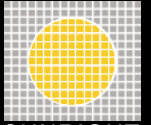


KESM INDUSTRIES BERHAD
(13022-A)

ANNUAL REPORT 2006

A Member of



SUNRIGHT



KESM, a world class award winning Company

Shipped Over 3 Billion Chips

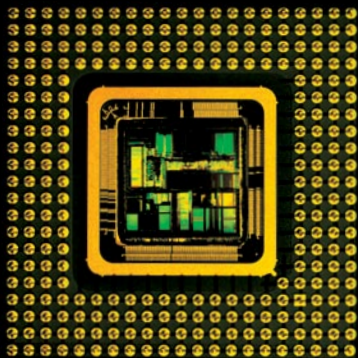
Approved By United States Defense
(DSCC)

Certified by BVQI-Car Quality Standard
(TS 16949)

Recognized By ISO 9000

Managed by 1,400 motivated and
committed employees

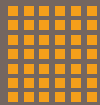




Backed by 28 years of solid experience and quality reputation, KESM is the largest independent provider of “burn-in and test” services in Malaysia. We enable our customers to create reliable chips for electronic products. We have established our market leadership in “burn-in and testing” of semiconductor devices for automotive, personal computers, communications and military applications. The Group shipped over 3 billion chips and we are still counting. When placed side by side, the chips form a continuous line wrapping twice around the circumference of the earth. We achieved success by our persistent focus on customer service, an interactive network of strategic partners constantly driving leading edge products, a relentless effort for continuous quality improvements, substantial investments on advanced equipment as well as a close alliance with Sunright to ride on their global network.

Chairman’s Statement	2	Directors’ Report,	
Board of Directors	4	Report of the Auditors and	25
Other Information on Directors	8	Audited Financial Statements	
Corporate Information	9	Shareholders’ Information	62
Audit Committee’s Report	10	Group Properties	65
Terms of Reference of Audit Committee	12	Notice of Annual General Meeting	66
Corporate Governance Statement	16	Notice of Dividend Entitlement	69
Other Information	21	Statement Accompanying	
Statement on Internal Control	22	Notice of Annual General Meeting	70
		Proxy Form	

CHAIRMAN'S STATEMENT



Dear Fellow Shareholders

For the third consecutive year, KESM Group achieved new record earnings and delivered the highest shipments of microchips. Once again, our management team swiftly executed many successful new product introductions or "NPI" devices, which were seamlessly introduced into high volume productions. We worked with our customers and built strong quality culture. We are emerging as a world class service company.

FINANCIAL PERFORMANCE

Even though the improved turnover in the second half of FY 2006 was significantly higher than the first half, it was not able to cover the weakness of a lower utilization of the equipment capacities in the first half. Consequently, the total sales dropped by 10 percent from RM181 million in 2005 to RM162.2 million in 2006. We trimmed expenses and aligned our costs to revenues. We recorded a net profit of RM14.1 million as compared to RM14.0 million in the last financial year.

CURRENT YEAR DEVELOPMENTS

We continued to achieve strong profits. We maintained our cash reserve of RM54.3 million and increased our net worth by 11%. We spent RM36.1 million in capital investments. The Group had funded this growth through a combination of working capital and external borrowings, without any capital raising exercise.

While these results are encouraging we have to continue to invest and ensure that we have the technology as well as people and financial resources to seize every prospective opportunity. In a highly capital intensive industry, the ready access to capital financing is a crucial factor to our success. With every new chip introduced by our clients to the markets, there are opportunities to upgrade and invest in the next generation of equipment in support of their advanced technology. We not only upgrade our technology to compete, we drive competitiveness by improving our process quality. In working closely with our customers, we launched 5 major quality improvement programs. These initiatives resulted in significant production yield improvements and cost savings. We were commended for our performances. The high reliability processing standard that we delivered to the automotive industry has built up our market reputation. Our quality service – particularly the quick response that we give to every customer – is our hallmark. We also won a major order to process components to U.S. military precision requirements, affirming KESM's ability to meet high demanding quality standard. These series of achievements provided a platform for a local operation to emerge as a world-class supplier.

BUSINESS OUTLOOK

In our focus on high growth market opportunities such as automobiles, personal computers and communication products, there is one thing in common – product changes! These products are constantly improving to meet the changes in consumer lifestyle. Every new product requires new chips to work reliably. KESM provides a service to stress the chips in an elevated temperature by a process known as “burn-in”. The “fittest” chips or absolutely reliable chips are “tested” and returned to our customers to manufacture electronic products assembled in note books, mobile phones etc. As demand for consumer digital electronics escalates, our customers are adding more and more features into their microchips. These mobile devices are growing and bringing opportunities for KESM.

We remain committed to our core businesses. “Burn-in and test” and “EMS” services have been the fundamental “building blocks” of our success. “Testing” services will form our next building block. The industry forecast for 2007 remains good. Gartner Inc. expects the industry to grow to new record levels from US\$257 billion in 2006 to US\$280 billion in 2007. We believe the market confidence will continue into 2007 as many of our customers are expanding their facilities and showing strong financial results. Apart from the concern of rising energy cost which will affect our operational margin, the change in ownership with a major client, which is waiting to be consummated, may have an impact on our business that is indeterminate at this time. Nevertheless, we are excited

with the increasing opportunities. We will continue to build on our #1 position in the market and remain focused in driving our businesses.

DIVIDEND

We are operating in the bright market segments of the industry and the growth forecast for FY 2007 remains good. Further investments will be necessary to accelerate our performance. Your Board has decided to change the dividend practice from maintaining a fixed dividend rate yearly, regardless of the performance of the Company, to a variable dividend rate, taking into account the Company’s performance and in relation to the climate governing the semiconductor industry. Given this change, the Board has recommended a first and final tax exempt dividend of 3%, amounting to approximately RM1,290,000 in respect of the financial year ended 31st July 2006. Subject to the approval of the shareholders at the forthcoming Annual General Meeting, the dividend will be paid on 2 February 2007.

I want to thank you for your interest in our Company. On behalf of the Board and our employees in the Company, we will always do our very best to make the most of our opportunities in the new year.

Samuel Lim Syn Soo
Executive Chairman
5 October 2006



BOARD OF DIRECTORS



MR. SAMUEL LIM SYN SOO
Aged 52, Singaporean
Non-Independent Executive Director

Mr. Samuel Lim is the Executive Chairman and Chief Executive Officer of the Company and has been on the Board since 6 September 1986. He is also a member of the Option Committee. Mr. Lim co-founded and led the Company to become Malaysia's largest independent provider of burn-in and testing services.

Mr. Lim has more than 36 years of experience in the semiconductor and electronics industry. Prior to KESM Industries Berhad, Mr. Lim held various senior positions in engineering, manufacturing and marketing at several multinational companies. As one of the local pioneers in the semiconductor industry, Mr. Lim also invented solutions to "Burn-in and test" of individual chips and was awarded three patents. He also sits on the Board of all the companies in Sunright Limited, a company listed on the Main Board of the Singapore Exchange Securities Trading Limited.

Mr. Lim holds a Diploma in Industrial Engineering (Canada) and was a registered engineer with the WOFAC Association.

Mr. Lim's holdings in the securities of the Company are as follows: -

	Direct Shareholdings	Indirect Shareholdings
Ordinary Shares of RM1.00 each	Nil	20,825,000 (Deemed interest by virtue of his substantial interest in Sunright Limited)
Share options of RM1.00 each	216,800	Nil



MR. KENNETH TAN TEOH KHOON
Aged 49, Singaporean
Non-Independent Executive Director

Mr. Tan was appointed to the Board on 20 January 1992. He is responsible for the strategic direction and new business initiatives of the Group, and the management of the Group's financial, corporate and investor relations. He is also a member of the Audit Committee and Option Committee of the Company.

Mr. Tan graduated with a Bachelor of Accountancy degree from the National University of Singapore and was a member of the Institute of Chartered Secretaries and Administrators, United Kingdom. He has been admitted as a Fellow of the Institute of Certified Public Accountants of Singapore.

Prior to joining the Group in 1987, he worked in an international accounting firm, a major property group in Singapore and subsequently in a diversified multinational group in the manufacturing and packaging industries.

Mr. Tan is currently an executive director of Sunright Limited and also sits on the Board of several other private limited companies in Singapore, Hong Kong, Malaysia, Taiwan, China, Philippines, Thailand and USA.

Mr. Tan's holdings in the securities of the Company are as follows: -

	Direct Shareholdings	Indirect Shareholdings
Share options of RM1.00 each	216,800	Nil



MS. LIM MEE ING
Aged 55, Singaporean
Non-Independent Non-Executive Director

Ms. Lim was appointed to the Board on 19 February 1990. She holds a Diploma from the Institute of Bankers, and has more than 18 years of working experience in the banking profession before her retirement in 1990. From 1973 to 1990, she worked with the Singapore Branch of Barclays Bank PLC in various senior positions. Prior to her exit, she was responsible for marketing the global securities and custodian services of the bank. Ms. Lim was also a director of Barclays Bank (S) Nominees Pte Ltd from September 1982 to March 1990. She was a member of the Committee on Securities Industry of the Association of Banks in Singapore from September 1987 to March 1990.

Ms. Lim is currently a non-executive director of Sunright Limited and also sits on the Board of several other private limited companies in Singapore and China.

BOARD OF DIRECTORS



DATO' DR. NORRAESAH HAJI MOHAMAD
Aged 58, Malaysian
Independent Non-Executive Director

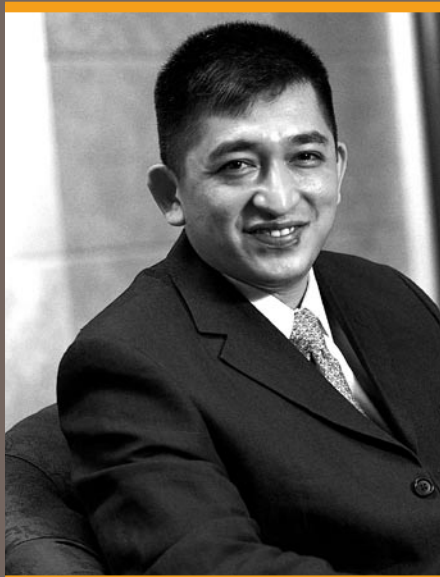
Dato' Dr. Norraesah was appointed to the Board on 20 October 1991. She is also the Chairman of the Audit Committee of the Company. Dato' Dr. Norraesah holds a Doctorate Degree in Economics Science (International Economics and Finance) from the University of Paris I, Pantheon-Sorbonne, France in 1986. She has over 34 years of working experience in banking, consultancy and international trade and commerce.

Dato' Dr. Norraesah worked with the International Trade Division of the Ministry of Trade and Industry (now known as the Ministry of International Trade and Industry) from 1972 to 1985, starting as an Assistant Director and later promoted to Senior Assistant Director. Between October 1987 to September 1988, she was with the Finance Division of the Federal Treasury holding the post of Principal Assistant Secretary. From October 1988 to October 1990, she was the Communication Manager of ESSO Production Malaysia Inc. and subsequently, took the position of Managing Director with a consultant firm providing financial advisory services. From 1991 to 1998, she was appointed as the Chief Representative of Credit Lyonnais Bank in Malaysia. She assumed the position of Chairman of Bank Rakyat from 2000 to 2003.

She is currently the Non-Executive Chairman of Penang Bridge Sdn. Bhd., Executive Chairman of MyEG Services Berhad and Embunaz Ventures Sdn Bhd and also sits on the Boards of Adventa Berhad, Ya Horng Electronic (M) Berhad, Protasco Berhad, SBC Corporation Berhad and Malaysian Oxygen Berhad, all listed on Bursa Malaysia Securities Berhad, and several other private limited companies in Malaysia.

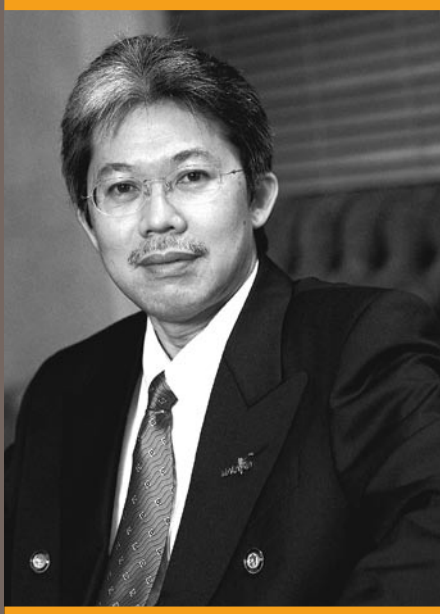
Dato' Dr. Norraesah's holdings in the securities of the Company are as follows: -

	Direct Shareholdings	Indirect Shareholdings
Ordinary Shares of RM1.00 each	7,500	604,500



ENCIK AHMAD RIZA BIN BASIR
Aged 46, Malaysian
Independent Non-Executive Director

Encik Ahmad Riza was appointed to the Board on 28 July 1994 and is also a member of the Audit Committee of the Company. Encik Ahmad Riza Bin Basir is a lawyer by training. He graduated with Bachelor of Arts in Law (Honours) degree from University of Hertfordshire, Hertford, United Kingdom and Barrister At Law (Lincoln's Inn), London in 1984 and was called to the Malaysian Bar in 1986. He is currently the Chairman of Fima Corporation Berhad. In addition, he is the Group Managing Director of Kumpulan Fima Berhad, a Director of Jerneh Asia Berhad, Jerneh Insurance Berhad, Manulife Insurance (Malaysia) Berhad, Malaysian Transnational Trading (MATTRA) Corporation Bhd and United Plantations Berhad. He also sits on the Boards of several other private limited companies in Malaysia.



TUAN HAJI ZAKARIAH BIN YET, AMS, AMN
Aged 51, Malaysian
Non-independent Non-Executive Director

Tuan Haji Zakariah has been serving as a member of the Board on 27 January 1995, as a representative of Lembaga Tabung Haji.

He has been with Lembaga Tabung Haji since 1979 and has served in several departments, including Finance, Administration, Investment and Branch Office operation.

In addition, he has wide experience in the private sector, holding important positions in two subsidiaries of Lembaga Tabung Haji which among others were as the Deputy Chief Executive Officer of TH Global Services Sdn Bhd from 16 June 2001 to 31 August 2002; Senior General Manager and Acting Chief Executive Officer of TH Travel & Services Sdn Bhd from 1 September 2002 to 16 August 2004. He was also a Board member at Urus Bina Sdn Bhd from 1994 to 1995.

Currently, Tuan Haji Zakariah is attached at Lembaga Tabung Haji as the General Manager of Human Resource Development and Quality Department.

He has a Diploma in Banking Studies from ITM and a Post Graduate Diploma in Engineering Business Management from UTM. He then undertook a twinning programme at Warwick University, United Kingdom and attained a Master of Science in Engineering Business Management.



