

MANAGEMENT DISCUSSION AND ANALYSIS

Due to the great demand in domestic steel market in the first half of 2004, the Company achieved a significant improvement in operating results with a better financial position. For the six months ended 30th June 2004, the Company's turnover amounted to Rmb4,289,239,000, representing an increase of Rmb1,679,221,000 or 64.34% as compared with the same period of last year. Profit before taxation amounted to Rmb536,388,000, representing an increase of Rmb147,865,000 or 38.06% as compared with the same period of last year. Earnings per share amounted to Rmb0.466, representing an increase of 24.03% as compared with the same period of last year.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN OPERATING REVENUE

In the first half year of 2004, the Company's turnover amounted to Rmb4,289,239,000, of which Rmb4,064,794,000 was derived from the sales of steel products, accounted for 94.77% of the total revenue and representing an increase of 68.93% over the same period of last year, and Rmb224,445,000 was derived from the sales of non-steel products such as water granulated slag, coking and smelting by-products, cutting steel leftover and hydroelectricity, which accounted for 5.23% of the total revenue and represented an increase of 10.16% over the same period of last year.

Turnover	First half of 2004		First half of 2003		Increase/ (decrease)
	Amount (Rmb0,000)	Percentage (%)	Amount (Rmb0,000)	Percentage (%)	
Steel plates	198,176	46.20	130,042	49.82	52.39
Steel sections	105,255	24.54	51,745	19.83	103.41
Wire rods	48,600	11.33	22,419	8.59	116.78
Steel billets	54,448	12.70	36,421	13.95	49.50
Subtotal	406,479	94.77	240,627	92.19	68.92
Others	22,445	5.23	20,375	7.81	10.16
Total	428,924	100	261,002	100	64.34

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN OPERATING REVENUE (CONTINUED)

During the first half of 2004, the Company's sales revenue of the steel products increased by Rmb1,658,520,000 as compared with the same period of last year, of which:

1. During the first half of 2004, the sales volume of the steel products amounted to 1,172,800 tonnes, representing an increase of 27.67% over the same period of last year, resulting in an increase of sales revenue by Rmb634,050,000.

Sales volume	First half year of 2004 (0,000 tonnes)	First half year of 2003 (0,000 tonnes)	Increase (%)	Increase in revenue (Rmb 0,000)
Steel plates	50.71	43.81	15.75	20,479
Steel sections	32.99	21.94	50.36	26,067
Wire rods	16.22	9.93	63.34	14,203
Steel billets	17.36	16.18	7.29	2,656
Total	117.28	91.86	27.67	63,405

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN OPERATING REVENUE (CONTINUED)

2. During the first half of 2004, the average selling price of steel products was Rmb3,466 per tonne, representing an increase of 32.34% over the same period of last year, resulting in an increase in sales revenue of Rmb1,024,470,000.

Selling price	First	First	Increase	Increase in
	half year	half year		
	of 2004	of 2003	(%)	revenue
	(Rmb / tonne)	(Rmb / tonne)		(Rmb 0,000)
Steel plates	3,908	2,968	31.67	47,667
Steel sections	3,191	2,359	35.27	27,429
Wire rods	2,997	2,258	32.73	11,987
Steel billets	3,136	2,251	39.32	15,364
Total	3,466	2,619	32.34	102,447

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

II. INCREASE IN PROFIT

Profit before tax amounted to Rmb536,388,000 for the first half of 2004, representing an increase of Rmb147,865,000 as compared with the same period of last year, which included:

1. Gross profit amounted to Rmb738,417,000, representing an increase of Rmb137,401,000 over the same period of last year.
 - (1) During the first half of 2004, the sales volume of steel products amounted to 1,172,800 tonne, an increase of 254,200 tonne, resulting in an increase of gross profit by Rmb167,010,000.
 - (2) During the first half of 2004, the average selling price of steel products was Rmb3,466 per tonne, an increase of Rmb847 per tonne, resulting in an increase of gross profit by Rmb1,024,447,000.
 - (3) The significant increase in purchase prices of ore, coal, alloy, pig iron, scrap iron and fuel, together with the increased fixed asset maintenance expenses and wage costs, which offset the decreased unit cost resulting from the increased output, the net increase in cost still led to a decrease in gross profit by Rmb1,054,080,000.
2. Other revenues amounted to Rmb14,517,000, representing an increase of Rmb9,587,000 as compared with the same period of last year.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

II. INCREASE IN PROFIT (CONTINUED)

3. Distribution costs amounted to Rmb67,905,000, representing an increase of Rmb3,578,000 as compared with the same period of last year, which was mainly attributable to an increase in ship inspection costs.
4. Administrative expenses amounted to Rmb102,295,000, representing an increase of Rmb16,894,000 as compared with the same period of last year, which was mainly attributable to the increased surcharges such as social insurance as a result of the increased wages.
5. Other operating expenses amounted to Rmb5,773,000, representing a decrease of Rmb32,398,000 as compared with the same period of last year. This was mainly attributable to the provisions for impairment loss of fixed assets.
6. Finance costs amounted to Rmb40,573,000, representing an increase of Rmb11,049,000 as compared with the same period of last year. This was mainly attributable to an increase in loans interest.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

III. IMPROVEMENT IN GEARING RATIO

As at 30th June 2004, the Company's total assets amounted to Rmb6,335,260,000, an increased of 7.17%; total liabilities amounted to Rmb2,838,271,000, an increased of 5.20%; the gearing ratio was 44.80%, a decrease of 0.72 percentage points; current assets amounted to Rmb2,839,690,000 and current liabilities amounted to Rmb2,317,271,000, representing a liquidity ratio of 122.54% which decreased by 7.85 percentage points as compared with the year ended 31st December 2003.

IV. DECREASE IN NET CASH INFLOW

Net cash inflow from operating activities recorded a decrease in the first half of 2004, which was attributable to the increased inventories and trade receivables due to the expansion of production scale and the increased prices of raw materials. In the first half of 2004, the Company's net cash inflow from operating activities was Rmb65,985,000. After deducting net cash outflow from investment activities of Rmb312,340,000 (mainly including modifications of sintering machine, continuous casting machine, medium plate plant's steel cutter and the cool rolled sheet project) and net cash outflow from financing activities of Rmb228,988,000 (mainly including the payment of annual dividend for 2003), the Company's bank balance and cash decreased by Rmb475,343,000. As at 30th June 2004, the Company's bank balance and cash amounted to Rmb871,240,000.