



ABOUT **DIMO**

Investing in Sustainable Futures

Dimo's portfolio consists of the world's most respected brands. We offer Sri Lankan customers the world's leading brands of passenger vehicles, commercial vehicles, material handling machinery, medical equipment, telecommunication solutions, electrical engineering solutions, power engines, power generation equipment, power tools, lighting equipment and other accessories.

We aim to deliver sustainable and creative value to our customers, our employees, our shareholders, our business partners, our financial partners, and the people of Sri Lanka. Our goal is to lead the pack in all our areas of business while investing in robust and rosy futures for generations yet unborn.

A New Excellence

Four key ideas drive Dimo's brand of entrepreneurship:

- Creating sustainable social wealth
- Being customer centric
- Designing imaginative solutions
- An unyielding commitment to the highest business ethics

This business framework, a unique type of Dimo flair, and an insatiable will to succeed, have helped us establish a new level of excellence for corporate activity in this country. Today we push that bar a little higher...

Vision To be the leader in all the businesses we are engaged in, by building a world-class team and partnering with the best in the world, to deliver, lasting and outstanding value to all our stakeholders.

The Values that Guide us Customer first; Partner with the world's best; Make work enjoyable and rewarding; Never compromise on Dimo's ethics; Benefactor of society and friend of the environment.

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HIGHLIGHTS

| | 2006/2007 Rs. '000 | 2005/2006 Rs. '000 | Change % | 2004/2005 Rs. '000 |
|---|-----------------------|-----------------------|-------------|-----------------------|
| Results for the year | | | | |
| Group turnover | 12,989,916 | 10,512,326 | 24 | 7,565,327 |
| Group profit before tax | 512,895 | 382,235 | 34 | 253,633 |
| Group profit after tax | 301,777 | 265,172 | 14 | 177,202 |
| Gross dividends | 72,600 | 60,000 | 21 | 50,000 |
| Group value added | 3,460,720 | 2,798,856 | 24 | 1,868,456 |
| Group revenue to government | 2,206,250 | 1,829,615 | 21 | 1,202,565 |
| Group net profit after tax as a % of gross turnover | 2.32 | 2.52 | (8) | 2.34 |
| Return on average capital employed % | 23.33 | 19.55 | 19 | 20.05 |
| Interest cover (Times) | 2.11 | 2.44 | (13) | 2.74 |
| Dividend cover (Times) | 4.16 | 4.42 | (6) | 3.54 |
| Price earnings (Times) | 4.66 | 5.22 | (11) | 5.81 |
| Dividend yield (%) | 5.00 | 4.33 | 15 | 4.85 |
| Position at the year end | | | | |
| Shareholders' funds | 1,506,508 | 1,216,030 | 24 | 1,005,858 |
| Total assets | 5,198,632 | 4,569,611 | 14 | 3,195,407 |
| Group employment (No. of persons) | 862 | 778 | 11 | 635 |
| Current ratio (Times) | 1.30:1 | 1.33:1 | – | 1.24:1 |
| Market capitalisation | 1,452,000 | 1,385,000 | 5 | 1,030,000 |
| Per share | | | | |
| Dividend (Rs.) | 6.00 | 6.00 | – | 5.00 |
| Earnings (Rs.) | 25.76 | 22.96 | 12 | 17.72 |
| Markert value (Rs.) - at year end | 120.00 | 138.50 | (13) | 103.00 |

OPERATIONAL HIGHLIGHTS



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02



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04



05

01 The latest addition - DIMO BATTAs **02** Commercial operations of the tyre retreading factory commenced
03 The recently introduced Mercedes-Benz R-Class **04** Introduction of a large fleet of TATA buses to the national transport network **05** The brand new showroom at Kurunegala

CHAIRMAN & CEO'S **REVIEW**

“Care A Word We
Simply

Every year we raise the Standard of Care a little higher

The essence of Dimeo is the standard of care we have developed over the years. Customer, employee, principal, the community and the natural environment are all recipients of this unique brand of care, honed and polished to a fresh level every year.

After-care relationships with our customers are passionate, committed and technologically appropriate for the product bought. Dimeo employees are cared for with dignity and working environments harness talent, provide security and inspire our employees to new levels of excellence.

Principals benefit from a relationship that is mutually beneficial. While we enhance their market shares and apply our unique standard of care to their products, our principals provide the technology and the 'know-how' to help us constantly enhance this standard of after-care.

Caring for the community is a fundamental Dimeo value. While we create financial value we do so with responsibility and a sense of caring for the community. Our systems of care are geared to reduce wastage, reuse wherever possible and nourish the natural environment for the next generation.



Passionately About

Care

”



Sustaining Growth, Profitability and Responsibility. Reporting on yet another year of high performance.

Dear Shareholder,

I am pleased to present the Annual Report and Audited Accounts of your Company and its subsidiaries for the year ended 31st March 2007. As these have been in your hands for the required period of time, it is proposed with your permission to take them as shareholder.

The year under review was a year of considerable challenge. The challenges were of such a magnitude that they overshadowed the significant progress we achieved during the year. One of the major challenges we faced was the substantial increase in interest rates and this affected Dimeo in two important ways. First it gave rise to a sizable increase in financial costs. Secondly, it had a negative impact on our sales, since our products are capital goods, often financed by borrowings.

Despite these challenges, profit before tax and turnover grew substantially, and the Company ended the year on a very satisfactory note. The steep increase in the interest rates is a matter of great concern.

While managing growth, it was also necessary to make prudent investments in the non-auto sector, which is very much a part of our strategic plan. Such substantial achievements in a year that presented considerable challenge, gives my team and me a sense of accomplishment.

Keeping Stakeholders Informed

This report documents in as much detail as possible, the business environment, the activities, results, financial position, and our future prospects, short, medium and long term.

While conforming to legal and statutory requirements, we have gone beyond these to provide details that will enable our stakeholders to be updated on the performance and prospects of the Group.

Global Developments

During the year under review, the Euro strengthened against the Dollar by 5.3%. Steel prices and all commodities, which are directly related to the auto and machinery industry increased during the year.

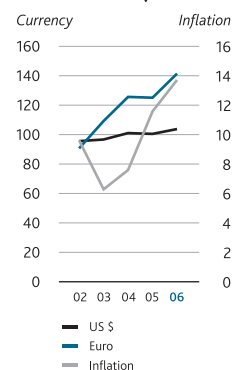
The Company's volume of imports from India has grown over the years and this has changed the geographical composition of our portfolio. Our offerings from India have improved both in quality and value over the years.

Local Developments

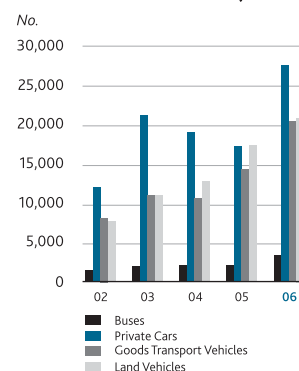
The Sri Lankan economy grew by 7.4% in 2006*, once again demonstrating its resilience. This growth rate was the highest recorded since 1978. Despite this growth, emerging inflationary threats are however, a matter of serious concern.

The government policy change with regard to tax on passenger cars and SUV's over 1000 cc has had an impact on your Company's vehicles business. Other sectors that the Company is involved saw a

Currency vs. Inflation (31st Dec.)



Registration of Motor Vehicles (31st Dec.)



*Source: Central Bank Annual Report - 2006

CHAIRMAN & CEO'S REVIEW

significant growth. More details on the industry environment of the Company's business segments can be found in the Business Review from pages 14 to 33.

The high interest environment has affected all our products, particularly the automobile market. Leasing interest rates have correspondingly snowballed and this has made vehicles more costly. Despite these conditions and increasing government levies, the Company increased market shares and took profitability to a new level confirming the confidence customers have in the products and solutions that 'Dimo Care' is able to offer.

The country is still trying to produce human resources with the skills and mindset that the private sector requires. The vocational training system does not produce people in sufficient numbers with relevant skills for the auto industry, leaving that burden to the private sector. The Dimo Automobile Training School is an initiative that the Company has taken to fill this gap.

Maintaining our High Performance

We are optimistic about Dimo's performance over the short to medium term. We are confident that we can make a quantum leap in profitability and growth during this period and take your Company to a new level of performance. The external environment and the volatile political situation continue to concern us but we are making every effort to ensure that the Company's growth stays on track despite adverse external conditions.

The past financial year was a year of high performance for Dimo. Your Company has grown phenomenally over the previous three years and last year was no different. Our pre-tax profit for 2006/07 was Rs. 512 mn, an impressive 34% increase over the previous year. Group turnover was Rs. 13 bn, a growth of 23.6%, but profit after tax grew only by 13.8% during the year under review. This was because of higher tax payments.

Rewarding our Shareholders

Your Board has paid an interim dividend of Rs. 3/- per share and a final dividend of Rs. 3/- per share is proposed for the financial year 2006/07. The dividend outflow will be enhanced by the increase in share capital.

Business Priorities

Funding Investments

The Company has built a strong reputation with our principals and customers with regard to Dimo's unique post-sales care. This has placed the Company in a position of strength to attract more world-class brands and businesses. The Company carefully selects the businesses it should invest in, maintaining a fine balance between investments in resources and long-term sustainable growth opportunities.

Business Spread:

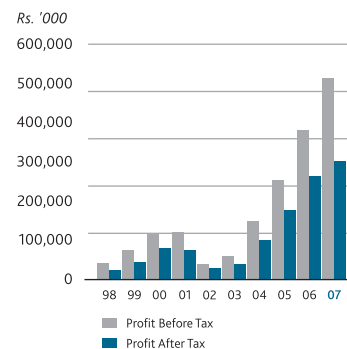
Building a Stronger Base for Growth

We will continue with our strategy of remoulding our product mix. While we were initially an automobile oriented company, Dimo has over the years progressively moved into other industries.

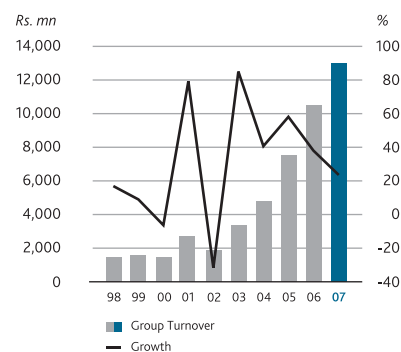
We will expand our non-auto businesses that have growth potential, for example in power engineering and building technology. We are also venturing into new business areas such as car park management systems, consultancy services with regard to warehousing and material handling, and the supply of health-care consumables. The Group has also recently gone into manufacturing and this will provide a stronger base for growth.

The broad spectrum of products we now have within the Dimo brand has enhanced our competitiveness and our potential for growth. We will continue to refashion our product-mix to ensure that we retain our competitive edge and are not dependent on any single industry for growth.

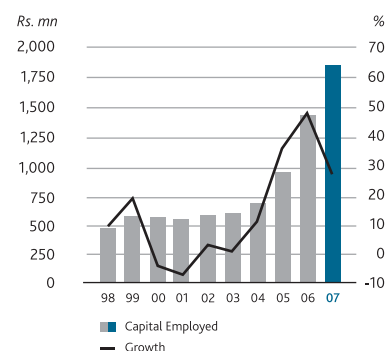
Profit Before Tax & Profit After Tax



Group Turnover



Capital Employed



CHAIRMAN & CEO'S REVIEW

We have made two strategic investments in the past two years. The first was in a tyre rebuilding plant at Homagama - a fully-owned subsidiary. This plant commenced operations in April 2006 and has already shown good results. The other is in an auto filter manufacturing plant at Kandana, in partnership with KLN India, which will commence commercial production on the 1st of June 2007. These new investments will also contribute to fuel our growth in the short to medium term.

Sustaining Relationships

The strength of the Company over the years has been the Dimo brand. Although we represent 56 of the world's leading brands, our mindset has not been one of just selling a product. Our goal has been to add value to our customers by giving them globally renowned products fortified by the nationally celebrated 'Dimo Care'.

The purchase of a product from Dimo does not conclude a deal with the customer. Rather it marks the beginning of a long-term relationship where we endeavour to provide continuous solutions to the customer. Through the Dimo branded after sales service, we attempt to provide constant assurance to customers that we are 'there' whenever they need us.

Over the years the Company has invested in human resources and necessary tools and equipment to provide customers with continuing solutions for their products after purchase. We have taken the Dimo standard of care to higher levels over the years and attempt to ensure that we delight the customer at every stage beyond the point of sale.

Keeping up with Technology

Most of the principals that we represent possess state-of-the-art technology and many of them are technology leaders. They in turn, impose stringent requirements on us. Maintaining these standards is a high priority in our business strategy.

Agility

Mergers have become common in the global business environment. Such acquisitions and diversifications can have an impact on our principals' business patterns and it is of paramount importance that we keep sufficiently agile. Towards this end, we constantly gear our resources and our technological know-how to an extent that our principals consider Dimo as their most preferred partner to do business in Sri Lanka.

Solving the Problem of Space

The Group has grown exponentially during the last five years. This has created a huge demand on our physical space. There is a need to accommodate higher levels of inventories and a need to accommodate employees recruited for the expanding business. Our inventories have increased from Rs. 483 mn to Rs. 2,097mn and our employees have increased from 595 to 862 over the past five years.

Challenges

There are two main challenges the Company faces in the short term: responding to changes in the external environment and managing its working capital.

The high tariffs and taxes and high interest rates that are now part of the external regulatory regime makes maintaining market shares and selling our products a considerable challenge.

Managing our working capital in the midst of a volatile interest regime is another challenge. For some years now this subject has received our close attention and has become a key component of the Dimo culture. In the past year, the increase in working capital has been 11%. The increase in revenue has been 24%. We are confident that we can rise to the occasion and manage our working capital in an effective way.

CHAIRMAN & CEO'S REVIEW

In the longer term, there are several challenges that we have to surmount and these remain important areas of focus receiving considerable management time and effort.

Remaining the No. 1 Choice

One of the challenges we will face over the next few years will be to sustain the growth in market share for our world-class brands.

While seeking to expand our market shares in the next few years, we will continue to invest in the requisite training and technology to ensure that the care we provide after sales is on par with the world's best. Our objective is to make Dimo invaluable to our principals and to create win-win solutions for us both.

In this respect we will continue to invest in state-of-the-art technology and in state-of-the-art training for our human resource team to power this technology. The highly sophisticated products that our principals now manufacture require the same level of sophistication in after-sales service. We are striving to ensure the same degree of sophistication in our 'after-care'.

With the increase in business activities, a separate logistics centre has been conceived. The infrastructure for the logistics centre will be considered in the forthcoming year.

The Dimo Ethic of Responsibility

We are proud that our growth has been built on a foundation of unyielding ethics and strong company values. Integrity, transparency, legality and strong governance have been core Dimo values which have driven the Company and will continue to drive the Company in the years ahead.

While we continue to focus on profitability, we know that this can only be achieved in the context of a society that is also being constantly enriched by our corporate activities. Our ISO certified Environmental

Management System provides a rigorous framework for managing the environmental impact of the Company's activities. In all our activities we make every attempt to reduce, reuse and recycle and endeavour to nourish the environment rather than deplete it.

Our CSR activities continue to empower communities and seek to provide new and sustainable opportunities for these groups. One of our key responsibilities is our employees and their families. We firmly believe that Dimo's responsibility as a corporate citizen should 'start at home' and with its own family. In this respect, I am proud to note the comprehensive medical cover we provide to all our employees, without discrimination, in every business unit. Often we have gone beyond this medical cover and provided support where employees and their families have had to undergo critical surgery or treatment for life threatening illnesses.

While we continue to empower communities outside Dimo, we will simultaneously empower our employees and their families as part of our obligations as a responsible corporate citizen.

How Dimo empowers communities and supports the environment is covered more comprehensively in the Company's Sustainability Report on pages 40 to 57.

Recently, as part of our corporate social responsibility, we organised a technology symposium on 'vehicles with hydrogen and fuel cell technology'. The symposium provided a unique opportunity for professionals from outside the Dimo team to get acquainted with the latest developments. This technology will enable a 'zero emissions future' making it environmentally friendly. We are looking at integrating other products into the Dimo portfolio that will provide the requisite level of luxury while being environmentally friendly and doubly safe.

CHAIRMAN & CEO'S REVIEW

Building the Dimo Team

Part of our growth strategy is to invest in developing the skills, capabilities and dynamism of the Dimo team. If we are to stay competitive and make the quantum leap, then we need a team that can take the Company to new heights.

One aspect of our human resource strategy is to build team spirit and camaraderie. Beyond that we attempt to provide opportunities for every team member to develop their skills and capacities in line with their own career plan. Last year we invested over Rs. 20 mn in training programmes for our staff and will make a similar or even greater investment this year too.

Our training school has provided new opportunities to people outside the Dimo team and to our customers. Young Sri Lankans have been exposed to state-of-the-art engineering practices with some of them even having the opportunity to 'learn the trade' at our principals' workshops in Germany, India and Singapore.

Our training school has now received global recognition and the 'Dimo Certificate' is a much sought after qualification. We are proud of the contribution made by us in this respect not just to the Dimo team but to the youth of Sri Lanka in general.

I must acknowledge here the efforts of the vibrant Employee Council at Dimo. The Employee Council was set up to respond to staff grievances and to harness new ideas among the workforce. The Council has worked astonishingly well for over seven years and has had a significant impact on the growth of the Company. Together we have been able to take collective responsibility for the well-being of the Company and have 'problem-solved' and strategised jointly for the future security of the Company, its employees and society in general.

Responding to Flooding

I must take this opportunity to apprise you of a concern that has troubled us greatly for some years now. This has to do with the flooding of Colombo city and particularly the properties on which many of your Company's operations are located.

We are now exploring a variety of options, to see how your Company can minimise the losses caused, not through the inefficiencies of the Company, but through the ineffectiveness of local and other authorities.

The New Legal Regime

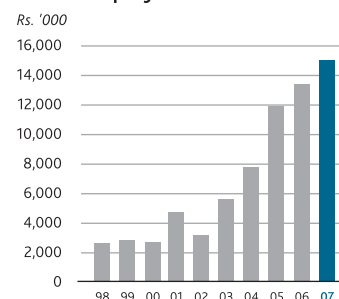
We welcome the new Companies Act No. 7 of 2007, which came into effect on the 3rd of May 2007. The Company is taking steps to respond to the new requirements of the Act and will soon apply to the Registrar of Companies to be formally registered as Diesel & Motor Engineering PLC.

Accolades

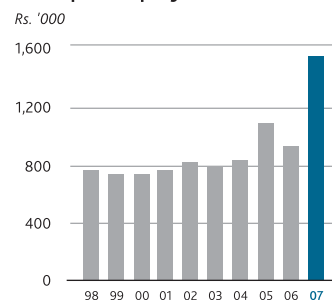
Last year our Annual Report won a number of awards at some of the major competitions. At the Institute of Chartered Accountants Awards we were placed first in the category of companies with up to five subsidiaries. At the ACCA Sustainability Reporting Awards we were the winner in the medium scale category. At the Business Excellence Awards organised by the National Chamber of Commerce, we were the winner in the trading category and first runner-up in the large category.

Recognition was also received from some of our business partners. The Company was placed third in the platinum category for the Bosch Automotive after-markets competition organised by Bosch Southeast Asia for the Asian region. We also received the 'Challenger Award' we received from Komatsu Fork Lift Asia Pte for being one of the leading distributors in the region.

Group Turnover per Employee



Property, Plant & Equipment per Employee



CHAIRMAN & CEO'S REVIEW

A New Trajectory of Growth

I am upbeat about the prospects of the Company in the short to medium term. Dimo has grown remarkably in the recent past and we are well placed to enhance this growth rate over the next few years. Your Board has taken three strategic decisions that we are convinced will power Dimo over the next few years:

- To add more world-class brands to our blue-chip product portfolio. These world-class brands come from a variety of sectors and industries and will give security to our product base by not making our brand dependent on any single sector.
- To invest substantially in human resource development and state-of-the-art technology. These investments will strengthen our after-care capacities and ensure that the standard of Dimo Care continues to rise.
- To invest in infrastructure expansion and the development of logistics facilities. While ensuring that our existing principals remain with us, these investments will enable us to attract new products to our portfolio and will ensure that the Dimo product quality and after-care service do not drop.

We think this strategy will provide more strength and security to the Dimo brand and help us deliver progressively increasing value to all our stakeholders over the next few years. Our business strategy is covered in more detail in the 'strategy & vision' overview on page 13.

A Warm Welcome and Thank You

I warmly welcome Dr. Harsha Cabraal, Dr. Uditha Liyanage and Mr. Ranjan Seevaratnam who joined the Board during the year as independent Non-Executive Directors. All three of them bring with them vast experience and expertise to the Board. I am confident that all shareholders will join me in wishing them well in their new appointments.

In accordance with the Company Articles, they will retire from the Board and shareholders will be requested to re-elect them at the Annual General Meeting.

I also take this opportunity to convey my heartfelt thanks to Mr. H.M.A. Jayasinghe who retired from the Board during the year. He will continue to act as an advisor to the Audit Committee. He contributed immensely to the growth of the Company.

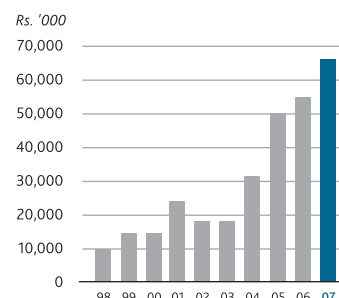
We could not have achieved this performance if not for the Dimo team. I would like to take this opportunity to thank everyone in the Dimo family for the dynamism and commitment they have shown over the past year. It is their flair and hard work that has made the Company what it is. My thanks also go out to our Management Team that has provided inspiration and direction to the Company. My thanks also go out to our principals, who have retained their faith in us as the Number 1 choice. We are proud to look after their interests in Sri Lanka.

Finally, to my colleagues on the Board, I would like to offer a warm word of appreciation. I have valued your counsel and advice at all times. I look forward to another rewarding and productive year at Dimo.



A.R. Pandithage
*Chairman, Managing Director/
 Chief Executive Officer*
 21st May 2007

Dividend Paid



BOARD OF DIRECTORS

**A.R. Pandithage****Chairman, Managing Director/Chief Executive Officer**

Joined the Company in June 1973. Appointed to the Board in June 1977. Appointed as Joint Managing Director in November 1984 and Managing Director in 1986. Appointed as the Chief Executive Officer in April 1994. Appointed as the Chairman, Managing Director & CEO in July 2004. Holder of Dipl. Ing. from Germany. Member of the Institute of Engineers, Germany (VDI). Deputy Chairman, Browns Dima Industrial Products (Pvt) Ltd. Director, Dial Textiles Ltd. Chairman, Audit Committee of Dial Textile Ltd.

A.G. Pandithage**Deputy Chief Executive Officer**

Joined the Company in September 1986. Appointed to the Board in December 1995. Fellow of the Chartered Institute of Management Accountants, UK. Member of IT Strategy Team Asia of Daimler Chrysler AG. Appointed as the Deputy Chief Executive Officer with effect from April 2006.

**A.N. Algama**

Joined the Company in June 1973. Appointed to the Board in November 1984. Past Chairman of The Ceylon Motor Traders' Association and Sri Lanka Tyre Importers' Association. Executive Committee Member of the Ceylon Chamber of Commerce - Imports Section.

**Dr. H. Cabral****

Appointed to the Board in October 2006. President's Counsel, PhD. in Corporate Law (University of Canberra), Commissioner - Law Commission of Sri Lanka, Member - Advisory Commission on Company Law, Member NCED (Legal Cluster), National Council for Economic Development.

**S.C. Algama**

Appointed to the Board in November 1984. Appointed as an Executive Director in 1994. Fellow of the Institute of Incorporated Engineers (SL). Council Member of the National Chamber of Commerce, Sri Lanka.

**R.A. Ebell***

Appointed to the Board in October 1986. Executive Director of Hayleys Ltd. Fellow of the Institute of Chartered Accountants, Sri Lanka. Fellow of the Chartered Institute of Management Accountants, UK. Diploma Holder and Member of the Chartered Institute of Marketing, UK. Past President of the Chartered Institute of Management Accountants - Sri Lanka Division.

B.C.S.A.P. Gooneratne

Joined the Company in January 2001. Appointed to the Board in April 2006. Fellow Member of the Institute of Chartered Accountants of Sri Lanka and holder of Master of Business Administration Degree from University of Sri Jaywardenepura.



H. M. A. Jayasinghe**

Appointed to the Board in July 1999. Served as Director of the Company till 31st December 2006. Fellow Member of the Institute of Chartered Accountants of Sri Lanka and a Fellow of the Chartered Institute of Management Accountants, UK. Partner of Ernst & Young and a Partner/Director of all its subsidiaries and associate companies. Alternative Chairman of Urgent Issues Task Force of Institute Of Chartered Accountants of Sri Lanka.



Dr. U. Liyanage**

Appointed to the Board in October 2006. Fellow Member of the Chartered Institute of Marketers of UK and holder of Master of Business Administration Degree from University of Sri Jayewardenepura. Ph.D. - University of Sri Jayewardenepura. Head, Academic Affairs and Senior Faculty, Marketing at the Postgraduate Institute of Management (PIM), Director of Ceylon Cold Stores Ltd., Chemanex Ltd., Ceylon Leather Products Ltd. and Q&E Advertising Ltd.



T.G.H. Peries

Joined the Company in January 1962 and appointed to the Board in August 1977.

A.M. Pandithage*

Appointed to the Board in September 1982. Deputy Chairman of Hayleys Ltd. Chief Executive Officer of the Hayleys Advantis Group. Former Director of the Sri Lanka Ports Authority and Jeya Container Terminal. Former Chairman of the Ceylon Association of Ships' Agents. Director of Sri Lanka Port Management & Consultancy Services Ltd.



R. Seevaratnam**

Appointed to the Board in January 2007. Fellow Member of the Institute of Chartered Accountants of Sri Lanka and England & Wales and holder of General Science Degree from University of London. Former senior partner of KPMG Ford, Rhodes, Thornton & Co. Director, Hatton National Bank Ltd., Haycarb Ltd., Dipped Products Ltd., Acme Printing & Packaging Ltd., Tokyo Cement Ltd., Tea Smallholder Factories Ltd.



R.C. Weerawardane

Joined the Company in February 1990. Appointed to the Board in June 2002. Certificate holder of the Chartered Institute of Marketing, UK.

* Non-Executive Directors ** Independent Non-Executive Directors

Group Management Committee A.R. Pandithage - Chairman, A.G. Pandithage - Deputy CEO, S.C. Algama - Executive Director, D.S. Amarasuriya - General Manager (Passenger Vehicle Service), M.V. Bandara - General Manager (Sales and Service - Commercial Vehicles), A.C.G. Dias - General Manager (Tyres), B.C.S.A.P. Gooneratne - Executive Director, E.D.C. Kodituwakku - General Manager (Finance & Controlling), A. Mapalagama - General Manager (Auto Components, Power Tools and Outdoor Equipment), R.C. Weerawardane - Executive Director **Audit Committee** R. Seevaratnam (Chairman w.e.f. 1st January 07), H. M. A. Jayasinghe (Resigned w.e.f. 1st January 07), Dr. H. Cabral, R.A. Ebell, Dr. U.P. Liyanage, A.M. Pandithage **Remuneration Committee** Dr. U.P. Liyanage (Chairman w.e.f. 1st January 07), H. M. A. Jayasinghe (Resigned w.e.f. 1st January 07), Dr. H. Cabral, R.A. Ebell, A.M. Pandithage, R. Seevaratnam **Nomination Committee** Dr. H. Cabral (Chairman w.e.f. 1st January 07), H. M. A. Jayasinghe (Resigned w.e.f. 1st January 07), Dr. U. Liyanage, R.A. Ebell, A.M. Pandithage, R. Seevaratnam

GROUP MANAGEMENT

COMMITTEE



01



02

01 A.R. Pandithage - *Chairman*

02 A.G. Pandithage - *Deputy Chief Executive Officer*



03



04

03 S.C. Algama - *Executive Director*

04 D.S. Amarasuriya - *General Manager - Passenger Vehicle Service*



05



06

05 M.V. Bandara - *General Manager - Sales & Service Commercial Vehicle*

06 A.C.G. Dias - *General Manager - Tyres*



07



08

07 B.C.S.A.P. Gooneratne - *Executive Director*

08 E.D.C. Kodituwakku - *General Manager - Finance & Controlling*



09



10

09 A. Mapalagama - *General Manager - Auto Components, Power Tools & Outdoor Equipment*

10 R.C. Weerawardane - *Executive Director*

STRATEGY & VISION

Driven by Vision

The Group's Corporate Strategy is directed towards achieving the Vision. The Vision of the Company appears on the inner front cover. The foundation for achieving the Corporate Vision is provided by the Intellectual Capital of the Company. It is also the catalyst that transforms the Group's resources into tangible results. The Corporate strategy, therefore, revolves around enhancing the quality, efficiency, effectiveness and sustainability of the elements of Intellectual Capital.

The model appearing on this page is an illustration of the Corporate Strategy process of the Group.

Intellectual Capital

In order to keep the intellectual capital at its best, the Company has a wide range of strategies & plans covering each vital element, viz. Customers, Principals, People, Technology and Processes.

Customer related strategies revolve around gaining, caring, managing and retaining customers and revenue growth. In promoting 'best in class' brands in Group's custody, every effort is made to enrich the technology through the 'Dimo Care'. From a customer point of view, the products and solutions delivered is a joint offering from a world-class Principal and Dimo, with its world-class care. Human Resources strategy covering recruitment, development and retention is geared to create people with a 'Vision driven Passion'. Investing in people and upgrading their skills to take care of the cutting edge technology holds the key in gaining a competitive advantage. Carefully thought strategies in marketing, finance,

information systems and supply chain management seek competitive advantage and growth through the entire range of processes in place.

Business Composition

The base for growth is presently provided by the auto sector. In the recent past, efforts have been underway to expand and grow the non-auto sector. The long-term strategy is to grow the non-auto sector to contribute a formidable portion of the Group's business, having the capacity to independently grow and contribute to the profitability in equal measure.

The Foundation and the Pillars

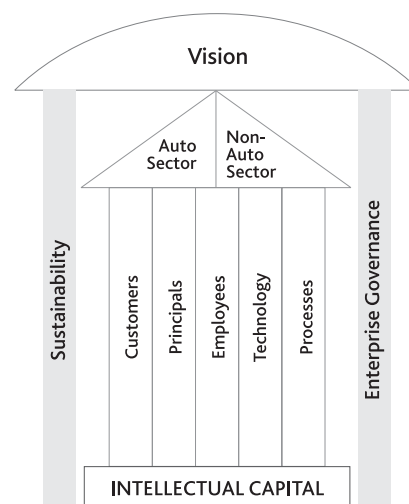
Whilst the intellectual capital provides the base for growth, enterprise governance and sustainability provide the structure and strength in the march towards reaching the vision. In other words they provide the pillars on which the future of the Company is built.

Therefore, the strategy in essence encompasses developing the intellectual capital on the pillars of enterprise governance and sustainability.

Formulation & Review Process

Review and modification of existing strategies and formulation of new strategies take place during the Annual Strategy Sessions. The Forum for these sessions includes the Chairman & Executive Directors, Members of the Group Management Committee and Heads of Business Units. The information required for these sessions are obtained at all levels across the organisation. Implementation of strategies is reviewed on a quarterly basis by the same forum.

Strategy Model





VEHICLES



BUSINESS PERFORMANCE

(VEHICLES)

Sale of Brand New Passenger Vehicles, 4WD Vehicles,
Commercial Vehicles, Special Purpose Vehicles & Pre-owned
Passenger Vehicles

Key Figures

| | 2006/07 | 2005/06 | Change % |
|---------------------------------------|---------|---------|----------|
| Segment Turnover (Rs. mn) | 8,827 | 7,277 | 21 |
| Segment Result (Rs. mn) | 594 | 330 | 80 |
| % Contribution to the Group Turnover | 68 | 69 | (1) |
| Segment Result/Segment Net Assets (%) | 25 | 17 | (8) |

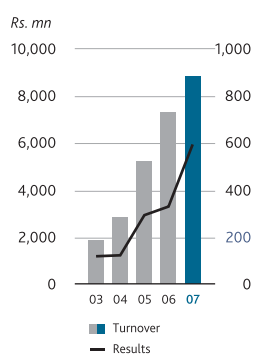
Key Principals

- Daimler AG
- Tata Motors Ltd.
- Chrysler International Corporation

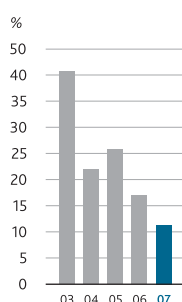
Customer Profile

| | B2C | B2B | B2G | Total |
|--|-------|-------|-----|--------|
| No. of Customers (accumulated) | 6,725 | 9,779 | 307 | 16,811 |
| Customer Satisfaction Index (weighted average %) | | | | 90.04 |

Business Segment
Turnover vs. Results



Return on
Total Assets



BUSINESS PERFORMANCE

(VEHICLES)

Passenger Cars - Mercedes-Benz

The price of luxury vehicles have increased by over 100% since 2004. Prices have been driven up mainly by tariff, which have increased substantially, and the depreciation of the Rupee against the Euro.

Mercedes-Benz continues to dominate the high end luxury car market. The turnover for the year was 98% of the budget. The 'S' class made a substantial contribution to overall figures. During the year, we introduced several new products which included the new generation of 'E' class cars; the 'R' class grand sports tourer; and 'B' class sports tourer.

Active promotions were carried out in the outstation areas, in order to introduce the Mercedes-Benz range of products including pre-owned to a broader market segment.

The high tariff regime remains a challenge for growth of this business. However, the launch of the new 'C' class sedan, with its new breathtaking design and the 'GL' class, is expected to boost sales this year.

The Mercedes-Benz Club of Sri Lanka which was promoted and supported by the Company, continued to engage in activities promoting a 'passion' for the brand.

Pre-Owned Vehicles

The availability of duty free permits had an impact on sales and the number of units sold decreased by 21% for the year under review. Prior to the sale of a pre-owned vehicle, the Company carries out a comprehensive refurbishment of the vehicle to ensure that they are in peak condition.

Tata Commercial Vehicles

This sector is dominated by Indian and reconditioned Japanese vehicles. The Government's Ten Year Development Framework for the transportation sector envisages the development of an efficient and safe transport system responsive to socio-economic development needs. Further, the transportation sector is to be developed by adding new buses to the State bus service.

Sales of heavy commercial trucks grew by 223% and medium commercial vehicles by 198%. We increased our market share in the trucks segment by 7 percentage points and in the buses segment by 8 percentage points. Since 2001 our market share of Tata Commercial Vehicles has grown fourfold.

The commercial vehicles business achieved its budgeted turnover for the year. The performance of the commercial vehicle business is significantly influenced by interest rates, as most of the transactions are financed by commercial borrowings. Inaccessibility to the markets in the North and East curtailed sales of commercial vehicles in those areas.

Intensive efforts are underway to consolidate our No. 1 position in the commercial vehicle sector.

During the year, we intensified our sales focus through our branches in Kurunegala, Matara and Anuradhapura and strengthened the distribution network for spares. Future plans include improving the infrastructure to support sales and after sales in Anuradhapura.



BUSINESS PERFORMANCE

(VEHICLES)

Light Commercial Vehicles

The Tata Ace mini truck continues to dominate the mini truck market and the 207 Cab is the leader in its category. Turnover of light commercial vehicles grew by over 100%.

The Tata Ace mini truck, commonly known as the 'Dimo Batta', which was launched in 2006, has contributed significantly to growth in sales. Last year, we invested Rs. 4 mn to upgrade the light commercial vehicle workshop facility and plans are underway to launching several new models in the ensuing year.

The 'Dimo Batta' has dramatically changed the landscape of the transport sector, opening new avenues for the cost conscious customer. However, the recent upward revision of tariff applicable to this category of vehicles is expected to have a negative impact for the growth in sales.

Tata Passenger Vehicles

Traditionally, this segment of the market has been dominated by reconditioned Japanese vehicles and there is intense competition from similar vehicles imported from India, China and Korea.

The Tata passenger vehicles cater to the market which is above 1000 cc and below 1500 cc. This business failed to achieve its budgeted turnover. Special efforts are underway to increase the market share and make major improvements to the profitability of this business.

The fuel efficient 'Xeta' was launched during the year. Several new products are planned to be launched this year. During the year Rs. 6.0 mn was invested in a new state-of-the-art showroom. Tata passenger vehicle customers enjoy an islandwide spare parts distribution network and a 24 hour road side assistance facility.

Chrysler and Jeep

Both Chrysler and Jeep target the luxury automobile segment. The Chrysler 300 and the Grand Cherokee were the foremost selling products that sold the best. Increased tariff and high interest rates had a significant impact on Chrysler and Jeep vehicle sales.

The Chrysler-Jeep will continue to receive the Dimo Care in Sri Lanka and the recently announced change in ownership of the brands would not have any impact on current operational activities.





VEHICLE PARTS AND SERVICES



BUSINESS PERFORMANCE

(VEHICLE PARTS AND SERVICES)

Repair of Passenger and Commercial Vehicles, Sale of Vehicle Spare Parts, Accessories, Components & Tyres

Key Figures

| | 2006/07 | 2005/06 | Change % |
|---------------------------------------|---------|---------|----------|
| Segment Turnover (Rs. mn) | 2,071 | 1,744 | 19 |
| Segment Result (Rs. mn) | 374 | 279 | 34 |
| % Contribution to the Group Turnover | 15 | 17 | (2) |
| Segment Result/Segment Net Assets (%) | 38 | 43 | (5) |

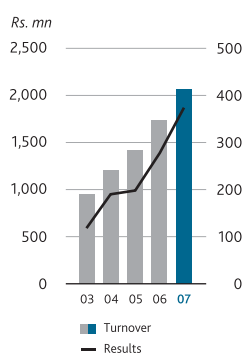
Customer Profile

| | B2C | B2B | B2G | Total |
|--|-------|-------|-----|-------|
| No. of Customers (accumulated) | 1,181 | 7,364 | 462 | 9,007 |
| Customer Satisfaction Index (weighted average %) | | | | 91.65 |

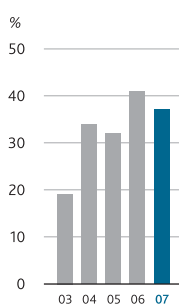
Key Principals

- Daimler AG
- Tata Motors Ltd.
- Robert Bosch GmbH
- Michelin
- Motor Industries Co. Ltd.
- MRF Ltd.
- BF Goodrich
- Bosch Automotive Systems Corporation
- Komatsu Forklift Asia (Pte) Ltd.
- Mahindra & Mahindra Ltd.
- Rane Brake Linings Ltd.
- Luk India (Pvt) Ltd.
- Blaupunkt Werke GmbH
- India Pistons Ltd.
- Shardlow India Ltd.
- Fenner (India) Ltd.