MR. YONG CHEE HOU
Aged 50, Malaysian
Independent Non-Executive Director

Mr. Yong was appointed to the Board on 11 January 2002 and is also a member of the Audit Committee of the Company. He graduated from the University of Hull, United Kingdom with a Bachelor of Science (Hons) Degree in Economics and Accounting and qualified as a member of the Institute of Chartered Accountants in England and Wales. He is a member of Malaysian Institute of Accountants. He has spent over 9 years in accountancy profession. Mr. Yong is also a director of a private limited company.

OTHER INFORMATION ON DIRECTORS

1. FAMILY RELATIONSHIP

None of the Directors have any family relationship with other Directors except for Ms. Lim Mee Ing, who is the spouse of Mr. Samuel Lim.

2. CONFLICT OF INTEREST

None of the Directors have any conflict of interest with the Company except for Messrs Samuel Lim, Kenneth Tan, Lim Mee Ing and Dato' Dr. Norraesah Haji Mohamad who are deemed to be interested in any transactions or contracts that the Group made or proposed to make with Sunright Group.

3. CONVICTIONS OF OFFENCES

None of the Directors have been convicted of any offence within the past ten (10) years other than traffic offence, if any.

4. DETAILS OF ATTENDANCE AT BOARD MEETINGS HELD IN THE FINANCIAL YEAR ENDED 31 JULY 2006

Name of Directors	No. of Meetings Attended	Percentage %
Mr. Samuel Lim Syn Soo	5 out of 5	100
Mr. Kenneth Tan Teoh Khoon	5 out of 5	100
Ms. Lim Mee Ing	5 out of 5	100
Dato' Dr. Norraesah Haji Mohamad	3 out of 5	60
Encik Ahmad Riza Bin Basir	5 out of 5	100
Tuan Haji Zakariah Bin Yet	5 out of 5	100
Mr. Yong Chee Hou	4 out of 5	80

CORPORATE INFORMATION

BOARD OF DIRECTORS

Mr. Samuel Lim Syn Soo

(Executive Chairman & Chief Executive Officer)

Mr. Kenneth Tan Teoh Khoon

(Executive Director)

Ms. Lim Mee Ing

(Non-Independent Non-Executive Director)

Dato' Dr. Norraesah Haji Mohamad

(Independent Non-Executive Director)

Encik Ahmad Riza Bin Basir

(Independent Non-Executive Director)

Tuan Haji Zakariah Bin Yet

(Non-Independent Non-Executive Director)

Mr. Yong Chee Hou

(Independent Non-Executive Director)

AUDIT COMMITTEE

Dato' Dr. Norraesah Haji Mohamad

(Chairman)

Mr. Kenneth Tan Teoh Khoon

(Member)

Encik Ahmad Riza Bin Basir

(Member)

Mr. Yong Chee Hou

(Member)

COMPANY SECRETARY

Ms. Leong Oi Wah

(MAICSA 7023802)

REGISTERED OFFICE

312, 3rd Floor
Block C, Kelana Square
17 Jalan SS7/26
47301 Petaling Jaya
Selangor Darul Ehsan
MALAYSIA
Tel: 03-7803 1126/7806 2116
Fax: 03-7806 1387/7806 1261

REGISTRARS

Symphony Share Registrars Sdn Bhd
Level 26, Menara Multi Purpose Capital Square
No. 8, Jalan Munshi Abdullah
50100 Kuala Lumpur
MALAYSIA
Tel: 03-2721 2222
Fax: 03-2721 2530/31

AUDITORS

Ernst & Young
Chartered Accountants
Level 23A, Menara Milenium
Jalan Damanlela
Pusat Bandar Damansara
50490 Kuala Lumpur
MALAYSIA

STOCK EXCHANGE LISTING

Bursa Malaysia Securities Berhad
Second Board

STOCK NAME

KESM

BURSA SECURITIES STOCK NO.

9334



AUDIT COMMITTEE'S REPORT

The Audit Committee ("the Committee") of KESM Industries Berhad is pleased to present the Audit Committee's Report for the financial year ended 31 July 2006 ("Year 2006").

MEMBERS OF THE AUDIT COMMITTEE

The Committee currently comprises the following directors: -

Chairman	:	Dato' Dr. Norraesah Haji Mohamad	Independent Non-Executive Director
Members	:	Mr. Kenneth Tan Teoh Khoon	Executive Director
	:	Encik Ahmad Riza Bin Basir	Independent Non-Executive Director
	:	Mr. Yong Chee Hou	Independent Non-Executive Director

The Committee is governed by the Terms of Reference as set out in pages 12 to 15 of this Annual Report.

MEETINGS DURING THE YEAR

The Committee met four (4) times in Year 2006. Other Board members, senior management staff and the company secretary attended the meetings upon invitation of the Committee. The representatives of the internal and external auditors were also present during deliberations which required their inputs and advice.

The meeting attendance record of the Committee members is as follows:

Name of Member	Designation	No. of Meetings held during the year	No. of Meetings attended	Percentage %
Dato' Dr. Norraesah Haji Mohamad	Chairman	4	2	50
Mr. Kenneth Tan Teoh Khoon	Member	4	4	100
Encik Ahmad Riza Bin Basir	Member	4	4	100
Mr. Yong Chee Hou	Member	4	3	75

SUMMARY OF THE ACTIVITIES OF THE COMMITTEE

During Year 2006, the Committee: -

1. reviewed the external auditors' reports in relation to the audit for the year ended 31 July 2005.
2. discussed and recommended the audited financial statements of the Company and of the Group for the year ended 31 July 2005 to be presented to the Board of Directors for approval.
3. recommended the re-appointment of the external auditors.
4. reviewed, discussed and recommended the unaudited quarterly results of the Group to be presented to the Board of Directors for approval.
5. reviewed and recommended related party transactions of the Group to be presented to the Board of Directors for ratification and approval.
6. reviewed and approved Internal Audit Charter and Internal Audit Plan.
7. reviewed and discussed the internal auditor's reports.
8. reviewed the Committee's Report in respect of the financial year ended 31 July 2005 and presented to the Board of Directors for approval.
9. reviewed the proposed amendments to the Terms of Reference of Audit Committee.

INTERNAL AUDIT ACTIVITIES

During the financial year, the internal auditors presented the audit reports in relation to the internal audit activities carried out according to the internal audit plan, which have been approved by the Committee. To monitor and ensure that audit recommendations have been effectively implemented, follow-up audit reviews reports on prior years' audits were also presented to the Committee.

EMPLOYEES SHARE OPTION SCHEME ("ESOS")

In accordance with the Listing Requirements of Bursa Malaysia Securities Berhad and pursuant to the ESOS for Year 2006, the grant of 160,000 share options in November 2005 to eligible executives were accurately offered.

A verification exercise was carried out for Year 2006 and the Committee is satisfied that the allocation of the above share options has complied with the criteria set out in the by-laws of the ESOS.



TERMS OF REFERENCE OF AUDIT COMMITTEE

1. CONSTITUTION

The Board has, on 19 September 2005, resolved to adopt these Revised Terms of Reference, for the Committee to carry out the responsibilities and functions prescribed in Part C of Chapter 15 of the Listing Requirements of Bursa Malaysia Securities Berhad (“Bursa Securities”).

2. COMPOSITION / QUORUM

The Committee shall be appointed by the Board from amongst the Directors of the Company and shall consist of not less than 3 members, of which the majority shall be Independent Directors of the Company; and at least one member of the Committee: -

- a) must be a member of the Malaysian Institute of Accountants; or
- b) if he/she is not a member of the Malaysian Institute of Accountants, he/she must have at least 3 years’ working experience and: -
 - i) he/she must have passed the examinations specified in Part I of the 1st Schedule of the Accountants Act 1967; or
 - ii) he/she must be a member of one of the associations of accountants specified in Part II of the 1st Schedule of the Accountants Act 1967; or
 - iii) fulfils such other requirements as prescribed by Bursa Securities.

In the event that a member of the Committee resigns, dies or for any other reason ceases to be a member resulting in non-compliance of any of the requirements above, the Board shall, within 3 months of that event, appoint such number of new members as may be required to fill the vacancy.

Alternate Directors shall not be appointed as members of the Committee.

3. TERMS OF MEMBERSHIP

Members of the Committee shall be appointed for an initial term of 3 years after which they will be eligible for re-appointment.

The appointment and performance of the members shall be subject to review by the Board at least once every 3 years to determine whether such members have carried out their duties in accordance with these terms of reference.

4. CHAIRMAN

The members shall elect a Chairman from among their number who shall be an Independent Director.

5. SECRETARY

The Company Secretary or his or her nominee shall be the Secretary of the Committee. In his or her absence, the Chairman shall appoint the Secretary.

6. MEETINGS

The Committee shall meet at least four times a year.

The notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed shall be forwarded to each member of the Committee and any other persons who may be required to attend, not fewer than 3 days prior to the date of the meeting.

In addition, the Committee Chairman may convene a meeting of the Committee if requested to do so by any member, or the internal or external auditors to consider any matter within the scope and responsibilities of the Committee or at the Committee Chairman's discretion.

Meetings of the Committee shall be held at any place within or out of Malaysia.

Members of the Committee may participate in a meeting of the Committee by means of telephone or other electronic means and all persons participating in the meeting can hear each other, and such participation in a meeting shall constitute presence in person at the meeting.

The Committee may establish any regulations from time to time to govern its administration.

7. ATTENDANCE AT MEETINGS

The quorum for meetings of the Committee shall consist of 2 members of which the majority present must be Independent Directors.

In the absence of the Committee Chairman and/or appointed deputy, the remaining members present shall elect one of their number to chair the meeting.

The head of finance, the head of internal audit (where such a function exists), and a representative of the external auditors shall normally attend meetings. The Committee may invite other Board members or any person to be in attendance to assist it in its deliberations. However, at least once a year the Committee shall meet with the external auditors without executive Board members present whenever deemed necessary.

8. RESOLUTIONS IN WRITING

A resolution in writing signed whether in original or by facsimile, by the requisite members of the Committee who are sufficient to form a quorum, shall be as valid and effectual as if it had been passed at a meeting of the Committee duly convened and held. Any such resolution may consist of several documents in like form, each signed by one or more members.

9. AUTHORITY AND RIGHTS

The Committee is authorised by the Board to investigate any activity within its terms of reference and shall:-

- a) have authority to investigate any matter within its terms of reference;
- b) have the resources which are required to perform its duties;
- c) have full and unrestricted access to any information pertaining to the Company and its subsidiaries;
- d) have direct communication channels with the external auditors and person(s) carrying out the internal audit function or activity (if any);

TERMS OF REFERENCE OF AUDIT COMMITTEE

- e) be able to obtain independent professional or other advice and to secure the attendance of outsiders with relevant experience and expertise, if it considers this necessary. In practice, should any expenditure in connection therewith be expected to exceed RM30,000 in total, the Committee should consult with the Chairman of the Board, or the Board, before proceeding;
- f) be able to convene meetings with the external auditors, excluding the attendance of the executive members of the Committee, whenever deemed necessary;
- g) have the authority to report any matter to Bursa Securities if it is of the view that a matter reported by it to the Board has not been satisfactorily resolved resulting in a breach of the Listing Requirements.

10. DUTIES

The functions of the Committee are to assist the Board to fulfil its responsibilities in relation to the Group's financial reporting and to examine the adequacy of the Group's internal control systems and corporate governance.

The duties of the Committee shall be: -

- 1) to discuss problems and reservations arising from the interim and final audits, and any matter the auditor may wish to discuss (in the absence of management where necessary).
- 2) to review the external auditor's management letter and management response.
- 3) review the following and report the same to the Board: -
 - a) with the external auditor, the audit plan, scope and nature of audit for the Company and of the Group, and ensure co-ordination where more than one audit firm is involved;
 - b) with the external auditor, his evaluation of the system of internal controls of the Company and of the Group;
 - c) with the external auditor, his audit report, and any matter the external auditor may wish to discuss (in the absence of management where necessary);
 - d) the assistance given by the employees to the external and internal auditors;
 - e) the adequacy of the scope, functions and resources of the internal audit functions and that it has the necessary authority to carry out its work;
 - f) the internal audit programme, processes, results of the internal audit programme, processes or investigation undertaken and whether or not appropriate action is taken on the recommendation of the internal audit function;
 - g) the quarterly results and year end financial statements, prior to the approval by the Board, focusing particularly on: -
 - i) changes in or implementation of major accounting policy or practice changes;
 - ii) significant and unusual events;
 - iii) significant audit adjustments arising from the audit;
 - iv) the going concern assumption; and
 - v) compliance with accounting standards, stock exchange and other legal requirements;

- h) any related party transaction and conflict of interest situation that may arise within the Company or the Group including any transaction, procedure or course of conduct that raises questions of management integrity;
 - i) any letter of resignation from the external auditors of the Company;
 - j) whether there is reason (supported by grounds) to believe that the Company's external auditor is not suitable for re-appointment; and
- 4) consider the major findings of internal investigations and management's response.
 - 5) recommend the nomination of a person or persons as external auditor.
 - 6) convene a meeting of the Committee to consider any matter the external auditor believes should be brought to the attention of the directors or shareholders.
 - 7) ensure that the Committee Chairman attends the Annual General Meetings to respond to any shareholder questions on the Committee's report and activities; and
 - 8) to undertake such other responsibilities as may be agreed to by the Board, or as may be required by law or the Listing Requirements of Bursa Securities.

11. REPORTING PROCEDURE

- 11.1 The Secretary shall be responsible for keeping the minutes of meeting of the Committee, circulating them to the members, the Board and the auditors who attended the meeting, and for ensuring compliance with Bursa Securities requirements. Such minutes shall be signed by the Chairman of the meeting at which the proceedings were held or by the Chairman of the next succeeding meeting.
- 11.2 The Committee shall submit a report to the Board as at the end of each financial year within 3 months from the said date to the Board for inclusion in the Company's annual report. The report of the Committee shall comprise paragraphs 15.16(3)(a) to (e) of the Listing Requirements of Bursa Securities.



CORPORATE GOVERNANCE STATEMENT

The Board of Directors (“the Board”) is committed to ensuring that good corporate governance practice is observed throughout the Group as a fundamental part of discharging its responsibilities to protect and enhance shareholder value and the financial performance of the Group. Hence, the Board will continue to evaluate the Group’s corporate governance procedures, introduce various measures and implement the best practices in so far as they are relevant to the Group, bearing in mind the nature of the Group’s businesses and the size of its business operations.

The statement below sets out how the Group has applied the Principles of the Malaysian Code of Corporate Governance (“the Code”) and the extent of compliance with the Best Practices of good corporate governance as set out in Part 1 and Part 2 of the Code.

BOARD OF DIRECTORS

Board Composition and Balance

The Company is led and managed by an experienced Board comprising members with a good mix of the necessary knowledge, skills and wide range of experience relevant to the Group.

As at the date of this report, the Board comprises seven (7) directors, five (5) of whom are non-executive. Of the non-executive directors, three (3) are independent. A brief description of the background of each director is presented on pages 4 to 7 of this Annual Report.

The Board is satisfied that the current Board composition fairly reflects the investment of minority shareholders in the Company.

