天工國際有限公司*

TIANGONG INTERNATIONAL COMPANY LIMITED

(incorporated in the Cayman Islands with limited liability)

Stock Code : 826

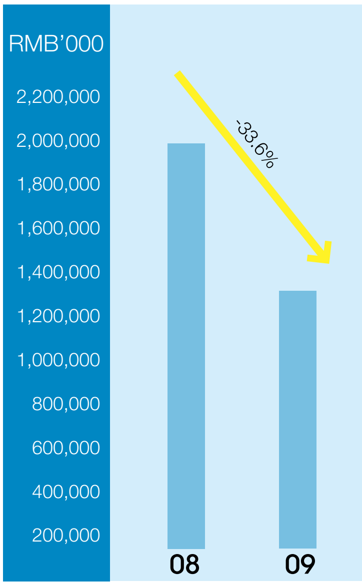
ANNUAL REPORT 2009

* For identification purpose only

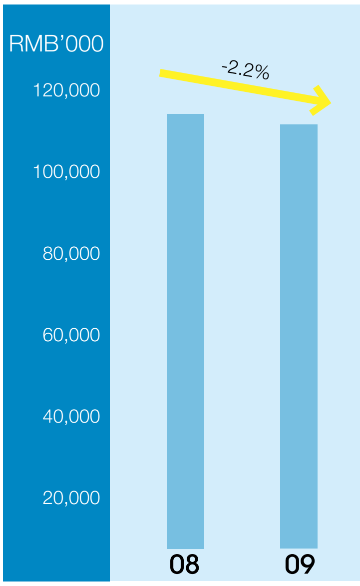
Contents

	Audited 2009 RMB'000	2008 RMB'000
Revenue	**1,323,752**	1,993,269
Net profit attributable to equity holders of the Company	**112,078**	114,643
Earnings per share (RMB)	**0.27**	0.27
Proposed final dividend per share (RMB)	**0.0534**	0.0536

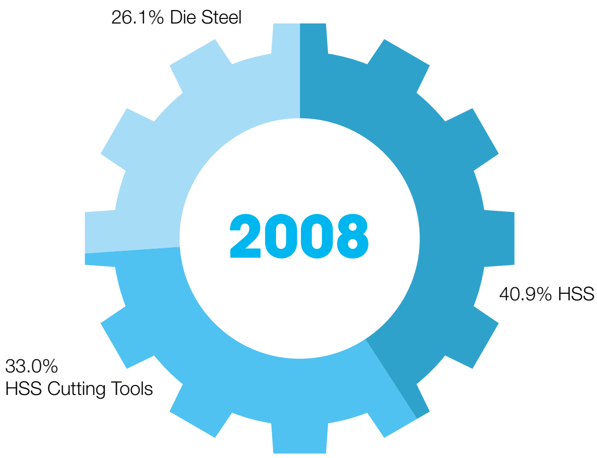
Revenue

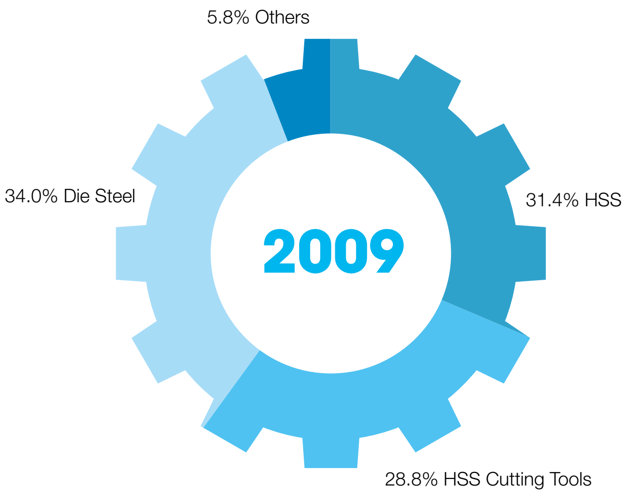


Net profit attributable to equity holders of the Company



Revenue by Product Mix





Riding on our market leader position with cost advantage and a wide product range, we are confident that we can continue to further expand our market share.

Zhu Xiaokun
Chairman

Dear Shareholders,

On behalf of the Board of Directors (the "Board") of Tiangong International Company Limited ("Tiangong International" or the "Company", together with its subsidiaries, collectively the "Group"), we are pleased to present to our shareholders the annual results for the year ended 31 December 2009.

Given the difficult global economic conditions, 2009 has been a challenging year for the Company. The impact of the 2008 financial tsunami persisted into the first half of 2009. As a result of the slowdown in the economy, economic activities as well as industrial and household consumption decreased which, in turn, have negatively affected the Company's sales in overseas and domestic market. Chinese government and many foreign governments implemented various economy stimulus measures which reversed the sliding trend. In the second half of the year 2009, some positive global and domestic economy signs are noticeable and we have also seen a rebound in our business.

During the year of 2009 under review, revenue of the Group decreased by 33.6% to approximately RMB1,323.8 million mainly because of a drop in demand for our products as a result of the slowdown in the economy. Profit attributable to equity holders of the Group declined 2.2% to approximately RMB112.1 million mainly due to the fact that increase in profit margin offsetting the effect from revenue decrease. Basic earnings per share was RMB0.27. To reward our shareholders, the Board proposed a final dividend of RMB0.0534 per share for the year ended 31 December 2009.

In the challenging year of 2009, Tiangong International has continued to be the leading integrated High Speed Steel ("HSS") and HSS cutting tools in China in terms of revenue and volume. After a slow market in the first half of 2009 caused by the weakened demand in tooling and machinery industries, we have seen a recovery in our sales order as the economy gradually picked up. Another encouraging sign is that we also managed to successfully implement cost control measures and increased our profit margin in the year. Riding on our market leader position with cost advantage and a wide product range, we are confident that we can continue to further expand our market share. We will also continue our rapid expansion of sales centre network in order to tap the rich domestic HSS and HSS cutting tools market.

Our die steel business has been growing rapidly in recent years and has become our largest revenue contributor. With the improvement in production rate and stringent control on production cost, we managed to improve the profit margin significantly. After years of experience in this industry, we have accumulated the production knowledge and technology. The Group will continue to develop this high potential business in the future. Our newly installed flat steel production line commenced production in 2009. Targetting the flat steel market with wider range of use and customer base, the outlook for our die steel business is positive.

In order to maintain growth and maximize returns to the shareholders of the Company. The Company will adopt the following strategies:

- To further expand HSS and HSS cutting tools domestic market by increasing the network of sales centres
- To further develop die steel business and increase market penetration
- To further enhance sales growth through brand building

Finally, on behalf of the Board, I would like to express my sincere gratitude for the continued support of our dedicated staff, shareholders, customers and business partners throughout the year. We always strive to achieve better results by delivering future sustainable business growth in order to repay all of our shareholders.

By order of the Board

Tiangong International Company Limited
Zhu Xiaokun
Chairman

Hong Kong, 13 April 2010

Management Discussion and Analysis

The following management discussion and analysis should be read in conjunction with our consolidated financial statements, which were audited by KPMG and reviewed by the audit committee of the Company. The Group is mainly engaged in the production and sales of HSS, HSS cutting tools and die steel. Our operations are classified into the following product segments:

HSS

HSS involves the purchase of various rare metals such as tungsten, molybdenum, chromium, vanadium and other raw materials, production of HSS for both internal supply to the Group's HSS cutting tools production and external sale to customers outside the Group. HSS typically has higher pressure and temperature tolerances than regular steel and is more wear resistant. It is widely used in more specific industrial applications such as automotive, machinery manufacture, aviation, chemical processing and electronics industries. The Group commenced its production of HSS in 1992.

HSS Cutting Tools

HSS cutting tools involves the production and sales of HSS cutting tools to external customers. Over 70% of its sales were exported to over 30 countries and regions throughout Europe, North America, Africa and the Middle East in 2008 and 2009. The Group produces an extensive range of HSS cutting tools products which can be categorized into four types — twist drill bits, screw taps, end mills and turning tools. This segment has been in operation since 1987, being the longest-established sector of the Group.

Die Steel

Die steel involves the purchase of various rare metals and other raw materials, production and sale of die steel to customers. The characteristics and production process of die steel are similar to those of HSS. It is suitable for application in dies and moulds for die casting and machining processes. The Group commenced its production of die steel in 2005.

Market Review

In 2009, the global economy was severely affected by the global financial crisis which was a result of the collapse of United States housing market in 2008. The global economy experienced one of the most serious slowdowns since the Great Depression. To respond to the crisis, various countries acted collectively to implement monetary and fiscal measures to boost the economy. As a result, the world economy began to recover slowly from the economic downturn. Encouraging signs in the macro-economy and various industries such as housing and retail exhibited an encouraging development trend.

The newly developed special steel products manufactured by Tiangong in the last two years to satisfy modern industrial need.

As China is an export driven economy, the significant drop in demand from overseas caused by the global financial crisis has significantly impacted the Chinese domestic economy. Following the actions of overseas central banks and government, the Chinese government has also implemented and continued to modify the Economic Stimulus Plan which includes increasing bank loans for enterprises, pumping public investment into infrastructure development as well as encouraging consumption in various industries. Such measures have reversed the economy contraction and the domestic economy is recovering gradually.

Gross Domestic Product in China in 2009 grew at 8.7%. The growth rate was slightly below that of 9.0% in 2008. Due to the slow down in domestic demand for cutting tools and machinery, China's annual HSS production decreased by 13.3% to 69,897 tonne in 2009. China's annual die steel production has dropped by 4.5% (2008: growth rate of 2.6%) to 401,890 tonne in 2009. The slowdown in die steel growth was attributable to the decrease in demand for domestic machineries and other consumer products that required moulding in the production process.

Business Review

The Group is the number one integrated HSS and HSS cutting tools manufacturer in China. According to China Special Steel Enterprise Association and China Machine Tool & Tool Builders' Association, the Group has been the largest manufacturer of HSS by volume in China from 2001 to 2009 and the largest HSS cutting tools manufacturer by revenue in China from 2007 to 2009.

Since the global financial crisis, some of our customers faced keener market competition. This forced them to improve on product quality and to exercise more stringent control over production cost to differentiate from other competitors. In order to enhance pricing and quality competitiveness and to expand their market shares, our customers tended to be more prudent in selecting suppliers.

Operating in this challenging environment, the Group which is the largest HSS and HSS cutting tools manufacturer with vertical integration, has cost advantages over other market players. With the largest range of products to offer and a long history of delivering quality products, the Group always satisfy the market and customers' needs. As a result, the Group managed to enhance its market share in the ongoing changing market.

The revenue from the sales of the three major products are set out below:

	For the year ended 31 December					
	2009		2008		change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
HSS	**415,571**	**31.4%**	815,316	40.9%	(399,745)	-49.0%
HSS cutting tools	**380,886**	**28.8%**	658,061	33.0%	(277,175)	-42.1%
Die steels	**450,327**	**34.0%**	519,892	26.1%	(69,565)	-13.4%
Others	**76,968**	**5.8%**	—	—	76,968	—
	1,323,752	**100.0%**	1,993,269	100.0%	(669,517)	-33.6%

HSS

The HSS market has slowed down as a result of the drop in industrial demand caused by the global financial crisis. Some of the customers need to utilize their excess inventory before placing replenishment orders with us. As a result, HSS revenue dropped and accounted for 31.4% of the Group's revenue for 2009 as compared to 40.9% for 2008. Due to the slowdown in industrial activities and drop in demand in the HSS market, the sales volume and sales price of HSS both decreased in the first half of 2009. Although the sales volume picked up in the second half of 2009, the sales price of HSS remained lower than in 2008 because of the decrease in raw material costs. As a result, the sales of HSS decreased from RMB815,316,000 in 2008 to RMB415,571,000 in 2009, representing a decrease of 49.0%. The Group's HSS domestic sales and export sales decreased by 41.2% and 71.4%, respectively. During the year, export sales fell more than domestic sales because demand from cutting tools and machinery manufacturers for HSS in North America and Europe remained relatively weak as a result of the financial crisis. We have noticed recovery trends in both markets in recent months. Set out below is a geographical breakdown of the sales of HSS for the two years ended 31 December 2008 and 31 December 2009:

	For the year ended 31 December					
	2009		2008		change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
HSS						
Domestic	**355,038**	**85.4%**	603,730	74.0%	(248,692)	-41.2%
Export	**60,533**	**14.6%**	211,586	26.0%	(151,053)	-71.4%
	415,571	**100.0%**	815,316	100.0%	(399,745)	-49.0%

HSS cutting tools

Revenues from sales of HSS cutting tools decreased by approximately 42.1% to RMB380,886,000 in 2009, accounting for approximately 28.8% of the Group's total revenue in 2009. During 2009, revenues from export sales of HSS cutting tools decreased by 38.3% to RMB292,341,000, mainly resulting from the decrease in demand for cutting tools in automobile, housing and machinery industries in North America and Europe. The Financial crisis had a significant negative impact on these industries in the first half of 2009. Positive signs are beginning to appear in these industries in the second half of the year. Domestic sales decreased by 52.0% to RMB88,545,000 for 2009 as a result of a decrease in orders by a few of our major customers who supply to overseas markets. Set out below is a geographical breakdown of the sales of HSS cutting tools for the two years ended 31 December 2008 and 31 December 2009:

	For the year ended 31 December					
	2009		2008		change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
HSS cutting tools						
Domestic	**88,545**	**23.2%**	184,525	28.0%	(95,980)	-52.0%
Export	**292,341**	**76.8%**	473,536	72.0%	(181,195)	-38.3%
	380,886	**100.0%**	658,061	100.0%	(277,175)	-42.1%

Die steel

Revenue from sales of die steel accounted for 34.0% of the Group's total revenue, becoming the largest revenue contributor to the Group for 2009. The Group's die steel revenue decreased by 13.4% from RMB519,892,000 in 2008 to RMB450,327,000 in 2009. Domestic sales increased by 64.5% to RMB401,276,000 in 2009 because of the increase in sales to the domestic automobile and machinery markets. During 2009, these domestic markets recovered gradually as a result of the Chinese Economic Stimilus Package. Export sales decreased by 82.2% to RMB49,051,000 in 2009. The drop was mainly due to the decrease in demand from manufacturing and automobile industries in North America and Europe as these industries remained weak as a result of the global financial crisis. Set out below is a geographical breakdown of the sales of die steel for the two years ended 31 December 2008 and 31 December 2009:

	For the year ended 31 December					
	2009		2008		change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
Die steel						
Domestic	**401,276**	**89.1%**	244,002	46.9%	157,274	64.5%
Export	**49,051**	**10.9%**	275,890	53.1%	(226,839)	-82.2%
	450,327	**100.0%**	519,892	100.0%	(69,565)	-13.4%

Financial Review

Net profit attributable to equity holders of the Company decreased slightly from RMB114,643,000 for 2008 to RMB112,078,000 for 2009. The slight decrease was mainly due to the net decrease resulting from the decrease in operating profit caused by the weaker market demand and the reduction in financial costs. Given the different market conditions, the three business lines experienced different levels of impact from the economic slowdown. As Die Steel business remained relatively more resilient, it overtook HSS business as the largest revenue contributor.

