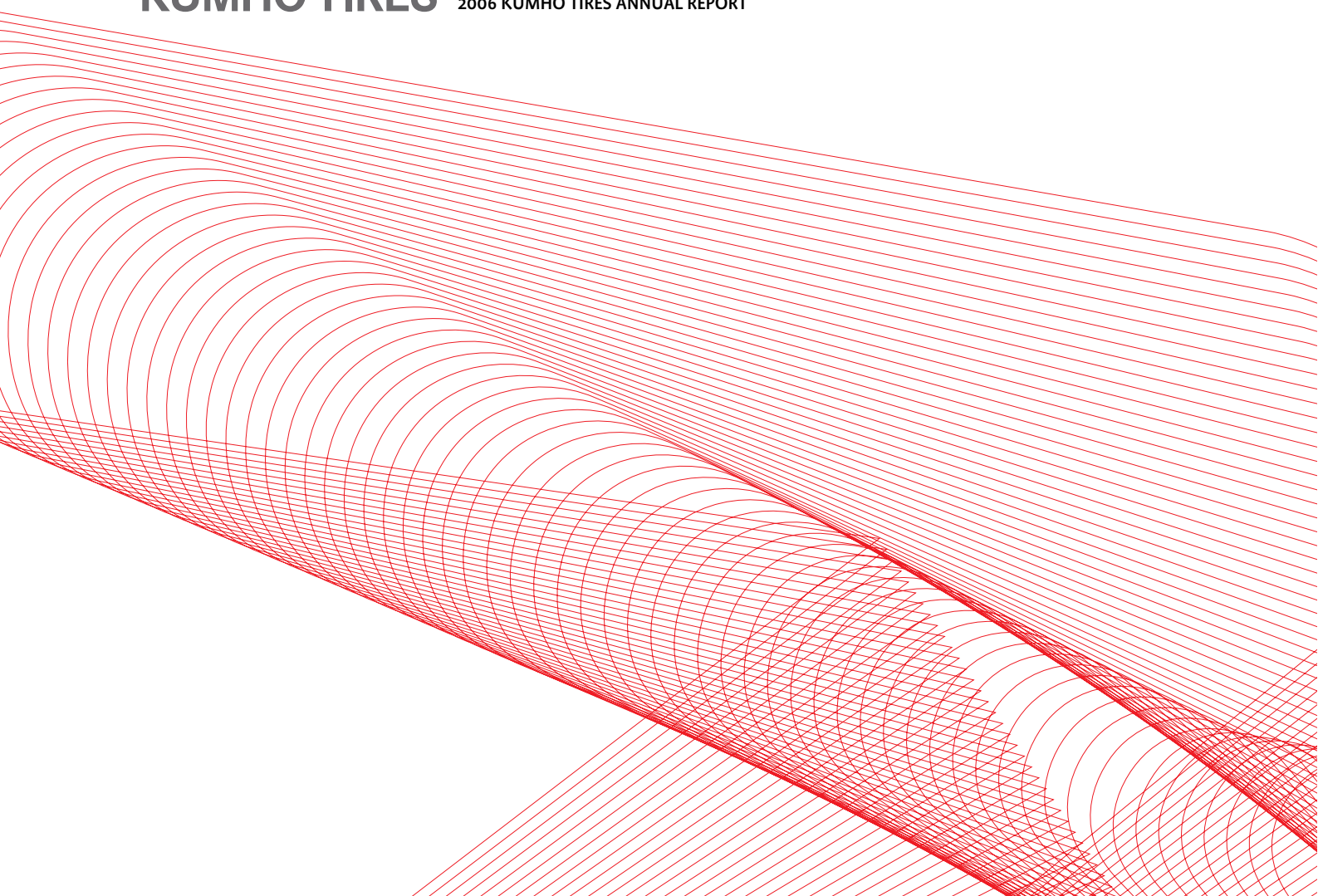




# KUMHO TIRES

2006 KUMHO TIRES ANNUAL REPORT



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## Growing up

There are several words that we use to express beauty:

harmony and balance, delight and satisfaction.

A company that harmonizes the life of mankind,

and appropriately balances production and distribution,

Where the joy of meeting customers is our greatest source of energy

Where customer satisfaction is upheld as the foremost value

Should we not say such a company is beautiful?

Kumho Tires aspires to become a company that extends a true beauty

through honest communication with the world.

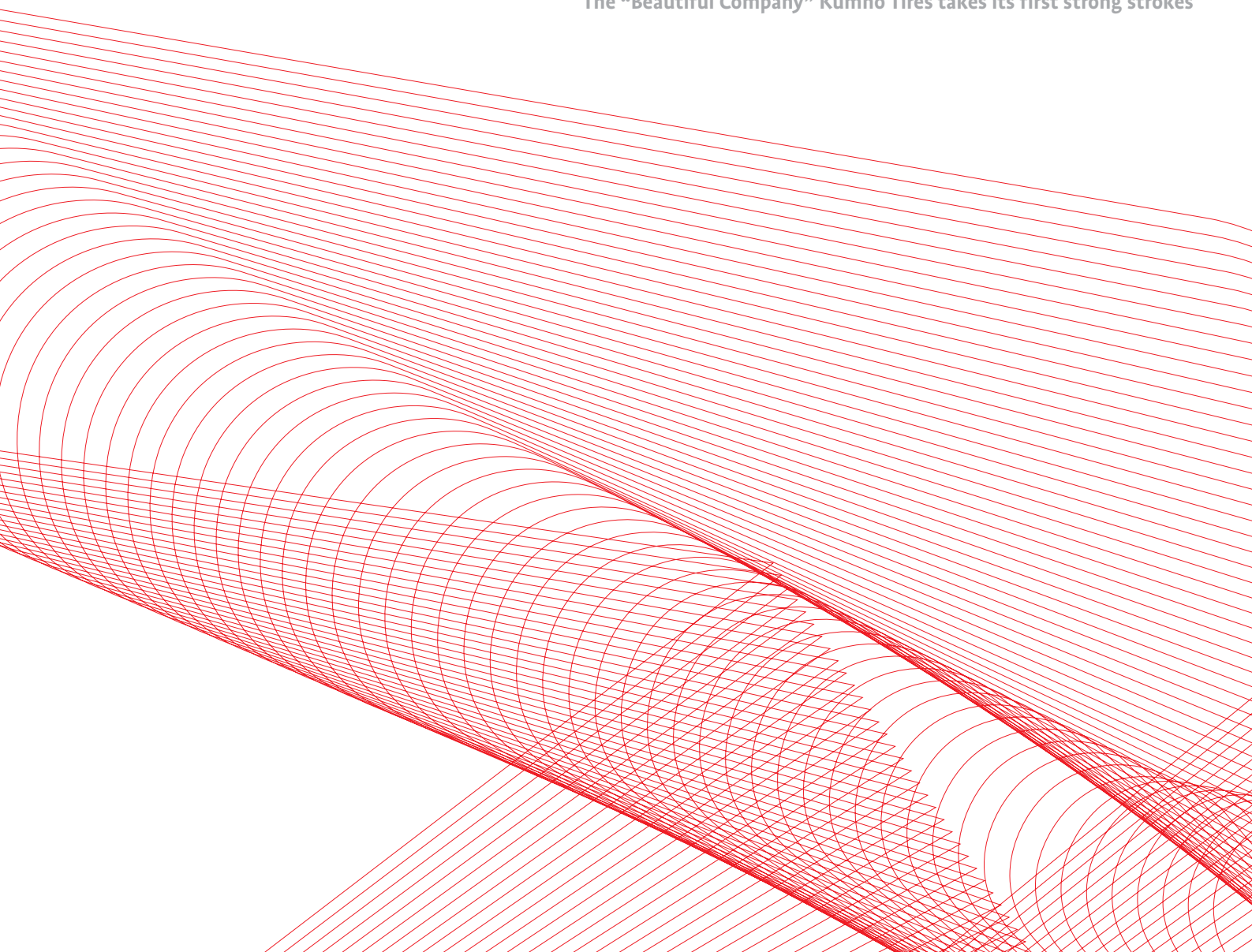
We will become a company that does nothing to

warrant criticism and keeps its promises

A strong, trusted company that performs all of its social responsibilities

and contributes to the community as a corporate citizen.

The “Beautiful Company” Kumho Tires takes its first strong strokes





## Milestones

Sep. 1960	Established Samyang Tire Co.	Feb. 1994	Became the first Korean tire company to acquire ISO 9001 certification
Sep. 1974	Completed construction of Gwangju Plant	Feb. 1996	Changed corporate name to Kumho Tire Co., Inc.
Nov. 1976	Exceeded annual production of 1 million units for the first time in Korea	Nov. 1996	Completed construction of Nanjing plant
Sep. 1981	Established Gwangju Central Research and Development Center	Jun. 1998	Established European Research Center (KETC)
Aug. 1984	Changed Corporate Official Name to Kumho Tires Co.	Mar. 2002	Selected as an official supplier for the Marlboro Masters of F3
Oct. 1989	Completed Construction of Gokseong Plant	Nov. 2002	Developed the world's first 26-inch UHP tire
Oct. 1990	Established U.S. Research Center (KATC)	Jun. 2003	Ranked the global 9th tire company





Jul. 2003 Spun off from Kumho Industrial Co. and established Kumho Tires Co., Inc.

Dec. 2003 Completed construction of Korea's first Automated Production Unit (APU) plant in Pyeongtaek

Aug. 2004 Selected as the Advanced Technology Research Center (ATC) Acquired ISO/TS 16949 certification

Feb. 2005 Became the first Korean company that dual-listed on the Korea Stock Exchange and the London Stock Exchange

Apr. 2005 Completed construction for the second plant at Nanjing in China

Mar. 2006 Established Korea's first tire history museum

May 2006 Groundbreaking for Changchun plant in China

Jul. 2006 Completed construction of Tianjin plant in China

Sep. 2006 Established Chinese Research and Development Center (KCTC)

Oct. 2006 Developed the world's first 32-inch UHP (Ultra High Performance) tire

Oct. 2006 Groundbreaking for Vietnamese plant

Dec. 2006 Established sales corporation at Shanghai in China

## Financial Highlights



	2006	2005	2004
	(Unit : KRW mn)	(Unit : KRW mn)	(Unit : KRW mn)
Sales	1,813,794	1,763,125	1,646,344
Operating Income	80,306	169,255	169,326
Ordinary Income	2,102	124,097	124,891
Net Income	970	98,199	100,383
Total Assets	2,409,782	2,205,897	1,656,296
Total Liabilities	1,499,856	1,238,961	1,038,718
Total Stockholders' Equity	909,926	966,936	617,578
Operating Margin (%)	4.4%	9.6%	10.2%
Debt Ratio (%)	164.8%	128.1%	168.1%

## Shareholder Information

In 2006, the KOSPI was closed with about 4 percent higher compared to the previous year, ending at 1,434.46 points. Tire-related shares had shown weak performance for the year due to external factors such as a skyrocketing natural rubber price and a strong won trend. Kumho Tires started off the year at 16,300 won, but the stock prices tended to slightly move in a trend between 11,000 and 13,000 won, along with profit loss in the second and the third quarters. Raw material prices including a natural rubber, which significantly affected last year's profitability, have shown a temporary rise early this year, but there is an optimistic outlook that tire-related shares would recover their profits because raw material prices are expected to stabilize in the long term. As of late 2006, 70 million shares are being issued. Foreign holdings, which accounted for 25.6 percent when the company was listed, are 25.8 percent as of Dec. 28 2006.

### Evaluation and Outlook

2006 was a difficult year for the tire industry which experienced profit losses due to rising raw material price, especially a natural rubber price and unstable foreign exchange rates. Kumho Tires' ordinary income was primarily dropped from equity losses because of the initial operation of Tianjin plant in China, last July. The loss, however, is a natural outcome that could find in manufacturing industry before a break-even point. Thus, for the last third quarter, the loss was comparatively higher.

Profitability for the new plant would gradually improve as it passes the break-even point as a marginal line. Generally, the break-even-point takes around 12~15 months from the initial operation. Therefore, we would expect satisfactory results from the new plant in the near future. Along with active overseas marketing activities, we have gradually expanded our foreign production capacity in order to improve profitability and increase cost competitiveness in manufacturing. We have also boosted profitability by focusing on higher margin product mix and continuously raising average sales prices on inch-up products.

In 2007, we would set up a global ERP system for efficient management and establish a global marketing strategy. We also plan to seek new markets other than North America and Europe in an effort to diversify exports, and enhance new OE businesses with foreign top automakers to raise brand awareness. Currently, we provide tires for Volkswagen. Through steady brand improvement and technological competitiveness, we won a supply contract of 18-inch UHP tire with Daimler Chrysler for upcoming 2007 Sebring Sedan last November, 2006. This year, we would start to supply high performance tires for Benz. Our efforts to strengthen internal competence and global competitiveness would increase operating profits for this year and this would lead to rises in the EPS as well.

## Message from the CEO





## Become the beautiful owner of a beautiful company.

### **We have confirmed the will for a new challenge.**

The new year has dawned. We wish you and your family good health and luck for this year.

Businesses will recall 2006 as being a more difficult year in management compared to previous years. The foreign exchange rate, oil prices, interest rates, and other external factors all played a part in worsening corporate competitiveness. In addition to this, the global business environment was none too smooth, making it a rough year for Kumho Tires as well. The export environment was not easy as dropping exchange rates diluted the effect of raising prices on exports. We were also influenced by the difficulties that automobile makers were experiencing between labor and management.

Despite these circumstances, Kumho Tires faced the difficult management environment right in the eye. Taking stronger vows in our purpose for challenges, we did our best to achieve balanced development by maintaining technology development and continuing external expansion. Thanks to these efforts, Kumho Tires was able to continue research and development in 2006 and by establishing foreign bases and expanding our distribution network, we were able to from the beginnings of a global multi-factory system. Moreover, the Kumho Group revealed a new corporate identity to celebrate its 60<sup>th</sup> anniversary and established a tire museum, a living history of half a century of Kumho Tire. We also achieved notable performance in establishing marketing strategies to create high value-added brands.

2006 was a difficult year for everyone, but it was also a precious time for Kumho Tires to lay down the foundation in becoming a global company through strategic management.

### **Strengthening global capacity**

Last year, Kumho Tires hastened its steps towards the global market, making earnest preparations for global market expansions by constructing a foreign plant and establishing a R&D institute. Beginning with the groundbreaking of the ChangChun plant-- our third Chinese plant-- in May, we completed construction of the Tianjin plant in July and signed a memorandum of understanding for the construction of a TBR plant in Nanjing. Construction of our Chinese research and development institute was completed in September, followed by a groundbreaking ceremony for our Vietnamese plant in October. In December, we established a sales corporation in Shanghai, securing a firm foothold to target the Chinese market. We are preparing for future active marketing in China.

We have established a "global ERP project" that will be the axis of our future management operations. We plan to successfully construct a comprehensive corporate resource management system to settle into a global management system at an early stage. We have also formed a mid-to long-term marketing strategy, laying down the cornerstone in boosting brand value and sales. Thus, Kumho Tires competes with global tire firms by staking out overseas markets and is expanding its distribution network and acquiring stable production in order to meet increasing demand for tires.

