

General

The Board of Directors of Diesel & Motor Engineering PLC has pleasure in presenting the Annual Report of the Board of Directors and audited Consolidated Financial Statements for the year ended 31st March 2010.

The Financial Statements have been prepared in accordance with the Sri Lanka Accounting Standards as required by the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 and conform to the requirements of the Companies Act No. 07 of 2007.

Principal Activities

The principal activities of the Group include import, sale and repair of passenger cars, commercial vehicles, material handling machinery, storage systems, construction machinery, agri machinery, medical equipment, power engineering solutions, power engines, power tools and import and sale of vehicle spares, components accessories and lighting products. Group activities also include manufacture and sale of retreaded tyres.

There was no significant change in:

- The nature of business of the Company or its subsidiaries except discontinuation of telecommunication sale and services business.
- The classes of business in the associate companies during the year that may have a significant impact on the state of the Company's affairs.

Group Structure

A diagram depicting the Group Structure is available on page 126.

Business Review and Future Developments

A review of financial and operational performance and future business developments of the Group are contained in the Chairman and CEO's Review (Pages 10 to 13), Business Performance Report (pages 20 to 47) and financial review (pages 48 to 55) These reports together with the Audited Financial Statements reflect the state of affairs of the Companies and Group.

Financial Statements

The Financial Statements of the Company and the Group appearing on pages 136 to 164 are prepared in conformity with the Sri Lanka Accounting Standards as required by Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 and comply with the requirements of the Companies Act No. 07 of 2007.

Financial Statements of the Company and the Group for the year ended 31st March 2010 certified by the General Manager - Finance and Controlling that it conforms to the requirements of the Companies Act No. 7 of 2007, and signed by the Chairman and Chief Financial Officer, are given on page 137 form an integral part of the Annual Report of the Directors.

Auditors' Report

The Financial Statements for the year ended 31st March 2010 have been audited by Messrs KPMG Ford, Rhodes, Thronton & Co. (Chartered Accountants) and their Report is given on page 135.

Significant Accounting Policies

The Significant Accounting Policies adopted in the preparation of Financial Statements are given on pages 142 to 146 of the Annual Report.

There were no material changes in the Accounting Policies adopted with that of last year.

Directorate

List of Directors

As at 31st March 2010, the Board of Directors of Diesel & Motor Engineering PLC consisted of eleven members. Qualifications and experience of the Directors are given on pages 14 and 15 of this Annual Report.

Following were the Directors of the Company as at the end of the financial year:

- A.R. Pandithage (Chairman, Managing Director & Chief Executive Officer)
- A.G. Pandithage (Deputy Chief Executive Officer)
- A.N. Algama (Executive Director)
- S.C. Algama (Executive Director)
- Dr. H. Cabral (Independent Non-Executive Director)
- B.C.S.A.P. Gooneratne (Executive Director)
- Dr. U.P. Liyanage (Independent Non-Executive Director)
- A.M. Pandithage (Non-Executive Director)
- T.G.H. Peries (Executive Director)
- R. Seevaratnam (Independent Non-Executive Director)
- R.C. Weerawardane (Executive Director)

Resignations, New Appointments and Re-elections to the Board

There were no new appointments made to the Board, during the financial year ended 31st March 2010.

Dr. H. Cabral, Dr. U. Liyanage, Mr. B.C.S.A.P. Gooneratne, and Mr. S.C. Algama retired by rotation in 2008/09 and were reappointed to the Board in accordance with the Articles by re-election at the Annual General Meeting during the year.

Mr. A.N. Algama, Mr. A.M. Pandithage, Mr. T.G.H. Peries and Mr. R. Seevaratnam retire by rotation in accordance with the Articles of Association and being eligible offer themselves for re-election at the AGM.

Directors' Responsibilities for Financial Statements

The Directors are responsible for the preparation and presentation of Financial Statements of the Company to reflect a true and fair view of the state of its affairs. The Statement of Directors' Responsibilities for the Financial Statements is given on page 134 of this Annual Report.

Directors' Shareholdings

The Directors and their close family members held 3,650,719 (2008/09 - 3,476,894) ordinary shares of the Company, which amounts to 41.96% (2008/09 - 39.95%) of the ordinary shares issued as at 31st March 2010.

The shareholdings of Directors and their close family members as at 31st March 2010 are as follows:

As at 31st March	2010 Shareholding - No. of Shares			2009 Shareholding - No. of Shares		
	Director	Spouse & Children under 18	Total	Director	Spouse & Children under 18	Total
A.R. Pandithage	971,798	910,297	1,882,095	971,798	910,297	1,882,095
A.N. Algama	261,872	-	261,872	264,172	-	264,172
A.M. Pandithage	178,745	41,033	219,778	178,745	41,033	219,778
A.G. Pandithage	515,505	44,165	559,670	339,380	44,165	383,545
S.C. Algama	392,278	6,856	399,134	392,278	6,856	399,134
T.G.H. Peries	191,284	136,886	328,170	191,284	136,886	328,170
	2,511,482	1,139,237	3,650,719	2,337,657	1,139,237	3,476,894

Interest Register

The Interest Register is maintained by the Company as required by the Companies Act No. 07 of 2007. The following entries were made during the year under review:

• Directors' Interest in Contracts

The Directors' interest in contracts are disclosed in the annexure to the Annual Report of the Board of Directors on page 133.

