

14. ACCOUNTANTS' REPORT

(Prepared for inclusion in the Prospectus)



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The Board of Directors
Favelle Favco Berhad
Lot 586, 2nd Mile
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41300 Klang
Selangor Darul Ehsan

6 June 2006

Dear Sirs,

Accountants' Report

1. Introduction

This report has been prepared by Messrs KPMG, an approved company auditor, for inclusion in the Prospectus of Favelle Favco Berhad ("FFB" or "the Company") to be dated 30 June 2006 in connection with the listing of FFB on the Second Board of Bursa Malaysia Securities Berhad ("Bursa Securities")

2. General information

2.1 Background

FFB was incorporated in Malaysia under the Companies Act, 1965 as a private limited company on 22 September 1992 under the name of Maxi Impact Sdn. Bhd. On 21 August 1995 and 17 June 2004 respectively, the Company changed its name to Favelle Favco Cranes Holdings Sdn. Bhd. and subsequently to Favelle Favco Sdn. Bhd. The Company was converted into a public limited company on 24 June 2004 and assumed its current name.

The principal activities of FFB and its subsidiaries ("FFB Group") are designing, manufacturing, supplying, servicing, trading and renting of cranes.

14. ACCOUNTANTS' REPORT (Cont'd)**2.2 Share capital**

At the date of incorporation, FFB's authorised, issued and fully paid-up share capital was RM2.00 comprising 2 ordinary shares of RM1.00 each. Subsequently, the issued and fully paid-up share capital was increased to RM60,000,000 comprising 120,000,000 ordinary shares of RM0.50 each as follows:

Date of issue	Number of ordinary shares	Issue price per ordinary share RM	Purpose	Issued and fully paid-up share capital (Cumulative) RM
22 September 1992	2	1.00	Incorporation	2
30 December 1995	11,999,998	1.00	Increase in working capital	12,000,000
10 October 1996	6,000,000	1.00	Increase in working capital	18,000,000
28 December 2001	32,000,000	1.00	Increase in working capital	50,000,000
19 May 2006	10,000,000	1.00	Increase in working capital	60,000,000
19 May 2006	120,000,000	0.50	Share split	60,000,000

Pursuant to the floatation scheme, the issued and fully paid-up share capital of FFB will be increased to RM84,000,010 comprising 168,000,020 ordinary shares of RM0.50 each.

In addition, an employees share options scheme is to be established for the granting of options to the executive Directors and eligible employees of the FFB Group to subscribe for new FFB shares representing up to 10.0% of the enlarged issued and paid-up share capital of FFB at any point in time during the subsistence of the scheme.

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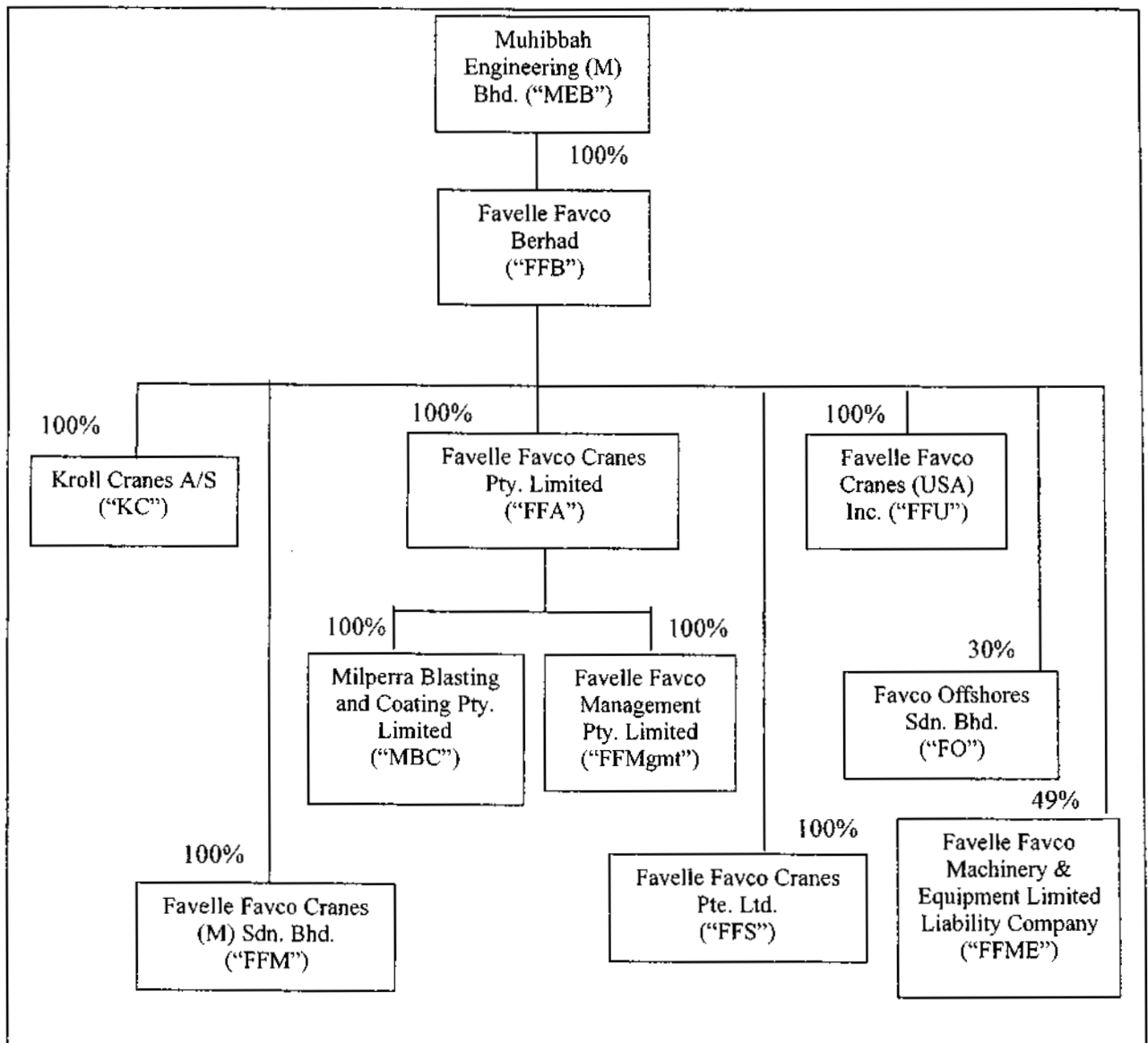
14. ACCOUNTANTS' REPORT (Cont'd)