Business Segment
Turnover vs. Results



Return on
Total Assets



India Pistons Ltd.



BUSINESS PERFORMANCE

(VEHICLE PARTS AND SERVICES)

Franchise Parts

The Company markets a range of auto spare parts and accessories. These include Mercedes-Benz, Tata, Chrysler, Jeep, Komatsu, Mahindra & Mahindra, Bomag and Class.

This sector showed a 30% growth in turnover during the year. Several new products of vehicles have fuelled growth in this sector. The growth in construction and agricultural sectors is expected to bring in similar results this year with spare parts sales of Komatsu and Bomag likely to increase. A strong demand for Mahindra & Mahindra and Claas parts in the agriculture sector is forecasted. We plan to appoint several authorised agents in key locations with a view to penetrating markets out of Colombo.

We anticipate a growth in Tata spares this year. The Company plans to invest in a new storage facility for Tata spare parts to support this growth.

Non-Franchise Parts

Our main market is the passenger and commercial vehicular segments. Our non-franchise products are marketed either under the Dimo brand or as a co-branded product with the original equipment manufacturer (OEM). The focus this year will be to increase our market share in the passenger car, light commercial vehicles and farm tractor spare parts markets.

Turnover of non-franchise products increased by a satisfactory 53% (25% in 2005/06) over the previous year. We are optimistic about prospects in this sector. There is a strong demand for spare parts of Indian passenger cars and light commercial vehicles of Indian origin and this is expected to stimulate growth in this sector. There is also a strong demand for spares in the four wheel and two wheel tractor sector.

A number of promotional activities were conducted over the past years to improve awareness of spare parts marketed.

The escalation of the conflict in the North and East has unfortunately had an impact on our sales to those regions.

Tyres

We target the passenger, commercial, construction and agricultural sectors and market world renowned brands of tyres such as Michelin, BF Goodrich and MRF.

The turnover was 15% above the previous year, though we fell marginally short of the budgeted figure.

With the increase in the volume of cars and light commercial vehicles, we expect significant growth in volumes.

Therefore, the Company has an opportunity to venture into a new market segment.

Our tyre retreading plant commenced commercial operations in September 2006 and plans have been made to expand this operation into other areas by the end of the ensuing financial year.



BUSINESS PERFORMANCE

(VEHICLE PARTS AND SERVICES)

Vehicle Services

We provide state-of-the-art repair and service facilities for passenger and commercial vehicles. The turnover from vehicle repair services increased by 34% (36% in 2005/06) during the year under review.

The commercial vehicle workshop performed well increasing its turnover by 51% (81% in 2005/06) supported by the increase in commercial vehicles sales. One of the biggest challenges we face is to train and retain skilled human resources to provide the state-of-the-art services which we are well known for.

The Company is in the process of designing new products that will provide added value to our customers. This includes 'full maintenance' contracts for fleet owners; a Fleet Owner's Club; Insurance Repair Promotional Scheme; and an Express Service for passenger cars.

The total investments in upgrading workshops facilities and the acquisition of courtesy cars amounted to Rs. 45.5 mn.

We are also likely to see a more stringent enforcement of environmental and pollution control standards and are taking steps to ensure that our operations comply with legal requirements and beyond.

During the past year, we had eight service campaigns including two at our commercial vehicles workshop at Siyambalape.





LIGHTING & POWER TOOLS



BUSINESS PERFORMANCE

(LIGHTING & POWER TOOLS)

Sale of Power Tools & Accessories, Lamps, Lighting Fittings & Accessories

Key Figures

| | 2006/07 | 2005/06 | Change % |
|---------------------------------------|---------|---------|----------|
| Segment Turnover (Rs. mn) | 354 | 272 | 30 |
| Segment Result (Rs. mn) | 50 | 45 | 11 |
| % Contribution to the Group Turnover | 3 | 3 | – |
| Segment Result/Segment Net Assets (%) | 38 | 37 | 1 |

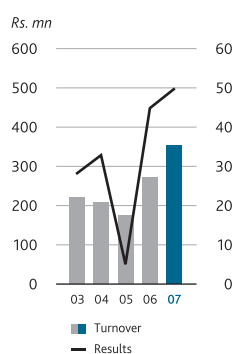
Key Principals

- Osram GmbH
- Vossloh-Schwabe GmbH
- SiTeco Lighting (M) Sdn.Bhd.
- Robert Bosch Ew.
- Shindaiwa Corporation
- Snapon Tools
- Komatsu Zenoah

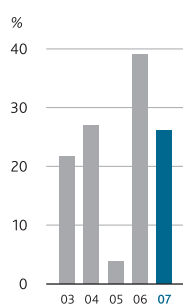
Customer Profile

| | B2C | B2B | B2G | Total |
|--|-----|------|-----|-------|
| No. of Customers (accumulated) | 59 | 1536 | 190 | 1,785 |
| Customer Satisfaction Index (weighted average %) | | | | 89.03 |

Business Segment
Turnover vs. Results



Return on
Total Assets


BOSCH
**ZENOAH
KOMATSU**
OSRAM
SIEMENS
siteco
**Everything you Need
SKIL**
Snap-on
VS Optoelectronic
A New Lighting Experience

BUSINESS PERFORMANCE

(LIGHTING & POWER TOOLS)

Lighting

According to the Central Bank Annual Report, the total electricity consumption increased by 8% in 2006. Electricity consumption in the industrial sector grew by 6% while in the domestic and general purposes sectors consumption decreased because of an increase in the tariff rates.

Dimo provides lighting solutions which include lighting designs, and markets a range of lamps, lighting fittings and lighting solutions from well-known brands such as Osram, Siemens, Siteco, Davis and Vossloh- Schwabe. These products are targeted at both domestic and industrial users.

Turnover grew by 40% (73% in 2005/06) during the year. The distribution network was reorganised to make our products more easily accessible. The rising cost of energy and the growth of activity in the construction sector (which grew by 8% in 2006), should help to maintain the growth momentum this year too.

Energy saving lamp import saw a significant increase during the year. A corresponding decline in the standard GLS lamps is also noted. This could be mainly attributed to the increasing cost of energy and the high awareness of the need for energy saving among consumers.

A number of new products were introduced last year. This included a new range of Osram CFLs and Siemens Low Voltage Switch Gear.

There is a growing demand for sophisticated decorative lighting solutions especially in the domestic and commercial sector with value added solutions. Both these trends are likely to drive the demand for effective, energy efficient and state-of the-art lighting solutions.

Efficient use of energy is considered to be a key theme in the National Energy Policy for Sri Lanka, singling positive signs for energy efficient lighting.



BUSINESS PERFORMANCE

(LIGHTING & POWER TOOLS)

Power Tools

The Company markets a range of products under this category including professional power tools, accessories, and outdoor power equipment. During the year under review, the portfolio of products was enhanced with the introduction of garage diagnostic equipment and hand tools from 'Snap-On'. The growth in turnover was 18% (35% in 2005/06) over the previous year.

There was a strong demand for 'Zenoah' outdoor products, 'Snap-On' tools and equipment and the 'Skill' range of power tools.

The Government's focus on improving vocational training facilities have stimulated a demand for tools and related equipment. Competing with 'unbranded' low-priced tools and equipment from China remains a major challenge.

Activity in the construction sector and the planned infrastructure projects, including road projects, are likely to generate a demand for power tools. The planned mechanisation of the plantations will create an additional demand as will the influx of foreign assistance into the Vocational Training system.





CONSTRUCTION & MATERIAL HANDLING MACHINERY



BUSINESS PERFORMANCE

(CONSTRUCTION & MATERIAL HANDLING MACHINERY)

Sale & Service of Earth Moving Machinery, Road Construction Machinery, Forklifts, Racking Systems, Tractors, Pumps, Dock Levellers, Car Parking Systems and Harvestors

Key Figures

| | 2006/07 | 2005/06 | Change % |
|---------------------------------------|---------|---------|----------|
| Segment Turnover (Rs. mn) | 1,202 | 802 | 50 |
| Segment Result (Rs. mn) | 125 | 125 | – |
| % Contribution to the Group Turnover | 9 | 8 | 1 |
| Segment Result/Segment Net Assets (%) | 21 | 42 | (21) |

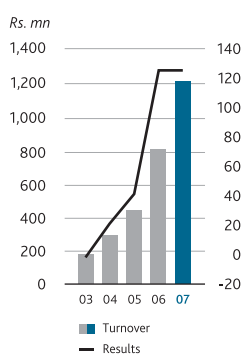
Customer Profile

| | B2C | B2B | B2G | Total |
|--|-----|-------|-----|-------|
| No. of Customers (accumulated) | 91 | 2,739 | 230 | 3,060 |
| Customer Satisfaction Index (weighted average %) | | | | 91.02 |

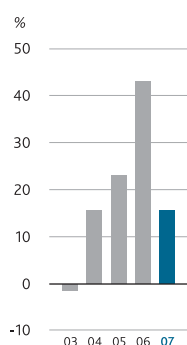
Key Principals

- Komatsu Forklift Asia (Pvt) Ltd.
- Bomag GmbH
- KSB AG
- Mahindra & Mahindra
- SSI Schaefer Systems International (Pte) Ltd.
- Claas India Ltd.
- Komatsu Used Equipment Corp.
- Everdigm
- Schwing Steiter

Business Segment
Turnover vs. Results



Return on
Total Assets



KOMATSU



Mahindra

CLAAS

BOMAG

KSB

SSI SCHAEFER
SOLUTIONS THAT FIT

mhe

DEMAG

EVERDIGM



SCHWING

BUSINESS PERFORMANCE

(CONSTRUCTION & MATERIAL HANDLING MACHINERY)

Construction Machinery

The construction sector grew by 8% in 2006. A number of road development projects, power projects and other infrastructure projects are presently underway. The construction of housing and condominium projects also expanded significantly, benefiting from the growing housing finance market and government intervention.

The Company markets a range of heavy machinery for the construction industry from principals world renown such as Komatsu, Bomag, Everdigm and Schwing Stetter.

Operations in this sector revived considerably last year. Despite set backs suffered due to high interest rates, the turnover achieved was 96% over the budget.

Among the new products introduced last year was the concrete batching plant from Schwing Stetter.

The construction of new roads, the modernisation of existing ones, anticipated coal power projects, reforestation projects and expansions to the port and airport are likely to generate a demand for heavy machinery. Also in the pipeline are projects to develop and rehabilitate irrigation systems. Public-private partnerships to develop the country's infrastructure will also create new opportunities in the near future.

Storage and Material Handling

We market a range of leading brands of storage and material handling products. Turnover grew by 18% (40% in 2005/06). Komatsu fork-lifts and Schaefer Racking systems generated a heavy demand.

We designed and installed one of the largest storage systems in the garments industry which included a locally designed and fabricated conveyor system. One of the major projects handled during the year was to supply and install a storage system for Sri Lanka Telecom.

The 'Gondola' building maintenance system from Mhe-Demag was introduced into the Sri Lankan market during the year. Automated car parking systems were also introduced into the product portfolio.

We anticipate a growth in the market for forklifts. The construction of a number of warehouses and logistics centres will also drive the demand for racking and storage systems.

Agri-Machinery

Dimo markets tractors, agricultural implements, harvesters and agricultural machinery from Mahindra & Mahindra and Claas harvesters. During the year Mahindra & Mahindra products increased their market share by 11 percentage points during the year.



BUSINESS PERFORMANCE

(CONSTRUCTION & MATERIAL HANDLING MACHINERY)

The number of tractor units sold grew by 55% and harvester units by 71% in the year under review. An aggressive islandwide sales campaign to improve the visibility of the Mahindra & Mahindra product range was carried out, well supported by our Principal. Our efforts to strengthen the distribution network will continue. The number of dealers for tractors, agricultural implements and agricultural machinery is to be increased from 20 to 50 during the coming year. Plans are underway to add more products to the range of tractors and harvesters.

The re-organisation of this business will have an important impact on its future growth.

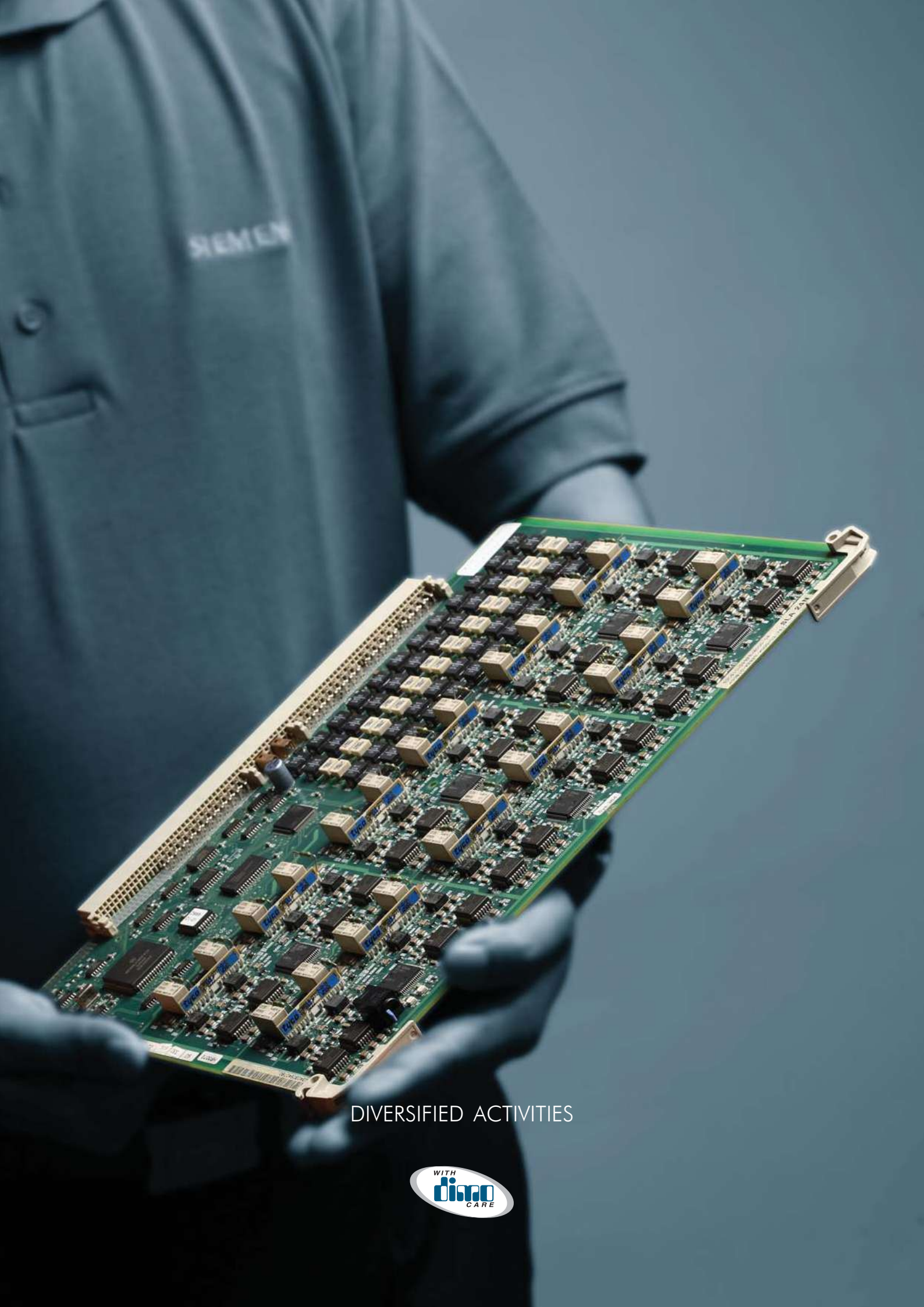
Fluid Management Systems

Dimo supplies the water and the sewerage sector with products from the world's leading manufacturer KSB. Turnover grew by 100% in the year under review as a direct result of the heightened activity in the construction sector especially in the large scale housing and condominium projects.

New environmental regulations have also seen an increase in the number of waste water plants. Projects relating to water supply and sanitation are potential areas of growth.

The market is likely to grow with the development of the rural water supply schemes and other infrastructure projects funded by donor agencies.





DIVERSIFIED ACTIVITIES



BUSINESS PERFORMANCE

(DIVERSIFIED ACTIVITIES)

Telecommunication Solutions, UPS Equipment, Medical Engineering Solutions, Diesel Engines for Marine Propulsion & Rail Traction, Power Engineering and Building Technologies

Key Figures

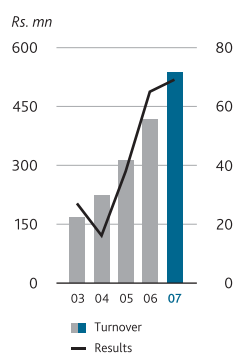
| | 2006/07 | 2005/06 | Change % |
|--------------------------------------|---------|---------|----------|
| Segment Turnover (Rs. mn) | 536 | 416 | 29 |
| Segment Result (Rs. mn) | 69 | 65 | 6 |
| % Contribution to the Group Turnover | 5 | 4 | 1 |
| Segment Result/Segment Assets (%) | 19 | 26 | (7) |

| | B2C | B2B | B2G | Total |
|--|-----|-------|-----|-------|
| No. of Customers (accumulated) | 91 | 1,601 | 154 | 1,810 |
| Customer Satisfaction Index (weighted average %) | | | | 92.95 |

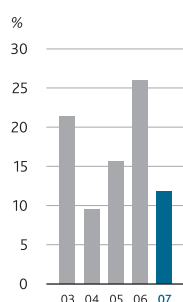
Key Principals

- Siemens AG
- Tognam
- Zeiss AG
- KHD Humboldt Wedag AG
- Dräger Medical
- Mtu Friedrichshafer GmbH
- York International
- Interpower - International (Pvt) Ltd.
- Power Source - International (Pvt) Ltd.
- Humphrey System
- Detroit Diesel Corporation
- Wortsila India Ltd.
- VM Motori SPA
- John Deere

Business Segment
Turnover vs. Results



Return on
Total Assets



JOHN DEERE

BUSINESS PERFORMANCE

(DIVERSIFIED ACTIVITIES)

Dimo is also engaged in the marketing of a range of engineering solutions that include telecommunication engineering, off road transportation systems, industrial refrigeration, power engineering and medical engineering.

Telecommunication Solutions

The rapid growth of the telecommunications sector continued in 2006. The subscriber network grew by 59%, benefiting from the introduction of advanced technology and the rapid expansion of networks.

The product portfolio of this business segment includes Enterprise Communication Networks Solutions, Uninterrupted Power Supply Systems (UPS) and telephone instruments. This business unit is a key supplier of telephone instruments to the fixed line telecom service providers in the country.

Despite a rapid increase in the installed base of enterprise networks, this business has not yet reached a level to make a significant contribution to the profitability of the Group. This remains a matter of concern. Special efforts are underway to overcome this situation.

Off-Road Transportation Systems

This business unit markets marine and rail engines and represents leading brands such as MTU and John Deere. Thirty-two locomotives of the Sri Lanka Railway and several marine craft of the Sri Lankan Navy is powered by the prestigious MTU engines.

The divestiture by Daimler Chrysler AG of its majority holding in MTU will have no material impact on the performance of this business.

The Company looks forward to a mutually beneficial and fruitful relationship with the brand MTU under the new owners.

This business unit lived up to expectations and is on track to achieving the results budgeted for in the ensuing year.

Industrial Refrigeration

The Company markets products from the reputed brand 'York'. We provide refrigeration solutions for production processes and storage facilities. The key market segments served are the food processing industry and the block and flake ice industry.

Industrial refrigeration solutions under the DIMO brand is part of the expansion activities planned for in the ensuing year.

Power Engineering

We are likely to witness an increase in demand for solutions and products under this business segment because of an increase in power requirements for the country.

The power engineering business serves two key sectors: Power engineering solutions and Buildings technology.

Power engineering solutions deals with power generation, distribution and transmission. The main customer for this business is the Ceylon Electricity Board (CEB). The other areas of business include energy management solutions, and the designing and installation of power transformers and switch gear. Key users are the national grid, high-rise buildings and industrial installations.



BUSINESS PERFORMANCE

(DIVERSIFIED ACTIVITIES)

Building technology deals with the design, supply and installation of fire detection, CCTV & Access control systems, and Building management systems.

Siemens, our main principal, as one of the largest electrical companies in the world, is also very keen on capturing a large market share in Sri Lanka and so we are upbeat about future prospects.

The business is well on the way to becoming a key player in the business composition of the Company, representing the non-auto sector.

Medical Engineering

The Government continues to play the leading role in the country's healthcare sector. In 2006, the total healthcare budget increased by 29%. The health policy framework also recognises the role of the private sector in providing Sri Lankans with an effective healthcare system.

The Group supplies the local health care sector with medical equipment from some of the world's leading suppliers including Siemens, Zeiss and Drager Medical.

The performance of this sector was not up to expectations. Government spending on the healthcare product lines that the Company serves was less than anticipated. Two major investments in private healthcare partially compensated for this loss.

Dimo was chosen to supply, install and maintain key equipment of the first privately owned hospital dedicated to oncology in Sri Lanka. The 'linear accelerator' from Siemens which was supplied for this project is a state-of-the-art equipment and another 'first' in Sri Lanka. Major investments were made in training engineers to provide pre-installation support and post-commissioning care.

Sri Lanka's first private hospital dedicated to ophthalmology chose to equip itself with cutting edge technology from the world's leader - Zeiss.

We are likely to see more private sector involvement in the health sector and we are looking at fresh opportunities that is emerging in this sector.



FINANCIAL REVIEW

The Group completed another successful year in what was a very challenging financial environment. Consistency in profit growth, increase in finance cost and a substantial increase in the assets base are some notable developments that continued from the previous year.

The growth in profit in a rapidly rising interest rate scenario is an affirmation of the Group's stable growth potential.

However, profit before tax fell short of the budgeted figure and rising finance costs is the main reason for this.

Whilst the existing businesses provided the platform for growth, the addition of new products and new businesses provided the impetus for future growth. The rapid increase in the size of operations is evident by the increase of turnover from Rs. 3.4 bn to Rs. 12.9 bn during the last five years. Total assets increased from Rs. 1.7 bn to Rs. 5.2 bn during the same period. Borrowings were the main source of funding for this growth, with retained earnings and proceeds from rights issues contributing in a smaller measure.

A five-year summary of key financial data captures the growth experienced by the Group during past five years:

| | 2002/03 Rs. mn | 2003/04 Rs. mn | 2004/05 Rs. mn | 2005/06 Rs. mn | 2006/07 Rs. mn. |
|---------------------------|-------------------|-------------------|-------------------|-------------------|--------------------|
| Performance | | | | | |
| Turnover | 3,405 | 4,797 | 7,565 | 10,512 | 12,989 |
| Gross Profit | 725 | 846 | 1,206 | 1,590 | 2,129 |
| Profit after Tax | 38 | 100 | 177 | 265 | 302 |
| Financial Position | | | | | |
| Total Assets | 1,727 | 2,252 | 3,195 | 4,570 | 5,199 |
| Current Assets | 1,198 | 1,692 | 2,461 | 3,794 | 4,193 |
| Borrowings | 867 | 958 | 1,609 | 2,795 | 2,840 |

Turnover

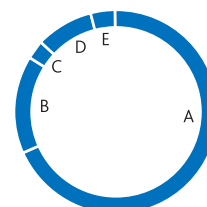
Turnover increased by 24% (39% in 2005/06) to Rs. 13 bn. This represents a compounded growth rate of 40% over a five-year period.

The vehicles segment contributed 68% (70% in 2005/06) to the turnover and recorded a 21% (40% in 2005/06) growth over the previous year. The key contributor to this was the Tata commercial vehicle business led by the 'Dimo Batta' which recorded a turnover increase of 21% (40% in 2005/06).

According to the Central Bank Annual Report, the number of vehicles registered in the country during the calendar year 2006 showed an increase of 31% (3% in 2005). Buses, goods transport vehicles and private cars were mainly responsible for the growth in the number of registrations during the year under review.

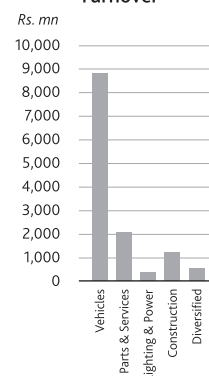
The vehicles spare parts and services, lighting and power tools, construction and material handling machinery and diversified activities segments recorded 19%, 30%, 50% and 29% increases in turnover respectively.

Segmental Turnover

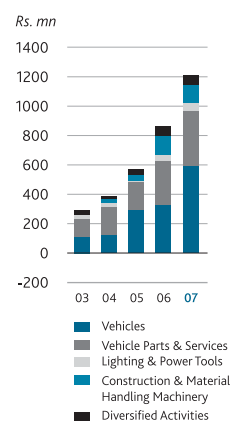


| | |
|--|-------|
| A Vehicles | 8,827 |
| B Parts & Services | 2,071 |
| C Lighting & Power Tools | 354 |
| D Construction & Material Handling Machinery | 1,202 |
| E Diversified Activities | 536 |

Business Segment Contribution to Turnover



Business Segment Profit from Operations



FINANCIAL REVIEW

Profitability

The gross profit increased by 34% (32% in 2005/06) to Rs. 2.1 bn (Rs 1.6 bn in 2005/06) which is higher than the increase in turnover of 24% (39% in 2005/06).

The segment results of vehicle parts and services, lighting and power tools and diversified activities, increased by 32% (40% in 2005/06), 16% (100% in 2005/06), and 9.5% (70% in 2005/06) respectively. The construction and material handling machinery segment results decreased by 13% in 2006/07 (increase of 215% in 2005/06).

Overheads

The increase of 29% (29% in 2005/06) in distribution expenses was approximately in line with the increase in turnover. A significant increase was noted in advertising, publicity and trade promotion activities.

The number of vehicles sold increased by 71% during the year under review.

Administrative expenses increased by Rs. 168 mn (Rs. 171 mn in 2005/06). The increase is largely attributable to the increase in staff costs. The number of employees increased by 11% during the year (23% in 2005/06).

Finance Expenses

Interest costs increased by 77% (73% in 2005/06) to Rs. 451 mn (Rs. 255 mn in 2005/06) mainly as a result of the increase in interest rates. The statistics shows that the Company's average interest rate has increased by 67% during the year. As a result of rising interest rates, the interest cover deteriorated from 2.4 times to 2.1 during the year under review.

Taxation

The income tax expense was Rs. 211 mn (Rs. 117 mn in 2005/06). The corporate income tax rate increased from 30% to 35%. This increase coupled with disallowable expenses relating to advertising and overseas travelling pushed the effective tax rate to 41% (31% in 2005/06). The reconciliation between accounting profit and taxable income is available on page 95.

Earnings

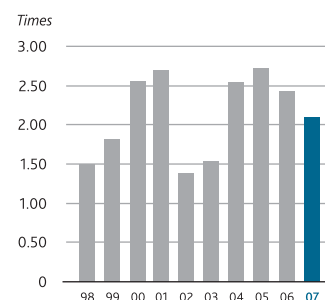
Profit from operations increased by 51% (63% in 2005/06) to Rs. 972 mn (Rs. 646 mn in 2005/06). This is a key performance indicator that is used to measure operational efficiency of a business unit without taking into consideration the volatility of interest rates.

The net profit after tax increased by 14% in 2006/07 (50% in 2005/06). This is in spite of a 51% increase in profit from operations during the year under review. Substantial increases in finance costs and tax expenses have had a negative impact on profit after tax.

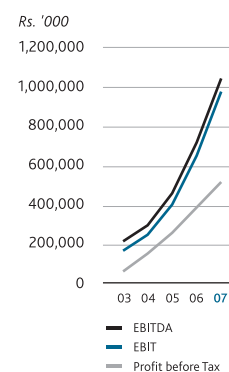
Property, Plant & Equipment

During the year under review, Rs. 306 mn was invested in property, plant & equipment (Rs. 120 mn in 2005/06). The Company spent Rs. 120 mn for the acquisition of a prime property situated opposite its Head Office. This property is to be developed to accommodate a workshop, service centre and offices to support the growth of the Company.

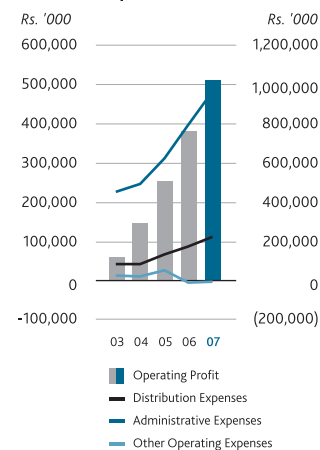
Interest Cover



Earnings



Operating Profit vs. Expenses



FINANCIAL REVIEW

Other key investments included expansion of commercial vehicles workshop; Upgrading of the light commercial vehicles workshop at Siyambalape; Relocation of the Kurunegala branch and the opening of a new showroom for Tata passenger cars. A substantial investment was made in acquiring four courtesy vehicles to provide a superior level of service to the Company's loyal customers.

Borrowings

Borrowings consist of term loans, import loans and bank overdrafts. Whilst the interest rates of term loans are fixed for two to three years, import loans are linked to money market rates.

Interest rates on overdrafts are reviewed periodically. A five-year term loan amounting to Rs. 117 mn (Rs. 415 mn in 2005/06) was obtained during the year. There is a marginal increase in the total borrowings as at the year end. The total borrowings outstanding as at the end of the year was Rs. 2,839 mn (Rs. 2,796 mn in 2005/06).

Cash Flow

Cash flow from operating activities was an inflow of Rs. 383 mn. This is compared to an outflow of Rs. 990 mn for the year 2005/06. The main contributing factor were reduction in trade receivables, a significant increase in payables and funds generated from operations.

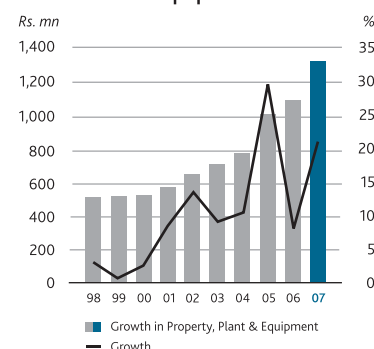
Despite a 24% increase in turnover a reduction was observed with regard to trade receivables. Cash received from customers during the year exceeded the turnover for the year. The cash outflow on account of capital expenditure amounted Rs. 305 mn (Rs. 123 mn in 2005/06).

During the year under review, the Company raised Rs. 55 mn through a rights issue. The outflow on account of servicing providers of finance in the form of interest and dividends amounted to Rs. 462 mn and Rs. 66 mn respectively. The Group cash and cash equivalent increased by Rs. 46 mn (Rs. 776 mn decrease in 2005/06).

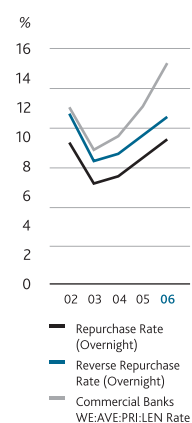
The Group possesses the necessary banking facilities to support its operations. Cash generated from operations and available banking facilities are adequate to finance working capital, capital expenditure, dividends and statutory payments.

Section 56 of Companies Act No. 7 of 2007, requires that a solvency test be carried out prior to the payment of dividends. In order to satisfy this requirement, the Company Auditors certified that the Company meets the required solvency levels. In doing so the Auditors confirmed that the Company has the ability to pay its debts as they become due in the normal course of business and that the value of the Company's assets is greater than the value of its liabilities and the Company's stated capital.

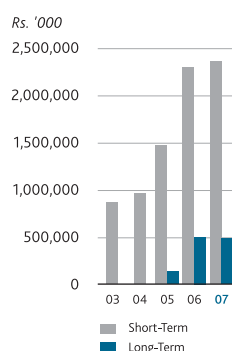
Growth in Property, Plant & Equipment



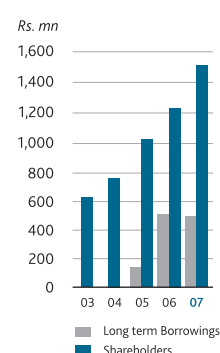
Interest Rates (31st Dec.)



Borrowings



Capital Structure



FINANCIAL REVIEW

The certification was obtained on 21st May 2007 based on the financial statements as at 31st March 2007. A computation carried out to establish the solvency is given below:

| | Rs. mn. |
|--------------------------|--------------|
| Non-Current Assets | 1,005 |
| Current Assets | 4,193 |
| Total Assets | 5,198 |
| Current Liabilities | 3,218 |
| Non-Current Liabilities | 474 |
| Total Liabilities | 3,692 |
| Stated Capital | 182 |
| | 1,324 |

Financial Priorities

The following are the Group's financial priorities that drive the Group's financial strategy:

- Optimising profitability through value addition and efficient utilisation of resources particularly through prudent working capital management.
- Striking a balance between growth and immediate profitability in allocating financial resources.
- Maintaining a healthy Balance Sheet.

Working Capital

The working capital as at the year end increased from 938 to 975. Prudent management of working capital is a key area of focus in our effort to produce a healthy Balance Sheet and to minimise finance costs. Inventories increased by 34% to Rs. 2.1 bn (Rs. 1.6 bn in 2005/06) due mainly to the high level of activity. However, strict control and monitoring enabled the Group to reduce trade receivables from Rs. 2.2 bn to Rs. 1.9 bn.

Treasury Management

The Group operates a central treasury function, which controls decisions in respect of cash management, utilisation of borrowing facilities, banking relationships and foreign currency exposure management. It enables effective cross utilisation of funds between business units. Policies are in place to guide the activities of the central treasury in terms of approval levels and the scope of decision making.

Retirement Benefits

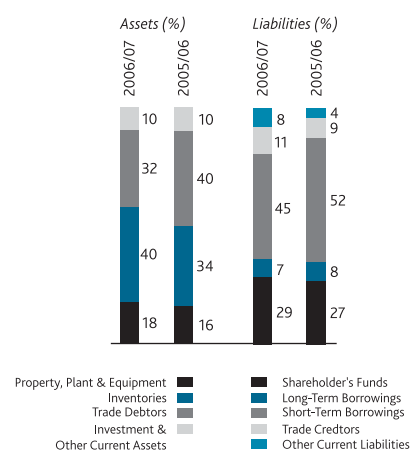
The Group accrues gratuity expenditure based on salary as at the end of the year. The provision for retirement gratuity as at 31st March 2007 amounted to Rs. 94 mn (Rs. 77 mn in 2005/06). The provision made for the year is Rs. 20 mn (Rs. 13 mn in 2005/06).

Contractual Obligations

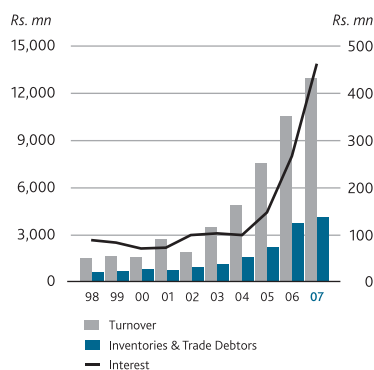
Financial contractual obligations to banks as at 31.03.2007 are given below:

| Obligation | Amount due 2007 Rs. mn | Amount due 2006 Rs. mn | Due date |
|----------------------------|---------------------------|---------------------------|---|
| Long-term Borrowing | 478 | 496 | Equal monthly instalment for 5 years |
| Short-term Borrowing | 2,218 | 2,282 | On maturity at terms ranging from one month to six months |
| Overdraft | 144 | 18 | On demand |
| Letter of Credit | 1,502 | 1,190 | As per LC condition |
| Bank Guarantees | 209 | 38 | As per Guarantee condition |
| Bid Bonds/Performance Bond | 148 | 41 | As per Bond condition |

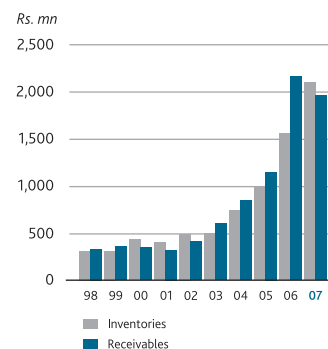
Balance Sheet Structure



Inventories & Trade Debtors vs. Turnover & Interest



Inventories & Receivables



FINANCIAL REVIEW

Foreign Currency Transactions

The US Dollar and the Euro are the principal currencies in which the Group's imports are denominated. A majority of receivables from foreign principals are also denominated in the same currencies. The Sri Lankan Rupee depreciated against the Dollar and Euro by 6% (3% in 2005/06) and 18% (2% in 2005/06) respectively.

Shareholders' Funds

Shareholders' funds increased to Rs. 1,507 mn from Rs. 1,216 mn. The increase of Rs. 302 mn in retained earnings and proceeds from the rights issue represent the increase.

Market capitalisation as at 31.03.2007 was Rs. 1.45 bn (Rs. 1.38 bn in 2005/06).

Earnings and Returns

Earnings Per Share (EPS) was Rs. 25.76 (Rs. 22.96 in 2005/06) representing a 12% increase during the year. The profit before tax recorded an impressive growth from Rs. 59 million in 2002/03 to Rs. 513 million in 2006/07. This contributed to a 67% compounded growth in EPS over five years.

Return on average capital employed and return on investment were 19% (22% in 2005/06) and 22% (24% in 2005/06) respectively.

The Directors have recommended a final dividend of Rs. 3/- per share, and this will bring the total dividend to Rs. 6/- per share for the year under review. The dividend cover was 4.16 times.

The Group possesses the necessary funds in order to finance the funding requirement that will arise due to the proposed final dividend.

The Group satisfies the solvency test requirements for payment of dividends as laid down in the Companies Act No. 7 of 2007.

Accounting and Financial Reporting

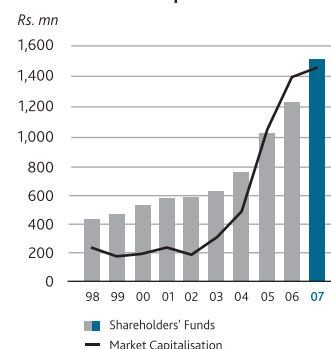
The Group strives to make meaningful disclosures of material information in the Annual Report and Accounts and has consistently focused on improving the presentation of information, within the framework of the Sri Lanka Accounting Standards.