The role of the Chairman and Chief Executive Officer (“CEO”) are not separated. Although the roles are combined, the Board is of the view that there are sufficient independent directors on the Board to ensure fair and objective deliberations at Board meetings and who are capable of exercising independent judgements. The Chairman/CEO always abstains from all deliberations and voting on matters, which he is directly or deemed, interested. All related party transactions involving him are dealt with in accordance with the provisions of the Listing Requirements of Bursa Malaysia Securities Berhad (“Bursa Securities”). Moreover, the senior independent non-executive director, Dato’ Dr. Norraesah Haji Mohamad, is available to deal with concerns regarding the Company where it could be inappropriate for these to be dealt with by the Chairman/CEO.

The Board is of the opinion that its current composition and size constitute an effective Board to the Company.

Re-election

In accordance with the Company’s Articles of Association, one third of the Board is required to retire at every Annual General Meeting (“AGM”) and be subject to re-election by shareholders. Newly appointed directors shall hold office until the next following AGM and shall then be eligible for re-election by shareholders.

Board Meetings

The Board meets on a scheduled basis, at least five (5) times a year to approve quarterly and annual financial results, recurrent related party transactions, annual budgets and any other matters that require the Board’s approval. Due notice is given for all scheduled meetings.

During the year under review, the Board had met on a total of five (5) occasions. The attendance of each individual director at these meetings are set out on page 8 of this Annual Report. All directors attended more than 50% of the Board meetings.

The Board is fully aware and acts on its specifically reserved matters for decision to ensure that the direction of the Company is firmly in its hands. During the year under review, the Board also resolved and approved the Company's matters through circular resolutions. Board members are provided with sufficient detailed information to facilitate their approvals.

DIRECTORS' TRAINING

All the Directors had already fulfilled his/her Continuing Education Programme obligations stipulated by Bursa Securities. The Directors are mindful that they should receive continuous training to broaden their perspectives and keep abreast with the new statutory and regulatory requirements. The Board views that this can be achieved through a mix of in-house training programs and external training programs that are deemed appropriate to aid them in the discharge of their duties as directors.

During Year 2006, the Directors attended training on various topics/seminars:-

Mode of Training	Title of Training	Duration of Training
In-house workshop	Malaysian Tax Education	1 Day
In-house briefing	Rights of Minority Shareholders	Half-day
In-house workshop	Performance Management Workshop	2 Days
In-house seminar	Credit Rating, Corporate Governance Detection and Prevention of Fraud	1 Day
In-house seminar	Succession Planning for Success	1 Day
In-house seminar	Regulation of the Securities Market – Insider Trading, False Trading and Market Rigging	1 Day

A tour of the upgraded facilities at the Company's plant at Sungei Way Free Industrial Zone was conducted to keep the Directors abreast of the developments in the market place.

From time to time during the normal proceedings of the meetings, the Directors also received updates and briefings, particularly on regulatory and industry developments, relevant new laws and changes to the accounting standards, from the management, company secretaries and auditors.

SUPPLY OF INFORMATION

The Chairman ensures that all Directors have full and unrestricted access to timely information, necessary in the furtherance of their duties.

Prior to each Board and Audit Committee meeting, every director is given an agenda and a set of papers containing reports and information relevant to the agenda items to facilitate active participation and informed decision making. The papers are issued in sufficient time to enable the directors to obtain further information and explanations, where necessary, so that they are properly briefed before the meetings. At each meeting, apart from receiving financial-oriented information from the management, the Board is also kept updated on the activities, operations and other performance factors affecting the Group's business and performance. Matters requiring any decision are in practice thoroughly discussed and deliberated by the Board. There is active and unrestricted participation by independent directors in the deliberations and decisions of the Board. All directors can and do have opportunity to call for additional clarification and information to assist them in their decision-making.

CORPORATE GOVERNANCE STATEMENT

Every director has full access to the advice and services of the company secretary and where required and in appropriate circumstances, is able to take professional advice at the Company's expense.

DIRECTORS' NOMINATION

The Code recommends the setting up of a Nominating Committee ("NC") to undertake the responsibility of administering a formal and transparent process for Director appointment and assessment of Board. The Company did not establish a NC as the Board itself can fulfill the role of NC.

Almost all the Directors have been in the Board since 1994 and are closely identified with the Group's business and success individually and collectively. The Directors have been able to effectively and capably execute their responsibilities, thus enabling the Group to grow over the years. The contribution and performance of each Director are apparent to the other Directors. At such time that the Board finds it requires new members to improve its working and quality, the Board would find suitable candidates and make appropriate recommendation.

DIRECTORS' REMUNERATION

The Board did not establish a Remuneration Committee ("RC") as recommended by the Code. The Board itself can fulfill the role of RC and will deliberate on the remuneration of directors during the normal proceedings of the meeting of directors.

The Board, as a whole, determines the remuneration of the directors with individual director abstaining from deliberations and voting on the decision in respect of his individual remuneration.

All directors are paid directors' fees as approved by the shareholders at AGM, based on the recommendation of the Board. For the year under review, none of the directors received fees of more than RM50,000 each.

As a guide, the Company seeks out prevailing market practices to determine the remuneration packages for directors. Details of directors' remuneration are set out on pages 43 and 44 of this Annual Report. The Code recommends detailed disclosure to be made for each director's remuneration. However, the Board is of the view that the transparency and accountability are not compromised by the band disclosure as permitted in the Listing Requirements of Bursa Securities.

AUDIT COMMITTEE

The composition and terms of reference of this Committee together with its report are set out on pages 10 to 15 of this Annual Report.

The Board of Directors has in line with the Listing Requirements reviewed the term of office and performance of the Audit Committee and each of its members and are satisfied that the Audit Committee has carried out their duties in accordance with their terms of reference.

INTERNAL AUDIT FUNCTION

The internal audit function of the Group is outsourced to a reputable international accounting/audit firm. The responsibilities of the internal auditors include conducting audits, submitting findings and the provision of independent report to the Audit Committee on the Group's systems of internal control. Being an independent function, the audit work is conducted with impartiality, proficiency and due professional care.

Details of the activities carried out by the internal auditors during the year under review are stated on page 11 of this Annual Report.

ACCOUNTABILITY AND AUDIT

Financial Reporting

The Board aims to provide and present a balanced and meaningful assessment of the Company's and of the Group's financial position and prospects in the annual financial statements, quarterly results announcements as well as the Chairman's statement in the annual report. The Board is assisted by the Audit Committee to oversee the Group's financial reporting processes and the quality of its financial reporting.

Directors' Responsibility For Preparing The Financial Statements

The Directors are required by the Companies Act, 1965 to prepare financial statements for each financial year which have been made out in accordance with the applicable approved accounting standards and give a true and fair view of the state of affairs of the Group and of the Company and of the results and cash flows for that year and cash flows of the Group and of the Company for the financial year then ended.

In preparing the financial statements, the Directors have :

- selected suitable accounting policies and applied them consistently;
- made reasonable and prudent judgements and estimates; and
- ensured that all applicable accounting standards have been followed.

The Directors have ensured the Group and the Company keeps proper accounting and other records which disclose with reasonable accuracy the financial position of the Group and of the Company and which enable them to ensure that the financial statements are drawn up to comply with the Companies Act, 1965.

The Directors also have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Internal Control

The Statement on Internal Control presented on pages 22 to 23 of this Annual Report provides an overview of the state of internal controls within the Group.

Relationship with the Auditors

The Company has always maintains a transparent relationship with its external auditors in seeking their professional advice and ensuring compliance with the accounting standards in Malaysia. The role of the Audit Committee in relation to the external auditors is described on page 10.

RELATIONS WITH SHAREHOLDERS

The Company maintains communication with its shareholders and investors to keep them informed of all major developments and performance of the Group through timely quarterly results announcements and various disclosures and announcements made to the Exchange via the Bursa Link, press releases, Company's annual reports and circulars to shareholders.

Additionally, the AGM and Extraordinary General Meetings provide an opportunity for the shareholders to seek and clarify any issues and to have a better understanding of the Group's performance. The Board encourages shareholders' active participation at such meetings. Members of the Board and the external auditors are also present to answer questions raised during the meetings.

Notices of each meeting are issued in a timely manner to all shareholders. Each item of special business included in the notice of AGMs is accompanied by a full explanation of the effects of a proposed resolution to facilitate full understanding and evaluation of issues involved.

CORPORATE GOVERNANCE STATEMENT

Throughout the year, the executive directors, who are responsible for investor relations of the Company, meet with analysts and institutional investors. Presentations based on permissible disclosures are made to explain the Group's strategies, performance and activities. Price sensitive and any information that may be regarded as undisclosed material information about the Group is however not disclosed in these exchanges until after the prescribed announcement to Bursa Securities has been made.

The Company also maintains a website (www.kesmi.com) through which shareholders and members of the public in general can gain access to information about the Group.

STATEMENT OF COMPLIANCE WITH THE BEST PRACTICES OF THE CODE

Apart from the dual roles held by the Executive Chairman/CEO and the setting up of a Nomination Committee and a Remuneration Committee, the Board considers that the Company has substantially complied with the Best Practices as set out in the Code throughout the financial year ended 31 July 2006.

This statement is made in accordance with the resolution of the Board of Directors at its meeting held on 19 September 2006.

OTHER INFORMATION

During the financial year under review,

1. SHARE BUYBACKS

The Company did not have a share buyback scheme in place.

2. OPTIONS, WARRANTS OR CONVERTIBLE SECURITIES

No options were exercised pursuant to the Company's employees share option scheme.

The Company did not issue any warrants or convertible securities.

3. AMERICAN DEPOSITORY RECEIPT (ADR) OR GLOBAL DEPOSITORY RECEIPT (GDR) PROGRAMME

The Company did not sponsor any ADR or GDR programme.

4. IMPOSITION OF SANCTIONS AND/OR PENALTIES

There were no sanctions and/or penalties imposed on the Company and its subsidiaries, Directors or management by the relevant regulatory bodies during the financial year.

5. NON-AUDIT FEES

The Company did not pay any non-audit fees to the external auditors.

6. PROFIT ESTIMATE, FORECAST OR PROJECTION

There was no profit estimate, forecast or projection or unaudited results released which differ by 10% or more from the audited results.

7. PROFIT GUARANTEES

There were no profit guarantees given by the Company.

8. MATERIAL CONTRACTS

No material contracts were entered into by the Company and its subsidiaries involving Directors' and major shareholders' interests.

9. CONTRACTS RELATING TO LOANS

There were no contracts relating to loans by the Company.

10. REVALUATION POLICY ON LANDED PROPERTIES

The carrying amounts of the landed properties at valuation are regularly reviewed such that the carrying amounts at balance sheet date are not materially different from their fair values.

Where properties are revalued, any surplus on revaluation is credited to the asset valuation reserve. A decrease in net carrying amount arising on revaluation of properties is charged to the income statement to the extent that it exceeds any surplus held in reserve relating to previous revaluation of the same class of properties.



STATEMENT ON INTERNAL CONTROL

INTRODUCTION

This Statement on Internal Control by the Board is made pursuant to Paragraph 15.27(b) of the Listing Requirements of Bursa Malaysia Securities Berhad. It outlines the nature and scope of internal control of the Group during the financial year under review.

BOARD'S DISCLOSURE ON RISK MANAGEMENT

The Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group and that the process is regularly reviewed by the Board and accords with The Statement on Internal Control – Guidance For Directors of Public Listed Companies.

BOARD'S RESPONSIBILITY

In accordance with Principle D II in Part 1 of the Malaysian Code on Corporate Governance, the Board is committed to maintain a sound system of internal control to safeguard shareholders' investment and the Group's assets. Accordingly, the Board acknowledges its responsibility for the Group's overall system of internal control which includes the establishment of an appropriate control environment and framework as well as reviewing its adequacy and integrity. However, it should be noted that due to the limitations that are inherent in any system of internal control such a system is designed to manage rather than eliminate the risk of failure to achieve the Group's business objectives. Accordingly, it can only provide reasonable and not absolute assurance against material misstatement or loss.

KEY ELEMENTS OF INTERNAL CONTROL

The key internal control structures of the Group are described below.

The Group's internal audit function is outsourced to a public accounting firm of international standing. The internal audit function facilitates the Board in its reviews of and evaluation of the adequacy and integrity of the Group's internal control systems.

The internal auditor adopts a risk-based approach and prepares its audit strategy and plan based on the risk profiles of the business units of the Group. Audits are carried out according to the annual audit plan approved by the Audit Committee. The resulting reports from the annual audits undertaken are presented to the Audit Committee at its regular meetings. Board members are invited when the Audit Committee meets to review, discuss, and direct actions on matters pertaining to reports, which among other matters, include findings relating to the adequacy and integrity of the internal control system of the Group. After the Audit Committee had deliberated on the reports, these are then forwarded to the operational management for attention and necessary actions. The operational management is responsible for ensuring recommended corrective actions on reported weaknesses were taken within the required time frame.

The annual internal audits therefore provide the Board with an independent assessment on the adequacy, efficiency and effectiveness of the Group's internal control systems in anticipating potential risk exposures over key business systems and processes and in controlling the proper conduct of business within the Group.

Apart from internal audit, the Board has in place an organisation structure with formally defined lines of responsibility and delegation of authority. A process of hierarchical reporting has been established which provides for a documented and auditable trail of accountability.

The monitoring and management of the Group is delegated to the two Executive Board members and senior operational management. The Executive Board members through their day-to-day involvement in the business operations and regular attendance at senior management level meetings, manage and monitor the Group's financial performance, key business indicators, operational effectiveness and efficiency, discuss and resolve significant business issues and ensure compliance with applicable laws, regulations, rules, directives and guidelines. These senior management meetings serve as a two-way platform for the Board, through the Executive Board members, to communicate and address significant matters in relation to the Group's business and financial affairs and provide update on significant changes in the business and the external environment which result in significant risks.

The Group's internal control procedures are set out in a series of standard operating practice manuals and business process manuals, to serve as guidance for proper measures to be undertaken and are subject to regular review, enhancement and improvement.

CONCLUSION

The Board is of the opinion that the system of internal control that has been instituted throughout the Group was satisfactory and has not resulted in any material losses that would require disclosure in the Group's annual report. Notwithstanding this, the Board will continue to review the control procedures to ensure the effectiveness and adequacy of the internal control system of the Group.

This statement is made in accordance with the resolution of the Board of Directors dated 19 September 2006.





Financial Statements

Directors' Report	25
Statement by Directors	30
Statutory Declaration	30
Report of the Auditors	31
Income Statements	32
Balance Sheets	33
Statements of Changes in Equity	34
Cash Flow Statements	35
Notes to the Financial Statements	37
Shareholders' Information	62
Group Properties	65
Notice of Annual General Meeting	66
Notice of Dividend Entitlement	69
Statement Accompanying Notice of Annual General Meeting	70
Proxy Form	

DIRECTORS' REPORT

The Directors have pleasure in presenting their report together with the audited financial statements of the Group and of the Company for the year ended 31 July 2006.

PRINCIPAL ACTIVITIES

The principal activities of the Company are investment holding, provision of semiconductor burn-in services and assembly of electronic components. The principal activities of its subsidiary companies are the provision of semiconductor burn-in and testing of semiconductor integrated circuits and assembly of electronic components.