3. Floatation scheme

3.1 Group structure

Existing structure

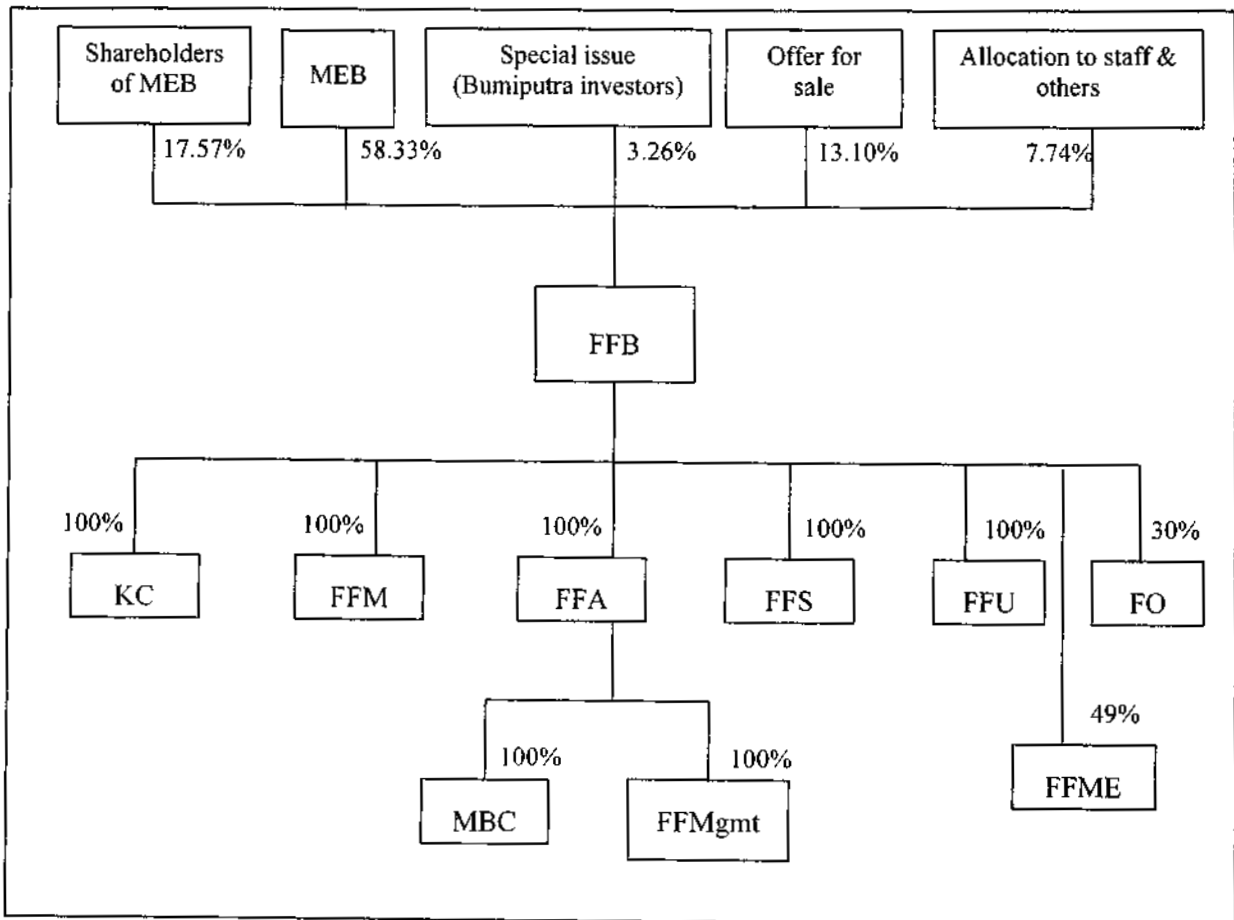


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▪ New structure

The new structure below is based on the assumption that the restricted issue to the shareholders of MEB will result in the issuance of 29,525,920 new FFB shares based on MEB's issued and paid-up capital of RM147,629,600 comprising 147,629,600 ordinary shares of RM1.00 each in MEB ("MEB Shares") as at 23 May 2006 and also on the assumption that the remaining 5,308,000 options to subscribe for 5,308,000 new MEB Shares pursuant to MEB's employee share option scheme are not exercised.



14. ACCOUNTANTS' REPORT (Cont'd)**3.2 Increase in share capital**

In conjunction with the listing of and quotation for the entire issued and paid-up share capital of FFB on the Second Board of Bursa Securities, FFB will undertake the following:

- a. Settlement of the entire net amount owing by FFB Group to the MEB Group in the following manner:
 - Amount owing to MEB of RM10.0 million are capitalised into 10,000,000 new ordinary shares of RM1.00 each in FFB at par (completed on 19 May 2006);
 - RM8.5 million to be settled from proceeds from the public issue;
 - The remaining net amount owing are settled by cash via bank borrowings
- b. Share split involving a change in the par value of FFB's ordinary shares from RM1.00 each to RM0.50 each resulting in the issued and paid-up share capital of RM60,000,000 comprising 120,000,000 ordinary shares of RM0.50 each ("FFB shares") from the existing 60,000,000 ordinary shares of RM1.00 each (completed on 19 May 2006).
- c. Public issue of 48,000,020 new FFB shares in the following manner:
 - i) Renounceable restricted issue of up to 30,587,520 new FFB shares by way of invitation to the shareholders of MEB on the basis of (1) new FFB share for every (5) existing MEB share held as at the entitlement date, at an issue price of RM0.55 per FFB share.
 - ii) Special issue of up to 6,086,300 new FFB shares to Bumiputra investors to be identified by FFB and approved by MITI at an issue price of RM0.55 per FFB share.
 - iii) Pink form issue of 13,000,000 new FFB shares to be reserved for application by the directors and eligible employees of MEB and FFB Group and persons who contributed to the success of FFB and its subsidiaries at an issue price of RM0.55 per FFB share.

The total number of shares to be issued arising from the renounceable restricted issue and the special issue to Bumiputra investors shall be fixed at 35,000,020 new FFB shares. Hence, the special issue represents the balancing figure after taking into consideration the actual number of shares to be issued under the renounceable restricted issue.
- d. Offer for sale by MEB of 22,000,000 existing FFB shares at an offer price of RM0.55 per FFB share, payable in full upon application.
- e. Employee Share Option Scheme ("ESOS") for the granting of options to the executive Directors and eligible employees of FFB Group to subscribe for new FFB shares representing up to 10.0% of the enlarged issued and paid-up share capital of FFB at any point in time during the subsistence of the scheme.
- f. Listing of and quotation for the entire enlarged issued and paid-up share capital of FFB amounting up to RM84,000,010 comprising 168,000,020 FFB Shares and such number of new FFB Shares to be issued pursuant to the ESOS on the Second Board of Bursa Securities.