### **We will become the leader of the tire industry development in China**

Kumho Tires was the first of all tire companies in the world to enter the Chinese market in 1994. Now, more than a decade later, Kumho Tires is operating plants in Nanjing and Tianjin, is constructing a plant in ChangChun, and will soon begin construction for a TBR plant in Nanjing. By operating four plants, the company seeks to preoccupy key distribution locations on mainland China. This will enable Kumho Tires to produce an annual 25 million units only in China in 2008.

Our Chinese plants were built recently or are in the process of being built and are therefore equipped with the most recent state-of-the-art production system in comparison to existing factories. The research and development center established in China in September 2006 (KCTC: Kumho China Technical Center) aims to research and develop products that are more well-equipped for the local needs of the Chinese market. The center will continue to be equipped with the finest facilities in the industry.

The brisk growth in the Chinese market is a mirror providing foresight into Kumho Tires' future. Not only do we plan to preoccupy in China's domestic market, we plan to utilize the region as a base for foreign exports and a foothold for our expansion to the global market. China poses a great significance in that we must lay sturdy groundwork upon which Kumho Tires can blossom into the infinite. Kumho Tires is also considering plans to construct plants in locations other than China in the future.

### **2007 is a year of strategic management and responsible management**

In the current tire market, the demand for high value added products is continuously growing and automobile manufacturing companies are expanding global distribution. Also, with new economic blocks such as BRICs rising as emerging markets, the future of the tire industry is shining brightly. In the market, we can only gain competitiveness by developing new technology, expanding distribution networks, and consolidating customer service.

Kumho Tires is marching forward with the vision of becoming one of the global top five tire companies by 2015. We are boosting brand recognition around the world through our global marketing strategy and strengthening our foreign OE business- applying core technology that is differentiated from our competitors on our products and creating ripple effects towards the domestic market.

In order to realize these dreams, we have designated Kumho Tires' management policy for 2007 as strategic management and responsibility management. In order to advance as a global company, we must establish a detailed, efficient goal and execute a strategic management plan towards that goal. In that process, we will do our utmost to do our best in displaying full responsibility for our management practices.

Kumho Tires is taking off with the vision of becoming one of the "top five tire companies in the world" by 2015. In order to achieve this, we are boosting brand recognition around the world through continued global marketing strategy. We are applying core technology that is differentiated from our competitors on our products to raise satisfaction on our product quality and continuously developing revolutionary products to meet market demand. We are also strengthening our foreign OE business by increasing product competitiveness and creating ripple effects towards the domestic market.

2007 will be a productive year for Kumho Tires' global management and a milestone in the company's history towards becoming 'the top five tire company in 2015'

### **Kumho Tires will become a "beautiful company"®**

Kumho Tires will become a "a company that does nothing to warrant criticism and keeps its promises; a strong, trusted company that performs all of its social responsibilities and contributes to the community as a corporate citizen."

We will carry out, one by one, our goals towards becoming a "beautiful" company, which include cooperative management with our partner companies, supporting diverse culture and arts activities, establishing a beautiful labor and management culture, and advocating environmentally-safe management practices.

Kumho Tires would like to thank once again our customers, foreign and domestic shareholders, and partners, all of whom have shown so much interest and care in our company. To return the support, we promise to continue our performance as a global corporation that opens up a better future, because you are the beautiful owners of our beautiful company.

We wish our customers, shareholders, and partners all a very happy new year, the best of health and happiness in your families, and hope that all you wish may come true.



Oh, Sae-chul  
President & CEO

## 2006 Overview

**Apr. 11**

**Release of XRP - the first run flat tire in Korea**

Kumho Tires released the first run flat tire in Korea, a new concept of tire that is designed to resist the effects of deflation and enable the vehicle to be driven even when it is punctured. The XRP(eXtended Runflat Performance) tire is a product for premium vehicles and has tremendously enhanced the driving comfort to conventional run-flat tires.

**May 18**

**Established new plant in ChangChun, China**

In China's ChangChun city located in Jilin province, Kumho Tires decided to build a tire plant with an annual capacity of 3.15 million units and held a groundbreaking ceremony last May. The ChangChun plant is the company's third plant in China; it will mainly produce OE tires for global automakers; especially UHP tires.

**Jun. 13**

**Awarded the Minister of Commerce, Industry, and Energy's Grand Prize for National Environmental Management**

In a tight competition with 14 other companies, Kumho Tires Gokseong plant was awarded the Minister's Award in Environmental Systems in the 2006 National Environmental Management Awards hosted jointly by the Ministry of Commerce, Industry, and Energy and Ministry of Environment. June 20 Racing Team won 3rd Place at 24 Hours of Le Mans.

**July. 4**

**Completed construction of plant in Tianjin, China**

Kumho Tires began initial production at its Tianjin plant in China last July. Built in the Tianjin Economic Technology Development Zone, the plant aims for annual production of 5.25 million units of UHP tires, focusing on sales in China and the overseas OE market.

**Jun. 20**

**3<sup>rd</sup> Place at 24 Hours of Le Mans P2 Class**

Partnering with the Miracle Motor Sports Team, Kumho Tires participated at the famous 24 Hours of Le Mans sports car race, one of the three largest motor sports events in the world. The team came in third place in the P2 class category out of 12. The Kumho Tires team, the only Korean team to participate in the event, was selected as one of 50 who were given the night to participate in the event. The team reported an outstanding record, becoming a prize-winner in only the second year of its participation.

**Apr. 11**



**May 18**



**Jun. 20**



**July. 4**





**Aug. 20**

**Winner of Super GT Round 6 in Japan**

Participating with the Toyota Cerumo team in the Super GT300, Japan's top racing event, Kumho Tires achieved first place in both the preliminary and finals of the sixth round (four car, 1,000-kilometer) of the Super GT series.

**Sept. 15**

**Established research and development center in China (KCTC)**

In September, 2006 Kumho Tires invested about \$36 million to establish a research and development center (Tianjin Economic technological Development Area) TEDA. The Kumho China Technical Center (KCTC) is equipped with the finest facilities in the industry to conduct performance test, product evaluation tests, and chemical analysis tests required for state-of-the-art tire research and development. Research workforce at this institute is continuously being expanded in numbers.

**Oct. 23**

**Developed world's first 32-inch SUV-purpose tire**

Kumho Tires developed the world's first super-large sports utility vehicle (SUV) tire, measuring 32 inches in rim diameter. This product maintains the height of the tire while expanding on the wheel's diameter and going slimmer on the thickness of the rubber layer. This maximizes ground connection when traveling at high speeds, thus enhancing safety.

**Oct. 25**

**Groundbreaking for tire production plant in Vietnam**

Kumho Tires held a groundbreaking ceremony for a plant in Binh Duong Province, Vietnam, last December. The facility will be able to produce 3.15 million units annually once it is completed in the first half of 2008. The UHP tires manufactured at this plant will be sold in Vietnam as well as other Asian countries, the Americas, and Europe.

**Nov. 27**

**Developed world's first environment friendly Lyocell-based tires**

Kumho Tires developed new products which incorporate a new environmentally friendly material known as Lyocell, a global first. Used in the production of tire cord for ultra-high performance (UHP) products, Lyocell can minimize environmentally hazardous materials produced during the manufacturing process. Beginning with UHP tires exported to Europe, Kumho Tires plans to steadily increase application of Lyocell cords to other tires in mass production.



Oct. 23

**Dec. 28**

**Completed construction of Chinese sales corporation**

Kumho Tires established a sales subsidiary in Shanghai to launch domestic sales in China. This comprehensive sales subsidiary will manage the tires produced at the Nanjing plant, Tianjin plant, and ChangChun plant (scheduled for completion in 2008) and secure a more efficient sales structure.

**Aug. 20**



**Sept. 15**



**Oct. 25**



**Dec. 28**



## Vision & Strategy

To be the “Global Top 5 Tire Company”





In 2005, Kumho Tires set a vision to become the “global top five tire company” and planted the seeds for aggressive management. During the past year, those seeds have sprouted, grown, and borne fruit, resulting in a joyful harvest. We have established a new construction and local research center in China, and broke ground for plant construction in Vietnam. In addition, we are swiftly releasing next-generation tires based on new technology that is being eyed by the world, and achieving outstanding performance at famous motor sports competitions.

The reason Kumho Tires concentrates all capacity on aggressive management is because it wishes to rewrite the history of the global tire industry with Kumho Tires’ name in the lead by building substance internally and gaining a firm position in the global market.

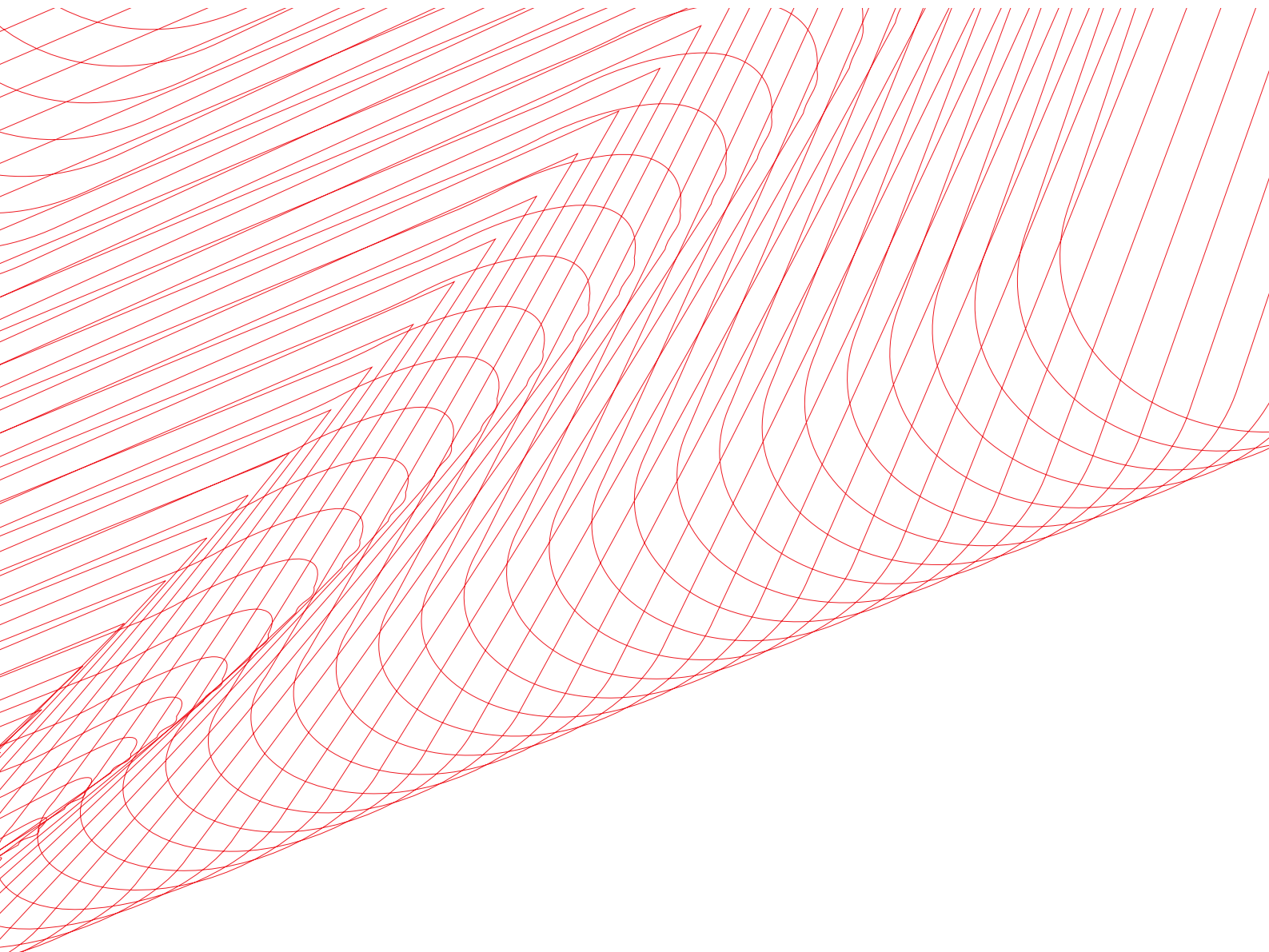
#### “Global Top 5 Tire Company”

Kumho Tires has taken strong roots in the global market and is preparing for leaping to the top. The world is watching every move we make with interest. In order to visualize Kumho Tires in the context of the world and realize the world through Kumho Tires, you must have the countenance to become a global leader.

## Ethical management

**Ethical management is a barometer that reads  
a company's dignity.**





Ethical management is one of the primary factors that can measure a company's future. The global corporate environment is moving towards an "ethics round". Companies that do not have ethical management will be ostracized and not even given the opportunity to compete in the global market.

Kumho Tires' efforts to become a beautiful company also begins by executing ethical management. In 2002, we formed a task force team that manages our ethical management system and announced a detailed ethics guideline, introducing ethical management into our management policy as a priority. In 2006, we published the "Ethical Management Guidebook" to share the significance of ethical management and the obstacles we faced during the process.