Revenue

Revenue of the Group for 2009 totaled RMB1,323,752,000, representing a decrease of approximately 33.6% when compared with RMB1,993,269,000 in 2008. The decrease was mainly attributable to the decrease in sales volume and sales price of HSS and HSS cutting tools.

Cost of sales

The Group's cost of sales decreased by RMB610,699,000 from RMB1,673,566,000 for 2008 to RMB1,062,867,000 for 2009, representing a decrease of approximately 36.5%. The decrease was higher than the 33.6% decrease in revenue during the year. This was mainly due to an improvement in profit margins for all three lines of businesses. As a percentage of total revenue, the Group's cost of sales decreased from approximately 84.0% in 2008 to approximately 80.3% in 2009.

Gross margin

For 2009, the gross margin was approximately 19.7% (2008: 16.0%). The increase was due to the increase in profit margin for all three businesses. Set out below is the gross margin for our three products for 2008 and 2009:

	2009	2008
HSS	**20.9%**	18.4%
HSS cutting tools	**16.2%**	13.1%
Die steel	**24.8%**	16.1%

HSS

In 2009, the gross margin of HSS increased from 18.4% to 20.9%. The increase was mainly due to the Group's tighter production cost control and reduction in raw material costs such as rare metals and scrap steel.

HSS cutting tools

The increase in HSS cutting tools gross margin from 13.1% in 2008 to 16.2% in 2009 was attributable to the increase in tax rebates on export HSS cutting tools sales and reduction in rare metal prices.

Die steel

The gross margin of die steel increased from 16.1% in 2008 to 24.8% in 2009 as a result of the higher production rate of die steel and increase in sales of higher profit market product specifications.

Other income

The Group's other income totaled RMB10,970,000 in 2009, representing an increase of RMB4,902,000 from RMB6,068,000 in 2008. The increase was attributable to the RMB10,158,000 government grants received from local governments in 2009.

Distribution expenses

The Group's distribution expenses were RMB29,573,000 (2008: RMB50,106,000), representing a decrease of approximately 41.0%. The decrease was mainly attributable to the decrease in commission and transportation expenses by RMB10,974,000 and RMB6,314,000 respectively, resulting from the decrease in sales. For 2009, the distribution expenses as a percentage of revenue were 2.2% (2008: 2.5%).

Administrative expenses

For 2009, the Group's administrative expenses decreased slightly from RMB61,155,000 in 2008 to RMB60,810,000 in 2009 primarily because the total staff cost, depreciation and bank charges decreased slightly over the year. For 2009, the administrative expenses as a percentage of revenue were 4.6% (2008: 3.1%).

Net finance cost

The Group's finance income was RMB2,736,000 for 2009, representing a decrease of RMB1,871,000 when compared with that of RMB4,607,000 for 2008. The decrease was mainly due to the decrease in interest rates during 2009.

The Group's finance expenses were RMB50,049,000 for 2009, representing a decrease of 48.0% when compared with the RMB96,162,000 for 2008. The decrease was attributable to the decrease of exchange loss of RMB25,152,000 and the capitalization of RMB27,860,000 interest during the building phase which was required by the revised accounting standard.

Income tax expense

The Group's income tax expense increased by RMB4,640,000 from RMB2,602,000 in 2008 to RMB7,242,000 in 2009. This increase was mainly due to the increase in income tax as Jiangsu Tiangong Tools Company Limited's tax exemption ended in 2008.

Profit for the year

As a result of the factors discussed above, the Group's profit slightly decreased by approximately 0.4% to RMB112,078,000 for 2009 from RMB112,510,000 for 2008. The Group's net profit margin increased from 5.6% in 2008 to 8.5% in 2009.

Profit attributable to equity holders of the Company

For 2009, profit attributable to equity holders of the Company was RMB112,078,000 (2008: RMB114,643,000), representing a decrease of 2.2%.

Liquidity and Financial Resources

As at 31 December 2009, the Group's current assets mainly included cash and cash equivalents of approximately RMB63,467,000, inventories of approximately RMB1,252,748,000, trade and other receivables of RMB656,959,000, pledged deposits of RMB119,358,000 and time deposits of RMB192,000,000. As at 31 December 2009, the interest bearing borrowings of the Group were RMB1,556,700,000, RMB1,379,700,000 of which were repayable within one year and RMB177,000,000 of which were repayable after more than one year. The Group's gearing ratio (calculated based on the total outstanding interest-bearing debt divided by the total assets) was 40.9%, higher than the 39.7% as at 31 December 2008. The increase was mainly attributable to the increase in investment in production equipment and increase for inventory for the die steel business. The majority of the borrowings of the Group were subject to interest payable at rates ranging from 2.40% to 5.76%. The Group did not enter into any interest rate swap to hedge itself against the risks associated with interest rates.

Capital Expenditures and Capital Commitments

For 2009, the Group's increase in fixed assets amounted to RMB254,550,000, which were mainly for the production plant and facilities for die steel. As at 31 December 2009, capital commitments were RMB236,815,000, of which RMB66,505,000 were contracted and RMB170,310,000 were authorised but not contracted for. The majority of the capital commitments were related to investment to completion production equipment installation.

Foreign Exchange Exposure

The Group's revenues were denominated in RMB, US dollars and Euros, with RMB accounting for the largest portion (approximately 69.6%). Approximately 30.4% of total sales and the Group's costs and operating profit were subject to exchange rate fluctuations. The Group has put in place measures such as monthly review of product pricing in light of foreign exchange fluctuation and incentivising overseas customers to settle balances on a more timely basis to minimize the financial impact from exchange rate exposure.

Pledge of Assets

As at 31 December 2009, the Group pledged certain bank deposits amounting to approximately RMB119,358,000 (2008: RMB63,600,000). Details are set out in the notes to the financial statements.

Employee's Remuneration and Training

As at 31 December 2009, the Group employed around 4,419 employees (31 December 2008: around 5,087). Total staff costs during the year amounted to RMB98,833,000 (2008: RMB115,217,000). The Group provided employees with remuneration packages comparable to the market rates and employees are further rewarded based on their performance according to the framework of the Group's salary, incentives and bonus scheme. In order to enhance the Group's productivity, and further improve the quality of the Group's human resources, the Group provides compulsory continuous training for all of its staff on a regular basis.

Contingent Liabilities

The Company had no material contingent liabilities as at 31 December 2009.

Prospects

The global financial crisis has caused a slowdown in domestic and overseas special steel industry and cutting tools industry. The hardest hit periods were the last quarter of 2008 and the first quarter of 2009 when a significant portion of the sales orders were cancelled. During 2009, the special steel and cutting tools industry began to recover. The overall market environment improved and there was a general upward trend on order quantities from customers. Leveraging on our leading market position and our pricing and product quality advantages over our competitors, we are confident that we will be able to resume our growing trend on all three business lines soon in the near future.

HSS

After years of rapid production capacity expansion, the Group's annual production capacity has reached 45,000 tonnes. Being the largest HSS manufacturer in China with capacity more than double that of the closest competitor, the Group has established a reputation as the largest HSS maker with reliability and quality. Given the decrease in raw material price and our stringent control on production cost, we managed to improve gross margin on a number of HSS products in 2009. In 2010, we will continue to build on the trend. Moreover, we will also continue to increase the promotion effort in the domestic market in order to place more focus on domestic HSS markets. Our number of sales centres have increased from 16 at the end of 2008 to 70 as at 31 December 2009. We plan to further expand our network of sales centres in 2010.

HSS cutting tools

China has the largest reserves of a number of rare metals. As high tariffs are imposed on export of these cutting tools raw materials, the Group has advantages over its overseas competitors. The Group will continue to build on its strength in overseas markets. Lately, the Group has invested on an advanced cutting tools production line covering the grinding, heat treatment and slot, surface and edge grinding processes. With the capacity to produce higher quality cutting tools, the Group will continue to place emphasis on selling more HSS cutting tools for professional use which have higher selling price and profit margins.

Die steel

Our die steel business has been growing rapidly in recent years and has now become the Group's largest revenue driver. After years of experience in producing die steel, the Group started to grip the production knowledge and technology. With the improvement in production rate, the Group has managed to improve die steel's gross margin significantly in 2009. Moreover, the commencement of production of the newly installed production line in the 2009. This enabled the Group to enter a new flat steel market, the products of which has a wider range of use and customer base. The Group's plan for 2010 is to continue to improve the gross margin by cost control measures and to develop and promote the flat steel business.

Executive Directors

Mr. ZHU Xiaokun, aged 53, is an Executive Director and the Chairman of the Group. He is responsible for the overall business development strategy of the Group and has over 20 years of experience in HSS and cutting tools industry. Mr. Zhu graduated from the Economic and Management Department of Jiangsu Radio and TV University. In 1984. he joined Danyang Houxiang Television Antenna Factory (the predecessor of TG Group) as the general manager. He led the factory to transform from a television antenna factory to an enterprise of HSS cutting tools in 1987 and also subsequently to expand to include the production of HSS in 1992. He has been acting as the Chairman of the Group since July 1997. In 1998, he was awarded as a National Township Factory Manager and was named as a National Township Entrepreneur in 2004 by Ministry of Agriculture.

Mr. ZHU Zhihe, aged 59, is an Executive Director and the Chief Executive Officer (General Manager) of the Group. He is responsible for the daily operations of the Group and has over 20 years of experience in factory management. Prior to joining the Group, he worked for Feida Village in Houxiang Town and Jiangsu Danyang Houxiang Gaoshi Bridge Yuming Metallic Factory. He joined the Group in 1993. During July 2000 to August 2006, he was an executive director and the vice general manager of Jiangsu Tiangong Tools Company Limited. He is now in charge of the production, operation and sales of HSS and die steels for TG Tools and TG Aihe.

Mr. ZHU Mingyao, aged 54, is an Executive Director of the Group. Prior to joining the Group, he worked for Qianxiang Village. In 1995, he joined the Group as the head of the sales division and factory manager of the smelting factory. From July 1997 to August 2006, he acted as an Executive Director and deputy general manager of Jiangsu Tiangong Tools Company Limited. He is currently in charge of the production, operation and management of TG Aihe.

Mr. YAN Ronghua, aged 41, is an Executive Director of the Group. He graduated from the Economic and Management Department of Jiangsu Radio and TV University. He joined the Group in 1994. He was appointed as the head of office administration and subsequently the assistant general manager of the Group. Mr. Yan is currently in charge of human resources management, external relations, secretarial and office administration of the Group.

Non-Executive Director

Mr. THONG Kwee Chee, aged 37, was appointed as a Non-Executive Director of the Company in September 2006. Mr. Thong is currently Vice President of Pinebridge Investment (previously known as AIG Global Investment) covering direct investment activities in the Greater China region. Prior to Pinebridge Investment, Mr. Thong is affiliated with Arthur Andersen, Meridian Asset Management (Malaysia) and China Development Industrial Bank. Mr. Thong holds BSc (Hons) in Accounting and Finance from Warwick University, England and Chartered Financial Analayst (CFA) qualification, since 2001.

Independent Non-Executive Directors

Mr. LI Zhengbang, aged 77, joined the Group in June 2007 as an Independent Non-Executive Director. He graduated from Harbin Institute of Technology in 1958 and was elected as the academician of the Chinese Academy of Engineering in 1999. He is a qualified senior engineer in the PRC and is currently a Professor and Supervisor of PhD candidates of the Central Iron & Steel Research Institute. Mr. Li has been engaged in the research and development of electroslag metallurgy for years and has been one of the few pioneers in this area. His achievement was recognized by The Science and Technology Committee of the People's Republic of China as one of the inventors of electroslag metallurgy technology in China. He has been granted special government subsidy by the State Council as a result of such achievement.

Mr. GAO Xiang, aged 66, joined the Group in July 2007 as an Independent Non-Executive Director. In July 1966, he graduated from Wuhan Institute of Mechanics, majoring in production craftsmanship of machines and equipment. He is a senior engineer. Under his leadership, the study of twist drill extrusion technology by Chengdu Tools Research Institute was honoured with Third Class Award of Technical Findings of the Ministry of Mechanics. His achievements are widely recognized in the industry, and he has been granted special government subsidy by the State Council since 1999 as a result of such achievements.