It remains committed to the adoption of best practices in its communications with shareholders and other users of financial statements, within the bounds of commercial confidentiality, to enable them to make informed judgments on the performance of the Group.

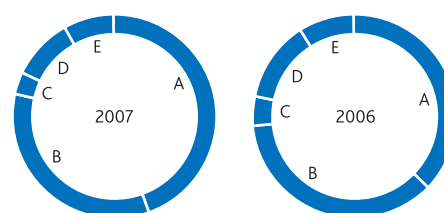
Return on Equity (ROE)

Return on equity has grown steadily in the last 3 years from 6% in 2002/03 to 20% in 2005/06. The ROE in the current financial year has however, shown a marginal decrease to 21%. The main cause of the fall in the ROE was the fall in the profit after tax which was affected by the increase in income tax charges in the year.

Shareholders' Funds vs. Market Capitalisation

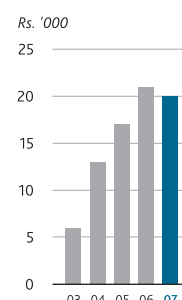


Composition of Gross Profit by Segment



| | 2007 | 2006 |
|--|------|------|
| A Vehicles | 44% | 37% |
| B Vehicles Parts & Services | 34% | 36% |
| C Lighting & Power Tools | 4% | 5% |
| D Construction & Material Handling Machinery | 10% | 13% |
| E Diversified Activities | 8% | 9% |

Return on Equity



FINANCIAL REVIEW

Economic Value Added (EVA)

Economic Value Added (EVA) is a performance measure developed by Stern Stewart & Co. Ltd. that attempts to measure the true economic profit produced by a Company. It is frequently also referred to as 'economic profit' and provides a measurement of a company's economic success (or failure) over a period of time.

| | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
|---|---------------------|---------------------|
| Total Capital Supplied | | |
| Shareholders' fund | 1,506,508 | 1,216,031 |
| Long-term interest bearing loans and borrowings | 477,565 | 495,800 |
| | 1,984,073 | 1,711,831 |
| Earnings | | |
| Profit after tax | 301,777 | 265,173 |
| Add: Interest on long-term borrowings | 58,925 | 48,297 |
| Adjusted earnings | 360,702 | 313,470 |
| Weighted average cost of capital (WACC) | 14.38% | 14.44% |
| Economic charge | 285,310 | 247,188 |
| Economic Value Added (EVA) | 75,392 | 66,282 |

| | Source | 2006/07 | 2005/06 |
|---|-----------------|---------|---------|
| Average Risk Free Rate (Average Treasury Bill Rate) | Central Bank | 11.88% | 9.70% |
| Beta Factor - DIMO | CSE | 0.37 | 0.89 |
| Market Rate of Return (based on ASPI) | CSE | 23.00% | 18.97% |
| All Share Price Index (ASPI) | CSE | 2,789.8 | 2,264.4 |
| Average Weighted Prime Lending Rate (AWPLR) | Central Bank | 14.13% | 11.35% |
| Rate of Income Tax | Applicable Rate | 35% | 30% |
| Cost of Equity (based on CAPM) | Computed | 15.99% | 17.95% |
| Cost of Debt (After Tax) | Computed | 9.18% | 7.95% |

Market Value Added (MVA)

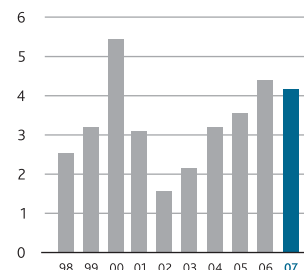
Market Value Added (MVA) is the difference between the current Market Value of the Company and the capital contributed by investors viz. shareholder equity. MVA is an indicator of shareholder wealth unlike EVA which is a performance measure. Market price of a share is a key variable in MVA, and its interpretation should take into account the impact of the Company's performance on the market price per share as well as the trends in the stock market.

The computation of the MVA of the Company is below:

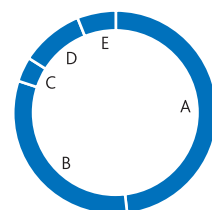
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
|-----------------------|---------------------|---------------------|
| Market Capitalisation | 1,452,000 | 1,385,000 |
| Shareholders' Funds | 1,506,508 | 1,216,031 |
| Market Value Addition | (54,508) | 168,969 |

MVA as at year end showed a negative value of Rs. 54.5 mn in the backdrop of a Rs. 290.4 mn increase in equity and a 13% decline in market value per share during the year.

Dividend Cover (Times)

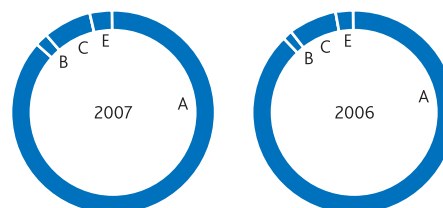


Segmental Contribution to EBITDA



| | |
|--|-----|
| A Vehicles | 48% |
| B Vehicles Parts & Services | 32% |
| C Lighting & Power Tools | 4% |
| D Construction & Material Handling Machinery | 10% |
| E Diversified Activities | 6% |

Cost and Expenses



| | 2007 | 2006 |
|----------------------------|------|------|
| A Cost of Sales | 86% | 87% |
| B Distribution | 2% | 2% |
| C Administrative | 8% | 8% |
| D Other Operating Expenses | 0% | 0% |
| E Finance Cost | 4% | 3% |

INTRODUCTION

Statement by the Chairman

Sustainable Entrepreneurship:

A Constant Learning Process

"I am convinced that stakeholder value maximisation and corporate social responsibility go hand-in-hand."

Today's corporate citizen cannot survive without paying due attention to their social responsibilities. Unlike the corporate entities of yesteryear today's companies are required to comply with a variety of regulatory and legal measures on sustainable development, enterprise governance and corporate responsibility.

A positive Corporate Social Responsibility (CSR) outlook is an asset to today's entrepreneurs as much as are financial assets. It facilitates acceptance and recognition among a wide spectrum of society. We are also conscious that financial growth should not compromise on corporate values and business ethics. Financial growth should be with integrity, equity and responsibility. The values of CSR moreover help us to keep in mind the impact of our corporate activities on all our stakeholders, including our employees, generations yet unborn and society in general.

Sustainable value creation is a dynamic process. As a Company we are constantly learning new things and every year we integrate new processes and systems into our business practices. We are constantly trying to refine our systems and processes to ensure that we continue to generate durable value for all our stakeholders without compromising on any of our principles and ethics.

Details of our policies and practices on sustainable entrepreneurship are contained in this report. Last year, our efforts in this area received external and objective recognition when we were placed first in the medium scale category at the ACCA Sustainability Reporting Awards.

The initiatives we have put in place have been the result of years of planning and ethical entrepreneurship. We will continue to evolve sustainable business practice that nurture human relationships, empower society and protect the environment in more meaningful ways.



A.R. Pandithage
Chairman

This is Dimo's third Sustainability Report.

This report is presented to our stakeholders with a view to sharing as complete a picture as possible on all aspects of the Company's activities. It documents some of the less visible and less tangible aspects of the Company's operations and shows how we are discharging our social responsibilities as a modern corporate citizen.

This Sustainability Report has two broad goals. First to communicate to our diverse stakeholders Dimo's processes of sustainable wealth creation in as detailed a manner as possible. Secondly, to trigger a process of reflection and review within the organisation and to consider how we could strengthen our operational procedures and business practices with regard to sustainable wealth creation. To us sustainable value creation is a dynamic process and every year we seek to push the bar higher.

The Report is divided into four sections. The first section examines our overall strategy to sustainable entrepreneurship. It looks at our efforts at creating sustainable and durable corporate solutions, balancing today's expectations with the needs of generations yet unborn. It also looks at our processes for stakeholder involvement in the decision making of the Company.

The second section looks at how we have added economic value to our major stakeholders and examines our interaction with the economic environment of the country.

The third section documents our interaction with the environment. We look at our efforts at preserving and nourishing our natural environment as we go about delivering sustainable value to our stakeholders.

DIMO QUALITY & ENVIRONMENT POLICY

"We at Dimo are committed to:

- Continuously improve our systems & processes
- Total customer satisfaction
- Develop human resources
- Conservation of resources
- Reducing waste
- Compliance to Legal Statutory and the requirements of the Principals

The fourth section examines how we interact with people: the people within our organisation and the people who form part of the wider social community.

The report conforms largely, though not entirely, with the G3 guidelines as published by the Global Reporting Initiative.

The report covers the operations of the business units directly under Diesel and Motor Engineering PLC and its subsidiaries. The environmental data has been extracted from our EMS reports, the operating data maintained by the different business units over the past year and from periodic on site analysis.

In our Business Review we look in detail at how the different business units of the Company have performed over the past year. Our organisational profile, product portfolio, and group structure are detailed elsewhere in the report. Our procedures of governance are detailed more exhaustively in the Enterprise Governance section.

In accordance with our standards on transparency in this Sustainability Report we attempt to report on both the positive and negative aspects of the Company's behaviour.

Responsible and Durable Value Addition**Dimo's Sustainable Values**

Six key ideas have guided our efforts at sustainable value creation:

- Put the customer first ... and make sure he or she remains there. Offer high quality, relevant products and services and constantly strive to raise the 'bar of excellence'.
- Create relationships, not transactions: ensure that relationships with principals, dealers, suppliers, employees, financial institutions, business partners and government, are fostered, fertilised and promoted for these are vital to the social empowerment we seek to achieve.
- Make work enjoyable, rewarding and productive: Reward initiative, dynamism and commitment, frown on lethargy, indifference and inactivity.
- Adopt uncompromising business ethics: never yield.
- Empower society. Explore every window for creating new opportunities and adding new social value.
- Love the physical environment intimately and never let her down.

An Overview of the Stakeholder Dialogue Process

| Stakeholder | Sustainability Issues & Concerns | Process of Engagement |
|--|---|--|
| Shareholders <ul style="list-style-type: none"> • Owners • Providers of capital | <ul style="list-style-type: none"> • Profits & Growth | <ul style="list-style-type: none"> • Annual General Meeting provides an opportunity to review the past year's performance and engage in discussions with the management • Quarterly and half yearly reports provide a contemporary review of performance during the year |
| Employees <ul style="list-style-type: none"> • The key resource for competitive advantage and sustainable growth | <ul style="list-style-type: none"> • Individual's future is linked to the Company's growth • Personal development, • Health & Safety • Balance between professional and personal life | <ul style="list-style-type: none"> • Employee Council meetings • Employee Portal of the Company network accessible to every employee. • Company's 'Open Door' policy encourages direct employees - management dialogue. • Annual Employee Surveys - voluntary and confidential. • Employee Intranet • Quarterly Newsletter |
| Customers <ul style="list-style-type: none"> • Principal source of sustenance | <ul style="list-style-type: none"> • Product quality • Availability • Standard of after care • Availability of after care | <p>Customer Relationship Management process (CRM) enables keeping in touch with the customer on a daily basis. It helps to respond to queries and problems from the customer. 'Problem solving' for challenges the customer faces is also done through the CRM process</p> <p>A Customer Satisfaction Index maintained by each department provides an assessment of satisfaction levels and helps to improve problem solving capacities within the Company</p> |
| Business Partners <ul style="list-style-type: none"> • Critical part of the value chain | <ul style="list-style-type: none"> • Market share • Profitability • After care | <p>A high speed 24 x 7 on-line link enables constant dialogue with principals. Issues discussed include product quality, marketing, customer satisfaction, 'problem solving' and employee motivation</p> <p>On site visits from principals and on site visits to principals' location also facilitate engagement</p> |

OUR STRATEGY FOR **SUSTAINABLE** ENTREPRENEURSHIP

Nothing Succeeds Like Success

We believe that our greatest social responsibility is to be a 'successful' corporate enterprise. Success as a corporate enterprise however, does not mean a thick bottom line, but rather a process of value creation that constantly benefits every segment of society today, tomorrow and the day after. We aim not just at economic or financial prosperity but social prosperity all round.

Listening to the Other:

Our Processes for Stakeholder Dialogue

Participation and inclusivity are the two key values that shape this process of stakeholder dialogue. Every year we seek to strengthen our processes of stakeholder dialogue.

Some stakeholders tend to dominate as in the case of customers and shareholders. At the same time we have in place processes of decision making that enable us to balance customer needs and shareholder demands with larger social and environmental goals and employee expectations. One of the challenges of sustainable corporate activity is to strike that fine balance amongst the demands of all stakeholder interests and ensure an equitable and enduring outcome.

Shareholder Dialog

The Annual General Meeting (AGM) provides a regular forum for shareholders to discuss the Company's performance, financial statements and accounts, proposed dividend disbursements, appointments to and resignations from the Board and other proposals. The Annual Report is distributed well in advance of the AGM and this gives shareholders an opportunity to assess the Company's performance and engage in a constructive dialogue with the management.

The Company also releases quarterly reports and this provides another way for shareholders to monitor the performance of the Company on a regular basis. Further, as the Company is listed on the Colombo Stock Exchange (CSE), details on share price movements and important corporate announcements are readily available to shareholders on the CSE website.

The Company also has in place an informal process that enables shareholders to communicate with the Company representatives on any issue. These communications are recorded and the Company ensures as quick a response as possible. In addition Shareholders may consult the Company Secretary at any time on any issue.

Employee - Management Dialogue

Employee Council

Our Employee Council meets every month. These Employee Council meetings provide a forum for an employee representative of every Business Unit to interact and engage with the Management Committee on a variety of issues. The meetings are always chaired by the Chairman/MD. Employees, through their representative, can put forward and discuss any idea or grievance.

Transparency is the essence of these dialogues. Minutes of these meetings are posted on the Employee Portal of the Company network. The Portal can be accessed by every employee and employees have an opportunity to get a sense of how the discussion went and to see what solutions were reached.

This process is supplemented by the Company's 'Open Door' policy which encourages employees to engage in direct

OUR STRATEGY FOR **SUSTAINABLE** ENTREPRENEURSHIP

dialogue with the management. This enables employees to get prompt attention for any grievance they may have or a response for any idea that they want to implement.

The Company is constantly looking at ways of improving the dialogue process between employee and management. Our goal is to simplify these processes, and make the channels of dialogue accessible to all employees at every level.

Employee Surveys

A more structured and formal process that we have entrenched is the annual 'Employee Survey'. Every year Dimo conducts an in-house employee survey. It is voluntary and confidential. Employee may choose to submit their name or send an anonymous response.

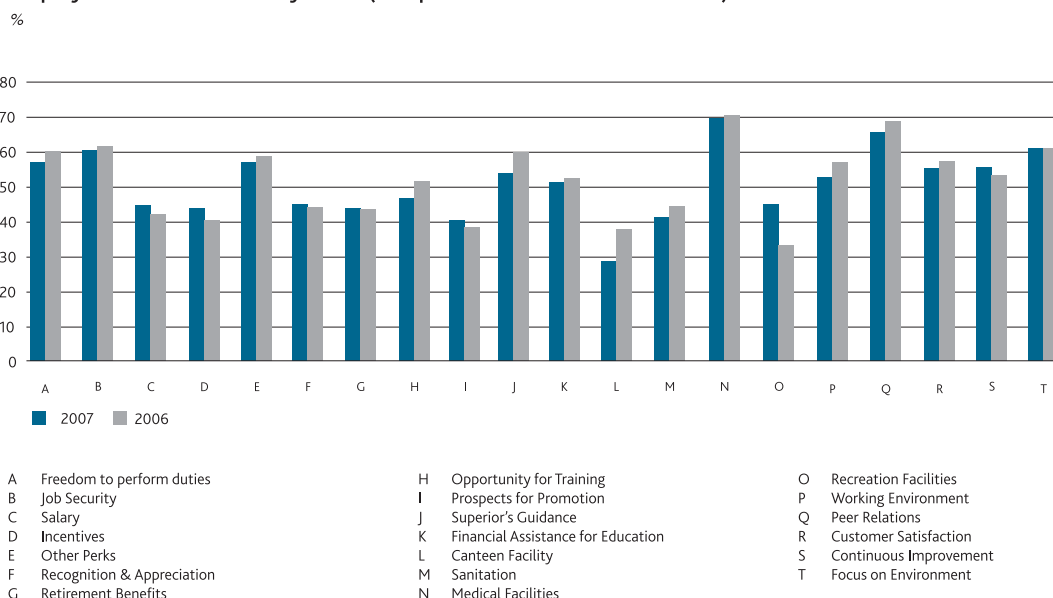
The annual employee survey provides yet another channel for employees to share their views with the management in a written form. The survey is structured and seeks employee opinion on a variety of areas.

A summary would then be prepared and this will be shared with the management and the Employee Council. Based on an analysis of this summary management and Employee Council members will formulate an action plan to respond to the comments contained in the employee survey.

The overall satisfaction index recorded this year was 52.23% as opposed to a 52.60% during the previous financial year. Out of a total of 862 employees 664 of them participated in the survey. This amounts to a response rate of nearly 78%. The Company finds that the survey conducted this year has been the most successful and representative when compared with last year's response rate of 35% (259 out of 733 employees responded).

Since this is used as a tool to identify areas for improvement improving canteen facilities would receive priority under welfare initiatives.

Employee Satisfaction Survey Index (comparison between 2006 & 2007)



OUR STRATEGY FOR **SUSTAINABLE** ENTREPRENEURSHIP

Employee Intranet and Newsletter

Dimo operates an employee intranet which carries information on each employee's attendance, news on training opportunities and upcoming Company events.

We also produce a quarterly newsletter which carries news about the Company. Employees are encouraged to be regular contributors to the newsletter.

Employees may also communicate via email with fellow employees, their immediate superiors and the management. Periodic meetings are held within each business unit and this provides another opportunity for dialogue and discussion.

Customer Relations

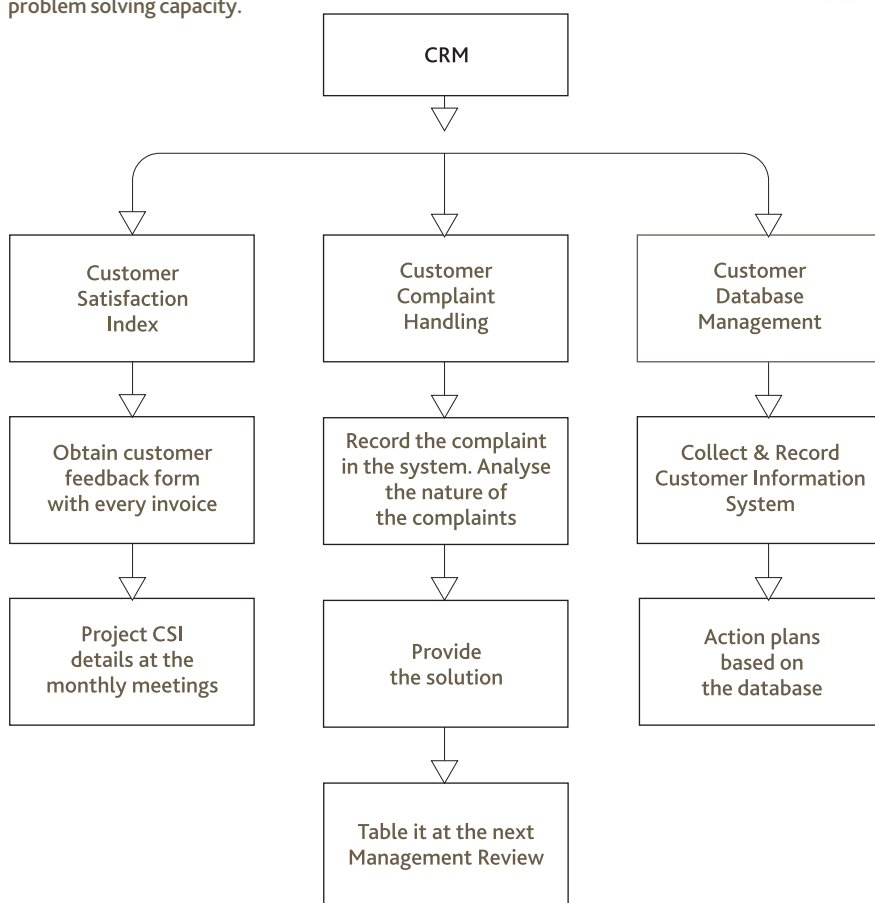
Establishing and nurturing good relationships with customers is a vital aspect of Dimo's operations. Understanding customer needs and responding to them is of fundamental importance to the long-term success of the Company.

Dimo's Customer Relationship Management process (CRM) provides the key interface through which the Company keeps in touch with the customer on a daily basis. Through the CRM, we maintain a dialogue with our customers and solicit opinions and new ideas and respond to queries and problems. Problem solving in respect of particular challenges the customer may have faced is also accomplished through the CRM process.

Our CRM process ensures that we respond instantly to customer problems. Once the problem is referred by the customer to Dimo, the Company will acknowledge the complaint on the day of referral. We then strive to provide a solution within a targeted date usually limited to six working days. In the process, the CRM department will analyse the issue from both perspectives - that of the customer and the Company - and co-ordinate the entire process until we provide a satisfactory solution to the customer.

The CRM Department maintains a Customer Satisfaction Index for each department, forwarding weekly reports to departmental heads. These reports contain an analysis of customer responses and enable the Company to keep improving its problem solving capacity.

Dimo quarterly News Letter



OUR STRATEGY FOR **SUSTAINABLE** ENTREPRENEURSHIP

Total number of complaints recorded at CRM

| | April | May | June | July | Aug. | Sept. | Oct. | Nov. | Dec. | Jan. | Feb. | Mar. | Total |
|---------|-------|-----|------|------|------|-------|------|------|------|------|------|------|-------|
| 2005/06 | 13 | 19 | 30 | 25 | 28 | 36 | 28 | 28 | 23 | 25 | 21 | 29 | 305 |
| 2006/07 | 13 | 32 | 25 | 28 | 37 | 49 | 54 | 57 | 32 | 48 | 29 | 54 | 458 |

Solutions provided

| Days | less | 6 | more | Total |
|-----------|------|----|------|-------|
| April | 11 | – | 2 | 13 |
| May | 23 | 5 | 4 | 32 |
| June | 25 | – | 0 | 25 |
| July | 12 | – | 16 | 28 |
| August | 22 | 6 | 9 | 37 |
| September | 22 | – | 27 | 49 |
| October | 32 | – | 22 | 54 |
| November | 35 | 2 | 20 | 57 |
| December | 6 | 1 | 25 | 32 |
| January | 25 | 1 | 22 | 48 |
| February | 20 | – | 9 | 29 |
| March | 29 | – | 25 | 54 |
| | 261 | 15 | 181 | 458 |

Pending at month end

| Sales Issues | Registration Issues | Product Issues | Parts Issues | Service Issues | Total |
|--------------|---------------------|----------------|--------------|----------------|-------|
| 1 | – | – | – | 1 | 2 |
| 1 | 1 | 2 | 1 | 2 | 7 |
| 1 | – | – | – | 2 | 3 |
| 4 | 2 | 3 | 3 | 4 | 16 |
| 6 | 2 | 2 | 5 | 7 | 22 |
| 18 | 3 | 1 | 3 | 9 | 34 |
| 4 | 6 | 6 | 4 | 5 | 25 |
| 2 | 3 | 10 | 4 | 4 | 23 |
| 1 | 3 | 6 | 4 | 5 | 19 |
| 4 | 5 | 6 | 9 | 5 | 29 |
| 5 | 2 | 3 | 5 | 5 | 20 |
| 4 | 2 | 5 | 5 | 6 | 22 |
| 51 | 29 | 44 | 43 | 55 | 222 |

All complaints were provided with a satisfactory solution eventually.

Principals

Our dialogue with our principals is facilitated by a high speed 24 x 7 on-line link. We are in constant communication with our principals on a variety of issues pertaining to product quality, marketing, customer satisfaction and employee motivation. We seek more than anything else, to build a long-term win-win relationship with our principals. Most of our business relationships have long, rich and satisfying histories.

Principals carry out periodic reviews of our performance, the quality of our 'aftercare' and the Company's compliance with other guidelines. Mystery shopping exercises, surveys, corporate identity audits and service excellence competitions provide other conduits for our principals to assess the Company and the 'performance' of their products.

GENERATING & SUSTAINING ECONOMIC VALUE FOR OUR STAKEHOLDERS

Management Approach

Creating and operating a sustainable business is our top priority. In so doing we seek to provide sustainable value to all our major stakeholders: shareholders, lending institutions, employees, customers, principals, suppliers, government, the larger society and disadvantaged communities. Wealth creation in the Dimo vision embraces monetary and non-monetary aspects. Sustainable business development enhances long-term profitability in our view.

Investors

The value that accrues to a shareholder is the combination of the dividends declared and the appreciation of the share value

over the medium to long-term. The Total Shareholders' Return chart captures in graphic form how Dimo has added value to its shareholders over the years. Here too sustainability has been our guiding principle and we have not sacrificed long-term gain for short-term benefits.

As of 31st March 2007 the Company's shareholder equity stood at Rs. 1,506 mn. The comparative figure for the last financial year was Rs. 1,216 mn. The increase in share equity was the result of an increase in net income after distribution of dividends.

Statement of Value Added

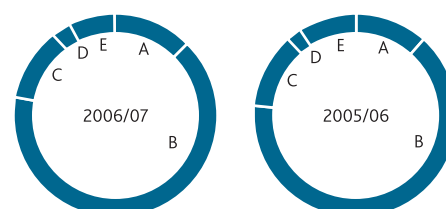
Value Created

| | Consolidated 2006/07 Rs. '000 | Consolidated 2005/06 Rs. '000 | Company 2006/07 Rs. '000 | Company 2005/06 Rs. '000 |
|--|-------------------------------------|-------------------------------------|--------------------------------|--------------------------------|
| Gross turnover | 12,989,916 | 10,512,326 | 12,449,644 | 10,096,026 |
| Other income | 28,380 | 27,527 | 29,221 | 27,462 |
| Less: Cost of material and services bought in | (9,557,576) | (7,740,997) | (9,164,286) | (7,448,590) |
| | 3,460,720 | 2,798,856 | 3,314,579 | 2,674,898 |

Value Shared with

| | Consolidated 2006/07 Rs. '000 | Consolidated 2005/06 Rs. '000 | Company 2006/07 Rs. '000 | Company 2005/06 Rs. '000 |
|--------------------------|-------------------------------------|-------------------------------------|--------------------------------|--------------------------------|
| Employees | 13 432,159 | 14 378,759 | 12 385,090 | 13 342,529 |
| Government | 64 2,206,250 | 65 1,829,608 | 65 2,163,764 | 67 1,797,960 |
| Lenders | 13 450,926 | 9 254,922 | 13 418,698 | 9 228,493 |
| Shareholders | 2 72,600 | 2 60,000 | 2 72,600 | 2 60,000 |
| Retained in the business | 8 298,785 | 10 275,567 | 8 274,427 | 9 245,916 |
| Depreciation set aside | 2 63,308 | 2 65,394 | 2 58,699 | 2 61,716 |
| Profit retained | 6 235,477 | 8 210,173 | 6 215,728 | 7 184,200 |
| | 100 3,460,720 | 100 2,798,856 | 100 3,314,579 | 100 2,674,898 |

Consolidated Value Added



| | 2007 | 2006 |
|----------------------------|------|------|
| A Employees | 13% | 14% |
| B Government | 64% | 65% |
| C Lenders | 13% | 9% |
| D Shareholders | 2% | 2% |
| E Retained in the business | 8% | 10% |

GENERATING & SUSTAINING ECONOMIC VALUE FOR OUR STAKEHOLDERS

Retaining Earnings for Long-Term Value Generation

The Statement of Retained Earnings discloses the undistributed profits retained for long-term value creation to strike a balance between immediate return and long-term wealth maximisation of our shareholders.

The retained earnings for a year represents the difference between the profit after tax for a period and the distributed profits for that same period.

Competitive, Market Based Rewards

Competitive remuneration is important in building a core team of employees and delivering sustainable value to all our stakeholders.

The Company shared Rs. 432 mn with its employees as salary and wages, statutory payments and retiring gratuity payments. This is in comparison to the Rs. 379 mn provided in 2005/06. A detailed breakdown appears on page 94, Note 42 to the accounts.

Principals & Suppliers

Our principals are the source of all our products. Here too our goal is to nurture long-term sustainable relationships that create win-win situations for both.

Our policy is to settle all outstanding dues promptly and to comply in full with all legal and contractual obligations.

Payments are always made according to agreed terms.

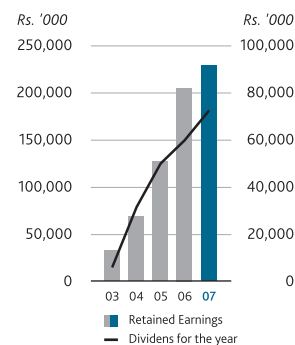
The 'cost of goods and services brought in' component in our Statement of Value Added appearing on page 46 provides the value transferred to them during the year.

Adding Value to the Government

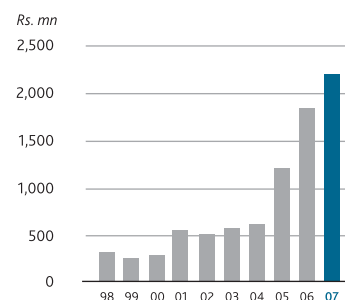
The Company ensures that all obligations to the Government is met as per legislation.

During the financial year, the Company paid out Rs. 2,206 mn (Rs. 1,830 mn in 2005/06) or 64% of its total value added by way of taxes and levies to the Government of Sri Lanka. This is 20% more than the sum paid during the previous financial year.

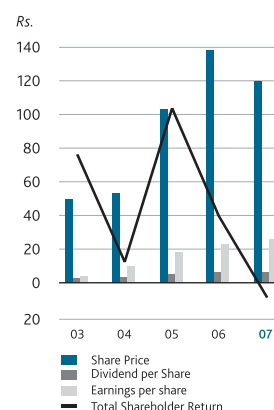
Retained Earnings vs Dividend Distributed



Group Revenue to Government



Total Shareholder Return



Total Shareholder Return

| Rs. | 2003 | 2004 | 2005 | 2006 | 2007 |
|----------------------------|-------|-------|--------|--------|--------|
| Share Price | 50.00 | 53.00 | 103.00 | 138.50 | 120.00 |
| Dividend Per Share | 3.00 | 3.50 | 5.00 | 6.00 | 6.00 |
| Total Shareholders' Return | 76.67 | 13.00 | 103.77 | 40.29 | (9.03) |
| Earnings Per Share | 3.88 | 10.03 | 17.72 | 22.96 | 25.76 |

CONSERVING & REPLENISHING THE

ENVIRONMENT

Management Approach

Central to our policy on sustainability is our effort to 'do no harm' to the physical environment and to constantly look at ways of replenishing our natural resources. No process of sustainable value creation can ignore the natural environment.

Our Environmental Management System (EMS) - the EMS has the ISO 14000 certification.

In 2005 our operations were certified with the Environmental Management System (EMS). This comprehensive plan allows us to measure the impact that our operations have on the environment and enables us to identify the steps we should take to minimise any adverse consequences. The EMS also helps to share energy saving processes and technologies within the Company and to reduce wastage.

Our EMS is guided by the Triple R concept: reduce, reuse and recycle.

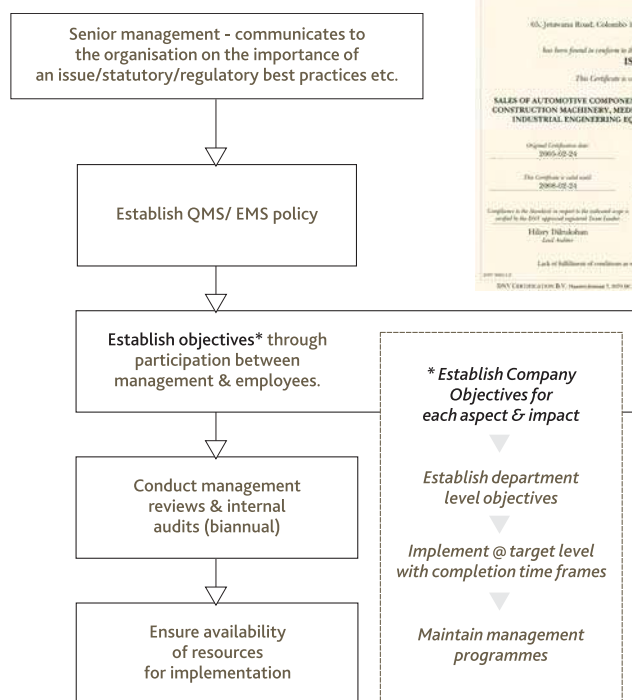
The EMS has helped us identify five strategic areas that require focused attention:

- Energy, water and fuel management
- Emissions management
- Waste management
- Noise control
- Material management

Energy Management

Dimo's primary source of energy is electricity. Our EMS enables us to monitor energy utilisation and to identify opportunities for further control and management.

QMS/EMS Process



Specific initiatives taken in this regard includes:

- Our incandescent lamps are progressively being replaced by energy saving lamps. It is our goal is to replace 100% of our lamps with energy saving lamps. All replacements during the year were energy saving bulbs.
- All computers in the Dimo Group revert to standby mode within five minutes of idling. All new units ordered by the Company come with low radiation levels.
- Air-conditioning units are regularly serviced and are set at a constant minimum of 24 degrees C. Natural sunlight is used wherever possible and staff is constantly made aware of the need to 'switch off'. Machinery is

CONSERVING & REPLENISHING THE ENVIRONMENT

operated at optimum energy levels and alternative sources of energy are constantly being explored.

Water Management

The Company's main source of water comes from the national supply.

Our main focus in this area is to significantly reduce our levels of water consumption through a more efficient utilisation of this resource. We will accompany this with the adoption of sophisticated water recycling and waste treatment processes throughout our facilities wherever this is possible.

Specific measures we have taken in this area include:

- The reuse of recycled water in example at the Siyambalape Branch, water is recycled twice before being discharged into the sewage system. This is because of the high level of waste from that particular facility. This water treatment plant was enhanced during the past year.
- Widespread employee education, to emphasise the need for water conservation, and to create a water friendly culture within the organisation.
- Installing water meters at various usage points to track consumption and drive conservation efforts further.
- Having water treatment plants at our locations to ensure that waste water is treated before being discharged into the public sewage system, with the introduction of a pH testing system. The system operates 24 hours a day and tests water at specified intervals to ensure that the discharged water conforms to legal limits.

Noise Control

Noise control has two dimensions. The first is to ensure that noise levels within our locations are minimised and well within the limits set down by the environmental regulations. The second is to ensure that the communities in the vicinity of our locations are not inconvenienced by noise emanating from our facilities.

The Diesel pump testing room at the Dimo Head Office was made sound proof during the year 2004/05. It continues to be in use.

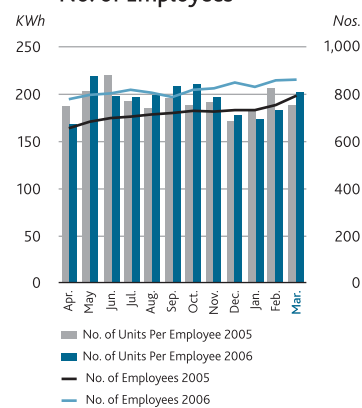
The Company periodically measure noise levels at various locations within each of our business premises. Noise levels at all our locations were found to be in accordance with legal limits.

Emissions to Air

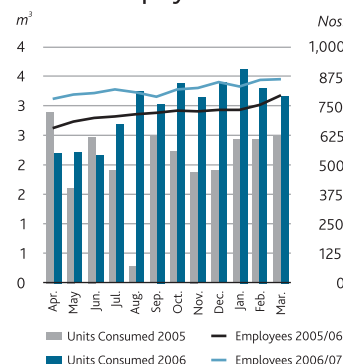
Dimo is committed to reducing ambient air emissions at every stage of its workshop operations. The following are some of the detailed measures we have adopted with a view to reducing air emissions:

- Carbon Dioxide (CO₂) is the most lethal of the six gases that contribute to global warming. Exhaust extractors at all our locations are designed to capture CO₂ and diesel fumes. These fumes are then excreted into a machine, which is carried upward to legally permissible limits before they are released to the air.
- All Dimo vehicles are subject to regular and stringent emission testing to ensure that they comply with the emission regulations under the National Environment Act.
- Ozone depleting emissions such as gas from air-conditioning units are recycled in special machines to avoid leakage into the environment.

Electricity Consumption per Employee vs. No. of Employees



Water Consumption per Employee vs. No. of Employees



Water treatment facility at the Siyambalape premises



CONSERVING & REPLENISHING THE ENVIRONMENT

- Our passenger car workshop in Colombo is fitted with exhaust gas and dust extractors, the former to deal with harmful gas emissions and the latter to absorb dust that emanates when air filters and brake components are cleaned.
- All our paint booths are fitted with filters to prevent the release of paint fumes and particles into the environment.
- Chemical spillage is extremely rare and our EMS contains detailed provisions for responding to such an eventuality.
- Oil waste is disposed of to the furnaces of authorised dealers.
- A 'take back' scheme which enables customers to return used tyres: which are then provided to a company which recycles the tyres and uses it as raw material. The number of tyres taken back during the year amounted to 830.

Waste

The Company's policy is to reduce waste as much as possible. Where waste does arise, we make every effort to reuse and recycle as much as is technically and economically feasible.

We have adopted the following measures as part of our Responsible Waste Control Policy:

- Colour coded containers in offices to segregate paper from plastics.
- Colour coded containers in dining areas to segregate food from wrapping materials.
- All used toner cartridges are recycled. Toners are collected by our supplier, who in turn, resends the used toner cartridges to the manufacturer. During the year we recycled approximately 60 cartridges in this manner.
- Segregated paper is disposed of to an authorised paper recycler.
- Awareness Campaigns within the organisation to create paperless offices in the future.
- Oil suckers are used to minimise oil spillage on the shop floor.

Paper Management

The Company's two broad objectives in this area are to:

- Reduce the consumption of paper
- Adopt environmentally friendly methods of disposing used paper.

The EMS implemented the following specific measures to achieve the above goals:

- Awareness campaigns within the organisation with a view to creating a paperless office.
- Staff are encouraged to reuse paper which has only a single side used.
- Awareness campaigns around the excessive printing of e-mails and other documents.
- All e-mails within are created with a message 'Please consider your environmental responsibility before printing this e-mail.'
- Initiatives to foster reuse of 'one sided' paper.
- The use of recyclable paper bags when selling products to customers at our sales outlets.