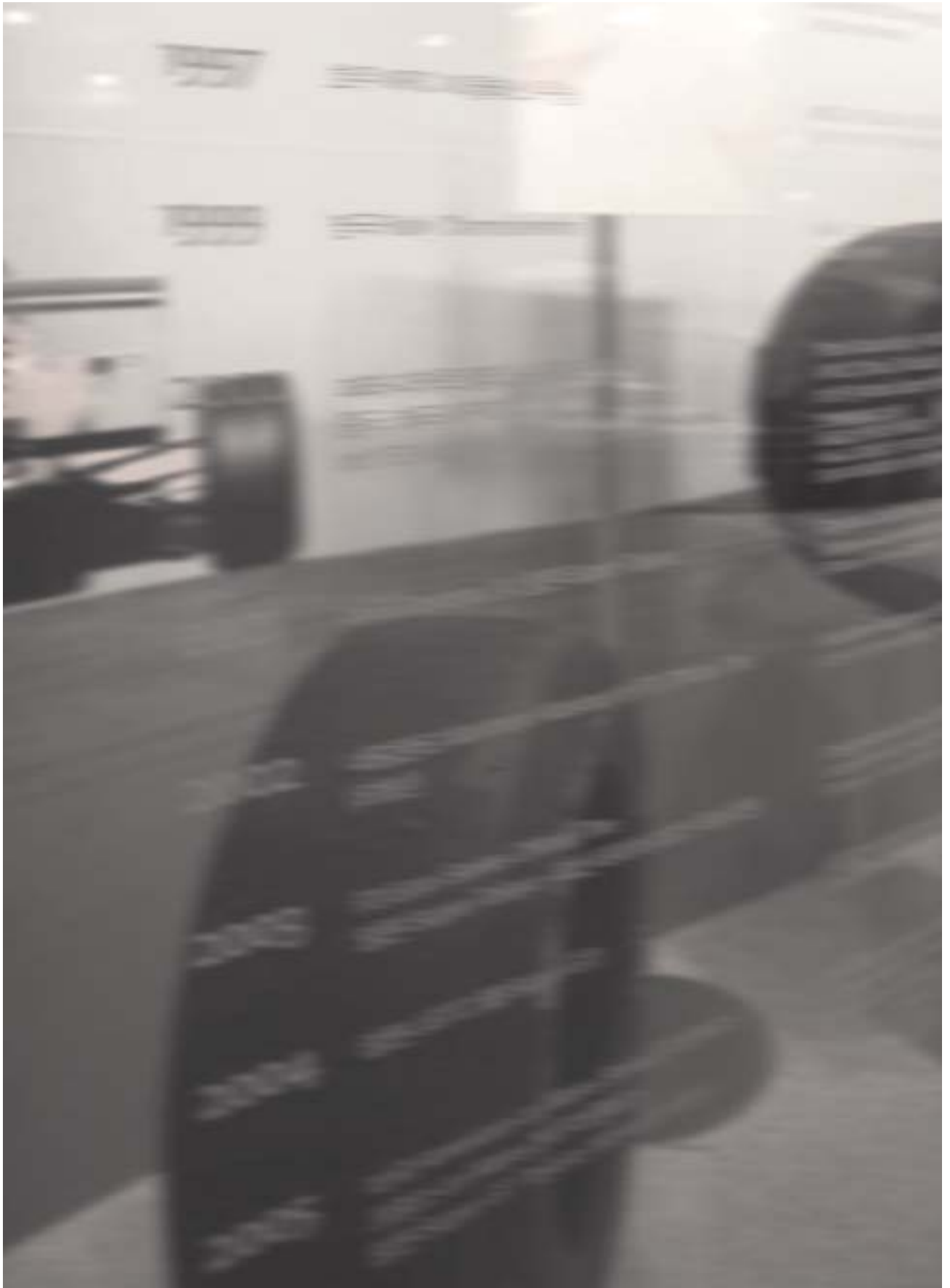
Building trust through open management, logical decision-making procedures, increasing profits through high value-added products, and developing future technology through R&D investment... Kumho Tires' transparent and ethical management is a leading power to boost its corporate value.

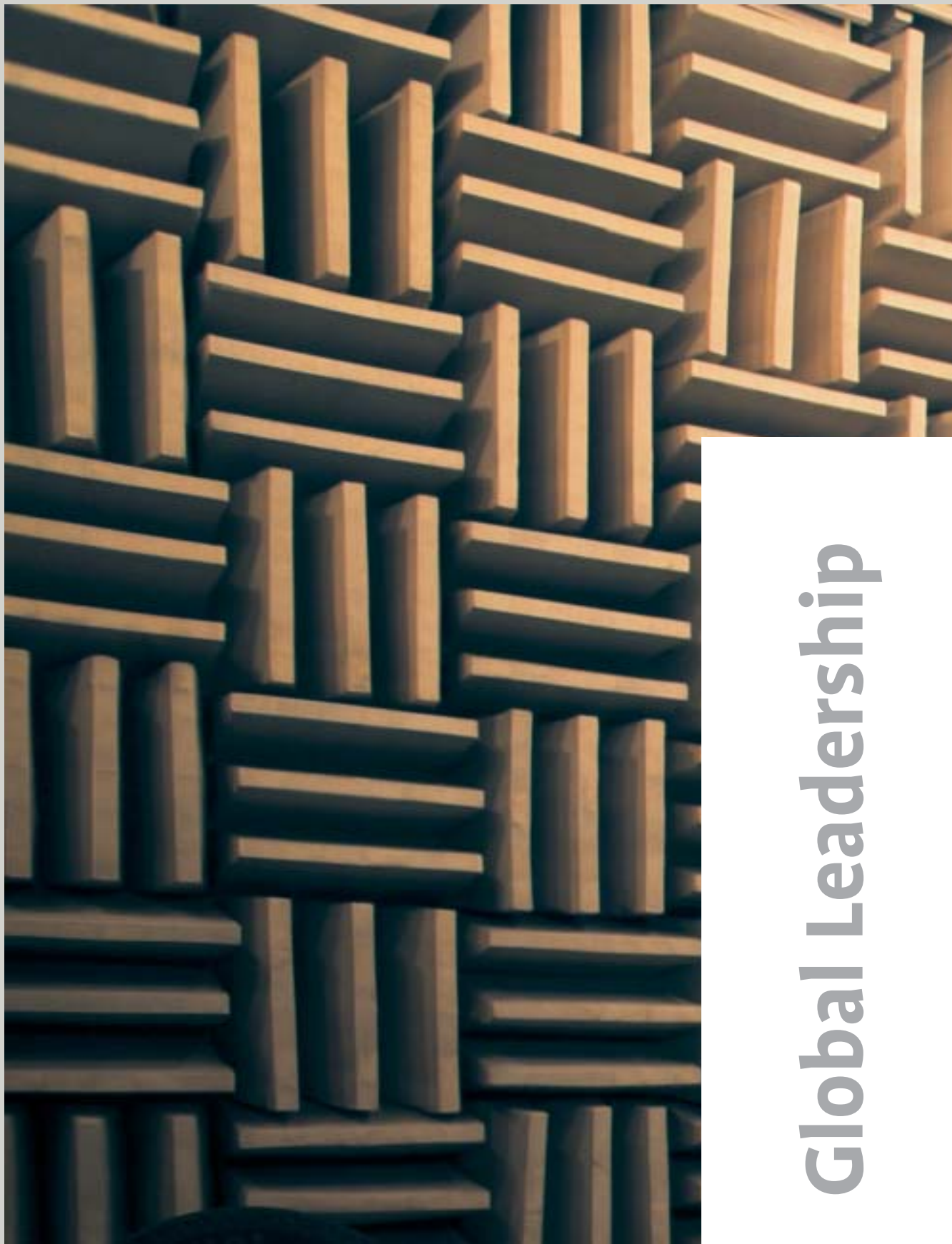
Dreams become technology

A step closer to the world's eye-level

Kumho Tires prepares all that you want.

# GROWING PARTNER





# Global Leadership



## Kumho Tires approaches the world with energetic footsteps



To achieve the vision of becoming one of the top 5 global companies, Kumho Tires is strengthening investment in overseas plant construction and building a global production network. Kumho Tires currently operates 7 foreign sales corporations and 14 branch offices, exporting tires to about 180 countries around the world.

### Foundation for overseas market expansion, Increase in role of Chinese market

China is already a new market that has the eyes and ears of the world. Kumho Tires already has a sales network of more than 10,000 sales outlets, occupying about 15 percent of the Chinese tire market. In addition to a plant in Nanjing, another was erected in Tianjin in July last year- the largest trade port of northern China. When the ChangChun plant and Nanjing TBR plant are all complete, Kumho Tires will be able to produce 25 million units a year in just China alone. This will not only facilitate the local market, but provide the company with a more stable foundation when entering the global stage.

### Overseas R&D network to enhance global perspective

The foremost requirement of a global company is to develop products that are fit for the local market and are wanted by local consumers. Kumho Tires established the research institutes in the United States (KATC) and Europe (KETC), and finally China (KCTC) last year, strengthening global R&D networks. By providing the best technology for top-quality tires that satisfy the tastes of the world, Kumho Tires increases its brand value.

### A tire selected by the world, strengthening overseas OE business

Kumho Tires is increasing brand awareness by strengthening its overseas OE (Original equipment) business. As a result, the company provides tires for Daimler Chrysler's 2007 Sebring sedans and new cars made by the Benz. The quality and excellence of Kumho Tires products have already been verified in Europe, where OE-purpose tires are being provided for Volkswagen. Kumho Tires decided to strengthen overseas OE business with 2006 as a pivot point and promote the name of KUMHO to the world.





# Tire Technology

## We will become the standard in global tire technology



Kumho Tires' technological goal is the quality level of the big three global tire makers. Kumho Tires, which was the first company to introduce supercom, develops racing tires, UHP tires, run flat tires, aroma tires, colored smoke tires, and even aviation tires that were considered the realm of developed makers. All of this was achieved with our own technology and now we confidently challenge domestic and foreign technology.

### Ultra High Performance Tires- a technology eyed by the world

UHP(Ultra High Performance) tires are used for high-quality, high-output automobiles. Kumho Tires unique technology enhanced tire performance by changing the rubber and wheel, therefore raising the standard for safety when driving at high speeds or ability to turn or break when traveling at high speeds. UHP sales continuously increased. In 2001, it made up only 9.9 percent of sales, but in 2006, the production M/S was up to 18.2 percent. More than 70 percent of UHP tires are exported to North American and European markets.

### The next-generation marathoner, Run-Flat tire

Kumho Tires introduced the first run-flat tire in Korea, which can run up to 80 kilometers per second even when it is punctured. Even when there is no air pressure within the tire, the tire minimizes altered energy and optimizes heat dispersion to maintain safety and driving comfort. The run-flat tire was extremely successful. In 2006, the total number of exports was five times that of the entire number of exports for the past three years. Until 2010, the run-flat tire replacement market alone will amount to 12 million, therefore Kumho Tires' great performance is expected.

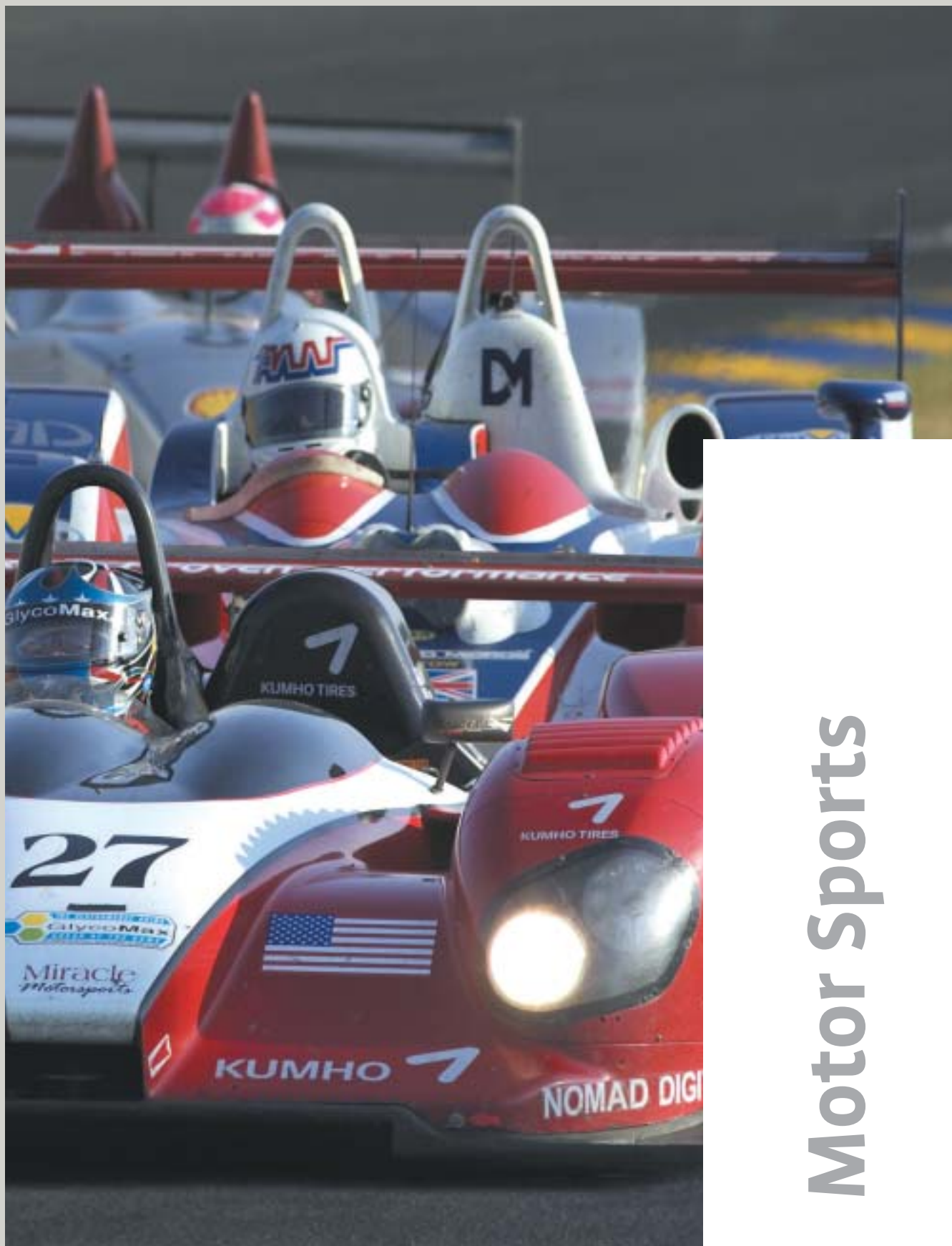
### X-Speed for extreme drivers

This tire, which is exclusively for high-speed driving, is appropriate for sports cars that can run up to 360 km/h. The tire requires high levels of technology, because it must maintain contact with the ground at high speeds but minimize heat generation and maximize heat protection. Currently, only a few global tire makers produce these tires, such as Michelin, but the only tires that can run up to 360 kilometers per hour are Germany's Continental and Kumho Tires' X-Speed. Since high-speed tires account for 16 percent of the entire tire market, and this product is expected to be well-received in the European market.

### My first choice lasts forever

According to a survey conducted by the largest online U.S. tire sales company Tire Rack, Kumho Tires ranked No. 1 out of 200 tire brands on the tire that people wanted to buy again. Also, in a consumer satisfaction survey on OE tires in Britain, conducted by the consumer research firm J.D. Power and Associates, Kumho Tires ranked second place. Kumho Tires' prominent performance in tire preference for both the first pick and the second choice proves that Kumho Tires' technology is being acknowledged in the global market.





# Motor Sports



## Kumho Tires' Destiny is to sprint a head of the world



"Kumho Tire and our team understand each other perfectly and have confirmed tremendous technological development. We are happy to be able to return our thanks," the head driver of the winner of the Super GT said. The Super GT is the most famous racing event in Japan. In 2000, Kumho Tires invested 5 billion won and developed F3 tires, which was only the beginning of what the company plans to do in the motor sports sector.

### Where the best tires compete against the best

Motor sports is an arena of technology and an exhibition place where carmakers and tire makers from around the world are given the opportunity to exhibit the peaks of their technology. It is also utilized as a marketing stage for the auto-related industry. Kumho Tires beat many renowned tire companies and was designated as the official tire for top prestigious international competitions such as the BP Ultimate Masters of F3 and Formula 3 Euro Series. Kumho Tires also participated in summit racing games such as the 24-hour Le Mans and Super GT, competing with global tire brands and achieving outstanding performance.

### Another venue to confirm Kumho Tires' technology

As Kumho Tires' technology begin shining through motor sports, the demand for UHP tires in the United States and Europe begin to increase, with the trend moving towards a global scale. By actively participating in international motor sports, Kumho Tires was able to flaunt its technology to the world and utilize data obtained from the events to develop and supply better products.