Mr. LAU Siu Fai, aged 52, joined the Group in July 2007 as an Independent Non-Executive Director. He is a registered financial planner of the Society of Registered Financial Planners, Hong Kong and a fellow member of the Institute of Financial Accountants. Mr. Lau was previously the Group Financial Controller of Imagination Solutions, the Regional Accounting Manager of the North Asia region of Quaker Oats Asia, Inc. The chief representative in Beijing office of the Mansion Electronic Engineering company Ltd and the Deputy General Manager of the Investment Related Trade Department of Chia Tai Intertrade Company, Limited. In October 2005, he was appointed as the financial adviser of Shantou University.

Senior Management

Mr. SHI Guorui, aged 63, is the chief financial officer of the Group. He graduated from the Industrial Accounting Department of the Soochow University in 1986. He is an accountant. Prior to joining the Group in July 2004, he worked for Jiangsu Province Zhenjiang Casting Factory, Zhenjiang Radio Electronic Factory, Jiangsu Province Zhenjiang Electronics Tube Factory, Zhenjiang Electronics Industry Company, Limited and Zhejiang Wireless Applicances and Materials Factory. He has extensive experience in finance and accounting.

Mr. ZHU Xingyuan, aged 58, is an executive director and a deputy general manager of TG Tools and Tianji Packaging. In 1984, he joined the Group as the vice factory manager of Danyang Houxiang Television Antenna Factory. He is currently in charge of the production, operation and management of HSS tools of the Group. He has over 20 years of experience in the management of tools production.

Mr. ZHU Wanglong, aged 51, is an executive director and a deputy general manager of TG Aihe. Prior to joining the Group, Mr. Zhu worked for Qianxiang Village and Danyang Machining Tools Factory. He joined the Group in July 1997 and has been in charge of product innovation, technology improvement, investment development and quality inspection. He has over 20 years of experience in the management of tools production.

Mr. WU Suojun, aged 37, is an executive director and a deputy general manager of TG Tools, and a deputy general manager of Tianfa Forging. Mr. Wu joined the Group in 1993 as a workshop officer. He is in charge of the production, operation and management of HSS.

Mr. JIANG Rongjun, aged 40, is an executive director and a deputy general manager of TG Tools and a deputy manager of Tianji Packaging. He joined the Group in 1985 as a workshop officer. Mr. Jiang is currently in charge of the sale of HSS tools and the export of die steel.

Mr. CHEN Jianguo, aged 50, is a assistant general manager of TG Tools and an executive director of TG Aihe. He joined the Group in 1996. Prior to joining the Group, Mr. Chen worked at the Houxiang branch of Danyang Construction Engineering Company, Jiangsu Feida Tools Company Limited. Mr. Chen is currently in charge of production security and human resources.

Mr. LEUNG Wai Yip, aged 34, is the financial controller and the company secretary of the Company. Mr. Leung joined the Group in June 2007. Prior to joining the Group, Mr. Leung was an internal auditor of the Swire Group and was previously a manager with the assurance and advisory business services department of Ernst & Young Certified Public Accountants. Mr. Leung graduated with a Bachelor of Commerce degree from the University of Alberta in Canada. He is a member of the American Institute of Certified Public Accountants, and an associate member of the Hong Kong Institute of Certified Public Accountants.

The Group strives to attain and maintain high standards of corporate governance as it believes that good corporate governance practices are fundamental to the Group's development and essential for safeguarding shareholders' interests. To achieve this objective, the Group strengthens its internal policies and procedures, provides continuous training to its staff and increases the transparency of its operation and accountability to all shareholders. The Group is committed to improving this practice and maintaining an ethical corporate culture. During the year, the Group had complied with the principles and code provisions set out in the Code on Corporate Governance Practices (the "Code") as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules").

The Board

The Board's primary role is to secure and enhance long-term shareholder value. It focuses on the Group's overall strategic policy and provides proper supervision to ensure effective management and to achieve sound returns for its shareholders. The Board has delegated the authority and responsibility for implementing business strategies and management of the daily operations of the Group's business to the management. The Board is mainly responsible for developing long term objectives and strategy of the Group, monitoring operation performance and results, monitoring performance of the management, establishing dividend policy and reviewing significant investment plans and decisions. The Board meets at least four times a year and additional meetings are held when required to discuss significant events and issues. The company secretary assists the Chairman in preparing the agenda for Board meetings. Board meetings are held with at least 14 days' advance notice, and all Directors would be served with an agenda with supporting papers at least 3 days before the Board meetings, so as to ensure that there is timely access to relevant information. The Group ensures that all the Board members are informed of the Group's latest development and thereby assists them in the discharge of their duties. The Directors may take independent professional advice when appropriate, at the Company's expense. Four Board meetings were held for the year ended 31 December 2009, with all the Directors attending. Minutes of the Board and Board Committees are taken by the company secretary. Such minutes of the Board and Board Committees, together with supporting papers, are open for inspection following reasonable notice by any Director. Draft and final versions of minutes are sent to all Directors for their comment and records.

Composition of the Board

The Board comprises four Executive Directors (Mr. Zhu Xiaokun, Mr. Zhu Zhihe, Mr. Zhu Mingyao and Mr. Yan Ronghua), one Non-Executive Director (Mr. Thong Kwee Chee) and three Independent Non-Executive Directors (Mr. Li Zheng Bang, Mr. Gao Xiang and Mr. Lau Siu Fai). Biographical details of the Directors of the Group as at the date of this report are set out on page 14 to 16 of this annual report.

Independent Non-Executive Directors account for more than one-third of the members of the Board. The Independent Non-Executive Directors come either from steel industry or have related professional background, bringing valuable expertise and experience that promotes the best interests of the Group and its shareholders. The role of the Independent Non-Executive Directors is to provide independent and objective opinions to the Board for its consideration. The Company has received confirmation from each Independent Non-Executive Director about his independence as set out in Rule 3.13 of the Listing Rules and continues to consider each of them to be independent.

Chairman and Chief Executive Officer

The Chairman of the Board is Mr. Zhu Xiaokun, and the chief executive officer is Mr. Zhu Zhihe. The Chairman's and the chief executive officer's roles are clearly defined to ensure their independence. The Chairman of the Board is responsible for the overall management of the Board and monitoring the Group's business strategies, while the chief executive officer is responsible for managing the daily operations of the Group.

Appointment and Re-election of Directors

A person may be appointed as a member of the Board at any time either by shareholders' resolutions in general meetings or by resolutions of the Board upon recommendation by the Nominations Committee of the Company. New Directors appointed by the Board during the year are required to retire and submit themselves for re-election at the first annual general meeting immediately following their appointments. All Directors are required to retire by rotation at least once every three years at the annual general meeting, subject to re-election by the shareholders. All Non-Executive Directors (including Independent Non-Executive Directors) are appointed for a term of not more than three years.

Board Committees

The Board has established three Board Committees to oversee different aspects of the Company's affairs. These Board Committees include Audit Committee, Remuneration Committee and Nomination Committee. The Board Committees have been structured to include a majority of Independent Non-Executive Directors as members in order to ensure that all relevant issues are reviewed independently and objectively. The terms of reference of the respective Board Committees have complied with the Code provisions and are available on the Company's website http://www.tggj.cn.

Audit Committee

The Audit Committee comprises two Independent Non-Executive Directors, namely, Mr. Lau Sui Fai, Mr. Gao Xiang and a Non-Executive Director, Mr. Thong Kwee Chee. The Chairman of the Audit Committee, Mr. Lau Sui Fai, possesses expertise in accounting, auditing and finance. Under its terms of reference, the Audit Committee is mainly responsible for overseeing the Company's financial reporting system and internal procedures, reviewing the financial information of the Company and overseeing the relationship with external auditors. These include reviewing and recommending for the Board's approval the interim and the annual financial statements; reviewing the external auditors' independence, objectivity and the effectiveness of the audit process; and reviewing and recommending to the Board for approval the external auditor's remuneration and review of the effectiveness of the internal control system of the Group.

The committee had two meetings in 2009 and one meeting to date in 2010 with full attendance. The meetings were held together with the external auditors of the Company, the Chief Financial Officer, and the Financial Controller of the Company, to discuss auditing, internal control and financial reporting matters which include the review of the interim and annual financial statements.

Remuneration Committee

The Remuneration Committee comprises one Executive Director, one Non-Executive Director and three Independent Non-Executive Directors, namely, Mr. Zhu Xiaokun, Mr. Thong Kwee Chee, Mr. Gao Xiang, Mr. Lau Siu Fai and Mr. Li Zhengbang. Mr. Li Zhengbang is the Chairman of the Remuneration Committee.

The primary role of the Remuneration Committee is to make recommendation to the Board on the Company's policy and structure for remuneration of Directors and senior management. No Director will take part in any discussion on his own remuneration. Details of the fees of the Directors are set out in note 10 to the financial statements. The Company's remuneration policy is to maintain fair and competitive remuneration packages based on business needs and market practice. Factors such as market rate, an individual's qualification, experience, performance and expected workload are taken into account during the remuneration package determination process.

Remuneration Committee had one meeting in 2009 and one meeting to date in 2010.

The meetings were held to assess the performance of the directors and senior management, discuss and review the overall remuneration policy and structure. Recommendations have been made to the Board.

Nomination Committee

It comprises one Executive Director, one Non-Executive Director and three Independent Non-Executive Directors, namely, Mr. Zhu Xiaokun, Mr. Thong Kwee Chee, Mr. Gao Xiang, Mr. Li Zhengbang and Mr. Lau Siu Fai. Mr. Gao Xiang is the Chairman of the Nomination Committee.

The primary responsibility of the Nomination Committee is making recommendations to the Board on matters relating to the appointment of Directors and succession planning for Directors, and assessing the independence of the Independent Non-Executive Directors.

The Nomination Committee had one meeting in 2009 and one meeting to date in 2010.

The meeting were held to discuss and review the composition and structure of the Board and senior management.

The Executive Directors and Non-Executive Directors were appointed based on their qualification and experience in relation to the Group's business. The Independent Non-Executive Directors were appointed based on their professional qualifications and experience in their respective areas.

Directors' Responsibility for the Financial Statements

The Directors are responsible for overseeing the preparation of accounts for each financial period with a view to ensuring that such accounts give a true and fair view of the state of affairs of the Group and of the results and cash flow for that financial period. The Company's accounts are prepared in accordance with all relevant statutory requirements and applicable accounting standards. The Company has selected appropriate accounting policies and has applied them consistently based on prudent and reasonable judgments and estimates.

Internal Control

A sound internal control system enhances the effectiveness and efficiency of operations, ensures compliance with laws and regulations and mitigates the Group's business risk. The Board is responsible for the system of internal control of the Group and reviewing its effectiveness.

The Board and the Group's management hold meetings on a regular basis to review and evaluate the Group's business operations, production processes and financial reporting processes in order to achieve reasonable assurance of the following:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations

To maintain an effective internal control system that helps the Group to achieve its business objectives and safeguard its assets, the Group has implemented measures including: (i) establishing written policies and work flow for major operations and production cycles; (ii) having in place appropriate segregation of duties; and (iii) setting proper authorization levels.

The Board, through the Audit Committee, reviewed the internal control system of the Group for the year ended 31 December 2009 and considered that the system of internal control of the Group had been in place and had been functioning effectively.

External Auditors

The Group's external auditors are KPMG. In order to maintain their independence, objectivity and effectiveness in performing the audit services, the Audit Committee pre-approved all audit services and discussed with KPMG the nature and scope of the audit services.

During 2009, the remuneration paid or payable to KPMG in respect of statutory audit services was RMB2,026,000.

Model Code for Securities Transactions

The Group has adopted a code of conduct governing securities transactions by Directors in compliance with the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules (the "Model Code"). Following a specific enquiry, each of the Directors confirmed that he complied with the required standard set out in the Model Code and the Group's code of conduct governing securities transactions by Directors during the 2009.

The Group has also adopted a code of conduct governing securities transactions by employees who may possess or have access to price sensitive information.

Investor Relationship and Communication

The Board and senior management recognize the importance of communication with shareholders and accountability to shareholders. Annual and interim reports offer comprehensive operational and financial performance information to shareholders and the annual general meetings provide a forum for shareholders to make comments and raise concerns to the Board directly. The Group's senior management also maintains close communication with investors, analysts and the media by other channels including roadshows, briefings and individual meetings. The Group has set up its own website http://www.tggj.cn, which is updated on a regular basis, as a means to provide updated information on the Company to investors.

The Board is pleased to submit the annual report together with the consolidated financial statements for the year ended 31 December 2009 which have been audited by the Company's auditor KPMG and reviewed by the audit committee of the Company.

Principal Activities

The principal activities of the Company are the production and sales of HSS, HSS cutting tools and die steel. The principal activities and other particulars of the subsidiaries are set out in note 17 to the financial statements.

Financial Statements

The profit of the Group for the year ended 31 December 2009 and the state of the Company's and the Group's affairs as at that date are set out in the financial statements on pages 30 to 77.

Results and Appropriations

The results of the Group for the year ended 31 December 2009 are set out in the consolidated statement of comprehensive income on page 30.

The Board proposed a final dividend payment of RMB0.0534 per share for the financial year ended 31 December 2009 (2008: RMB0.0536).

Charitable Donations

Charitable donations made by the Group during the year amounted to RMB1,300,000 (2008: 2,107,000).

Property, Plant and Equipment

Details of the movements in the property, plant and equipment of the Group and the Company during the year are set out in note 14 to the financial statements.