There have been no significant changes in the nature of these activities during the year.

RESULTS

	Group RM'000	Company RM'000
Profit after taxation and minority interest	14,133	8,138

There were no material transfers to or from reserves or provisions during the year.

In the opinion of the Directors, the results of the operations of the Group and of the Company during the financial year were not substantially affected by any item, transaction or event of a material and unusual nature.

DIVIDEND

On 23 January 2006, the Company paid a first and final tax exempt dividend of 1.75 sen per share amounting to RM752,509 (2005: RM752,509), as reported in the Directors' report of the previous financial year.

At the forthcoming Annual General Meeting, a first and final tax exempt dividend in respect of the financial year ended 31 July 2006, of 3 sen per ordinary shares will be proposed for shareholders' approval. The financial statements for the current financial year do not reflect this proposed dividend. Such dividend, if approved by the shareholders, will be accounted for in equity as an appropriation of retained profits in the financial year ending 31 July 2007.

DIRECTORS

The Directors of the Company in office since the date of the last report and at the date of this report are:

Samuel Lim Syn Soo
Kenneth Tan Teoh Khoon
Lim Mee Ing
Dato' Dr Norraesah Haji Mohamad
Ahmad Riza Bin Basir
Tuan Haji Zakariah Bin Yet
Yong Chee Hou

Neither at the end of the financial year, nor at any time during that year, did there subsist any arrangement to which the Company was a party, whereby Directors might acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate other than those arising from share options granted pursuant to the Company's Employees Share Option Scheme ("ESOS").

DIRECTORS' REPORT

DIRECTORS (CONTD.)

The following Directors who held office at the end of the financial year had, according to the register required to be kept under Section 134 of the Companies Act 1965, interests in shares and options in the Company as stated below:

	Number of Ordinary Shares of RM1.00 Each			At 31.7.2006
	At 1.8.2005	Bought	Sold	
Dato' Dr Norraesah Haji Mohamad				
- Direct interest	7,500	-	-	7,500
- Deemed interest	857,000	-	252,500	604,500
Samuel Lim Syn Soo				
- Deemed interest	20,825,000	-	-	20,825,000

	Option Price	Options to Subscribe for Ordinary Shares of RM1.00 Each			At 31.7.2006
		At 1.8.2005	Granted	Exercised	
Samuel Lim Syn Soo					
First Option*	RM2.192	50,000	-	-	50,000
Second Option*	RM2.464	50,000	-	-	50,000
Third Option*	RM2.344	50,000	-	-	50,000
Fourth Option	RM3.100	34,000	-	-	34,000
Fifth Option	RM2.500	20,000	-	-	20,000
Sixth Option	RM1.927	-	12,800	-	12,800
Kenneth Tan Teoh Khoon					
First Option*	RM2.192	50,000	-	-	50,000
Second Option*	RM2.464	50,000	-	-	50,000
Third Option*	RM2.344	50,000	-	-	50,000
Fourth Option	RM3.100	34,000	-	-	34,000
Fifth Option	RM2.500	20,000	-	-	20,000
Sixth Option	RM1.927	-	12,800	-	12,800

* Adjusted to include the effect of bonus issue of shares of 3 for 2 existing shares made on 4 December 2002 by the Company.

By virtue of his interest in shares in the Company, Samuel Lim Syn Soo is also deemed interested in shares in all the Company's subsidiaries to the extent the Company has an interest.

Since the end of the previous financial year, no Director has received or become entitled to receive a benefit (other than benefits included in the aggregate amount of emoluments and fees received or due and receivable by the Directors as shown in Note 5 to the financial statements) by reason of a contract made by the Company or a related corporation with any Director or with a firm of which a Director is a member or with a company in which the Director has a substantial financial interest except as disclosed in Note 23 to the financial statements.

SHARE CAPITAL

No new shares were issued during the financial year.

EMPLOYEES SHARE OPTION SCHEME ("ESOS")

The extension of duration of the Company's ESOS for eligible full-time employees and directors of the Company and its subsidiary companies and amendments to certain clauses in the By-Laws were approved by shareholders at an Extraordinary General Meeting held on 21 November 2005. The ESOS has been extended for a period of five (5) years expiring on 4 December 2010.

The maximum number of new shares which may be subscribed on the exercise of options granted under the ESOS shall not, in aggregate, exceed fifteen percent (15%) of the total issued and paid-up ordinary share capital of the Company at any point of time during the existence of the scheme.

The Option Price is determined according to the By-Laws of the ESOS and shall be the higher of:

- (a) the weighted average market price of the shares of the Company for the five (5) market days immediately preceding the date of offer with a discount of not more than 10%, if deemed appropriate; or
- (b) the par value of the share.

The persons to whom the options have been granted do not have any right to participate by virtue of such options in any share issue of any other company.

During the financial year, a total of 160,000 new options for ordinary shares of RM1.00 each in the Company were granted to eligible employees of the Group pursuant to the ESOS at an Option Price of RM1.927 per share. Of this total, 138,200 options had been accepted and the names of employees granted these options are disclosed in Note 28 to the financial statements.

The particulars of the options granted to eligible employees as at 31 July 2006 are as follows:

	Option Price RM	Granted	Number of options Accepted	Exercised	Lapsed	Total available
First Option*	2.192	1,001,000	997,000	(386,500)	(178,000)	432,500
Second Option*	2.464	462,000	461,000	(40,000)	(28,500)	392,500
Third Option*	2.344	460,000	456,000	(38,000)	(46,000)	372,000
Fourth Option	3.100	312,800	297,800	-	(12,000)	285,800
Fifth Option	2.500	168,000	151,000	-	(16,000)	135,000
Sixth Option	1.927	160,000	138,200	-	(4,000)	134,200
		2,563,800	2,501,000	(464,500)	(284,500)	1,752,000

*Adjusted to include the effect of bonus issue of shares of 3 for 2 existing shares made on 4 December 2002 by the Company.

DIRECTORS' REPORT

OTHER STATUTORY INFORMATION

- (a) Before the income statements and balance sheets of the Group and of the Company were made out, the Directors took reasonable steps:
 - (i) to ascertain that proper action had been taken in relation to the writing off of bad debts and the making of provision for doubtful debts and satisfied themselves that there are no known bad debts and that no provision for doubtful debts was necessary; and
 - (ii) to ensure that any current assets which were unlikely to realise their values as shown in the accounting records in the ordinary course of business had been written down to an amount which they might be expected so to realise.
- (b) At the date of this report, the Directors are not aware of any circumstances which would render:
 - (i) it necessary to write off any debts or to make any provision for doubtful debts in respect of these financial statements; and
 - (ii) the values attributed to current assets in the financial statements of the Group and of the Company misleading.
- (c) At the date of this report, the Directors are not aware of any circumstances which have arisen which render adherence to the existing method of valuation of assets or liabilities of the Group and of the Company misleading or inappropriate.
- (d) At the date of this report, the Directors are not aware of any circumstances not otherwise dealt with in this report or financial statements of the Group and of the Company which would render any amount stated in the financial statements misleading.
- (e) As at the date of this report, there does not exist:
 - (i) any charge on the assets of the Group or of the Company which has arisen since the end of the financial year which secures the liabilities of any other person; or
 - (ii) any contingent liability in respect of the Group or of the Company which has arisen since the end of the financial year.
- (f) In the opinion of the Directors:
 - (i) no item, transaction or event of a material and unusual nature has arisen in the interval between the end of the financial year and the date of this report which is likely to affect substantially the results of the operations of the Group or of the Company for the financial year in which this report is made; and
 - (ii) no contingent liability or other liability has become enforceable or is likely to become enforceable within the period of twelve months after the end of the financial year which will or may affect the ability of the Group or of the Company to meet their obligations as and when they fall due.

AUDITORS

The auditors, Ernst & Young, have expressed their willingness to continue in office.

Signed on behalf of the Board in accordance with a resolution of the Directors

Samuel Lim Syn Soo

Kuala Lumpur, Malaysia
19 September 2006

Kenneth Tan Teoh Khoon



STATEMENT BY DIRECTORS

PURSUANT TO SECTION 169(15) OF THE COMPANIES ACT 1965

We, Samuel Lim Syn Soo and Kenneth Tan Teoh Khoon, being two of the Directors of KESM Industries Berhad, do hereby state that, in the opinion of the Directors, the accompanying financial statements set out on pages 32 to 61 are drawn up in accordance with applicable MASB Approved Accounting Standards in Malaysia and the provisions of the Companies Act 1965 so as to give a true and fair view of the financial position of the Group and of the Company as at 31 July 2006 and of the results and the cash flows of the Group and of the Company for the year then ended.

Signed on behalf of the Board in accordance with a resolution of the Directors

Samuel Lim Syn Soo

Kenneth Tan Teoh Khoon

Kuala Lumpur, Malaysia
19 September 2006

STATUTORY DECLARATION

PURSUANT TO SECTION 169(16) OF THE COMPANIES ACT 1965

I, Kenneth Tan Teoh Khoon, being the Director primarily responsible for the financial management of KESM Industries Berhad, do solemnly and sincerely declare that the financial statements set out on pages 32 to 61 are to my best knowledge and belief, correct and I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the Oaths and Declarations Act 2000.

Subscribed and solemnly declared by the abovementioned
Kenneth Tan Teoh Khoon in Singapore on 6 October 2006

Kenneth Tan Teoh Khoon

Before me,

Chia Choon Yang
Notary Public

REPORT OF THE AUDITORS

TO THE MEMBERS OF KESM INDUSTRIES BERHAD

We have audited the financial statements set out on pages 32 to 61. These financial statements are the responsibility of the Company's Directors.

It is our responsibility to form an independent opinion, based on our audit, on the financial statements and to report our opinion to you, as a body, in accordance with Section 174 of the Companies Act 1965 and for no other purpose. We do not assume responsibility to any other person for the content of this report.

We conducted our audit in accordance with applicable Approved Standards on Auditing in Malaysia. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Directors, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion:

- (a) the financial statements have been properly drawn up in accordance with the provisions of the Companies Act 1965 and applicable MASB Approved Accounting Standards in Malaysia so as to give a true and fair view of:
 - (i) the financial position of the Group and of the Company as at 31 July 2006 and of the results and the cash flows of the Group and of the Company for the financial year then ended; and
 - (ii) the matters required by Section 169 of the Companies Act 1965 to be dealt with in the financial statements; and
- (b) the accounting and other records and the registers required by the Act to be kept by the Company and by its subsidiaries have been properly kept in accordance with the provisions of the Act.

We are satisfied that the financial statements of the subsidiaries that have been consolidated with the financial statements of the Company are in the form and content appropriate and proper for the purpose of the preparation of the consolidated financial statements and we have received satisfactory information and explanations required by us for those purposes.

The auditors' reports on the financial statements of the subsidiaries were not subject to any qualification material to the consolidated financial statements and did not include any comment required to be made under Section 174 (3) of the Act.

Ernst & Young
AF: 0039
Chartered Accountants

See Huey Beng
No. 1495/03/07(J)
Partner

Kuala Lumpur, Malaysia
19 September 2006

INCOME STATEMENTS

YEAR ENDED 31 JULY 2006

	Note	Group		Company	
		2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Revenue	3	162,159	180,985	49,685	49,766
Other operating income		1,286	3,237	1,276	838
Total operating income		163,445	184,222	50,961	50,604
Raw materials and consumables used		(41,903)	(55,411)	(663)	(687)
Staff costs	4	(33,760)	(34,566)	(16,053)	(15,902)
Depreciation of property, plant and equipment		(34,584)	(38,779)	(7,056)	(7,143)
Other operating expenses		(31,499)	(33,648)	(17,403)	(17,984)
Profit from operating activities	5	21,699	21,818	9,786	8,888
Interest income	6	1,455	691	1,249	1,955
Interest expense	7	(3,025)	(3,405)	(324)	(515)
Profit before taxation		20,129	19,104	10,711	10,328
Taxation	8	(4,647)	(3,645)	(2,573)	(2,290)
Profit after taxation		15,482	15,459	8,138	8,038
Minority interest		(1,349)	(1,478)	-	-
Profit after taxation and minority interest		14,133	13,981	8,138	8,038
Earnings per share					
- Basic	9	33 sen	33 sen		
- Diluted	9	33 sen	32 sen		
Dividend per share in respect of the year	10			3.00 sen	1.75 sen

The accompanying notes form an integral part of the financial statements.

BALANCE SHEETS

AS AT 31 JULY 2006

	Note	Group		Company	
		2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
NON-CURRENT ASSETS					
Property, plant and equipment	11	111,713	110,495	27,801	29,315
Subsidiary companies	12	-	-	4,715	4,715
		111,713	110,495	32,516	34,030
CURRENT ASSETS					
Other investments	13	3,548	4,084	3,548	4,084
Inventories	14	15,421	5,282	174	155
Trade and other receivables	15	41,860	38,358	10,524	9,798
Tax recoverable		-	623	-	-
Due from subsidiaries	16	-	-	24,740	11,149
Deposits with licensed banks	17	49,544	49,904	26,958	32,695
Cash and bank balances		4,718	4,632	2,193	1,460
		115,091	102,883	68,137	59,341
CURRENT LIABILITIES					
Trade and other payables	18	37,829	21,941	6,579	6,382
Borrowings	19	18,463	22,551	1,108	3,433
Taxation		2,704	3,766	2,390	2,737
		58,996	48,258	10,077	12,552
NET CURRENT ASSETS					
		56,095	54,625	58,060	46,789
		167,808	165,120	90,576	80,819
FINANCED BY:					
Share capital	20	43,001	43,001	43,001	43,001
Reserves	21	91,132	77,752	35,628	28,243
		134,133	120,753	78,629	71,244
Minority interest		6,094	4,745	-	-
		140,227	125,498	78,629	71,244
NON-CURRENT LIABILITIES					
Borrowings	19	12,667	26,968	1,395	484
Deferred tax liabilities	22	14,914	12,654	10,552	9,091
		27,581	39,622	11,947	9,575
		167,808	165,120	90,576	80,819

The accompanying notes form an integral part of the financial statements.

STATEMENTS OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 JULY 2006

Note	Share capital RM'000	Non-distributable			Distributable	Total RM'000
		Share premium RM'000	Asset revaluation reserve RM'000	Reserve on consolidation RM'000	Retained profits RM'000	
Group						
At 31 July 2004	42,996	642	7,433	430	56,012	107,513
Exercise of options to subscribe for ordinary shares in the Company	5	7	-	-	-	12
Profit after taxation and minority interest	-	-	-	-	13,981	13,981
Dividend	-	-	-	-	(753)	(753)
At 31 July 2005	43,001	649	7,433	430	69,240	120,753
Profit after taxation and minority interest	-	-	-	-	14,133	14,133
Dividend	10	-	-	-	(753)	(753)
At 31 July 2006	43,001	649	7,433	430	82,620	134,133

Note	Share capital RM'000	Non-distributable			Distributable	Total RM'000
		Share premium RM'000	Asset revaluation reserve RM'000	Merger relief reserve RM'000	Retained profits RM'000	
Company						
At 31 July 2004	42,996	642	2,124	1,215	16,970	63,947
Exercise of options to subscribe for ordinary shares in the Company	5	7	-	-	-	12
Profit after taxation	-	-	-	-	8,038	8,038
Dividend	-	-	-	-	(753)	(753)
At 31 July 2005	43,001	649	2,124	1,215	24,255	71,244
Profit after taxation	-	-	-	-	8,138	8,138
Dividend	10	-	-	-	(753)	(753)
At 31 July 2006	43,001	649	2,124	1,215	31,640	78,629

The accompanying notes form an integral part of the financial statements.