1. Caring for the environment - use of recycled paper bags
2. Clearly marked bins for collecting used papers ready for recycling
3. In-house notices to promote energy saving actions



PEOPLE

INVESTING IN THEIR HABITAT, THEIR FUTURE & THEIR POTENTIAL

Investing in people is very much a part of the Dimo sustainability policy. This includes investments in the people who work for the organisation and investments in the people who form part of the larger community.

Our intellectual capital in the form of our people and processes is one of the Company's most significant assets. Our goal is to nourish and nurture this intellectual capital to produce sustainable and durable outcomes for all stakeholders including the people themselves.

Valuing the Employee

Fundamental to our People Policy is to treat every employee with equal concern and respect. Dimo is an equal opportunity employer and an employee once recruited will be treated according to merit and the flair displayed.

At Dimo we strive to make work enjoyable, rewarding and productive. We focus on rewarding initiative, dynamism and commitment and sanction lethargy, indifference and inactivity. Dimo workplaces are stimulating and invigorating environments where each employee sees himself or herself as part of the larger Dimo team. Thus, the workplace supports not just professional endeavour but is a place of warmth, laughter, joviality and team building.

Our Current Strength

Dimo had 862 employees as of 31st March 2007.

Age Analysis as at 31st March 2007

| Age Group | Non-Executive | | | Executive | | | Total |
|-----------|---------------|--------|-------|-----------|--------|-------|-------|
| | Male | Female | Total | Male | Female | Total | |
| Above 61 | 4 | – | 4 | 5 | – | 5 | 9 |
| 51 - 60 | 38 | 2 | 40 | 36 | 4 | 40 | 80 |
| 46 - 50 | 25 | – | 25 | 32 | 6 | 38 | 63 |
| 41 - 45 | 27 | – | 27 | 42 | 7 | 49 | 76 |
| 36 - 40 | 38 | – | 38 | 51 | 1 | 52 | 90 |
| 31 - 35 | 58 | 2 | 60 | 66 | 9 | 75 | 135 |
| 26 - 30 | 133 | 7 | 140 | 77 | 11 | 88 | 228 |
| 21 - 25 | 124 | 15 | 139 | 27 | 8 | 35 | 174 |
| Below 20 | 6 | – | 6 | 1 | – | 1 | 7 |
| Total | 453 | 26 | 479 | 337 | 46 | 383 | 862 |

A Stimulating Workplace

Performance related incentives are offered by the Company and 'super performers' duly rewarded. Longevity of service is given special recognition and treated as a milestone for the employee concerned. Every employee receives comprehensive life assurance and is covered 24 hours a day. In addition, full-time employees are provided with distress loans, loans for the purchase of consumer products, reimbursement of professional examination fees.

Employees rewarded for their much appreciated help towards containing the fire at the main stores

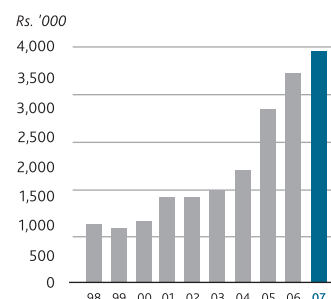


Employee - Management Relations

Dimo conducts an annual strategy presentation to the staff of every business unit, where all employees are informed of the Company's future direction and strategy. This forum is also used to spread the Dimo values of sustainability.

Employee representatives are invited to public award ceremonies at which the Company's achievements are recognised.

Value Added per Employee



INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

Instead of traditional trade unions employees have an Employee Council which looks after staff welfare. This is discussed under the employees section under Stakeholder Engagements on pages 41 to 45.

Occupational Health and Safety

The ISO 14000 standards require the Company to set and meet health and safety standards every year.

No serious injuries or occupational diseases have been reported over the past 05 years. There were 22 minor incidents at the workplace where employees suffered injuries. The root causes were identified and corrected.

The following are some of the specific measures we have taken to improve health and safety levels:

- In-house nursing facilities are provided at Colombo Head Office & at Siyambalape. A consultant doctor visits everyday and employees can schedule consultations at no cost to the employee.
- A mobile laboratory makes visits to all our locations twice a week and the reports of medical tests are provided to the employee at no cost to the employee.
- Special protective clothing and eyewear is provided to all employees who require this. Constant efforts are made to enhance the design and the comfort levels of such protective gear.
- The Company's equipment used at the workshops are state-of-the-art and equipped with modern safety mechanisms to prevent injury to employees.

- A comprehensive firefighting drill was conducted for the employees at the Colombo and all locations during the year.

Training and Education

We are striving at all times to create a world-class workforce and this means that our staff must be exposed to continuous learning and skills development processes.

The Company invests substantially in human resource training spending Rs. 22 mn last year in this regard. For 2006/07, we provided 1,170 foreign training days.

| | Local Training | Overseas Training | Total |
|-------------------------|-------------------|----------------------|-------|
| No. of Programmes | 121 | 57 | 178 |
| No. of Participant days | 2,417 | 1,170 | 3,587 |

The Employees' Personal Development Plan is discussed each year with their line managers during the time of appraisals and the same evaluated at the end of the year.

It is a policy of the Company to reimburse job related educational expenses and subscriptions for membership to professional bodies.

Our opportunities for training are 'in-house' programmes of experiential learning, foreign seminars, workshops, and 'on the job' training. All those who receive training are expected to share 'lessons learned' with their teams and to cascade the benefits of the training to every level and to maximise the return on training investment.

The Company also conducts attitude development and motivational programmes to enhance productivity and foster commitment.

INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

Our training programme also include training on occupational health and safety. The importance of safety gear is constantly stressed. Health awareness programmes are also periodically conducted.

The 5S process supports the ISO 14000 standards and last year employee representatives were taken to the winner of the national 5S award, Unilever, to learn more of their best practices.

Equality of Opportunity

Women are recruited as automobile mechanics and service advisors, many of which have historically been perceived as male dominated professions. Culturally however, it appears that jobs in the workshops attract more males than females.

In the case of training too women are encouraged to enrol and there has been a significant increase in the number of female supervisors and the number of women at the middle and higher levels of management.

Welfare

Employees enjoy a wide range of welfare benefits under the Company's staff welfare scheme. Some of these include:

- Meals at subsidised rates.
- Free school books to employee children.
- An annual Kiddies Christmas Party which bring all the families together.
- A special programme for school children to enable them to develop a vision for themselves.

- Uniforms and footwear for drivers and workshop staff.
- An annual excursion allowance for every employee.
- Special awards to recognise the educational achievements of employees' children.
- Free transport four times a day between Siyambalape and Colombo.
- A Mercedes-Benz for employee weddings.
- Medical expenses as outlined earlier.
- A death donation fund where Company and employee contribute in equal measure. On the death of an employee or an immediate family member the fund releases Rs. 45,000/- in the case of an employee and Rs. 40,000/- in case of a family member.

Human Rights

The Company treats every employee with equal concern and respect and respects the inherent dignity of all employees. In addition, we endeavour at all times to ensure that our suppliers, dealers and other business partners also respect human rights in their business practices.

As noted above the Company adheres to a policy of non-discrimination and facilitates equality of opportunity for all its employees. Dimo's commitment to its employees is reflected in the high degree of loyalty generated. As the graph below shows 44.3% of our employees have been in service for over five years and 28.2% for over 10 years.

There have been no cases of discrimination brought against the Company.

Dimo's annual strategy presentation for all staff members to unveil the Company's annual strategic direction



INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

Service Analysis at at 31st March 2007

| Service Group | Non-Executive | | | Executive | | | Total |
|---------------|---------------|--------|-------|-----------|--------|-------|-------|
| | Male | Female | Total | Male | Female | Total | |
| Above 31 | 2 | 1 | 3 | 7 | – | 7 | 10 |
| 26 - 30 | 14 | 1 | 15 | 22 | 4 | 26 | 41 |
| 21 - 25 | 11 | – | 11 | 12 | 4 | 16 | 27 |
| 16 - 20 | 14 | – | 14 | 33 | 4 | 37 | 51 |
| 11 - 15 | 55 | 1 | 56 | 51 | 7 | 58 | 114 |
| 05 - 10 | 62 | 2 | 64 | 67 | 8 | 75 | 139 |
| Below 4 | 295 | 21 | 316 | 145 | 19 | 164 | 480 |
| Total | 453 | 26 | 479 | 337 | 46 | 383 | 862 |

The Company has had no cases of unfair dismissal being brought against it during the past year. No cases were recorded in the recent past either.

Child Labour

Our belief is that children below the age of 18 should be in school and not at work. Every child has an inherent right to education and the Company will uphold that right at all times. We apply this same standard to all our business partners and to those others to whom we outsource services.

Freedom of Religion

All employees can practise their religion and the Company makes every attempt to be flexible enough to allow all religious communities to freely practise their religion.

Empowering Communities

While we invest in the people who work for the organisation we also invest in the people who form part of the larger community. Society is one of our key stakeholders and sustainability policy is geared to adding durable value to the lives of all people.

We seek through our activities to empower communities and people and to decrease their independence on handouts and charity.

Our sustainability policy in this area is aimed at generating sustainable, durable and independent solutions which ensure that capacities are built within communities to generate their own responses and to seek long solutions to their problems.

The following are some of activities based on this philosophy:

- Dimo Automobile Training School (DATS).

Begun in 1990, the Dimo Automobile Training School (DATS) provides state-of-the-art training to 32 students at each selection cycle without any charge or obligation on their part save to apply due diligence to their training.

The first stage in the selection process is the placement of an advertisement in leading newspapers. Shortlisted candidates are then called for an aptitude test followed by a mathematical & English test.

Students hard at work at the Dimo Automobile Training School



INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

During training the trainees receive a monthly allowance, subsidised meals, uniforms and footwear at the Company's cost. They are also entitled to Company medical facilities and insurance cover.

The two-year course exposes them to Mercedes, TATA, Bosch and Japanese vehicle maintenance and electrical technology, and leads to a competitive examination. On the completion of their two-year course DATS trainees are offered positions at Dimo, depending on the vacancies available. However, they are under no obligation to accept such employment. The DATS programme also offers trainees the opportunity of spending time in with our principals in Germany and being exposed to first-hand learning experiences in a state-of-the-art environment. The Dimo certificate is recognised by Sri Lankan engineering companies.

- Dimo regularly sponsors career days and participates in Industry Day and similar programmes conducted by the National Universities.
- Close links are maintained with professional institutions to source candidates as well as to improve their professional knowledge.

Training is provided to National Apprenticeship Board (NAB) apprentices as well as 'in-plant training' to students from other institutions such as the Universities of Moratuwa, Peradeniya and Ruhuna, the Technical Colleges of Kegalle and Kandy and other institutions such as NAITA, NCIT, NDT, AETI, VIT, TTI, CETRAC etc. They are trained in automobile technology, telecommunications and power systems. Over 200 of these apprentices have been absorbed into the Company since 2000.

Specific Community Interventions

Beyond these the Company has also made specific interventions to uplift community life over the past year:

- The Company donated two diesel engines and one petrol engine to the Faculty of Engineering in the University of Ruhuna.
- Donated 1,000 caps and t-shirts *which contained an anti-drug slogan* in aid of the Anti Narcotics week conducted by the Police Narcotics Bureau in June 2006.
- Refurbished the Montessori at Siyambalape.
- Installed a state-of-the-art bus stop at our Kurunegala Branch with a water filter.
- Donated a Dimo Batta to an Institution 'Guna Jaya Sathuta Padanama' at Seenigama.
- Trained two tsunami affected boys from the 'Guna Jaya Sathuta Padanama' on power tool handling and repairs and donated equipment to them to commence a business on their own.

Legal Compliance

All relevant licenses are obtained on time and renewals done as and when required.

Bribery & Corruption

The Dimo policies do not tolerate ethically unsound or corrupt practices either on the part of our employees or business partners. Our business practices prohibit any form of bribery.

1. Refurbished Montessori at Siyambalape
2. Bus Stop at Kurunegala Branch
3. Presenting the Dimo Batta to the Seenigama village



INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

Political Contributions

Dimo is not affiliated to any political organisation. Our actions are not influenced by political considerations and our goal is to deliver sustainable value to society in the long term.

Health & Safety of the Society

The health & safety of society is paramount consideration as is the health & safety of our customers. The Company is conscious of the impact that its products may have on the health & safety of customers and society in general. Our health & safety processes at the workplace are ISO 14000 certified and therefore in compliance with international standards.

Dimo conducts regular product oriented training seminars and workshops for customers, particularly for the users of heavy machinery and construction equipment. These programmes focus on the correct use of the equipment

Dimo also provides specialised user training and service training in respect of the sophisticated medical equipment, marine engines and the other high-tech products over and above mandatory requirements.

Products & Services

Dimo has enjoyed a sustained relationship with its Principals, most of whom are ISO 14001 certified world leaders in their fields producing some of the most respected products.

Many of the products we market conform to internationally acceptable standards and the following are some specific examples of how we seek to ensure sustainable environments:

- All Mercedes-Benz, Jeep, and Chrysler vehicles conform to Euro IV standards.
- All Tata vehicles are fitted with 'Cummins' engines known for their low operating 'cost on' both with regard to fuel and oil.
- Osram lighting appliances have an energy efficiency rating of over 80%. This helps to reduce energy consumption by as much as 80% and cuts CO₂ emissions by half. All Osram lamps can be recycled.
- Siteco lighting solutions make maximum use of natural light and minimise light pollution.

INVESTING IN **PEOPLE**, THEIR HABITAT, THEIR FUTURE & POTENTIAL

- After years of use a customer can return a Mercedes-Benz to the factory for environmentally friendly disposal in accordance with the 'end of life' vehicle law. All Mercedes-Benz vehicles meet the statutory regulations governing the suitability of the vehicle's design for reuse and recycling.
- Komatsu forklifts refurbishment scheme fits electric and LPG engines to their reconditioned machines, eliminating internal combustion.
- The Michelin 'Green' tyres', which are ISO 14001 certified, uses silica instead of carbon black.
- The Bosch power tools recycling system enables dealers to pay for and take back old batteries for recycling. Plastics are also recycled. The packaging is fully recyclable cardboard.
- Dima was the first Company to introduce non asbestos clutch plates in Sri Lanka.
- Siemens medical equipment: have radiation levels on an average is less than our competitors.
- The KSB pumps which we market have energy conservation features.
- The Mahindra & Mahindra tractors are among the most economic in their category.
- York refrigerators use environmentally friendly refrigerants and are CFC free.
- MTU engines conform to Euro II and III standards.
- Komatsu heavy machinery conforms to Euro II standards.
- Siemens power generation solutions offer renewable power solutions such as Wind Mills and Biomass generation.
- Siemens Building Management Systems has the ability to reduce power consumption of high rise buildings and industrial applications by between 10% - 15%.

The indicators relating to this sustainability report which have been selected by the Company based on the GRI Index have been placed on pages 120 to 121.

This Assurance Report provided by KPMG Ford, Rhodes, Thornton & Company is on page 58.

The Company has engaged the services of KPMG Ford, Rhodes, Thornton & Company (KPMG) as an independent assurance provider to validate our sustainability report.

ASSURANCE REPORT



KPMG Ford, Rhodes, Thornton & Co.
(Chartered Accountants)
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To the Readers of the Sustainability Report 2007

Introduction

We have been engaged by Diesel and Motor Engineering Company Limited, now known as Diesel and Motor Engineering PLC ('DIMO') to review the Sustainability Report 2007 (further referred to as 'The Report'). The Report, including the identification of material issues, is the responsibility of DIMO's management. Our responsibility is to issue an assurance report on The Report.

Context and scope

In The Report, DIMO describes its efforts and progress in relation to Sustainability. Our engagement was designed to provide the readers of The Report with:

Reasonable assurance on whether:

- the data on financial performance, as specified on pages 46 and 47 of The Report are properly derived from Financial Statements of DIMO for the year ended 31 March 2007;

Limited assurance on whether:

- the data on Indicators for 2007 specified on pages 120 and 121 are fairly stated;
- the other information in The Report is fairly stated.

'Fairly stated' means that the reported information properly reflects the information contained in the underlying sources such that it is consistent with the source information. Reasonable assurance is a higher level of assurance than limited assurance, which is reflected in the nature and depth of the work performed.

Standards and Criteria

We conducted our engagement in accordance with the Sri Lanka Auditing Practice Statement (SLAPS 3), applicable to review engagements, and the International Standard on Assurance Engagements (ISAE 3000):

Assurance Engagements other than Audits

or Reviews of Historical Financial Information, issued by the International Auditing and Assurance Standards Board. Amongst others, these standards require that:

- the assurance team members possess the specific knowledge, skills and professional competencies needed to understand and review the information in The Report;
- when providing limited assurance, which is a lower level than reasonable assurance, a negative form of conclusion is used.

There are no generally accepted standards for reporting sustainability performance. DIMO applies its own internal sustainability reporting criteria, derived from Sustainability Reporting Guidelines of the Global Reporting Initiative and its stakeholder engagement process as detailed on page 41 of The Report.

Considerations and Limitations

Environmental and social performance data are subject to inherent limitations given their nature and the methods used for determining, calculating and estimating such data. To obtain a thorough understanding of the financial results and financial position of DIMO, the reader should consult DIMO's audited financial statements for the year ended 31st March 2007, included in the Annual Report from page 84 to 106.

Work undertaken and Conclusions

We reviewed the reliability of the data on Indicators for 2007 based on reviews of:

- the systems used to generate, aggregate and report these data;
- the data reported by the relevant business units to corporate level;
- the data validation processes at corporate and business level; and
- the data trends in discussions with management.

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Based on the above, the data for Indicators for 2007, specified on pages 120 and 121 do not appear to be unreliable.

Financial Data

We have reconciled the data on financial performance reported on pages 46 and 47 of The Report with the audited Financial Statements of DIMO for the year ended 31st March 2007.

Based on the above, we conclude that the data on financial performance reported on pages 46 and 47 are properly derived from the Financial Statements of DIMO for the year ended 31st March 2007 for which the independent auditors issued an unqualified audit opinion dated 21st May 2007 on page 83 of the Annual Report:

Other Information

We reviewed the other information in The Report, based on:

- an analysis of the systems and processes used to generate this information;
- review of internal documentation and sources;
- interviews with staff for the information; and
- our knowledge and understanding of the sector and DIMO's business.

Based on the above, the other information in The Report does not appear to be unfairly stated.

Ford Rhodes Thornton & Co.
KPMG FORD, RHODES, THORNTON & CO.
Chartered Accountants
Colombo
21st May 2007

R.N. Asirwatham FCA
S. Sirikananathan FCA
Ms. M.P. Perera FCA
C.P. Jayatilake FCA
W.W.J.C. Perera FCA

A.N. Fernando FCA
M.R. Mihular FCA
P.Y.S. Perera FCA
T.J.S. Rajakarier FCA
Ms. S. Joseph ACA



DET NORSKE VERITAS AS
CoreRatings

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London SE1 9DE
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Corporate Governance Rating

Diesel & Motor Engineering PLC



CG = Corporate Governance

Rating scale:
10 (highest) - 1 (lowest)

Rating Summary

Governance Policy and Business Ethics



Risk Management



Board and Management Organisation



Board and Executive Composition



Ownership Structure and Control



Investor Rights and Relations



Financial Disclosure and Audit



0 5 10

May 2007

Rating Summary

The rating of Diesel & Motor Engineering PLC (Dimo or 'the Company') reflects the thinking of the Sri Lankan markets as they strive to implement formal governance requirements for companies. As such, the methodology takes into account both international best practice and the direction of Sri Lankan governance regulations. This is evidenced by the consultation that occurred between The Institute of Chartered Accountants of Sri Lanka (ICASL) and the Securities and Exchange Commission in consultation with the Colombo Stock Exchange (CSE). This spearheaded the joint initiative to formulate standards on corporate governance for mandatory compliance by companies listed on the Colombo Stock Exchange. These standards have been incorporated into the listing Rules of the Colombo Stock Exchange.

Dimo has earned an overall rating of 6, which reflects its proactive approach to implementing sound corporate governance practices within the Company. There is a well balanced board with a good mix of internal professionals, non-executive and independent Directors to drive the Company forward and efficient management processes to ensure internal control.

Dimo has two significant shareholders, the Pandithage family which own approximately 27% of the Company and the Hayleys Group who have a similar shareholding. In Dimo's case, the two major shareholders have provided stability, strength and depth to



the Board as well as enhancing both business and governance processes. The Company Chairman/Managing Director/Chief Executive Officer (Chairman/MD/CEO), Mr. A.R. Pandithage has successfully managed the complex issues associated with the aspirations of the founding family members and those related to ensuring the long-term commercial viability of what was essentially a family owned and run business through the introduction of external professional management. In our opinion, the present ownership structure has had a positive benefit to the Company's minority shareholders.

Dimo has a sound understanding of good governance practice, is committed to open an ethical business, and is striving to improve its governance practices to further embed these into the organisation. The Chairman/MD/CEO has been pragmatic in his approach to raising governance at Board level to ensure that all parties can be successfully accommodated.

The Company needs to develop a transparent ethical policy and code of conduct that is accompanied by descriptions of how policies are communicated and what compliance monitoring instruments are in place. Equally, strong risk management policies and systems need to be put in place and embedded throughout the Company's operations.

In the rating we looked carefully at those areas where a dominant shareholder can exert undue influence. The combined role of Company Chairman and Managing Director does raise concerns in this regard. While the Company had sound reasons at the time to pursue this structure, it needed to provide a transparent justification for doing so including the provision of some time frame by which it would return to a more usual management structure. However, no evidence could be found to suggest that the Company is acting against the interests of the public minority shareholders in this matter. The overall assessment of the Board of Directors is high but additional formal, written policies, procedure would increase clarity allowing for even greater confidence in the way the Board operates.

The Company's minority shareholders are generally well catered for. The Articles of Association define basic shareholder rights and timely and sufficient information in order to attend and actively participate in the AGM is provided. The Audit Committee responsibly carries out its role of ensuring that the interests of shareholders are properly protected in relation to financial reporting and internal control. Overall financial disclosure is considered sound and governance disclosure is generally good.

Det Norske Veritas

21st May 2007

ENTERPRISE GOVERNANCE

The Concept of Enterprise Governance covers the entire accountability framework of a business ensuring that responsibilities are clearly defined and processes are outlined and implemented. The two aspects of enterprise governance: business performance and conformance are discussed in this review. These areas cover the processes and systems that the Board has in place to ensure that the Company's resources are used efficiently and prudently to achieve the Company's business objectives. It also covers the Company's governance structure and processes that have been established to ensure accountability, responsibility and transparency in our business operations.

Business Governance

Strategic Planning Process

The Board's main responsibility in this regard is the formulation of the strategic vision and mission of the Company. In addition, the Board is responsible for the overall corporate policy and strategy, monitoring performances, reviewing risks and giving approval for major investment decisions.

While the Board sets the broad parameters for the business as a whole, these parameters are translated into specific objectives by the business units. Each business unit is required to set their specific objectives in line with the parameters set down by the Board.

Business units present their annual budgets and forecast for the future along with the non-financial information such as market conditions, competition, challenges and opportunities to the Board. The Board evaluates and provides the necessary

guidance/feedback where necessary. Once the necessary amendments have been incorporated, formal approval is given by the Board. In addition to each business unit's strategic objectives, key performance indicators are also agreed at the commencement.

Implementation Process

Implementation of the Company's business strategy is done through the Board appointed Group Management Committee (GMC). The GMC exercises direct supervision over every Business Unit including support services. This supervisory role is exercised in accordance with guidelines laid down by the Board. A management team consisting of the GMC, heads of the business units and the heads of the corporate service units meet every month to discuss and review operational issues.

Business Unit managers convey their views to the respective GMC member. These views in turn are discussed at the GMC meetings.

While the business units have substantial autonomy in their day-to-day operations, each business unit is overlooked by a member of the GMC. The business units are responsible for achieving their individual targets.

The Board is provided with regular information, which enables them to evaluate performance in comparison to the overall business objectives. This includes information on key performance indicators, budgets, financial statements, customers, market developments, employees and principals.

ENTERPRISE GOVERNANCE

Operational results of each business unit are reviewed quarterly by the Board of Directors and projected results are compared with budgets and key performance indicators.

Individual objectives of employees' are set out in line with the business unit's overall objective and are reviewed on a biannual basis. The performance of individual executives is evaluated based on their level of achievement which in turn, is linked to their remuneration package and promotions.

Corporate Governance

Governance Policy

The Company is committed to a policy of transparent, accountable and responsible governance. The Board's objective is to deliver superior returns to all stakeholders and it is done in accordance with the highest standards of corporate and business ethics. In this regard, we have established clear lines of responsibility and accountability within the entire Group.

The Company conforms to the standards contained in the Code of Best Practices issued by the Institute of Chartered Accountants of Sri Lanka, listing rules of the Colombo Stock Exchange and best practices of Corporate Governance.

Business Ethics

The Group's business principles and values apply to all employees and set out the fundamental standards to be followed by all in their day-to-day actions.

All employees are expected to comply with the following principles:

- Engage in honest and ethical conduct.
- Avoid conflicts of interest.
- Preserving confidentiality of information.

- Take such measures as appropriate to ensure that the Group complies with all applicable laws, rules and regulations and provide complete, accurate and timely disclosure in reports that the Company files or submits to any stakeholder.
- Ensure that business affairs are conducted in a transparent manner.
- Report promptly to the GMC on any violation of business principles and values.

The Company is in the process of documenting a Code of Conduct for employees.

Chairman & Chief Executive Officer

The functions of the Chairman and Chief Executive Officer (CEO) are vested in the same person. The Company believes that the dual role played by the Chairman and CEO does not compromise on the principles of good corporate governance. This is further ensured by the significant presence of non-executive and independent Directors on the Board. These Directors provide a mechanism for critically reviewing all aspects of the Company's operations. They ensure that no single individual has unfettered powers of decision making and bring an independent judgment to bear on issues of strategy, performance and risk. The presence of a Lead Director adds more emphasis to transparency in governance affairs.

The Chairman ensures that good governance is practised through the entirety of the organisation; that there is a balance of power on the Board and both executive and non-executive Directors have opportunities for effective participation; that the Board

ENTERPRISE GOVERNANCE

has full knowledge of the Company's affairs and is in complete control; and facilitates effective communication with all of the Company's stakeholders.

The Chairman and CEO's performance is reviewed by the Nomination Committee and the Remuneration Committee. Each committee consists of three independent non-executive Directors including the lead Director and two non-executive Directors.

Board Responsibilities

The Board is responsible for the Company's overall strategic direction and performance of the business as a whole. It provides leadership and vision to the institution and fosters a culture of integrity, transparency and accountability across the Group. The Board monitors and evaluates risks, monitors performance, takes decisions on important investment decisions and is also responsible for sound internal financial controls.

The Board consists of a mix of seven executive Directors (which includes the Chairman), two non-executive Directors and three independent non-executive Directors. A balance of Directors ensures that the Board functions are separate from other aspects of the Company's operations such as governance and management.

A list of Directors with brief biographies appears on pages 10 and 11.

The Directors' Responsibilities for the Financial Statements are described on page 82.

Board Independence and Effectiveness

Each Director brings in a wide range of skills, knowledge and experience. The presence of non executive and independent non-executive Directors on the Board provide an added level of transparency.

Board members are free to suggest the inclusion of items on the agenda of Board Meetings and carry out their duties in the interest of the Company without any undue influence from other parties.

All Board members including non-executive Directors receive information on the operations and performance of the Company on a monthly basis. This procedure helps to eliminate information asymmetry between executive Directors and non-executive Directors. The Directors are provided with comprehensive data on financial and non-financial information prior to Board meetings. Additional information may be requested by any member of the Board as and when required. A sophisticated management information system is in place and provides relevant and current information.

Lead Director

Mr. R. Seevaratnam, who is an independent non-executive Director, functions as the Lead Director to whom concerns relating to governance of the Company can be conveyed if and when the need arises. The Lead Director presides at Board Meetings in the absence of the Chairman. The Board continues to reassess the role of the Lead Director on a regular basis.

Appointment of Members and Re-election

The Nomination Committee recommends suitable candidates to the Board after evaluating the necessary experience and expertise against required needs.

The non-executive Directors are nominated for selection based on their expertise in their respective field.

ENTERPRISE GOVERNANCE

Three independent non-executive Directors were appointed to the Board during the year. All three Directors are well experienced professionals in their relevant fields and will bring to the Board a wealth of expertise:

- Dr. H. Cabral
(w.e.f. 1st October 2006)
- Dr. U.P. Liyanage
(w.e.f. 1st October 2006)
- Mr. R. Seevaratnam
(w.e.f. 1st January 2007)

Independent non-executive Director, Mr. H.M.A. Jayasinghe, resigned from the Board with effect from 1st January 2007.

The Company's Articles of Association requires any Director appointed by the Board to hold office till the next Annual General Meeting, at which he or she could be reappointed by the shareholders.

New appointments are made known to the public through the Colombo Stock Exchange and the media.

In terms of the Articles of Association, one-third of the Directors retire by rotation and offer themselves for re-appointment at the Annual General Meeting.

Shareholders have the opportunity to elect and remove the members of the Board in accordance with Company's Articles and the Companies Act.

Board's understanding of the Company's Business

Following the appointment to the Board, the Directors are given an opportunity to get an in-depth understanding of the Company's business, its strategy, risks and processes, at their discretion.

Training is provided to the executive Directors to equip them to discharge their responsibilities effectively. This includes training provided by principals, external and in-house training.

The expenses of individual Directors in obtaining independent professional advice are borne by the Company subject to the Board approval.

Evaluation of Board Performances

The performances of all executive Directors are evaluated by the Nomination Committee and the Remuneration Committee. Achievement of budgeted results and key performance indicators are important measuring tools in performance evaluation.

The effectiveness of the individual independent Directors are reviewed and assessed by the Board on a regular basis.

Meetings and Attendance

Every member dedicates sufficient time for the Board's affairs by attending Board meetings, Committee meetings, performance and strategy review meetings. In addition, the Board Members communicate with each other through circulars, e-mails, telephone conversations and letters.

The number of meetings held and their attendance is given in the table appearing on page 66.

The Company Secretary

The Company Secretary assists the Chairman in all aspects pertaining to the functions of the Board of Directors. He helps in arranging Board meetings and in making available all the necessary information to the Board for their deliberations.

ENTERPRISE GOVERNANCE

Members of the Board have unrestricted access to the advice and services of the Company Secretary. The appointment and removal of the Company Secretary rests with the Board.

The Board's Committees

The Board has several committees to assist in discharge of its responsibilities more effectively.

Audit Committee

The Audit Committee is a sub-committee of the Board and its main purpose is to assist the Board in the effective discharge of its responsibilities on financial reporting and corporate control. It assists the Board in monitoring compliance with applicable laws and other regulatory requirements. The Committee is responsible for reviewing the financial reporting system and Financial Statements including compliance with relevant accounting standards and Company policies.

The Audit Committee determines the appointments, evaluations, terms of engagement and fees of the auditors. Committee also ensures that the objectivity and independence of the auditors are not impaired in any way as a result of the additional professional services performed by them.

The Board of Directors appoints members to the Audit Committee. It consists of three independent non-executive Directors and two non-executive Directors. The Chairman is Mr. R. Seevaratnam, an experienced Chartered Accountant.

Mr. H.M.A. Jayasinghe, who served as Chairman of the Audit Committee retired from the Board and will continue as an independent Consultant to the Committee.

Any member of the Board including the Chairman, Chief Executive Officer and Deputy Chief Executive Officer may attend the meetings by invitation.

The Committee has a terms of reference which clearly sets out its responsibilities and authority.

The report of the Audit Committee is available on pages 72 to 73.

Committee meetings and the attendance of members is given in the table appearing on page 66.

The Remuneration Committee

The Remuneration Committee is responsible for determining a framework and policy on the remuneration of the Chairman, Chief Executive Officer, executive Directors and members of the senior management.

The Company aims to attract and retain high calibre executives by ensuring that their rewards are competitive and linked to both individual and business performance. Whilst recognising the market demands and the contribution of the executives to the overall performance, the Company believes that the remuneration policy should at the same time be aligned with shareholder interests.

The Board of Directors appoints members to the Remuneration Committee.

ENTERPRISE GOVERNANCE

The Committee consists of three independent non-executive Directors and two non-executive Directors. The Chairman is Dr. U.P. Liyanage, an independent non-executive Director. The Committee is entitled to obtain professional advice at the Company's expense.

Total Directors' emoluments are disclosed in Note 41 on page 94.

Committee meetings and the attendance of members is contained in the table.

The report of the Remuneration Committee is available on page 74.

Nomination Committee

The Committee's main role is to nominate suitable candidates as and when vacancies occur on the Board. The Committee is involved in succession planning and in ensuring smooth management transitions. It reviews the size and structure of the Board on a continuing basis and constantly reviews the balance of skills, knowledge and experience of the Directors. The Committee is also engaged in a review of the independence of Directors including actual, potential or perceived conflicts of interest.

The Committee consists of three independent non-executive Directors and two non-executive Directors. Its chair is Dr. H. Cabral, an independent Director.

The Committee is entitled to obtain professional advice at the Company's expense.

The Committee has specific terms of references defining its scope and authority.

The report of the Nomination Committee is available on page 75.

Board and Committee Meetings and the attendance of members

| Name | Board | Audit Committee | Nominations Committee | Remuneration Committee |
|------------------------|-------|-----------------|-----------------------|------------------------|
| A.R. Pandithage | 7/7 | – | – | – |
| R. Seevaratnam ** 1 | 1/1 | 1/1 | 1/1 | 1/1 |
| Dr. H. Cabral ** 2 | 2/3 | 1/2 | 1/1 | 1/1 |
| Dr. U.P. Liyanage ** 2 | 3/3 | 2/2 | 1/1 | 1/1 |
| A.N. Algama | 7/7 | – | – | – |
| A.M. Pandithage * | 7/7 | 5/5 | 1/1 | 1/1 |
| A.G. Pandithage | 6/7 | – | – | – |
| B.C.S.A.P. Gooneratne | 7/7 | – | – | – |
| H.M.A. Jayasinghe ** 3 | 5/6 | 4/4 | – | – |
| R.A. Ebell * | 5/7 | 4/5 | 1/1 | 1/1 |
| R.C. Weerawardane | 7/7 | – | – | – |
| S.C. Algama | 7/7 | – | – | – |
| T.G.H. Peries | 7/7 | – | – | – |

* Non-Executive Director

** Independent Non-Executive Director

1 Appointed w.e.f. 1st January 2007

2 Appointed w.e.f. 1st October 2006

3 Resigned w.e.f. 1st January 2007

Risk Management

Developing and implementing a sound and transparent risk management strategy is a key responsibility of the Audit Committee.

A more comprehensive review of the risk management strategy is provided on pages 68 to 71.

Internal Controls

The main responsibility lies with the Board for establishing an effective system of internal controls. A sound system of internal control helps establish better levels of operational efficiency, provides more reliable financial data, and enables early detection of non-compliance with laws and regulations. Outsourcing of the internal audit function has enhanced its independence aspect. The internal audit plan is agreed with the internal auditors at the beginning of each financial year by the Audit Committee. However, the internal auditors have the freedom to carry out any additional tasks they feel necessary.

ENTERPRISE GOVERNANCE

Financial Reporting

All the financial statements of the Company are prepared in accordance with Sri Lanka Accounting Standards. The Board makes every endeavour to present a balanced and objective assessment of the Company's position, performance and prospects. These are discussed in detail in the following reports:

- Directors' Report - pages 78 to 81.
- Chairman's & CEO's Review - pages 2 to 9.
- Financial Review - pages 34 to 39.
- Business Performance Review - pages 14 to 33.

The Board has the necessary expertise in financial reporting and also has the services of four qualified accountants.

Investor Rights and Relations

The Company communicates regularly with its shareholders updating them on the Company's position, performance and prospects. The Annual Report provides the most comprehensive review of the Company's performance and prospects. This is supplemented by quarterly reports and other circulars, when necessary.

The Annual General Meeting provides a forum for shareholders to raise any queries. The Chairmen of the Audit, Remuneration and Nomination Committees are present at the Annual General Meeting. All Directors were present at the last AGM of the Company.

Every shareholder is entitled to one vote per share.

The transactions of the Directors and their immediate family members are disclosed in Note 27 to the financial statements. The Directors' shareholdings are contained on page 110.

Employees

The monthly Employees Council meetings provide a forum for employees to communicate with the management on a regular basis. The Company's 'Open Door' policy encourages employees to raise any matter of concern with any member of the management including the Chairman.

This process is detailed in the Sustainability Report appearing from pages 40 to 57.

Corporate Social Responsibility

The Board is involved in ensuring that the Company's growth is aligned with its contribution to the economy, environment and the society. More details on this is available in the Sustainability Report.

RISK MANAGEMENT

Risk management is an integral part of the Company's business strategy. Risk identification and a systematic process to manage them is vital if growth and profitability are to be sustained. In this section we look at the different tools and practices that the Company uses to identify and manage the many different types of risks it faces.

The Company's risk management strategy ensures that the Company takes well calculated risks while protecting the integrity and well-being of the Company.

Once the risks are identified and prioritised the most appropriate counter strategy to manage, minimise or eliminate these risks will be implemented. The Board of Directors and the Audit Committee continuously review the implementation of the selected risk managing strategy and if necessary, take steps to modify or change it.

Risk Management Process

The identification, development, implementation and review of a effective risk management strategy are some of the key objectives of the Audit Committee. The identification of risks calls for a sound enterprise-wise reporting system. An early warning system to track emerging risks is built into this reporting structure.

The Group Management Committee (GMC) which consists of executive Directors and senior managers of the Company is responsible for directing business units on risk management. The heads of business units convey their views on aspects of risks and their management to the respective GMC member which in turn, will be discussed at the GMC meetings.

An effective system of Internal Controls is in place to minimise the risk of irregularities and fraud taking place within the Company. However, a sound internal control system can only provide a reasonable assurance that it will bring to light within a reasonable time any irregularity or non-compliance.

A firm of Chartered Accountants which acts in the capacity of Internal Auditors of the Company, communicates their findings to the Audit Committee by way of periodic reports and presentations to the Audit Committee every quarter.

The finance function assists GMC in identifying operational risks. The findings of finance department are communicated to GMC for their consideration.

The monthly management reports, special investigation reports, internal audit reports and structured information sent to the Audit Committee are some of the key tools used in risk identification.

The Monthly Operational Results

The monthly operational results which are a key reporting tool is used as a risk review mechanism by identifying significant deviations from original objectives. This in turn, enables the management to take corrective steps at an early stage.