Reserves

Details of movements in the reserves of the Company and of the Group during the year are set out in note 29 to the financial statements and in the consolidated statements of changes in equity, respectively.

Distributable Reserves

Distributable reserves of the Company as at 31 December 2009, calculated in accordance with the Companies Law (Cap. 22) (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, amounted to RMB894,902,000.

Pre-emptive Rights

There is no provision for pre-emptive rights under the Company's articles of association and there is no restriction against such rights under the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

Share Capital

Details of the movements in share capital of the Company during the year are set out in note 29 to the financial statements.

Directors

The Directors during the financial year were:

Executive Directors

Mr. Zhu Xiaokun
Mr. Zhu Zhihe
Mr. Zhu Mingyao
Mr. Yan Ronghua

Non-Executive Directors

Mr. Thong Kwee Chee

Independent Non-Executive Directors

Mr. Li Zhengbang
Mr. Gao Xiang
Mr. Lau Siu Fai

Directors will retire by rotation in accordance with the requirement of the Listing Rules in the annual general meetings. The Non-Executive Directors and Independent Non-Executive Directors are appointed for periods of three years.

The Company considers that Mr. Li Zhengbang, Mr. Gao Xiang and Mr. Lau Siu Fai are independent pursuant to the criteria set out in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules") and that a confirmation of independence has been received from each of them.

Directors' Interests and Short Positions in Shares, Underlying Shares and Debentures

As at 31 December 2009, the interests, long positions or short positions of the Directors and chief executive of the Company in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were recorded in the register required to be kept under Section 352 of the SFO, or which were notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") (set out in Appendix 10 of the Listing Rules) were as follows:

(a) Interests in the Company

Director's name	Interests	Ordinary shares held	Approximate attributable interest (%)
Mr. Zhu Xiaokun (Note)	Corporate interests	220,183,000(L)	52.49

Notes:

As at 31 December 2009,

(1) Tiangong Holdings Company Limited ("THCL") held 210,000,000 Ordinary shares. THCL was held as to 89.02% and 10.98% by Zhu Xiaokun and Yu Yumei, the spouse of Zhu Xiaokun, respectively. Zhu Xiaokun is deemed to be interested in the 210,000,000 Shares held by THCL.

(2) Silver Power (HK) Limited, which was wholly-owned by Zhu Xiaokun, held 10,183,000 Ordinary shares.

(L) represents long position

(b) Interests in the shares of associated corporation

Name of Director	Name of associated corporation	Nature of interests and capacity	Total Number of Shares	Approximate percentage of interests (%)
Zhu Xiaokun	THCL	Beneficial owner	44,511(L)	89.02
Yu Yumei	THCL	Beneficial owner	5,489(L)	10.98

(L) represents long position

Save as disclosed above, as at the annual report date, as far as the Company's directors are aware, none of the Company's directors and chief executive had any other interests, long positions or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations.

SUBSTANTIAL SHAREHOLDERS' INTERESTS

As at 31 December 2009, save for the Company's Directors or chief executives as disclosed above, the following persons have an interest or short position in the shares or the underlying shares of the Company which are required to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, which were recorded in the register required to be kept under Section 336 of the SFO:

Substantial shareholders' name	Ordinary shares	Approximate Attributable interest (%)
THCL (Note 1)	210,000,000(L)	50.06
Yu Yumei (Note 1)	210,000,000(L)	50.06
AIG Global Emerging Markets Fund II, LP.	21,000,000(L)	5.01
AIG GEM II G.P., L.P. (Note 2)	21,000,000(L)	5.01
AIG GEM II G.P., Co. (Note 2)	21,000,000(L)	5.01
AIG Capital Partners, Inc. (Note 2)	21,000,000(L)	5.01
AIG Global Asset Management Holdings Corp. (Note 2)	21,000,000(L)	5.01
AIG Capital Corporation (Note 2)	21,000,000(L)	5.01
AIG Asia Opportunity Fund II, L.P.	30,000,000(L)	7.15
AIG AOF II G.P., L.P. (Note 3)	30,000,000(L)	7.15
AIG Asian Opportunity II G.P. Ltd. (Note 3)	30,000,000(L)	7.15
AIG Global Investment Corporation (Asia) Ltd. (Note 3)	30,000,000(L)	7.15
American International Assurance Company (Bermuda) Limited (Note 3)	39,000,000(L)	9.30
American International Reinsurance Company, Ltd. (Note 4)	39,000,000(L)	9.30
AIG Life Holdings (International) LLC (Note 4)	39,000,000(L)	9.30
American International Group, Inc. (Note 5)	60,000,000(L)	14.30
Considine Jill m (Note 6)	60,000,000(L)	14.30
Feldberg B Chester (Note 6)	60,000,000(L)	14.30
Foshee L Douglas (Note 6)	60,000,000(L)	14.30
United State Treasury (Note 7)	60,000,000(L)	14.30

Notes:

(1) THCL is owned as to 89.02% by Mr Zhu Xiaokun and 10.98% by his spouse, Madam Yu Yumei.

(2) AIG GEM II G.P., L.P. is deemed to be interested in the Shares in the capacity as the general partner of AIG Global Emerging Markets Fund II, L.P. AIG GEM II G.P., Co. is deemed to be interested in the Shares in the capacity as the general partner of AIG GEM II G.P., L.P. AIG Capital Partners, Inc. is deemed to be interested in the deemed interests of AIG GEM II G.P., Co., its wholly-owned subsidiary. AIG Global Asset Management Holdings Corp. is deemed to be interested in the deemed interests of AIG Capital Partners, Inc., its wholly-owned subsidiary. AIG Capital Corporation is deemed to be interested in the deemed interests of AIG Global Asset Management Holdings Corp., its wholly-owned subsidiary.

(3) AIG AOF II G.P., L.P. is deemed to be interested in the Shares in the capacity as the general partner of AIG Asian Opportunity Fund II, L.P. AIG Asian Opportunity II G.P. Ltd. is deemed to be interested in the Shares in the capacity as the general partner of AIG AOF II G.P., L.P. AIG Global Investment Corporation (Asia) Ltd. is deemed to be interested in the deemed interests of AIG Asian Opportunity II G.P. Ltd., its wholly-owned subsidiary. American International Assurance Company (Bermuda) Limited holds 9,000,000 Shares and is also deemed to be interested in the deemed interests of AIG Global Investment Corporation (Asia) Ltd., its wholly-owned subsidiary.

(4) American International Reinsurance Company, Ltd. is deemed to be interested in the Shares and the deemed interests of American International Assurance Company (Bermuda) Limited, its wholly-owned subsidiary. AIG Life Holdings (International) LLC. is deemed to be interested in the deemed interests of American International Reinsurance Company, Ltd., its wholly-owned subsidiary.

(5) American International Group, Inc. is deemed to be interested in the Shares and the deemed interests of AIG Capital Corporation and AIG Life Holdings (International) LLC.

(6) Considine Jill m., Feldberg B Chester and Foshee L Douglas reported that they were deemed to be interested in the shares as they were joint trustees (together another person) of AIG Credit Facility Trust.

(7) United State Treasury reported that it was deemed to be interested in the shares as it was a beneficial of the AIG Credit Facility Trust.

Arrangements to Acquire Shares or Debentures

Save as disclosed above, at no time during the year was the Company or any of its subsidiaries, holding companies or fellow subsidiaries a party to any arrangements to enable a Director of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

Biographical Details of Directors and Senior Management

Brief biographical details of the Directors and the senior management are set out on pages 14 to 16.

Share Options Scheme

The Company adopted a share options scheme, but the Company has not granted any share options.

Directors' and Controlling Shareholders' Interests in Contracts

Save as disclosed under the heading "Connected transactions" below and "Related party transactions" in note 32 to the financial statements, no Director or controlling shareholder or any of their respective subsidiaries had a material interest, either directly or indirectly, in any contract of significance to the business of the Group, to which the Company, or any of its holding companies, subsidiaries or fellow subsidiaries was a part, during the year.

During the year, no contract of significance for the provision of services to the Group by a controlling shareholder or any of its subsidiaries was made.

Directors' Service Contracts

No Director of the Company proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries, which is not determinable by the employing company within one year without payment of compensation (other than statutory compensation).

Purchase, Sales or Redemption of Shares

During the year ended 31 December 2009, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of its securities.

Corporate Governance

During the year ended 31 December 2009, the Company has, so far where applicable, met the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules").

Audit Committee

The Audit Committee comprises of three non-executive directors, two of which are independent non-executive directors. The Audit Committee held a meeting on 8 April 2010 to consider and review the annual results of the Group and to give their opinion and recommendations to the Board. The Audit Committee considers that the 2009 annual results of the Company have complied with the applicable accounting standards and the Company has made appropriate disclosure thereof.

Major Customers and Suppliers

The information in respect of the Group's sales and purchases attributable to the major customers and suppliers during the financial year ended 31 December 2009 is as follows:

	Percentage of the Group's total	
	Sales	**Purchases**
The largest customer/supplier	7.86%	5.91%
Five largest customers/suppliers in aggregate	27.57%	21.61%

At no time during the year had the Directors, their associates or any shareholder of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interest in these major customers and suppliers.

Connected Transactions

Certain related party transactions as disclosed in note 32 to the financial statements also constituted connected transactions under the Listing Rules, and are required to be disclosed in accordance with Chapter 14A of the Listing Rules. The following transactions between certain connected parties (as defined in the Listing Rules) and the Company have been entered into and/or are ongoing for which relevant disclosure had been made by the Company in the Prospectus.

One-off Connected Transactions

No one-off connected transactions occurred after the listing of the Company.

Continuing Connected Transactions

The following transactions fall under the de minimis provision set forth in rule 14.A33(3) of the listing rule and is therefore exempt from reporting, announcement and independent shareholders' approval.

Lease of office premises

Jiangsu Tiangong Tools Company Limited ("TG Tools"), a wholly-owned subsidiary of the Company and Jiangsu Tiangong Group Company Limited ("TG Group"), entered into a lease agreement dated 28 February 2007, by which TG Group leased to TG Tools the office premises at Tiangong building for a term commencing from 1 January 2007 to 31 December 2009 with fixed annual rentals of RMB600,000, which was determined under normal commercial terms and with reference to an independent valuation. The rental is payable on an annual basis. During the year, the Group incurred rentals of office premises to TG Group which amounted to RMB600,000. On 6 January 2010. TG Tools and TG Group renewed the lease agreement for a term commencing from 1 January 2010 to 31 December 2012 with an annual rental of RMB600,000, which was determined under normal commercial terms with reference to an independent Valuer.

TG Group, a collective enterprise established under the laws of PRC, is wholly owned by Mr. Zhu Xiaokun and Madam Yu Yumei. Given that Mr. Zhu Xiaokun is an Executive Director of the Company and Mr. Zhu Xiaokun and Madam Yu Yumei are the controlling shareholders of the Company, TG Group, an associate under the Listing Rules, is a connected person by virtue of Rule 14A.11 (4) of the Listing Rules.

Amenity Facilities Provision Agreement

TG Tools, Tiangong Aihe Special Steel Company Limited ("TG Aihe"), Danyang Tianfa Forging Company Limited ("Tianfa Forging"), Danyang Tianji Tools Packaging Company Limited ("Tianji Packaging") and TG Group, entered into an agreement dated 7 July 2007, by which TG Group's amenity facilities will be open to employees of TG Tools, TG Aihe, Tianfa Forging and Tianji Packaging for a fixed annual amenity fee of RMB400,000 for a term commencing from 1 July 2007 to 31 December 2009. The fixed annual fee was determined under normal commercial terms and with reference to the depreciation expenses and maintenance costs of facilities. The rental is payable on an annual basis. On 6 January 2010. TG Tools and TG Group renewed the lease agreement for a term commencing from 1 January 2010 to 31 December 2012 with an annual rental of RMB400,000, which was determined under normal commercial terms with reference to an independent Valuer. During the year, the Group incurred amenity fee of RMB400,000 to TG Group. TG Tools, TG Aihe, Tianfa Forging and Tianji Packaging are all wholly-owned subsidiaries of the Company. TG Group, as defined above, is an associate under the Listing Rules and is a connected person by virtue of Rule 14A.11 (4) of the Listing Rules.

The Company has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules with regard to the above Continuing Connected Transactions.

The Independent Non-executive Directors have reviewed the above non-exempt continuing connected transactions of the Group and have confirmed that these transactions have been entered into:

(i) in the ordinary and usual course of business of the Group;

(ii) on normal commercial terms;

(iii) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; and

(iv) have not exceeded the respective cap amounts set out in the relevant agreements referred to above.

The auditors of the Company have reported to the Directors that during the financial year:

(i) the above continuing connected transactions have been approved by the board of Directors;

(ii) the above continuing connected transactions have been entered into in accordance with the terms of the agreements governing such transactions; and

(iii) the respective cap amounts set out in the relevant agreements referred to above have not been exceeded.

Financial Information Summary

A financial summary of the Group is set out on page 78 of this annual report.

Directors' Interests in Competing Business

During the year and up to the date of this annual report, none of the Directors are considered to have interests in any business which competes or is likely to compete, either directly or indirectly, with the businesses of the Group, pursuant to the Listing Rules.

Management Contracts

No contracts concerning the management and/or administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

Sufficiency of Public Float

Based on the information that is publicly available to the Company and within the knowledge of the Directors of the Company as at the date of this annual report, the Company has maintained sufficient public float as required under the Listing Rules.

Auditors

The financial statements for the year were audited by KPMG who will retire at the conclusion of the forthcoming annual general meeting and, being eligible, will offer themselves for re-appointment.

