gross profit, which was offset by a decrease in selling prices resulting in a decrease of $747,094 in gross profit.

Gross margin was 36.0% for the three months ended September 30, 2006, a decrease of 2.3% from 38.3% for the same period of 2005. The decrease in selling prices during the third quarter of 2006 was greater than the decrease in cost. The Company plans to take the following measures in the remaining three months of 2006 to further decrease its cost:

(1) Reduce labor costs. The Company has purchased certain advanced production equipment, which optimizes manufacturing cycles, and further improves productivity capacity and efficiency. The Company estimates that its labor costs will be reduced by 3% as compared to 2005 as a result of its optimized manufacturing cycles and reduced standard labor hours.

(2) Reduce the cost of raw materials. In 2006, the Company plans to continue to control the costs of its raw materials in two ways: First, volume purchase of major raw materials will be made through a bidding process, and for purchases of smaller quantities of non major materials, “target prices” will be set to guide such purchases. Second, technical personnel have been encouraged to reevaluate the product structure and production techniques to optimize product design, reduce the weight of parts and wastage in the production process, and thus reduce the cost of raw materials. The Company estimates that its material cost will be reduced by 2% as a result of these measures.

(3) Reduce manufacturing expenses. In 2006, the Company will reexamine the standard material consumption rates, and regulate the program of approval and usage for supplementary materials, such as oil, cutting tools, dies and other supplies. The Company estimates that its manufacturing expenses would be reduced by 1% through these measures.

SELLING EXPENSES

Selling expenses were $1,540,030 for the three months ended September 30, 2006, as compared to $1,151,638 for the same period of 2005, an increase of $388,392 or 33.7%. The increased selling expenses for the three months ended September 30, 2006 were mainly due to the following factors:

(1) Increased “3-R Guarantees” service expenses. “3-R Guarantees” service expenses were $421,966 for the three months ended September 30, 2006, as compared to $257,953 for the same period of 2005, an increase of $164,013 or 63.6%. The Company has increased its warranty rate to cover the product claim risks arising from its increased market share, including but not limited to the following factors: (a) The Company had extended its term of service from two years or 30,000 kilometers, whichever comes first, to three years or 50,000 kilometers, whichever comes first, to improve its product competitiveness in the market. The Management estimated that this would result in an increase of warranty reserves. (b) The consumer rights protection policies of "recall" stipulated by the Chinese Government had led to increased “3-R Guarantees” service charges, including the recalling of flawed vehicles policy.

(2) Increased provision for market development: In 2006, the Company recorded a higher provision for market development to strengthen its development in domestic and overseas markets to reach its sales target for this year. For the three months ended September 30, 2006, the Company recorded a provision of $586,586 for market development expenses based on its sales target established at the beginning of 2006, as compared to $233,287 for the same period of 2005, an increase of $353,299 or 151.4%.

(3) Increased transportation expenses. The Company recorded $324,728 of transportation expenses for the three months ended September 30, 2006, as compared to $150,629 for the same period of 2005, an increase of $174,099 or 115.6%, resulting from increased transportation volume.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses were $2,139,440 for the three months ended September 30, 2006, as compared to $846,238 for the same period of 2005, an increase of $1,293,202 or 152.8%. The increased general and administrative expenses for the three months ended September 30, 2006 were mainly due to the following factors:

(1) Increased salaries and wages. The salaries and wages of administrative staff were $589,868 for the three months ended September 30, 2006, as compared to $333,167 for the same period of 2005, an increase of $256,701 or 77.0%, mainly due to the two joint ventures of Jielong and Wuhu incorporated by the Company which led to an increase of administrative staff, as well as increased production in 2006 which led to an increase of workload for management.

(2) Increased administrative expenses. Administrative expenses were $465,929 for the three months ended September 30, 2006, as compared to $287,873 for the same period of 2005, an increase of $178,056 or 61.9%, mainly due to (i) significant increase in administrative expenses, such as meeting costs, traveling and entertainment, and (ii) increased office supplies after incorporating two joint ventures.

(3) Provision for doubtful accounts. Provision for doubtful accounts was $601,086 for the three months ended September 30, 2006, as compared to recovery of $28,839 for the same period of 2005, an increase of $629,925. The Company's accounts receivable increased during the three months ended September 30, 2006 as a result of increased sales volume. Management believes that the Company should record a higher provision for doubtful accounts to cover estimated credit losses.

(4) Increased stock-based compensation. On July 6, 2006, the Company issued options to purchase 7,500 shares of common stock to each of its three independent directors. These stock options vested immediately upon grant and were exercisable at $7.94 per share over a period of five years. The aggregate fair value of these options, calculated pursuant to the Black-Scholes option-pricing model, was estimated to be $131,625, which was charged to operations for the three months ended September 30, 2006, while there was no similar expense in the same period of 2005.