CASH FLOW STATEMENTS

YEAR ENDED 31 JULY 2006

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
CASH FLOWS FROM OPERATING ACTIVITIES				
Profit before taxation	20,129	19,104	10,711	10,328
Adjustments for:				
(Gain)/loss on disposal of property, plant and equipment	(141)	(2,271)	-	7
Plant and equipment written off	4	-	4	-
Depreciation of property, plant and equipment	34,584	38,779	7,056	7,143
Impairment of property, plant and equipment	-	589	-	589
Realised loss/(gain) on foreign exchange	21	40	4	(3)
Unrealised loss on foreign exchange	294	41	13	-
Gain on disposal of quoted shares	(765)	(259)	(765)	(259)
Writedown/(write back) in value of quoted shares	132	(217)	132	(217)
Dividend income	(205)	(202)	(205)	(202)
Interest expense	3,025	3,405	324	515
Interest income	(1,455)	(691)	(1,249)	(1,955)
Operating profit before working capital changes	55,623	58,318	16,025	15,946
Changes in working capital:				
Inventories	(10,139)	1,011	(19)	3
Receivables	(3,502)	(830)	(726)	2,621
Subsidiary companies	-	-	(13,591)	9,235
Payables	6,157	3,505	70	(158)
Cash generated from operations	48,139	62,004	1,759	27,647
Tax paid	(2,826)	(2,397)	(1,459)	(1,273)
Interest paid	(3,025)	(3,405)	(324)	(515)
Interest received	1,455	691	1,249	1,955
Net cash generated from operating activities	43,743	56,893	1,225	27,814

CASH FLOW STATEMENTS

YEAR ENDED 31 JULY 2006

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of investment in quoted shares	(577)	(3,889)	(577)	(3,889)
Proceeds from disposal of quoted shares	1,746	2,154	1,746	2,154
Dividend income	205	202	205	202
Purchase of property, plant and equipment	(26,659)	(52,736)	(5,436)	(4,532)
Proceeds from disposal of property, plant and equipment	410	7,245	-	7
Net cash used in investing activities	(24,875)	(47,024)	(4,062)	(6,058)
CASH FLOWS FROM FINANCING ACTIVITIES				
Payments of hire purchase obligations	(3,404)	(4,028)	(1,608)	(2,174)
Repayments of term loans	(26,161)	(21,593)	(2,180)	(2,880)
Drawdown of term loans	11,176	31,886	2,374	-
Issue of new shares	-	12	-	12
Dividend paid	(753)	(753)	(753)	(753)
Net cash (used in)/generated from financing activities	(19,142)	5,524	(2,167)	(5,795)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(274)	15,393	(5,004)	15,961
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	54,536	39,143	34,155	18,194
CASH AND CASH EQUIVALENTS AT END OF YEAR	54,262	54,536	29,151	34,155
Cash and cash equivalents at end of year comprise:				
Deposits with licensed banks	49,544	49,904	26,958	32,695
Cash and bank balances	4,718	4,632	2,193	1,460
	54,262	54,536	29,151	34,155

The accompanying notes form an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

1. CORPORATE INFORMATION

The principal activities of the Company are investment holding, provision of semiconductor burn-in services and assembly of electronic components. The principal activities of its subsidiary companies are the provision of burn-in and testing of semiconductor integrated circuits and assembly of electronic components. There have been no significant changes in the nature of these activities during the year.

The Company is a public limited company, incorporated and domiciled in Malaysia and is listed on the Second Board of the Bursa Malaysia Securities Berhad. The registered office of the Company is at 312, 3rd Floor, Block C, Kelana Square, No. 17, Jalan SS7/26, 47301 Petaling Jaya, Selangor Darul Ehsan, Malaysia.

The principal place of business of the Company is located at Lot 4, Jalan SS 8/4, Sungei Way Free Industrial Zone, 47300 Petaling Jaya, Selangor Darul Ehsan, Malaysia.

The financial statements are expressed in Ringgit Malaysia.

The financial statements were authorised for issue by the Board of Directors in accordance with a resolution of the Directors on 19 September 2006.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Preparation

The financial statements of the Group and of the Company are prepared under the historical cost convention, modified to include the revaluation of certain property, plant and equipment and comply with the provisions of the Companies Act 1965 and applicable MASB Approved Accounting Standards in Malaysia.

(b) Basis of Consolidation

The Group financial statements incorporate the financial statements of the Company and all its subsidiary companies. The subsidiaries are consolidated using either the acquisition or merger method of accounting.

Under the acquisition method of accounting, the results of a subsidiary company acquired or disposed during the year are included from the date of acquisition or up to date of disposal. At the date of acquisition, the fair values of the subsidiary's net assets are determined and these values are reflected in the Group financial statements.

The net difference between the acquisition cost and attributable fair value of net assets acquired is reflected as goodwill or negative goodwill as appropriate. Goodwill or negative goodwill is dealt with through income statement.

Under the merger method of accounting, the results of a subsidiary company are included as if the subsidiary has been combined throughout the current and previous financial years. Merger deficit arising is eliminated against retained profit reserve in the year in which the merger method of accounting is applied.

Intra-group transactions, balances and resulting unrealised gains are eliminated on consolidation and the consolidated financial statements reflect external transactions only. Unrealised losses are eliminated on consolidation unless costs cannot be recovered.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(b) Basis of Consolidation (Contd.)

The gain or loss on disposal of a subsidiary company is the difference between net disposal proceeds and the Group's share of its net assets together with any unamortised balance of goodwill and exchange differences.

Minority interests in the consolidated balance sheet consist of the minorities' share of the fair value of the identifiable assets and liabilities of the acquiree as at acquisition date and the minorities' share of movements in the acquiree's equity since then.

(c) Revenue Recognition

Revenue is recognised upon passage of title to the customer which generally coincides with the delivery, or the rendering of service to the customer.

Interest income is recognised on an accrual basis.

Dividend income is recognised when the right to receive such dividends is established.

Rental income is recognised over the period of tenancy.

(d) Subsidiary Companies

Subsidiary companies are those companies in which the Group has power to exercise control over the financial and operating policies so as to obtain benefits from their activities.

Investments in subsidiary companies are stated at cost less impairment losses.

(e) Property, Plant and Equipment

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

The cost of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the property, plant and equipment to working condition for its intended use. Expenditure for additions, improvements and renewals are capitalised and expenditure for maintenance and repairs are charged to the income statement.

When property, plant and equipment are sold or retired, their cost or valuation and accumulated depreciation are removed from the financial statements and any gain or loss resulting from their disposal/retirement is included in the income statement. Any remaining attributable revaluation surplus is taken to distributable reserve.

The carrying amounts of the property, plant and equipment at valuation is reviewed regularly such that the carrying amounts at balance sheet date are not materially different from their fair values.

Where property, plant and equipment are revalued, any surplus on revaluation is credited to the asset revaluation reserve. A decrease in net carrying amount arising on revaluation of property, plant and equipment is charged to the income statement to the extent that it exceeds any surplus held in reserve relating to previous revaluation of the same class of property, plant and equipment.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(f) Depreciation

Depreciation of property, plant and equipment is provided for on a straight line basis to write off the cost of each asset to its residual value over the estimated useful life at the following estimated useful lives:

Buildings	20 years
Leasehold improvements	5 years
Plant, machinery and test equipment	1.5 to 5 years
Motor vehicles	5 years
Office equipment, furniture and fittings and computers	3 to 10 years

No depreciation is provided on capital work-in-progress. Long term leasehold land which has unexpired lease period exceeding 50 years is also not depreciated as its economic life and residual value are such that the depreciation and accumulated depreciation are not material. Short-term leasehold land is amortised evenly over the unexpired lease period.

Fully depreciated property, plant and equipment are retained in the financial statements until they are no longer in use but no further charge for depreciation is made in respect of these assets.

Upon the disposal of an item of property, plant and equipment, the difference between the net disposal proceeds and the net carrying amount is recognised in the income statement and the unutilised portion of the revaluation surplus on that item is taken directly to retained profits.

(g) Leases

A lease is recognised as a finance lease if it transfers substantially to the Group all risks and rewards incident to an ownership. All other leases are classified as operating leases.

Assets acquired by way of finance lease is stated at an amount equal to the lower of their fair values and the present value of the minimum lease payments at the inception of the leases, less accumulated depreciated and impairment losses. The corresponding liability is included in the balance sheet as borrowings. In calculating the present value of the minimum lease payments, the discount factor used is the interest rate implicit in the lease, when it is practicable to determine; otherwise, the Group's incremental borrowing rate is used.

Lease payments are apportioned between the finance costs and the reduction of the outstanding liability. Finance costs, which represent the difference between the total leasing commitments and the fair value of the assets acquired, are recognised as an expense in the income statement over the term of the relevant lease so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

The depreciation policy for leased assets is in accordance with that for depreciable property, plant and equipment as described in Note 2(f).

(h) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials on a weighted average basis and in the case of finished products, includes direct labour and attributable production overheads based on normal level of activity. Net realisable value represents the estimated selling price less anticipated cost of completion and estimated costs to conclude the sale.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(i) Financial Instruments

Financial instruments are recognised in the balance sheet when the Group becomes a party to the contractual provisions of the instrument. Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. The particular recognition method adopted for financial instruments recognised in the balance sheet is disclosed in the individual accounting policies associated with each item.

(i) Short Term Investments

Quoted investments are stated at the lower of cost and market value, determined on an aggregate basis.

(ii) Receivables

Known bad debts are written off and specific provision is made for any debt considered to be doubtful of collection. In addition, an estimate is made on doubtful debts based on a review of all outstanding amounts at year end.

(iii) Payables

Payables are carried at cost which is the fair value of the consideration to be paid in the future for goods and services rendered, whether or not billed to the Company.

(iv) Interest-Bearing Borrowings

Interest-bearing bank loans are recorded at the amount of proceeds received, net of transaction costs.

All borrowing costs are recognised as an expense in the income statement in the year in which they are incurred.

(j) Provisions for Liabilities

Provisions for liabilities are recognised when the Group has a present obligation as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount can be made. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate. Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditure expected to be required to settle the obligation.

(k) Foreign Currencies

Transactions arising in foreign currencies during the year are recorded at rates closely approximating those ruling on the transaction dates. Foreign currency monetary assets and liabilities are reported in Ringgit Malaysia at the exchange rates ruling at the balance sheet date. All exchange differences are dealt with through the income statement.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(k) Foreign Currencies (Contd.)

The principal exchange rates used for each respective unit of foreign currency ruling at the balance sheet date are as follows:

	2006 RM	2005 RM
Singapore Dollars	2.31	2.25
United States Dollars	3.67	3.75
Japanese Yen	3.19	3.34
Euro Dollars	4.57	4.53

(l) Income Tax

Income tax on the profit and loss for the year comprises current and deferred tax. Current tax is the expected amount of income tax payable in respect of the taxable profit for the year and is measured using the tax rates that have been enacted at the balance sheet date.

Deferred taxation is provided for, using the liability method, on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts in the financial statements. In principle, deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised for all deductible temporary differences, unused tax losses and unused tax credits to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, unused tax losses and unused tax credits can be utilised. Deferred tax is not recognised if the temporary differences arises from goodwill or negative goodwill or from the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction, affects neither accounting profit nor taxable profit.

Deferred taxation is measured at the tax rates that are expected to apply in the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date. Deferred tax is recognised in the income statement, except when it arises from a transaction which is recognised directly in equity, in which case the deferred tax is also recognised directly in equity, or when it arises from a business combination that is an acquisition, in which case the deferred tax is included in the resulting goodwill or negative goodwill.

(m) Impairment of Assets

At each balance sheet date, the Group reviews the carrying amounts of its assets to determine whether there is any indication of impairment. If any indication exists, impairment is measured by comparing the carrying values of the assets with their recoverable amount. Recoverable amount is the higher of net selling price and value in use, which is measured by reference to discounted future cash flows.

An impairment loss is recognised as an expense in the income statement immediately, unless the asset is carried at revalued amount. Any impairment loss of a revalued asset is treated as a revaluation decrease to the extent of any unutilised previously recognised revaluation surplus for the same assets. Reversal of impairment losses recognised in prior years is recorded when the impairment losses recognised for the asset no longer exist or have decreased.

(n) Cash and Cash Equivalents

Cash and cash equivalents comprise cash and bank balances, demand deposits and other short term highly liquid investments, which are readily convertible to cash with insignificant risk of changes in value, net of outstanding bank overdrafts.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

(o) Employee Benefits

(i) Short Term Benefits

Wages, salaries, bonuses and social security contributions are recognised as an expense 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 the absences occur.

(ii) Defined Contribution Plans

As required by law, companies in Malaysia make contributions to the state pension scheme, the Employees Provident Fund. Such contributions are recognised as an expense in the income statement as incurred.

(iii) Equity Compensation Benefits

The Company's Employees Share Option Scheme allows the Group's employees to acquire shares of the Company. No compensation cost or obligation is recognised. When the options are exercised, equity is increased by the amount of the proceeds received.

3. REVENUE

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Burn-in and testing services	111,327	115,925	49,685	49,766
Sales and assembly of electronic equipment	50,832	65,060	-	-
	<u>162,159</u>	<u>180,985</u>	<u>49,685</u>	<u>49,766</u>

4. STAFF COSTS

Salaries and wages	26,165	27,334	9,951	10,221
Pension costs - defined contribution plans	1,577	1,514	541	480
Social security costs	226	212	73	59
Short term accumulating compensated absences	69	20	66	(31)
Others	5,723	5,486	5,422	5,173
	<u>33,760</u>	<u>34,566</u>	<u>16,053</u>	<u>15,902</u>

Staff costs above exclude Directors remuneration.