Internal Audit Reports

Internal audit reports may include any non-compliance with policy, laws or processes. Non-compliance with laws and regulations have financial and non-financial implications. They also recommend improvements to the existing systems and procedures to strengthen the internal controls within the organisation. In order to ensure previously reported irregularities are not repeated; follow up actions are also regularly monitored.

Risk Exposure

Like any other corporate enterprise the Company is exposed to a broad array of risks. Some of critical risks that the Company is facing are discussed and analysed below.

Economic Risk

Economic risks are those changes in the economic environment that have the potential to affect the Company adversely. Recently, the Company had to respond to a

RISK MANAGEMENT

number of shifts in the local economic environment, many of which had an impact on the Company's business.

Steadily depreciating rupee and rising interest rates were some of the issues the Company had to manage. Rising interest rates was the factor that had the most impact on the Company's activities since the majority of the Company's vehicles were purchased through financing arrangements. On the other hand it diminished the Company's profit through an increase in finance cost.

Effective management of working capital is seen as the key measure against rising interest rates.

Industry Risk

Industry risks arise from sudden changes within each industry. These could be driven by new customer trends such as the demand for fuel efficient and environmentally friendly cars or it could result from the entry of new/alternative products into the market. With a view to minimising these risks, the Company closely monitors development in the international market and also competitor strategies and promptly develops counter strategies that may be necessary. An effort is made to strongly position the Dima brand and explore every available opportunity for the introduction of new and innovative products. The Company represents global leaders and is in a position of advantage due to constant technology innovations by them.

Market/Portfolio Risk

The Vehicles and Vehicle Parts/ Service segments that forms the Group's core business, accounts for 84% of its turnover. Although we have taken steps to diversify our product portfolio in recent years we are still heavily dependant on the automobile industry and a downward trend in this sector will again have negative implications.

The Groups' strategy is firmly directed towards reducing the imbalance in the product portfolio. The Group is developing its competencies in the areas of marketing and distribution and in providing engineering solutions to commerce and industry.

Compliance with Laws & Regulations

Laws, regulations and accepted principles have a considerable impact on any business. Regular review of compliance is done by the Management, Audit Committee and Internal Auditors. The Group Management Committee is placed with the responsibility of identifying any changes to legislations and educating relevant personnel promptly.

Operational Risk

Operational risks arise in a variety of ways related to the day-to-day functioning of the Company.

Relationships with Principals

Our relationships with principals are one of the mainstays of our business and a disruption of this can have negative consequences.

The Company has focused on developing a mutually beneficial relationship with principals in an effort to minimise the risk. Targets are met and the after care conforms to the rigorous standards set down by the principals. We are constantly looking for new opportunities to develop relationships with new principals and to reduce our dependence on any single sector or principal.

Foreign Exchange Rates

Foreign currency exposure arising out of trading activities are hedged through forward contracts, when appropriate. An impact on profits arises when translating foreign currency assets and liabilities into local currency at the Balance Sheet date. A hedging of this impact is available to the extent that trade receivables and foreign currency bank account balances cover the exposure on foreign currency payables.

RISK MANAGEMENT

Loss of Data

The Company operates in a fully computerised environment and the loss of important data arising from technological failure is another risk we have to guard against. The Company makes daily back-ups to guard against the risk of losing vital data. Regular maintenance of our equipment ensures that the risk of system failure is minimised. Off-site storage of data back-ups is another measure taken to minimise risks.

Technological Obsolescence

The non-availability of state-of-the-art technology can have an impact on performance. The Company makes regular investments in cutting edge technology. Staff are constantly exposed to new technologies and trained for the better application of existing technologies.

Information Security

Employees are made aware of the importance of the security of information and maintaining confidentiality. Some information is accessible only to selected employees so as to ensure that leakage of vital information does not affect the Company adversely. The ethical values that we propagate also stress the need to maintain confidentiality.

Credit Risk

Strict control measures are in place to mitigate the Credit Risk. Credit facilities are extended to customers in accordance with Group Credit Policy. Customers are evaluated prior to extending credit facilities to them. Processes employed for credit extension include approvals prior to granting credit facilities, periodic review of receivables by senior management, credit suspension on overdue accounts and legal procedures for recovery of long overdue receivables.

Liquidity

Unavailability of sufficient funds may disturb the smooth functioning of Company's day-to-day operations. The Group seeks to ensure that banking facilities are in place to cover its forecasted cash needs for a period of at least

twelve months. Cash requirements of the Group are regularly and closely monitored and matched with banking facilities available; to ensure that requisite funds are available for operations and investment. The unutilised overdraft/ short-term loan facilities at 31st March 2007 were Rs. 1,693 mn (Rs. 294 mn in 2005/06).

Frauds & Errors

The management has put in place a system of internal controls, to minimise the risk of fraud and irregularities and safeguard the Group's assets. Internal controls include continuous internal audit, the findings of which are reviewed by the management as well as the Audit Committee.

Customers

The Company's Customer Relationship Management process helps it respond effectively and efficiently to customer complaints and develop relevant solutions. The Company is constantly upgrading its level of aftercare and employees are periodically trained in this regard. We promote customer loyalty through a number of innovative schemes and have developed a diverse customer base.

Human Resources

Risks stemming from the Company's human resource base have also to be managed. The Company's human resources are its most important asset and recruitment and retention of committed and capable employees are a constant challenge. A succession plan minimises the impact that the exit of employees has on the performance of the Company.

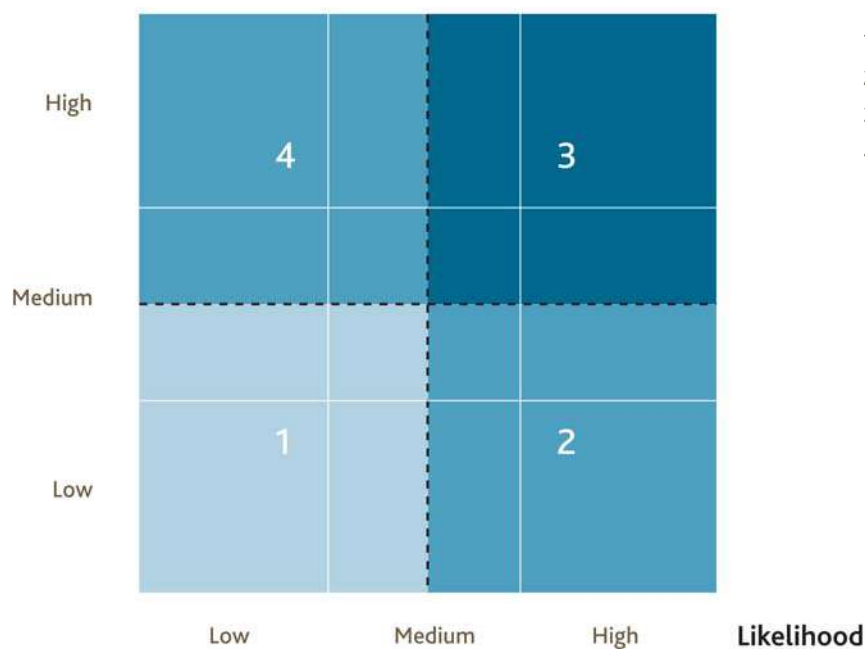
Labour Relations

The regular meetings of the Employees Council provides a forum to discuss employee concerns and help the management to then respond to them. The Company's remuneration package is in line with market rates. Regular training is provided to our employees both to motivate them and also to expose them to state-of-the-art technology. The Employee Satisfaction Index appears on page 43.

RISK MANAGEMENT

Risk Matrix

Impact



- 1 Relatively low risks
- 2 Risks that happen on a day to day basis
- 3 Risks that threaten business objectives
- 4 Significant risks that are less likely to happen

| | Likelihood | Impact |
|------------------------------------|------------|--------|
| Economic Risk | H | M |
| Industry Risk | L | H |
| Market Portfolio Risk | L | H |
| Compliance with Laws & Regulations | M | M |
| Operational Risk | | |
| Relationship with Principals | L | M |
| Foreign Exchange Rate | H | L |
| Loss of Data | M | M |
| Technological Obsolescence | L | M |
| Information Security | M | M |
| Liquidity | L | H |
| Credit | H | L |
| Fraud & Error | M | M |
| Customers | M | M |
| Human Resources | L | H |
| Labour Relations | L | M |

Risk mapping is carried out in order to assess the likelihood of occurrence and the impact on the business in the event of occurrence. It is based on the following:

- Likelihood of occurrence is measured on the basis of past experience and the preventive measures in place. A ranking of high, medium and low in terms of the probability of occurrence is assigned for each risk.
- The impact of the event is assessed by ascertaining the loss it would inflict (financially, operationally or both) and the extent of the impact. By considering these two factors the impact is categorised as low, medium & high.

AUDIT COMMITTEE REPORT

The Audit Committee is established for the purpose of assisting the Board in fulfilling their oversight responsibilities regarding the integrity of the financial statements, risk management, internal control, and compliance with legal & regulatory requirements, review of external auditor's performances & independence and internal audit function.

The Audit Committee is formally constituted as a Sub-Committee of the Main Board, to which it is accountable.

The followings are the principal activities carried out by the Audit Committee during the year ended 31st March 2007.

Financial Reporting

The Committee considered the quarterly and annual financial statements and reviewed the Annual Report including the financial statements prior to publication.

The review included:

- Any changes in accounting policies
- Compliance with Accounting Standards
- Adequacy of provisions against possible losses
- Material changes arising from the audit

Meetings of Audit Committee

Five meetings were held during the year ended 31st March 2007. The internal auditors attend meetings quarterly.

Risk Management

The Audit Committee regularly reviews the Company's risk management procedures and continuously monitors the effectiveness of risk strategy employed to mitigate the risk. The areas covered include:

- Regular review of country situations
- Setting of suitable exposure limit
- Having a contingency plan in place

Compliance with Laws & Statutory Payments

The Audit Committee was submitted reports by the management and internal auditors on the status of compliance with laws, filing of statutory returns and making of statutory payments.

Internal Control

The Committee is satisfied that an effective system of internal control is in place to provide reasonable assurance on the safeguarding of the Company's assets and reliability of financial statements produced. Effectiveness of Company's system of internal controls is evaluated through reports furnished by internal auditors, external auditors and the management.

Internal Auditors

The internal audit function is outsourced to Messrs. SJMS Associates, a firm of Chartered Accountants which represents Messrs. Deloitte Touche Tohmatsu in Sri Lanka. Internal auditors directly submitted their findings to the Audit Committee quarterly and their reports are made available to external auditors.

The Audit Committee monitors and reviews:

- The follow-up action taken on the recommendation of the internal auditors
- The internal audit programmes and results of the internal audit process
- Effectiveness of the internal audit function

AUDIT COMMITTEE REPORT

External Auditors

The Audit Committee reviews the independence and objectivity of the external auditors and conduct a formal review of effectiveness of the external audit process. The Audit Committee has met with the external auditors to review the financial statements during the annual audit.

The Committee reviewed the non-audit services and its impact on the independence of the external auditors.

The Audit Committee has approved the extension of current external auditors, by one year, and recommended to the Board the re-appointment. On the recommendation of the Audit Committee, the Directors will be proposing the re-appointment of Messrs KPMG Ford, Rhodes, Thornton & Co. at the AGM in June 2007.

Audit Committee Performance

The annual performance of the Audit Committee was evaluated by other members of the Board of Directors and was deemed satisfactory.

Conclusion

The Audit Committee is satisfied that the effectiveness of the organisational structure of the Group and the implementation of the Group's accounting policies and operational controls provide reasonable assurance that the affairs of the Group are managed in accordance with Group policies and that Group assets are properly accounted for and adequately safeguarded.



R. Seevaratnam

Chairman - Audit Committee

Colombo

21st May 2007

REMUNERATION COMMITTEE REPORT

The Remuneration Committee is a sub-committee of the Board. It was established for the purpose of recommending the remuneration of the Board of Directors including Chairman, Chief Executive Officer and senior management.

The members of the Committee, including its Chairman, are appointed by the Board.

The Committee has acted within the parameters set by its terms of reference.

The composition of the Committee changed during the year.

Mr. H.M.A. Jayasinghe who was the Chairman of the Committee resigned with effect from 1st January 2007.

The Chairman of the Board attends the Committee meetings by invitation. However, he does not participate in any discussion pertaining to his remuneration.

The remuneration packages linked to the individual performances are aligned with the Company's long-term strategy.

The Directors' emoluments are disclosed on page 94.

The Committee meets as and when a need arises. The Remuneration Committee meetings and members attendance is given on page 66.



Dr. U.P. Liyanage

Chairman - Remuneration Committee

Colombo

21st May 2007

NOMINATION COMMITTEE REPORT

The Nomination Committee is established for the purpose of advising the Board in relation to nominations, retirement, succession and training of the Board and members of senior management. It also advises the Board on issues relating to Directors' conflict of interest and independence.

The members to the Committee are appointed by the Board of Directors.

The Committee has acted within the parameters set by its terms of reference.

The composition of the Committee changed during the year.

The Committee meets as and when a need arises.

The key activities carried out during the year by the Committee is as follows:

- Review the structure, size and composition of the Board.
- Evaluate the independence and effectiveness of the Non-Executive Directors.
- Review the process of identifying and developing senior managers throughout the Group who have potential to succeed members of the Group senior management.
- Carry out evaluation of Executive Directors and their performance.

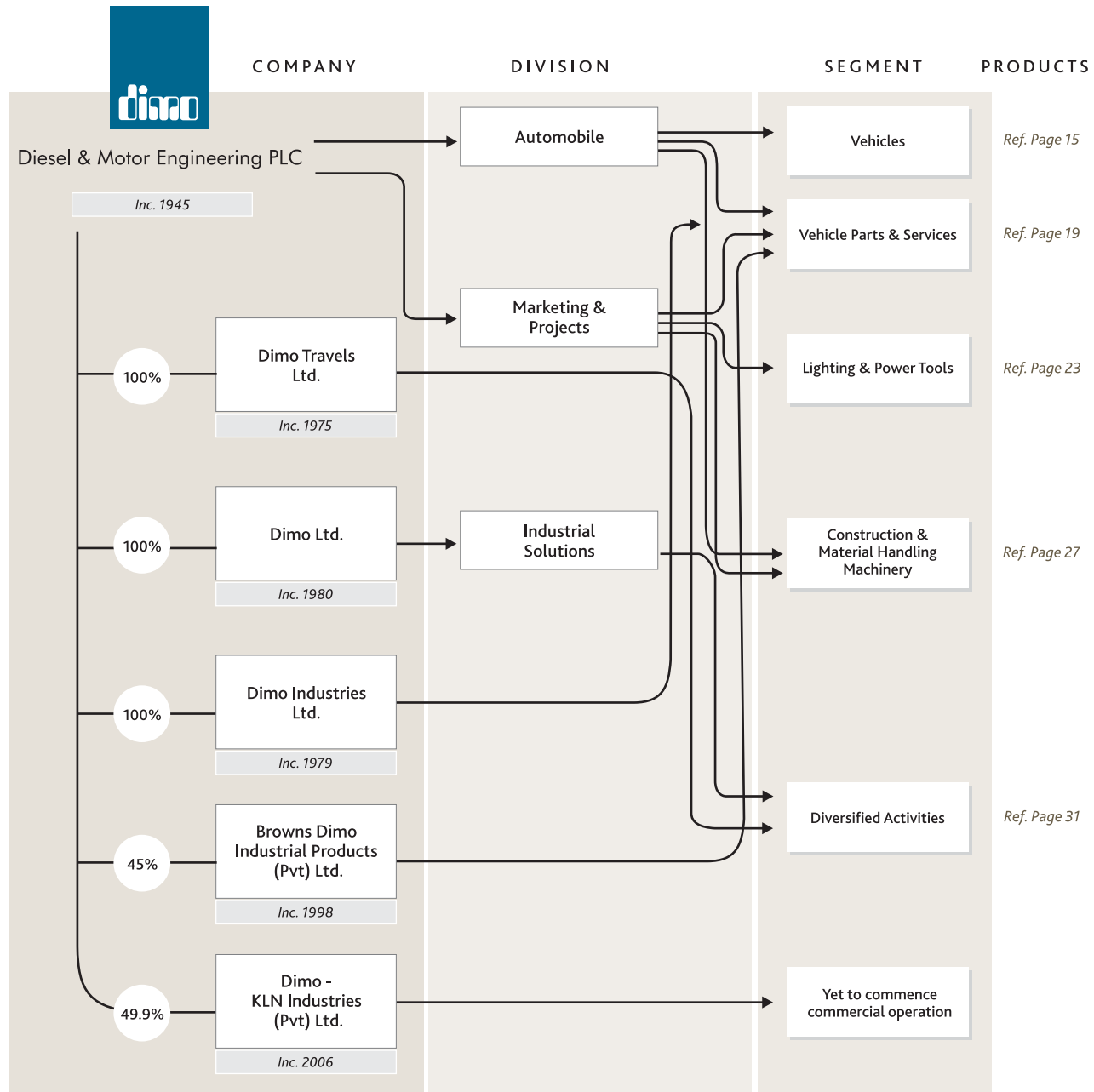


Dr. H. Cabral

Chairman - Nomination Committee

Colombo
21st May 2007

GROUP STRUCTURE



Directors:

Diesel & Motor Engineering PLC - Shown on Page 10

Dimo Travels Ltd. - A.R. Pandithage (Chairman), S.C. Algama

Dimo Ltd. - A.R. Pandithage (Chairman), A.G. Pandithage, S.C. Algama, R.H. Fernando, R.C. Weerawardane, B.C.S.A.P. Gooneratne

Dimo Industries Ltd. - A.R. Pandithage (Chairman), S.C. Algama, A.G. Pandithage, R.C. Weerawardane, B.C.S.A.P. Gooneratne, A.C.G. Dias

Browns Dimo Industrial Products (Pvt) Ltd. - M.V. Theagarajah (Chairman), A. R. Pandithage (Deputy Chairman), K.D.P. Fernando,

R.C. Weerawardane, A. Mapalagama, A. Munidasa, J.M.G. Candappa, Mrs. K.C.S. Abeyesundere

Dimo - KLN Industries (Pvt) Ltd. - A. R. Pandithage (Chairman), Gita Shetty, Nakul Shetty, Prasanna Kumar Shetty, R.C. Weerawardane, A.A.D. Perera

FINANCIAL REPORTS

- Report of the Directors 78 ■ Statement of Directors' Responsibilities 82
- Report of the Auditors 83 ■ Income Statements 84 ■ Balance Sheets 85
- Statements of Changes in Equity 86 ■ Cash Flow Statements 87
- Significant Accounting Policies 88 ■ Notes to the Financial Statements 92

FINANCIAL CALENDAR

| | |
|--|-------------------|
| Results - 1st Quarter ended 30th June 2006 | 1st August 2006 |
| Results - 2nd Quarter ended 30th September 2006 | 24th October 2006 |
| Results - 3rd Quarter ended 31st December 2006 | 9th February 2007 |
| Interim Dividend paid | 9th March 2007 |
| Annual Report - Financial Year ended 31st March 2007 | 29th May 2007 |
| 62nd Annual General Meeting | 20th June 2007 |
| Final Dividend Proposed | 20th June 2007 |
| Final Dividend Payable | 27th June 2007 |

REPORT OF THE DIRECTORS

The Directors of Diesel & Motor Engineering Co. Ltd. (now known as Diesel & Motor Engineering PLC), a public limited liability company incorporated in Sri Lanka in 1945 under the Companies Ordinance No. 51 of 1938 present their Report and the Consolidated Financial Statements for the year ended 31st March 2007, which were approved at a meeting held on 21st May 2007. The Financial Statements have been prepared in accordance with the Sri Lanka Accounting Standards as required by Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995.

GROUP ACTIVITIES

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

BUSINESS REVIEW

A review of operations, developments and outlook is available in the Chairman & CEO's Review on pages 2 to 9, Financial Review on pages 34 to 39 and Business Review on pages 14 to 33.

Segment turnover and other segment information are available on pages 92 & 93.

The Directors recommend a final dividend of Rs.3/- per share (2005/06 - Rs.3/- per share) payable on 27th June 2007 to the shareholders of the issued ordinary shares of the Company as at close of the business on 21st June 2007. This dividend together with the interim dividend of Rs. 3/- per share (2005/06 - Rs. 3/- per share) results in a total dividend of Rs. 6/- per share (2005/06 - Rs. 6/- per share).

In accordance with Section 56 of the Companies Act No. 7 of 2007, a solvency test was carried out by the Company's Auditors, prior to recommending the final dividend.

PROPERTY, PLANT & EQUIPMENT

Group expenditure on property, plant & equipment during the year amounted to Rs. 305,543,358/- (2005/06 - Rs. 120,961,287/-).

Information relating to movement in property, plant & equipment is given in Note 10 to the Financial Statements.

GROUP INVESTMENT

Information relating to investments other than in subsidiaries is available in Notes 12, 13 & 14 to the Financial Statements.

RESULTS AND DIVIDENDS

| | 2006/07 Rs.'000 | 2005/06 Rs.'000 |
|---|--------------------|--------------------|
| Turnover | | |
| The gross of the Group was | 12,989,916 | 10,512,326 |
| Profit | | |
| After making provision for bad and doubtful debts and all known liabilities and after charging a sum of Rs. 63,037,571/- (2005/06 - Rs. 65,395,028/-) for depreciation of property, plant & equipment the profit made by the Group before tax was | 512,895 | 382,235 |
| Income tax expense | (211,118) | (117,062) |
| Group profit after taxation | 301,777 | 265,173 |
| Appropriations | | |
| Interim dividend paid | (36,300) | (30,000) |
| Retained profit brought forward | 104,101 | 68,928 |
| Available for appropriation | 369,578 | 304,101 |

REPORT OF THE DIRECTORS (CONTD.)

SHARE CAPITAL

During the year, the Company made a bonus issue of one share for every ten shares held, thereby increasing the issued and fully paid-up share capital from Rs. 100 mn to Rs. 110 mn and a right issue of one share for every ten shares held, thereby increasing the issued and fully paid-up share capital from Rs. 110 mn to Rs. 121 mn.

The authorised and issued share capital of the Company were Rs. 200,000,000/- and Rs. 121,000,000/- respectively at the end of the year.

RESERVES

The total reserves as at 31st March 2007 stand at Rs. 1,385,507,149/- (2005/06 - Rs. 1,116,030,102/-) comprising capital reserves of Rs. 373,021,385/- (2005/06 - Rs. 339,021,385/-) and revenue reserves of Rs. 1,012,485,765/- (2005/06 - Rs. 777,008,717/-).

The Statement of Changes in Equity on page 86 gives the movement in equity during the year.

MARKET VALUE OF FREEHOLD LAND

A qualified independent valuer last revalued the freehold land of the Company on 20th August 2004.

STATUTORY PAYMENTS

Directors confirm that all payments in respect of 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. 674,129/- (2005/06 - Rs. 782,498/-). A sum of Rs. 145,000/- (2005/06 - Rs. 82,500/-) made to government approved charities.

TAXATION

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%.

ENTERPRISE GOVERNANCE

The report on Enterprise Governance is given on page 61 to 67.

With a view to obtaining an independent opinion on Corporate Governance initiatives, Messrs. Det Norske Veritas AS (DNV) was engaged to review the Company's Corporate Governance framework and issue a Corporate Governance rating along with a review report containing shortcomings and suggestions. A summary of the rating report is available on pages 59 & 60.

DIRECTORS' RESPONSIBILITIES FOR FINANCIAL STATEMENTS

The Statement of Directors' Responsibilities for the Financial Statements is given on page 82.

BOARD COMMITTEES

The Reports of the Chairman of Audit, Remuneration and Nomination Committees are available on pages 72 to 73, respectively.

COMPLIANCE WITH LAWS & REGULATIONS

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

SHARE INFORMATION

Information relating to shareholding, earnings, net assets per share, market value of shares, dividends and share trading are available on pages 108 to 111.

SHAREHOLDING

There were 1,137 registered shareholders as at 31st March 2007. The percentage of shares held by the public as at 31st March 2007 was 44% of the issued shares.

The twenty major shareholders as at 31st March 2007 and the number of shares held and their percentage shareholding are given on page 110.

SHAREHOLDER

The Company has made all endeavours to ensure equitable treatment to all shareholders.

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.

REPORT OF THE DIRECTORS (CONTD.)

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, encourage the identification and development of skills, promote the use of initiative and 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 862 (2005/06 - 778).

HEALTH & 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. 6,343,158/-.

ENVIRONMENT

The Group is sensitive to the needs of the environment, not only in terms of compliance with relevant statutory obligations, but more generally in

terms of the need to be efficient in the use of energy and water and in reducing the and handling of waste material. It is the Group's policy to minimise adverse effects on the environment and to promote corporation and compliance with relevant authorities and regulations. The business activities of the Group can have an indirect impact on the environment if necessary preventive measures are not taken. The steps taken to prevent possible indirect impact are outlined in the Sustainability Report on pages 40 to 57.

QUALITY

The Group is committed to maintain 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.

EVENTS OCCURRING AFTER BALANCE SHEET DATE

The Companies Act No. 7 of 2007 was enacted with effect from 3rd May 2007. The Board has taken the necessary initiatives for a smooth transition to the new regime.

As required by Section 485 (5) (b) of the Act, the Company is deemed to have changed its name to Diesel & Motor Engineering PLC. However, as the financial statements have been

prepared as at 31st March 2007, which is prior to the Companies Act No. 7 of 2007 coming into effect, the Companies has been identified in the financial statements as Diesel and Motor Engineering Co. Ltd.

In accordance with Section 486 of the Companies Act No. 7 of 2007, the Memorandum of Association will be deemed part of the Articles of the Company.

As required by Section 487 of the Companies Act No. 7 of 2007, the Company will be making an application to the Registrar-General of Companies to obtain a new number.

No other circumstances have arisen since the Balance Sheet date, which would require adjustment to or disclosure in the financial statements.

CONTINGENCIES & COMMITMENTS

Contingent Liabilities and Capital Commitments made as at 31st March 2007 is given in Notes 25 to the financial statements.

GOING CONCERN

The Directors are of the opinion that the Company has adequate resources to continue in operational existence for the foreseeable future. The financial statements have been prepared

REPORT OF THE DIRECTORS (CONTD.)

adopting the going concern basis as stated in the Statement of Directors' Responsibilities.

DIRECTORATE

The names of the Directors who held office during the financial year and their brief profiles appear on page 10 and 11.

Dr. H. Cabral was appointed to the Board of Directors with effect from 1st October 2006 and seeks re-election at the Annual General Meeting.

Dr. U.P. Liyanage was appointed to the Board of Directors with effect from 1st October 2006 and seek re-election at the Annual General Meeting.

Mr. H.M.A. Jayasinghe resigned from the Board of Directors with effect from 1st January 2007.

Mr. R. Seevaratnam was appointed to the Board of Directors with effect from 1st January 2007 and seek re-election at the Annual General Meeting.

Mr. S.C. Algama, Mr. R.A. Ebell and Mr. A.M. Pandithage retire by rotation in accordance with the Articles and being eligible, offer themselves for re-election at the Annual General Meeting.

DIRECTORS' SHAREHOLDINGS

The Directors and their spouses held 3,399,497(2005/06 - 2,771,985) ordinary shares of the Company, which amounts to 28.10% (2005/06 - 27.72%) of the ordinary shares issued as at 31st March 2007.

The shareholdings of Directors and their spouses as at 31st March 2007 are as follows:

| | 2006/07 | 2005/06 |
|-----------------|-----------|-----------|
| A.R. Pandithage | 1,874,661 | 1,515,134 |
| A.N. Algama | 187,455 | 140,150 |
| A.M. Pandithage | 219,778 | 199,723 |
| A.G. Pandithage | 383,545 | 300,754 |
| S.C. Algama | 399,134 | 316,280 |
| T.G.H. Peries | 334,924 | 299,932 |

DIRECTORS' INTEREST IN CONTRACTS

Directors' interest in contracts of the Company are disclosed in Note 26 to the financial statements, and have been declared at meetings of the Directors. The Directors have no direct or indirect interest in any other contract or proposed contract with the Company.

ANNUAL GENERAL MEETING

The Annual General Meeting will be held at the Registered Office of the Company, No. 65, Jetawana Road, Colombo 14 on 20th June 2007. The Notice of Annual General Meeting is given on page 122.

AUDITORS

In accordance with the Companies Act No. 7 of 2007, a resolution proposing the reappointment of Messrs. KPMG Ford, Rhodes, Thornton & Co., Chartered Accountants, as Auditors to the Company will be submitted at the Annual General Meeting.

By Order of the Board,



B.C.S.A.P. Gooneratne
Secretary

Colombo, 21st May 2007

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Companies Act No. 17 of 1982 required the Directors to prepare and present Financial Statements for each financial year giving a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and the profit or loss of the Company and the Group for the financial year.

The responsibilities of the Directors in relation to the Financial Statements of the Company and the Group are set out in following statement.

The responsibility of the Auditors in relation to the Financial Statements appears in the report of the Auditors on page 83.

As per the provision of the Companies Act No. 17 of 1982 the Directors are required to prepare for each financial year and place before a general meeting of shareholders the Financial Statements, which comprise:

- I. A Statement of Income, which presents a true and fair view of the profit or loss of the Group for the financial year; and
- II. A Balance Sheet, which presents a true and fair view of the state of affairs of the Company and its subsidiary as at the end of the

financial year and which complies with the requirements of the Companies Act No. 17 of 1982 and Sri Lanka Accounting Standards.

In addition the Directors have to ensure that in preparing the Financial Statements;

- a) appropriate Accounting Policies have been used in consistent manner;
- b) where necessary prudent judgment and estimate have been made.

The Directors are responsible for ensuring that the companies within the group keep sufficient accounting records to disclose with reasonable accuracy, the financial position of the Company and the Group as required by the Companies Act No. 17 of 1982 and the listing rules of the Colombo Stock Exchange.

The Directors are required to provide the Auditors with every opportunity to take what ever steps necessary and undertake any inspection deemed necessary to enable them to form their audit opinion.

The Directors are also responsible for taking reasonable measures to safeguard the assets of the Group, and in that context to have proper regard to the establishment of appropriate systems of internal control with a view to prevention and detection of fraud and other irregularities.

The Directors, having reviewed the financial budget and cash flows for the year to 31st March 2008 and the bank facilities, consider that the Group has adequate resources to continue in operation, and have continued to adopt the going concern basis in preparing financial statements.

The Board noted the responsibility brought upon by the Companies Act No. 7 of 2007 on preparation of financial statements.

By Order of the Board,



B. C. S. A. P. Gooneratne
Secretary

Colombo
21st May 2007

REPORT OF THE AUDITORS



KPMG Ford, Rhodes, Thornton & Co.
(Chartered Accountants)
32A, Sir Mohamed Macan Markar Mawatha,
P. O. Box 186,
Colombo 00300,
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TO THE MEMBERS OF DIESEL & MOTOR ENGINEERING CO. LTD. (NOW KNOWN AS DIESEL & MOTOR ENGINEERING PLC)

We have audited the Balance Sheet of Diesel & Motor Engineering Company Ltd. as at 31st March 2007, the Consolidated Balance Sheet of the Company and its Subsidiaries as at that date, and related Statements of Income, Changes in Equity and Cash Flows for the year then ended, together with the Accounting Policies and Notes exhibited on pages 88 to 106 of the Annual Report.

Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing and presenting these financial statements in accordance with the Sri Lanka Accounting Standards. Our responsibility is to express an opinion on these Financial Statements, based on our audit.

Basis of Opinion

We conducted our audit in accordance with the Sri Lanka Auditing Standards, which require that we plan and perform the audit to obtain reasonable assurance about whether the said financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the said financial statements, assessing the accounting

principles used and significant estimates made by the Directors, evaluating the overall presentation of the financial statements, and determining whether the said financial statements are prepared and presented in accordance with the Sri Lanka Accounting Standards. We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit. We therefore believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, so far as appears from our examination, the Company maintained proper books of account for the year ended 31st March 2007, and to the best of our information and according to the explanations given to us, the said Balance Sheet and related Statements of Income, Changes in Equity and Cash Flows, the Accounting Policies and Notes thereto, which are in agreement with the said books and have been prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act, No. 17 of 1982 and give a true and fair view of the Company's state of affairs as at 31st March 2007 and of its profit and cash flows for the year then ended.

In our opinion, the Consolidated Balance Sheet and related Statements of Income, Changes in Equity, Cash Flows and the Accounting Policies and Notes thereto have been properly prepared and presented in accordance with the Companies Act No. 17 of 1982 and the Sri Lanka Accounting Standards, and give a true and fair view of the state of affairs as at 31st March 2007, and its profit and cash flows for the year ended of the Company and its Subsidiaries dealt with thereby, so far as concerns the members of the Company.

Directors' Interest in Contracts with the Company

According to the information made available to us, the Directors of the Company were not directly or indirectly interested in contracts with the Company during the year ended 31st March 2007, except as stated in Note 26 to these financial statements.

Ford Rhodes Thornton & Co.

**KPMG FORD, RHODES,
THORNTON & CO.**
Chartered Accountants
Colombo
21st May 2007

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R.N. Asirwatham FCA
S. Sirikananathan FCA
Ms. M.P. Perera FCA
C.P. Jayatilake FCA
W.W.J.C. Perera FCA

A.N. Fernando FCA
M.R. Mihular FCA
P.Y.S. Perera FCA
T.J.S. Rajakarier FCA
Ms. S. Joseph ACA

INCOME STATEMENTS

| For the year ended 31st March | Note | Consolidated | | Company | |
|--|------|---------------------|-----------------|---------------------|-----------------|
| | | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 |
| Gross turnover | 1 | 12,989,916 | 10,512,326 | 12,449,644 | 10,096,026 |
| Turnover tax | | (131,578) | (116,649) | (127,565) | (113,075) |
| Net turnover | | 12,858,338 | 10,395,677 | 12,322,079 | 9,982,951 |
| Cost of sales | | (10,728,925) | (8,804,681) | (10,365,846) | (8,534,174) |
| Gross profit | | 2,129,413 | 1,590,996 | 1,956,233 | 1,448,777 |
| Other operating income | 2 | 28,065 | 25,903 | 29,152 | 27,462 |
| Distribution expenses | | (226,057) | (175,712) | (219,147) | (170,491) |
| Administrative expenses | | (960,714) | (792,028) | (859,633) | (719,499) |
| Other operating expenses | 3 | 1,630 | (3,611) | 1,897 | (4,516) |
| Profit from operations | 4 | 972,337 | 645,548 | 908,502 | 581,733 |
| Finance income | 5 | 2,317 | 2,117 | 2,237 | 2,058 |
| Finance expenses | 5 | (464,494) | (267,860) | (435,105) | (239,475) |
| Net finance cost | 5 | (462,177) | (265,743) | (432,868) | (237,417) |
| Share of profit of equity accounted investee | 6 | 2,735 | 2,430 | – | – |
| Profit before taxation | | 512,895 | 382,235 | 475,634 | 344,316 |
| Income tax expense | 7 | (211,118) | (117,062) | (193,606) | (105,116) |
| Profit for the year | | 301,777 | 265,173 | 282,028 | 239,200 |
| Attributable to: | | | | | |
| Equity holders of the Company | | 301,777 | 265,173 | 282,028 | 239,200 |
| Minority interest | | – | – | – | – |
| Profit for the year | | 301,777 | 265,173 | 282,028 | 239,200 |
| Basic earnings per ordinary share (in Rs.) | 8 | 25.76 | 22.96 | 24.07 | 20.71 |
| Dividends per ordinary share (in Rs.) | 9 | 6.00 | 6.00 | 6.00 | 6.00 |


Figures in brackets indicate deductions.

The Accounting Policies from pages 88 to 91 and Notes from pages 92 to 106 form an integral part of these Financial Statements.

BALANCE SHEETS

| As at 31st March | | Consolidated | | Company | |
|---|------|------------------|------------------|------------------|------------------|
| | Note | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 |
| ASSETS | | | | | |
| Property, plant & equipment | 10 | 941,490 | 714,574 | 893,764 | 704,080 |
| Investments in subsidiaries | 11 | — | — | 350 | 350 |
| Investment in equity accounted investee | 12 | 21,729 | 19,071 | 6,750 | 6,750 |
| Investment in joint venture | 13 | — | — | 6,000 | — |
| Other long-term investments | 14 | 41,678 | 41,678 | 41,671 | 41,671 |
| Deferred tax assets | 20 | 473 | — | — | — |
| Total non-current assets | | 1,005,370 | 775,323 | 948,535 | 752,851 |
| Inventories | 15 | 2,097,128 | 1,561,551 | 2,005,682 | 1,489,461 |
| Trade & other receivables | 16 | 1,919,744 | 2,162,639 | 1,641,823 | 1,993,192 |
| Reveivables from subsidiaries | | — | — | 168,204 | 88,894 |
| Cash & cash equivalents | 17 | 176,390 | 70,098 | 175,521 | 69,942 |
| Total current assets | | 4,193,262 | 3,794,288 | 3,991,230 | 3,641,489 |
| TOTAL ASSETS | | 5,198,632 | 4,569,611 | 4,939,765 | 4,394,340 |
| EQUITY AND LIABILITIES | | | | | |
| Share capital | 18 | 121,000 | 100,000 | 121,000 | 100,000 |
| Share premium | 18 | 61,500 | 27,500 | 61,500 | 27,500 |
| Reserve on revaluation of land | 18 | 311,522 | 311,522 | 311,522 | 311,522 |
| General reserve | 18 | 642,908 | 472,908 | 573,082 | 423,082 |
| Retained earnings | | 369,578 | 304,101 | 307,706 | 241,978 |
| Total equity attributable to equity holders of the Company | | 1,506,508 | 1,216,031 | 1,374,810 | 1,104,082 |
| Long-term interest bearing loans and borrowings | 19 | 345,546 | 384,200 | 345,546 | 384,200 |
| Deferred tax liabilities | 20 | 31,327 | 34,829 | 31,327 | 34,616 |
| Deferred income | 21 | 3,218 | 932 | 3,218 | 932 |
| Retirement benefit obligations | 22 | 93,753 | 76,981 | 86,703 | 70,445 |
| Total non-current liabilities | | 473,844 | 496,942 | 466,794 | 490,193 |
| Current portion of long-term | | | | | |
| Interest-bearing loans and borrowings | 19 | 158,532 | 111,600 | 158,532 | 111,600 |
| Trade & other payables | 23 | 586,137 | 391,509 | 552,752 | 382,548 |
| Income tax payable | | 113,001 | 53,171 | 111,144 | 52,218 |
| Short-term interest-bearing loans and borrowings | 24 | 2,360,610 | 2,300,358 | 2,275,733 | 2,253,699 |
| Total current liabilities | | 3,218,280 | 2,856,638 | 3,098,161 | 2,800,065 |
| TOTAL LIABILITIES | | 3,692,124 | 3,353,580 | 3,564,955 | 3,290,258 |
| TOTAL EQUITY AND LIABILITIES | | 5,198,632 | 4,569,611 | 4,939,765 | 4,394,340 |

I certify that the financial statements of the Company give a true and fair view of the state of affairs of the Company as at 31st March 2007 and of its profit for the year then ended.