DEPRECIATION AND AMORTIZATION EXPENSES

For the three months ended September 30, 2006, the depreciation and amortization expenses excluding those recorded in cost of sales were $904,622, as compared to $607,392 for the three months ended September 30, 2005, an increase of $297,230 or 48.9%, as a result of USAI, one of the Company's Joint-ventures of, amortizing intangible assets for the three months ended September 30, 2006, while there were no such expenses for the same period of 2005.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses were $206,732 for the three months ended September 30, 2006, as compared to $261,711 for the same period of 2005, a decrease of $54,979 or 21.0%, as a result of the Company's R & D department focusing on applications of prior purchased technologies.

INCOME FROM OPERATIONS

Income from operations was $3,398,569 for the three months ended September 30, 2006, as compared to $2,794,094 for the three months ended September 30, 2005, an increase of $604,475 or 21.6%, as a result of an increase of $2,528,320 or 44.7% in gross profit and an increase of $1,923,845 or 67.1% in operating expenses.

OTHER NON-OPERATING INCOME

Other non-operating income was $93,632 for the three months ended September 30, 2006, as compared to $18,518 for the three months ended September 30, 2005, an increase of $75,114 or 405.6%, as a result of the Company receiving approximately $87,000 in subsidies from the government related to the introduction of domestic equipment, while there was no such item in the same period of 2005.

FINANCIAL EXPENSES

Financial expenses were $295,121 for the three months ended September 30, 2006, as compared to $333,885 for the three months ended September 30, 2005, a decrease of $38,764 or 11.6%, primarily due to decreased discount charges resulting from decreased volume of bills discounted.

INCOME BEFORE INCOME TAXES

Income before income taxes was $3,197,080 for the three months ended September 30, 2006, as compared to $2,478,727 for the three months ended September 30, 2005, an increase of $718,353 or 29.0%, as a result of an increase in income from operations of $604,475 or 21.6%, an increase in other non-operating income of $75,114 or 405.6%, and a decrease in financial expenses of $38,764 or 11.6%.

INCOME TAXES

Income taxes expense was $470,617 for the three months ended September 30, 2006, as compared to $597,427 for the three months ended September 30, 2005, a decrease of $126,810 or 21.2%. The decrease in income taxes reflects the Company's having received approximately $150,000 in tax refunds from the Government, while there was no such refunds in 2005. In accordance with the relevant regulations of income taxes stipulated by the Ministry of Finance and the State Administration of Taxation, 40% of domestic equipment purchases are refundable from the increased income taxes of the purchasing year over those of the year before.

INCOME BEFORE MINORITY INTERESTS
Income before minority interests was $2,726,463 for the three months ended September 30, 2006, as compared to $1,881,300 for the three months ended September 30, 2005, an increase of $845,163 or 44.9%, as a result of an increase in income before income taxes of $718,353 or 29.0%, and a decrease in income taxes of $126,810 or 21.2%.

MINORITY INTERESTS
Minority interests in the earnings of the Sino-foreign Joint-ventures amounted to $1,194,340 for the three months ended September 30, 2006, as compared to $804,388 for the three months ended September 30, 2005, an increase of $389,952 or 48.5%. The increase was primarily due to an increase in net income for two of the Company's Sino-foreign Joint-ventures Henglong and Zhejiang. Minority shareholders own 55.5% of Henglong's equity and 49% of Zhejiang's equity during the three months ended September 30, 2006.

NET INCOME
Net income was $1,532,123 for the three months ended September 30, 2006, as compared to a net income of $1,076,912 for the three months ended September 30, 2005, an increase of $455,211 or 42.3%, as a result of an increase in income before minority interests of $845,163 or 44.9%, and an increase in minority interests of $389,952 or 48.5%.

RESULTS OF OPERATIONS — NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005:

Total Revenues
Total sales revenues consist of product sales and net revenue from sales of materials and other assets. Total sales revenues for the nine months ended September 30, 2006 increased by $23,014,829, representing a 49.8% decrease, to $69,266,279 as compared to $46,251,450 for the same period of the prior year. Other sales were $1,154,242 for the nine months ended September 30, 2006, as compared to $1,248,758 of the same period of 2005, a decrease of $94,516 or 7.6%, mainly due to a decline in sales of automobiles to customers under barter trade with no cash payment.

NET PRODUCT SALES
Net sales were $68,112,037 for the nine months ended September 30, 2006, as compared to $45,002,692 for the nine months ended September 30, 2005, an increase of $23,109,345 or 51.4%. The increase in net sales in 2006 as compared to 2005 was a result of the following factors:

(1) Primarily, the increase in sales was due to an increase in sales of domestic passenger vehicles. As a result, sales of steering gear and pumps for domestic passenger vehicles for the nine months ended September 30, 2006 increased 66.6% and 101.4% over the same periods of 2005, respectively.

(2) For the nine months ended September 30, 2006, sales of steering gears and accessories for commercial vehicles increased by 14.1% as compared to the same period of 2005, mainly due to the Company having expanded its market share by adopting technical innovation.