14. ACCOUNTANTS' REPORT (Cont'd)



4. Information on subsidiaries and associates

The subsidiaries and associates of FFB under the listing scheme as at the date of this report and their principal activities are as follows:

	Date and place of incorporation	Issue and paid up capital	Effective equity interest %	Principal activity
<i>Subsidiary</i>				
Favelle Favco Cranes (M) Sdn. Bhd. ("FFM")	14 July 1995 Malaysia	RM10 million	100	Designing manufacturing, supply, servicing, trading and renting of cranes.
Favelle Favco Cranes (USA) Inc. ("FFU")	3 September 1997 United States of America	USD21 million	100	Designing, manufacturing, supply, servicing, trading and renting of cranes.
Favelle Favco Cranes Pty. Limited ("FFA")	16 December 1994 Australia	AUD5.4 million	100	Designing, manufacturing, supply, servicing and renting of cranes.
Favelle Favco Management Pty. Limited ("FFMgmt")	31 May 1995 Australia	AUD2	100	Management services.
Milperra Blasting and Coating Pty. Limited ("MBC")	26 June 1996 Australia	AUD1.292 million	100	Dormant
Favelle Favco Cranes Pte. Ltd. ("FFS")	2 June 1995 Singapore	SGD3 million	100	Supplying, servicing, trading and renting of cranes.
Kroll Cranes A/S ("KC")	1 September 1985 Denmark	DKK20 million	100	Designing, manufacturing, supply, servicing, trading and renting of cranes.
<i>Associate</i>				
Favco Offshores Sdn. Bhd. ("FO")	11 April 1995 Malaysia	RM0.6 million	30	Designing, manufacturing, supply, servicing, trading and renting of cranes and marine plant and undertaking other engineering works.
Favelle Favco Machinery & Equipment Limited Liability Company ("FFME")	21 November 2004 United Arab Emirates	AED0.15 million	49	Supplying, servicing, trading and renting of cranes.

14. ACCOUNTANTS' REPORT (Cont'd)



5. Financial statements and auditors

The present financial year end of all companies in the FFB Group is 31 December.

The financial statements of FFB, FFM and FO for the financial years ended 31 December 2003 to 2005 were audited by KPMG Malaysia.

The financial statements of FFS for the financial years ended 31 December 2003 to 2005 were audited by KPMG Singapore.

The financial statements of FFA and MBC for the financial years ended 31 December 2003 to 2005 were audited by Bentleys MRI.

The financial statements of FFMgmt, a wholly owned subsidiary of FFA, were not prepared and audited for the financial years under review. Management represented that the income and expenses of the company were absorbed by FFA.

The financial statements of FFU for the financial years ended 31 December 2003 to 2005 were audited by Burton Mc Cumber & Cortez, LLP.

The financial statements of KC for the financial years ended 31 December 2003 and 2004 were audited by KPMG Denmark. The financial statements for the year ended 31 December 2005 was audited by Nielsen & Christensen.

The financial statements of FFME for the financial years ended 31 December 2005 was audited by AGN Mak.

The auditors' reports of all the companies for all the relevant financial years under review, were not subject to any qualification.

KPMG Singapore and KPMG Denmark are member firms of KPMG International.

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6. Favelle Favco Berhad and its subsidiaries ("FFB Group")

6.1 Summarised consolidated results

We set out below the summarised consolidated results of the FFB Group for the three financial years ended 31 December 2005.

	Notes	← For the year ended 31 December →		
		2003 RM'000	2004 RM'000	2005 RM'000
Revenue	6.1.1	193,510	266,965	335,646
Cost of sales	6.1.2	(161,053)	(224,467)	(285,193)
Gross profit		32,457	42,498	50,453
Operating profit before exceptional items		5,261	7,194	14,722
Exceptional items	6.1.3	-	8,777	(571)
Operating profit after exceptional items		5,261	15,971	14,151
Interest expense		(3,574)	(3,299)	(5,377)
Interest income		270	203	182
Share of profit/(loss) of an associate		4	9	(73)
Profit before taxation		1,961	12,884	8,883
Taxation		(372)	432	(1,703)
Profit after taxation		1,589	13,316	7,180
Effective tax rate (%)	6.1.4	18.97	(3.35)	19.17
Gross margin (%)		16.77	15.92	15.03
Pre-tax profit margin (%)		1.01	4.83	2.65
NTA per ordinary share (RM)		0.87	1.20	1.25
Current ratio (times)		1.50	1.25	1.17
Gearing ratio (times)		1.16	1.22	1.95
Interest coverage ratio (times)		1.55	4.91	2.65
Gross dividend rate*		-	-	-
After tax return on shareholders' funds (%)		3.09	19.65	10.21
Weighted average number of ordinary shares ('000)		50,000	50,000	50,000
Earnings per share (RM)	6.1.5			
- Gross		0.04	0.26	0.18
- Net		0.03	0.27	0.14

*FFB has not paid or declared any dividends since its incorporation.

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Notes to summary of results

6.1.1 Revenue

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Revenue			
Contract revenue	143,765	222,642	280,854
Sales of goods	30,288	28,589	30,353
Services rendered	19,457	15,734	24,439
	193,510	266,965	335,646
Growth rate (%)	(11)	38	26
<i>(Revenue in 2002: RM216 million)</i>			

6.1.2 Cost of sales

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cost of sales			
Contract costs	(127,232)	(193,542)	(260,592)
Sales of goods	(22,498)	(23,822)	(15,196)
Services rendered	(11,323)	(7,103)	(9,405)
	(161,053)	(224,467)	(285,193)

6.1.3 Exceptional items

The exceptional items in 2004 were in respect of gain on disposal of property, plant and equipment amounting to RM18.8 million; which was partially set-off by provision of restructuring costs of RM5.8 million, impairment loss on property, plant and equipment of RM2.5 million and write off of goodwill on acquisition of business assets amounting to RM1.7 million.

The exceptional item in 2005 was in respect of goodwill written off on acquisition of business assets amounting to RM0.6 million.