On behalf of the Board of Directors

Tiangong International Company Limited
Zhu Xiaokun
Chairman

Hong Kong, 13 April 2010

Independent auditor's report to the shareholders of
Tiangong International Company Limited
(Incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of Tiangong International Company Limited (the "Company") set out on pages 30 to 77, which comprise the consolidated and company balance sheets as at 31 December 2009, and the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility

The directors of the Company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the disclosure requirements of the Hong Kong Companies Ordinance. The responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the content of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2009 and of the Group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG
Certified Public Accountants
8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

13 April 2010

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2009

	Note	2009 RMB'000	2008 RMB'000
Revenue	5	**1,323,752**	1,993,269
Cost of sales		**(1,062,867)**	(1,673,566)
Gross profit		**260,885**	319,703
Other income	7	**10,970**	6,068
Distribution expenses		**(29,573)**	(50,106)
Administrative expenses		**(60,810)**	(61,155)
Other expenses		**(14,839)**	(7,843)
Profit from operations		**166,633**	206,667
Finance income		**2,736**	4,607
Finance expenses		**(50,049)**	(96,162)
Net finance costs	8(i)	**(47,313)**	(91,555)
Profit before income tax	8	**119,320**	115,112
Income tax expense	9	**(7,242)**	(2,602)
Profit and total comprehensive income for the year		**112,078**	112,510
Attributable to:			
Equity holders of the Company		**112,078**	114,643
Non-controlling interest		**—**	(2,133)
Profit and total comprehensive income for the year		**112,078**	112,510
Earnings per share	13		
Basic (RMB)		**0.27**	0.27

The notes on Page 35 to 77 form part of these financial statements. Details of dividends payable to equity shareholders of the Company attributable to the profit for the year are set out in Note 29(b).

	Note	2009 RMB'000	2008 RMB'000
Non-current assets			
Property, plant and equipment	14	**1,348,285**	1,093,735
Lease prepayments	15	**62,639**	97,106
Goodwill	16	**21,959**	21,959
Other investments	18	**10,000**	10,000
Deferred tax assets	28(b)	**10,032**	5,476
		1,452,915	1,228,276
Current assets			
Inventories	19	**1,252,748**	1,111,282
Trade and other receivables	20	**656,959**	616,901
Pledged deposits	21	**119,358**	63,600
Time deposits	22	**192,000**	115,000
Cash and cash equivalents	23	**63,467**	96,021
Assets classified as held for sale	24	**64,778**	—
		2,349,310	2,002,804
Current liabilities			
Interest-bearing borrowings	25	**1,379,700**	1,093,865
Trade and other payables	26	**645,124**	442,257
Income tax payables	28(a)	**14,964**	13,383
Deferred income	27	**1,162**	—
		2,040,950	1,549,505
Net current assets		**308,360**	453,299
Total assets less current liabilities		**1,761,275**	1,681,575
Non-current liabilities			
Interest-bearing borrowings	25	**177,000**	190,000
Deferred income	27	**8,351**	9,900
Deferred tax liabilities	28(c)	**8,202**	3,546
		193,553	203,446
Net assets		**1,567,722**	1,478,129
Capital and reserves			
Share capital	29(a),(c)	**31,806**	31,806
Reserves	29(a),(d)	**1,535,916**	1,446,323
Total equity		**1,567,722**	1,478,129

Approved and authorised for issue by the board of directors on 13 April 2010.

Zhu Xiao Kun	**Yan Rong Hua**
Director	*Director*

The notes on Page 35 to 77 form part of these financial statements.

Balance Sheet

As at 31 December 2009

	Note	2009 RMB'000	2008 RMB'000
Non-current assets			
Property, plant and equipment	14	**107**	136
Interests in subsidiaries	17	**928,127**	1,111,379
		928,234	1,111,515
Current assets			
Trade and other receivables	20	**–**	1,239
Cash and cash equivalents	23	**1,771**	3,740
		1,771	4,979
Current liabilities			
Interest-bearing borrowings	25	**–**	170,865
Trade and other payables	26	**3,297**	10,055
		3,297	180,920
Net current liabilities		**(1,526)**	(175,941)
Net assets		**926,708**	935,574
Capital and reserves			
Share capital	29(a),(c)	**31,806**	31,806
Reserves	29(a),(d)	**894,902**	903,768
Total equity		**926,708**	935,574

Approved and authorised for issue by the board of directors on 13 April 2010.

Zhu Xiao Kun
Director

Yan Rong Hua
Director

The notes on Page 35 to 77 form part of these financial statements.

	Attributable to equity holders of the Company								
	Share capital RMB'000 (Note 29(c))	Share premium RMB'000 (Note 29(d))	Capital reserve RMB'000 (Note 29(d))	Merger reserve RMB'000 (Note 29(d))	PRC statutory reserve RMB'000 (Note 29(d))	Retained earnings RMB'000	Total RMB'000	Non-controlling interest RMB'000	Total equity RMB'000
At 1 January 2008	31,806	886,566	56,998	91,925	67,085	229,106	1,363,486	20,878	1,384,364
Acquisition of non-controlling interest	–	–	–	–	–	–	–	(18,745)	(18,745)
Total comprehensive income for the year	–	–	–	–	–	114,643	114,643	(2,133)	112,510
Transfer to reserve	–	–	–	–	17,962	(17,962)	–	–	–
At 31 December 2008	31,806	886,566	56,998	91,925	85,047	325,787	1,478,129	–	1,478,129
Dividends approved in respect of the previous year (see Note 29(b))	–	–	–	–	–	(22,485)	(22,485)	–	(22,485)
Total comprehensive income for the year	–	–	–	–	–	112,078	112,078	–	112,078
Transfer to reserve	–	–	–	–	22,635	(22,635)	–	–	–
At 31 December 2009	31,806	886,566	56,998	91,925	107,682	392,745	1,567,722	–	1,567,722

The notes on Page 35 to 77 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2009

	2009 RMB'000	2008 RMB'000
Operating activities		
Profit before income tax	**119,320**	115,112
Adjustments for:		
Depreciation	**69,131**	58,089
Amortisation of lease prepayments	**2,001**	1,958
Interest income	**(2,736)**	(4,607)
Interest on bank loans	**50,049**	70,464
Gain on disposal of property, plant and equipment	**(350)**	(96)
Gain on acquisition of non-controlling interest	**—**	(2,339)
Operating profit before changes in working capital	**237,415**	238,581
Change in inventories	**(141,466)**	(226,246)
Change in trade and other receivables	**(37,861)**	(93,989)
Change in trade and other payables	**185,798**	45,220
Change in deferred income	**(387)**	—
Income tax paid	**(5,561)**	(176)
Net cash generated from operating activities	**237,938**	(76,610)
Investing activities		
Interest received	**2,736**	4,607
Proceeds from disposal of property, plant and equipment	**24,327**	377
Payment for the purchase of property, plant and equipment	**(331,307)**	(360,991)
Payment for lease prepayments	**—**	(33,773)
Net payment for acquisition of time deposits	**(77,000)**	(115,000)
Net payment for acquisition of pledged deposits	**(55,758)**	22,697
Payment for acquisition of non-controlling interest	**—**	(16,406)
Net cash used in investing activities	**(437,002)**	(498,489)
Financing activities		
Proceeds from new interest-bearing borrowings	**1,896,900**	2,021,191
Repayment of interest-bearing borrowings	**(1,624,065)**	(1,436,295)
Interest paid	**(83,840)**	(70,464)
Dividends paid to equity shareholders of the Company	**(22,485)**	—
Net cash generated from financing activities	**166,510**	514,432
Net decrease in cash and cash equivalents	**(32,554)**	(60,667)
Cash and cash equivalents at 1 January	**96,021**	156,688
Cash and cash equivalents at 31 December	**63,467**	96,021

The notes on Page 35 to 77 form part of these financial statements.

1 Reporting entity

Tiangong International Company Limited (the "Company") was incorporated in the Cayman Islands on 14 August 2006 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961 as consolidated and revised) of the Cayman Islands. The consolidated financial statements of the Company as at and for the year ended 31 December 2009 comprise the Company and its subsidiaries (together referred to as the "Group"). The Company's shares have been listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 26 July 2007.

2 Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs") promulgated by the International Accounting Standards Board ("IASB"). IFRSs include International Accounting Standards and interpretations. These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

The IASB has issued certain new and revised IFRSs that are first effective or available for early adoption for the current accounting period of the Group and the Company. Note 4 provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statement.

(b) Basis of measurement

These financial statements have been prepared on historical cost basis.

These consolidated financial statements are presented in Renminbi ("RMB"). Except for per share data, financial information presented in RMB has been rounded to the nearest thousand.

(c) Accounting estimates and judgements

The preparation of the financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is discussed in Note 33.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, and have been applied consistently by Group entities, except as explained in Note 4, which addresses changes in accounting policies.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see Note 3(h)), unless the investment is classified as held for sale (or included in a disposal group that is classified as held for sale).

(ii) Transaction eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(iii) Non-controlling interests

Non-controlling interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Company, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity holders of the Company. Non-controlling interests in the results of the Group are presented on the face of the consolidated statement of comprehensive income as an allocation of the total comprehensive income for the year between non-controlling interests and the equity holders of the Company.

Where losses applicable to a non-controlling interest exceed its interest in the equity of a subsidiary, the excess, and any further losses applicable to the non-controlling interest, are charged against the Group's interest except to the extent that the non-controlling interest has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the non-controlling interest's share of losses previously absorbed by the Group has been recovered.

(b) Goodwill

Goodwill arising on the acquisition of a non-controlling interest in a subsidiary represents the excess of the cost of the investment over the carrying amount of the interest in the net assets acquired at the date of exchange. Negative goodwill is recognised immediately in the consolidated statement of comprehensive income.

Goodwill is measured at cost less accumulated impairment losses (see Note 3(h)).

3 Significant accounting policies (continued)

(c) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period.

Non-monetary assets and liabilities denominated in foreign currencies that are measured in terms of historical costs are translated using the foreign exchange rates ruling at the transaction date.

Foreign currency differences arising on retranslation are recognised in the consolidated statement of comprehensive income.

(ii) Foreign operations

The assets and liabilities of foreign operations are translated to RMB at exchange rates at the reporting date. The income and expenses of foreign operations are translated to RMB at exchange rates at the dates of the transactions.

The resulting foreign currency differences are recognised directly in a separate component of equity, foreign currency translation reserve. When a foreign operation is disposed of, in part or in full, the relevant amount in the foreign currency translation reserve is transferred to the consolidated statement of comprehensive income.

(d) Other investments in equity securities

The Group's and the Company's policies for investments in equity securities, other than investments in subsidiaries, associates and jointly controlled entities, are as follows:

Investments in equity securities are initially stated at fair value, which is their transaction price unless fair value can be more reliably estimated using valuation techniques whose variables include only data from observable markets. Cost includes attributable transaction costs.

The Group's investments in equity securities are classified as available-for-sale financial assets. The Group's investments in equity securities do not have a quoted market price in an active market and the relevant fair value cannot be reliably measured, and therefore are recognised in the balance sheet at cost less impairment losses (see Note 3(h)).

Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments or they expire.

3 Significant accounting policies (continued)

(e) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses (see Note 3(h)).

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, and the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs (see Note 4). Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised net in the consolidated statement of comprehensive income.

(ii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in the consolidated statement of comprehensive income as incurred.

(iii) Depreciation

Depreciation of an asset begins when it is available to use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

Depreciation is calculated over the depreciable amount, which is the cost of an asset, or other amount substituted for cost, less its residual value.

Depreciation is recognised in the consolidated statement of comprehensive income on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets are depreciated over the shorter of the lease term and their useful lives.

The estimated useful lives for the current and comparative periods are as follows:

- Plant and buildings 20 years
- Machinery 5–20 years
- Motor vehicles 8 years
- Office equipment and others 5 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

(f) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Other leases are operating leases and the leased assets are not recognised on the Group's balance sheet.

3 Significant accounting policies (continued)

(g) Inventories

Inventories are measured at the lower of cost and net realisable value.

The cost of inventories is based on the weighted average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(h) Impairment

(i) Financial assets

A financial asset not carried at fair value through profit and loss is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Group on terms that the Group would not consider otherwise, indications that a debtor or issuer will enter bankruptcy, the disappearance of an active market for a security. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

For unquoted equity securities carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in the consolidated statement of comprehensive income.

3 Significant accounting policies (continued)

(h) Impairment (continued)

(i) Financial assets (continued)

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost, the reversal is recognised in the consolidated statement of comprehensive income. For unquoted equity securities carried at cost, impairment losses are not reversed.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually at each reporting date whether or not there is any indication of impairment.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to cash-generating units that are expected to benefit from the synergies of the combination.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in the consolidated statement of comprehensive income. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(i) Trade and other receivables

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less allowance for impairment of doubtful debts (see Note 3(h)), except for the Company's receivables from its subsidiaries without any fixed repayment term or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less allowance for impairment of doubtful debts.

(j) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

3 Significant accounting policies (continued)

(k) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between the amount initially recognised and redemption value being recognised in the consolidated statement of comprehensive income over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

(l) Trade and other payables

Trade and other payables are initially recognised at fair value and subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(m) Employee benefits

(i) Short term employee benefits

Salaries, annual bonuses, and staff welfare are accrued in the year in which the associated services are rendered by employees of the Group.

(ii) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the consolidated statement of comprehensive income when they are due, except to the extent that they are included in the cost of inventories not yet recognised as an expense.

(n) Provisions and contingent liabilities

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(o) Revenue

Revenue from the sale of goods in the course of ordinary activities is measured at the fair value of the consideration received or receivable, net of returns, value added tax, trade discounts and volume rebates. Revenue is recognised when persuasive evidence exists, usually in the form of an executed sales agreement, that the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably. If it is probable that discounts will be granted and the amount can be measured reliably, then the discount is recognised as a reduction of revenue as the sales are recognised.