GROSS PROFIT
For the nine months ended September 30, 2006, gross profit was $24,606,337, as compared to $16,706,521 for the nine months ended September 30, 2005, an increase of $7,899,816 or 47.3%. The gross profit from other sales for the nine months ended September 30, 2006, increased by $56,322, representing a 28.1% increase, to $256,836 as compared to $200,514 for the same period of the prior year, primarily resulting from the increase in sale price.

PRODUCT GROSS PROFIT
For the nine months ended September 30, 2006, gross profit was $24,349,501, as compared to $16,506,008 for the nine months ended September 30, 2005, an increase of $7,843,492 or 47.5%. The increase in unit sales contributed to an increase of $8,548,387 in gross profit, a decrease in unit cost resulted in an increase of $2,310,513 in gross profit, which was partially offset by a decrease in selling prices resulting in a decrease of $3,015,407 in gross profit.

Gross margin was 35.8% for the nine months ended September 30, 2006, compared to the same period of 2005, a decrease of 0.9% from 36.7%. The decrease in selling prices was partially offset by a cost reduction for the nine months ended September 30, 2006.

SELLING EXPENSES

Selling expenses were $5,419,420 for the nine months ended September 30, 2006, as compared to $3,818,669 for the same period of 2005, an increase of $1,600,751 or 41.9%. The increased selling expenses for the nine months ended September 30, 2006 were mainly due to the following factors:

(1) Increased “3-R Guarantees” service expenses. “3-R Guarantees” service expenses were $2,626,177 for the nine months ended September 30, 2006, as compared to $1,567,646 for the same period of 2005, an increase of $1,058,531 or 67.5%. The Company has increased its warranty rate to satisfy the increased needs of “3-R Guarantees” service expenses, including but not limited to the following factors: (a) The Company had extended its term of service from two years or 30,000 kilometers, whichever comes first, to three years or 50,000 kilometers, whichever comes first, to improve its product competitiveness in the market. The Management estimated that it would result in an increase of warranty reserves. (b) In 2005 the Chinese Government had fully implemented the consumer rights protection policies of "recall" which began in 2004 (including the recalling of flawed vehicles policy), which led to increased “3-R Guarantees” service charges.

(2) Increased provision for market development: In 2006, the Company recorded a higher provision for market development to strengthen its development in domestic and overseas markets to reach its sales target for this year. For the nine months ended September 30, 2006, the Company recorded a provision of $788,898 for market development expenses based on its sales target established at the beginning of 2006, as compared to $630,877 for the same period of 2005, an increase of $158,021 or 25.1%.

(3) Increased transportation expenses. The Company recorded $1,142,565 of transportation expenses for the nine months ended September 30, 2006, as compared to $632,988 for the same period of 2005, an increase of $509,577 or 80.5%, resulting from increased transportation volume.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses were $6,529,130 for the nine months ended September 30, 2006, as compared to $4,010,754 for the same period of 2005, an increase of $2,518,376 or 62.8%. The increased general and administrative expenses for the nine months ended September 30, 2006 were mainly due to the following factors:

(1) Increased Salaries and wages. The salaries and wages of administrative staff were $2,074,713 for the nine months ended September 30, 2006, as compared to $950,839 for the same period of 2005, an increase of $1,123,874 or 118.2%, mainly due to the two joint ventures of Jielong and Wuhu incorporated by the Company which led to an increase of administrative staff, as well as increased production in 2006 which led to an increase of workload for management.

(2) Increased administrative expenses. Administrative expenses were $1,456,216 for the nine months ended September 30, 2006, as compared to $1,086,013 for the same period of 2005, an increase of $370,204 or 34.1%, mainly due to (i) a significant increase in administrative expenses, such as meeting costs, traveling and entertainment expenses, and (ii) increased office supplies after incorporating two joint ventures.

(3) Provision for doubtful accounts. The Company recorded $1,861,107 of provision for doubtful accounts for the nine months ended September 30, 2006, as compared to a collection of $19,110 for the same period of 2005, an increase of $1,841,997. The Company’s accounts receivable increased during the nine months ended September 30, 2006 as a result of increased sales volume. Management believes that the Company should record a higher provision for doubtful accounts to cover estimated credit losses.

(4) Increased stock-based compensation. On July 6, 2006, the Company issued options to purchase 7,500 shares of common stock to each of its three independent directors. These stock options vested immediately upon grant and were exercisable at $7.94 per share over a period of five years. The aggregate fair value of these options, calculated pursuant to the Black-Scholes option-pricing model, was estimated to be $131,625, which was charged to operations

for the nine months ended September 30, 2006.

On June 28, 2005, the Company issued options to purchase 7,500 shares of common stock to each of its three independent directors. Such stock options vested immediately upon grant and were exercisable at $6.83 per share over a period of five years. The aggregate fair value of these options, calculated pursuant to the Black-Scholes option-pricing model, was estimated to be $68,850, which was charged to operations for the nine months ended September 30, 2005.