6.1.4 Effective tax rate

The effective tax rate in 2003 and 2005 was lower than the statutory tax rate mainly due to the utilisation of brought forward unutilised tax losses by certain subsidiaries to set-off against their taxable income.

In addition, FFM was granted pioneer status under the Promotion of Investment Act, 1986 whereby the entire statutory income of FFM, from its sales of cranes, was exempted from tax.

Negative effective tax rate in 2004 was mainly due to overprovision of prior year tax expense.

14. ACCOUNTANTS' REPORT *(Cont'd)*



Notes to summary of results (continued)

6.1.5 Earnings per share

The basic gross and net earnings per share are calculated based on the profit before and after taxation attributable over the weighted average number of ordinary shares outstanding during the year.

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14. ACCOUNTANTS' REPORT (Cont'd)



6.2 Summarised consolidated balance sheets

We set out below the summarised consolidated balance sheets of the FFB Group for the three financial years ended 31 December 2005.

	Notes	← As at 31 December →		
		2003 RM'000	2004 RM'000	2005 RM'000
Property, plant and equipment	6.2.1	41,489	38,068	61,855
Investment in associates	6.2.2	306	314	312
Development costs	6.2.3	3,688	5,154	6,362
Deferred expenditure		-	557	350
Other intangible assets	6.2.4	4,134	2,179	1,356
Deferred tax assets	6.2.5	-	620	-
		49,617	46,892	70,235
Current assets				
Inventories	6.2.6	60,242	57,936	72,850
Trade and other receivables	6.2.7	106,031	168,220	228,443
Tax recoverable		919	1,721	1,799
Cash and cash equivalents	6.2.8	10,853	9,127	17,564
		178,045	237,004	320,656
Current liabilities				
Trade and other payables	6.2.9	63,157	96,179	146,317
Bills payable		18,654	31,691	73,302
Bank overdrafts, loans and hire purchase	6.2.10	33,332	50,656	44,560
Provisions	6.2.11	3,677	10,988	10,406
		118,820	189,514	274,585
Net current assets		59,225	47,490	46,071
		108,842	94,382	116,306
Financed by:				
Share capital		50,000	50,000	50,000
Reserves		1,403	17,768	20,351
Shareholders' funds		51,403	67,768	70,351
Long term and deferred liabilities				
Term loans and hire purchase	6.2.12	7,607	505	18,983
Provisions	6.2.11	1,722	828	-
Deferred tax liabilities	6.2.5	635	604	1,451
Long term advances due to holding company		47,475	24,677	25,521
		57,439	26,614	45,955
		108,842	94,382	116,306

14. ACCOUNTANTS' REPORT (Cont'd)



Notes to summarised balance sheets

6.2.1 Property, plant and equipment

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Freehold land	2,363	239	9,207
Buildings	11,764	7,110	23,835
Cranes	18,002	21,322	18,076
Plant, equipment & motor vehicles	9,360	7,777	10,260
Capital work in progress	-	1,620	477
	41,489	38,068	61,855

6.2.2 Investment in associates

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Unquoted shares, at cost	180	180	256
Share of post acquisition reserves	126	134	56
	306	314	312

6.2.3 Development costs

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cost	7,836	11,173	13,944
Accumulated amortisation	(4,148)	(6,019)	(7,582)
	3,688	5,154	6,362

6.2.4 Other intangible assets

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Intellectual property	1,288	1,036	784
Goodwill on consolidation	1,143	1,143	572
Goodwill on acquisition of business assets	1,703	-	-
	4,134	2,179	1,356

14. ACCOUNTANTS' REPORT (Cont'd)



6.2.5 Deferred tax assets/(liabilities)

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Deferred tax assets			
Unutilised tax losses	-	620	-
Deferred tax liabilities			
Unutilised tax losses	977	-	350
Temporary differences	(1,612)	(604)	(1,801)
	<u>(635)</u>	<u>(604)</u>	<u>(1,451)</u>

6.2.6 Inventories

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
At cost:			
Cranes	15,451	8,778	8,263
Crane components	19,170	25,620	32,781
Work-in-progress	14,719	14,964	16,354
At net realizable value:			
Cranes	7,092	5,643	5,737
Crane components	3,810	2,931	9,715
	<u>60,242</u>	<u>57,936</u>	<u>72,850</u>

	← As at 31 December 2005 →			
	0 – 30 days RM'000	30 – 60 days RM'000	> 60 days RM'000	Total RM'000
Inventories	1,470	35,390	35,990	72,850
% of inventories	<u>2.02</u>	<u>48.58</u>	<u>49.40</u>	<u>100.00</u>

14. ACCOUNTANTS' REPORT (Cont'd)



6.2.7 Trade and other receivables

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Progress billings receivable	9,325	13,230	2,414
Trade receivables	40,047	40,156	66,905
Less: Allowance for doubtful debts	(2,832)	(3,645)	(2,258)
	37,215	36,511	64,647
Amount due from contract customers	48,316	107,139	147,258
Holding company	544	1,702	4,262
Related companies	5,033	2,112	1,105
Associates	-	229	428
Affiliated companies	1,964	-	116
Other receivables, deposits and prepayments	3,634	7,297	8,213
	106,031	168,220	228,443

	Credit period	← As at 31 December 2005 →						Total RM'000
		← Within credit period →			← Exceeded credit period →			
		0 – 30 days	31 – 60 days	61 – 90 days	3 – 6 months	6 – 12 months	> 12 months	
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000		
Trade receivables	90 days	28,620	8,667	9,257	6,538	5,883	7,940	66,905
% of trade receivables		42.78	12.95	13.84	9.77	8.79	11.87	100.00

6.2.8 Cash and cash equivalents

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cash and bank balances	10,853	8,765	16,023
Deposit placed with a licensed bank	-	362	1,541
	10,853	9,127	17,564

14. ACCOUNTANTS' REPORT (Cont'd)



6.2.9 Trade and other payables

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Trade payables	29,425	51,455	88,927
Amount due to contract customers	3,233	14,772	20,385
Holding company	11,369	9,412	7,427
Related companies	2,430	2,984	4,261
Associates	438	-	50
Affiliated companies	486	491	468
Other payables and accrued expenses	15,776	17,065	24,799
	63,157	96,179	146,317

	Credit period	← As at 31 December 2005 →						Total RM'000
		← Within credit period →			← Exceeded credit period →			
		0 – 30 days RM'000	31 – 60 days RM'000	61 – 90 days RM'000	3 – 6 months RM'000	6–12 months RM'000	> 12 months RM'000	
Trade payables	60 days	57,081	10,617	9,483	6,983	2,796	1,967	88,927
% of trade payables		64.19	11.94	10.66	7.85	3.15	2.21	100.00