### Accelerating development for F1 tires, the peak of motor sports

Kumho Tires' ultimate goal is to develop and supply tires for the F1, the peak of motor sports. Currently, only Bridgestone and Michelin, respectively the first and second largest tire companies in the world, are providing F1 tires. This makes it a natural goal for Kumho Tires, which seeks to become a top global brand.



A shoulder to lean on...

A warm hand to hold on to...

Kumho Tires seeks that bigger smile on your face

# GROWING HAPPINESS





## 36.5 , the body temperature of Kumho Tires, the beautiful company

After being named the “beautiful company” in February 2006, Kumho Tires’ social contribution activities have donned bigger wings. Kumho Tires will take the initiative in keeping the world warm and transferring warm spirits to one another.

### **Customer safety comes first, Free tire inspection service**

Every year during holidays or vacation, you may see Kumho Tires’ service cars at rest areas on the expressway. We examine tire pressure, tire conditions, check to see if there is a spare tire, and other tire inspection services for free. After the inspection, a sticker with the inspection results are placed on the tires and the customers are told how to manage their tires.

### **“Sharing” is a power that makes human beings and society stronger**

The Hanwoorihoi group at Gwangju plant has been helping less fortunate people repair their houses for the past few years. Last year, the group repaired a house for a senior citizen living alone and an old orphanage playground. Funds that are collected from all employees every month since 2000 are used for charity. Kumho Tire employees also participate in diverse forms of volunteer work including helping farmers, delivering lunches for disabled people, and visiting child protection facilities to cook and clean. These activities go beyond the act of volunteering, and become a strong force in Kumho Tires’ own growth.

### **What Kumho Tires does best**

In October 2006, Kumho Tires held a motor sports experience event at the Yongin Speedway for children in welfare facilities. That day, 23 children experienced riding real racing cars and spent a fun day visiting the track and riding the cars. Previously, Kumho tires also invited local children to the ECSTA Time Trial game, which it was sponsoring. Kumho Tires plans to continuously host such hands-on events for youth to nurture their dreams and hopes.

**Social Contribution**



#### Developing tires to protect healthy lives of human beings

Kumho Tires is doing its best to develop environment-friendly tires. Some of the tires it has developed include low-weight tires that are lighter and burn less fuel, low fuel-efficiency tires, low-noise tires, and life-extension tires, which induce balanced abrasion in order to lengthen the tire's lifespan. Kumho Tires plans to continue developing new materials with low levels of pollutants and apply these materials to develop ultra low fuel-efficient tires for electric cars that will be used in the near future.

Kumho Tires received first place in environmental preservation in the 2006 Korea Social Contribution Awards. Kumho Tires received the ISO 14001 certification- a first for a domestic tire company- and will continue to develop new tires based on environment-friendly management principles.

#### Environmental Management Report Publication- To the beautiful future with nature

The annual environmental management report that Kumho Tires publishes contains case studies on the efforts and results of how the company incorporated environmentally-friendly factors into all procedures of production. The publication also introduces employee activities and campaigns such as 'Keep 1 company, 1 mountain, 1 stream clean'. Kumho Tires will continue to publish this report in an effort to become a model for environmentally friendly management.

#### Dreaming to be No. 1- Kumho Tires Environmental Science

Kumho Tires has a scientific system that evaluates the entire life cycle assessment with environmental set standards during each process of production. The environmental effects that are consumed and discharged in all procedures of product production are analyzed and evaluated from selecting raw materials and manufacturing to shipping and recycling. Thanks to the performance of this kind of environmental management activity, Kumho Tires' air pollution rate was less than the legal standard of 50 percent and water pollution rate was far less than the legal standard of 100 percent.

## Kumho Tires' faces come to resemble the smile of nature



## Environmental Management



## Kumho Tires Historical View



Founding History Zone



Corporate History Zone

## Kumho Tires' history is the pride of preparing for tomorrow

In March 2006, Kumho Tires became the first Korean tire company to open a tire history pavilion. Here, you can study the history of tire development, and see the quality and technology of the tires that are being so recognized for their excellence in overseas markets. The tire history pavilion was established based on research of case studies of the past three years, data collection, and records organizing, and corporate data.

# TECHNOLOGY INNOVATOR



Tire Structure and Aircraft Landing Gear Exhibition



Motor sports Zone



Future Zone

### From the past to the present, reflecting on 50 years of challenges

The Tire History museum, located in the main building of Kumho Tires' Gwangju plant is divided into six exhibition zones under the theme of "continuation of the trace of wheels." The 'Tire Zone' shows the major manufacturing process of the tire; the 'New Technology Zone,' 'Promotion zone' and 'Founding History Zone.' The motor sports zone, which exhibits the F3 machine racing car and tires used by the winners, is especially popular among visitors. Visitors to the pavilion can also press buttons to conduct core tests on tires, such as examining rubber friction, resistance elasticity, and turning resistance. Riding simulators offers an experience as if one is actually riding a vehicle.

### From the present to the future, thinking of 50 years of challenges to come

Along with the history pavilion, a separate exhibition hall in the lobby of the research institute portrays the present and future of Kumho tires. The concept of the exhibition is "technology innovator" and it displays Kumho Tires' technology standing at the top of the world through state-of-the-art core technology demonstrations. The prints of the tire are beautiful in that they are repetitive. For those who follow the prints, those are cairns for the future, and for those who leave their prints, those are pride. The history of Kumho Tires, which pursues continuous change, is communication between the past and the present and the prints that we will follow in the future. Those prints will help draw the world's finest prints for the future.

Precious memories collect with time

Looking back on the path we have walked, we think of where we must go

Kumho Tires is confident that tomorrow is brighter than today

# GROWING FUTURE



## FINANCIAL STATEMENTS

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Statement of Appropriations of Retained Earnings | Statement of Cash Flows

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Report on the Review of Internal Accounting Control System

Report on the Operations of the Internal Accounting Control System



## Report of Independent Auditors



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To the Shareholders and Board of Directors of  
KUMHO TIRE CO., INC.

We have audited the accompanying non-consolidated balance sheets of KUMHO TIRE CO., INC. (the "Company") as of December 31, 2006 and 2005, and the related non-consolidated statements of income, appropriations of retained earnings and cash flows for the years then ended, expressed in Korean won. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the Republic of Korea. 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 management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the non-consolidated financial statements referred to above present fairly, in all material respects, the financial position of KUMHO TIRE CO., INC. as of December 31, 2006 and 2005, and the results of its operations, the changes in its retained earnings and its cash flows for the years then ended in conformity with accounting principles generally accepted in the Republic of Korea.

Accounting principles and auditing standards and their application in practice vary among countries. The accompanying financial statements are not intended to present the financial position, results of operations and cash flows in conformity with accounting principles and practices generally accepted in countries and jurisdictions other than the Republic of Korea. In addition, the procedures and practices used in the Republic of Korea to audit such financial statements may differ from those generally accepted and applied in other countries. Accordingly, this report and the accompanying financial statements are for use by those who are informed about Korean accounting principles or auditing standards and their application in practice.

A handwritten signature in blue ink that reads "Samil Accounting Corporation".

Seoul, Korea  
March 2, 2007

This report is effective as of March 2, 2007, the audit report date. Certain subsequent events or circumstances, which may occur between the audit report date and the time of reading this report, could have a material impact on the accompanying non-consolidated financial statements and notes thereto. Accordingly, the readers of the audit report should understand that there is a possibility that the above audit report may have to be revised to reflect the impact of such subsequent events or circumstances, if any.

## Non-Consolidated Balance Sheets

December 31, 2006 and 2005

(in millions of Korean won)

	2006	2005
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	25,152	283,817
Short-term financial instruments (Note 3)	478	90,749
Short-term investment securities (Note 4)	2	9
Trade accounts and notes receivable, net (Notes 6, 14, 20 and 21)	310,594	263,304
Other accounts receivable (Notes 20 and 21)	24,434	18,968
Short-term loans receivable (Note 25)	208	298
Accrued income	375	768
Advance payments	1,303	2,417
Prepaid expenses	7,957	6,653
Derivative instruments (Note 27)	2,406	2,094
Inventories (Note 7)	214,348	160,553
Deferred income tax assets (Note 17)	5,432	2,653
<b>Total current assets</b>	<b>592,689</b>	<b>832,283</b>
Long-term financial instruments (Note 3)	39	52
Available-for-sale securities (Note 5)	742	-
Equity method investments (Note 8)	651,337	203,749
Guarantee deposits	24,049	24,365
Long-term prepaid expenses	1,703	2,225
Long-term loans receivable, net (Note 25)	32	41
Deferred income tax assets (Note 17)	12,599	5,283
Property, plant and equipment, net (Notes 9, 11 and 12)	1,014,439	1,019,366
Intangible assets, net (Note 10)	112,152	118,533
<b>Total assets</b>	<b>2,409,781</b>	<b>2,205,897</b>
<b>Liabilities and Shareholders' Equity</b>		
<b>Current liabilities</b>		
Trade accounts payable (Notes 20 and 21)	133,659	148,662
Short-term borrowings (Note 11)	233,909	270,193
Current maturities of debentures, net (Note 12)	199,702	-
Current maturities of long-term debts, net (Note 12)	135,531	283
Other accounts payable (Notes 20 and 21)	53,055	71,554
Accrued expenses (Notes 20 and 21)	36,273	29,022

## Non-Consolidated Balance Sheets

December 31, 2006 and 2005

(In millions of Korean won)

	2006	2005
Income tax payable (Note 17)	10,409	21,530
Advances received	6,535	4,358
Withholdings	7,354	9,882
Derivative instruments (Note 27)	6,746	6
<b>Total current liabilities</b>	<b>823,173</b>	<b>555,490</b>
Debentures, net (Note 12)	283,953	308,958
Long-term borrowings, net (Note 12)	254,449	235,228
Accrued severance benefits, net (Note 13)	114,210	115,214
Provision for warranty expense	24,071	24,071
<b>Total liabilities</b>	<b>1,499,856</b>	<b>1,238,961</b>
Commitments and contingencies (Note 14)		
Shareholders' equity		
Common stock (Note 1)	350,000	350,000
Additional paid-in capital	427,707	427,707
Retained earnings (Note 15)	154,909	195,939
Capital adjustments		
Gain on valuation of equity method investments (Note 8)	647	1,060
Loss on valuation of equity method investments (Note 8)	(23,338)	(7,770)
<b>Total shareholders' equity</b>	<b>909,925</b>	<b>966,936</b>
<b>Total liabilities and shareholders' equity</b>	<b>2,409,781</b>	<b>2,205,897</b>

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

## Non-Consolidated Statements of Income

Years Ended December 31, 2006 and 2005

(in millions of Korean won, except per share amounts)

	2006	2005
<b>Sales (Notes 16, 21 and 26)</b>	<b>1,813,794</b>	<b>1,763,125</b>
<b>Cost of sales (Notes 16, 21 and 23)</b>	<b>1,462,638</b>	<b>1,326,464</b>
Gross profit	351,156	436,661
<b>Selling and administrative expenses (Notes 22 and 23)</b>	<b>270,850</b>	<b>267,406</b>
Operating income	80,306	169,255
<b>Non-operating income</b>		
Interest income	17,903	3,841
Gain on valuation of equity method investments (Note 8)	1,282	4,894
Gain on foreign currency transactions	14,969	12,727
Gain on foreign currency translation	7,717	5,381
Gain on disposal of property, plant and equipment	1,493	3,206
Gain on derivatives transactions	572	3,423
Gain on valuation of derivatives (Note 27)	1,165	2,094
Others	530	358
	45,631	35,924
<b>Non-operating expenses</b>		
Interest expense	46,963	40,198
Loss on valuation of equity method investments (Note 8)	35,737	4,776
Loss on foreign currency transactions	9,697	14,373
Loss on foreign currency translation	2,295	1,022
Loss on disposal of short-term investment securities	2	88
Loss on disposal of property, plant and equipment	1,679	3,800
Loss on disposal of account receivables	17,282	13,454
Donations	2,326	2,424
Loss on disposal of inventories	408	332
Loss on derivatives transactions	572	1
Loss on valuation of derivatives (Note 27)	6,760	6
Others	114	608
	123,835	81,082
Ordinary income before income tax expense	2,102	124,097
Income tax expense (Note 17)	1,132	25,898
<b>Net income</b>	<b>970</b>	<b>98,199</b>
<b>Per share data (In Korean won)</b>		
Ordinary income per share (Note 19)	14	1,457
Earnings per share (Note 19)	14	1,457

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

## Non-Consolidated Statements of Appropriations of Retained Earnings

Years Ended December 31, 2006 and 2005 (Date of Appropriations : March 16, 2007 and March 17, 2006 for the years ended December 31, 2006 and 2005, respectively )

(in millions of Korean won)

	2006	2005
<b>Retained earnings before appropriations</b>		
Unappropriated retained earnings carried over from prior year	24,489	92,490
Net income	970	98,199
	25,459	190,689
<b>Appropriations of retained earnings</b>		
Legal reserve (Note 15)	2,100	4,200
Cash dividends (Note 18)		
(Dividends per share(in Korean won) :		
2006: 300(6%)		
2005: 600(12%)	21,000	42,000
Other reserves	-	120,000
	23,100	166,200
<b>Unappropriated retained earnings carried forward to subsequent year</b>	2,359	24,489

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



## Non-Consolidated Statements of Cash Flows

Years Ended December 31, 2006 and 2005

(in millions of Korean won)

	2006	2005
<b>Cash flows from operating activities</b>		
Net income	970	98,199
Adjustments to reconcile net income to net cash provided by operating activities		
Bad debt expense	3,164	1,809
Depreciation	131,279	118,166
Accrual of severance benefits	60,285	56,590
Amortization of intangible assets	7,182	7,146
Loss on disposal of property, plant and equipment	1,679	3,800
Loss on foreign currency translation	2,295	1,022
Loss on disposal of inventories	408	332
Interest expense (discounted present value)	1,351	13,568
Loss on disposal of short-term investment securities	2	88
Loss on valuation of equity method investments	35,737	4,776
Loss on valuation of derivatives	6,760	6
Gain on foreign currency translation	(7,716)	(5,381)
Gain on valuation of equity method investments	(1,282)	(4,894)
Gain on disposal of property, plant and equipment	(1,493)	(3,206)
Gain on valuation of derivatives	(1,165)	(2,094)
Others	(55)	(9)
	238,431	191,719
<b>Changes in operating assets and liabilities</b>		
Increase in trade accounts and notes receivable	(51,684)	(66,521)
Increase in other accounts receivable	(6,437)	(8,178)
Decrease(increase) in accrued income	393	(735)
Decrease(increase) in advance payments	1,114	(169)
Decrease(increase) in prepaid expenses	(1,302)	243
Decrease in derivative instruments assets	852	-
Increase in inventories	(54,204)	(44,030)
Increase in deferred income tax assets	(10,019)	(4,295)
Decrease in long-term other accounts receivable	-	6,506
Increase(decrease) in trade accounts payable	(14,400)	18,486
Increase in advances received	2,177	1,183
Increase(decrease) in withholdings	(2,526)	3,889
Decrease in other accounts payable	(18,387)	(22,348)