DEPRECIATION AND AMORTIZATION EXPENSES

For the nine months ended September 30, 2006, the depreciation and amortization expenses excluding those recorded in cost of sales were $2,846,716, as compared to $1,992,163 for the nine months ended September 30, 2005, an increase of $854,553 or 42.9%, as a result of USAI, one of the Company's Joint-ventures, amortizing intangible assets for the nine months ended September 30, 2006, while there were no such expenses for the same period of 2005.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses were $647,873 for the nine months ended September 30, 2006, as compared to $757,660 of the same period of 2005, a decrease of $109,787 or 14.5%, as a result of the Company's R & D department focusing on applications of prior purchased technologies.

INCOME FROM OPERATIONS

Income from operations was $9,163,198 for the nine months ended September 30, 2006, as compared to $6,127,275 for the nine months ended September 30, 2005, an increase of $3,035,923 or 49.5%, as a result of an increase of $7,899,816 or 47.3% in gross profit and an increase of $4,863,893 or 46.0% in operating expenses.

OTHER NON-OPERATING INCOME

Other non-operating income was $94,257 for the nine months ended September 30, 2006, as compared to $27,183 for the nine months ended September 30, 2005, an increase of $67,074 or 246.7%, as a result of the Company receiving approximately $87,000 in subsidies from the government related to the introduction of domestic equipment, while there was no such item in the same period of 2005.

FINANCIAL EXPENSES

Financial expenses were $806,984 for the nine months ended September 30, 2006, as compared to $941,486 for the nine months ended September 30, 2005, a decrease of $134,502 or 14.3%, primarily due to decreased discounting charges resulting from the decreased volume of bills discounted.

INCOME BEFORE INCOME TAXES

Income before income taxes was $8,450,471 for the nine months ended September 30, 2006, as compared to $5,212,972 for the nine months ended September 30, 2005, an increase of $3,237,499 or 62.1%, as a result of an increase in income from operations of $3,035,923 or 49.5%, an increase in other non-operating income of $67,074 or 246.7%, and a decrease in financial expenses of $134,502 or 14.3%.

INCOME TAXES

Income taxes expense was $1,522,067 for the nine months ended September 30, 2006, as compared to $1,150,750 for the nine months ended September 30, 2005, an increase of $371,317 or 32.3%. The increase in income taxes reflects an increase in income before income taxes, and Zhejiang, one of the Company's Sino-foreign Joint-ventures, has ended its two-year tax holiday as of December 2005 and has begun to pay income tax in 2006. The decrease in income taxes reflects that the Company received approximately $510,000 in tax refunds from the Government, while there was no such refunds in 2005. In accordance with the relevant regulations of income taxes stipulated by the Ministry of Finance and the State Administration of Taxation, 40% of domestic equipment purchases are refundable from the increased income taxes of purchasing year over those of the year before.

INCOME BEFORE MINORITY INTERESTS

Income before minority interests was $6,928,404 for the nine months ended September 30, 2006, as compared to $4,062,222 for the nine months ended September 30, 2005, an increase of $2,866,182 or 70.6%, as a result of an increase in income before income taxes of $3,237,499 or 62.1%, and an increase in income taxes of $371,317 or 32.3%.

MINORITY INTERESTS

Minority interests in the earnings of the Sino-foreign Joint-ventures amounted to $3,550,247 for the nine months ended September 30, 2006, as compared to $1,617,073 for the nine months ended September 30, 2005, an increase of $1,933,174 or 119.5%. The increase was primarily due to an increase in net income for two of the Company's Sino-foreign Joint-ventures Henglong and Zhejiang. Minority shareholders own 55.5% of Henglong's equity and 49% of Zhejiang's equity during the nine months ended September 30, 2006, respectively.

NET INCOME

Net income was $3,378,157 for the nine months ended September 30, 2006, as compared to a net income of $2,445,149 for the nine months ended September 30, 2005, an increase of $933,008 or 38.2%, as a result of an increase in income before minority interests of $2,866,182 or 70.6%, and an increase in minority interests of $1,933,174 or 119.5%.

LIQUIDITY AND CAPITAL RESOURCES

Capital resources and use of cash

The Company has historically financed its liquidity requirements from a variety of sources, including short-term borrowings under bank credit agreements, bankers' acceptance, issuances of capital stock and internally generated cash. As of September 30, 2006, the Company has cash and cash equivalents of $18,424,513, as compared to $12,374,944 as of December 31, 2005.

The Company has working capital of $24,036,897 as of September 30, 2006, as compared to $8,006,688 as of December 31, 2005, an increase of $16,030,209.

The Company had bank loans maturing less than one year of $16,229,713 and bankers' acceptance of $12,688,036 as of September 30, 2006. The Company currently expects to be able to obtain more bank loans and bankers' acceptance bills again once it can provide adequate mortgages security. If the Company is not able to do so, it will have to refinance such debt as it becomes due or to repay that debt to the extent it has cash available from operations or from the proceeds of additional issuances of capital stock. The mortgages related to the above-mentioned bank loans and banker's acceptance bills will be devalued by $4,271,328 as a result of depreciation. If the Company expects to be able to obtain $16,229,713 of bank loans and $12,688,036 of banker's acceptance bills, it is required to provide $4,271,328 of mortgages. The Company will obtain fewer loans with reduction of $2,067,446 if it cannot provide enough mortgages ($4,271,328 at 48% mortgage rates). The Company anticipates that the reduction of bank loans will not have a material adverse effect on its liquidity. On March 20, 2006, the Company has entered into a $15,000,000 equity line of credit of Standby Equity Distribution Agreement with Cornell Capital Partners, LP. As of September 30, 2006, the Company has adequate and working capital, as well as $14,700,000 available under the above-mentioned equity line of credit. The Company views these capitals as providing an ample available source of back-up liquidity in case of an unanticipated event.