6.2.10 Bank overdrafts, loans and hire purchase

		← As at 31 December →		
		2003 RM'000	2004 RM'000	2005 RM'000
Current				
Term loans	-secured	3,810	5,528	6,329
	-unsecured	2,660	3,040	-
Bank overdrafts	-secured	-	2,523	2,296
	-unsecured	10,338	9,457	10,199
Revolving credits	-secured	-	-	1,323
	-unsecured	16,400	23,400	23,416
Onshore foreign currency loan	-unsecured	-	4,560	-
Insurance premium finance	-unsecured	-	1,960	772
Hire purchase liabilities		124	188	225
		33,332	50,656	44,560

14. ACCOUNTANTS' REPORT (Cont'd)



6.2.11 Provisions

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Current			
Warranties	3,677	5,156	6,467
Restructuring costs	-	5,832	3,939
	3,677	10,988	10,406
Non-current			
Warranties	1,722	828	-
	1,722	828	-

6.2.12 Term loans and hire purchase

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Non-current			
Term loans - secured	4,422	277	18,474
- unsecured	3,040	-	-
Hire purchase liabilities	145	228	509
	7,607	505	18,983

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6.3 Statements of changes in equity



	Share capital RM'000	Translation reserve RM'000	Reserves		Sub total RM'000	Total RM'000
			Reserves arising on consolidation RM'000	Retained profit/ (Accumulated losses) RM'000		
At 1 January 2003	50,000	4,728	2,145	(14,307)	(7,434)	42,566
Change in accounting policy	-	-	(2,145)	2,145	-	-
Effect of adopting FRS 3*	50,000	4,728	-	(12,162)	(7,434)	42,566
Restated balance	-	7,285	-	-	7,285	7,285
Exchange differences on translation of financial statements of foreign entities	-	7,285	-	-	7,285	7,285
Net gain not recognized in the income statement	-	(37)	-	-	(37)	(37)
Realisation of reserve on disposal of a subsidiary	-	-	-	1,589	1,589	1,589
Net profit for the year	50,000	11,976	-	(10,573)	1,403	51,403
At 31 December 2003/1 January 2004	-	3,049	-	-	3,049	3,049
Exchange differences on translation of financial statements of foreign entities	-	3,049	-	-	3,049	3,049
Net gain not recognized in the income statement	-	-	-	-	-	-
Net profit for the year	50,000	15,025	-	2,743	17,768	67,768
At 31 December 2004/1 January 2005	-	(4,597)	-	-	(4,597)	(4,597)
Exchange differences on translation of financial statements of foreign entities	-	(4,597)	-	-	(4,597)	(4,597)
Net gain not recognized in the income statement	-	-	-	7,180	7,180	7,180
Net profit for the year	50,000	10,428	-	9,923	20,351	70,351
At 31 December 2005						

*The Group early adopted FRS 3, Business Combinations, during financial year ended 31 December 2005. Comparatives have been restated to reflect the change in accounting policy.

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6.4 Consolidated cash flow statements

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cash flow from operating activities			
Profit before taxation	1,961	12,884	8,883
Adjustment for:			
Allowance for doubtful debts	846	1,131	329
Amortisation of development costs	1,053	1,608	2,011
Amortisation of intellectual property	252	252	252
Depreciation	7,445	6,808	7,832
(Gain)/Loss on disposal of property, plant and equipment	6	(18,794)	27
Goodwill written off	-	-	571
Interest expense	3,574	3,299	5,377
Interest income	(270)	(203)	(182)
Unrealised gain on foreign exchange	(5,732)	(4,296)	2,792
Share of profit of an associate (net of tax)	(3)	(8)	73
Inventory written off	424	-	-
Addition of provisions	2,744	13,037	4,498
Reversal of provisions	(2,853)	(1,647)	(2,194)
Operating profit before working capital changes	9,447	14,071	30,269
Changes in working capital:			
Development costs incurred	(4,377)	-	(3,496)
Inventories	6,530	2,306	(15,143)
Trade and other receivables	(29,598)	(62,653)	(63,137)
Trade and other payables	4,136	46,789	91,747
Cash (used in)/generated from operations	(13,862)	513	40,240
Interest paid	(1,524)	(1,814)	(3,666)
Interest received	270	203	182
Income taxes paid	(886)	(990)	(443)
Warranties paid	(754)	(965)	(3,463)
Net cash (used in)/generated from operating activities	(16,756)	(3,053)	32,850
Cash flow from investing activities			
Acquisition of associate	-	-	(76)
Proceeds from disposal of property, plant and equipment	1,124	86	77
Proceeds from disposal of a subsidiary	468	-	-
Purchase of property, plant and equipment	(3,573)	(9,206)	(34,710)
Net cash used in investing activities	(1,981)	(9,120)	(34,709)
Cash flow from financing activities			
Advance from holding company	6,002	1,201	844
Interest paid	(2,050)	(1,485)	(1,711)
Payment of hire purchase liabilities	(179)	(105)	(213)
Repayment of onshore foreign currency loan	-	-	(4,560)

14. ACCOUNTANTS' REPORT (Cont'd)



6.4 Consolidated cash flow statements (continued)

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cash flow from financing activities (continued)			
Proceeds from term loans	-	6,771	21,120
Proceeds from revolving credits	-	7,000	-
Repayment of term loans	(3,192)	(6,067)	(4,951)
Repayment of revolving credits	-	-	(60)
Net cash generated from financing activities	581	7,315	10,469
Exchange difference on translation of the financial statements of foreign operations	216	1,069	124
Net (decrease)/increase in cash and cash equivalents	(17,940)	(3,789)	8,734
Cash and cash equivalents at beginning of the year	15,502	515	(2,853)
Foreign exchange difference on opening balance	2,953	421	(812)
Cash and cash equivalents at end of year	515	(2,853)	5,069
Cash and cash equivalents comprise:-			
Cash and bank balances	10,853	8,765	16,023
Deposits	-	362	1,541
Bank overdrafts	(10,338)	(11,980)	(12,495)
	515	(2,853)	5,069

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14. ACCOUNTANTS' REPORT (Cont'd)