	Group		Company	
	2006	2005	2006	2005
Average number of employees (excluding Directors) during the year	<u>1,412</u>	<u>1,390</u>	<u>492</u>	<u>482</u>

5. PROFIT FROM OPERATING ACTIVITIES

This is arrived at after charging/(crediting):

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Auditors' remuneration	123	123	58	58
Directors' emoluments	1,796	1,592	856	782
Depreciation of property, plant and equipment	34,584	38,779	7,056	7,143
Impairment of property, plant and equipment	-	589	-	589
Writedown/(write back) in value of quoted share	132	(217)	132	(217)
Rent of equipment	54	427	-	5
Realised loss/(gain) on foreign exchange	21	40	4	(3)
Rent of factory	1,049	1,157	1,049	1,157
Unrealised loss on foreign exchange	294	41	13	-
Bad debt recovered	(8)	(9)	-	-
(Gain)/loss on disposal of property, plant and equipment	(141)	(2,271)	-	7
Plant and equipment written off	4	-	4	-
Gain on disposal of quoted shares	(765)	(259)	(765)	(259)
Gross dividends from other investments	(205)	(202)	(205)	(202)
Rental income from a subsidiary	-	-	(325)	(325)

Directors' Emoluments

Directors of the Company

Executive

- fees	992	838	62	38
- salaries and other emoluments	657	620	657	620
	1,649	1,458	719	658

Non-Executive

- fees	134	134	124	124
- allowances	13	-	13	-
	147	134	137	124

Total Directors' emoluments	1,796	1,592	856	782
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NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

5. PROFIT FROM OPERATING ACTIVITIES (CONTD.)

Directors' Emoluments (contd.)

Directors of the Company (contd.)

The number of Directors of the Company whose total emoluments during the year fell within the following bands is analysed below:

	Number of Directors	
	2006	2005
Executive Directors:		
RM300,001 to RM350,000	-	1
RM350,001 to RM400,000	1	-
RM1,100,001 to RM1,150,000	-	1
RM1,250,001 to RM1,300,000	1	-
Non-executive Directors:		
Less than RM50,000	5	5

Executive Directors of the Company have been granted the following number of options under the Employees Share Option Scheme:

	Group/Company	
	2006 '000	2005 '000
Balance brought forward	408	368
Granted	26	40
Balance carried forward	434	408

The share options were granted on the same terms and conditions as those offered to other employees of the Group.

6. INTEREST INCOME

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Interest income from:				
- deposits with licensed banks	1,455	691	909	293
- loan to subsidiary	-	-	221	220
- advance to subsidiary	-	-	119	1,442
	1,455	691	1,249	1,955

7. INTEREST EXPENSE

Interest expense on:				
- term loans	2,444	2,745	130	251
- hire purchase contracts	387	470	194	264
- loan from corporate shareholder	117	118	-	-
- revolving credits	77	72	-	-
	3,025	3,405	324	515

8. TAXATION

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Malaysian taxation based on results for the year:				
- current	2,786	3,229	1,112	1,350
- over provision in prior years	(399)	(55)	-	(118)
	2,387	3,174	1,112	1,232
Deferred tax (Note 22)				
- current	2,329	994	1,488	1,020
- (over)/under provision in prior years	(69)	(523)	(27)	38
	2,260	471	1,461	1,058
	4,647	3,645	2,573	2,290

A reconciliation of income tax expense applicable to profit before taxation at the statutory income tax rate to income tax expense at the effective income tax rate of the Group and of the Company is as follows:

	Group	
	2006 RM'000	2005 RM'000
Profit before taxation	20,129	19,104
Taxation at Malaysian statutory tax rate of 28% (2005: 28%)	5,636	5,349
Effect of different tax rates used due to incentives and others	(80)	(80)
Income not subject to tax	(50)	(154)
Expenses not deductible for tax purpose	178	578
Utilisation of reinvestment allowances	(569)	(1,470)
Over provision of income tax expense in prior years	(399)	(55)
Over provision of deferred tax in prior years	(69)	(523)
Tax charge for the year	4,647	3,645
	Company	
	2006 RM'000	2005 RM'000
Profit before taxation	10,711	10,328
Taxation at Malaysian statutory tax rate of 28% (2005: 28%)	2,999	2,892
Income not subject to tax	(46)	(154)
Expenses not deductible for tax purpose	105	417
Utilisation of reinvestment allowances	(458)	(785)
Over provision of income tax expense in prior years	-	(118)
(Over)/under provision of deferred tax in prior years	(27)	38
Tax charge for the year	2,573	2,290

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

9. EARNINGS PER SHARE

	Group	
	2006 RM'000	2005 RM'000
Profit after taxation and minority interest	14,133	13,981
	Number ('000)	Number ('000)
Weighted average number of ordinary shares in issue for basic earnings per share	43,001	43,001
Adjustment for conversion of options under ESOS to ordinary shares	-	86
	43,001	43,087
Basic earnings per share	33 sen	33 sen
Diluted earnings per share	33 sen	32 sen

The effect on the basic earnings per share for the current financial year arising from the assumed conversion of the options is anti-dilutive. Accordingly, the diluted earnings per share for the current year is presented as equal to basic earnings per share.

10. DIVIDEND

	Company	
	2006 RM'000	2005 RM'000
Paid		
First and final tax exempt dividend of 1.75 sen per ordinary share for 2005 based on issued share capital of 43,000,500 shares paid on 23 January 2006	-	753
Proposed		
First and final tax exempt dividend of 3 sen per ordinary share for 2006 to be proposed in the forthcoming Annual Meeting	1,290	-
Dividend per share	3.00 sen	1.75 sen

11. PROPERTY, PLANT AND EQUIPMENT

	Long term leasehold land	Short term leasehold land	Buildings	Leasehold improvements	Plant, machinery and test equipment	Motor vehicles	Office equipment, furniture and fittings and computers	Capital work-in- progress	Total
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Group									
Cost/Valuation									
At 1 August 2005	3,500	3,020	22,350	2,032	239,039	1,016	6,128	1,530	278,615
Additions	-	-	-	262	18,175	43	636	16,959	36,075
Disposals	-	-	-	-	(319)	-	(6)	-	(325)
Write off	-	-	-	-	(748)	-	(127)	-	(875)
Reclassification	(3,500)	3,500	-	-	1,530	-	-	(1,530)	-
At 31 July 2006	-	6,520	22,350	2,294	257,677	1,059	6,631	16,959	313,490
Representing:									
At cost	-	-	-	2,294	257,677	1,059	6,631	16,959	284,620
At valuation	-	6,520	22,350	-	-	-	-	-	28,870
	-	6,520	22,350	2,294	257,677	1,059	6,631	16,959	313,490
Accumulated Depreciation and Impairment Losses									
At 1 August 2005	-	71	1,308	1,540	160,301	507	4,393	-	168,120
Depreciation charge	-	143	1,531	188	31,777	150	795	-	34,584
Disposals	-	-	-	-	(51)	-	(5)	-	(56)
Write off	-	-	-	-	(746)	-	(125)	-	(871)
At 31 July 2006	-	214	2,839	1,728	191,281	657	5,058	-	201,777
Net Book Value									
At 31 July 2006:									
At cost	-	-	-	566	66,396	402	1,573	16,959	85,896
At valuation	-	6,306	19,511	-	-	-	-	-	25,817
	-	6,306	19,511	566	66,396	402	1,573	16,959	111,713
At 31 July 2005:									
At cost	-	-	-	492	78,738	509	1,735	1,530	83,004
At valuation	3,500	2,949	21,042	-	-	-	-	-	27,491
	3,500	2,949	21,042	492	78,738	509	1,735	1,530	110,495

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

11. PROPERTY, PLANT AND EQUIPMENT (CONTD.)

	Long term leasehold land	Short term leasehold land	Buildings	Leasehold improvements	Plant, machinery and test equipment	Motor vehicles	Office equipment, furniture and fittings and computers	Capital work-in- progress	Total
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Group									
Details at 31 July 2004									
Cost	-	-	-	1,730	210,242	1,016	5,115	1,027	219,130
Valuation	3,500	3,020	22,350	-	-	-	-	-	28,870
Accumulated depreciation and impairment losses	-	-	-	1,282	131,187	353	3,762	-	136,584
Depreciation charge for 2005	-	71	1,308	195	36,315	154	736	-	38,779

	Long term leasehold land	Short term leasehold land	Buildings	Leasehold improvements	Plant, machinery and test equipment	Motor vehicles	Office equipment, furniture and fittings and computers	Total
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Company								
Cost/Valuation								
At 1 August 2005	3,500	320	11,030	1,097	78,201	509	3,629	98,286
Additions	-	-	-	241	4,887	-	418	5,546
Write off	-	-	-	-	(4)	-	(79)	(83)
Reclassification	(3,500)	3,500	-	-	-	-	-	-
At 31 July 2006	-	3,820	11,030	1,338	83,084	509	3,968	103,749
Representing:								
At cost	-	-	-	1,338	83,084	509	3,968	88,899
At valuation	-	3,820	11,030	-	-	-	-	14,850
	-	3,820	11,030	1,338	83,084	509	3,968	103,749

11. PROPERTY, PLANT AND EQUIPMENT (CONTD.)

	Long term leasehold land	Short term leasehold land	Buildings	Leasehold improvements	Plant, machinery and test equipment	Motor vehicles	Office equipment, furniture and fittings and computers	Total
	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
Company								
Accumulated Depreciation and Impairment Losses								
At 1 August 2005	-	6	552	968	64,515	304	2,626	68,971
Depreciation charge	-	78	774	76	5,633	67	428	7,056
Write off	-	-	-	-	(2)	-	(77)	(79)
At 31 July 2006	-	84	1,326	1,044	70,146	371	2,977	75,948
Net Book Value								
At 31 July 2006:								
At cost	-	-	-	294	12,938	138	991	14,361
At valuation	-	3,736	9,704	-	-	-	-	13,440
	-	3,736	9,704	294	12,938	138	991	27,801
At 31 July 2005:								
At cost	-	-	-	129	13,686	205	1,003	15,023
At valuation	3,500	314	10,478	-	-	-	-	14,292
	3,500	314	10,478	129	13,686	205	1,003	29,315
Details at 31 July 2004								
Cost	-	-	-	1,071	74,562	509	3,043	79,185
Valuation	3,500	320	11,030	-	-	-	-	14,850
Accumulated depreciation and impairment losses	-	-	-	830	57,981	231	2,262	61,304
Depreciation charge for 2005	-	6	552	75	6,067	73	370	7,143

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

11. PROPERTY, PLANT AND EQUIPMENT (CONTD.)

The properties were revalued by the Directors based on valuations conducted by Colliers, Jordan Lee & Jaafar, a firm of independent professional valuers, in June 2004. The valuers used the cost method of valuation and the comparison method of valuation to determine the market value of the properties.

Had the properties been carried at cost less accumulated depreciation, their carrying amounts would have been as follows:

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Long term leasehold land	-	85	-	85
Short term leasehold land	464	390	261	181
Buildings	8,801	9,704	3,981	4,357

The Company has not received the title deed to a leasehold land with a carrying amount of RM3,430,000 (2005: RM3,500,000).

The aggregate net book values of plant, machinery and test equipment of the Group and of the Company of RM29,996,000 (2005: RM48,393,000) and RM2,328,000 (2005: RM3,682,000) respectively, are pledged as securities for term loans obtained.

The carrying amounts of property, plant and equipment held under hire purchase arrangements as at balance sheet date are as follows:

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Plant, machinery and test equipment	3,751	8,921	1,047	4,211
Office equipment, furniture and fittings and computers	50	86	50	75
Motor vehicles	172	493	79	205
	3,973	9,500	1,176	4,491

Acquisitions of property, plant and equipment during the financial year were made by the following means:

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Cash payments	26,024	41,203	5,436	3,944
Hire purchase	-	1,583	-	386
Financed by creditors	10,051	635	110	-
	36,075	43,421	5,546	4,330

11. PROPERTY, PLANT AND EQUIPMENT (CONTD.)

Fully depreciated property, plant and equipment which are still in use as at balance sheet date are as follows:

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
At cost:				
Plant, machinery and test equipment	125,521	108,857	54,033	52,324
Leasehold improvements	1,371	1,250	896	890
Office equipment, furniture and fittings and computers	3,670	2,970	2,232	1,808
Motor vehicles	273	273	172	172
	<u>130,835</u>	<u>113,350</u>	<u>57,333</u>	<u>55,194</u>

12. SUBSIDIARY COMPANIES

	Company	
	2006 RM'000	2005 RM'000
At cost:		
Unquoted shares	<u>4,715</u>	<u>4,715</u>

The subsidiary companies are:

Name of Company	Country of Incorporation	Principal Activities	Equity Interest	
			2006 %	2005 %
KESP Sdn Bhd	Malaysia	Provision of semiconductor burn-in and cold testing services and assembly of electronic components	100	100
KESM Test (M) Sdn Bhd	Malaysia	Testing of semiconductor integrated circuits	65.38	65.38

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

13. OTHER INVESTMENTS

	Group/Company	
	2006 RM'000	2005 RM'000
Shares quoted in Malaysia		
- At cost	3,062	3,688
- At market value	486	396
	<u>3,548</u>	<u>4,084</u>
Market value	<u>6,402</u>	<u>4,739</u>

14. INVENTORIES

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
At cost:				
Raw materials	13,586	3,972	-	-
Consumables	687	623	174	155
Work-in-progress	141	17	-	-
Finished goods	940	670	-	-
Inventories in transit	67	-	-	-
	<u>15,421</u>	<u>5,282</u>	<u>174</u>	<u>155</u>
Cost of inventories recognised as an expense during the year	<u>39,414</u>	<u>53,891</u>	<u>59</u>	<u>145</u>

15. TRADE AND OTHER RECEIVABLES

Trade receivables	39,963	36,609	9,686	8,800
Non-trade receivables				
- sundry debtors	424	313	193	192
- current account with related parties	187	73	16	35
- prepayments	748	818	140	284
- deposits	538	545	489	487
	<u>41,860</u>	<u>38,358</u>	<u>10,524</u>	<u>9,798</u>

The Group's normal trade credit term ranges from 30 days to 95 days (2005: 30 days to 95 days).

Related parties refer to a substantial corporate shareholder, Sunright Limited, in which certain Directors have financial interests, and its subsidiaries.

Amounts due from related parties are unsecured, non-interest bearing and have no fixed terms of repayment.

16. DUE FROM SUBSIDIARIES

	Company	
	2006 RM'000	2005 RM'000
Amounts due from subsidiaries comprise:		
Loan receivable	2,595	2,595
Advances	14,400	-
Others	7,745	8,554
	<u>24,740</u>	<u>11,149</u>

These amounts are unsecured, interest free and have no fixed terms of repayment except for loan receivable and advances which bore interest at commercial rates during the financial year.

17. DEPOSITS WITH LICENSED BANKS

In the previous financial year, fixed deposits of the Group amounting to RM32,000 were pledged to banks as security for credit facilities granted to the Group.

The average maturities of deposits at the end of the financial year and the weighted average effective interest rates of the Group and Company were as follows:

	Group		Company	
	2006	2005	2006	2005
Average maturities of deposit at the financial year	24 days	31 days	30 days	30 days
Weighted average effective interest rates	2.80%	2.62%	2.71%	2.53%

18. TRADE AND OTHER PAYABLES

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Trade payables	10,283	4,845	191	90
Non-trade payables				
- current account with related parties	1,011	44	333	-
- accrual for Directors' fees	1,138	972	198	162
- balance due for acquisitions of property, plant and equipment	10,051	635	110	-
- others	15,346	15,445	5,747	6,130
	<u>37,829</u>	<u>21,941</u>	<u>6,579</u>	<u>6,382</u>

The normal trade credit terms granted to the Group range from 30 days to 60 days (2005: 30 days to 60 days).