3 Significant accounting policies (continued)

(p) Government grants

Government grants are recognised initially as deferred income when there is reasonable assurance that they will be received and the Group will comply with the conditions associated with the grant. Grants that compensate the Group for expenses incurred are recognised in the consolidated statement of comprehensive income on a systematic basis in the same periods in which the expenses are recognised. Grants that compensate the Group for the cost of an asset are recognised in the consolidated statement of comprehensive income on a systematic basis over the useful life of the asset.

(q) Lease payments

Payments made under operating leases are recognised in the consolidated statement of comprehensive income on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Lease prepayments in the consolidated balance sheet represent the cost of land use rights paid to the People's Republic of China (the "PRC") land bureau. Land use rights are carried at cost less accumulated amortisation and accumulated impairment losses (see Note 3(h)). Amortisation is charged to the consolidated statement of comprehensive income on a straight-line basis over the respective periods of the rights.

(r) Finance income and expenses

Finance income represents interest income from deposits placed with banks, which is recognised as it accrues in the consolidated statement of comprehensive income, using the effective interest method.

Finance costs comprise interest expense on borrowings and net foreign currency losses that are recognised in the consolidated statement of comprehensive income. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in the consolidated statement of comprehensive income using the effective interest method.

Foreign currency gains and losses are reported on a net basis.

(s) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the consolidated statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In additional, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

3 Significant accounting policies (continued)

(s) Income tax (continued)

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for deductible temporary differences to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of dividends are recognised at the same time that the liability to pay the related dividend is recognised.

(t) Dividends distributed

Dividends distributed are recognised as a liability in the period in which they are declared.

(u) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the comprehensive income attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the comprehensive income attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

(v) Segment reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the Group's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of products and services, the nature of production processes, the type or class of customers, the methods used to distribute the products or provide the services, and the nature of the regulatory environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

3 Significant accounting policies (continued)

(w) Related parties

For the purpose of these financial statements, a party is considered to be related to the Group if:

(i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Group or exercise significant influence over the Group in making financial and operating policy decisions, or has joint control over the Group;

(ii) the Group and the party are subject to common control;

(iii) the party is an associate of the Group or a joint venture in which the Group is a venturer;

(iv) the party is a member of key management personnel of the Group or the Group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;

(v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or

(vi) the party is a post-employment benefit plan which is for the benefit of employees of the Group or of any entity that is a related party of the Group.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

(x) Non-current assets held for sale

A non-current asset (or disposal group) is classified as held for sale if it is highly probable that its carrying amount will be recovered through a sale transaction rather than through continuing use and the asset (or disposal group) is available for sale in its present condition. A disposal group is a group of assets to be disposed of together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction.

Immediately before classification as held for sale, the measurement of the non-current assets (and all individual assets and liabilities in a disposal group) is brought up-to-date in accordance with the accounting policies before the classification. Then, on initial classification as held for sale and until disposal, the non-current assets (except for certain assets as explained below), or disposal groups, are recognised at the lower of their carrying amount and fair value less costs to sell.

Impairment losses on initial classification as held for sale, and on subsequent remeasurement while held for sale, are recognised in the consolidated statement of comprehensive income. As long as a non-current asset is classified as held for sale or is included in a disposal group that is classified as held for sale, the non-current asset is not depreciated or amortised.

3 Significant accounting policies (continued)

(y) New standards and interpretations not yet adopted

Up to the date of this report, the IASB has issued the following new standards, amendments to standards and interpretations which are not yet effective for the year ended 31 December 2009. The Group has not early adopted these new standards, amendments to standards and interpretations in the preparation of the financial statements.

	Effective for accounting periods beginning on or after (unless specified)
Improvements to IFRSs 2008 (only the amendments to IFRS 5)	1 July 2009
IFRS 1 (revised 2008), *First-time adoption of International Financial Reporting Standards*	1 July 2009
IFRS 3 (revised 2008), *Business combination*	Applied to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009
Amended IAS 27, *Consolidated and separate financial statements*	1 July 2009
Amendment to IAS 39, *Financial instruments: Recognition and measurement — Eligible hedged items*	1 July 2009
IFRIC 17, *Distributions of non-cash assets to owners*	1 July 2009
Improvements to IFRSs 2009	1 July 2009 or 1 January 2010
Amendment to IFRS 1, *First-time adoption of International Financial Reporting Standards — Additional exemptions for first-time adopters*	1 January 2010
Amendment to IFRS 2, *Share-based payment — Group cash-settled share-based payment transactions*	1 January 2010
Amendment to IAS 32, *Financial instruments: Presentation — Classification of rights issues*	1 February 2010
IFRIC 19, *Extinguishing financial liabilities with equity instruments*	1 July 2010

3 Significant accounting policies (continued)

(y) New standards and interpretations not yet adopted (continued)

	Effective for accounting periods beginning on or after (unless specified)
Amendment to IFRS 1, *First-time adoption of International Financial Reporting Standards — Limited exemption from comparative IFRS 7 disclosures for first-time adopters*	1 July 2010
Revised IAS 24, *Related party disclosures*	1 January 2011
Amendments to IFRIC 14, IAS 19 — *The limit on a defined benefit asset, minimum funding requirements and their interaction — Prepayments of a minimum funding requirement*	1 January 2011
IFRS 9, *Financial instruments*, Basis for conclusions on IFRS 9, and Amendments to other IFRSs and guidance on IFRS 9	1 January 2013

The Group is in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the company's results of operations and financial position.

4 Changes in accounting policies

The IASB has issued one new IFRS, a number of amendments to IFRSs and new Interpretations that are first effective for the current accounting period of the Group. Of these, the following developments are relevant to the Group's financial statements:

- IFRS 8, *Operating segments*
- IAS 1 (revised 2007), *Presentation of financial statements*
- Improvements to IFRSs (2008)
- Amendment to IAS 27, *Consolidated and separate financial statements — cost of an investment in a subsidiary, jointly controlled entity or associate*
- IAS 23 (revised 2007), *Borrowing costs*

4 Changes in accounting policies (continued)

The "Improvements to IFRSs (2008)" comprise a number of minor and non-urgent amendments to a range of IFRSs which the IASB has issued as an omnibus batch of amendments. The amendments have not resulted in any significant changes to the Group's accounting policies. The impact of the remainder of these developments is as follows:

(a) IFRS 8 requires segment disclosure to be based on the way that the Group's chief operating decision maker regards and manages the Group, with the amounts reported for each reportable segment being the measures reported to the Group's chief operating decision maker for the purposes of assessing segment performance and making decisions about operating matters. This contrasts with the presentation of segment information in prior years which was based on a disaggregation of the Group's financial statements into segments based on related products and services and on geographical areas. The adoption of IFRS 8 has resulted in the presentation of segment information in a manner that is more consistent with internal reporting provided to the Group's most senior executive management (see Note 4). Corresponding amounts have also been provided on a basis consistent with the revised segment information.

(b) As a result of the adoption of IAS 1 (revised 2007), details of changes in equity during the period arising from transactions with equity holders in their capacity as such have been presented separately from all other income and expenses in a revised consolidated statement of changes in equity. All other items of income and expense are presented in the consolidated statement of comprehensive income, if they are recognised as part of profit or loss for the period, or otherwise in a new primary statement, the consolidated statement of comprehensive income. Corresponding amounts have been restated to conform to the new presentation. This change in presentation has no effect on reported profit or loss, total income and expense or net assets for any period presented.

(c) The amendment to IAS 27 has removed the requirement that dividends out of pre-acquisition profits should be recognised as a reduction in the carrying amount of the investment in the investee, rather than as income. As a result, as from 1 January 2009 all dividends receivable from subsidiaries, associates and jointly controlled entities, whether out of pre- or post-acquisition profits, will be recognised in the Company's statement of comprehensive income and the carrying amount of the investment in the investee will not be reduced unless that carrying amount is assessed to be impaired as a result of the investee declaring the dividend. In such cases, in addition to recognising dividend income in statement of comprehensive income, the Company would recognise an impairment loss. In accordance with the transitional provisions in the amendment, this new policy will be applied prospectively to any dividends receivable in the current or future periods and previous periods have not been restated.

(d) As a result of the adoption of IAS 23 (revised 2007), in respect of borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009, the Group capitalises borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Previously the Group immediately recognised all borrowing costs as an expense. This change in accounting policy was due to the prospective adoption of IAS 23 (revised 2007) in accordance with the transitional provisions of this standard; comparative figures have not been restated. The Group has capitalised borrowing costs with respect to property, plant and equipment under construction. (see Note 3(e) and 8(i)).

The Group or the Company has not applied any new standard or interpretation that is not yet effective for the current accounting period (see Note 3(y)).

5 Revenue

Revenue represents mainly the sales value of high alloy steel, including high speed steel ("HSS") and die steel ("DS"), and HSS cutting tools after eliminating intercompany transactions. The sales value of goods sold is stated after allowances for goods returned and deduction of any trade discounts, and excludes value added tax or other sales taxes.

6 Segment reporting

The Group manages its business by divisions, which are mainly organised by business lines. On first-time adoption of IFRS 8, *Operating segments* and in a manner consistent with the way in which information is reported internally to the Group's most senior executive management for the purpose of resource allocation and performance assessment, the Group has identified the following three reportable segments. No operating segments have been aggregated to form the following reportable segments.

— *High speed steel ("HSS")* The HSS segment manufactures and sells high speed steel for the steel industry.

— *HSS cutting tools* The HSS cutting tools segment manufactures and sells HSS cutting tools for the tool industry.

— *Die steel ("DS")* The DS segment manufactures and sells die steel for the steel industry.

(a) Segment results, assets and liabilities

In accordance with IFRS 8, segment information disclosed has been prepared in a manner consistent with the information used by the Group's most senior executive management for the purpose of assessing segment performance and allocating resources between segments. In this regard, the Group's senior executive management monitors the results, assets and liabilities attributable to each reportable segment on the following bases:

Segment assets include all tangible, intangible assets and current assets with the exception of other investments, pledged deposits, time deposits, cash and cash equivalents, deferred tax assets and other corporate assets. Segment liabilities include trade and bills payables, non-trade payables and accrued expenses attributable to the manufacturing and sales activities of the individual segments.

Revenue and expenses are allocated to the reportable segments with reference to sales generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

The measure used for reporting segment profit is "adjusted EBIT", i.e. "adjusted earnings before interest and taxes", where "interest" is regarded as net finance costs. To arrive at adjusted EBIT the Group's earnings are further adjusted for items not specifically attributed to individual segments, such as directors' and auditor's remuneration and other administrative expenses.

In addition to receiving segment information concerning adjusted EBIT, management is provided with segment information concerning revenue (including inter segment sales), interest income and expense from cash balances and borrowings, depreciation and amortisation used by the segments in their operations.

6 Segment reporting (continued)

(a) Segment results, assets and liabilities (continued)

Information regarding the Group's reportable segments as provided to the Group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the years ended 31 December 2009 and 2008 is set out below.

	Year ended and as at 31 December 2009				
	HSS RMB'000	HSS cutting tools RMB'000	DS RMB'000	Others* RMB'000	Total RMB'000
Revenue from external customers	**415,571**	**380,886**	**450,327**	**76,968**	**1,323,752**
Inter-segment revenue	**144,305**	**—**	**—**	**—**	**144,305**
Reportable segment revenue	**559,876**	**380,886**	**450,327**	**76,968**	**1,468,057**
Reportable segment profit (adjusted EBIT)	**80,161**	**50,318**	**100,078**	**755**	**231,312**
Reportable segment assets	**872,295**	**979,294**	**1,488,068**	**41,559**	**3,381,216**
Reportable segment liabilities	**209,238**	**162,873**	**228,972**	**41,448**	**642,531**

	Year ended and as at 31 December 2008				
	HSS RMB'000	HSS cutting tools RMB'000	DS RMB'000	Others RMB'000	Total RMB'000
Revenue from external customers	815,316	658,061	519,892	—	1,993,269
Inter-segment revenue	330,590	—	—	—	330,590
Reportable segment revenue	1,145,906	658,061	519,892	—	2,323,859
Reportable segment profit (adjusted EBIT)	135,893	67,366	66,338	—	269,597
Reportable segment assets	1,022,031	868,464	1,034,816	—	2,925,311
Reportable segment liabilities	220,496	75,574	136,966	—	433,036

* Revenues from segments below the quantitative thresholds are mainly attributable to the business of selling chemical products.

6 Segment reporting (continued)

(b) Reconciliations of reportable segment revenue, profit or loss, assets and liabilities

	2009 RMB'000	2008 RMB'000
Revenue		
Reportable segment revenue	**1,391,089**	2,323,859
Other revenue	**76,968**	—
Elimination of inter-segment revenue	**(144,305)**	(330,590)
Consolidated revenue	**1,323,752**	1,993,269

	2009 RMB'000	2008 RMB'000
Profit		
Reportable segment profit	**230,557**	269,597
Other profit	**755**	—
	231,312	269,597
Net finance costs	**(47,313)**	(91,555)
Other unallocated head office and corporate expenses	**(64,679)**	(62,930)
Consolidated profit before income tax	**119,320**	115,112

	2009 RMB'000	2008 RMB'000
Assets		
Reportable segment assets	**3,339,657**	2,925,311
Other assets	**41,559**	—
	3,381,216	2,925,311
Other investments	**10,000**	10,000
Deferred tax assets	**10,032**	5,476
Pledged deposits	**119,358**	63,600
Time deposits	**192,000**	115,000
Cash and cash equivalents	**63,467**	96,021
Other unallocated head office and corporate assets	**26,152**	15,672
Consolidated total assets	**3,802,225**	3,231,080

6 Segment reporting (continued)

(b) Reconciliations of reportable segment revenue, profit or loss, assets and liabilities (continued)

	2009 RMB'000	2008 RMB'000
Liabilities		
Reportable segment liabilities	**601,083**	433,036
Other liabilities	**41,448**	—
	642,531	433,036
Interest-bearing borrowings	**1,556,700**	1,283,865
Income tax payables	**14,964**	13,383
Deferred tax liabilities	**8,202**	3,546
Other unallocated head office and corporate liabilities	**12,106**	19,121
Consolidated total liabilities	**2,234,503**	1,752,951

(c) Geographical information

The Group's business is managed on a worldwide basis, but participates in four principal economic environments, the PRC, North America, Europe and Asia (other than the PRC).