E. D. C. Kodituwakku

General Manager Finance & Controlling / Member - Group Management Committee

The Directors are responsible for the preparation and presentation of these Financial Statements.

Signed for and on behalf of the Board,



A. R. Pandithage

Chairman, Managing Director/Chief Executive Officer



B. C. S. A. P. Gooneratne

Director

21st May 2007

The Accounting Policies from pages 88 to 91 and Notes from pages 92 to 106 form an integral part of these Financial Statements.

STATEMENTS OF CHANGES IN EQUITY

| Consolidated | Note | Share Capital Rs.'000 | Share Premium Rs.'000 | Revaluation Reserve Rs.'000 | General Reserve Rs.'000 | Retained Earnings Rs.'000 | Total Rs.'000 |
|--|------|-----------------------------|-----------------------------|-----------------------------------|-------------------------------|---------------------------------|------------------|
| 2006/07 | | | | | | | |
| Balance as at 1st April 2006 | | 100,000 | 27,500 | 311,522 | 472,908 | 304,101 | 1,216,031 |
| Profit for the year | | – | – | – | – | 301,777 | 301,777 |
| Total recognised income and expenses for the period | | 100,000 | 27,500 | 311,522 | 472,908 | 605,878 | 1,517,808 |
| Transfer to/(from) general reserve | | – | – | – | 170,000 | (170,000) | – |
| Bonus Issue | | 10,000 | (10,000) | – | – | – | – |
| Rights Issue | | 11,000 | 44,000 | – | – | – | 55,000 |
| Dividends to shareholders | 9 | – | – | – | – | (66,300) | (66,300) |
| Balance as at 31st March 2007 | | 121,000 | 61,500 | 311,522 | 642,908 | 369,578 | 1,506,508 |
| 2005/06 | | | | | | | |
| Balance as at 1st April 2005 | | 100,000 | 27,500 | 311,522 | 372,908 | 193,928 | 1,005,858 |
| Profit for the year | | – | – | – | – | 265,173 | 265,173 |
| Total recognised income and expenses for the period | | 100,000 | 27,500 | 311,522 | 372,908 | 459,101 | 1,271,031 |
| Transfers to/(from) general reserve | | – | – | – | 100,000 | (100,000) | – |
| Dividends to shareholders | 9 | – | – | – | – | (55,000) | (55,000) |
| Balance as at 31st March 2006 | | 100,000 | 27,500 | 311,522 | 472,908 | 304,101 | 1,216,031 |
| Company | | | | | | | |
| | | Share Capital Rs.'000 | Share Premium Rs.'000 | Revaluation Reserve Rs.'000 | General Reserve Rs.'000 | Retained Earnings Rs.'000 | Total Rs.'000 |
| 2006/07 | | | | | | | |
| Balance as at 1st April 2006 | | 100,000 | 27,500 | 311,522 | 423,082 | 241,978 | 1,104,082 |
| Profit for the year | | – | – | – | – | 282,028 | 282,028 |
| Total recognised income and expenses for the period | | 100,000 | 27,500 | 311,522 | 423,082 | 524,006 | 1,386,110 |
| Transfer to/(from) general reserve | | – | – | – | 150,000 | (150,000) | – |
| Bonus Issue | | 10,000 | (10,000) | – | – | – | – |
| Rights Issue | | 11,000 | 44,000 | – | – | – | 55,000 |
| Dividend to shareholders | 9 | – | – | – | – | (66,300) | (66,300) |
| Balance as at 31st March 2007 | | 121,000 | 61,500 | 311,522 | 573,082 | 307,706 | 1,374,810 |
| 2005/06 | | | | | | | |
| Balance as at 1st April 2005 | | 100,000 | 27,500 | 311,522 | 323,082 | 157,778 | 919,882 |
| Profit for the year | | – | – | – | – | 239,200 | 239,200 |
| Total recognised income and expenses for the period | | 100,000 | 27,500 | 311,522 | 323,082 | 396,978 | 1,159,082 |
| Transfers to/(from) general reserve | | – | – | – | 100,000 | (100,000) | – |
| Dividends to shareholders | 9 | – | – | – | – | (55,000) | (55,000) |
| Balance as at 31st March 2006 | | 100,000 | 27,500 | 311,522 | 423,082 | 241,978 | 1,104,082 |

Figures in brackets indicate deductions.

The Accounting Policies from pages 88 to 91 and Notes from pages 92 to 106 form an integral part of these Financial Statements.

CASH FLOW STATEMENTS

| For the year ended 31st March | Consolidated | | Company | |
|--|--------------------|--------------------|--------------------|--------------------|
| | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 |
| Operating Activities | | | | |
| Cash receipts from customers | 13,175,265 | 9,789,791 | 12,665,483 | 9,378,359 |
| Cash paid to suppliers and employees | (12,176,773) | (10,471,964) | (11,717,838) | (10,053,055) |
| Cash generated from operations | 998,492 | (682,173) | 947,645 | (674,696) |
| Interest paid | (460,172) | (237,573) | (430,783) | (211,144) |
| Income taxes paid | (155,186) | (70,687) | (137,969) | (63,656) |
| Cash flows from operating activities | 383,134 | (990,433) | 378,893 | (949,496) |
| Investing Activities | | | | |
| Proceeds from disposal of property, plant & equipment | 15,358 | 29,761 | 21,314 | 29,696 |
| Investment in joint venture | – | – | (6,000) | – |
| Dividends received | 1,934 | 1,924 | 1,934 | 1,924 |
| Interest received | 383 | 193 | 303 | 134 |
| Acquisition and construction of property, plant & equipment | (305,311) | (123,352) | (263,441) | (118,746) |
| Cash flows from investing activities | (287,636) | (91,474) | (245,890) | (86,992) |
| Financing Activities | | | | |
| Proceeds from rights issue | 55,000 | – | 55,000 | – |
| Proceeds from long-term loans | 117,670 | 450,000 | 117,670 | 450,000 |
| Repayment of long-term loans | (135,905) | (89,200) | (135,905) | (89,200) |
| Dividends paid | (66,363) | (55,000) | (66,363) | (55,000) |
| Repayment of finance lease obligations | (19,860) | – | (19,860) | – |
| Cash flows from financing activities | (49,458) | 305,800 | (49,458) | 305,800 |
| Net increase/(decrease) in cash & cash equivalents | 46,040 | (776,107) | 83,545 | (730,688) |
| Cash & cash equivalents at beginning of the year | (2,230,260) | (1,454,153) | (2,183,757) | (1,453,069) |
| Cash & cash equivalents at end of the year (Note A) | (2,184,220) | (2,230,260) | (2,100,212) | (2,183,757) |
| A. Analysis of Cash & Cash Equivalents | | | | |
| Bank and cash balances (Note 17) | 176,390 | 70,098 | 175,521 | 69,942 |
| Bank borrowings (Note 24) | (2,360,610) | (2,300,358) | (2,275,733) | (2,253,699) |
| Cash & cash equivalents | (2,184,220) | (2,230,260) | (2,100,212) | (2,183,757) |

Figures in brackets indicate deductions.

The Accounting Policies from pages 88 to 91 and Notes from pages 92 to 106 form an integral part of these Financial Statements.

SIGNIFICANT ACCOUNTING POLICIES

1. GENERAL

The Consolidate Financial Statements of Diesel & Motor Engineering Company Ltd. for the year ended 31st March 2007 comprise the Company and its fully-owned subsidiaries (together referred to as the 'Group') and the Group's interest in an associate. The Directors authorised the Financial Statements for issue on 21st May 2007.

All companies in the Group are limited liability companies, incorporated and domiciled in Sri Lanka. The parent company and its subsidiaries have the registered office and principal place of business located at No. 65, Jetawana Road, Colombo 14.

i. Statement of Compliance

The Consolidated financial statements have been prepared in accordance with Sri Lanka Accounting Standards (SLAS's) adopted by the Institute of Chartered Accountants of Sri Lanka (ICASL), and the requirements of the Companies Act No. 17 of 1982, and Sri Lanka Accounting & Auditing Standards Act No. 15 of 1995.

ii. Responsibility for Financial Statements

The Board of Directors is responsible for the preparation & presentation of the financial statements. The statement containing of the Directors Responsibility for preparation of Financial Statements is given on page 82.

iii. Basis of Preparation

The Consolidated financial statements are presented in Sri Lankan Rupees rounded to the nearest thousand and are prepared on a historical cost basis, except that certain land included in property, plant & equipment is stated at a valuation as explained in Note 10 to the financial statements.

The accounting policies are consistent with those used in the previous year except on instances where the revised standards have been adopted:

SLAS 3 (Revised) - Presentation of Financial Statements
SLAS 5 (Revised) - Inventories
SLAS 10 (Revised) - Accounting Policies, Changes in Accounting Estimates & Errors
SLAS 12 (Revised) - Events after the Balance Sheet date
SLAS 14 (Revised) - Income Taxes
SLAS 18 (Revised) - Property, Plant & Equipment
SLAS 19 (Revised) - Leases
SLAS 21 (Revised) - The Effects of Changes in Foreign Exchange Rates
SLAS 26 (Revised) - Consolidated and Separate Financial Statements
SLAS 27 (Revised) - Investments in Associates
SLAS 30 (Revised) - Related Party Disclosures
SLAS 31 (Revised) - Interests In Joint Ventures
SLAS 34 (Revised) - Earnings per Share

The preparation of financial statements in conformity with SLAS require management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets & liabilities, income & expenses. The estimates and related assumptions are based on past experience and reviewed on an ongoing basis.

iv. Basis of Consolidation

The Group Financial Statements comprise consolidation of the financial statements of the Company, its subsidiaries in terms of Sri Lanka Accounting Standard No. 26 on Consolidated and Separate Financial Statements, its associate company in terms of Sri Lanka Accounting Standard No. 27 - Investments in Associates and its joint venture in terms of Sri Lanka Accounting Standard No. 31 - Interest in Joint Ventures.

a) Subsidiaries

Subsidiaries are those entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the Consolidated financial statements from the date that control commences until the date that control ceases. There is no minority interest in the Consolidated Financial Statements since all subsidiary companies are wholly owned.

b) Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. The Consolidated financial statements include the Group's share of the total recognised gains and losses of associates on an equity accounting basis, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

c) Joint Ventures

Joint ventures are jointly controlled entities under a contractual agreement whereby the parties involved undertake an economic activity that is subject to joint control. The Consolidated financial statements include the Group's proportionate share of the joint venture assets, liabilities, revenue & expenses with item of a similar nature on a line by line basis.

d) Transactions Eliminated on Consolidation

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions are eliminated

SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

in preparing the Consolidated Financial Statements. Unrealised gains arising from transactions with associates are eliminated to the extent of the Group's interest in the associate.

- e)** The Financial Statements of all companies in the Group are prepared to a common financial year of 1st April to 31st March.

v. Foreign Currency Transactions

The Financial Statements are presented in Sri Lankan Rupees which is also the functional currency. Transactions in foreign currencies are translated into Sri Lankan Rupees at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the Balance Sheet date are translated into Sri Lankan rupees at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the Income Statement.

vi. Segment Reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those other segments.

The segment reporting is presented on the primary format, business segments, as per the Sri Lanka Accounting Standard No. 28 - Segment Reporting.

Inter-segment pricing is determined on an arm's length basis.

Segment information is based on the identified product segments reflecting the Group 'core' and 'non-core' business activities. Segment information includes revenue, segment result, assets, liabilities and cash flows.

Segment assets and liabilities include those operational assets and liabilities that can be allocated to the segment on a reasonable basis.

Segment expenses consist of direct expenses pertaining to and directly attributable to the segment.

Considering activities of the operations, segment information based on geographical segments does not arise.

2. ASSETS AND BASES OF THEIR VALUATIONS

Assets classified as current assets on the Balance Sheet are cash and bank balances and those which are expected to be realised in cash during the normal operating cycle or within one year from the Balance Sheet date, whichever is shorter.

i. Property, Plant & Equipment

Property, plant & equipment is stated at cost or valuation less any accumulated depreciation and any accumulated impairment losses.

a) Cost

The cost of property, plant & equipment is the cost of acquisition or construction together with any expenses incurred in bringing the assets to their working condition for their intended use.

Where an item of property, plant & equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant & equipment.

b) Revaluation

A revaluation of property, plant & equipment is done when there is a substantial distinction between the fair value (market value) and the book value of the asset and is normally undertaken by professionally qualified valuers. When an item of

property, plant & equipment is revalued, the entire class of that property, plant & equipment to which that asset belongs is revalued. If the carrying amount is increased as a result of a revaluation, the increase is credited directly to equity under the heading of revaluation surplus. When an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognised as an expense. However, a revaluation decrease is charged directly against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation surplus in respect of that same asset.

c) Subsequent Expenditure

Expenditure incurred to replace a component of an item of property, plant & equipment that is accounted for separately, is capitalised. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant & equipment. All other expenditure is recognised in the Income Statement as an expense as incurred.

d) Depreciation

Depreciation is charged to the Income Statement on a straight-line basis over the estimated useful lives of items of property, plant & equipment.

Depreciation of an asset begins when it is available for use.

Freehold land is not depreciated.

Leasehold assets are depreciated over the lease period.

The estimated useful lives are as follows:

| | Years |
|-------------------------------|-------|
| Buildings | 36-40 |
| Plant & Machinery | 08-13 |
| Workshop Implements | 03-04 |
| Motor Vehicles | 03-04 |
| Furniture & Fittings | 09-13 |
| Office Equipment & Electrical | 06-10 |
| Computer Hardware & Software | 03-04 |

SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The residual value, useful life and depreciation method of assets are reviewed annually and if the expectations differ from original estimates the changes are accounted in accordance with SLAS - 10 Accounting Policies, Changes in Accounting Estimates and Errors.

e) Capital Work-in-Progress

Capital expenditure incurred during the year, which are not completed as at the Balance Sheet date are shown as capital work-in-progress.

f) Derecognition

An item of property, plant & equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognising of an assets is recognised in the Income Statement in the year it is derecognised.

ii. Intangible Assets

The Group had no intangible assets as at the Balance Sheet date.

iii. Investments

Long-Term Investments

Investments in quoted and unquoted shares held on long-term basis are stated at cost. Investments in subsidiaries associates and Joint Ventures are treated as long-term investments and carried at cost in the parent company's financial statements. Provision for diminution in value is made when in the opinion of the Directors there has been decline other than temporary in the value of the investment.

iv. Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is based on the Weighted Average Cost Price principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition.

Work-in-progress is valued at cost of materials.

A provision is made for all non-moving and obsolete items of inventory.

v. Trade and Other Receivables

Trade and other receivables are stated in the accounts at their estimated realisable value. A provision has been made in respect of bad & doubtful debts. Debts that are known to be uncollectible are written off.

vi. Cash & Cash Equivalents

Cash & cash equivalents comprise cash balances and demand deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash & cash equivalents for the purpose of the Statement of Cash Flows.

vii. Impairment

An asset is impaired when its carrying amount exceeds its recoverable amount. Impairment test is carried out annually at the Balance Sheet date. Any impairment loss is recognised immediately in the Income Statement. Any impairment loss of a revalued asset is charged to the revaluation reserve to the extent that impairment loss does not exceed the amount held in the revaluation reserve in respect of that same asset.

3. LIABILITIES AND PROVISIONS

Liabilities classified as current liabilities on the Balance Sheet are those, which fall due for payment on demand or within one year from the Balance Sheet date. Non-current liabilities are those balances that fall due for payment after one year from the Balance Sheet date.

i. Employee Benefits

a) Defined Contribution Plans

Contributions to defined contribution plans, EPF & ETF, are recognised as an expense in the Income Statement as incurred.

b) Defined Benefits Plans - Retiring Gratuity

Provision has been made in the Accounts for retiring gratuity from the first year of service for all employees in conformity with Sri Lanka Accounting Standard (SLAS 16) - Retirement Benefit Costs. However, under the Payment of Gratuity Act No. 12 of 1983, liability to an employee arises only on completion of five years service.

The liability has not been actuarially valued and is not externally funded.

The liability is calculated on the basis of half a month's salary for each completed year of service.

ii. Deferred Income

The excess of sales proceeds over the carrying value of an asset in a sale and lease back transaction is classified as Deferred Income. Deferred Income is systematically amortised to the Income Statement over the lease period.

iii. Trade and Other Payables

Trade and other payables are stated at their cost.

iv. Provisions

A provision is recognised in the Balance Sheet when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

4. INCOME & EXPENSES

For the purpose of presentation of the Income Statement, the function of expenses method is adopted, as it represents fairly the elements of the Company performance.

i. Turnover

The net Group turnover excludes turnover taxes and trade discounts. The gross turnover represents the invoiced value of goods & services to customers outside the Group.

ii. Revenue

a) Goods Sold & Services Rendered

Revenue from the sale of goods is recognised in the Income Statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue from services rendered is recognised in the Income Statement on the invoicing of the job after completion. In instances where the revenue from services spreads over a period of time, income will be recognised on the basis of percentage of completion.

b) Service Support Income

Service support commission income from foreign principals is accounted for on an accrual basis once the shipment is effected.

c) Other Operating Income

Other operating income comprises mainly of gain on disposal of property, plant & equipment, bad debt recoveries, sale of scrapped items and motor vehicle valuation fees, etc.

iii. Expenses

a) Lease Payments - Operating Leases

Payments made under operating leases are recognised in the Income Statement on a straight-line basis over the term of the lease.

IV. Borrowing Costs

Borrowing Costs are recognised as an expense in the year in which they are incurred, except to the extent where borrowing costs that are directly attributable to the acquisition, construction, or production of a qualifying asset that take a substantial period of time to get ready for its intended use or sale, is capitalised as part of that asset.

a) Net Finance Costs

Financing costs comprise interest expenses on borrowings, interest receivable on funds invested, dividend income and foreign exchange gain and losses. Interest income is recognised in the Income Statement as it accrues, taking into account the effective yield on the asset.

Dividend income is recognised when the shareholder's right to receive payment is established.

V. INCOME TAX

a) Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the Income Statement.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted at the Balance Sheet date, and any adjustment to tax payable in respect of previous years.

The provision to income tax is based on the profit for financial year adjusted in accordance with the Inland Revenue Act. No. 10 of 2006 and amendments thereto.

b) Deferred Tax

Deferred tax is calculated on temporary differences between Tax base and Accounting base at the Balance Sheet.

Deferred tax is provided for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes (Accounting base) and the amounts used for taxation purposes (Tax base). The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted at the Balance Sheet date.

Deferred tax assets and liabilities are measured at the tax rates that have been enacted or substantially enacted at the Balance Sheet date.

5. CASH FLOW STATEMENT

The Cash Flow Statement has been prepared using the 'direct method'.

Interest paid is classified as operating cash flows; interest and dividend received are classified as investing cash flows, while dividends paid are classified as financing cash flows for the purpose of presenting the Cash Flow Statement.

6. EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

All material post Balance Sheet events have been considered and where appropriate adjustment to or disclosure has been made according to SLAS 12 (Revised) - Events after the Balance Sheet date in the respective Notes to the financial statements.

7. CAPITAL COMMITMENTS AND CONTINGENCIES

Capital commitments and contingent liabilities of the Group are disclosed in respective Notes to the financial statements. Refer Note 30 (page 106)

8. COMPARATIVE INFORMATION

Where necessary comparative information has been reclassified to conform to the current year's presentation.

NOTES TO THE FINANCIAL STATEMENTS

1. SEGMENT INFORMATION

The Group comprises the following main business segments:

| Segment | Products & Services |
|---|---|
| Vehicles | - Sale of brand new Passenger Vehicles, 4WD Vehicles, Commercial Vehicles, Special Purpose Vehicles and Pre-owned Passenger Vehicles. |
| Vehicle Parts & Service | - Repair of Passenger & Commercial Vehicles, Sale of Vehicle Spare Parts, Accessories, Components and Tyres. |
| Lighting & Power Tools | - Sale of Power Tools & Accessories, Lamps, Lighting Fittings and Lighting Accessories. |
| Construction & Material Handling Machinery | - Sale & Service of Earth Moving Machinery, Road Construction Machinery, Fork-Lifts, Racking Systems, Tractors Pumps and Dock Levellers. |
| Diversified Activities | - Sale & Service of Telecommunication Equipment, Medical Equipment, Generating Sets, Turbines, UPS Equipment, Diesel Engines for Marine Propulsion, Rail Traction and Power Generation and the Business of Travel Agents. |

| | Vehicles | | Vehicle Parts & Service | | Lighting & Power Tools | | Construction & Material Handling Machinery | | Diversified Activities | | Total | |
|---|------------------|------------------|-------------------------|------------------|------------------------|-----------------|--|-----------------|------------------------|-----------------|-------------------|-------------------|
| <i>As at 31st March</i> | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 |
| Business Segment Turnover & Results | | | | | | | | | | | | |
| Total external revenue | 9,041,292 | 7,414,755 | 2,104,363 | 1,766,324 | 355,125 | 272,793 | 1,258,905 | 822,644 | 573,845 | 438,888 | 13,333,530 | 10,715,404 |
| Inter-segment revenue | 214,446 | 137,088 | 32,808 | 22,163 | 948 | 921 | 57,173 | 20,317 | 38,239 | 22,589 | 343,614 | 203,078 |
| Total segment revenue | 8,826,846 | 7,277,667 | 2,071,555 | 1,744,161 | 354,177 | 271,872 | 1,201,732 | 802,327 | 535,606 | 416,299 | 12,989,916 | 10,512,326 |
| Segment results | 594,895 | 330,075 | 368,938 | 279,357 | 51,727 | 44,731 | 109,693 | 125,495 | 69,872 | 63,759 | 1,195,125 | 843,417 |
| Unallocated income | - | - | - | - | - | - | - | - | - | - | 28,380 | 27,527 |
| Unallocated expenses | - | - | - | - | - | - | - | - | - | - | (251,168) | (225,396) |
| Profit from operations | - | - | - | - | - | - | - | - | - | - | 972,337 | 645,548 |
| Financing cost - net | - | - | - | - | - | - | - | - | - | - | (462,177) | (265,743) |
| Income from equity accounted investee | - | - | - | - | - | - | - | - | - | - | 2,735 | 2,430 |
| Income tax expense | - | - | - | - | - | - | - | - | - | - | (211,118) | (117,062) |
| Profit for the period | - | - | - | - | - | - | - | - | - | - | 301,777 | 265,173 |
| Business Segment Assets & Liabilities | | | | | | | | | | | | |
| Segment assets | 2,331,953 | 2,519,072 | 959,235 | 716,776 | 134,528 | 117,525 | 522,338 | 388,498 | 372,262 | 252,193 | 4,320,316 | 3,994,064 |
| Investment in equity accounted investee | - | - | - | - | - | - | - | - | - | - | 21,729 | 19,071 |
| Unallocated assets | - | - | - | - | - | - | - | - | - | - | 856,587 | 556,476 |
| Total assets | 2,331,953 | 2,519,072 | 959,235 | 716,776 | 134,528 | 117,525 | 522,338 | 388,498 | 372,262 | 252,193 | 5,198,632 | 4,569,611 |
| Segment liabilities | 2,015,164 | 2,021,799 | 479,536 | 293,029 | 2,470 | 23,994 | 168,377 | 142,854 | 122,288 | 63,691 | 2,787,835 | 2,545,367 |
| Unallocated liabilities | - | - | - | - | - | - | - | - | - | - | 904,289 | 808,213 |
| Total liabilities | 2,015,164 | 2,021,799 | 479,536 | 293,029 | 2,470 | 23,994 | 168,377 | 142,854 | 122,288 | 63,691 | 3,692,124 | 3,353,580 |
| Business Segment other Information excluding unallocated amounts | | | | | | | | | | | | |
| Capital expenditure | 20,513 | 35,509 | 94,357 | 42,064 | 818 | 193 | 12,194 | 7,012 | 19,072 | 4,744 | 146,954 | 89,522 |
| Depreciation | 8,364 | 7,368 | 22,921 | 21,366 | 373 | 495 | 6,953 | 6,820 | 3,777 | 3,678 | 42,388 | 39,727 |
| Non-cash expenses other than depreciation | 5,532 | 2,732 | 9,220 | (2,957) | (2,937) | (3,870) | 4,432 | 6,017 | 1,161 | (4,574) | 17,408 | (2,652) |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

| | Vehicles | | Vehicle Parts & Services | | Lighting & Power Tools | | Construction & Material Handling Machinery | | Diversified Activities | | Consolidated | |
|--|-----------------|-----------------|--------------------------|-----------------|------------------------|-----------------|--|-----------------|------------------------|-----------------|------------------|-----------------|
| As at 31 March | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 | 2007 Rs.'000 | 2006 Rs.'000 |
| Business Segment Cash Flow | | | | | | | | | | | | |
| Operating activities | 785,497 | (1,012,308) | 83,345 | 245,792 | 15,173 | 42,238 | (14,357) | (164,949) | (44,359) | (124,602) | 825,299 | (1,013,829) |
| Investing activities | (20,513) | (35,508) | (94,918) | (42,064) | (818) | (193) | (12,194) | (7,012) | (12,655) | (4,744) | (141,098) | (89,521) |
| Unallocated Cash Flows | | | | | | | | | | | | |
| Common expenses | | | | | | | | | | | (309,381) | 94,083 |
| Income taxes paid | | | | | | | | | | | (155,186) | (70,687) |
| Proceeds from disposal of property, plant & equipment | | | | | | | | | | | 9,403 | 29,761 |
| Investment in shares | | | | | | | | | | | | — |
| Dividends received | | | | | | | | | | | 1,934 | 1,924 |
| Interest received | | | | | | | | | | | 383 | 193 |
| Acquisition of construction of property, plant & equipment | | | | | | | | | | | (155,716) | (33,831) |
| Proceeds from issue of shares | | | | | | | | | | | 55,000 | |
| Proceeds from long-term loan | | | | | | | | | | | 117,670 | 450,000 |
| Repayment of long-term loan | | | | | | | | | | | (135,905) | (89,200) |
| Dividends paid | | | | | | | | | | | (66,363) | (55,000) |
| Net increase/(decrease) in cash & cash equivalents | | | | | | | | | | | 46,040 | (776,107) |

Figures in brackets indicate outflows.

Segment information is presented in respect of the Group's business segments. The primary format, business segment, is based on the Group's management and internal reporting structure. Segment results, assets and liabilities include those items directly attributable to a segment as well as those that can be allocated to the segment on a reasonable basis. Considering activities of the operations, segment information based on geographical segments does not arise.

The presentation of segmentation is based on the nature of product line in the context of its domain.

2. OTHER OPERATING INCOME

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Gain on disposal of property, plant & equipment | 6,293 | 10,164 | 6,256 | 10,099 |
| Sundry income | 13,575 | 3,782 | 14,453 | 3,782 |
| Reversal of slow moving inventories | 8,197 | 11,957 | 8,443 | 13,581 |
| | 28,065 | 25,903 | 29,152 | 27,462 |

3. OTHER OPERATING EXPENSES

| | Consolidated | | Company | |
|-----------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Provision/(Reversal) of bad debts | 1,630 | (3,611) | 1,897 | (4,516) |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

4. PROFIT FROM OPERATIONS

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| 4.1 Profit from Operations is stated after charging/(crediting) all expenses/income including the following: | | | | |
| Directors' emoluments | 30,164 | 19,961 | 28,641 | 14,696 |
| Auditor's Remuneration | | | | |
| - Audit service | 950 | 815 | 780 | 675 |
| - Non-Audit service | 146 | 249 | 101 | 222 |
| Depreciation on property, plant & equipment | 63,038 | 65,394 | 58,699 | 61,715 |
| Amortisation of deferred income | (2,285) | (509) | (2,285) | (509) |
| Legal fees | 16,659 | 3,938 | 12,874 | 3,618 |
| Donations | 674 | 782 | 674 | 782 |
| Staff expenses (Note 4.2) | 432,159 | 378,759 | 385,090 | 342,529 |

4.2 Staff Expenses

| | Consolidated | | Company | |
|--|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Defined contribution plan costs (EPF & ETF) | 43,453 | 28,904 | 38,614 | 25,606 |
| Defined benefit plan costs (Retiring gratuity) | 20,008 | 13,401 | 19,349 | 12,806 |
| Other staff costs | 368,698 | 336,454 | 327,127 | 304,117 |
| | 432,159 | 378,759 | 385,090 | 342,529 |
| Average number of employees for the year | 820 | 714 | 728 | 635 |

5. NET FINANCE COST

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Finance Costs | | | | |
| Interest on long-term borrowings | (58,925) | (48,297) | (58,925) | (48,297) |
| Interest on short-term borrowings | (389,613) | (206,624) | (357,385) | (180,195) |
| Interest on finance leases | (2,388) | — | (2,388) | — |
| Net loss on translation of foreign currency | (13,568) | (12,939) | (16,407) | (10,983) |
| | (464,494) | (267,860) | (435,105) | (239,475) |
| Finance Income | | | | |
| Dividend income | 1,934 | 1,924 | 1,934 | 1,924 |
| Interest income | 383 | 193 | 303 | 134 |
| | 2,317 | 2,117 | 2,237 | 2,058 |
| | (462,177) | (265,743) | (432,868) | (237,417) |

6. SHARE OF PROFIT OF EQUITY ACCOUNTED INVESTEE

| | Consolidated | |
|--|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Browns Dimo Industrial Products (Pvt) Ltd. | 2,735 | 2,430 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

7. INCOME TAX EXPENSE

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Current Tax Expense | | | | |
| Company | 189,780 | 104,513 | 189,780 | 104,513 |
| Subsidiaries | 16,530 | 11,522 | – | – |
| | 206,310 | 116,035 | 189,780 | 104,513 |
| Under provision in respect of previous years | 8,706 | – | 7,115 | – |
| Share of associate company income tax | 77 | 188 | – | – |
| | 215,093 | 116,223 | 196,895 | 104,513 |
| Deferred Tax Expenses | | | | |
| Origination/(Reversal) of temporary differences | (3,975) | 839 | (3,289) | 603 |
| Income tax expense | 211,118 | 117,062 | 193,606 | 105,116 |

7.1 Reconciliation of Accounting Profit to Income Tax Expense

| | Consolidated | | Company | |
|----------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Profit before tax | 512,895 | 382,235 | 475,634 | 344,316 |
| Associate Company profit | (2,735) | (2,430) | – | – |
| Disallowable expenses | 159,871 | 84,253 | 148,534 | 79,919 |
| Capital allowances | (64,506) | (63,970) | (60,685) | (59,735) |
| Allowable expenses | (15,490) | (4,027) | (15,346) | (4,027) |
| Income not liable to tax | (2,825) | (10,672) | (2,745) | (10,548) |
| Taxable income | 587,210 | 385,389 | 545,392 | 349,925 |
| Income tax thereon | | | | |
| Tax at 15% | 830 | 465 | 830 | 465 |
| Tax at 20% | – | 7 | – | – |
| Tax at 35%-30% | 205,480 | 104,048 | 188,950 | 104,048 |
| Tax at 32.5% | – | 11,515 | – | – |
| Current tax expense | 206,310 | 116,035 | 189,780 | 104,513 |

Corporate income tax has been computed in accordance with the Inland Revenue Act, No. 10 of 2006.

The Companies within the Group are liable to income tax at 35%. The tax on export profit is 15%.

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

8. BASIC EARNINGS PER SHARE

Basic earnings per shares is calculated by dividing the net profit for the year attributable to the ordinary shareholders by the weighted average number of ordinary shares in issue during the year. The weighted average number of ordinary shares in issue during the year and the previous year are adjusted for the right issue and scrip issue made during the year.

| | Consolidated | | Company | |
|---|-------------------|------------|-------------------|------------|
| | 2006/07 | 2005/06 | 2006/07 | 2005/06 |
| Profit attributable to ordinary shareholders (Rs. '000) | 301,777 | 265,172 | 282,028 | 239,200 |
| Weighted average number of shares (i) | 11,715,000 | 11,550,000 | 11,715,000 | 11,550,000 |
| Basic earnings per ordinary share (Rs.) | 25.76 | 22.96 | 24.07 | 20.71 |
| (i) Qualifying ordinary shares at the beginning of the year | 11,000,000 | 11,000,000 | 11,000,000 | 11,000,000 |
| Effect of shares issued during the year | | | | |
| Scrip issue | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 |
| Rights issue | 715,000 | 550,000 | 715,000 | 550,000 |
| Weighted average number of ordinary shares at the year end | 11,715,000 | 11,550,000 | 11,715,000 | 11,550,000 |

There were no potentially dilutive ordinary shares outstanding at any time during the year.

9. DIVIDENDS

| | Company | |
|--|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Interim Paid - Rs. 3/- per share (2005/2006 - Rs. 3/- per share) | 36,300 | 30,000 |
| Final proposed - Rs. 3/- per share (2005/2006 - Rs. 3/- per share) | 36,300 | 30,000 |
| | 72,600 | 60,000 |
| Dividends (inclusive of proposed dividend) per share | 6.00 | 6.00 |

Directors have recommended the payment of a final dividend of Rs. 3/- per share for the year ended 31st March 2007, (2005/2006 - Rs. 3/- per share) which will be declared at the Annual General Meeting to be held on 20th June 2007.

In accordance with SLAS 12 (Revised) on Events after the Balance Sheet date, this proposed dividend has not been recognised as a liability in the financial statements as at the year end.

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

10. PROPERTY, PLANT & EQUIPMENT

| | Freehold Land | Leasehold Land | Buildings & Premises | Plant & Machinery | Tools & Implements | Motor Vehicles | Computer Hardware & Software | Electrical Fixtures, Fittings, & Office Equipment | Total 31.03.07 | Total 31.03.06 |
|---------------------------------|------------------|-------------------|----------------------------|----------------------|-----------------------|-------------------|---------------------------------------|---|-------------------|-------------------|
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| a) CONSOLIDATED | | | | | | | | | | |
| Cost or Valuation | | | | | | | | | | |
| Balance brought forward | 346,433 | 2,400 | 180,781 | 124,541 | 84,336 | 106,430 | 127,037 | 110,481 | 1,082,439 | 1,001,597 |
| Additions | 113,808 | – | 51,727 | 29,350 | 7,582 | 66,271 | 24,733 | 12,071 | 305,542 | 120,961 |
| | 460,241 | 2,400 | 232,508 | 153,891 | 91,918 | 172,701 | 151,770 | 122,552 | 1,387,981 | 1,122,558 |
| Disposals | – | – | – | (1,079) | – | (13,407) | (58,869) | (187) | (73,542) | (40,119) |
| Balance carried forward | 460,241 | 2,400 | 232,508 | 152,812 | 91,918 | 159,294 | 92,901 | 122,365 | 1,314,439 | 1,082,439 |
| Depreciation | | | | | | | | | | |
| Balance brought forward | – | 720 | 35,649 | 49,587 | 63,236 | 63,886 | 92,997 | 65,539 | 371,614 | 326,742 |
| Charge for the year | – | 80 | 6,240 | 10,261 | 8,218 | 18,699 | 12,823 | 6,716 | 63,037 | 65,394 |
| On disposals | – | – | – | (756) | – | (10,628) | (46,661) | (139) | (58,184) | (20,522) |
| Balance carried forward | – | 800 | 41,889 | 59,092 | 71,454 | 71,957 | 59,159 | 72,116 | 376,467 | 371,614 |
| Net book value at year end | 460,241 | 1,600 | 190,619 | 93,720 | 20,464 | 87,337 | 33,742 | 50,249 | 937,972 | 710,825 |
| Capital work-in-progress | | | | | | | | | 3,518 | 3,749 |
| Carrying amount | | | | | | | | | 941,490 | 714,574 |
| b) COMPANY | | | | | | | | | | |
| Cost or Valuation | | | | | | | | | | |
| Balance brought forward | 346,433 | 2,400 | 178,323 | 121,854 | 77,263 | 103,114 | 120,313 | 103,940 | 1,053,640 | 976,919 |
| Additions | 113,808 | – | 32,563 | 12,622 | 7,227 | 65,291 | 22,089 | 10,072 | 263,672 | 116,355 |
| | 460,241 | 2,400 | 210,886 | 134,476 | 84,490 | 168,405 | 142,402 | 114,012 | 1,317,312 | 1,093,274 |
| Disposals | – | – | – | (1,079) | – | (13,318) | (58,176) | (187) | (72,760) | (39,634) |
| Balance carried forward | 460,241 | 2,400 | 210,886 | 133,397 | 84,490 | 155,087 | 84,226 | 113,825 | 1,244,552 | 1,053,640 |
| Depreciation | | | | | | | | | | |
| Balance brought forward | – | 720 | 33,902 | 47,902 | 58,837 | 61,182 | 89,080 | 61,686 | 353,309 | 311,631 |
| Charge for the year | – | 80 | 6,214 | 9,102 | 7,157 | 18,505 | 11,359 | 6,282 | 58,699 | 61,715 |
| On disposals | – | – | – | (756) | – | (10,540) | (46,267) | (139) | (57,702) | (20,037) |
| Balance carried forward | – | 800 | 40,116 | 56,248 | 65,994 | 69,147 | 54,172 | 67,829 | 354,306 | 353,309 |
| Net book value at year end | 460,241 | 1,600 | 170,770 | 77,149 | 18,496 | 85,940 | 30,054 | 45,996 | 890,246 | 700,331 |
| Capital work-in-progress | | | | | | | | | 3,518 | 3,749 |
| Carrying amount | | | | | | | | | 893,764 | 704,080 |

Notes

- The value of the land owned by Diesel & Motor Engineering Co. Ltd. was assessed by a qualified valuer as at 20th August 2004. The valuation of land has been written up to correspond with the market value on the respective date. The purchase cost of the land stated as Rs. 346,432,754/- is Rs. 34,910,616/-.
- There were no tax implications or tax liabilities pertaining to revaluation of land stated in Note 10 above.
- The leasehold land situated at Anuradhapura is on a 30 year lease and expires in 2026.
- There has been no permanent fall in the value of property, plant & equipment which require a provision for impairment.
- There were no borrowings against mortgage of property, plant & equipment.