# Non-Consolidated Statement of Cash Flows

Year Ended December 31, 2006 and 2005

(In millions of Korean won)

	2006	2005
Increase(decrease) in accrued expenses	7,251	(19,334)
Increase(decrease) in income tax payable	(11,121)	6,349
Decrease in derivative instruments liabilities	(20)	(2,339)
Payment of severance benefits	(56,254)	(50,183)
Transfer of accrual of severance benefits	127	109
Deposits for severance benefit insurance	(5,162)	(29,911)
Increase in provision for warranty expense	-	1,329
	(219,602)	(209,949)
Net cash provided by operating activities	19,799	79,969
<b>Cash flows from investing activities</b>		
Collection of long-term loans receivable	64	64
Proceeds from short-term financial instruments	150,992	187,099
Proceeds from long-term financial instruments	27	55
Proceeds from short-term investment securities	33	1,058
Collection of short-term loans receivable	723	370
Dividends received from equity method investments	2,878	1,926
Decrease in guarantee deposits	5,025	7,587
Decrease in long-term prepaid expenses	581	883
Disposal of property, plant and equipment	10,675	14,753
Acquisition of short-term financial instruments	(60,721)	(277,254)
Acquisition of investment securities	(29)	(1,124)
Acquisition of long-term financial instruments	(14)	-
Acquisition of available for sale securities	(742)	-
Payment of guarantee deposits	(4,710)	(6,352)
Increase in long-term prepaid expenses	(59)	(1,995)
Acquisition of property, plant and equipment	(137,213)	(111,876)
Acquisition of intangible assets	(801)	(140)
Short-term loans granted	(633)	(377)
Acquisition of equity method investments	(500,977)	(98,279)
Net cash used in investing activities	(534,901)	(283,602)

## Non-Consolidated Statement of Cash Flows

Year Ended December 31, 2006 and 2005

(In millions of Korean won)

	2006	2005
<b>Cash flows from financing activities</b>		
Proceeds from short-term borrowings	-	186,589
Proceeds from long-term borrowings	177,654	260,626
Issuance of debentures	174,168	308,874
Issuance of common stock	-	277,707
Repayment of current maturities of long-term borrowings	(100)	(125,657)
Repayment of short-term borrowings	(36,010)	-
Repayment of long-term borrowings	(17,275)	(402,201)
Payment of dividends	(42,000)	(27,500)
Net cash provided by financing activities	256,437	478,438
Net increase(decrease) in cash and cash equivalents	(258,665)	274,805
<b>Cash and cash equivalents</b>		
Beginning of year	283,817	9,012
End of year	25,152	283,817

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

# Non-Consolidated Financial Statements

December 31, 2006 and 2005

## 1. The Company

KUMHO TIRE CO., INC. (the "Company") was incorporated on June 30, 2003, under the laws of the Republic of Korea to engage in manufacturing and selling tires. Kumho Industrial Co, Ltd. contributed and transferred its tire business to the Company on June 30, 2003.

The Company has its headquarters in Gwangju, operates manufacturing plants in various locations including Gwangju and Gokseong, and has several overseas affiliates and research centers.

The Company issued and listed 6.8 million shares of common stock (issue amount: 99,620 million) on February 17, 2005, on the Korea Exchange. The Company also issued and listed 22.4 million shares of Global Depository Shares, representing 11.2 million shares of common stock (issue amount: US\$160 million), on the London Stock Exchange on February 16, 2005. Furthermore, the Company issued additional four million shares of Global Depository Shares, representing two million shares of common stock, (issue amount: US\$29 million) on March 2, 2005, through the execution of stock purchase options granted to J.P. Morgan Securities Ltd.

The Company is authorized to issue 200 million shares with a par value per share of 5,000. As of December 31, 2006, the Company has an outstanding capital stock amounting to 350,000 million.

The Company's major shareholders and their respective percentage of ownership as of December 31, 2006, are as follows:

	Number of Shares Owned	Percentage of Ownership (%)
Korea Kumho Petrochemical Co., Ltd.	23,932,000	34.19
Cooper Tire & Rubber Company	7,500,000	10.71
Others	38,568,000	55.10
Total	70,000,000	100.0

# Non-Consolidated Financial Statements

December 31, 2006 and 2005

## 2. Summary of Significant Accounting Policies

The significant accounting policies followed by the Company in the preparation of its non-consolidated financial statements are summarized below:

### Basis of Financial Statement Presentation

The Company maintains its accounting records in Korean won and prepares statutory financial statements in the Korean language (Hangul) in conformity with accounting principles generally accepted in the Republic of Korea. Certain accounting principles applied by the Company that conform with financial accounting standards and accounting principles in the Republic of Korea may not conform with generally accepted accounting principles in other countries. Accordingly, these non-consolidated financial statements are intended for use by those who are informed about Korean accounting principles and practices. The accompanying financial statements have been condensed, restructured and translated into English from the Korean language non-consolidated financial statements.

### Accounting Estimates

The preparation of the non-consolidated financial statements requires management to make estimates and assumptions that affect amounts reported therein. Although these estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future, actual results may differ from those estimates.

### Application of the Statements of Korean Financial Accounting Standards

The Korean Accounting Standards Board has published a series of Statements of Korean Financial Accounting Standards (SKFAS), which will gradually replace the existing financial accounting standards established by the Korean Financial Supervisory Commission. As SKFAS Nos. 18 through 20 became applicable to the Company on January 1, 2006, the Company adopted these Standards in its financial statements covering periods beginning January 1, 2006.

The Company adopted early the Interpretations of SKFAS 06-2 'Accounting treatment of deferred income taxes related to investments in subsidiaries, equity method investees and shares in joint ventures' in the financial statements for the year ended December 31, 2006 (Note 17).

### Revenue Recognition

Revenues from sale of finished goods and merchandise are recognized upon delivery when the significant risks and rewards of ownership of the goods are transferred to the buyer.



#### Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts, notes and other accounts receivable based on historical collection experience and estimated collectibility of the receivables.

#### Investments in Securities

The Company accounts for equity and debt securities under the provisions of SKFAS No. 8, Investments in Securities. This statement requires investments in equity and debt securities to be classified into three categories: trading, available-for-sale and held-to-maturity.

Securities are initially carried at cost, including incidental expenses, with cost being determined using the gross average method. Debt securities, which the Company has the intent and ability to hold to maturity, are generally carried at cost, adjusted for the amortization of discounts or premiums. Premiums and discounts on debt securities are amortized over the term of the debt using the effective interest rate method. Trading and available-for-sale securities are carried at fair value, except for non-marketable securities classified as available-for-sale securities whose fair value may not be determined, which are carried at cost. Non-marketable debt securities are carried at a value using the present value of future cash flows, discounted at a reasonable interest rate determined considering the credit ratings by independent credit rating agencies.

Unrealized valuation gains or losses on trading securities are charged to current operations, and those resulting from available-for-sale securities are charged to capital adjustments, the accumulated amount of which shall be charged to current operations when the related securities are sold, or when an impairment loss on the securities is recognized. Impairment losses are recognized in the statement of income when the recoverable amounts are less than the acquisition cost of securities or adjusted cost of debt securities after the amortization of discounts or premiums.

#### Equity Method Investments

Investments in equity securities of companies, over which the Company exercises a control or significant influence, are recorded using the equity method of accounting. Under the equity method, the Company records changes in its proportionate ownership in the book value of the investee in current operations, as capital adjustments or as adjustments to retained earnings, depending on the nature of the underlying change in book value of the investee.

The Company discontinues the equity method of accounting for investments when the Company's share in the accumulated losses of the investees equals the costs of the investments, and until the subsequent cumulative changes in its proportionate net income of the investees equal its cumulative proportionate net losses not recognized during the periods when the equity method was suspended. Differences between the initial purchase price and the Company's initial proportionate ownership in the net book value of the investee are amortized over 20 years using the straight-line method, and the amortization is charged to current operations.

## Non-Consolidated Financial Statements

December 31, 2006 and 2005

In addition, proportionate share in the difference between fair value of the investee's identifiable assets (liabilities) and book value is amortized according to the investee's accounting for the assets and liabilities.

Unrealized profit included in inventories and property, plant and equipment from transaction between the Company and equity method investees is calculated based on gross margin by product and eliminated considering the percentage of ownership. However, unrealized profit arising from sales by the Company to equity method investees which are its consolidated subsidiaries is fully eliminated. Unrealized profit arising from sales between equity method investees is also eliminated considering the percentage of ownership.

Foreign currency financial statements of equity method investees are translated into Korean won using the exchange rates in effect as of the balance sheet date for assets and liabilities, and annual average exchange rates for income and expenses. Any resulting translation gain or loss is included in the capital adjustments account, a component of shareholders' equity.

In accordance with SKFAS No. 15, Equity Method, equity in earnings and losses of the investees are shown in the statement of income as gross amounts. Likewise, positive and negative capital adjustments are shown in the balance sheet in gross amounts.

### Sale or Discount of Accounts Receivable

The Company sells or discounts certain accounts or notes receivable to financial institutions, and accounts for the transactions as sales of the receivables if the control over the receivables is substantially transferred to the buyers. The losses from the sale of the receivables are charged to current operations as incurred.

### Inventories

The quantity of inventory on hand is verified using the perpetual inventory system, which continuously updates the quantity of the inventory during the period, and by physical count as of the balance sheet date. Inventories are stated at the lower of cost or market, with cost being determined using the weighted-average method for merchandises, finished goods, the moving-average method for raw materials and supplies, and the specific identification method for material-in-transit and merchandise-in-transit.

If the net realizable value of inventory is less than its cost, a contra inventory account representing the valuation loss, is presented to reduce the inventory to its net realizable value. The said valuation loss is recorded as cost of sales. If, however, the circumstances which caused the valuation loss ceased to exist, causing the market value to rise above the carrying amount, the valuation loss is reversed limited to the original carrying amount before valuation. The said reversal is a deduction from cost of sales.

#### Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows:

	Estimated Useful Lives
Buildings	30-40 years
Structures	15-20 years
Machinery and equipment	8 years
Vehicles	4 years
Tools	4 years
Furniture and fixtures	4 years

Routine maintenance and repairs are charged to expense as incurred. Expenditures, which enhance the value or materially extend the useful life of the related assets, are capitalized as additions to property, plant and equipment.

The Company recognizes an impairment loss when the carrying amount of an asset exceeds its recoverable amount. The impairment loss is recognized in the income statement and is deducted from the acquisition cost of the impaired asset. If there is a subsequent recovery from the impairment, a reversal of the previous write-down is made limited to the amount of the original cost. The reversal amount of the previously recognized loss is credited to current operations as a gain.

#### Intangible Assets

Intangible assets, comprising industrial property rights and goodwill, are recorded at cost and amortized using the straight-line method over the following estimated useful lives.

	Estimated Useful Lives
Goodwill	20 years
Industrial property rights	5 years

## Non-Consolidated Financial Statements

December 31, 2006 and 2005

Research costs are charged to operations as incurred. Costs incurred for new products or technologies, which can be clearly defined and measured and which have probable future economic benefits, are accounted for as development costs and are capitalized. Other development costs are recognized in the period incurred as normal development expenses.

Capitalized development costs are amortized over their economic lives not to exceed 20 years using the straight-line method. If collectible development costs are valued at less than the book value and such difference is material, then the difference should be subtracted directly from the book value and reclassified as collectable development costs. The difference between the book value and the collectible development costs are accounted for as loss on valuation of development costs and expensed in the year incurred.

As of the date of spin-off, the Company has recognized goodwill for the purchase amount exceeding the shares of the purchasing company whose fair values of assets and liabilities are identifiable. Such goodwill is amortized over its economic lives not to exceed 20 years using the straight line method. Goodwill recognized at the date of the acquisition will be valued every year based on its recoverability. If recoverable amounts are less than its book value and if such difference is material, then the difference is accounted for as loss on valuation of goodwill and expensed in the year of incurrence.

### Premiums and Discounts on Debentures

The Company accounts for the difference between the face amount and issued amount of debentures after deducting other expenses and commission related to the issuance of debentures as premiums or discounts. Premiums or discounts on debentures are amortized using the effective interest rate method over the term of the debentures and the resulting amortization is recorded as interest expense.

### Present Value Discount Account

The Company records incidental expenses arising from syndicated loans as present value discount account. Such present value discount account is amortized using the effective interest rate method over the due period as interest expenses.

### Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated into Korean won at 929.6: US\$1, the exchange rate in effect at December 31, 2006 ( 1,013: US\$1 as of December 31, 2005), and resulting translation gains or losses are recognized in current operations.

#### Accrued Severance Benefits

Employees and directors with at least one year of service are entitled to receive a lump-sum payment upon termination of their employment with the Company based on their length of service and rate of pay at the time of termination. Accrued severance benefits represent the amount payable assuming all eligible employees and directors were to terminate their employment as of the balance sheet date.

The Company has made deposits to the National Pension Fund in accordance with the National Pension Funds Law. The use of the deposit is restricted to the payment of severance benefits. Accordingly, accrued severance benefits in the accompanying non-consolidated balance sheet are presented net of this deposit.

Accrued severance benefits are funded approximately 53.4% (2005: 52.0%) as of December 31, 2006, through a group severance insurance plan and are presented as deduction from accrued severance benefits. The Company paid severance benefits amounting to 56,254 million (2005: 50,183 million) for the year ended December 31, 2006.

#### Impairment Loss

Assets other than marketable securities, investment securities, restructured receivables and assets with present value discounts are stated at cost. However, declines in fair value arising from obsolescence, physical damage or a sharp decline in the market value are recorded as impairment losses and included in current operations.

#### Warranty Reserve

The Company accrued warranty reserves for the estimated costs of future repairs and recalls, based on the experience and the expectation of future repairs. Estimated costs of product warranties amounting to 24,071 million are charged to operations for the year ended December 31, 2006 and 2005. Warranty reserve is recorded as long-term liabilities since the warranty expense is to be incurred over several years and the incurrence period of which cannot be readily and reasonably determined.

#### Income Taxes

The Company recognizes deferred income taxes for anticipated future tax consequences resulting from temporary differences between amounts reported for financial reporting and income tax purposes. Deferred income tax assets and liabilities are computed on such temporary differences by applying enacted statutory tax rates applicable to the years when such differences are expected to be reversed. Deferred income tax assets are recognized to the extent that it is almost certain that such deferred income tax assets will be realized. The total income tax provision includes current tax expenses under applicable tax regulations and the change in the balance of deferred income tax assets and liabilities.

## Non-Consolidated Financial Statements

December 31, 2006 and 2005

In accordance with SKFAS No. 16, Deferred Income Tax, which became effective on January 1, 2006, the Company classified deferred tax assets and liabilities into current and non-current, and within each classification, amounts for deferred tax assets and liabilities are offset against each other and presented as net amount. Deferred tax effects applicable to items in the shareholders' equity are directly reflected in the shareholders' equity account.