In presenting geographical information, segment revenue is based on the geographical location of customers. Substantially all of the Group's assets and liabilities are located in the PRC and accordingly, no geographical analysis of segment assets, liabilities and capital expenditure is provided.

	2009 RMB'000	2008 RMB'000
Revenue		
The PRC	**921,827**	1,007,715
North America	**195,345**	365,148
Europe	**118,275**	376,136
Asia (other than the PRC)	**78,490**	222,774
Others	**9,815**	21,496
Total	**1,323,752**	1,993,269

7 Other income

	2009 RMB'000	2008 RMB'000
Government grants*	**10,158**	3,423
Net gain on disposal of property, plant and equipment	**350**	96
Gain on acquisition of non-controlling interest	**—**	2,339
Others	**462**	210
	10,970	6,068

* Jiangsu Tiangong Tools Company Limited ("TG Tools") received unconditional grants amounting to RMB9,771,000 (2008: RMB3,423,000) from the local government in Danyang concerning the encouragement of its development and recognised amortisation of government grants related to assets of RMB387,000 during 2009 (see Note 27).

8 Profit before income tax

Profit before income tax is arrived at after charging/(crediting):

(i) Net finance cost

	2009 RMB'000	2008 RMB'000
Interest income	**(2,736)**	(4,607)
Finance income	**(2,736)**	(4,607)
Interest on bank loans	**77,363**	70,464
Less: interest capitalised into property, plant and equipment under construction*	**(27,860)**	—
Net foreign exchange loss	**546**	25,698
Finance expenses	**50,049**	96,162
Net finance cost	**47,313**	91,555

* The borrowing costs have been capitalised at a rate of 3.51%–6.72% per annum (2008: nil) (see Note 4(d)).

(ii) Staff costs

	2009 RMB'000	2008 RMB'000
Wages, salaries and other benefits	**95,112**	111,663
Contributions to defined contribution plans	**3,721**	3,554
	98,833	115,217

The Group participates in defined contribution pension funds managed by the PRC local government authorities. According to the respective pension fund regulations, the Group is required to pay annual contributions determined by the respective authorities in the PRC. The Group remits all the pension fund contributions to the respective social security offices, which are responsible for the payments and liabilities relating to the pension funds. The Group has no obligation for payment of retirement and other post-retirement benefits of employees other than the contributions described above.

(iii) Other items

	2009 RMB'000	2008 RMB'000
Cost of inventories*	**1,062,867**	1,673,566
Depreciation	**69,131**	58,089
Amortisation of lease prepayments	**2,001**	1,958
Impairment loss for doubtful debts	**13,259**	4,744
Auditor's remuneration	**2,026**	2,004
Write down of inventories	**13,796**	9,962
Operating lease charges	**1,433**	1,468

* Cost of inventories includes RMB153,021,000 (2008: RMB144,338,000) relating to staff costs, depreciation expenses and write down of inventories which amounts are also included in the respective total amounts disclosed separately above or in Note 8(ii) for each of these types of expenses.

9 Income tax expense

(a) Income tax expense in the consolidated statement of comprehensive income represents:

	2009 RMB'000	2008 RMB'000
Current tax		
Provision for PRC income tax	**7,142**	1,342
Deferred tax		
Origination and reversal of temporary differences	**100**	1,260
	7,242	2,602

(i) Pursuant to the rules and regulations of the Cayman Islands and British Virgin Islands, the Group is not subject to any income tax in the Cayman Islands or British Virgin Islands.

(ii) The provision for PRC income tax is based on the respective corporate income tax rates applicable to the subsidiaries located in the PRC as determined in accordance with the relevant income tax rules and regulations of the PRC.

On 16 March 2007, the Fifth Plenary Session of the Tenth National People's Congress passed the Corporate Income Tax Law of the People's Republic of China (the "new tax law") which has taken effect on 1 January 2008. According to the new tax law, the applicable tax rates of the Group's operating subsidiaries in the PRC are unified at 25% with effect from 1 January 2008.

Pursuant to the income tax rules and regulations of the PRC, foreign-invested enterprises located in the PRC are entitled to a tax holiday of a tax-free period for two years from their first profit-making year of operations and thereafter, they are subject to PRC enterprise income tax at 50% of the applicable income tax rate for the following three years. For the enterprises that do not benefit from such tax holiday due to their non-profit making status, the period of time for which such tax holiday applies shall be calculated commencing from the year of 2008.

The statutory income tax rate applicable to TG Tools is 25% (2008: 25%). On 21 August 2006, China Tiangong Company Limited ("CTCL") acquired the entire equity interests in TG Tools. As a result, TG Tools became a wholly foreign-owned enterprise and was exempted from PRC enterprise income tax for 2007 and 2008 and subject to PRC enterprise income tax rate at 50% of its applicable tax rate for 3 years from 2009 due to the above-mentioned tax holiday.

Tiangong Aihe Special Steel Company Limited ("TG Aihe") is exempted from PRC enterprise income tax for 2008 and 2009 due to the above-mentioned tax holiday.

Danyang Tianfa Forging Company Limited ("Tianfa Forging") is subject to the statutory income tax rate 25%.

9 Income tax expense (continued)

(b) Reconciliation between tax expense and accounting profit at applicable tax rates:

	2009 RMB'000	2008 RMB'000
Profit before income tax	**119,320**	115,112
Notional tax on profit before income tax, calculated using the Group's PRC statutory tax rate of 25% (2008: 25%)	**29,830**	28,778
Effect of preferential tax rates	**(22,647)**	(30,227)
Tax effect of non-deductible expenses	**950**	505
Deferred tax liabilities in respect of withholding tax on undistributed profits of subsidiaries	**(891)**	3,546
	7,242	2,602

10 Directors' remuneration

Details of the directors' remuneration are as follows:

Year ended 31 December 2009

	Fees RMB'000	Basic salaries, allowances and other benefits RMB'000	Contributions to retirement benefit schemes RMB'000	Bonus RMB'000	Total RMB'000
Executive directors					
Zhu Xiaokun	–	71	11	4,120	4,202
Zhu Zhihe	–	65	9	32	106
Zhu Mingyao	–	34	10	–	44
Yan Ronghua	–	68	10	29	107
Non-executive directors					
Thong Kwee Chee	–	–	–	–	–
Independent non-executive directors					
Li Zhengbang	60	–	–	–	60
Gao Xiang	36	–	–	–	36
Lau Siu Fai	96	–	–	–	96
Total	192	238	40	4,181	4,651

10 Directors' remuneration (continued)

Year ended 31 December 2008

	Fees RMB'000	Basic salaries, allowances and other benefits RMB'000	Contributions to retirement benefit schemes RMB'000	Bonus RMB'000	Total RMB'000
Executive directors					
Zhu Xiaokun	—	77	11	3,160	3,248
Zhu Zhihe	—	69	9	30	108
Zhu Mingyao	—	50	10	10	70
Yan Ronghua	—	73	10	27	110
Non-executive directors					
Thong Kwee Chee	—	—	—	—	—
Independent non-executive directors					
Li Zhengbang	60	—	—	—	60
Gao Xiang	24	—	—	—	24
Lau Siu Fai	84	—	—	—	84
Total	168	269	40	3,227	3,704

11 Individuals with highest emoluments

Of the five individuals with the highest emoluments, two (2008: one) are directors whose emoluments are disclosed in Note 10 above. The aggregate of the emoluments in respect of the other three (2008: four) individuals are as follows:

	2009 RMB'000	2008 RMB'000
Basic salaries, allowances and other benefits	**818**	910
Contributions to retirement benefit schemes	**32**	51
Bonus	**123**	170
	973	1,131

The above individuals' emoluments are within the band of Nil to Hong Kong dollars (HKD) 1,000,000.

No emoluments were paid by the Group to the directors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office in the current year or the prior year.

12 Profit attributable to equity holders of the Company

The consolidated profit attributable to equity holders of the Company includes a profit of RMB13,619,000 (2008: a loss of RMB9,504,000) which has been dealt with in the financial statements of the Company.

13 Earnings per share

(i) Basic earnings per share

The calculation of basic earnings per share at 31 December 2009 was based on the profit attributable to ordinary shareholders of RMB112,078,000 (2008: RMB114,643,000) and a weighted average number of ordinary shares outstanding of 419,500,000 (2008: 419,500,000).

(ii) Diluted earnings per share

No dilutive potential ordinary shares were in issue as at 31 December 2009 (2008: Nil).

14 Property, plant and equipment

The Group

	Plant and buildings RMB'000	Machinery RMB'000	Motor vehicles RMB'000	Office equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:						
Balance at 1 January 2008	209,353	444,683	5,987	29,954	261,762	951,739
Additions	73	72,567	584	2,868	342,228	418,320
Transfer from construction in progress	45,580	33,650	–	–	(79,230)	–
Disposals	–	(499)	(264)	–	–	(763)
Balance at 31 December 2008	255,006	550,401	6,307	32,822	524,760	1,369,296
Additions	765	94,526	782	5,233	255,664	356,970
Transfer from construction in progress	37,961	115,210	–	–	(153,171)	–
Transfer to assets held for sale	(32,312)	–	–	–	–	(32,312)
Disposals	–	–	(1,946)	–	–	(1,946)
Balance at 31 December 2009	261,420	760,137	5,143	38,055	627,253	1,692,008
Depreciation:						
Balance at 1 January 2008	(42,906)	(156,328)	(1,710)	(17,010)	–	(217,954)
Charge for the year	(10,716)	(41,137)	(687)	(5,549)	–	(58,089)
Written back on disposals	–	391	91	–	–	482
Balance at 31 December 2008	(53,622)	(197,074)	(2,306)	(22,559)	–	(275,561)
Charge for the year	(11,617)	(50,873)	(658)	(5,983)	–	(69,131)
Written back on disposals	–	–	969	–	–	969
Balance at 31 December 2009	(65,239)	(247,947)	(1,995)	(28,542)	–	(343,723)
Carrying amounts:						
At 31 December 2009	196,181	512,190	3,148	9,513	627,253	1,348,285
At 31 December 2008	201,384	353,327	4,001	10,263	524,760	1,093,735

(i) All plant and buildings are located in the PRC.

(ii) Pursuant to the lease agreements entered into between the Group and Jiangsu Tiangong Group Company Limited ("TG Group") on 28 February 2007 and 7 July 2007, the Group is required to pay RMB600,000 per annum for the lease of office premises from the TG Group effective from 1 January 2007 to 31 December 2009, and to pay RMB400,000 per annum for the lease of amenity facilities from the TG Group effective from 1 July 2007 to 31 December 2009 (see Note 32(a)).

(iii) The property, plant and equipment owned by the Company with carrying amounts of RMB107,000 at 31 December 2009 (2008: RMB136,000) are all office equipment.

15 Lease prepayments

	The Group 2009 RMB'000	2008 RMB'000
Cost:		
Balance at 1 January	**102,219**	68,446
Additions	**—**	33,773
Transfer to assets held for sale	**(33,702)**	—
Balance at 31 December	**68,517**	102,219
Amortisation:		
Balance at 1 January	**(5,113)**	(3,155)
Charge for the year	**(2,001)**	(1,958)
Transfer to assets held for sale	**1,236**	—
Balance at 31 December	**(5,878)**	(5,113)
Carrying amounts:		
At 31 December	**62,639**	97,106
At 1 January	**97,106**	65,291

Lease prepayments represent the cost of land use rights in respect of land located in the PRC with a lease period of 50 years when granted.

16 Goodwill

	The Group RMB'000
Cost:	
At 31 December 2008 and 2009	**21,959**
Accumulated impairment losses:	
At 31 December 2008 and 2009	**—**
Carrying amounts:	
At 31 December 2008 and 2009	**21,959**

For the purpose of impairment testing, goodwill is allocated to the Group's operating divisions which represent the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Goodwill is allocated to the Group's cash-generating units identified according to the reportable segments as follows:

	2009 RMB'000	2008 RMB'000
Die steel	**21,959**	21,959

16 Goodwill (continued)

The recoverable amount of the DS cash-generating unit was determined based on value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rate, growth rate and gross margin. The Group prepared cash flow forecasts derived from the two-year financial budgets and extrapolated cash flows for the following eighteen years based on an estimated growth rate of 3%-8% (2008: 3%-8%), a discount rate of 6.6% (2008: 6.5%) and a gross margin of 16%-18% (2008: 13%-15%). The growth rate used does not exceed the long-term average growth rate for the business in which the cash-generating unit operates.

Management determined the budgeted gross margin and growth rate based on past performance and its expectation for market development. The discount rates used are pre-tax and reflect specific risks relating to the relevant segments.