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

11. INVESTMENTS IN SUBSIDIARIES

| | Group Interest % | Company 2006/07 Rs.'000 | 2005/06 Rs.'000 |
|---|------------------------|-------------------------------|--------------------|
| Unquoted | | | |
| Dimo Ltd. | | | |
| 25,000 ordinary shares of Rs. 10/- each | 100 | 250 | 250 |
| Dimo Industries Ltd. | | | |
| 500 ordinary shares of Rs. 100/- each | 100 | 50 | 50 |
| Dimo Travels Ltd. | | | |
| 500 ordinary shares of Rs. 100/- each | 100 | 50 | 50 |
| | | 350 | 350 |

The principal activities of the Company is given on page 78.

12. INVESTMENT IN EQUITY ACCOUNTED INVESTEE

| | Group Interest % | Consolidated 2006/07 Rs.'000 | 2005/06 Rs.'000 | Company 2006/07 Rs.'000 | 2005/06 Rs.'000 |
|--|------------------------|------------------------------------|--------------------|-------------------------------|--------------------|
| Unquoted | | | | | |
| Browns Dimo Industrial Products (Pvt) Ltd. | | | | | |
| 675,000 ordinary shares of Rs. 10/- each | 45 | 6,750 | 6,750 | 6,750 | 6,750 |
| Group share of net assets | | 14,979 | 12,321 | — | — |
| Group investment in equity accounted investee | | 21,729 | 19,071 | 6,750 | 6,750 |

The principal activity of the Company is given on page 78.

13. INVESTMENTS IN JOINT VENTURE

| | Company 2006/07 Rs.'000 | 2005/06 Rs.'000 |
|------------------------------------|-------------------------------|--------------------|
| DIMO KLN Industries (Private) Ltd. | 6,000 | — |
| | 6,000 | — |

The Company invested Rs. 6 mn in Dimo KLN Industries (Pvt) Ltd. which is a joint venture between the Company and KLN Engineering Product (Pvt) Ltd. to manufacture filters for automobiles.

14. OTHER LONG-TERM INVESTMENTS

| | Consolidated 2006/07 Rs. '000 | 2005/06 Rs. '000 | Company 2006/07 Rs. '000 | 2005/06 Rs. '000 |
|--|-------------------------------------|---------------------|--------------------------------|---------------------|
| Quoted | | | | |
| Hunas Falls Hotels Ltd. - 900 (31.03.06 - 900) ordinary shares of Rs. 10/- each (Market value as at 31.03.07 - Rs. 31,725/-) | 14 | 14 | 7 | 7 |
| Hatton National Bank Ltd. - 10,000 (31.03.06 - 10,000) non-voting ordinary shares of Rs. 10/- each (Market value as at 31.03.07 - Rs. 477,500/-) | 700 | 700 | 700 | 700 |
| Hayleys Ltd. - 539,599 (31.03.06 - 539,599) ordinary shares of Rs. 10/- each (Market value as at 31.03.07 - Rs. 76,623,058/-) | 40,964 | 40,964 | 40,964 | 40,964 |
| | 41,678 | 41,678 | 41,671 | 41,671 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

15. INVENTORIES

| | Consolidated | | Company | |
|-----------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Stock in trade & work-in-progress | 2,126,870 | 1,608,933 | 2,038,586 | 1,532,712 |
| Provision for slow moving stock | (40,450) | (48,647) | (36,072) | (44,516) |
| | 2,086,420 | 1,560,286 | 2,002,514 | 1,488,196 |
| Goods-in-transit | 10,708 | 1,265 | 3,168 | 1,265 |
| | 2,097,128 | 1,561,551 | 2,005,682 | 1,489,461 |

16. TRADE AND OTHER RECEIVABLES

| | Consolidated | | Company | |
|------------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Trade receivables | 1,670,724 | 1,933,890 | 1,388,775 | 1,753,560 |
| Provision for bad debts | (77,855) | (79,492) | (50,953) | (52,849) |
| | 1,592,869 | 1,854,398 | 1,337,822 | 1,700,711 |
| Deposits against imports | 215,750 | 196,153 | 214,260 | 196,153 |
| Deposits and prepayments | 72,322 | 72,975 | 59,870 | 59,907 |
| National Security Levy recoverable | 11,930 | 11,930 | 11,294 | 11,294 |
| Non-trade receivables | 24,279 | 23,913 | 16,233 | 22,102 |
| Loans to employees (Note 16.1) | 2,594 | 3,270 | 2,344 | 3,025 |
| | 1,919,744 | 2,162,639 | 1,641,823 | 1,993,192 |

16.1 Loans to Employees (amount granted over Rs. 20,000/-)

The movement of loans disbursed to employees exceeding Rs. 20,000/- are given below, as per Section 201 (2) of the Companies Act No. 17 of 1982.

Loans over Rs. 20,000/- were granted to 212 employees during the year within the Group (174 employees in 2005/06).

| | Consolidated | | Company | |
|---------------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Balance at the beginning of the year | 1,872 | 1,630 | 1,743 | 1,536 |
| Granted during the year | 4,865 | 4,027 | 4,354 | 3,578 |
| | 6,737 | 5,657 | 6,097 | 5,114 |
| Repaid during the year | (4,277) | (3,785) | (3,887) | (3,371) |
| Balance at the end of the year | 2,460 | 1,872 | 2,210 | 1,743 |

16.2 No Loans have been granted to the Directors of the Company.

17. CASH & CASH EQUIVALENTS

| | Consolidated | | Company | |
|------------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Bank balances | 171,331 | 66,640 | 170,512 | 66,484 |
| Cash in hand | 5,059 | 3,458 | 5,009 | 3,458 |
| Cash & cash equivalents | 176,390 | 70,098 | 175,521 | 69,942 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

18. CAPITAL AND RESERVES

| | Consolidated | | Company | |
|--------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Share Capital | | | | |
| Issued and fully paid up | 121,000 | 100,000 | 121,000 | 100,000 |
| Capital Reserves | | | | |
| Share premium | 61,500 | 27,500 | 61,500 | 27,500 |
| Reserve on revaluation of land | 311,522 | 311,522 | 311,522 | 311,522 |
| | 373,022 | 339,022 | 373,022 | 339,022 |
| General Reserves | 642,908 | 472,908 | 573,082 | 423,082 |

The General Reserves represent reserves available for distribution.

Authorised Share Capital

The authorised share capital comprises 20,000,000 ordinary shares. All shares have a par value of Rs. 10/-.

Issued Share Capital

| | Number of Ordinary Shares in Issue | |
|----------------------|---------------------------------------|-------------------|
| | 2007 | 2006 |
| At 01.04.2006 | 10,000,000 | 10,000,000 |
| Scrip Issue | 1,000,000 | – |
| Rights Issue | 1,100,000 | – |
| At 31.03.2007 | 12,100,000 | 10,000,000 |

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at Annual General Meetings of the Company.

19. INTEREST-BEARING LOANS AND BORROWINGS

Non-current portion of the interest bearing loans and borrowings:

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Term Loan (19.1) | 334,032 | 384,200 | 334,032 | 384,200 |
| Finance lease obligations (19.2) | 11,514 | – | 11,514 | – |
| | 345,546 | 384,200 | 345,546 | 384,200 |
| Current portion of the interest bearing loans and borrowings: | | | | |
| Term Loan (19.1) | 143,533 | 111,600 | 143,533 | 111,600 |
| Finance lease obligations (19.2) | 14,999 | – | 14,999 | – |
| | 158,532 | 111,600 | 158,532 | 111,600 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

19.1 Term Loan (Unsecured)

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Non-Current | | | | |
| At the beginning of the year | 495,800 | 135,000 | 495,800 | 135,000 |
| Unsecured bank loan - obtained | 117,670 | 450,000 | 117,670 | 450,000 |
| | 613,470 | 585,000 | 613,470 | 585,000 |
| Repayments during the year | (135,905) | (89,200) | (135,905) | (89,200) |
| At the end of the year | 477,565 | 495,800 | 477,565 | 495,800 |
| Transferred to current liabilities (repayable within one year) | 143,533 | 111,600 | 143,533 | 111,600 |
| Non-current portion of the long-term loan | 334,032 | 384,200 | 334,032 | 384,200 |

Analysis of loans is as follows:

| | Amount Rs. '000 | Within 1 year Rs. '000 | 1-2 year Rs. '000 | 2-5 year Rs. '000 | 31.03.07 Rs. '000 | 31.03.06 Rs. '000 |
|--------------------------------|--------------------|---------------------------|----------------------|----------------------|----------------------|----------------------|
| LENDER | | | | | | |
| Sampath Bank Ltd. | 150,000 | 30,000 | 30,000 | 15,000 | 75,000 | 105,000 |
| Commercial Bank of Ceylon Ltd. | 350,000 | 69,600 | 69,600 | 89,000 | 228,200 | 297,800 |
| Hatton National Bank Ltd. | 217,670 | 43,933 | 43,933 | 86,499 | 174,365 | 93,000 |
| | 717,670 | 143,533 | 143,533 | 190,499 | 477,565 | 495,800 |

These loans were obtained on a clean basis and is repayable in 60 equal monthly instalments.

19.2 Finance Lease Obligations

| | Consolidated | | Company | |
|---|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| At the beginning of the year | — | — | — | — |
| Obtained during the year | 51,274 | — | 51,274 | — |
| Repayments during the year | (19,860) | — | (19,860) | — |
| At the end of the year | 31,414 | — | 31,414 | — |
| Finance charges unamortised | (4,901) | — | (4,901) | — |
| | 26,513 | — | 26,513 | — |
| Transferred to current liabilities (repayable within one year) | 14,999 | — | 14,999 | — |
| Non-current portion of finance lease obligation | 11,514 | — | 11,514 | — |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

Analysis of finance lease obligations by year of repayment

| | Consolidated | | Company | |
|---------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Payable within one year | | | | |
| Gross lease liability | 17,772 | — | 17,772 | — |
| Finance charges unamortised | (2,773) | — | (2,773) | — |
| | 14,999 | — | 14,999 | — |
| Payable within one to two years | | | | |
| Gross lease liability | 13,642 | — | 13,642 | — |
| Finance charges unamortised | (2,128) | — | (2,128) | — |
| | 11,514 | — | 11,514 | — |

The finance lease obligations relates to assets acquired on sale and lease back terms. The excess of sales proceeds over carrying amount (gain), on the transaction has been deferred and amortised to the financial statement over the lease period. The unamortised gain is classified as deferred income. The Assets acquired on finance lease have been given out on hire purchase terms.

20. DEFERRED TAX ASSETS & LIABILITIES

20.1 Deferred Tax Liabilities

| | Consolidated | | Company | |
|--------------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Balance at the beginning of the year | 34,616 | 33,990 | 34,616 | 34,013 |
| Transfer from/(to) Income Statement | (3,289) | 839 | (3,289) | 603 |
| Balance at the end of the year | 31,327 | 34,829 | 31,327 | 34,616 |

20.2 Deferred Tax Assets

| | Consolidated | |
|--------------------------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Balance at the beginning of the year | (213) | — |
| Transfer from/(to) Income Statement | 686 | — |
| Balance at the end of the year | 473 | — |

The deferred tax asset is arising from temporary differences. No comparative figure is available as there were no deferred tax assets in the previous year.

21. DEFERRED INCOME

| | Consolidated | | Company | |
|---------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| At the beginning of the year | 932 | 1,441 | 932 | 1,441 |
| Income deferred during the year | 4,570 | — | 4,570 | — |
| Amortised during the year | (2,284) | (509) | (2,284) | (509) |
| Balance at the end of the year | 3,218 | 932 | 3,218 | 932 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

22. RETIREMENT BENEFIT OBLIGATIONS

| | Consolidated | | Company | |
|--|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Provision for Retiring Gratuity | | | | |
| Balance at the beginning of the year | 76,981 | 67,606 | 70,445 | 61,665 |
| Charge for the year | 20,008 | 13,401 | 19,349 | 12,806 |
| Payments during the year | (3,236) | (4,026) | (3,091) | (4,026) |
| Balance at end of the year | 93,753 | 76,981 | 86,703 | 70,445 |

23. TRADE AND OTHER PAYABLES

| | Consolidated | | Company | |
|-------------------------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Trade payables | 380,725 | 83,028 | 364,006 | 79,089 |
| Advances received | 33,258 | 72,895 | 33,258 | 72,895 |
| Payable due to subsidiaries | — | — | 467 | 441 |
| Interest payable | 1,070 | 23,719 | 1,070 | 23,719 |
| Unclaimed dividend | 2,284 | 2,347 | 2,284 | 2,347 |
| VAT/Turnover tax payable | 67,704 | 73,885 | 64,269 | 72,830 |
| Other payables and accrued expenses | 101,096 | 135,635 | 87,398 | 131,227 |
| | 586,137 | 391,509 | 552,752 | 382,548 |

24. SHORT-TERM INTEREST BEARING BORROWINGS

| | Consolidated | | Company | |
|-----------------------|---------------------|---------------------|---------------------|---------------------|
| | 2006/07 Rs. '000 | 2005/06 Rs. '000 | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Short-term bank loans | 2,218,243 | 2,281,918 | 2,145,342 | 2,238,698 |
| Bank overdrafts | 142,367 | 18,440 | 130,391 | 15,001 |
| | 2,360,610 | 2,300,358 | 2,275,733 | 2,253,699 |

Unutilised short-term loans and overdraft facilities as at 31st March 2007 amounted to Rs. 1,692,888,545/-.

Inventories & book debts amounting to Rs. 95,000,000/- are pledged as securities for current interest-bearing loans and borrowings.

25. CONTINGENT LIABILITIES

The contingent liability as at 31st March 2007 on guarantees given by Diesel & Motor Engineering Co. Ltd. to third parties in respect of bid bonds and performance bonds amounted to Rs. 356,600,952/- (2005/06 - Rs. 78,933,423/-).

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

26. DIRECTORS' INTEREST IN CONTRACTS

26.1 Directors' Interest in Contracts with the Company

The Directors of the Company are also Directors of the following companies:

| Name of the Company | Name of the Directors | Relationship |
|--|---------------------------|---|
| Diesel & Motor Engineering Company Ltd. | Mr. A.R. Pandithage | Chairman, Managing Director/ Chief Executive Officer |
| | Mr. A.G. Pandithage | Deputy Chief Executive Officer |
| | Mr. A.N. Algama | Director |
| | Mr. S.C. Algama | Director |
| | Mr. T.G.H. Peries | Director |
| | Mr. R.C. Weerawardane | Director |
| | Mr. B.C.S.A.P. Gooneratne | Director |
| Dimo Ltd. | Mr. A.R. Pandithage | Chairman |
| | Mr. S.C. Algama | Director |
| | Mr. A.G. Pandithage | Director |
| | Mr. R.C. Weerawardane | Director |
| | Mr. B.C.S.A.P. Gooneratne | Director |
| Dimo Travels Ltd. | Mr. A.R. Pandithage | Chairman |
| | Mr. S.C. Algama | Director |
| Dimo Industries Ltd. | Mr. A.R. Pandithage | Chairman |
| | Mr. S.C. Algama | Director |
| | Mr. A.G. Pandithage | Director |
| | Mr. R.C. Weerawardane | Director |
| | Mr. B.C.S.A.P. Gooneratne | Director |
| Dimo KLN Industries (Pvt) Ltd. | Mr. A.R. Pandithage | Chairman |
| | Mr. R.C. Weerawardane | Director |
| Browns Dimo Industrial Products (Pvt) Ltd. | Mr. A.R. Pandithage | Deputy Chairman |
| | Mr. R.C. Weerawardane | Director |

26.2 The Company has entered into contracts in the normal course of business with the following companies in which a Director of the Company is also a Director of the said Company.

| Name of the Company | Name of the Directors | Nature of Transaction | Value Rs. |
|-----------------------------------|-----------------------|-----------------------------------|-----------|
| Air Global Ltd. | Mr. A.M. Pandithage | Air passage | 9,011,925 |
| Global Holidays (Pvt) Ltd | Mr. A.M. Pandithage | Air passage | 7,120,858 |
| Hayleys Consumer Products Ltd. | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Purchases of consumer items | 2,913,525 |
| Hayleys Advantis Ltd. | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Sales of lighting & power tools | 1,707,575 |
| Hayleys - MGT Knitting Mills Ltd. | Mr. R.A. Ebell | Services of forklift & telephones | 995,505 |
| MIT Cargo (Pvt) Ltd. | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Services of shipping & warehouse | 942,123 |
| Logiwiz Ltd. | Mr. A.M. Pandithage | Services of storage & delivery | 878,219 |

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

| Name of the Company | Name of the Directors | Nature of Transaction | Value |
|-----------------------------------|-----------------------|---|---------|
| Hayleys Industrial Solutions Ltd. | Mr. R.A. Ebell | Sales of power tools & telephone system & services telephones | 613,008 |
| N Y K Line Lanka (Pvt) Ltd. | Mr. A.M. Pandithage | Services of storage & delivery | 271,788 |
| Haytrans Lanka Ltd. | Mr. A.M. Pandithage | Services for freight forwarding | 251,784 |
| Hayleys Industrial Solutions Ltd. | Mr. A.M. Pandithage | Generator sevices | 225,124 |
| Hayleys ADC Textile Ltd. | Mr. R.A. Ebell | Hiring fork-lift | 101,601 |
| Hayleys Ltd. | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Sales of UPS & tyres | 95,744 |
| Ravi Industries Group | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Sales of spare parts | 59,915 |
| Clarion Shipping (Pvt) Ltd. | Mr. A.M. Pandithage | Services for shipping facilities | 28,557 |
| Toyo Cushion Lanka (Pvt) Ltd. | Mr. A.M. Pandithage | Maintainance | 26,677 |
| Hayleys Ltd. | Mr. R.A. Ebell | | |
| | Mr. A.M. Pandithage | Training carried out | 14,338 |
| Haychem Ltd. | Mr. R.A. Ebell | Sales of spare parts | 7,607 |
| Hayleys Electronic Ltd | Mr. R.A. Ebell | Purchases of electronic items | 5,164 |

26.3 Mr. A.R. Pandithage, a Director of Diesel & Motor Engineering Co. Ltd. has entered into a contract of leasing in respect of following residential premises to the Company:

| Lessor | Premises | Monthly Rental |
|-----------------|---|----------------|
| A.R. Pandithage | No. 11/2, Sri Sunandarama Road, Kalubowila | Rs. 2,528/- |

27. RELATED PARTIES

(a) Transactions with Subsidiaries, Associates and Joint Ventures

| Name of the Company | Nature of Relationship | Percentage of Share-holding | Balance as at end of the year | |
|-------------------------------------|------------------------|-----------------------------|-------------------------------|---------------------|
| | | | 2006/07 Rs. '000 | 2005/06 Rs. '000 |
| Dimo Ltd. | Subsidiary | 100% | 127,903 | 88,894 |
| Dimo Industries (Pvt) Ltd. | Subsidiary | 100% | 39,713 | 12,365 |
| Dimo Travels Ltd. | Subsidiary | 100% | (467) | (440) |
| Browns Dimo Industrial Products Ltd | Associates | 45% | Nil | Nil |
| Dimo KLN Industries (Pvt) Ltd. | Joint Venture | — | 6,587 | Nil |

Inter-company transactions were carried out at arm's length basis in the normal course of business operations.

The Gurantees & Letter of Credit taken on behalf of Dimo Ltd. amounted to Rs. 78,368,557/-.

The transactions with Hayleys Ltd. which owns 28% of Company shares is disclosed in Note 26.2. Transactions with all other entities which are controlled by Hayleys Ltd. have been carried out at arm's length in the normal course of business and is also disclosed in Note 26.2 to the Financial Statements.

There has been no provision made for bad & doubtful debts or write-off against any related parties.

NOTES TO THE FINANCIAL STATEMENTS (CONTD.)

(b) Transactions with key management personnel & their close family members

Key management personnel includes members of the Board of Directors of the Company, its subsidiaries, associates and joint ventures.

The Directors emoluments for the year ending 31st March 2007 amounted to Rs. 30 mn (2005/06 - Rs. 20 mn).

There are no long-term, post employment, terminal benefits and share based payments made to the Directors during the year

There have been no transactions made with key management personnel other than those disclosed in Note 26 to the Financial Statements.

Close family members of key management personnel have had no transactions with the Company during the year.

Diesel & Motor Engineering Co. Ltd. provides office space & services such as accounting, secretarial, personnel and other back office services to subsidiary companies and the cost incurred in the provision of such facilities has been recovered.

Certain products manufactured by Browns Dimo Industrial Products (Pvt) Ltd., are marketed by Diesel & Motor Engineering Co. Ltd.

The Company has made sales amounting to Rs. 91,666/- to Browns Dimo Industries (Pvt) Ltd. during the year in respect of sale and repairs to pumps & power tools. Total value of products purchased by Diesel & Motor Engineering Co. Ltd. during the year amounted to Rs. 25,280,978/-.

Directors of the Company and their spouses control 28% of the voting shares of the Company. The Directors shareholding is given in the Directors' Report appearing on pages 78 to 80.

There are no related parties or related party transactions other than the above and those disclosed in Note 26 to the Financial Statements.

28. WARRANTIES

Warranties extended to products marketed by the Group are limited to those given by the respective manufacturers.

29. GROUP ENTERPRISES

The Parent Company of the Group is Diesel & Motor Engineering Company Co. Ltd., which has fully-owned subsidiaries namely Dimo Ltd., Dimo Travels Ltd. and Dimo Industries Ltd. and associate company Browns Dimo Industrial Products (Pvt) Ltd. Dimo KLN Industries (Pvt) Ltd. is a joint venture under Diesel & Motor Engineering Co. Ltd. There is no ultimate holding company for Diesel & Motor Engineering Co. Ltd.

30. COMMITMENTS

Capital expenditure commitments as at 31st March 2007 amounted to Rs. 1,295,005/- (2005/06 - Rs. 2,596,238/-).

31. EVENTS OCCURRING AFTER BALANCE SHEET DATE

No events have been arisen since the Balance Sheet date which would require adjustment to or disclosure in the financial statements.

The Companies Act No. 7 of 2007 was enacted with effect from 3rd May 2007. The Board has taken the necessary initiatives for a smooth transition to the new regime. As required by Section 485 (5) (b) of the Act, the Company is deemed to have changed its name to Diesel & Motor Engineering PLC.

TEN YEAR SUMMARY

| Year ended 31st March | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|------------|------------|
| | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 | Rs.'000 |
| Trading Results | | | | | | | | | | |
| Group turnover | 1,461,643 | 1,592,399 | 1,494,939 | 2,686,939 | 1,843,662 | 3,404,734 | 4,796,905 | 7,565,327 | 10,512,326 | 12,989,916 |
| Profit before taxation | 43,603 | 73,961 | 115,140 | 119,992 | 38,753 | 58,912 | 148,396 | 253,633 | 382,235 | 512,895 |
| Taxation | (19,243) | (28,122) | (36,762) | (46,102) | (10,523) | (20,119) | (48,131) | (76,431) | (117,062) | (211,118) |
| Profit after taxation | 24,360 | 45,839 | 78,378 | 73,890 | 28,230 | 38,793 | 100,265 | 177,202 | 265,173 | 301,777 |
| Assets | | | | | | | | | | |
| Non-current assets | 462,265 | 454,933 | 454,940 | 480,468 | 517,030 | 528,826 | 559,752 | 734,720 | 775,323 | 1,005,370 |
| Current assets | 791,706 | 739,792 | 786,502 | 803,832 | 952,905 | 1,197,756 | 1,692,349 | 2,460,687 | 3,794,288 | 4,193,262 |
| | 1,253,971 | 1,194,725 | 1,241,442 | 1,284,300 | 1,469,935 | 1,726,582 | 2,252,101 | 3,195,407 | 4,569,611 | 5,198,632 |
| Equity & Liabilities | | | | | | | | | | |
| Capital | 48,000 | 48,000 | 48,000 | 60,000 | 60,000 | 60,000 | 90,000 | 100,000 | 100,000 | 121,000 |
| Reserves | 371,340 | 402,779 | 466,757 | 504,647 | 514,877 | 553,670 | 652,435 | 905,858 | 1,116,031 | 1,385,508 |
| Shareholders' funds | 419,340 | 450,779 | 514,757 | 564,647 | 574,877 | 613,670 | 742,435 | 1,005,828 | 1,216,031 | 1,506,508 |
| Non-current liabilities | 152,743 | 213,924 | 61,923 | 69,049 | 73,824 | 79,589 | 94,909 | 208,037 | 496,942 | 473,844 |
| Current liabilities | 681,888 | 530,022 | 664,762 | 650,604 | 821,234 | 1,033,323 | 1,414,757 | 1,981,512 | 2,856,638 | 3,218,280 |
| | 1,253,971 | 1,194,725 | 1,241,442 | 1,284,300 | 1,469,935 | 1,726,582 | 2,252,101 | 3,195,407 | 4,569,611 | 5,198,632 |
| Cash Flows | | | | | | | | | | |
| Operating activities | 15,204 | 20,714 | 87,912 | 88,131 | (102,684) | (153,014) | (39,915) | (587,299) | (990,433) | 383,134 |
| Investing activities | (19,755) | (11,542) | (15,746) | (53,658) | (56,104) | (57,827) | (75,584) | (97,584) | (91,474) | (287,636) |
| Financing activities | 221,229 | (56,729) | (108,476) | (201,671) | (12,640) | (17,488) | 26,434 | 92,125 | 305,800 | (49,458) |
| | 216,678 | (47,557) | (36,310) | (167,198) | (171,428) | (228,329) | (89,065) | (592,758) | (776,107) | 46,040 |
| Key Indicators | | | | | | | | | | |
| Earnings per share (Rs.) (*) (**) | 2.11 | 3.97 | 6.79 | 6.40 | 2.44 | 3.36 | 8.68 | 15.34 | 22.96 | 25.76 |
| Net assets per share | | | | | | | | | | |
| at year end (Rs.) | 87.36 | 93.91 | 107.24 | 94.11 | 95.81 | 102.28 | 82.49 | 100.59 | 101.60 | 124.50 |
| Market value per share at | | | | | | | | | | |
| year end (Rs.) | 50.00 | 35.00 | 39.00 | 38.00 | 30.00 | 50.00 | 53.00 | 103.00 | 138.50 | 120.00 |
| Return on average shareholders' equity (%) | 6 | 11 | 16 | 14 | 5 | 7 | 15 | 20 | 24 | 22 |
| Dividends proposed/declared (Rs.) | 9,600 | 14,400 | 14,400 | 24,000 | 18,000 | 18,000 | 31,500 | 50,000 | 60,000 | 72,600 |
| Dividends cover (time covered) | 3 | 3 | 5 | 3 | 2 | 2 | 3 | 4 | 4 | 4 |
| Price earnings ratio (times) | 24 | 9 | 6 | 6 | 12 | 15 | 6 | 7 | 6 | 5 |
| Dividend per share | 2.00 | 3.00 | 3.00 | 4.00 | 3.00 | 3.00 | 3.50 | 5.00 | 6.00 | 6.00 |
| Annual sales growth (%) | 17 | 9 | (6) | 80 | (31) | 85 | 41 | 58 | 39 | 24 |
| Current ratio (time) | 1.16 | 1.39 | 1.18 | 1.24 | 1.16 | 1.16 | 1.20 | 1.24 | 1.33 | 1.30 |

* Scrip issue of one share for every four shares held was made during the year 2000/01. Scrip issue of one share for every nine shares held was made during the year 2004/05. Scrip issue of one share for every ten shares was made during the year 2006/07.

** Rights issue of one ordinary share for every two ordinary shares held was made in August 2003. Rights issue of one ordinary share per every ten ordinary shares held was made during the year 2006/07. Earning per share has been adjusted accordingly.

SHARE INFORMATION

1. STOCK EXCHANGE LISTING

The issued ordinary shares of Diesel & Motor Engineering PLC, are listed with the Colombo Stock Exchange of Sri Lanka. The audited Consolidated Income Statements for the year ended 31st March 2007 and the audited Balance Sheets at that date have been submitted to the Colombo Stock Exchange within three months of the Balance Sheet date.

2. SHAREHOLDERS

The number of Shareholders as at 31st March 2007 was 1,137 (887 as at 31st March 2006).

| Number of Shares held | Residents | | | Non-Residents | | | Total | | |
|-----------------------|----------------------|-------------------|--------------|----------------------|------------------|--------------|----------------------|-------------------|---------------|
| | No. of Share-holders | No. of Shares | % | No. of Share-holders | No. of Shares | % | No. of Share-holders | No. of Shares | % |
| 1 - 500 | 780 | 94,190 | 0.78 | 4 | 877 | 0.01 | 784 | 95,067 | 0.79 |
| 501 - 5,000 | 254 | 383,159 | 3.17 | 6 | 10,889 | 0.09 | 260 | 394,048 | 3.26 |
| 5,001 - 10,000 | 24 | 174,649 | 1.44 | 3 | 20,050 | 0.17 | 27 | 194,699 | 1.61 |
| 10,001 - 20,000 | 15 | 201,778 | 1.67 | — | — | — | 15 | 201,778 | 1.67 |
| 20,001 - 30,000 | 6 | 142,040 | 1.17 | — | — | — | 6 | 142,040 | 1.17 |
| 30,001 - 40,000 | 9 | 310,554 | 2.57 | — | — | — | 9 | 310,554 | 2.57 |
| 40,001 - 50,000 | 8 | 299,048 | 2.47 | — | — | — | 8 | 344,100 | 2.47 |
| 50,001 - 100,000 | 8 | 611,967 | 5.06 | — | — | — | 8 | 611,967 | 5.06 |
| 100,001 - 1,000,000 | 17 | 5,201,562 | 42.99 | 1 | 114,759 | 0.95 | 18 | 5,316,321 | 43.94 |
| 1,000,001 & Over | 1 | 3,397,611 | 28.07 | 1 | 1,136,867 | 9.39 | 2 | 4,489,426 | 37.46 |
| Total | 1,122 | 10,816,558 | 89.39 | 15 | 1,283,442 | 10.61 | 1,137 | 12,100,000 | 100.00 |

Of the issued share capital, over 88% is held by residents of Sri Lanka.

| Categories of Shareholders | 31st March 2007 | | | 31st March 2006 | | |
|----------------------------|----------------------|-------------------|---------------|----------------------|---------------|--------|
| | No. of Share-holders | No. of Shares | % | No. of Share-holders | No. of Shares | % |
| Individuals | 1,053 | 7,030,784 | 58.11 | 818 | 5,746,734 | 57.47 |
| Institutions | 84 | 5,069,216 | 41.89 | 69 | 4,253,266 | 42.53 |
| Total | 1,137 | 12,100,000 | 100.00 | 887 | 10,000,000 | 100.00 |

3. MARKET VALUE OF SHARES

The market value of an ordinary share of Diesel & Motor Engineering PLC, as at 31st March 2007 was Rs. 120.00 (Rs. 138.50 as at 31st March 2006).

4. DIVIDEND PAYMENTS

| | 2007 Rs. mn | 2006 Rs. mn |
|---|----------------|----------------|
| Interim dividend - Rs. 3/- per share | 36 | 30 |
| Proposed & final dividend - Rs. 3/- per share | 36 | 30 |

Final dividend to be declared on 20th June 2007

Final dividend to be payable on 27th June 2007

SHARE INFORMATION (CONTD.)

5. SHARE TRADING INFORMATION FROM 1ST APRIL TO 31ST MARCH

| | 2007 | 2006 | 2005 | 2004 |
|------------------------------|-------------------------------|-----------------------|-----------------------|-----------------------|
| Highest (Rs.) | 155.00 (Jun. 20, 2006) | 153.00 (Feb. 6, 2006) | 150.00 (Jan. 4, 2005) | 99.00 (July 23, 2003) |
| Lowest (Rs.) | 100.00 (Dec. 29, 2006) | 102.25 (Jan. 5, 2006) | 50.00 (Apr. 6, 2004) | 40.00 (Feb. 10, 2004) |
| No. of transactions | 902 | 2,241 | 1,536 | 555 |
| No. of shares traded | 400,000 | 1,249,300 | 728,000 | 360,300 |
| Value of shares traded (Rs.) | 50,471,950 | 163,854,550 | 66,423,875 | 27,503,400 |
| No. of days traded | 197 | 213 | 174 | 149 |
| No. of market days | 240 | 241 | 234 | 241 |
| Liquidity (%) | 3.31 | 12.49 | 7.28 | 4.00 |
| CSE All Share Price Index | 2,789.8 | 2,264.40 | 1,751.88 | 1,284.2 |
| Milanka Price Index | 3,837.6 | 2,877.70 | 2,392.19 | 2,021.00 |
| Motor Sector | 3,360.9 | 2,067.3 | 1,153.75 | 604.80 |

6. PUBLIC SHAREHOLDING

| | | | | |
|------------------|------------------|-----------|-----------|-----------|
| Number of Shares | 5,302,892 | 3,388,464 | 3,373,364 | 3,011,887 |
| % | 43.83 | 33.88% | 33.73% | 33.47% |

7. HISTORY OF SHARE ISSUES

| Year | Issue | No. of Shares | Price |
|---------|--|---------------|-----------|
| 2006/07 | Rights (one share per every ten shares held) | 1,100,000 | Rs. 55.00 |
| 2006/07 | Bonus (one share per every ten shares held) | 1,000,000 | Nil |
| 2004/05 | Bonus (one share per every nine shares held) | 1,000,000 | Nil |
| 2003/04 | Rights (one share for every two shares held) | 3,000,000 | Rs. 20.00 |
| 2000/01 | Bonus (one share per every four shares held) | 1,200,000 | Nil |
| 1995/96 | Bonus (one share per every three shares held) | 1,200,000 | Nil |
| 1994/95 | Bonus (one share per every five shares held) | 600,000 | Nil |
| 1992/93 | Rights (one share for every five shares held) | 500,000 | Rs. 75.00 |
| 1991/92 | Rights (one share for every three shares held) | 500,000 | Rs. 30.00 |
| 1991/92 | Bonus (one share per every four shares held) | 500,000 | Nil |
| 1989/90 | Rights (one share for every two shares held) | 500,000 | Rs. 10.00 |
| 1987/88 | Bonus (one share per every share held) | 500,000 | Nil |
| 1980/81 | Bonus (one share per every share held) | 250,000 | Nil |

SHARE INFORMATION (CONTD.)

8. CHANGES IN SHAREHOLDINGS OF DIRECTORS AND THEIR SPOUSES DURING 2006/2007

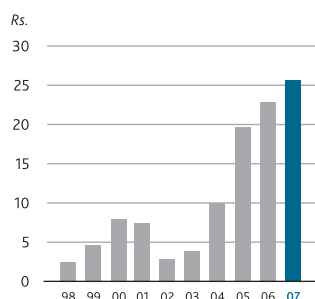
| Name | As at 31.03.06 | Movement | As at 31.03.07 | % |
|-----------------|----------------|----------|------------------|-------|
| A.R. Pandithage | 1,515,134 | 359,527 | 1,874,661 | 15.49 |
| A.N. Algama | 140,150 | 47,305 | 187,455 | 1.55 |
| S.C. Algama | 316,280 | 82,854 | 399,134 | 3.30 |
| A.G. Pandithage | 300,754 | 82,791 | 383,545 | 3.17 |
| A.M. Pandithage | 199,735 | 20,043 | 219,778 | 1.82 |
| T.G.H. Peries | 299,932 | 34,992 | 334,924 | 2.77 |
| | 2,771,985 | 627,512 | 3,399,497 | 28.10 |

9. MAJOR SHAREHOLDERS AS AT

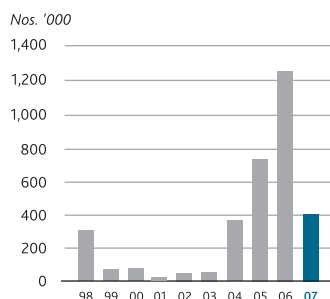
| Name of Shareholder | 31st March 2007 | | Name of Shareholder | 31st March 2006 | |
|--|------------------|--------------|---|-----------------|-------|
| | Total Shares | % | | Total Shares | % |
| Hayleys Ltd. | 3,397,611 | 28.08 | Hayleys Ltd. | 2,807,944 | 28.08 |
| Thurston Investments Ltd. | 1,136,867 | 9.40 | Thurston Investments Ltd. | 1,031,607 | 10.32 |
| Mr. A.R. Pandithage | 971,798 | 8.03 | Mr. A.R. Pandithage | 786,610 | 7.87 |
| Mrs. J.C. Pandithage | 902,863 | 7.46 | Mrs. J.C. Pandithage | 728,524 | 7.29 |
| Mr. A.K. Pandithage | 417,640 | 3.45 | Mr. A.K. Pandithage | 330,602 | 3.31 |
| Mr. S.C. Algama | 392,276 | 3.24 | Mrs. D.G. Pandithage | 320,227 | 3.20 |
| The estate of the late Mrs. D.G. Pandithage | 352,249 | 2.91 | Mr. S.C. Algama | 310,613 | 3.11 |
| Mr. A.G. Pandithage | 339,380 | 2.80 | Mr. K. Aloysius | 270,642 | 2.71 |
| Mr. K. Aloysius | 327,476 | 2.71 | Mr. A.G. Pandithage | 264,254 | 2.64 |
| Mr. T.G.H. Peries | 198,038 | 1.64 | Mr. T.G.H. Peries | 177,308 | 1.77 |
| Mr. A.N. Algama | 187,455 | 1.55 | Mr. A.M. Pandithage | 162,435 | 1.62 |
| Mr. A.M. Pandithage | 178,745 | 1.48 | The estate of the late Mr. A.A.C.A. Algama | 149,433 | 1.49 |
| The estate of the late Mr. A.A.C.A. Algama | 164,376 | 1.36 | Elgin Investments Ltd. | 148,100 | 1.48 |
| Dr. D. Jayanththa | 154,100 | 1.27 | Mr. A.N. Algama | 140,150 | 1.40 |
| Mrs. M.S. Peries | 136,886 | 1.13 | Dr. D. Jayanththa | 125,600 | 1.26 |
| Mr. L.P. Algama | 131,931 | 1.09 | Mrs. M.S. Peries | 122,624 | 1.23 |
| Mr. A.C. Pandithage | 126,332 | 1.04 | Mr. L.P. Algama | 109,035 | 1.09 |
| The estate of the late N.U. Algama | 116,515 | 0.96 | Mr. A.C. Pandithage | 96,666 | 0.97 |
| Elgin Investments Ltd. | 114,759 | 0.95 | The Estate of the late N.U. Algama | 96,294 | 0.96 |
| JB Cocoshell (Pvt) Ltd. | 103,500 | 0.86 | Mrs. G.E.M. Algama | 87,953 | 0.88 |
| | 9,850,797 | 81.41 | | 8,266,621 | 82.66 |

SHARE INFORMATION (CONTD.)