### Derivative financial instruments

All derivative instruments are accounted for at fair value with the resulting valuation gain or loss recorded as an asset or liability. If the derivative instrument is not designated as a hedging instrument, the gain or loss is recognized in earnings in the period of change. Fair value hedge accounting is applied to a derivative instrument with the purpose of hedging the exposure to changes in the fair value of an asset or a liability or a firm commitment that is attributable to a particular risk.

The gain or loss, both on the hedging derivative instrument and on the hedged item attributable to the hedged risk, is reflected in current operations. Cash flow hedge accounting is applied to a derivative instrument with the purpose of hedging the exposure to variability in expected future cash flows of an asset or a liability or a forecasted transaction that is attributable to a particular risk. The effective portion of the gain or loss on a derivative instrument designated as a cash flow hedge is recorded as a capital adjustment and the ineffective portion is recorded in current operations. The effective portion of the gain or loss recorded as a capital adjustment is reclassified to current operations in the same period during which the hedged forecasted transaction affects earnings.

### 3. Restricted Bank Deposits

Restricted bank deposits as of December 31, 2006 and 2005, consist of the following:

	(in millions of Korean won)	
	2006	2005
Short-term financial instruments	478	525
Long-term financial instruments	39	25
	517	550

### 4. Short-term investment securities

All short-term investment securities as of December 31, 2006 and 2005, are in the form of government and public bonds.



#### 5. Available-for-sale securities

Available-for-sale securities as of December 31, 2006 and 2005, consist of the following:

(in millions of Korean won)

	Percentage of Ownership (%)	Acquisition Cost		Book Value <sup>1</sup>		Net Asset Value <sup>2</sup>	
		2006	2005	2006	2005	2006	2005
RUBBERNETWORK.COM	5.28	742	?	742	?	245	?

<sup>1</sup> Non-marketable equity security whose fair value could not be reliably measured due to the lack of historical information on the future cash flows of investee, is stated at its acquisition cost.

<sup>2</sup> Net asset value is stated at the net asset value of the investee based on the most recent financial statement made available to investors.

#### 6. Trade Accounts and Notes Receivable

Receivables as of December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

	2006	2005
Trade accounts receivable and notes receivable	328,375	277,921
Less : Allowance for doubtful accounts	(17,781)	(14,617)
	310,594	263,304

#### 7. Inventories

Inventories as of December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

	2006	2005
Finished goods	121,662	89,773
Merchandises	386	259
Work in process	15,441	12,737

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(in millions of Korean won)		
	2006	2005
Raw materials	9,395	8,844
Supplies	2,515	1,602
Materials-in-transit	60,494	44,956
Merchandise-in-transit	4,455	2,382
	214,348	160,553

### 8. Equity Method Investments

Details of the equity method investments as of December 31, 2006 and 2005, are as follows:

(in millions of Korean won)							
	Percentage of Ownership (%)	Acquisition Cost		Book Value <sup>1</sup>		Net Asset Value <sup>2</sup>	
	2006.12.31	2006	2005	2006	2005	2006	2005
Nanjing Kumho Tire <sup>2</sup>	-	-	110,621	-	106,022	-	69,275
Kumho Tire U.S.A.	100.00	-	-	-	-	(35,311)	1,717
Kumho Tyre U.K.	100.00	-	-	-	133	(4,075)	380
Kumho Tire Europe	100.00	-	-	-	556	(12,226)	(3,437)
Kumho Tire Japan	100.00	1,293	1,293	1,445	854	424	496
Kumho Tire Canada	100.00	-	-	1,012	422	760	733
Kumho Tyre Australia	100.00	-	-	-	501	64	1,189
Kumho Tire HongKong. <sup>2</sup>	100.00	183,641	83,633	136,532	81,396	144,121	84,046
Kumho PFV1 Inc.	80.00	15,200	15,200	12,348	13,865	12,348	13,865
Daewoo Engineering & Construction <sup>3</sup>	5.61	500,000	-	500,000	-	155,608	-
Total		700,134	210,747	651,337	203,749	261,713	168,264

<sup>1</sup> The equity method of accounting is applied based on the affiliates' most recent available financial statements.

<sup>2</sup> The Company transferred all of its shares in Nanjing Kumho Tire to Kumho Tire HongKong as a contribution in kind in 2006.

<sup>3</sup> As of December 31, 2006, the fair value of equity investments in Daewoo Engineering & Construction amounts to 63,637 million. Since the total ownership including indirect investment through affiliated company is more than 20%, the equity method of accounting was applied on this investee.

Details of equity method investments for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

	Beginning Balance	Acquisition (Disposition)	Valuation Gain or Loss	Increase(Decrease) in Capital Adjustments	Dividend	Ending Balance
Nanjing Kumho Tire	106,022	(99,030)	(1,057)	(3,057)	(2,878)	-
Kumho Tire U.S.A.	-	-	-	-	-	-
Kumho Tyre U.K.	133	-	(133)	-	-	-
Kumho Tire Europe	556	-	(556)	-	-	-
Kumho Tire Japan	854	-	630	(39)	-	1,445
Kumho Tire Canada	422	-	652	(62)	-	1,012
Kumho Tyre Australia	501	-	(501)	-	-	-
Kumho Tire HongKong	81,396	100,007	(31,973)	(12,898)	-	136,532
Kumho PFV1 Inc.	13,865	-	(1,517)	-	-	12,348
Daewoo Engineering & Construction	-	500,000	-	-	-	500,000
2006	203,749	500,977	(34,455)	(16,056)	(2,878)	651,337
2005	106,327	98,279	118	952	(1,927)	203,749

The accumulated unamortized differences between the purchase price and the underlying proportionate net book value of equity investments are amortized over their economic lives not to exceed 20 years using the straight-line method, along with changes in such amounts for the years ended December 31, 2006 and 2005, as follows:

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(in millions of Korean won)

	Beginning Balance	Increase	Amortization	Increase (Decrease) due to investments in kind	Ending Balance
Nanjing Kumho Tire	44,884	-	(1,251)	(43,633)	-
Kumho Tire U.S.A.	22,190	-	(1,268)	-	20,922
Kumho Tyre U.K.	288	-	(16)	-	272
Kumho Tire Europe	12,848	-	(734)	-	12,114
Kumho Tire Japan	915	-	(52)	-	863
Kumho Tire Canada	1,536	-	(88)	-	1,448
Kumho Tyre Australia	(14)	-	1	-	(13)
Kumho Tire HongKong	-	-	(1,251)	43,633	42,382
Kumho PFV1 Inc.	-	-	-	-	-
Daewoo Engineering & Construction	-	344,392	-	-	344,392
2006	82,647	344,392	(4,659)	-	422,380
2005	87,384	-	(4,737)	-	82,647

For the year ended December 31, 2006, unrealized profit amounting to 40,058 million (2005: 46,719 million) was eliminated as a result of the valuation of equity method investments.

The Company suspended the equity method of accounting when the Company's share of losses exceeded the carrying value of its investment. The Company's unrecorded share of loss of the equity method investee is as follows:

(in millions of Korean won)

	January 1, 2006	Increase	December 31, 2006 <sup>1</sup>
Kumho Tire U.S.A.	6,972	33,932	40,904
Kumho Tire U.K.	-	3,972	3,972
Kumho Tire Europe	-	4,812	4,812
Kumho Tyre Australia	-	2,094	2,094
Total	6,972	44,810	51,782

<sup>1</sup> Capital adjustments from gain and loss on valuation of equity method investments are included in the unrecorded share in the losses of investees.

Capital adjustments in shareholders' equity resulting from equity method investments as of and for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

2006				
	Beginning Balance	Increase (Decrease)	Disposal (Realized)	Ending Balance
Nanjing Kumho Tire	(7,455)	(3,057)	10,512	-
Kumho Tire U.S.A.	-	-	-	-
Kumho Tyre U.K.	(48)	-	-	(48)
Kumho Tire Europe	647	-	-	647
Kumho Tire Japan <sup>1</sup>	(176)	19	-	(157)
Kumho Tire Canada <sup>1</sup>	-	(45)	-	(45)
Kumho Tyre Australia	(91)	-	-	(91)
Kumho Tire HongKong	413	(23,410)	-	(22,957)
Kumho PFV1 Inc.	-	-	-	-
Daewoo Engineering & Construction	-	-	-	-
Increase resulting from equity method	1,060	(413)	-	647
Decrease resulting from equity method	(7,770)	(26,080)	10,512	(23,338)

<sup>1</sup> This amount is net of deferred income tax effect of the capital adjustments from gain and loss on valuation of equity method investments.

(in millions of Korean won)

2005				
	Beginning Balance	Increase (Decrease)	Disposal (Realized)	Ending Balance
Nanjing Kumho Tire	(7,174)	(281)	-	(7,455)
Kumho Tire U.S.A.	-	-	-	-
Kumho Tyre U.K.	6	(54)	-	(48)

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2005				
	Beginning Balance	Increase (Decrease)	Disposal (Realized)	Ending Balance
Kumho Tire Europe	(394)	1,041	-	647
Kumho Tire Japan1	(99)	(77)	-	(176)
Kumho Tire Canada1	(6)	6	-	-
Kumho Tyre Australia	5	(96)	-	(91)
Increase resulting from equity method	11	1,049	-	1,060
Decrease resulting from equity method	(7,673)	(97)	-	(7,770)

### 9. Property, Plant and Equipment

Changes in property, plant and equipment for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

2006						
	Land	Buildings	Machinery and equipment	Construction-in-progress	Others	Total
Beginning balances	153,502	248,897	462,675	46,693	107,599	1,019,366
Acquisition	-	-	-	131,756	5,457	137,213
Transfer	7,870	18,789	53,557	(112,308)	32,092	-
Disposal	(2,700)	(2,141)	(3,713)	-	(2,307)	(10,861)
Depreciation	-	(7,350)	(82,175)	-	(41,754)	(131,279)
Ending Balance	158,672	258,195	430,344	66,141	101,087	1,014,439
Accumulated depreciation	-	(24,420)	(257,793)	-	(109,648)	(391,861)



(in millions of Korean won)

2005						
	Land	Buildings	Machinery and equipment	Construction-in-progress	Others	Total
Beginning balances	152,381	249,748	502,048	24,700	112,127	1,041,004
Acquisition	-	-	-	104,213	7,662	111,875
Transfer	4,815	7,572	46,399	(82,220)	23,434	-
Disposal	(3,694)	(1,358)	(8,409)	-	(1,886)	(15,347)
Depreciation	-	(7,065)	(77,363)	-	(33,738)	(118,166)
Ending Balance	153,502	248,897	462,675	46,693	107,599	1,019,366
Accumulated depreciation	-	(17,213)	(175,784)	-	(72,465)	(265,462)

As of December 31, 2006, the value of the Company's land, as determined by the local government in Korea for property tax assessment purposes, amounts to approximately 152,059 million.

As of December 31, 2006, substantial portions of the Company's land, buildings and machinery are pledged as collateral for long-term and short-term debt obligations of up to 273,600 million, US\$457 million and JPY2,532 million in aggregate (Notes 11 and 12). Property, plant and equipment are insured against fire up to 1,844,249 million with The Korea Development Bank as the beneficiary of the insured amount.

#### 10. Intangible Assets

Changes in intangible assets for the years ended December 31, 2006 and 2005, are as follows:

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2006			
	Goodwill	Industrial Property Rights	Total
Beginning balance	117,700	833	118,533
Acquisition	-	801	801
Amortization	(6,726)	(456)	(7,182)
Ending balance	110,974	1,178	112,152

(in millions of Korean won)

2005			
	Goodwill	Industrial Property Rights	Total
Beginning balance	124,426	1,114	125,540
Acquisition	-	140	140
Amortization	(6,726)	(421)	(7,147)
Ending balance	117,700	833	118,533

The Company has classified the amortization of intangible assets as selling and administrative expense for the years ended December 31, 2006 and 2005.

### 11. Short-Term Borrowings

Short-term borrowings as of December 31, 2006 and 2005, consist of the following:

(in millions of Korean won)

	Annual Interest Rate (%)		
	Dec. 31, 2006	2006	2005
Bank overdraft	5.59~6.02	59,278	-
Commercial papers issued	6.06	25,000	150,000
General term-loans including US\$ 17.846 million (2005: US\$ 16.313 million)	5.36~6.34	69,652	34,587

(in millions of Korean won)

	Annual Interest Rate (%)		
	Dec. 31, 2006	2006	2005
Usance of US\$ 86.035 million (2005: US\$ 84.507 million)	5.66	79,979	85,606
		233,909	270,193

The Company has bank overdraft agreements with The Korea Development Bank and other banks amounting to 74,200 million. Also substantial portions of the Company's property, plant and equipment are pledged as collateral for the borrowings above (Note 9).

#### 12. Long-Term Borrowings

Debentures as of December 31, 2006 and 2005, consist of the following:

(in millions of Korean won)

	Annual Interest Rate (%)		
	Dec. 31, 2006	2006	2005
Non-guaranteed debentures	4.76 ~ 5.53	485,000	310,000
Less: Discount on debentures		(1,345)	(1,042)
		483,655	308,958
Less: Current portion		199,702	-
		283,953	308,958

Long-term borrowings as of December 31, 2006 and 2005, consist of the following:

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(in millions of Korean won)			
	Annual Interest Rate (%)		
	Dec. 31, 2006	2006	2005
Won currency loans	5.66 ~ 6.18	257,850	197,950
Less: Current portion		(135,500)	(100)
		122,350	197,850
Foreign currency loans of US\$ 125,538 million, JPY 2,093,959 million (2005: US\$ 20,951 million, JPY 2,104,653 million)	2.01 ~ 6.86	133,071	39,324
Less: Current portion US\$ 0.098 million, JPY 10.694 million (2005: US\$ 0.189 million)		(175)	(191)
		132,896	39,133
		255,246	236,983
Less: Present value discount		(797)	(1,755)
		254,449	235,228

Current maturities of long-term borrowings as of December 31 2006 and 2005, consist of the following:

(in millions of Korean won)		
	2006	2005
Won currency long-term loans	135,500	100
Foreign currency long-term loans of US\$ 0.098 million, JPY 10.694 million (2005: US\$ 0.189 million)	175	191
	135,675	291
Less: Present value discount	(144)	(8)
	135,531	283

The aggregate annual maturities of the long-term borrowings outstanding at December 31, 2006, are as follows:

(in millions of Korean won)				
Year Ending	Debentures	Won Currency Loans	Foreign Currency Loans	Total
2008	110,000	15,625	8,961	134,586
2009	75,000	91,150	115,062	281,212
2010	100,000	15,575	8,873	124,448
Total	285,000	122,350	132,896	540,246

As of December 31, 2006, a substantial portion of the Company's property, plant and equipment are pledged as collateral for the borrowings above (Note 9).