• Acquisition/Disposal of Shares by Directors

176,125 shares were transmitted to Mr. A.G. Pandithage during the year.

2,300 shares were disposed by Mr. A.N. Algama during the year.

• Directors' Remuneration

Directors' remuneration in respect of the Group and the Company are given on Note 8 to the Financial Statements on page 149.

• Insurance

The Directors' and Officers' Liability insurance policy was renewed during the year.

All directors have disclosed the nature and extent of their interest in relation to any transaction with the Company as per the Section 192 of the Companies Act.

During the year there were no instances pertaining to the voting on matters on which Directors had a material interest.

Directors' Meetings

The number of Directors' meetings, Board Committee meetings and their attendance details are presented in the Enterprises Governance Report on page 107.

Internal Control System and Risk Management

The Board considers that strong internal controls are integral to the sound management of the Company and is committed to maintaining strict financial, operational and risk management controls over all its activities. The Group Management Committee has put in place an effective and

comprehensive system of internal controls covering financial, operational and compliance control. The Directors have outsourced a part of the internal audit function to review and report on the effectiveness of the internal controls.

The Risk Management Report is available on pages 117 to 120.

The Board is satisfied with the effectiveness of the system of internal controls for the year under review and up to the date of approval of the Annual Report and the Financial Statements.

Board Committees

The Board, while assuming the overall responsibility and accountability for the affairs in the management of the Company, has appointed committees with specific terms of reference. Accordingly, the following Committees have been constituted by the Board.

- Audit Committee
- Remuneration Committee
- Nomination Committee

The Reports of the above committees are given on pages 121 to 123 of this Annual Report.

Auditors

The Company's Auditors during the period under review were Messrs KPMG Ford, Rhodes, Thornton & Co., Chartered Accountants.

The Auditors - were paid Rs. 1.75 mn for the year ended 31st March 2010 (2008/09 - 1.35 mn) as Audit fees by the Group. In addition, Auditors were paid Rs. 0.16 mn (2008/09 - Rs. 0.43 mn) for audit-related services and Rs. 2.99 mn (2008/09 - Rs. 0.63 mn) for non-audit services, by the Group.

Based on the declaration made by Messrs KPMG Ford, Rhodes, Thornton & Co., Chartered Accountants and as far as the Directors are aware, the Auditors do not have any other relationship or interest in contracts with the Company or with any of its Subsidiaries.

Appointment of Auditors

The retiring Auditors - Messrs KPMG Ford, Rhodes, Thornton & Co., Chartered Accountants are willing to continue in office. A resolution on reappointing them as Auditors and granting authority to the Directors to decide their remuneration will be proposed at the Annual General Meeting.

Turnover

The Company recorded a turnover of Rs. 9,557 mn in 2009/10 (for 2008/09 - Rs. 8,667 mn). The Group turnover for 2009/10 is Rs. 10,530 mn (for 2008/09 - Rs. 9,187 mn).

Segment turnover and other segment information are available on pages 147 and 148.

Human Resources

The Group promotes to its employees the need for the highest standards of integrity and ethics in business dealings, including compliance with all relevant legislation and codes of practice. Employees are regarded as the key to being able to translate policies and strategies into commercial success.

The Group is committed to providing a working environment in which this process can succeed.

Adequate measures are taken to ensure that all employees have the opportunity to understand and appreciate the Group's objectives and policies. The employment policy of the Group embodies the principal of equal opportunity. The Group aims to create an opportunity for participation and involvement, identification and development of skills, promote the use of initiative and to stimulate personal advancement. Reward systems recognise success at both the corporate and individual level. The number of persons employed by the Company and its subsidiaries at the year end was 864 (2008/09 - 870).

Health and Safety

The Group safeguards occupational health and hygiene of its employees by providing a safe working environment and complying with all relevant statutory obligations. The Group also has an employees' medical scheme and expenditure in relation to this for the year was Rs. 14,759,291/-.

Quality

The Group is committed to maintaining its long established reputation of being a symbol of quality. All employees are encouraged to regard the continuous improvement of quality standards as a key to competitive advantage.

Operational Results and Dividends of the Group

	2009/10 Rs. '000	2008/09 Rs. '000
Turnover		
The Gross Turnover	10,530,587	9,187,966
Profit		
After making provision for bad and doubtful debts and all known liabilities and after charging a sum of Rs. 94,887,174/- (2008/09 - Rs. 97,615,652/-) for depreciation of property, plant & equipment the profit made by the Group before tax was	420,095	175,082
Income tax expense	(141,842)	(72,054)
Group profit after taxation from continuing operations	278,253	103,028
Loss from discontinued operations	(29,956)	(13,584)
Group profit after taxation	248,297	89,444
Retained earnings brought forward	367,443	520,221
Surplus on actuarial valuation of retirement benefit obligations at the beginning of the year	-	8,028
Appropriations		
Dividend paid	(52,214)	(30,250)
Transfers to general reserve	-	(220,000)
Available for appropriation	563,526	367,443

Dividends on Ordinary Shares

The Directors approved a final dividend of Rs. 4/- per share (2008/09 - Rs. 3 per share - Final) payable on 9th June 2010 to the shareholders of the issued ordinary shares of the Company as at close of the business on 31st May 2010. In accordance with Section 56 of the Companies Act No. 07 of 2007, a solvency test was carried out by the Company's Auditors, prior to recommending the final dividend.