6.5 FFB

6.5.1 Summarised results

	Notes	← For the year ended 31 December →		
		2003 RM'000	2004 RM'000	2005 RM'000
Revenue	6.5.2	8,125	30	8,901
Operating profit before exceptional items		11,449	389	1,316
Other operating expenses				
- exceptional items	6.5.3	(9,163)	(4,650)	-
Other operating income				
- exceptional items	6.5.3	-	18,798	-
Operating profit		2,286	14,537	1,316
Interest expense		(509)	(576)	(955)
Interest income		3	3	4
Profit before taxation		1,780	13,964	365
Taxation		-	-	-
Profit after taxation		1,780	13,964	365
Effective tax rate (%) *		-	-	-
Gross margin (%)**		100.00	100.00	100.00
Pre-tax profit margin (%)		21.91	46,546.67	4.10
NTA per ordinary share (RM)		0.68	0.99	1.00
Current ratio (times)		1.52	1.41	2.03
Gearing ratio (times)		0.47	0.29	0.22
Interest coverage ratio (times)		4.50	25.24	1.38
Gross dividend rate*		-	-	-
After tax return on shareholders' funds (%)		4.89	27.72	0.72
Weighted average number of ordinary shares ('000)		50,000	50,000	50,000
Earnings per share (RM)	6.5.4			
- Gross		0.04	0.28	0.01
- Net		0.04	0.28	0.01

*The company's dividend income, rental income and interest income from overseas subsidiaries were exempted from tax

**There are no cost of sales as the company is principally an investment holding company, thus gross margin is 100%

14. ACCOUNTANTS' REPORT (Cont'd)



Notes to summary of results

6.5.2 Revenue

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Revenue			
Rental income	104	30	-
Dividends	8,021	-	8,901
	8,125	30	8,901
Growth rate (%)	127.15	(99.63)	29,570
<i>(Revenue in 2002: RM3,577k)</i>			

6.5.3 Exceptional items

The exceptional items in 2003 were related to loss on disposal of a subsidiary and allowance for doubtful debts.

The exceptional items in 2004 were in respect of gain on disposal of property, plant and equipment amounting to RM18.8 million; which was partially set-off by provision of restructuring costs of RM0.5 million, impairment loss on property, plant and equipment of RM2.5 million and write off of goodwill on acquisition of business assets amounting to RM1.7 million.

6.5.4 Earnings per share

The basic gross and net earnings per share are calculated based on the profit before and after taxation attributable over the weighted average number of ordinary shares outstanding during the year.

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14. ACCOUNTANTS' REPORT (Cont'd)



6.6 Summarised balance sheets

	← As at 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Property, plant and equipment	5,219	2,486	2,357
Investments in subsidiaries	29,027	29,027	29,027
Investment in associate	180	180	256
Deferred expenditure	-	557	350
Other intangible assets	2,252	439	329
Long term advances due from a subsidiary	39,805	33,456	24,244
	76,483	66,145	56,563
Current assets			
Trade and other receivables	30,489	30,558	38,753
Tax recoverable	20	23	27
Cash and cash equivalents	29	13	13
	30,538	30,594	38,793
Current liabilities			
Trade and other payables	6,034	6,787	7,678
Bank overdrafts, loans and hire purchase	14,060	14,440	11,416
Provisions	-	460	-
	20,094	21,687	19,094
Net current assets	10,444	8,907	19,699
	86,927	75,052	76,262
Financed by :-			
Share capital	50,000	50,000	50,000
(Accumulated losses)/Retained profits	(13,588)	376	741
Shareholder's funds	36,412	50,376	50,741
Deferred and long term liabilities :-			
Borrowings	3,040	-	-
Long term advances due to holding company	47,475	24,676	25,521
	50,515	24,676	25,521
	86,927	75,052	76,262

14. ACCOUNTANTS' REPORT (Cont'd)



6.7 Statements of changes in equity

	Share capital RM'000	Retained profit/ (Accumulated loss) RM'000	Total RM'000
At 1 January 2003	50,000	(15,368)	34,632
Net profit for the year	-	1,780	1,780
At 31 December 2003/1 January 2004	50,000	(13,588)	36,412
Net profit for the year	-	13,964	13,964
At 31 December 2004/1 January 2005	50,000	376	50,376
Net profit for the year	-	365	365
At 31 December 2005	50,000	741	50,741

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14. ACCOUNTANTS' REPORT (Cont'd)



6.8 Cash flow statements

	← For the year ended 31 December →		
	2003 RM'000	2004 RM'000	2005 RM'000
Cash flow from operating activities			
Profit before taxation	1,780	13,964	365
Adjustment for:			
Allowance for doubtful debts	9,000	-	6,000
Amortisation of intellectual property	110	110	110
Depreciation	69	17	129
Gain on disposal of property, plant and equipment	-	(18,798)	-
Interest expense	509	576	955
Interest income	(3)	(3)	(4)
Unrealised (gain)/loss on foreign exchange	(3,534)	(1,133)	1,169
Addition of provisions	-	4,650	-
Reversal of provisions	-	-	(460)
Loss on disposal of a subsidiary	163	-	-
Operating profit/(loss) before working capital changes	8,094	(617)	8,264
Changes in working capital:			
Inventories	-	-	-
Trade and other receivables	(7,633)	1,883	(8,312)
Trade and other payables	(5,044)	753	891
Cash (used in)/generated from operations	(4,583)	2,019	843
Interest paid	(509)	(576)	(955)
Interest received	3	3	4
Income taxes paid	(15)	(3)	(4)
Net cash (used in)/generated from operating activities	(5,104)	1,443	(112)
Cash flow from investing activities			
Acquisition of associate	-	-	(76)
Repayment from a subsidiary	29	-	3,212
Proceeds from disposal of a subsidiary	597	-	-
Net cash generated from investing activities	626	-	3,136
Cash flow from financing activities			
Advance from holding company	6,002	1,201	-
Repayment of term loans	(1,520)	(2,660)	(3,024)
Net cash generated from/(used in) financing activities	4,482	(1,459)	(3,024)
Net increase/(decrease) in cash and cash equivalents	4	(16)	-
Cash and cash equivalents at beginning of the year	25	29	13
Cash and cash equivalents at end of year	29	13	13
Cash and cash equivalents comprise:-			
Cash and bank balances	29	13	13

14. ACCOUNTANTS' REPORT (Cont'd)**7. Summary of significant accounting policies**

The following accounting policies are adopted by the FFB Group and are consistent with those adopted in previous years except for the early adoption of the following Financial Reporting Standards ("FRS") in 2005:-

- (i) FRS 3, Business Combination;
- (ii) FRS 136, Impairment of Assets, and
- (iii) FRS 138, Intangible Assets

The effects of the changes in the above accounting policies are disclosed in Item 9 to these financial statements.