Financing activities:

(a) Bank loans
As of September 30, 2006, the principal outstanding under the Company's credit facilities and lines of credit was as follows:

Bank	Amount available	Amount borrowed
Comprehensive credit facilities Bank of China	$ 12,484,395	$ 9,277,903
Comprehensive credit facilities China Construction Bank	8,739,076	6,866,417
Comprehensive credit facilities CITIC Industrial Bank	2,496,879	2,496,879
Comprehensive credit facilities Shanghai Pudong Development Bank	4,993,758	3,650,312
Comprehensive credit facilities Jingzhou Commercial Bank	6,242,197	2,496,879
Comprehensive credit facilities Industrial and Commercial Bank of China	1,373,283	1,137,453
Total	$ 36,329,588	$ 25,925,843

The Company could entrust banks to issue notes payable or bank loans within its credit line by a 364-day revolving line. The Company refinanced its short-term debt during early 2006 at annual interest rates of 5.580% to 7.254%, and for terms of six to twelve months. Pursuant to the refinancing arrangement, the Company pledged $22,476,567 of equipment, $5,000,100 land use right and $3,609,288 property as security for its comprehensive credit facility with Bank of China; pledged $2,547,628 land use right and $2,131,361 property as security for its comprehensive credit facility with CITIC Industrial Bank; pledged $1,494,032 land use right and $6,481,885 as security for its comprehensive credit facility with Shanghai Pudong Development Bank; pledged $8,347,378 land use right as security for its comprehensive credit facility with Jingzhou Commercial Bank; pledged $1,344,485 land use right and $908,312 property as security for its comprehensive credit facility with Industrial and Commercial Bank of China; Jiulong, one of the Company’s Joint-venture, has entered into comprehensive credit facilities with China Construction Bank, which was guaranteed by Henglong, the other Joint-venture of the Company.

(b)Financing from investors:

On March 20, 2006, the Company entered into a Standby Equity Distribution Agreement with Cornell Capital Partners, LP with a total amount of $15 million. The Company has utilized $300,000 as of September 30, 2006. Under the agreement, Cornell Capital Partners, LP has committed to provide funding to be drawn down over a 24-month period at the Company's discretion.

If the Company fails to obtain the same or similar terms for any debt or equity refinancing to meet its debt obligation, or fails to obtain extensions of maturity dates of these obligations as they become due, its overall liquidity and capital resources will be adversely affected.

Cash Requirements:

The following table summarizes the Company's expected cash outflows resulting from financial contracts and commitments. The Company has not included information on its recurring purchases of materials for use in its manufacturing operations. These amounts are generally consistent from year to year, closely reflecting the Company's levels of production, and are not long-term in nature (less than three months).

		Payment Upon Due			
	Total	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Short-term bank loans	$ 16,229,713	$ 16,229,713	$ —	$ —	$ —
Notes payable	12,688,036	12,688,036	—	—	—
Other contractual purchase commitments, including information technology	1,626,099	510,990	785,109	330,000	—
Total	$ 30,543,848	$ 29,428,739	$ 785,109	$ 330,000	$ —

Short-term bank loans:

The following table summarizes the contract information of short-term borrowings between the banks and the Company:

Bank	**Purpose**	**Borrowing Date**	**Borrowing Term (Year)**	**Annual Percentage Rate**	**Date of Interest Payment**	**Date of payment**	**Amount**
Bank of China	Working Capital	February 7, 2006	1	5.580%	Pay monthly	February 6, 2007	$ 624,220
Bank of China	Working Capital	March 8, 2006	1	5.580%	Pay monthly	March 7, 2007	1,872,659
Bank of China	Working Capital	May 16, 2006	1	5.850%	Pay monthly	May 15, 2007	2,496,879
Jingzhou Commercial Bank	Working Capital	March 28, 2006	1	7.254%	Pay monthly	March 27, 2007	2,496,879
CITIC Industrial Bank	Working Capital	June 15, 2006	1	5.850%	Pay monthly	June 14, 2007	2,496,879
Shanghai Pudong Development Bank	Working Capital	September 14, 2006	1	5.580%	Pay monthly	September 13, 2007	2,496,879
China Construction Bank	Working Capital	January 20, 2006	1	5.580%	Pay monthly	January 19, 2007	2,496,879

China Construction Bank	Working Capital	February 16, 2006	1	5.580%	Pay monthly	February 15, 2007	1,248,439
Total							$ 16,229,713

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The Company should use the capital under the guidance described in the table. If the Company failed, it will be charged a penalty interest at 100% of the specified loan rate. The Company has to pay interest under the interest rate described in the table on the 20th of each month. If the Company fails, it will be charged compounded interest at the specified rate. The Company has to repay the principal outstanding on the specified date in the table. If it fails, it will be charged a penalty interest at 50% of the specified loan rate. Management believes that the Company had complied with such financial standard as of September 30, 2006, and will continue to comply with them.