Amounts due to related parties, as defined in Note 15, are unsecured, non-interest bearing and have no fixed terms of repayment.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

19. BORROWINGS

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Revolving credits - unsecured	1,500	1,500	-	-
Hire purchase payables (a)	1,342	4,746	484	2,092
Term loans - secured (b)	26,914	41,899	2,019	1,825
Other loan - unsecured (c)	1,374	1,374	-	-
	31,130	49,519	2,503	3,917
Amounts repayable within 12 months:				
Revolving credits - unsecured	(1,500)	(1,500)	-	-
Hire purchase payables	(1,159)	(3,404)	(355)	(1,608)
Term loans - secured	(15,804)	(17,647)	(753)	(1,825)
	(18,463)	(22,551)	(1,108)	(3,433)
Amounts repayable after 12 months	12,667	26,968	1,395	484
(a) Hire purchase payables				
Within one year	1,288	3,791	397	1,802
After one year and not later than 5 years	204	1,492	144	541
	1,492	5,283	541	2,343
Future finance charges	(150)	(537)	(57)	(251)
Present value of hire purchase liabilities	1,342	4,746	484	2,092
Present value of hire purchase liabilities:				
Within one year	1,159	3,404	355	1,608
After one year and not later than 5 years	183	1,342	129	484
	1,342	4,746	484	2,092

The hire purchase liabilities bore interest at commercial rates during the financial year.

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
(b) Term loans - secured				
The term loans are repayable as follows:				
Financial year ending 31 July				
2006	-	17,647	-	1,825
2007	15,804	14,434	753	-
2008	8,912	7,487	809	-
2009	2,198	2,331	457	-
	26,914	41,899	2,019	1,825

19. **BORROWINGS (CONTD.)**

(b) **Term loans - secured (Contd.)**

The secured term loans are secured by way of:

- (i) first party pledge over the Group's and Company's property, plant and equipment with aggregate net book values of RM29,996,000 (2005: RM48,393,000) and RM2,328,000 (2005: RM3,682,000), respectively, as referred to in Note 11;
- (ii) negative pledge; and
- (iii) corporate guarantee provided by the Company.

The secured term loans bore interest at commercial rates during the financial year.

(c) **Other loan - unsecured**

Other loan represents an unsecured loan obtained from a minority shareholder of a subsidiary company who is also a corporate shareholder of the Company. This loan bore interest at commercial rates during the financial year and is not expected to be repaid in the next 12 months.

20. **SHARE CAPITAL**

	Group/Company		Group/Company	
	2006 Number ('000)	2005 Number ('000)	2006 RM'000	2005 RM'000
Authorised:				
Ordinary shares of RM1 each				
As at 1 August/31 July	50,000	50,000	50,000	50,000
Issued and fully paid:				
Ordinary shares of RM1 each				
As at 1 August	43,001	42,996	43,001	42,996
Exercise of options	-	5	-	5
As at 31 July	43,001	43,001	43,001	43,001

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

21. RESERVES

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Distributable:				
Retained profits	82,620	69,240	31,640	24,255
Non-distributable:				
Share premium	649	649	649	649
Asset revaluation reserve	7,433	7,433	2,124	2,124
Reserve on consolidation	430	430	-	-
Merger relief reserve	-	-	1,215	1,215
	91,132	77,752	35,628	28,243

As at balance sheet date, the Company has sufficient tax exempt account balance to distribute tax exempt dividends of approximately RM8,752,000 (2005: RM9,469,000). Based on estimated tax credit available under Section 108 of the Income Tax Act 1967 as at balance sheet date, the Company is able to frank payments of dividends amounting to RM16,747,000 (2005: RM12,987,000). Distribution of dividends in excess of these amounts would be subjected to tax at the prevailing statutory tax rate.

22. DEFERRED TAXATION

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
At the beginning of financial year	12,654	12,183	9,091	8,033
Recognised in the income statement (Note 8)	2,260	471	1,461	1,058
At the end of financial year	14,914	12,654	10,552	9,091
Presented after appropriate offsetting as follows:				
Deferred tax liabilities subject to income tax	14,914	12,654	10,552	9,091

Deferred Tax Liabilities of the Group

	Property, plant and equipment	Revaluation surplus	Others	Total
	RM'000	RM'000	RM'000	RM'000
At 1 August 2004	2,295	3,604	10,503	16,402
Recognised in the income statement	(1,680)	(115)	2,783	988
At 31 July 2005	615	3,489	13,286	17,390
Recognised in the income statement	(615)	(177)	3,246	2,454
At 31 July 2006	-	3,312	16,532	19,844

22. DEFERRED TAXATION (CONTD.)

Deferred Tax Assets of the Group

	Property, plant and equipment RM'000	Others RM'000	Total RM'000
At 1 August 2004	(3,139)	(1,080)	(4,219)
Recognised in the income statement	78	(595)	(517)
At 31 July 2005	(3,061)	(1,675)	(4,736)
Recognised in the income statement	(947)	753	(194)
At 31 July 2006	(4,008)	(922)	(4,930)

Deferred Tax Liabilities of the Company

	Property, plant and equipment RM'000	Revaluation surplus RM'000	Others RM'000	Total RM'000
At 1 August 2004	59	1,774	9,864	11,697
Recognised in the income statement	(17)	(11)	1,180	1,152
At 31 July 2005	42	1,763	11,044	12,849
Recognised in the income statement	(27)	(92)	1,047	928
At 31 July 2006	15	1,671	12,091	13,777

Deferred Tax Assets of the Company

	Property, plant and equipment RM'000	Others RM'000	Total RM'000
At 1 August 2004	(2,811)	(853)	(3,664)
Recognised in the income statement	(80)	(14)	(94)
At 31 July 2005	(2,891)	(867)	(3,758)
Recognised in the income statement	223	310	533
At 31 July 2006	(2,668)	(557)	(3,225)

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

22. DEFERRED TAXATION (CONTD.)

Deferred tax assets have not been recognised in respect of the following items:

	Group	
	2006 RM'000	2005 RM'000
Unutilised reinvestment allowances	63,291	67,758

The unutilised reinvestment allowances are available indefinitely for offset against future taxable profits of the respective subsidiaries.

23. SIGNIFICANT RELATED PARTY TRANSACTIONS

Significant transactions between the Company and related parties, including subsidiaries during the financial year were as follows:

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Transactions with Sunright Limited, a corporate shareholder in which certain Directors have financial interests, and its subsidiary companies				
Management fees charged by Sunright Limited	2,632	4,038	1,207	1,578
Interest on loan from Sunright Limited	117	118	-	-
Purchase of property, plant and equipment from:				
- KESU Systems & Service, Inc.	-	77	-	-
- KEST Systems & Service Ltd	-	950	-	684
Sale of property, plant and equipment to:				
- KES Systems, Inc.	7	7	-	7
- KEST Systems & Service Ltd	275	-	-	-
Purchases from:				
- KES Systems & Service (1993) Pte Ltd	323	1,151	230	937
- Kestronics (M) Sdn Bhd	145	130	27	11
Transactions with subsidiary companies				
Rent of factory to subsidiary company			325	325
Purchase of property, plant and equipment from subsidiary company			123	-
Interest on loan and advances to subsidiary company			340	1,662

The Directors are of the opinion that the above transactions were in the normal course of business and at terms mutually agreed between the companies.

24. CONTINGENT LIABILITIES

	Company	
	2006 RM'000	2005 RM'000
Unsecured:		
Guarantees granted to licensed banks and financial institutions in respect of credit facilities extended to subsidiary companies	31,854	43,181

25. CAPITAL COMMITMENTS

	Group		Company	
	2006 RM'000	2005 RM'000	2006 RM'000	2005 RM'000
Authorised and contracted for	1,928	731	1,738	703

26. SEGMENT INFORMATION

Segment information is not presented as the Group operates primarily in the electronic industry in Malaysia.

27. FINANCIAL INSTRUMENTS

(a) Financial Risk Management Objectives and Policies

The Group's financial risk management policy seeks to ensure that adequate financial resources are available for the development of the Group's business whilst managing its interest rate, foreign exchange, liquidity and credit risks. The Group's risk management approach seeks to minimise the potential material adverse impact of those exposures.

(b) Interest Rate Risk

The Group obtains additional financing through bank borrowings and leasing arrangements. The Group's policy is to obtain the most favourable interest rates available.

Surplus funds are placed with reputable licensed banks.

Information relating to the Group's interest rate exposure is also disclosed in the notes on borrowings, including leasing obligations.

NOTES TO THE FINANCIAL STATEMENTS

- 31 JULY 2006

27. FINANCIAL INSTRUMENTS (CONTD.)

(c) Foreign Exchange Risk

The Group has transactional currency exposures which arises from property, plant and equipment purchases made in currencies other than its functional currency. The principal foreign currencies which the Group has exposure to are Singapore Dollars, United States Dollars, Japanese Yen and Euro Dollars. Transactional exposures in currencies other than the entity's functional currency are kept to a minimum.

The net unhedged financial assets and financial liabilities of the Group companies that are not denominated in their functional currencies are as follows:

	2006 RM'000	2005 RM'000
Net Financial Liabilities		
Non-functional Currencies:		
Singapore Dollars	(1,209)	(1,565)
United States Dollars	(4,842)	(3,383)
Japanese Yen	(5)	(69)
Euro Dollars	(281)	-
	(6,337)	(5,017)

(d) Credit Risk

The carrying amounts of investments and trade and other receivables represent the Group's maximum exposure to credit risk. No other financial assets carry a significant exposure to credit risk.

Financial transactions and the placement of surplus cash in short term interest-bearing deposits are restricted to reputable financial institutions.

(e) Liquidity Risk

The Group's cash and short-term deposits, operating cash flows, availability of banking facilities and debt maturity profile are actively managed to ensure adequate working capital requirements and that repayment and funding needs are met.

(f) Fair Values

The carrying amounts of the financial assets and liabilities, other than those disclosed below, approximate their fair values due to the short-term maturity of these financial instruments.

(i) Borrowings

The carrying amount of the borrowings approximate their fair values as these instruments bear interest at floating rates.

(ii) Other Investments

The fair value of quoted investments is determined by reference to the market price at the balance sheet date and is disclosed in Note 13.

28. EMPLOYEES SHARE OPTION SCHEME (“ESOS”)

Options granted and accepted under ESOS during the financial year ended 31 July 2006 are as follows:

Name of Employees	Number of Options Granted
Augustus Balu A/L Palaniandy Vincent	2,000
Chau Chee Keong	3,000
Chee Kok Leong	1,000
Chong Wan Kit	2,000
Hing Kam Lan	2,000
Ibrahim Bin Bujang	3,000
Jannet Marcus A/P Masi	3,000
Kee Eng Yin	13,000
Koay Chin Chye	2,000
Lee Yoon Yin	2,000
Leong Choi Wan	2,000
Leow Soo How	2,000
Liew Pow Yeong	2,000
Lim Chee Seng	13,000
Lim Eng Guan	800
Lim Swee Leu	2,000
Lim Tee Wan	2,000
Looi Kwok Hoong	5,000
Maharan bt Mohamed Tajuddin Ariffin	1,000
Manjit Singh A/L Kehar Singh	2,000
Mohd Zaki Bin Mahmood	2,000
Murugathan A/L Peruma	3,000
Ng Boon Hin	3,000
Ooi Hoon Koh	800
Rahanah Binti Mohd Shoib	2,000
S Swami Vivekananda A/L Subranyam	2,000
Samuel Lim Syn Soo	12,800
Saravanan A/L Govida Padachi	2,000
Sylvia Francis	2,000
Tan Eng Hong	3,000
Tan Teoh Khoo	12,800
Tang Chin Huat	1,000
Tee Hong Hiong	5,000
Teoh Choo Kuan	7,600
Than Bee Heong	2,000
Wong Hoo Mooi	2,000
Wong Yin Lek	2,000
Yaw Kwee Huay	2,000
Yeo Kean Kee	2,400
Yeoh Phaik Suan	2,000
Yong Yih Ling	2,000

SHAREHOLDERS' INFORMATION

AS AT 29 SEPTEMBER 2006

ANALYSIS OF SHAREHOLDINGS

Authorized share capital	:	RM50,000,000.00
Issued and paid-up capital	:	RM43,000,500
Type of shares	:	Ordinary shares of RM1.00 each
Voting Rights	:	One vote per ordinary share

ANALYSIS BY SIZE OF HOLDINGS

Number of Holders	Holdings	Total Holdings	%
2	Less than 100	100	-
248	100 to 1,000 shares	218,800	0.51
915	1,001 to 10,000 shares	3,597,100	8.37
139	10,001 to 100,000 shares	3,549,500	8.25
8	100,001 to less than 5% of issued shares	6,359,000	14.79
2	5% and above of issued shares	29,276,000	68.08
	Total	43,000,500	100.00

SUBSTANTIAL SHAREHOLDERS (PER REGISTER OF SUBSTANTIAL SHAREHOLDERS)

Name of Shareholders	Number of Shares Held	Percentage of Shareholdings
1. Sunright Limited	20,825,000	48.43
2. Samuel Lim Syn Soo	20,825,000*	48.43
3. Lembaga Tabung Haji	8,451,000	19.65

* Deemed interest by virtue of his substantial shareholdings in Sunright Limited.

DIRECTORS' SHAREHOLDINGS (PER REGISTER OF DIRECTORS' SHAREHOLDING)

SHARES IN THE COMPANY

Name of Director	Direct	%	Number of Shares Held	
			Deemed Interest	%
1. Samuel Lim Syn Soo	-	-	20,825,000*	48.43
2. Kenneth Tan Teoh Khoon	-	-	-	-
3. Lim Mee Ing	-	-	-	-
4. Dato' Dr. Norraesah Haji Mohamad	612,000	1.42	-	-
5. Ahmad Riza Bin Basir	-	-	-	-
6. Tuan Haji Zakariah Bin Yet	-	-	-	-
7. Yong Chee Hou	-	-	-	-

* Deemed interest by virtue of his substantial shareholdings in Sunright Limited.

SHARES IN RELATED CORPORATION

KESM Test (M) Sdn Bhd

Name of Director	Direct	%	Number of Shares Held	
			Deemed Interest	%
1. Samuel Lim Syn Soo	-	-	692,308*	34.62
	-	-	1,307,692**	65.38

KESP Sdn Bhd

Name of Director	Direct	%	Number of Shares Held	
			Deemed Interest	%
1. Samuel Lim Syn Soo	-	-	1,200,000**	100

* Deemed interest by virtue of his substantial shareholdings in Sunright Limited.

** Deemed interest by virtue of his substantial shareholdings in KESM Industries Berhad.

EMPLOYEES SHARE OPTION SCHEME ("ESOS")

The following Directors are deemed to have interest in the shares of the Company by virtue of options granted under the Company's ESOS.