(a) Basis of accounting

The proforma consolidated financial statements of the FFB Group are prepared on the historical cost basis except as disclosed in the notes to the proforma consolidated financial statements and in compliance with the provisions of the Companies Act, 1965 and applicable approved accounting standards in Malaysia.

(b) Basis of consolidation

Subsidiaries are those enterprises controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

Investment in subsidiaries are stated in the Company's balance sheet at cost less impairment losses. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

A subsidiary is excluded from consolidation when either control is intended to be temporary if the subsidiary is acquired and held exclusively with a view of its subsequent disposal in the near future and it has not previously been consolidated or it operates under severe long term restrictions which significantly impair its ability to transfer funds to the Company. Subsidiaries excluded on these grounds are accounted for as investments.

All business combinations are accounted for by applying the purchase method.

Under the purchase method of accounting, the results of subsidiaries acquired or disposed of during the year are included from the date of acquisition or up to the date of disposal. At the date of acquisition, the fair values of the subsidiaries' net assets are determined and these values are reflected in the FFB Group financial statements. The excess of the acquisition cost over the fair values of the subsidiaries' net assets is reflected as goodwill. The excess of the fair values of the subsidiaries' net assets over the acquisition cost, after reassessment, is recognised immediately in the income statement.

Intragroup transactions and balances and the resulting unrealised profits are eliminated on consolidation. Unrealised losses resulting from intragroup transactions are also eliminated unless cost cannot be recovered.

14. ACCOUNTANTS' REPORT (Cont'd)



7. Summary of significant accounting policies (continued)

(c) Associate

Associates are those enterprise in which the FFB Group has significant influence, but not control, over the financial and operating policies.

The consolidated financial statements include the total recognised gains and losses of associates on an equity accounted basis from the date that significant influence effectively commences until the date that significant influence effectively ceases.

Unrealised profits arising on transactions between the FFB Group and its associates which are included in the carrying amount of the related assets and liabilities are eliminated partially to the extent of the FFB Group's interests in the associates. Unrealised losses on such transactions are also eliminated partially unless cost cannot be recovered.

Goodwill on acquisition is calculated based on the fair value of net assets acquired.

(d) Affiliated company

An affiliated company is a company in which the holding company holds a long term investment of between 20% to 50% of the equity capital.

(e) Property, plant and equipment

Freehold land and capital work-in-progress are stated at cost. All other property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses, if any.

Depreciation

Depreciation commences when the assets are ready for their intended use.

Freehold land and capital work-in-progress are not amortised.

The straight-line method is used to write off the cost of the other assets over the term of their estimated useful lives at the following principal annual rates:

Buildings	2% - 10%
Cranes	6 $\frac{2}{3}$ % - 10%
Plant, equipment and motor vehicles	8% - 33 $\frac{1}{3}$ %

(f) Intangible assets

(i) *Development costs*

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the income statement as an expense as incurred.

Expenditure on development activities, where research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the FFB Group has sufficient resources to complete development.

14. ACCOUNTANTS' REPORT (Cont'd)**7. Summary of significant accounting policies (continued)****(f) Intangible assets (continued)****(i) Development costs (continued)**

The expenditure capitalised includes the remuneration of staff directly involved in the development activities, cost of materials and an appropriate proportion of overheads. Other development expenditure is recognised in the income statement as an expense as incurred. Capitalised development expenditure is stated at cost less accumulated amortisation and impairment losses, if any.

Capitalised development expenditure is amortised and recognised as an expense on a systematic basis so as to reflect the pattern in which the related economic benefits are recognised of five to eight years.

(ii) Intellectual property

Intellectual property consists of rights to trade name, know how and industrial property rights and is stated at cost less accumulated amortisation and impairment losses, if any. Intellectual property is amortised and recognised as an expense over ten years on a systematic basis so as to reflect the pattern in which the related economic benefits are recognised, unless the Directors consider that a continuing benefit will not accrue.

(iii) Goodwill arising on consolidation

Goodwill arising on consolidation represents the difference between the acquisition cost and the fair values of the net identifiable assets acquired of the subsidiaries and associates at the date of acquisition.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is not amortised but is tested annually for impairment. In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment in the associate.

(g) Investments

Investments in subsidiaries and associates are stated at cost in the Company, less impairment loss, where applicable. An allowance is made when the Directors are of the view that there is a diminution in their value which is other than temporary.

(h) Trade and other receivables

Trade and other receivables are stated at cost less allowance for doubtful debts.

(i) Employee benefits**(i) Short term employee benefits**

Wages, salaries and bonuses are recognised as expenses in the year in which the associated services are rendered by employees of the Group. Short term accumulating compensated absences such as paid annual leave are recognised when services are rendered by employees that increase their entitlement to future compensated absences, and short term non-accumulating compensated absences such as sick leave are recognised when absences occur.

14. ACCOUNTANTS' REPORT (Cont'd)**7. Summary of significant accounting policies (continued)****(i) Employee benefits (continued)****(ii) Defined contribution plans**

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

(j) Provision

A provision is recognised when it is probable that an outflow of resources embodying economic benefits will be required to settle a present obligation (legal or constructive) as a result of a past event and a reliable estimate can be made of the amount.

(i) Provision for warranties

A provision for warranties for the manufacture of cranes is recognised when the defect liability periods have commenced. It is based on historical warranty data and a weighting of all possible outcomes against the associated probabilities.

(ii) Provision for restructuring cost

A provision for restructuring cost is recognised when the FFB Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

(k) Liabilities

Borrowings and trade and other payables are stated at cost.

(l) Amount due from/(to) contract customers

Amount due from/(to) contract customers on the manufacture of cranes is stated, using the percentage of completion method, at cost plus attributable profits less foreseeable losses and less progress billings. Cost includes all direct construction costs and other related costs. Where progress billings exceed the aggregate amount due from contract customers plus attributable profits less foreseeable losses, the net credit balance on all such contracts is shown in trade and other payables as amount due to contract customers.

(m) Inventories

Inventories comprise crane components, work-in-progress and assembled cranes and are stated at the lower of cost and net realisable value. Crane components are determined on a first-in, first-out basis. Cost of work-in-progress and assembled cranes are determined on a specific identification basis.

Cost of crane components comprises the original purchase price plus incidentals in bringing these inventories to their present location and condition.