#### 13. Accrued Severance Benefits

Changes in accrued severance benefits for the years ended December 31, 2006 and 2005, consist of the following:

(in millions of Korean won)		
	2006	2005
Beginning balance	248,939	242,423
Provision for severance benefits	60,285	56,590
Succession of accrued severance benefits	127	109
Actual severance payments	(56,254)	(50,183)
	253,097	248,939
Less: Cumulative deposits to National Pension Fund	(3,592)	(4,353)
Severance insurance deposits	(135,295)	(129,372)
Ending balance	114,210	115,214

#### 14. Commitments and Contingencies

As of December 31, 2006 and 2005, the Company has provided guarantees amounting to US\$ 372.072 million (equivalent to 345,878 million) and US\$ 139.333 million (equivalent to 141,144 million), for the operations of its overseas affiliates as follows:

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			(in thousands of US dollar)	
			2006	2005
Kumho Tire Japan	US\$	15,738	US\$	15,845
Kumho Tire Canada		-		447
Kumho Tyre U.K.		-		896
Kumho Tire Tainjin		167,920		122,145
Kumho Tire Changchun		104,000		-
Kumho Tyre Austrailia		18,014		-
Kumho Tire HongKong		66,400		-
			US\$ 372,072	US\$ 139,333

As of December 31, 2006, the Company has provided guarantees amounting up to 1,372 million for the borrowings of Tire Net Corporation, one of its suppliers.

Unmatured trade accounts receivable sold as of December 31, 2006, amount to 326,295 million.

As of December 31, 2006, The Korea Development Bank and other banks have provided the Company with guarantees in relation to the opening of letters of credit. In addition, the Company has been provided with performance guarantees by Seoul Guarantee Insurance Company and others.

The Company has provided Kia Motors Corporation with two promissory notes as collateral in connection with performance guarantees.

As of December 31, 2006, the Company has technical assistance and license agreements with affiliated companies, Nanjing Kumho Tire Co., Ltd., Tianjin Kumho Tire Co., Ltd. and other affiliated company.

As of December 31, 2006, the Company has granted put options to the International Finance Corporation (IFC) and other shareholders of Nanjing Kumho Tire Co., Ltd. (Nanjing Kumho) which give them the right to request the Company to purchase their shares. Further, the Company has also agreed with the IFC and others that it should maintain ownership of more than 51% in the investee, Nanjing Kumho, until Nanjing Kumho's loans are fully paid, and that should the said investee suffer financial insolvency resulting in a default, the Company is required to provide subordinated loans.



The Company has entered into a contract with Standard Chartered First Bank Korea Ltd. and other creditors of Kumho PFVI Inc., a related party, to provide funds by way of increasing capital investment or providing subordinated loans in case Kumho PFVI Inc. suffers financial difficulties.

As of December 31, 2006, the Company is a defendant in several lawsuits filed by customers in relation to product liability. The ultimate outcome of these cases cannot presently be determined. The Company is also insured by Hyundai Marine & Fire Insurance Co., Ltd. and other insurance companies against future claims (Note 9).

The Company has entered into an agreement with Korea Kumho Industrial Co., Ltd. which prohibits the Company from selling, transferring, offering as a collateral, or disposing all or part of its shares of Daewoo Engineering & Construction in any other method for three years and one month from December 15, 2006, the purchase date of the shares without the prior consent from Korea Kumho Industrial Co., Ltd.

The Company also has an agreement with Korea Kumho Industrial Co., Ltd., where if Korea Kumho Industrial Co., Ltd. disposes of its shares in Daewoo Engineering & Construction, and loses its majority shareholder position, the Company may also sell all or part of its shares of Daewoo Engineering & Construction under the same conditions as Korea Kumho Industrial Co., Ltd.

#### 15. Retained Earnings

The Commercial Code of the Republic of Korea requires the Company to appropriate a portion of retained earnings as a legal reserve in an amount equal to a minimum of 10% of its cash dividends until such reserve equals 50% of its capital stock. The reserve is not available for dividends but may be transferred to capital stock or used to reduce accumulated deficit, if any.

Retained earnings as of December 31, 2006 and 2005, consist of:

	(in millions of Korean won)	
	2006	2005
Legal reserve	9,450	5,250
Reserve for business expansion	50,000	-
Reserve for dividend equalization	20,000	-
Reserve for facilities	50,000	-
Retained earnings before appropriations	25,459	190,689
	154,909	195,939

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### 16. Sales and Cost of Sales

Details of sales and cost of sales for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)		
	2006	2005
<b>Sales</b>		
Sales of finished goods	1,632,068	1,640,311
Sales of merchandise	158,987	107,544
Others	22,739	15,270
	1,813,794	1,763,125
<b>Cost of sales</b>		
Cost of finished goods sold	1,345,469	1,249,846
Cost of merchandise sold	114,367	75,418
Others	2,802	1,200
	1,462,638	1,326,464

### 17. Income Taxes

Income tax expense for the years ended December 31, 2006 and 2005, consists of the following:

(in millions of Korean won)		
	2006	2005
Current income tax	11,150	30,193
Deferred income tax from temporary differences <sup>1</sup>	(10,095)	(4,295)
Deferred income taxes added to shareholders' equity <sup>2</sup>	77	-
Income tax expense	1,132	25,898

<sup>1</sup> Changes in deferred income tax from temporary differences are computed as follows:

(in millions of Korean won)		
	2006	2005
Beginning	7,936	3,641
Ending	18,031	7,936
Change	(10,095)	(4,295)

<sup>2</sup> Change in deferred income taxes added to shareholders' equity follows:

(in millions of Korean won)			
	Beginning	Ended	Deferred income taxes
Negative capital adjustment	-	(77)	77

The differences between taxable income and net income before income taxes for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)			
	Details	2006	2005
Temporary Differences	Allowance for doubtful accounts	2,423	1,307
	Provision for warranty expense	-	1,329
	Equity in earnings(losses) of equity-method investees	38,180	(118)
	Equity method investments	(1,847)	1,847
	Derivative financial instruments	7,684	(4,427)
	Accrued severance benefits	24,987	15,638
	Others	415	42
	Sub total	71,842	15,618
Non-temporary Differences	Taxes and dues	16	28
	Interest paid	993	740
	Deemed interest of suspense payments	860	411
	Others	641	1,778
	Sub total	2,510	2,957
		74,352	18,575

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The changes in temporary differences for the years ended December 31, 2006 and 2005, and the deferred income tax assets as of December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

	Beginning Balance	Increase (Decrease)	Ending Balance	Deferred income tax Assets (Liabilities)	
				Current	Non-current
Allowance for doubtful accounts	12,168	2,423	14,591	4,012	-
Provision for warranty expense	3,322	-	3,322	-	913
Equity in earnings(losses) of equity-method investees	(1,639)	38,810	36,541	-	388
Equity method investments	1,847	(1,847)	-	-	-
Derivative financial instruments	(2,088)	7,684	5,596	1,539	-
Accrued severance benefits	15,638	24,987	40,625	-	11,172
Decrease resulting from equity method	-	278	278	-	77
Others	42	137	179	-	49
	29,290	71,842	101,132	5,551	12,599
Bad debt expenses	(434)	-	(434)	(119)	-
<b>2006</b>	<b>28,856</b>	<b>71,842</b>	<b>100,698</b>	<b>5,432</b>	<b>12,599</b>
<b>2005</b>	<b>13,238</b>	<b>15,618</b>	<b>28,856</b>	<b>2,653</b>	<b>5,283</b>

The Company does not recognize the income tax effect resulting from the temporary differences of 12,955 million incurred from the valuation of equity method investments due to the uncertainty of the disposal of the investment in the foreseeable future.

The statutory income tax rate applicable to the Company, including resident tax surcharges, is 27.5% (2005: 27.5%). However, due to non-temporary differences and utilization of tax credits, the Company's effective tax rate is approximately 53.8% for the year ended December 31, 2006 (2005: 20.9%).

The Company adopted an early of Interpretations of SKFAS 06-2 'Accounting treatment of deferred income taxes related to investments in the subsidiaries and equity method investees' in the financial statements for the year ended December 31, 2006. Due to this accounting change, the income tax expense increased by 1,833 million, deferred income tax assets (non-current) decreased by 1,756 million, and negative capital adjustment decreased by 176 million.

### 18. Dividend Information

Dividends for the years ended December 31, 2006 and 2005, were calculated as follows:

	2006	2005
Number of common shares	70,000,000 shares	70,000,000 shares
Par value	5,000	5,000
Dividend ratio	6%	12%
Cash dividends	21,000,000,000	42,000,000,000

Dividend payout ratio for the years ended December 31, 2006 and 2005, follows:

	2006	2005
Dividend	21,000,000,000	42,000,000,000
Net income	970,130,370	98,199,192,962
Dividend payout ratio	2164.7%	42.8%

#### 19. Earnings per Share

Earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the year. Ordinary income per share is computed by dividing ordinary income allocated to common stock, which is net income allocated to common stocks as adjusted by extraordinary gain or losses, net of related income taxes, by the weighted average number of common shares outstanding during the year.

	2006	2005
(1) Weighted average number of common shares outstanding <sup>1</sup>	70,000,000 shares	67,397,260 shares
(2) Net income for common shares	970,130,370	98,199,192,962
(3) Basic earnings per share ((2)/(1))	14	1,457

<sup>1</sup> The number of common shares is calculated by using the weighted-average method.

There are no outstanding dilutive securities as of December 31, 2006 and 2005. Accordingly, basic earnings and ordinary income per share are identical to fully diluted earnings per share.

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### 20. Assets and Liabilities Denominated in Foreign Currencies

Significant monetary assets or liabilities denominated in foreign currencies as of December 31, 2006 and 2005, other than accounts presented elsewhere in the non-consolidated financial statements, are as follows:

(in millions of Korean won, foreign currencies in thousands)

	Foreign Currencies				Won Equivalent
	US\$	JPY	EUR	Others <sup>1</sup>	
<b>Assets</b>					
Trade accounts receivable	98,238	134,843	12,528	9,635	118,554
Other accounts receivable	15,421	-	58	109	15,486
2006	113,659	134,843	12,586	9,744	134,040
2005	101,096	197,619	8,680	6,239	120,765
<b>Liabilities</b>					
Trade accounts payable	93,554	-	2	-	87,574
Other accounts payable	1,119	95,500	6	-	1,885
2006	94,673	95,500	8	-	89,459
2005	78,946	3,701	374	812	81,264

<sup>1</sup> Won equivalent of other foreign currencies.

### 21. Related Party Transactions

The Company's controlling company is Kumho Petrochemical Co., Ltd., while the Company's subsidiaries are Kumho Tire U.S.A., Kumho Tyre U.K., Kumho Tire Europe, Kumho Tire Japan, Kumho Tire Canada, Kumho Tyre Australia, Kumho Tire HongKong and Kumho PFVl. The subsidiaries of Kumho Tire HongKong are Nanjing Kumho Tire, Kumho Tire Tianjin, Kumho Tire Changchun, Kumho Tire Vietnam and Kumho Tire China.

Significant transactions entered into in the ordinary course of business with related parties for the years ended December 31, 2006 and 2005, and the related account balances outstanding as of December 31, 2006 and 2005, are summarized as follows:



(in millions of Korean won)				
Companies	Revenues <sup>1</sup>	Purchases	Receivables <sup>2</sup>	Payables
Controlling company	-	123,765	-	32,615
Affiliates	741,684	133,749	87,480	20,955
Others	3,265	108,510	1,915	13,559
2006	744,949	366,024	89,395	67,129
2005	802,789	282,091	86,489	65,701

<sup>1</sup> Revenues include sales of property, plant and equipment of 4,118 million for the year ended December 31, 2006 (2005: 6,880 million) whose book values amount to 3,481 million (2005: 6,424 million).

<sup>2</sup> Receivables are presented as net of allowance for bad debt of £903 million (2005: 553 million) as of December 31, 2006. The 350 million bad debt expense was recognized in 2006.

As of December 31, 2006, the Company has provided guarantees for its overseas affiliates (Note 14).

Significant management compensation expenses for the year ended December 31, 2006, are as follows:

(in millions of Korean won)	
2006	
Short-term salaries	4,207
Post-retirement benefits	1,123
Total	5,330

The above compensation expenses include all benefits provided to directors of the board, internal auditors and executives who are responsible for the planning, operations and control of the Company.

## 22. Selling and Administrative expenses

Selling and administrative expenses for the years ended December 31, 2006 and 2005, are summarized as follows:

## Non-Consolidated Financial Statements

December 31, 2006 and 2005

(in millions of Korean won)		
	2006	2005
Salaries	48,553	43,366
Severance benefits	10,930	9,663
Welfare expenses	7,560	7,313
Depreciation	7,618	6,818
Advertising expenses	24,951	26,703
Freight	89,197	100,436
Sales commissions	5,802	5,462
Warranty expense	10,529	8,146
Others	65,710	59,499
	270,850	267,406

### 23. Value Added Information

Details of accounts included in the computation of value added for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean Won)				
	2006			2005
	Selling and Administrative expenses	Cost of sales	Total	Total
Salaries and wages	48,553	277,411	325,964	297,707
Severance benefits	10,930	49,355	60,285	56,590
Welfare expenses	7,560	40,975	48,535	45,226
Rental charges	8,816	2,112	10,928	10,595
Depreciation	7,618	123,661	131,279	118,166
Taxes and dues	4,204	11,092	15,296	13,102
	87,681	504,606	592,287	541,386

#### 24. Environmental Investments

Environmental investments of the Company for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)		
	2006	2005
Facilities for prevention of air pollution	977	1,222
Facilities for sanitation	1,208	573
Others	2,642	2,364
<b>Total</b>	<b>4,827</b>	<b>4,159</b>

#### 25. Contributions to Society

The Company's contributions to society for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)		
	2006	2005
Scholarship	700	850
Donation for social welfare	327	394
Donation to cultural organizations	800	890
Others	499	290
<b>Total</b>	<b>2,326</b>	<b>2,424</b>

As part of its employee welfare program, the Company extends housing loans to its qualified employees. As of December 31, 2006, outstanding loans to employees amounted to 526 million (2005: 680 million).

#### 26. Geographical Segment Information

The Company's sales by geographical segments for the years ended December 31, 2006 and 2005, are as follows:

## Non-Consolidated Financial Statements

December 31, 2006 and 2005

(in millions of Korean won)		
	2006	2005
Domestic	759,229	691,764
North America	432,904	418,291
Europe	269,550	299,565
Asia	51,528	52,455
Others	300,583	301,050
<b>Total</b>	<b>1,813,794</b>	<b>1,763,125</b>

### 27. Foreign Currency Forward Agreement

The Company has a future exchange contract to trade with The Korea Development Bank. Details of the foreign currency forward agreement as of December 31, 2006, are as follows:

(in millions of Korean won, Euros in thousands)			
	Contract	Valuation gain	Valuation loss
Forward exchange	EUR 149,983	53	2,466

The Company entered into derivative instrument contracts including foreign currency forwards and interest rates swaps to hedge the exposure to changes in foreign exchange currency and interest rates.

Contracting date	Maturity date	Contract amount	Terms of interest payment	Valuation Gain <sup>1</sup>	Valuation loss <sup>1</sup>
2006.08.28	2009.08.28	100,000	Receiving : 3M LIBOR+ 0.84%, Payable : 5.75%	1,112	4,294

<sup>1</sup> The Company recognized valuation gain and loss in current operations.

### 28. Subsequent Event

On January 4, 2007, the Company provided guarantees amounting to £71.755 million for the borrowings of Kumho Tire HongKong from KDB Asia Limited.