Name of Directors	Exercise Price	Options Granted to Subscribe for Ordinary Shares of RM1.00 Each
1. Samuel Lim Syn Soo	RM2.192 *	50,000*
	RM2.464 *	50,000*
	RM2.344 *	50,000*
	RM3.10	34,000
	RM2.50	20,000
	RM1.927	12,800
		216,800
2. Kenneth Tan Teoh Khoon	RM2.192 *	50,000*
	RM2.464 *	50,000*
	RM2.344 *	50,000*
	RM3.10	34,000
	RM2.50	20,000
	RM1.927	12,800
		216,800

* Adjusted to include the effect of bonus issue of shares of 3 for 2 existing shares made on 4 December 2002 by the Company.

SHAREHOLDERS' INFORMATION

AS AT 29 SEPTEMBER 2006

THIRTY LARGEST SHAREHOLDERS

Name of Shareholders	Number of Shares Held	Percentage of Shareholdings
1. Sunright Limited	20,825,000	48.43
2. Lembaga Tabung Haji	8,451,000	19.65
3. Wong Tee Kim @ Wong Tee Fatt	2,150,000	5.01
4. Tan Teong Siew	2,057,500	4.78
5. BHLB Trustee Berhad TA Small Cap Fund	726,500	1.69
6. Norraesah Binti Mohamad	604,500	1.41
7. Tan Kim Hin	405,000	0.94
8. Cimsec Nominees (Asing) Sdn Bhd Exempt An for CIMB-GK Securities Pte Ltd	157,500	0.37
9. Tan Jin Tuan	143,000	0.33
10. Wong Yoke Fong @ Wong Nyok Fing	115,000	0.27
11. Wong Yoon Tet	98,000	0.23
12. Soo Chern Chin @ Soo Chai	97,400	0.22
13. Lim Siew Geok	95,000	0.22
14. Citigroup Nominees (Tempatan) Sdn Bhd Pledged securities account for Susy Ding	90,400	0.21
15. Capital Dynamics Asset Management Sdn Bhd	70,000	0.16
16. Lee Siew Lin	67,000	0.15
17. Public Nominees (Tempatan) Sdn Bhd Pledged securities account for Sii Lik Kung Inter-Pacific Equity Nominees (Tempatan) Sdn Bhd	60,500	0.14
18. Kim Eng Securities Pte Ltd for Goh Seng Kee	60,000	0.14
19. Ter Kham Ee	55,000	0.13
20. Lee Hau Hian	54,000	0.12
21. Tan Chap Thong Sdn Bhd	50,000	0.12
22. Wee Pock Soon @ Ho Pock Soon	50,000	0.12
23. Wong Ban Sun	50,000	0.12
24. Lean Teik Chooi	50,000	0.12
25. Amsec Nominees (Asing) Sdn Bhd Fraser Securities Pte Ltd for Ramesh s/o Pritamdas Chandiramani	50,000	0.12
26. Simon Wong Yoon Thye	50,000	0.12
27. Wong Yoon Chyuan	50,000	0.12
28. Goh Chuan Seng	50,000	0.12
29. Mayban Nominees (Tempatan) Sdn Bhd Capital Dynamics Asset Management Sdn Bhd for Perkasa Trading Sdn Bhd	48,000	0.11
30. Sushil Kaur a/p Sudar Shan Singh	45,600	0.10
Total	36,875,900	85.76

GROUP PROPERTIES

AS AT 31 JULY 2006

Location	Description / Existing use	Date of Last Revaluation	Tenure	Approximate Land Area / Built-up Area (sq m)	Approximate Age Of Building (Years)	Net Book Value (RM'000)
KESM Industries Berhad						
Lot 4, Kawasan MIEL Phase 1 Sungei Way Free Industrial Zone Jalan SS8/4 Selangor Darul Ehsan	Industrial land/ Factory and Office premises	10 Jun 2004	No individual qualified title has been yet issued Note (a)	5,064/ Phase I – 2,315 Phase II – 3,169 Phase III – 3,345	Phase I - 10 Phase II - <8 Phase III - <9	3,430/ Phase I – 2,354 Phase II – 3,077 Phase III – 3,828
Factory Lot Nos. A5 and A6 Kawasan MIEL Batang Kali Phase II Selangor Darul Ehsan	Industrial land/ Factory and Office premises	17 Jun 2004	Leasehold for 60 years expiring on 13 Oct 2052	2,753/ 879	15	305/445
KESP Sdn. Bhd.						
Plot 253 Jalan Kampong Jawa Bayan Lepas Free Industrial Zone (Phase 3) Penang	Industrial land/ Factory and Office premises	22 Jun 2004	Leasehold for 60 years expiring on 7 Aug 2045	8,085/ 11,617	Phase I – 14 Phase II – 10 Phase III – 7	2,571/ 8,927
42-17-19 Desa Green Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	17	94
42-15-12A Desa Green Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	17	94
15-4-7 Kota Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	14	94
15-7-4 Kota Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	14	94
Block 16-3A-3 Taman Seri Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	13	99
Block 18-9-11 Taman Seri Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	13	104
33-11-21 Taman Pekaka Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	10	94
Block 16-1-3 Taman Seri Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	13	101
Block 18-6-5 Taman Seri Nibong Penang	3-bedroom apartment/ employees' hostel	22 Jun 2004	Freehold	65.03	13	105

Note: -

(a) Malaysian Industrial Estates Sendirian Berhad, the developer of the industrial land, has indicated that the land title when issued will be leasehold for a period of 99 years.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the Thirty-Fifth Annual General Meeting of the Company will be held at Kristal Suite 1 & 2, 1st Floor, West Wing, Hilton Petaling Jaya, No. 2 Jalan Barat, 46200 Petaling Jaya, Selangor Darul Ehsan, Malaysia on Thursday, 4 January 2007 at 10.30 a.m. for the following purposes: -

AGENDA

- | | | |
|----|--|--------------|
| 1. | To receive the Audited Financial Statements for the financial year ended 31 July 2006 together with the reports of the Directors and of the Auditors thereon. | Resolution 1 |
| 2. | To declare a first and final tax exempt dividend of 3 sen per share in respect of the financial year ended 31 July 2006. | Resolution 2 |
| 3. | To approve payment of Directors' fees in respect of the financial year ended 31 July 2006. | Resolution 3 |
| 4. | To re-elect the following Directors retiring pursuant to Article 80 of the Company's Articles of Association and being eligible, offer themselves for re-election: - | |
| | (a) Mr Yong Chee Hou | Resolution 4 |
| | (b) Mr Kenneth Tan Teoh Khoon | Resolution 5 |
| 5. | To re-appoint Messrs Ernst & Young as the Company's Auditors and to authorise the Board of Directors to fix their remuneration. | Resolution 6 |
| 6. | As Special Business: - | |

To consider and if thought fit, pass the following Resolutions as Ordinary Resolutions:-

- | | | |
|-----|--|--------------|
| (a) | <p>ORDINARY RESOLUTION NO. 1
 Authority to issue shares by Company pursuant to Section 132D of the Companies Act, 1965</p> <p>"THAT pursuant to Section 132D of the Companies Act, 1965, and subject always to the approval of the relevant authorities, the Directors be and are hereby empowered to issue shares in the Company, from time to time to such persons and upon such terms and conditions and for such purposes as the Directors may, in their absolute discretion, deem fit, provided that the aggregate number of shares to be issued pursuant to this resolution does not exceed 10% of the issued share capital of the Company for the time being, and that the Directors be and are also empowered to obtain the approval for the listing of and quotation for the additional shares so issued on Bursa Malaysia Securities Berhad and that such authority shall continue in force until the conclusion of the next Annual General Meeting of the Company."</p> | Resolution 7 |
|-----|--|--------------|

(b) **ORDINARY RESOLUTION NO. 2**
Authority to allot shares pursuant to the Employees Share Option Scheme

"THAT subject always to the approval of the relevant authorities, authority be and is hereby given to the Directors to issue shares in the capital of the Company at any time upon such terms and conditions and for such purposes as the Directors, may, in their discretion, deem fit including but not limited to such shares as may be issued pursuant to the exercise of the options under the Employees Share Option Scheme as approved by an ordinary resolution passed at the Extraordinary General Meeting of the Company held on 21 November 2005 provided that the aggregate number of shares to be issued pursuant to this resolution does not exceed 15% of the issued share capital of the Company for the time being."

Resolution 8

7. To transact any other business which may be properly transacted at an Annual General Meeting, due notice of which shall have been previously given in accordance with the Companies Act, 1965 and the Company's Articles of Association.

BY ORDER OF THE BOARD
LEONG OI WAH (MAICSA 7023802)
Company Secretary

Petaling Jaya
27 October 2006

NOTES: -

1. A member entitled to attend and vote at the Annual General Meeting is entitled to appoint a proxy/proxies who may but need not be a member/members of the Company to attend and vote in his/her stead and Section 149(1)(b) of the Companies Act, 1965 shall not apply.
2. When a member appoints two or more proxies the appointments shall be invalid unless he/she specifies the proportions of his/her holdings to be represented by each proxy.
3. The instrument appointing a proxy shall be in writing under the hand of the appointer or his/her attorney duly authorized in writing or, if the appointer is a corporation, either under its common seal or under the hand of an officer or attorney duly authorized.
4. The instrument appointing a proxy must be deposited at the Registered Office at 312, 3rd Floor, Block C, Kelana Square, 17 Jalan SS7/26, 47301 Petaling Jaya, Selangor Darul Ehsan, Malaysia, at least forty-eight (48) hours before the time appointed for holding the Meeting or any adjournment thereof.

NOTICE OF ANNUAL GENERAL MEETING

EXPLANATORY NOTES ON SPECIAL BUSINESS: -

(a) Resolution pursuant to Section 132D of the Companies Act, 1965

The proposed Resolution No. 7 will give powers to the Directors to issue up to a maximum ten per centum (10%) of the issued share capital of the Company for the time being for such purposes as the Directors would consider in the interest of the Company.

This authority, unless revoked or varied by the Company at a general meeting, will expire at the conclusion of the next Annual General Meeting of the Company.

(b) Resolution pursuant to the Employees Share Option Scheme

The proposed Resolution No. 8 authorises the Directors to issue shares in the Company upon the exercise of the options under the Employees Share Option Scheme up to an aggregate amount not exceeding 15% of the issued share capital of the Company for the time being.

This authority, unless revoked or varied at a general meeting, will expire at the next Annual General Meeting of the Company.

NOTICE OF DIVIDEND ENTITLEMENT

NOTICE IS HEREBY GIVEN that the First and Final Tax Exempt Dividend of 3 sen per share in respect of the financial year ended 31 July 2006, if approved at the forthcoming Annual General Meeting, will be paid on 2 February 2007 to Depositors registered in the Record of Depositors on 19 January 2007. A Depositor shall qualify for entitlement only in respect of:

- a) Shares transferred into the Depositor's securities accounts before 4.00 p.m. on 19 January 2007, in respect of ordinary transfers; and
- b) Shares bought on Bursa Malaysia Securities Berhad ("Bursa Securities") on a cum entitlement basis according to the Rules of Bursa Securities.

BY ORDER OF THE BOARD
LEONG OI WAH (MAICSA 7023802)
Company Secretary

Petaling Jaya
27 October 2006



STATEMENT ACCOMPANYING NOTICE OF ANNUAL GENERAL MEETING

1. **The names of Directors who are standing for re-election: -**

- (a) Mr. Yong Chee Hou
- (b) Mr. Kenneth Tan Teoh Khoon

2. **The details of attendance of directors at Board meetings**

Total of five (5) meetings were held during the financial year ended 31 July 2006. Details of attendance of each Director are set out on page 8 of the Annual Report.

3. **The place, date and hour of the 35th Annual General Meeting**

Place : Kristal Suite 1 & 2
1st Floor, West Wing
Hilton Petaling Jaya
No. 2 Jalan Barat
46200 Petaling Jaya
Selangor Darul Ehsan
Malaysia

Date & Time : Thursday, 4 January 2007 at 10:30 a.m.

4. **Further details of Directors who are standing for re-election.**

The details of the Directors are set out on pages 5 and 7 of the Annual Report.

PROXY FORM

I/We _____ (Full Name in Block Letters)
of _____ (Address)
being a member / members of KESM Industries Berhad hereby appoint

Name	Address	NRIC/ Passport No.	Proportion of Shareholdings (%)

and/or (delete as appropriate)

Name	Address	NRIC/ Passport No.	Proportion of Shareholdings (%)

or failing him/her, the Chairman of the Meeting as my/our proxy/proxies to attend and vote for me/us on my/our behalf, and if necessary, to demand a poll, at the Thirty-Fifth Annual General Meeting of the Company to be held at Kristal Suite 1 & 2, 1st Floor, West Wing, Hilton Petaling Jaya, No. 2 Jalan Barat, 46200 Petaling Jaya, Selangor Darul Ehsan, Malaysia on Thursday, 4 January 2007 at 10.30 a.m. and at any adjournment thereof.

I/We direct my/our proxy/proxies to vote for or against the Resolutions to be proposed at the meeting as indicated hereunder. If no specific direction as to voting is given or in the event of any item arising not summarized below, my/our proxy/proxies may vote or abstain from voting at his/her discretion.

No.	Resolutions	For*	Against*
1.	Receive Audited Financial Statements, Directors' Report and Report of the Auditors		
2.	Approval of first and final dividend		
3.	Approval of Directors' fees		
4.	Re-election of Mr Yong Chee Hou as Director		
5.	Re-election of Mr Kenneth Tan Teoh Khoon as Director		
6.	Re-appointment of Auditors		
7.	Approval to issue shares pursuant to Section 132D of the Companies Act, 1965		
8.	Approval to allot shares pursuant to Employees Share Option Scheme		

* Please indicate your vote "For" or "Against" with an "X" within the box provided.

Signed this _____ day of _____ 2006 / 2007

Total Number of Shares Held

Signature/Common Seal of Shareholder(s)

NOTES :

1. A member entitled to attend and vote at the Annual General Meeting is entitled to appoint a proxy/proxies who may but need not be a member/members of the Company to attend and vote in his/her stead and Section 149(1)(b) of the Companies Act, 1965 shall not apply.
2. When a member appoints two or more proxies the appointments shall be invalid unless he/she specifies the proportions of his/her holdings to be represented by each proxy.
3. The instrument appointing a proxy shall be in writing under the hand of the appointer or his/her attorney duly authorized in writing or, if the appointer is a corporation, either under its common seal or under the hand of an officer or attorney duly authorized.
4. The instrument appointing a proxy must be deposited at the Registered Office at 312, 3rd Floor, Block C, Kelana Square, 17 Jalan SS7/26, 47301 Petaling Jaya, Selangor Darul Ehsan, Malaysia, at least forty-eight (48) hours before the time appointed for holding the Meeting or any adjournment thereof.

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Affix
postage
here

The Company Secretary
KESM INDUSTRIES BERHAD (13022-A)
312, 3rd Floor
Block C, Kelana Square
17 Jalan SS7/26
47301 Petaling Jaya
Selangor Darul Ehsan
MALAYSIA

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KESM INDUSTRIES BERHAD (13022-A)

Lot 4, SS 8/4

Sungei Way Free Industrial Zone

47300 Petaling Jaya

Selangor Darul Ehsan

Malaysia

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Fax: (603) 787-58558