The following table summarizes the contract information of issuing notes payable between the banks and the Company:

Purpose	Term (Month)	Due Date		Amount Payable on Due Date
Working Capital	3-6	October, 2006	$	1,114,253
Working Capital	3-6	November, 2006		1,583,895
Working Capital	3-6	December, 2006		1,451,186
Working Capital	3-6	January, 2007		4,617,478
Working Capital	3-6	February, 2007		2,424,469
Working Capital	3-6	March, 2007		1,496,754
Total			$	12,688,036

The Company should use the capital under the guidance described in the table. If it fails, the banks will no longer issue the notes payable, and it may have adverse effect on the liquidity and capital resources of the Company. The Company has to deposit sufficient cash in the designated account of the bank on the due date of notes payable for payment to the suppliers. If the bank had advanced payment for the Company, it will be charged a penalty interest at 150% of the specified loan rate. Management believes that the Company had complied with such financial standards as of September 30, 2006, and will continue to comply with them.

The Company had approximately $1,626,099 of capital commitment as of September 30, 2006, arising from equipment purchases for expanding production capacity. The Company intends to pay off $510,990 in the remaining three months of 2006 using its working capital. Management believes that it will not have a material adverse effect on the Company’s liquidity.

Cash flows:

(a) Operating activities

Three months ended September 30, 2006

The Company’s operations provided cash of $1,294,237 for the three months ended September 30, 2006, as compared to cash of $3,070,659 for the three months ended September 30, 2005, a decrease of $1,776,422, reflecting an increased pledged deposits and inventory. An increase in pledged deposits contributed a $1,686,315 decrease in cash outflow, mainly as a result of certain maturing notes payable in early October 2006, therefore the Company deposited sufficient cash into the banks in advance to prepared for payment to suppliers when those notes mature. An increase in inventory contributed a $2,761,466 increase in cash outflow, mainly due to the Company’s intention to produce sufficient inventories to meet increasing demands in the fourth quarter of 2006, a peak time for the Company. In view of the 364-day revolving notes payable in October and the increased inventories which will be turned into cash in peak season, the Company anticipates that an increase in pledged deposits and inventory will not have a material adverse effect on its future operating activates.

Nine months ended September 30, 2006

The Company's operations provided cash of $3,611,863 for the nine months ended September 30, 2006, as compared to cash of $10,754,403 for the nine months ended September 30, 2005, a decrease of $7,142,540, primarily due to increased accounts and notes receivable. First, cash outflow increased by $4,871,578 along with increased accounts receivables, mainly due to an increase in sales this year of 49.8% as compared to the same period of 2005. The credit terms on sale of goods between customers and the Company generally ranged from 3 - 4 months, which resulted in increased accounts receivable so long as sales increased. This is a normal capital circulation and the Company believes that it will not have a material adverse effect on future cash flows. Second, cash outflow increased by $5,039,566 along with increased notes receivable, mainly due to the Company having sufficient working capital this year and reducing the discount on notes receivable to save interest expenses. Since the notes payable were based on bank credit standing, they might turn into cash any time as the Company elects. Therefore, the increase of notes receivable will not have a material adverse effect on the Company's future operating activities.

(b) Investing activities

Three months ended September 30, 2006

During the three months ended September 30, 2006, the Company expended net cash of $2,547,752 in investment activities, as compared to $3,252,490 for the same period of 2005, a decrease of $704,738. The main investment activities during this period are purchase of property, plant and equipment for newly incorporated joint ventures. Currently, the projects are in their early preparatory stage and the Company will complete them next quarter. Management believes that these investing activities will not have a material adverse effect on the Company's future operating activities, because the capital required for purchase of property, plant and equipment for the newly incorporated joint ventures will be contributed by the shareholders on a timely basis.

Nine months ended September 30, 2006

During the nine months ended September 30, 2006, the Company expended net cash of $4,655,210 in investment activities, as compared to $9,710,451 for the same period of 2005, a decrease of $5,055,241. The main investment activities during this period are purchase of property, plant and equipment for newly incorporated joint ventures. Currently, the projects are in their early preparatory stage and the Company will complete them next quarter. Management believes that these investing activities will not have a material adverse effect on the Company's future operating activities, because capital required for purchase of property, plant and equipment for the newly incorporated joint ventures will be contributed by the shareholders on a timely basis.

(c) Financing activitiesæ

Three months ended September 30, 2006

During the three months ended September 30, 2006, the Company expended net cash of $114,472 in financing activities, as compared to providing net cash of $1,826,479 for the three months ended September 30, 2005, a decrease of $1,940,951, principally due to reduced demand for bank loans during this period, resulting from timing differences in bank loans and revolving credit lines.