### 29. Operating Results for the Final Interim Period

Significant operating results for the three-month periods ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won except per share amounts)

	2006	2005
Sales	506,076	472,747
Ordinary income(loss)	(4,928)	42,671
Net income(loss)	(5,463)	31,142
Weighted average number of common shares outstanding	70,000,000 shares	70,000,000 shares
Basic ordinary income(loss) per share	(78)	445

### 30. Supplemental Cash Flow Information

Significant transactions not affecting cash flows for the years ended December 31, 2006 and 2005, are as follows:

(in millions of Korean won)

	2006	2005
Reclassification of current portion of long-term debts	335,500	291
Reclassification of construction-in-progress to property, plant and equipment	112,308	82,220
Reclassification from machinery-in-transit to machinery	4,901	7,649
Total	452,709	90,160

### 31. Approval of Financial Statements

The December 31, 2006 non-consolidated financial statements of the Company were approved by the Board of Directors on February 26, 2007.

### 32. Reclassification of Prior Year Financial Statements

Certain amounts in the financial statements as of and for the year ended December 31, 2005, have been reclassified to conform to the December 31, 2006 financial statement presentation. These reclassifications have no effect on previously reported net income or shareholders' equity.

## Report of Independent Accounts' Review of Internal Accounting Control System

To the President of  
KUMHO TIRE CO., INC.

We have reviewed the accompanying management's report on the operations of the Internal Accounting Control System ("IACS") of KUMHO TIRE CO., INC. (the "Company") as of December 31, 2006. The Company's management is responsible for designing and operating IACS and for its assessment of the effectiveness of IACS. Our responsibility is to review the management's report on the operations of the IACS and issue a report based on our review. The management's report on the operations of the IACS of the Company states that "based on its assessment of the operations of the IACS as of December 31, 2006, the Company's IACS has been designed and is operating effectively as of December 31, 2006, in all material respects, in accordance with the IACS standards established by the Internal Accounting Control System Operations Committee (IACSOC) of the Korea Listed Companies Association."

Our review was conducted in accordance with the IACS review standards established by the Korean Institute of Certified Public Accountants. Those standards require that we plan and perform, in all material respects, the review of management's report on the operations of the IACS to obtain a lower level of assurance than an audit. A review is to obtain an understanding of a company's IACS and consists principally of inquiries of management and, when deemed necessary, a limited inspection of underlying documents, which is substantially less in scope than an audit.

A company's IACS is a system to monitor and operate those policies and procedures designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the Republic of Korea. Because of its inherent limitations, IACS may not prevent or detect a material misstatement of the financial statements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on our review, nothing has come to our attention that causes us to believe that management's report on the operations of the IACS, referred to above, is not presented fairly, in all material respects, in accordance with the IACS standards established by IACSOC.

Our review is based on the Company's IACS as of December 31, 2006, and we did not review management's assessment of its IACS subsequent to December 31, 2006. This report has been prepared pursuant to the Acts on External Audit for Stock Companies in Korea and may not be appropriate for other purposes or for other users.



March 2, 2007

## Report on the Operations of the Internal Accounting Control System

To the Board of Directors and Auditor (Audit Committee) of  
KUMHO TIRE CO., INC.

I, as the Internal Accounting Control Officer ("IACO") of KUMHO TIRE CO., INC. ("the Company"), assessed the status of the design and operations of the Company's internal accounting control system ("IACS") for the year ended December 31, 2006.

The Company's management including IACO is responsible for designing and operating IACS.

I, as the IACO, assessed whether the IACS has been effectively designed and is operating to prevent and detect any error or fraud which may cause any misstatement of the financial statements, for the purpose of establishing the reliability of financial reporting and the preparation of financial statements for external purposes. I, as the IACO, applied the IACS standard for the assessment of design and operations of the IACS.

Based on the assessment on the operations of the IACS, the Company's IACS has been effectively designed and is operating as of December 31, 2006, in all material respects, in accordance with the IACS standards.

January 25, 2007

Taisoo Kim

Internal Accounting Control System Officer

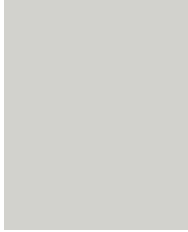
Sae-Chul Oh

Chief Executive Officer or President

# Board Members



**Oh, Sae-Chul**  
President and Chief  
Executive Officer of  
Kumho Tire Co., Inc



**Oh, Jang Hwan**  
Kumho Tires Co.  
Vice president of  
business and sales

## OUR INNOVATIVE LEADERS



**Kim, Chang Nyun**  
Kumho Tires Co.  
Senior Executive Vice  
president of  
Administrative Division



**Noh, Neil**  
Kumho Tires Co.  
Senior Executive Vice  
president of Marketing  
Division



**Han, Min Hyun**  
Kumho Tires Co.  
Senior Vice president of  
research and development  
division



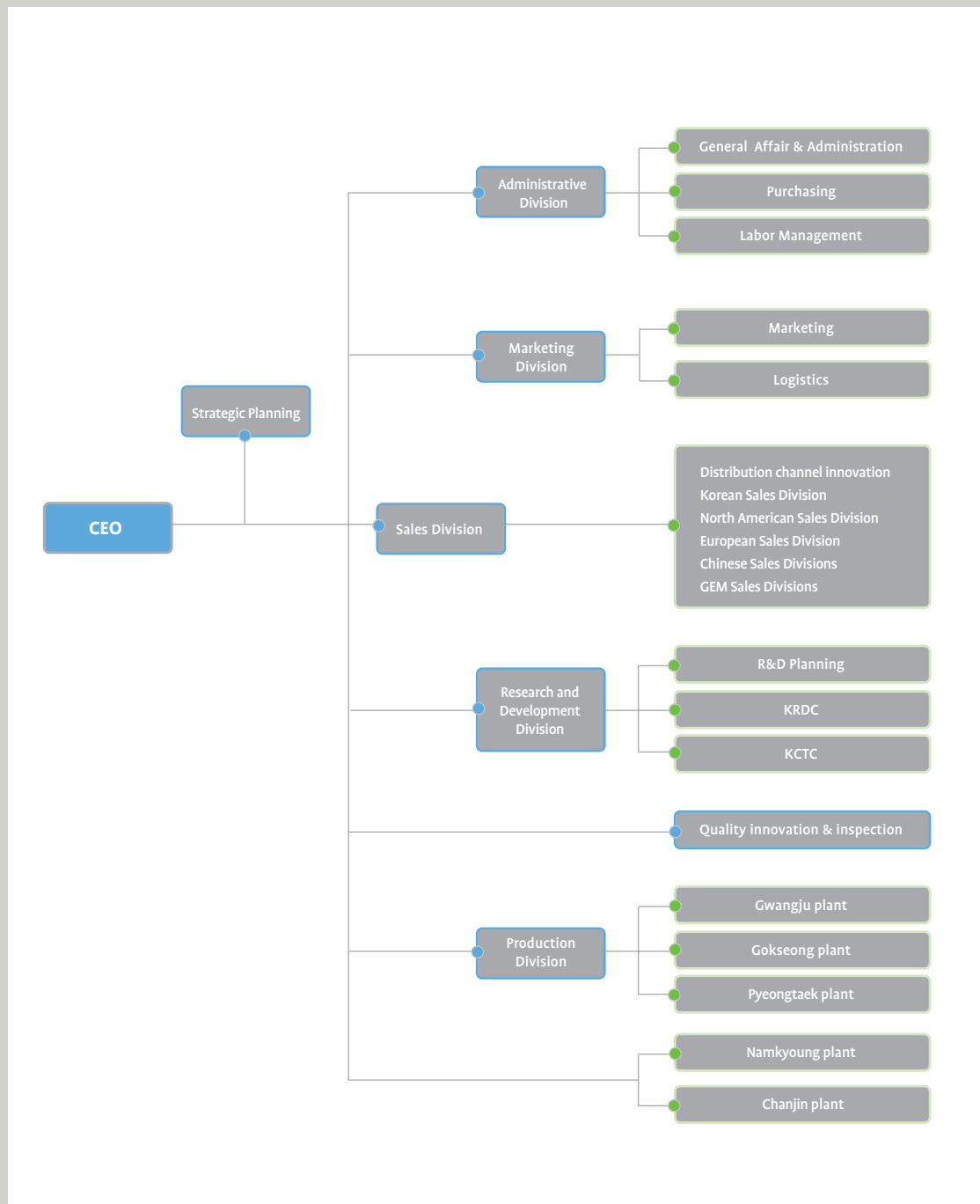
**Kim, Chun Sik**  
Kumho Tires Co.  
Senior Vice president of  
production division



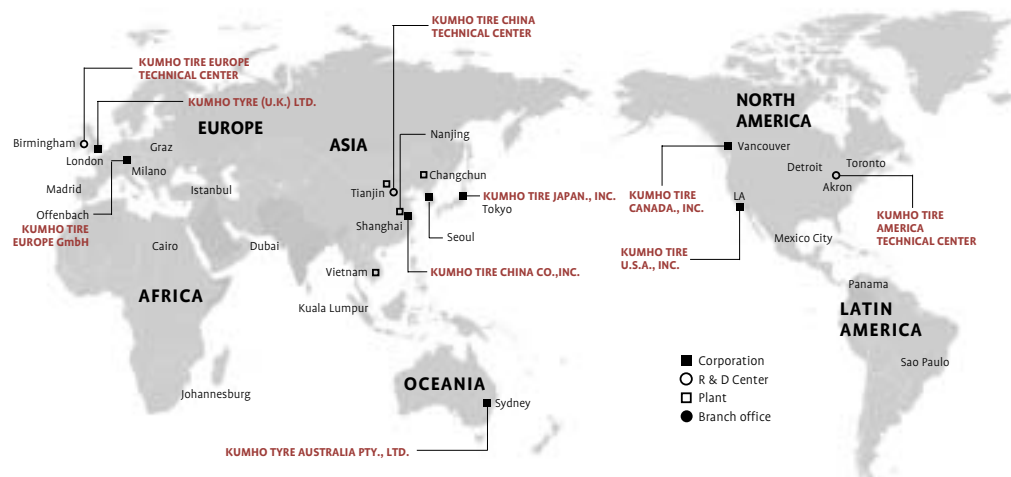
**Rhee, Chang Hyon**  
Kumho Tires Co.  
Senior Vice president of  
Strategic Planning



# Organization



# Global Network



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## BINH DUONG PLANT

Construction on Vietnamese plant slated for 2008

## KUMHO TIRE CO., INC.

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### HEAD OFFICE & GWANGJU PLANT

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FAX : 82-62-941-3161  
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## Company Information

Headquarter	Kumho Tires Co., Ltd. Asiana Building, 57 Sinmunno 1ga Jongno-gu Seoul, Korea
Representative	Oh, Sae-chul
Date of foundation	September 1960
Capital stock	350 billion won
Number of shares(common stock)	70 million shares
Employees	Office workers 1,061   Technicians 4,324   Others 119   Total 5,504

## Investor Relations Contacts

Kim, Tai-soo      Vice President/ Administration & Finance

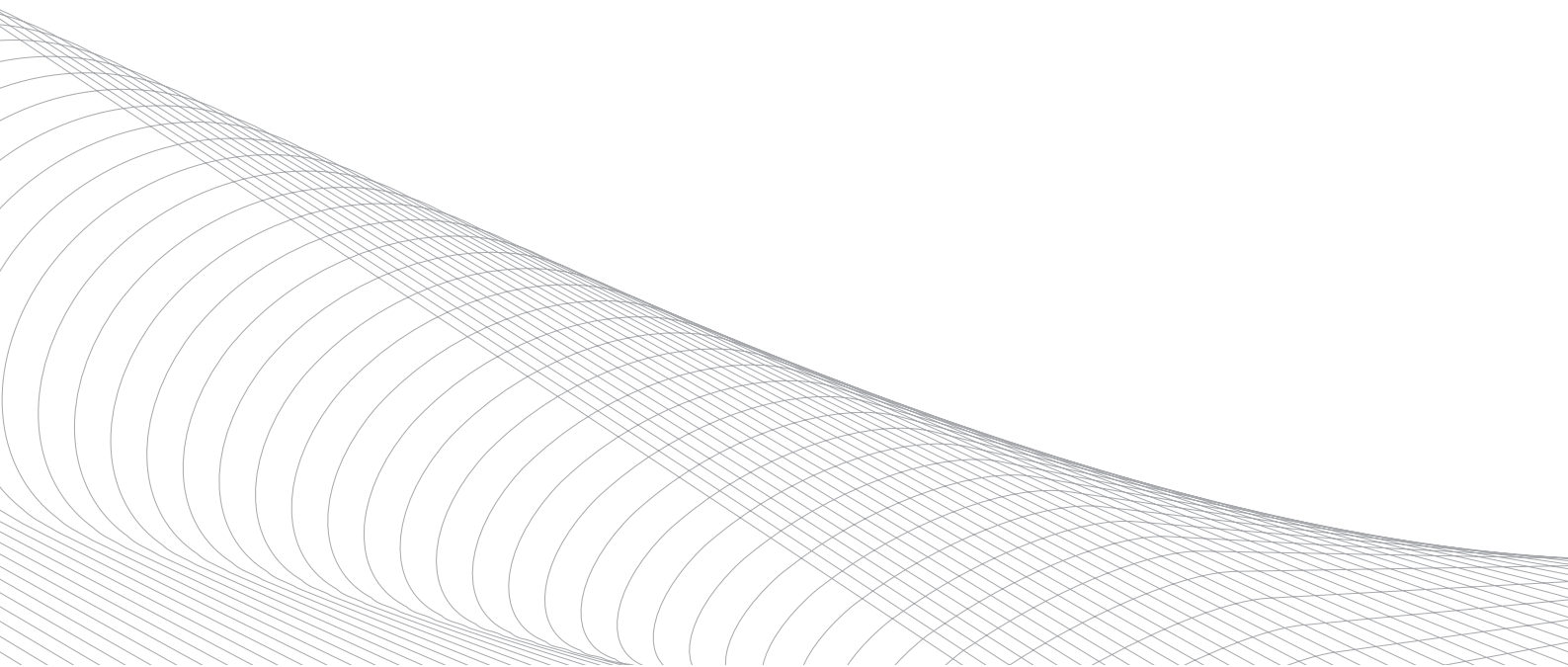
Koo, Sung-lim      Manager/ IR team

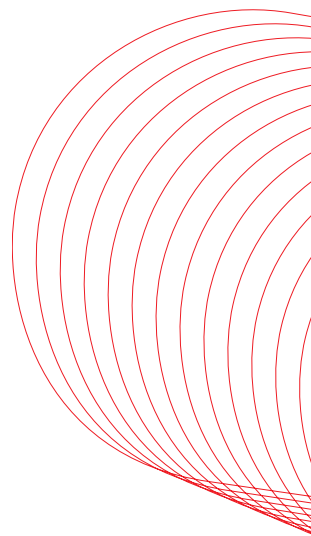
Lee, Eun-kyong      Assistant Manager/ IR team

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