Income Tax

It is the Group's policy to provide for deferred taxation on all known temporary differences. The income tax rate applicable to all companies in the Group is 35%. Tax on export profit is 15%.

Statutory Payments

Directors, to the best of their knowledge and belief, confirm that all statutory liabilities including EPF, ETF and taxes have been made on time during the financial year.

Donations

The donations made during the year amounted to Rs. 1,165,505/- (2008/09 - Rs. 859,834/-).

Property, Plant & Equipment

Group expenditure on property, plant & equipment during the year amounted to Rs. 36,886,566/- (2008/09 - Rs. 118,096,174/-). Information relating to movement in property, plant & equipment is given in Note 13 to the Financial Statements.

Market Value of Freehold Land

A qualified independent valuer last revalued the freehold land of the Company on 30th September 2008 and the carrying value of the freehold land has been adjusted accordingly. The details of the freehold land are given in Notes to the Financial Statements on page 154.

Group Investment/Divestment

There were no new equity Investments made during the year.

After continuous monitoring of the market environment and the performance of business operation the Board decided to divest its 49% holding in Dimo KLN Industries (Pvt) Ltd. and 45% holding in Browns Dimo Products Industrial (Pvt) Ltd. The Financial Statements have been prepared giving due recognition to the above decisions.

Discontinued Operations

Upon review of the feasibility of the continuity of telecommunication sales and services business, the Board decided to exit from the said business, during the year. This business made a loss of Rs. 29,956,101/-. Carrying value of assets pertaining to this business have been adjusted to reflect their realisable value, unless they are transferred to other business units of the Group.

Stated Capital

The stated capital of the Company as at 31st March 2010 was Rs. 182.5 mn (in 2009 - Rs. 182.5 mn). The number of shares in issue as at 31st March 2010 was 8,702,389 (2008/09 - 8,702,389).

Reserves

The total reserves as at 31st March 2010 stand at Rs. 2,018,427,956/- (2008/09 - Rs. 1,822,344,084/-) comprising capital reserves of Rs. 1,135,611,833/- (2008/09 - Rs. 1,135,611,833/-) and revenue reserves of Rs. 882,815,956/- (2008/09 - Rs. 686,732,251/-). The movement in reserves during the year is set out in the Statement of Changes in Equity on page 138.

Share Information

Information relating to shareholding, earnings net assets per share, market value of shares, dividends and share trading are available on pages 166 to 168.

Shareholdings

There were 1,196 registered shareholders as at 31st March 2010. The percentage of shares held by the public as at 31st March 2010 was 43% of the issued shares. The twenty major shareholders as at 31st March 2010, the number of shares held and their percentage shareholding are given on page 166.

Equitable Treatment to Shareholders

The Directors at all times ensure that all shareholders are treated equitably.

Compliance with Laws and Regulations

To the best of the knowledge and belief of the Directors, the Company has not engaged in any activities contravening the laws and regulations of the country.

Outstanding Litigation

In the opinion of the Directors and the Company Lawyers and legal counsel, litigations currently pending against the Company will not have a material impact on the reported financial results or future operations of the Company. The details of the litigations against the Company are given on page 164.

Events Occurring after the Balance Sheet Date

There have not been any material events that occurred subsequent to the date of the Balance Sheet which require adjustments to or disclosure in the Financial Statements.

Contingencies and Commitments

Information on Contingent Liabilities and Capital Commitments as at 31st March 2010 are given in Note 36.2 to the Financial Statements.

Going Concern

The Board of Directors has reviewed Group's Budget, availability of banking facilities and other necessary information and is satisfied that the Group has adequate resources to continue in business for the foreseeable future. Accordingly, going concern basis has been adopted in preparation of the Financial Statements.

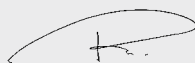
Amendments to the Articles of the Association

In order to comply with a requirement of the Colombo Stocks Exchange a Special Resolution is to be passed at the Annual General Meeting, amending the articles. The Notice of Meeting contains the Special Resolution to be passed.

Annual General Meeting

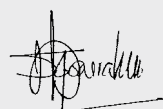
The Annual General Meeting will be held at the Registered Office of the Company, No. 65, Jetawana Road, Colombo 14 on 29th June 2010. The Notice of Annual General Meeting is given on page 163.

By order of the Board of Directors,



A.R. Pandithage

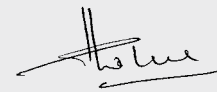
Chairman, Managing Director &
Chief Executive Officer



B.C.S.A.P. Gooneratne

Secretary

Colombo
18th May 2010



R.C. Weerawardane

Director