Nine months ended September 30, 2006

During the nine months ended September 30, 2006, the Company obtained net cash of $6,491,517 through financing activities, as compared to $491,293 for the nine months ended September 30, 2005, an increase of $6,000,224 as a result of following factors:

(1) Net cash provided in financing activities increased during the period as a result of issuing common stock and financing: For the nine months ended September 30, 2006, the Company raised $4,926,000 of cash by issuing 654,589 shares of common stock to organizational investors for investment of new joint ventures, and raised additional $101,240 of cash due to exercise of options by independent directors. The Company raised a total $5,027,240 of net cash during the nine months ended September 30, 2006.

(2) Net cash provided in financing activities increased during the period as a result of an increase in capital investment by minority shareholders of joint ventures: The minority shareholders of joint ventures have contributed $1,420,926 during the nine months ended September 30, 2006, including Shanghai Hongxi Investment Inc., the minority shareholder of USAI investing $436,954; HongKong Tongda, the minority shareholder or Jielong investing $135,034; and Wuhu Chery Technology Co., Ltd., the minority shareholder of Wuhu investing $848,936 by cash. During the nine months ended September 30, the net cash inflow from capital contribution by minority shareholders of Sino-foreign joint ventures was $1,420,926 .

OFF-BALANCE SHEET ARRANGEMENTS

At September 30, 2006 and 2005, the Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements.

COMMITMENTS AND CONTINGENCIES

The following table summarizes the Company’s contractual payment obligations and commitments as of September 30, 2006:

Payment Obligations by Period

	2006(a)	**2007**	**2008**	**2009**	**2010**	**Thereafter**	**Total**
Obligations for service agreement	$ —	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 550,000
Obligations for purchasing agreement	$ 510,990	$ 565,109	$ —	$ —	$ —	$ —	$ 1,076,099
Total	$ 510,990	$ 675,109	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 1,626,099

(a) Remaining 3 months in 2006.

SUBSEQUENT EVENTS

None

Item 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

CREDIT RISK: The Company’s financial instruments that are exposed to concentration of credit risk consist primarily of cash and cash equivalents, accounts receivable from customers and other receivable due from related parties, which were controlled by Mr. Hanlin Chen, the Company’s Chairman.

Cash and cash equivalents are maintained with major state-owned banks in the PRC. The Management has not evaluated the credit risk from banks based on its notion that state-owned banks command considerable funds with good reputation.

The Company’s business activity is primarily with customers in the PRC. The Company periodically performs credit analysis and monitors the financial condition of its clients in order to minimize credit risk. Because of the increase of activities and business, and the increase of customers’ accounts receivable, there is no assurance that foresaid measures will be completely effective. The Company has approximately $33,000,000 of accounts receivable as of September 30, 2006, the Company’s revenues and/or operating cash flow would be materially and adversely affected if there is a 3% allowance for doubtful accounts which is a reduction of approximately $1,100,000 for the Company.

Other receivables due from related parties, was $5,722,836 as of September 30, 2006. These amounts will be due on demand on or before December 31, 2006, if related parties fail to pay on schedule, it is expected to have a material effect on the Company's operating cash flow.

CURRENCY EXCHANGE RATE RISK: The Company's currency exchange rate risks consist primarily of currency from financing. The Company's financing activities were settled in US dollars and deposited in its bank account in US dollars, while the Company conducts virtually all of its business and investment activity in China and the value of its business is effectively denominated in Renminbi. The Company converts US dollars into RMB to conduct its investment activities and business. The Company does not hedge its RMB - US dollar exchange rate exposure. The Company has dollar holdings of approximately $3,900,000 as at September 30, 2006, if the exchange rate between US dollars and RMB were to increase by 10%, the Company would potentially suffered loss of approximately $390,000. Therefore, the Company will choose to reduce its exposures through financial instruments (hedges) that provide offsets or limits to its exposures when considered appropriate.

MARKET INTEREST RATE RISK: The Company has $30,000,000 of short-term revolving credit lines with annual interest expenses of $1,770,000 based on full utilization at current rates. Bank loan rates in China have a history of volatility and have been rising recently, and if market interest rates increase by 10%, such increases could result in increased loan interest for the company.

RISK OF INVENTORY PRICES: The risk to inventory prices of the Company comes from the upward movement in prices of raw materials and the downward movement of selling price. In recent years, price fluctuation on raw materials was not excessive, but prices for steering gear have fluctuated significantly. During the years 2003-2005, prices for steering gear have decreased approximately 10% each year on average. In 2005, the output and sales of domestic commercial vehicles has decreased greatly as compared to 2004, as a result of state macro-controls. One of the Joint-ventures of the Company, Jiulong, also suffered similarly as a supplier of commercial vehicles. There is no sign that the market will recover. As of September 30, 2006, Jiulong's inventory amount was approximately $6,000,000. If selling prices of steering gear decreases by 10%, then the income of the Company will decrease by $600,000. In 2006, the Company will take the following two measures to reduce inventories to a reasonable level thus decreasing the risk from inventory prices:
(1) Further develop the market in order to utilize finished goods inventory through increased sales.
(2) Improve internal information flows, balance inventories in various warehouses, and avoid unnecessary production.
But there is no assurance that the aforesaid measures will be effective.