Cost of work-in-progress and assembled cranes consist of crane components, direct labour and an appropriate proportion of fixed and variable production overhead.

14. ACCOUNTANTS' REPORT (Cont'd)**7. Summary of significant accounting policies (continued)****(n) Cash and cash equivalents**

Cash and cash equivalents consist of cash on hand, balances and deposits with banks and highly liquid investments which have an insignificant risk of changes in value. For the purpose of the cash flow statement, cash and cash equivalents are presented net of bank overdrafts.

(o) Impairment

The carrying amount of assets, other than inventories, assets arising from construction contracts and deferred tax assets and financial assets (other than investments in subsidiaries and associates), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For goodwill, intangible assets that have an indefinite useful life and intangible assets that are not yet available for use, the recoverable amount is estimated at each annual balance sheet date.

An impairment loss is recognised whenever the carrying amount of an asset or the cash-generating unit to which it belongs exceeds its recoverable amount. Impairment losses are recognised in the income statement, unless the asset is carried at a revalued amount, in which case the impairment loss is charged to equity.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units (group of units) and then, to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount is the greater of the asset's net selling price and its value in use. In assessing value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. However, an impairment loss in respect of goodwill is not reversed.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. The reversal is recognised in the income statement, unless it reverses an impairment loss on a revalued asset, in which case it is taken to equity.

(p) Hire purchase

Property, plant and equipment acquired under hire purchase arrangements are capitalised at their purchase cost and depreciated on the same basis as owned assets. The total amounts payable under hire purchase agreements are included as hire purchase liabilities.

14. ACCOUNTANTS' REPORT (Cont'd)

**7. Summary of significant accounting policies (continued)****(q) Capitalisation of borrowing costs**

Borrowing costs incurred on development activities are capitalised. Capitalisation of borrowing costs will cease when the assets are ready for their intended use.

The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation is the weighted average of the borrowing costs applicable to the FFB Group's borrowings that are outstanding during the year.

Capitalisation of borrowing costs is suspended during extended periods in which active development is interrupted.

(r) Income tax

Tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Deferred tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Temporary differences are not recognised for goodwill not deductible for tax purpose and the initial recognition of assets or liabilities that at the time of transaction affects neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

(s) Foreign currency**(i) Foreign currency transactions**

Transactions in foreign currencies are translated to Ringgit Malaysia at rates of exchange ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Ringgit Malaysia at the foreign exchange rates ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated to Ringgit Malaysia at the foreign exchange rates ruling at the date of transactions.

14. ACCOUNTANTS' REPORT (Cont'd)



7. Summary of significant accounting policies (continued)

(s) Foreign currency (continued)

(ii) Financial statements of foreign operations

The FFB Group's foreign operations are not considered an integral part of the Group's operations. Accordingly, the assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to Ringgit Malaysia at exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to Ringgit Malaysia at average exchange rates applicable throughout the year. Foreign exchange differences arising on translation are recognised directly in equity.

The closing rates used in the translation of foreign currency monetary assets and liabilities and the financial statements of foreign operations are as follows:

1USD	RM3.78	(2004: 1USD	RM3.80)
1SGD	RM2.27	(2004: 1SGD	RM2.32)
1AUD	RM2.76	(2004: 1AUD	RM2.96)
1DKK	RM0.60	(2004: 1DKK	RM0.70)
1GBP	RM6.52	(2004: 1GBP	RM7.31)
1EURO	RM4.48	(2004: 1EURO	RM5.17)
1THB	RM0.09	(2004: 1THB	RM0.10)
1BND	RM2.27	(2004: 1BND	RM2.32)

(t) Revenue

(i) Construction contracts

Revenue from the manufacture of cranes is recognised on the percentage of completion method, measured by reference to the proportion of contract costs incurred for contract work performed to date that reflect work performed bear to the total estimated contract costs.

When the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that is probable will be recoverable and contract costs are recognised as an expense in the period in which they are incurred.

An expected loss on a contract is recognised immediately in the income statement.

(ii) Goods sold and services rendered

Revenue from trading of crane inventories and crane components is measured at the fair value of the consideration receivable and 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 by reference to the value of works performed. Where the outcome of the transaction cannot be estimated reliably, revenue is recognised only to the extent of the expenses recognised that are recoverable.

Revenue from rental of cranes and premises is recognised in the income statement as it accrues.

14. ACCOUNTANTS' REPORT (Cont'd)

**7. Summary of significant accounting policies (continued)****(t) Revenue (continued)****(iii) Dividend income**

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

(iv) Interest income

Interest income is recognised in the income statement as it accrues, taking into account the effective yield on the asset.

When the Directors are of the view that recoverability of the interest income is uncertain, interest is suspended until it is realised on cash basis.

(u) Expenses**(i) Hire purchase payment**

The interest component of hire purchase payments is recognised in the income statement so as to give a constant periodic rate of interest on the outstanding liability at the end of each accounting period.

(ii) Financing costs

All interest and other costs incurred in connection with borrowings are expensed as incurred, other than borrowing costs directly attributable to the development activities which are capitalized.

8. Restatement of prior year balances

During the financial year ended 31 December 2005, the Group early adopted FRS 3, Business Combinations, which becomes effective for the financial year beginning on or after 1 January 2006. In accordance with the transitional provisions of FRS 3, the negative goodwill was derecognised with a corresponding adjustment to the opening balance of the retained earnings at 1 January 2005.

The financial statements of the Group for the years ended 31 December 2003 and 2004 have been restated for the derecognition of the negative goodwill. The effect of the change in accounting policy had been reflected in the statement of changes in equity.

14. ACCOUNTANTS' REPORT (Cont'd)



9. Comparative figures

The following comparatives have been restated to reflect the change in accounting policy as explained in Item 8.

Statement of changes in equity	Group	
	As restated RM'000	As previously stated RM'000
Group		
Accumulated losses at 1 January 2003	12,162	14,307
Accumulated losses at 1 January 2004/31 December 2003	10,573	12,718
Retained profits at 31 December 2004	2,743	598
	=====	=====

10. Event subsequent to the balance sheet date

On 24 March 2006, the Securities Commission approved the proposed listing of Favelle Favco Berhad on the Second Board of Bursa Malaysia Securities Berhad, subject to the fulfilment of certain conditions.

Yours faithfully,

KPMG
Firm Number: AF 0758
Chartered Accountants

Foong Mun Kong
Partner
Approval Number: 2613/12/06(J)