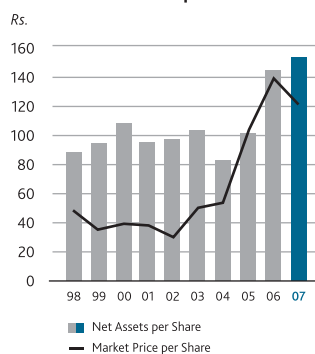
Earnings per Share



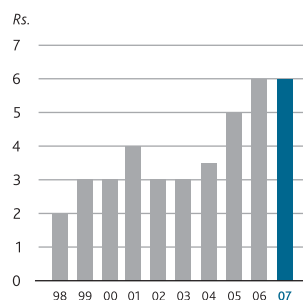
Number of Shares Traded



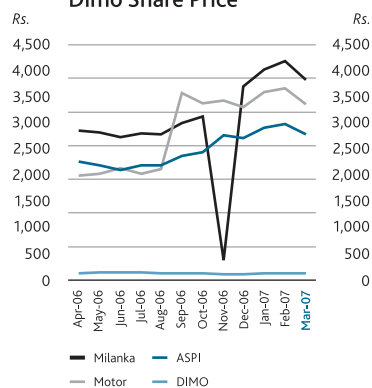
Net Assets per Share vs. Market Price per Share



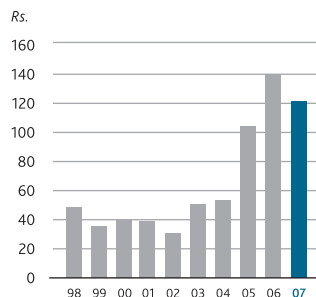
Dividends per Share



All Share, Sensitive Price & Motor Sector Index vs. Dimo Share Price



Market Price per Share



BRANCH NETWORK

Dimo continues to expand and enhance our branch network to ensure convenience to our customers.



01



06



02



07



03



08



04



09



05



10

1. Head Office,
65, Jetawana Road, Colombo 14
2. TATA Light,
Commercial Vehicle Showroom -
61, Jetawana Road, Colombo 14
3. TATA Passenger Car Showroom
and Workshop -
467, Sirimavo Bandaranaike Mawatha,
Colombo 14
4. Mercedes-Benz & Chrysler Showroom -
378 - 385, R.A. De Mel Mawatha,
Colombo 3
5. TATA Showroom -
385 A, R.A. De Mel Mawatha, Colombo 3
6. Siyambalape Complex -
135, Mahena Road, Siyambalape,
Biyagama
7. Hoarding - Kurunegala Branch -
27 A, Colombo Road, Malpitiya, Boyagane,
Kurunegala
8. Dimo Mart -
50, 51, Jetawana Road, Colombo 14
9. Matara Branch -
401, Kumaratunga Munidasa Mawatha,
Pamburana, Matara
10. Commercial & Heavy Machinery
Workshop -
562/126, D.S. Senanayake Mawatha,
Anuradhapura.

HISTORICAL NOTE

Diesel & Motor Engineering PLC, was established in 1939 as a partnership by the late Messrs. T.S. Peries, P.D. Alexander, C.A. Algama and H.A. Algama who were entrepreneurs in their own right, along with the late Mr. F.K. Heller.

The Company began operations with a staff of 29. Initially business was only confined to automobile sales and servicing. This focus continued until 1945 when DIMO was incorporated as a Private Limited Liability Company.

In 1964, DIMO was converted into a Public Quoted Company by obtaining a listing at the Colombo Brokers' Association, as it was then known. What began as an automobile sales and servicing concern in 1939, has since grown in size as well as in scope, and presently has a workforce of 862. The Company has a record of 68 years experience in the automobile and engineering industry and over the years has made a major contribution towards the development of the transportation sector in Sri Lanka.

DIMO is probably the oldest sole distributor for Mercedes-Benz Passenger and Commercial Vehicles, in the Asian Region. In Sri Lanka, DIMO is colloquially known as the "Benz Company".

Dimo Industries Ltd. and Dimo Ltd., were incorporated as wholly-owned subsidiaries in the 70's. Dimo Industries Ltd., was established to manufacture automobile parts locally, while Dimo Ltd., was for the sale and service of Telecommunications, Power Engineering and Medical equipment.

In 1986 Hayleys Group acquired approximately 37% of the equity capital making DIMO an Associate Company of it. Hayley's Group current holding is 28% of the equity. A New divisional organisational structure emerged in 1987 to support and nurture the development of the

Company and to institutionalise the corporate management process.

The Dimo automobile training school; which is the only one of its kind in the private sector was established in 1990 and sets a two-year course designed by Mercedes-Benz, to international standards.

DIMO is involved in a number of related fields and represents many prestigious principals. Daimler, TATA, Chrysler, MTU, Bosh, Komatsu, Siemens, Michelin, Osram, and Mahindra & Mahindra to name but a few. During the last two decades turnover from mere Rs.129 mn has grown to Rs.13 bn. The share capital has increased from Rs. 5 mn to Rs.121 mn through rights issues and capitalisation of reserves. The market capitalisation of the Company has increased from Rs. 518 mn to Rs.1.45 bn during this period. In 1996, the Company relocated its after sales and service workshops of commercial vehicles construction machinery and power systems at Siyambalape, Biyagama. The workshop complex is equipped with state-of-the-art machinery and equipment.

Presently, the Company's showroom and branch network include the Mercedes-Benz/Chrysler/Tata Passenger car showroom located at R.A. De Mel Mawatha.

The Dimo Mart showroom located at Jetawana Road, and the Branch offices located at Kurunegala, Matara and Anuradhapura.

The Head Office at Jetawana Road is conveniently and spaciouly located in an area of approximately 10,000 sq metres in a central commercial sector in Colombo. The complex houses the Company's administrative and sales offices, passenger car and automotive workshops with its showrooms.

In 1998, Browns Dimo Industrial Products (Pvt) Ltd., was formed to undertake the activities of Dimo Industries Ltd. and Browns Group Industrial Products Ltd, a subsidiary of Brown and Company Ltd. Dimo and Browns own 45% each of the equity of this new company whilst the balance 10% is held by the DFCC Bank.

The commencement of commercial production during the year 2006 of the tyre retreading at Homagama is another important milestone.

With the implementation of the new Companies Act, the Company is deemed to have changed its name to Diesel & Motor Engineering PLC.

1. Colombo passenger car workshop in 1970s.
2. Messrs. P.D. Alexander and T.S. Peries at Daimler AG - Germany with the first Automobile.



KEY PRINCIPALS



CHINA

Infinite Shanghai Communication
Terminals Ltd.

FRANCE

Michelin

GERMANY

Blaupunkt Werke GmbH
Bomag GmbH
Zeiss AG
Daimler AG
Drageger Medical
Hofmann Werkstatt-Technik GmbH
KHD Humboldt Wedag AG
KSB AG
Mannesmann Dematic AG
Osram GmbH
Robert Bosch GmbH
Siemens AG
Vossloh-Schwabe GmbH

INDIA

Claas India Ltd.
Delux Bearings Ltd.
Fenner(India) Ltd.
India Pistons Ltd.
KLN Engineering Products (Pvt) Ltd.
Luk India Pvt Ltd.
Mahindra & Mahindra Ltd.
Motor Industries Co. Ltd.
MRF Ltd.
Rane Brake Linings Ltd.
Shardlow India Ltd.
Tata Motors Ltd.

ITALY

VM MOTORI SPA

JAPAN

Bosch Automotive Systems Corporation
Komatsu Forklift Asia Pte Ltd.
Komatsu Used Equipment Corp.
Somatsu Zenoah

MALAYSIA

Davex Engineering (M) SDN Bhd.
PK Electronics
SiTeco Lighting (M) Sdn Beherd
SSI Schaefer Systems International Pte Ltd.

SINGAPORE

DaimlerChrysler South East Asia
Ptd Ltd.
Komatsu Asia Pte Ltd.
Siemens Ag
York International (Pvt) Ltd.

USA

BF Goodrich
Chrysler International Corporation
Humphery Systems
Snapon Tools
John Deere Marine Engineers

SWITZERLAND

Tognam

KEY PRINCIPALS (CONTD.)

PRINCIPALS REPRESENTED AND DURATION OF RELATIONSHIP

| Name | Country | Brand | No. of Years |
|--|-------------|---------------------------------|--------------|
| Daimler AG | Germany | Mercedes Benz | 68 |
| Robert Bosch GmbH | Germany | Bosch | 53 |
| KHD Humboldt Wedag AG | Germany | KHD | 47 |
| Siemens AG | Germany | Siemens | 47 |
| Tata Motors Ltd. | India | Tata | 46 |
| Komatsu Forklift Asia Pte Ltd. | Japan | Komatsu | 38 |
| KSB AG | Germany | KSB | 38 |
| Motor Industries Co. Ltd. | India | Mico | 38 |
| York International (Pvt) Ltd. | Singapore | York, Sabroe, Stal, Frick, Gram | 31 |
| Bomag GmbH | Germany | Bomag | 28 |
| Mannesmann Dematic AG | Germany | Mannesmann | 28 |
| Bosch Automotive Systems Corporation | Japan | Zexel | 23 |
| Zeiss AG | Germany | Carl Zeiss | 22 |
| mtu Friedrichshafen GmbH | Germany | Mtu | 20 |
| Tognam | Switzerland | Mtu/DDC | 20 |
| Mahindra & Mahindra Ltd. | India | Mahindra | 17 |
| Michelin | France | Michelin | 14 |
| Osram GmbH | Germany | Osram | 13 |
| Rane Brake Linings Ltd. | India | Rane | 13 |
| Blaupunkt Werke GmbH | Germany | Blaupunkt | 12 |
| DaimlerChrysler South East Asia Ptd Ltd. | Singapore | Mercedes-Benz/Chrysler/Jeep | 12 |
| India Pistons Ltd. | India | IPL | 12 |
| Luk India Pvt Ltd. | India | LUK | 12 |
| KLN Engineering Products (pvt) Ltd. | India | KLN | 11 |
| Shardlow India Ltd. | India | Shardlow | 11 |
| Fenner (India) Ltd. | India | Fenner & Pioneer | 10 |
| PK Electronics | Malaysia | PK | 10 |
| Rane Engine Valves Ltd. | India | Evi | 10 |
| Vossloh-Schwabe GmbH | Germany | VS | 10 |
| Bimetal Bearings Ltd. | India | Bimite | 9 |
| Humphery | USA | Humphery | 8 |
| SiTeco Lighting (M) Sdn Beherd | Malaysia | SiTeco | 8 |
| BF Goodrich | USA | BF Goodrich | 7 |
| Infinite Shanghai Communication Terminals Ltd. | China | Siemens | 6 |
| John Deere Marine Engineers | USA | John Deere | 6 |
| MRF | India | MRF | 6 |
| Davex Engineering (M) SDN Bhd | Malaysia | Davis | 5 |
| Drager Medical | Germany | Draeger | 5 |
| Interpower International Ltd. | UK | Interpower | 5 |
| Power Source International Pte. Ltd. | Singapore | Europower | 5 |
| SSI Schaefer Systems International Pte Ltd. | Malaysia | Schaefer | 5 |
| Akzo Nobel Coatings India Pvt Ltd. | India | International | 4 |
| Claas India Ltd. | India | CLAAS | 4 |
| Chrysler International Corporation | USA | Chrysler | 3 |
| Everdigm | South Korea | Rhino | 3 |
| Komatsu Used Equipments Corp. | Japan | Komatsu | 3 |
| Komatsu Zenoah | Japan | Komatsu Zenoah | 2 |
| Schwing Stetter | India | Stetter | 2 |
| Gabriel India Ltd. | India | Gabriel | 1 |
| I.O.L. TEC | France | I.O.L. TEC | 1 |
| Snapon Tools | USA | Hoffmann/JBC | 1 |
| Wartsila India Ltd. | India | Wartsila | 1 |
| Bhagat Forge Ltd. | India | Bhagat Forge | 1 |
| Bosch Chassies Systems India Ltd. | India | KBX | 1 |
| Eicher Dem (Eicher Motors Ltd.) | India | Eicher Dem | 1 |
| Sri Bhavan Castings Ltd. | India | SBP | 1 |
| Victor Gaskets India Ltd. | India | Victor | 1 |
| VM MOTORI S.P.A | Italy | VM MOTORI | 1 |

COUNTRY INFORMATION



PHYSICAL FEATURES

| | |
|--------------------|---------------------|
| Total area | 65,610 Sq. K.M. |
| Land area | 62,705 Sq. K.M. |
| Capital | Sri Jayawardenapura |
| Commercial Capital | Colombo |

| | 2006 | 2005 | 2004 | 2003 | 2002 |
|---|---------|---------|---------|---------|---------|
| DEMOGRAPHICS | | | | | |
| Mid-year population (mn persons) | 19.8 | 19.7 | 19.5 | 19.3 | 19.0 |
| Labour force (mn persons) | 7.5 | 8.1 | 8.0 | 7.6 | 7.1 |
| Labour force participation rate (%) | 51.2 | 48.3 | 48.6 | 48.9 | 50.3 |
| Unemployment rate (% of labour force) | 6.5 | 7.7 | 8.3 | 8.4 | 8.8 |
| KEY ECONOMIC INDICATORS | | | | | |
| GDP at market price (Rs. bn) | 2,802 | 2,366 | 2,029 | 1,761 | 1,582 |
| GDP per capita (US \$) | 1,197 | 1,197 | 1,030 | 948 | 870 |
| GDP growth (%) | 7.4 | 6.0 | 5.4 | 6 | 4 |
| Inflation rate (%) | 13.7 | 11.6 | 7.6 | 6.3 | 9.6 |
| Fiscal deficit (% of GDP) | -8.4 | -8.7 | -8.2 | -8 | -8.9 |
| Current account balance (% of GDP) | -4.9 | -2.8 | -3.2 | -0.4 | -1.4 |
| External assets (months of same year imports) | 4.7 | 5.7 | 5.2 | 5.8 | 4.9 |
| Overall debt service ratio | | | | | |
| (% of export of goods & services) | 12.7 | 7.9 | 11.6 | 11.6 | 13.2 |
| Total external debt & liabilities (% of GDP) | 53 | 56.3 | 65.9 | 64.7 | 63.1 |
| INTEREST RATES (percentage per annum at end-year) | | | | | |
| Treasury bill rate | | | | | |
| 91 days | 12.76 | 10.10 | 7.25 | 7.35 | 9.92 |
| 364 days | 11.5 | 10.37 | 7.65 | 7.24 | 9.91 |
| Repurchase rate (overnight) | 10 | 8.75 | 7.5 | 7 | 9.75 |
| Reverse repurchase rate (overnight) | 11.5 | 10.25 | 9 | 8.5 | 11.75 |
| Commercial Banks | | | | | |
| Weighted average - prime lending rate | 15.19 | 12.2 | 10.2 | 9.3 | 12.2 |
| Weighted average - deposit rate | 7.6 | 6.2 | 5.3 | 5.3 | 7.5 |
| EXCHANGE RATES | | | | | |
| Annual average Rs./US\$ | 103.96 | 100.5 | 101.19 | 96.52 | 95.66 |
| End-year Rs./US\$ | 107.71 | 102.12 | 104.61 | 96.74 | 96.73 |
| CAPITAL MARKETS | | | | | |
| All share price index | 2,722.4 | 1,922.2 | 1,506.9 | 1,062.1 | 815.1 |
| Milanka price index | 3,711.8 | 2,451.1 | 2,073.7 | 1,897.8 | 1,374.6 |
| Value of shares traded (Rs. million) | 105,154 | 114,599 | 59,052 | 73,657 | 30,183 |
| Market capitalisation (Rs. billion) | 834.8 | 584.0 | 382.1 | 262.8 | 162.6 |
| Market capitalisation (% GDP) | 30 | 25 | 19 | 15 | 10 |

KEY SOCIAL INDICATORS

Population & Vital Statistics

| | |
|----------------------------------|---------------------------|
| Age distribution (%) (2006) | |
| 0-14 years | 26.6% |
| 15-64 years | 67.0% |
| 65 years & over | 6.4% |
| Population density (2005) | 317 persons per sq. km. |
| Crude birth rate (2005) | 18.1 per '000 |
| Crude death rate (2005) | 6.5 per '000 |
| Rate of natural increase (2005) | 11.6 per '000 |
| Infant mortality rate (2004) | 12.0 per '000 live births |
| Dependency ratio (2004) | 49.35% |
| Average household size (2003/04) | 4.31 |

EXPECTATION OF LIFE AT BIRTH (2004)

| | |
|--------|------------|
| Male | 71.7 years |
| Female | 77.0 years |

LITERACY RATE (2003/04)

| | |
|---------|--------|
| Overall | 92.50% |
| Male | 94.50% |
| Female | 90.60% |

HUMAN DEVELOPMENT INDEX (2004)

| | |
|-----------------------------|----|
| Ranking among 177 countries | 93 |
|-----------------------------|----|

EMPLOYMENT (2006)

| | |
|-------------|-------|
| Agriculture | 32.2% |
| Industry | 26.6% |
| Service | 41.2% |

POVERTY

| | |
|--|-------|
| Population below US \$ 1 a day (1990 - 2004) | 5.6% |
| Population below US \$ 2 a day (1990 - 2004) | 41.6% |

COUNTRY INFORMATION (CONTD.)

SECTORIAL COMPOSITION AND INCREASE IN GROSS DOMESTIC PRODUCT (GDP)

| | As a Share of GDP (%) | | Rate of Change (%) | | Contribution to Change (%) | |
|------------------------------|-----------------------|--------|--------------------|------|----------------------------|--------|
| | 2006 | 2005 | 2006 | 2005 | 2006 | 2005 |
| Agriculture Sector | 16.80 | 17.20 | 4.70 | 1.90 | 11.1 | 4.4 |
| Industrial Sector | 27.00 | 27.00 | 7.20 | 8.30 | 26.3 | 36.3 |
| Services Sector | 56.20 | 55.80 | 8.30 | 6.20 | 62.6 | 59.3 |
| Gross Domestic Product (GDP) | 100.00 | 100.00 | 7.40 | 6.00 | 100.00 | 100.00 |

MOTOR VEHICLES REGISTRATION (UNITS)

| | 2006 | 2005 | 2004 | % Change | |
|--|---------|---------|---------|----------|--------|
| | | | | 2006 | 2005 |
| New registration of motor vehicles (No.) | 300,522 | 229,665 | 223,842 | 30.9 | 2.6% |
| Buses | 3,346 | 2,069 | 2,167 | 61.7 | -4.5% |
| Private cars | 27,578 | 17,283 | 19,116 | 59.6 | -9.6% |
| Dual purpose vehicles | 7,245 | 6,851 | 10,736 | 5.8 | -36.2% |
| Goods transport vehicles | 20,436 | 14,262 | 10,703 | 43.3 | 33.3% |
| Land Vehicles | 20,825 | 17,423 | 12,857 | 19.5 | 35.5% |

PHYSICAL & SOCIAL INFRASTRUCTURE FACILITIES

| | Unit | 2005 |
|---|---------------------|-------|
| Water Supply & Sanitation | | |
| Access to safe drinking water | per cent | 92.5 |
| Access to pipe borne water | per cent | 38.9 |
| Electricity | | |
| Households with electricity | per cent | 78.1 |
| Per capita electricity consumption | kWh/person | 394 |
| Communications | | |
| Telephone Density | | |
| Fixed lines | per 100 persons | 9.5 |
| Including cellular phones | per 100 persons | 36.8 |
| Internet and e-mail | per 1,000 persons | 6.5 |
| Public Health | | |
| Hospital beds | per 1,000 persons | 3.1 |
| Persons per doctor | Number | 2,061 |
| Nurses | per 10,000 persons | 10.3 |
| Government expenditure on health | per cent of GDP | 2.1 |
| General Education | | |
| School density (area covered by a school) | sq. km. | 6 |
| Pupil/teacher ratio (Government schools) | Number | 19 |
| Age specific enrolment ratio (Age 5-19 years) | per cent | 75.2 |
| University Education | | |
| Pupil/teacher ratio | Number | 15.2 |
| Age specific enrolment ratio (Age 20-24 years) | per cent | 3.6 |
| Progression to University from GCE (A/L) | | |
| Eligibility for university admission | per cent | 59.4 |
| Admission as a percentage of eligibility | per cent | 14.0 |
| Government expenditure on education | per cent of GDP | 2.8 |
| Banking | | |
| Total number of commercial banks | Number | 23 |
| Domestic banks | Number | 11 |
| Foreign banks | Number | 12 |
| ATM's | per 100,000 persons | 5.6 |
| Credit card issued | per 100,000 persons | 4,080 |
| Banking density | | |
| No. of bank branches | per 100,000 persons | 7.6 |

COUNTRY INFORMATION (CONTD.)

KEY EXTERNAL

- Issuance of foreign currency denominated Sri Lanka Nation Building Bonds (SLNBB) to non-resident Sri Lankans was initiated.
- The Government opened the rupee denominated Treasury bond market for foreign investors subject to a limit of 5% of the total Treasury bond outstanding amount.
- The Cheque Imaging & Truncation project was implemented.
- A direction was issued to all authorised foreign currency exchange dealers permitting them to offer and engage in Sri Lankan rupee based foreign currency options.
- The Colombo Stock Exchange (CSE) continues to remain the best performing share market in Asia with the All Share Price Index (ASPI) and the Milanka Price Index (MPI) rising by 42% & 51% respectively.
- New policy guidelines were issued for regulation of Commercial Bank share ownership.
- The ten-year Horizon Development Framework (Ten-year Vision) was issued.
- The CPC enters into two hedging agreements to import oil.

The following proposals were made during the Government's Budget presented on 8th December 2006:

- The following changes were proposed for Corporate Tax Rates:

| | Prevailing Y/A 2006/07 | Proposed Y/A 2007/08 |
|--|---------------------------|-------------------------|
| PAL - 'CIF' Value of Imports | | |
| ● Processing/Manufacturing for re-export | — | — |
| ● Other goods | 2.50% | 3.00% |
| ● Selected plant & machinery | 2.50% | 2.00% |

- The following changes were proposed for Economic Service Charge:

| | Prevailing Y/A 2006/07 | Proposed Y/A 2007/08 |
|------------------------|---------------------------|-------------------------|
| Turnover base | Current Qtr. | Current Qtr. |
| Minimum threshold p.q. | Rs. 10 mn | Rs. 7.5 mn |
| Maximum charge p.q. | Rs. 15 mn | Rs. 15 mn |
| Set-off | Any income tax | Any income tax |
| Carry forward | 3 years | 5 years |
| Exclusion | Out of services | Offshore Services |

- The Markup on CIF value on importation of goods will be increased from 7% to 10%.
- Increase the depreciation allowance on machinery used in the construction industry from 12.5% to 25%.
- The VAT Act will be amended to provide for the exemption of the importation of any bus by any bus owner holding a valid route permit.
- Input Credit on VAT will be restricted to input tax allowable for any taxable period or 85% of the output tax declared, for the taxable period whichever is lower.
- VAT on high technological medical equipment was reduced from 15% to 5%.
- A 5% non-refundable VAT was imposed on every person who is on the border of VAT threshold of Rs. 1.0 mn.
- The rate will be reduced from 15% to 5% on certain high-tech medical equipment.
- Regional Infrastructure development levy of 2.5% was imposed on motor vehicles.
- Excise Duty on motor cars was including station wagons/racing cars, whose cylinder capacity does not exceed 1600 cc was reduced from 115% to 95%.

Sources: Central Bank of Sri Lanka Annual Reports/KMPG Budget Highlights

CSR INDICATORS AS PER G3 GUIDELINES

| | Section/Details |
|--|--|
| Profile | |
| Statement from CEO | Sustainability Report |
| Organisational Profile | |
| Name of the Company | Corporate Information |
| Primary brands, products and/or services | Business Performance |
| Location of organisation's headquarters | Corporate information |
| Countries in which the organisation operates | Not applicable |
| Nature of ownership and legal form | Corporate information |
| Markets served | Business Performance |
| Awards received during the reporting period | Chairman's Review |
| Report Profile | |
| Reporting period | 31.3.2007 |
| Date of most recent previous report | 31.3.2006 |
| Reporting cycle | 12 months |
| Governance, Commitments and Engagement | |
| Governance structure of the organisation | Enterprise Governance |
| Verify whether the Chair of the highest governance body is also an executive officer | Enterprise Governance |
| Mechanisms for shareholders and employees to provide recommendations or directions to the highest governance body | Sustainability Report |
| Linkage between compensation for members of the highest governance body | Enterprise Governance/ Remuneration Committee Report |
| Processes in place for the highest governance body to ensure that conflicts of interest are avoided | Enterprise Governance/ Nominations Committee Report |
| Process for determining the qualifications and expertise of the members of the highest governing body for guiding the organisations strategy | Enterprise Governance/ Board of Directors |
| Identification and management of economic, environmental and social performance etc. | Sustainability Report |
| Processes for evaluating the highest governance body's own performance | Enterprise Governance |
| Commitments to External Initiatives | Not reported |
| Stakeholder Engagement | |
| List of stakeholder groups engaged by the organisation | Sustainability Report |
| Approaches to stakeholder engagement | Sustainability Report |
| Economic Performance Indicators | |
| Direct economic value generated and distributed | Sustainability Report |

CSR INDICATORS AS PER G3 GUIDELINES (CONTD.)

| | Section/Details |
|--|-----------------------|
| Environmental Performance Indicators | |
| Direct energy usage & conservation and efficiency initiatives | Sustainability Report |
| Consumption of materials - Paper management | Sustainability Report |
| Water usage & initiative to recycle & reuse | Sustainability Report |
| Emissions, Affluents and Waste, initiatives to reduce emissions | Sustainability Report |
| Initiatives to mitigate environmental impacts of products and services and extent of impact mitigation | Sustainability Report |
| Bio-diversity | Not directly affected |
| Transport | Not reported |
| Labour Practices and Decent Work Performance Indicators | |
| Employment | |
| Total workforce by gender & age | Sustainability Report |
| Labour/Management Relations | |
| Occupational Health & Safety | |
| Rates of injury, occupational diseases and number of work-related fatalities by region | Sustainability Report |
| Training & Education | |
| Employee training per year | Sustainability Report |
| Percentage of employees receiving regular performance and career development reviews | Sustainability Report |
| Human Rights Performance Indicators | |
| Investment & Procurement practices | Not reported |
| Total number of incidents of discrimination and actions taken | Nil |
| Freedom of Association and Collective bargaining | Not reported |
| Child Labour | |
| Operations identified as having a significant risk for incidents of child labour and measures taken to contribute to the elimination of child labour | Sustainability Report |
| Forced & Compulsory Labour | Not reported |
| Indigenous Rights | Nil |
| Society Performance Indicators | |
| Community | Sustainability Report |
| Corruption | Not reported |
| Anti-competitive behaviour | Not reported |
| Compliance | Not reported |
| Product Responsibility Performance Indicators | |
| Customer Health & Safety | Not reported |
| Practices related to customer satisfaction, including results of surveys measuring customer satisfaction | Sustainability Report |
| Compliance - Monetary fines for non-compliance with laws & regulations | Nil |

Note: G3 guidelines have been issued by the Global Reporting Initiatives.

GLOSSARY OF FINANCIAL TERMS

Accounting policies

Specific principles, bases, conventions, rules and practices adopted by an enterprise in preparing and presenting Financial Statements.

Accrual basis

The principle that revenues & costs are matched with one another, irrespective of the period of receipt or payment.

Basic earnings per share

Profit attributable to ordinary shareholders divided by the weighted average number of shares in issue.

Bonus issue (Scrip issue)

The capitalisation of reserves of a company by the issue of additional shares to existing shareholders, in proportion to their holdings. Such shares are normally fully paid-up with no cash called for.

Borrowings

All interest bearing liabilities.

Capital employed

Total assets less interest free liabilities, deferred income and provisions.

Capital Reserves

Reserves identified for a specific purpose. These reserves cannot be distributed to shareholders in the form of dividends. It consist of Revaluation Reserve arising from the revaluation of properties owned by the Company.

Cash equivalents

Liquid investments with original maturity periods of three months or less.

Contingent liabilities

A condition or situation at the Balance Sheet date of which the financial effect will be determined only on the occurrence, or non-occurrence of one or more uncertain future events.

Current ratio

Current assets divided by current liabilities.

Deferred taxation

The net effect on items which have been included in the Income Statements, which would only qualify for inclusion on a tax return at a further date.

Dividend cover

Profit after taxation divided by gross dividend. This ratio is a measure of the number of times gross dividend is covered by profit after taxation.

Dividend yield

Gross dividend per share as a percentage of the market price. A measure of return on investment.

Effective rate of tax

Provision for tax excluding deferred tax, divided by net profit before tax.

Equity

Shareholders' funds.

Exchange gain/loss

The increase/decrease in value of foreign currency denominated assets and liabilities when converted to or realised in local currency during the year.

Gearing

Borrowings to capital employed.

General reserve

Reserves available for distributions and investment.

Gross dividend

The portion of profit including tax withheld distributed to shareholders.

Gross profit ratio

The percentage of gross profit to net turnover.

Interest cover

Profit before taxation plus financing cost divided by financing cost.

Key performance Indicators (KPI)

Are quantifiable measurements, agreed to before hand that reflect the critical success factors of a company.

Market capitalisation

The number of ordinary shares issued multiplied by the market price of each share at a given date. This is also known as the Market Value of a company.

Materiality

The principle that Financial Statements should separately disclose items which are significant enough to affect evaluation or decisions of users.

Net assets per share

Shareholders' funds divided by the number of ordinary shares in issue.

Price earnings ratio

Market price of a share divided by earnings per share as reported at that date.

Related parties

Parties who could control or significantly influence the financial and operating policies of the business.

Return on average capital employed

Profit before tax plus net interest cost divided by average capital employed.

Return on average shareholders' funds

Profit after taxation divided by average shareholders' funds.

Revenue reserves

Reserves available for distribution to shareholders & investments.

Rights issue

The raising of new capital by granting existing shareholders the right to subscribe to new shares in proportion to their current holdings. These shares are normally issued at a discount on their market price.

Segment

A Business unit that is a distinguishable component of the Group and engaged in similar operations.

Share capital

Consists of issued and paid up ordinary shares.

Substance over form

Whether the accounting treatment in the Financial Statements of transactions reflect the financial reality and substance, rather than the legal form of the transaction & events which underlies them.

Strategy

A course of action, including the specification of resources required, to achieve a specified objective.

Total shareholder return

Represents the change in share value of a listed Company over a period of time (typically 1 year), plus dividends, expressed as a percentage of the opening share value.

Treasurership

The function concerned with the provision and use of finance. It also includes provision of capital, short-term borrowings, foreign currency management, banking, collections and money market investments.

Triple bottom line reporting

Is a framework for measuring and reporting corporate performance against Economic, Social and Environmental parameters.

Turnover per employee

Consolidated turnover of the Company for the year divided by the number of employees at the year end.

Value added

Value added is the wealth created by the operations of the Group. The value is distributed among the employees, shareholders, as financing cost, to the Government by way of taxes and the balance retained within the business.

Working capital

Capital required to finance the day-to-day operations computed as the excess of current assets over current liabilities.

NOTICE OF MEETING

NOTICE IS HEREBY GIVEN that the Sixty-Second Annual General Meeting of Diesel & Motor Engineering PLC will be held at the Registered Office of the Company, No. 65, Jetawana Road, Colombo 14, on Wednesday, 20th June 2007 at 3.00 p.m. and the business to be brought before the meeting will be:

AGENDA

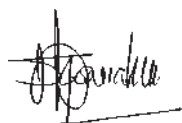
- To consider and adopt the Report of the Directors and the Statement of Accounts for the year ended 31st March 2007, with the Report of the Auditors thereon.
- To declare a dividend as recommended by the Directors.
- To re-elect Mr. S.C. Algama, who retires by rotation at the Annual General Meeting, a Director.*
- To re-elect Mr. R.A. Ebell, who retires by rotation at the Annual General Meeting, a Director.*
- To re-elect Mr. A.M. Pandithage, who retires by rotation at the Annual General Meeting, a Director.*
- To elect Dr. H. Cabral, who has been appointed by the Board of Directors since last Annual General Meeting as a Director*
- To elect Dr. U.P. Liyanage, who has been appointed by the Board of Directors since last Annual General Meeting as a Director*
- To elect Mr. R. Seevaratnam, who has been appointed by the Board of Directors since last Annual General Meeting as a Director*
- To reappoint KPMG Ford, Rhodes, Thornton & Co., as Auditors for the ensuing year and authorise the Directors to determine their remuneration.
- To authorise the Directors to determine contributions to charities.
- To consider any other business.

** The profiles of the Directors proposed for election/re-election are given on page ... of the Annual Report.*

NOTE

- A member is entitled to appoint a proxy to attend and vote instead of himself and a proxy need not be a member of the Company.** A form of proxy is enclosed for this purpose. The instrument appointing a proxy must be deposited at the Registered Office, No. 65, Jetawana Road, Colombo 14, not less than forty-eight hours before the time fixed for the Meeting.
- It is proposed to post ordinary dividend warrants on 27th June 2007 and in accordance with the rules of the Colombo Stock Exchange, the shares of the Company will be quoted ex-dividend with effect from 21st June 2007.

By Order of the Board,
Diesel & Motor Engineering PLC



B.C.S.A.P. Gooneratne
Secretary

Colombo
21st May 2007

FORM OF PROXY

I/We,
of
being a member/members of DIESEL & MOTOR ENGINEERING PLC hereby appoint:

1.of
.....
Holder of NIC No. or failing him/them
2. ASOKA RANJITH PANDITHAGE (Chairman of the Company) of Colombo or, failing him, one of the Directors of the Company as my/our proxy to vote as indicated hereunder for me/us and on my/our behalf at the Sixty-Second Annual General Meeting of the Company to be held on Wednesday, 20th June 2007 and at every poll which may be taken in consequence of the aforesaid meeting and at any adjournment thereof.

| | For | Against |
|--|--------------------------|--------------------------|
| (1) To consider and adopt the Report of the Directors and the Statement of Accounts for the year ended 31st March 2007, with the Report of the Auditors thereon. | <input type="checkbox"/> | <input type="checkbox"/> |
| (2) To declare a dividend as recommended by the Directors. | <input type="checkbox"/> | <input type="checkbox"/> |
| (3) To re-elect Mr. S. C. Algama, who retires by rotation at the Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (4) To re-elect Mr. R. A. Ebell, who retires by rotation at the Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (5) To re-elect Mr. A. M. Pandithage, who retires by rotation at the Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (6) To elect Dr. H. Cabral, who has been appointed by the Board of Directors since last Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (7) To elect Dr. U. P. Liyanage who has been appointed by the Board of Directors since last Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (8) To elect Mr. R. Seevaratnam, who has been appointed by the Board of Directors since last Annual General Meeting, a Director. | <input type="checkbox"/> | <input type="checkbox"/> |
| (9) To reappoint KPMG Ford, Rhodes, Thornton & Co. as Auditors and authorise the Directors to determine their remuneration. | <input type="checkbox"/> | <input type="checkbox"/> |
| (10) To authorise the Directors to determine contributions to charities. | <input type="checkbox"/> | <input type="checkbox"/> |

The proxy may vote as he thinks fit on any other resolution brought before the meeting.

Dated this day of 2007.

Witness:

.....
.....

.....
Signature of Shareholder

1. A proxy need not be a member of the Company.
2. Instructions to fill the proxy (please see overleaf).

FORM OF PROXY (CONTD.)

INSTRUCTIONS AS TO COMPLETION

1. To be valid this form of proxy must be deposited at the Registered Office, No. 65, Jetawana Road, Colombo 14, by 3.00 p.m. on Monday, 18th June 2007.
2. In perfecting the form of proxy please ensure that all details are legible.
3. If you wish to appoint a person as your proxy, please insert the relevant details overleaf and initial against this entry.
4. Please indicate with a X in the spaces provided how your proxy is to vote on each resolution. If no indication is given the proxy in his discretion will vote as he thinks fit. Please also delete if you do not wish your proxy to vote as he thinks fit on any other resolution brought before the meeting.
5. In the case of a company/corporation, the proxy must be under its common seal which should be affixed and attested in the manner prescribed by its Articles of Association.
6. In the case of a proxy signed by an Attorney, the Power of Attorney must be deposited at the registered office for registration.
7. In the case of non-resident shareholders, the stamping will be attended to on return of the completed form of proxy to Sri Lanka.

NAME OF THE COMPANY

Diesel & Motor Engineering PLC

LEGAL FORM

A Quoted Public Company with Limited Liability,
Incorporated in Sri Lanka in 1945.

COMPANY REGISTRATION

NUMBER PVS 249 PBS

FOUNDED 1939

ACCOUNTING YEAR END

31st March

STOCK EXCHANGE LISTING

The ordinary shares of the Company are listed with the
Colombo Stock Exchange of Sri Lanka.

AUDITORS

KPMG Ford, Rhodes, Thornton & Co.
Chartered Accountants,
P.O. Box 186,
Colombo, Sri Lanka.

INTERNAL AUDITORS

SJMS Associates
Chartered Accountants
2, Castle Street,
Colombo 04, Sri Lanka.

LAWYERS

M/s. F J & G De Saram & Company
Attorneys-at-Law
No. 216, De Saram Place,
Colombo 10, Sri Lanka.

BANKERS

Hatton National Bank Ltd.
Commercial Bank of Ceylon Ltd.
NDB Bank
Citibank N.A.
Nations Trust Bank
People's Bank
Hongkong & Shanghai Banking Corporation Ltd.
Sampath Bank Ltd.

COMPANY SECRETARY

B.C.S.A.P. Gooneratne, F.C.A., M.B.A. (Sri J.)

HEAD AND REGISTERED OFFICE

P.O. Box 339, No. 65, Jetawana Road,
Colombo 14, Sri Lanka.
Telephone: 2449797, 2338883
<http://www.dimolanka.com>
E-mail: dimo@dimolanka.com
Facsimile: 2449080

CORPORATE GOVERNANCE RATING

The Company received a rating of 6 (CG) from
Det Norske Veritas (DNV).