ITEM 4. CONTROLS AND PROCEDURES

(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES
The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the Securities and Exchange Commission, the "SEC". The Company's disclosure controls and procedures are also designed to ensure that information required to be disclosed in the reports filed under the Exchange Act of 1934, the "Exchange Act", is accumulated and communicated to management, including its principal executive and financial officers, as appropriate, to allow timely decisions regarding required disclosure.

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including its principal executive and financial officers, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon and as of the date of that evaluation, the Company's principal executive and financial officers concluded that the Company's disclosure controls and procedures are effective to provide reasonable assurance that information the Company is required to disclose in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to its management, including its chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

(b) CHANGES IN INTERNAL CONTROLS

There was no change in the Company’s internal control over financial reporting that occurred during its last fiscal quarter that has materially affected, or is reasonably likely to materially affect, its internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

The Company is not currently a party to any threatened or pending legal proceedings, other than incidental litigation arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

ITEM 1A. Risk Factors

Risks Factors that May Affect Our Results

The Company’s businesses, 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:

<u>Risks Related to the Company’s Business and Industry</u>

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, molded 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 nine months ended September 30, 2006, approximately 13.9% of the Company's sales were to Brilliance China Automotive Holdings Limited, approximately 11.0% of the Company's sales were to Beiqi Foton Motor Co., Ltd., approximately 15.6% of the Company's sales were to Chery Automobile Co., Ltd. and approximately 10.5% of the Company's sales 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 requirement. 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, particularly engineers and other employees with electronics expertise, 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 87.2% of its outstanding common stock and may have conflicts of interest with its minority stockholders.

Members of the Company's management beneficially own approximately 87.2% 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 13% 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 are 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 enterprises, 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 negative 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 23,289,495 shares of common stock outstanding as of September 30**,** 2006, 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 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.

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 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS. None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES. None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS. None.

ITEM 5. OTHER INFORMATION. None.

ITEM 6. EXHIBITS

A list of exhibits required to be filed as part of this report is set forth in the Index to Exhibits, which immediately precedes such exhibits, and is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CHINA AUTOMOTIVE SYSTEMS, INC.
(Registrant)

Date: November 13, 2006 By: /s/ HANLIN CHEN
Hanlin Chen,
President and Chief Executive Officer

Date: November 13, 2006	By:	/s/ DAMING HU Daming Hu, Chief Financial Officer

INDEX TO EXHIBITS

Exhibit Number	Description of Document
3(i).1	Certificate of Incorporation*
3(i).2	Certificate of Amendment of Certificate of Incorporation**
3(ii).1	By - laws***
10.1	Standby Equity Distribution Agreement dated March 20, 2006 between the Company and Cornell Capital Partners, LP****
10.2	Placement Agent Agreement dated March 20, 2006 between the Company and Newbridge Securities Corporation****
10.3	Registration Rights Agreement dated March 20, 2006 between the Company and Cornell Capital Partners, LP****
10.4	Securities Purchase Agreement dated March 20, 2006 between the Company and Cornell Capital Partners, LP****
10.5	Investor Registration Rights Agreement dated March 20, 2006 between the Company and Cornell Capital Partners, LP****
10.6	Warrant to purchase 86,806 shares of common stock at $14.40 per share, issued to Cornell Capital Partners, LP****
10.7	Warrant to purchase 69,444 shares of common stock at $18.00 per share, issued to Cornell Capital Partners, LP****
10.8	Joint-venture Agreement, dated March 31, 2006, as amended on May 2, 2006, between Hongkong Great Genesis Group Co., Ltd. and Wuhu Chery Technology Co., Ltd.*****
21.1	Subsidiaries of the Company******
31.1	Rule 13a-14(a)/15d-14(a) Certification -Hanlin Chen******
31.2	Rule 13a-14(a)/15d-14(a) Certification -Daming Hu******
32.1	Section 1350 Certification -Hanlin Chen******
32.2	Section 1350 Certification - Daming Hu******

* Incorporated by reference to exhibit 3(i) to the Company's Form 10SB Registration Statement filed on August 27, 2001.

** Incorporated by reference to Appendix A to the Company's Schedule 14C Definitive Information Statement filed on April 21, 2003.

*** Incorporated by reference to exhibit 3(ii) to the Company's Form 10SB Registration Statement filed on August 27, 2001.

**** Incorporated by reference to the exhibit of the same number to the Company's Form S-3 Registration Statement (File No. 333 - 133331) filed on April 17, 2006.

***** Incorporated by reference to the exhibit 10.8 to the Company's Form 10Q Quarterly Report on May 10, 2006.

****** Filed herewith