17 Interests in subsidiaries

	The Company	
	2009	2008
	RMB'000	RMB'000
Unlisted shares, at cost	**400**	400
Receivables from subsidiaries	**927,727**	1,110,979
	928,127	1,111,379

The receivables from subsidiaries included in the interests in subsidiaries above are unsecured, interest-free and have no fixed terms of repayment.

Details of the subsidiaries as at 31 December 2009 are set out below. The class of shares held is ordinary unless otherwise stated.

Name of company	Place and date of incorporation	Percentage of equity attributable to the Company: Direct	Percentage of equity attributable to the Company: Indirect	Issued and fully paid-up/ registered capital	Principal activities
CTCL	British Virgin Islands, 14 August 2006	100%	–	USD–/USD50,000	Investment holding
TG Tools (i)	the PRC, 7 July 1997	–	100%	RMB844,300,000/ RMB844,300,000	Manufacture and sales of high speed steel and cutting and drilling tools
TG Aihe (ii)	the PRC, 5 December 2003	–	100%	RMB401,438,000/ RMB401,438,000	Manufacture and sales of die steel
Tianfa Forging (ii)	the PRC, 11 October 2000	–	100%	USD18,600,000/ USD18,600,000	Precision forging and sales of high speed steel
Danyang Tianji Tools Packaging Company Limited ("Tianji Packaging") (iii)	the PRC, 13 May 2002	–	100%	RMB2,000,000/ RMB2,000,000	Manufacture and sales of packaging materials
China Tiangong (Hong Kong) Company Limited	Hong Kong, 13 June 2008	–	100%	HKD1/HKD1	Investment holding

17 Interests in subsidiaries (continued)

Note:

(i) TG Tools is a wholly foreign-owned enterprise incorporated in the PRC.

(ii) TG Aihe and Tianfa Forging are incorporated in the PRC as sino-foreign equity joint ventures.

(iii) Tianji Packaging is incorporated in the PRC as a domestic company.

18 Other investments

	The Group	
	2009	2008
	RMB'000	RMB'000
Non-current investments		
Available-for-sale financial assets	**10,000**	10,000

Available-for-sale financial assets represent unlisted equity securities. As there is no quoted market price in an active market for these investments, they are stated at cost less impairment losses.

The Group's exposure to credit risk related to other investments is disclosed in Note 30.

19 Inventories

(i) Inventories in the balance sheet comprise:

	The Group	
	2009	2008
	RMB'000	RMB'000
Raw materials	**54,349**	50,009
Work in progress	**629,264**	551,862
Finished goods	**569,135**	509,411
	1,252,748	1,111,282
Inventories carried at fair value less cost to sell	**489,750**	469,275

(ii) The analysis of the amount of inventories recognised as an expense is as follows:

	The Group	
	2009	2008
	RMB'000	RMB'000
Carrying amount of inventories sold	**1,049,071**	1,663,604
Write down of inventories	**13,796**	9,962
	1,062,867	1,673,566

20 Trade and other receivables

	The Group		The Company	
	2009 **RMB'000**	2008 RMB'000	**2009** **RMB'000**	2008 RMB'000
Trade and bills receivables	**624,766**	504,421	**–**	–
Less: impairment loss for doubtful debts (see Note 20(b))	**(43,521)**	(30,262)	**–**	–
Net trade and bills receivables	**581,245**	474,159	**–**	–
Prepayments	**49,670**	125,555	**–**	–
Non-trade receivables	**26,044**	17,187	**–**	1,239
	656,959	616,901	**–**	1,239

Substantially all of the trade receivables are expected to be recovered within one year.

The Group's and the Company's exposure to credit and currency risks related to trade and other receivables are disclosed in Note 30.

(a) Ageing analysis

Included in trade and other receivables are trade and bills receivables (net of impairment loss for doubtful debts) with the following ageing analysis as of the balance sheet date:

	The Group	
	2009 **RMB'000**	2008 RMB'000
Current	**360,734**	166,622
Less than 3 months past due	**148,649**	182,030
More than 3 months but less than 6 months past due	**24,884**	97,628
More than 6 months but less than 12 months past due	**30,375**	25,355
More than 12 months but less than 24 months past due	**16,603**	2,524
Amounts past due	**220,511**	307,537
	581,245	474,159

(b) Impairment of trade and bills receivables

Impairment losses in respect of trade and bills receivables are recorded using an allowance account unless the Group is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade and bills receivables directly (see Note 3(h), (i)).

The movement in the impairment loss for doubtful debts during the year, including both specific and collective loss components, is as follows:

	The Group	
	2009 **RMB'000**	2008 RMB'000
At 1 January	**30,262**	25,518
Impairment loss recognised	**13,259**	4,744
At 31 December	**43,521**	30,262

20 Trade and other receivables (continued)

(c) Trade and bills receivables that are not impaired

The ageing analysis of trade and bills receivables that are neither individually nor collectively considered to be impaired are as follows:

	The Group 2009 RMB'000	2008 RMB'000
Neither past due nor impaired	**360,734**	166,622
Less than 3 month past due	**38,245**	10,009
More than 3 months but less than 6 months past due	**8,148**	38,625
Amounts past due but not impaired	**46,393**	48,634
	407,127	215,256

Receivables that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, management believes that no impairment allowance is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable. The Group does not hold any collateral over these balances.

21 Pledged deposits

Bank deposits of RMB119,358,000 (2008: RMB63,600,000) have been pledged to banks as security for the Group to issue bank acceptance bills and other banking facilities. The pledge in respect of the bank deposits will be released upon the settlement of the related bills payables by the Group and the termination of related banking facilities.

The Group's exposure to credit, currency and interest rate risks are disclosed in Note 30.

22 Time deposits

Time deposits on the consolidated balance sheet represent bank deposits that are over 3 months of maturity at acquisition.

The Group's exposure to credit and interest rate risks are disclosed in Note 30.

23 Cash and cash equivalents

	The Group		The Company	
	2009 RMB'000	2008 RMB'000	**2009 RMB'000**	2008 RMB'000
Deposits with banks within three months of maturity at acquisition	**—**	50,000	**—**	—
Cash at bank and in hand	**63,467**	46,021	**1,771**	3,740
	63,467	96,021	**1,771**	3,740

The Group's and the Company's exposure to credit and currency risks are disclosed in Note 30.

24 Non-current assets held for sale

A land use right and the vacant building thereon are presented as a disposal group held for sale as the Group has entered into a frame agreement with a local authority and has received a refundable deposit of RMB23,000,000 before 31 December 2009. Subject to the finalisation of the consideration payable and the entering into of a binding contract, the disposal is expected to take place in 2010.

The disposal group comprised assets with the following carrying values:

The Group

	The Group 2009 RMB'000
Property, plant and equipment — Building	**32,312**
Lease prepayments — Land use right	**32,466**
	64,778

No impairment loss on the remeasurement of the disposal group to the lower of its carrying amount and its fair value less costs to sell has been recognised in other expenses, as the consideration of the disposal under negotiation is no less than the carrying value of the assets plus costs to sell.

25 Interest-bearing borrowings

This note provides information about the contractual terms of the Group's interest-bearing borrowings, which are measured at amortised cost. More information about the Group's and the Company's exposure to interest rate, foreign currency and liquidity risks is disclosed in Note 30.

		The Group		The Company	
		2009 RMB'000	2008 RMB'000	**2009 RMB'000**	2008 RMB'000
Current					
Unsecured bank loans	(i)	**1,229,700**	1,093,865	**—**	170,865
Current portion of non-current unsecured bank loans		**150,000**	—	**—**	—
		1,379,700	1,093,865	**—**	170,865
Non-current					
Unsecured bank loans	(ii)	**327,000**	190,000	**—**	—
Less: Current portion of non-current unsecured bank loans	(ii)	**(150,000)**	—	**—**	—
		177,000	190,000	**—**	—
		1,556,700	1,283,865	**—**	170,865

(i) Current unsecured bank loans carried interest at annual rates ranging from 2.40% to 5.40% (2008: 3.51% to 6.93%) and were all repayable within one year.

Current unsecured bank loans of RMB90,000,000 (2008: RMB nil) were guaranteed by an entity in the same city. Current unsecured bank loans of RMB100,000,000 were guaranteed by a local commercial bank (2008: RMB240,000,000 guaranteed by three local commercial banks).

25 Interest-bearing borrowings (continued)

(ii) Non-current unsecured bank loans carried interest at annual rates ranging from 4.78% to 5.76% (2008: 5.76% to 7.47%).

The Group's non-current bank loans were repayable as follows:

	The Group	
	2009	2008
	RMB'000	RMB'000
Within 1 year	**150,000**	—
Over 1 year but less than 2 years	**177,000**	150,000
Over 2 years but less than 3 years	**—**	40,000
	177,000	190,000
	327,000	190,000

26 Trade and other payables

	The Group		The Company	
	2009	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade and bills payables	**489,636**	373,379	**—**	—
Non-trade payables and accrued expenses	**154,488**	67,878	**3,297**	10,055
Payables due to related parties (see Note 32(b))	**1,000**	1,000	**—**	—
	645,124	442,257	**3,297**	10,055

The Group and the Company exposure to liquidity and currency risks related to trade and other payables is disclosed in Note 30.

Included in trade and other payables are trade and bills payables with the following ageing analysis as of the balance sheet date:

	The Group	
	2009	2008
	RMB'000	RMB'000
Due within 3 months	**361,235**	268,650
Due after 3 months but within 6 months	**121,067**	92,830
Due after 6 months but within 12 months	**4,891**	7,877
Due after 1 year but within 2 years	**2,443**	4,022
	489,636	373,379

27 Deferred income

Deferred income consists of conditional government grants received for completion of certain construction projects. At 31 December 2009, the construction projects have been completed and the amount recognised as deferred income in the balance sheet after amortisation, amounts to RMB9,513,000 of which RMB8,351,000 is classified as non-current.

28 Income tax in the consolidated balance sheet

(a) Current taxation in the consolidated balance sheet represents:

	The Group 2009 RMB'000	2008 RMB'000
At the beginning of the year	**13,383**	12,217
Provision for PRC income tax for the year	**7,142**	1,342
PRC income tax paid	**(5,561)**	(176)
At the end of the year	**14,964**	13,383

(b) Deferred tax assets recognised

The components of the Group's deferred tax assets recognised in the consolidated balance sheet and the movements during the year are as follows:

	Impairment loss for doubtful debts RMB'000	Write down of inventories RMB'000	Total RMB'000
At 1 January 2008	3,190	—	3,190
Recognised in consolidated statement of comprehensive income	622	1,664	2,286
At 31 December 2008	3,812	1,664	5,476
Recognised in consolidated statement of comprehensive income	2,066	2,490	4,556
At 31 December 2009	5,878	4,154	10,032

(c) Deferred tax liabilities recognised and not recognised

The components of the Group's deferred tax liabilities recognised in the consolidated balance sheet and the movements during the year are as follows:

	Undistributed profits of subsidiaries RMB'000	Deductible capitalised borrowing costs RMB'000	Total RMB'000
At 1 January 2008	—	—	—
Recognised in consolidated statement of comprehensive income	3,546	—	3,546
At 31 December 2008	3,546	—	3,546
Recognised in consolidated statement of comprehensive income	(1,005)	5,661	4,656
At 31 December 2009	2,541	5,661	8,202

28 Income tax in the consolidated balance sheet (continued)

(c) Deferred tax liabilities recognised and not recognised (continued)

Pursuant to the new tax law in the PRC, 10% withholding tax is levied on the foreign investor in respect of dividend distributions arising from a foreign investment enterprise's profit earned after 1 January 2008. As at 31 December 2009, deferred tax liabilities of RMB2,541,000 (2008: RMB3,546,000) have been recognised in respect of the tax that would be payable on the distribution of the retained profits of the Group's PRC subsidiaries. Deferred tax liabilities of RMB7,600,000 (2008: RMB8,780,000) have not been recognised, as the Company controls the timing of the reversal of temporary differences associated to undistributed profits of these subsidiaries and it has been determined that it is probable that certain of the profits earned by the Group's PRC subsidiaries for the period from 1 January 2008 to 31 December 2009 will not be distributed in the foreseeable future.

29 Capital, reserves and dividends

(a) Movements in components of equity

The reconciliation between the opening and closing balances of each component of the Group's consolidated equity is set out in the consolidated statement of changes in equity. Details of the changes in the Company's individual components of equity between the beginning and the end of the year are set out below:

The Company

	Share capital RMB'000 Note 29(c)	Share premium RMB'000 Note 29(d)(i)	Retained earnings RMB'000	Total RMB'000
At 1 January 2008	31,806	886,566	26,706	945,078
Loss for the year	—	—	(9,504)	(9,504)
At 31 December 2008	31,806	886,566	17,202	935,574
Dividends approved in respect of the previous year (see Note 29(b)(ii))	—	—	(22,485)	(22,485)
Total comprehensive income for the year	—	—	13,619	13,619
At 31 December 2009	31,806	886,566	8,336	926,708

(b) Dividends

(i) Dividends payable to equity holders of the Company attributable to the year:

	2009 RMB'000	2008 RMB'000
Dividend proposed after the balance sheet date of RMB0.0534 per share (2008: RMB0.0536)	**22,401**	22,485
	22,401	22,485

29 Capital, reserves and dividends (continued)

(b) Dividends (continued)

(ii) Dividends payable to equity holders of the Company attributable to the previous financial year, approved and paid during the year:

	2009 RMB'000	2008 RMB'000
Special dividend in respect of the previous financial year, approved and paid during the year of RMB0.0536 per share (2008: Nil)	**22,485**	—
	22,485	—

(c) Share Capital

Authorised, issued and fully paid share capital:

Authorised:

	2009 No. of Shares ('000)	2009 Amount USD '000	2008 No. of Shares ('000)	2008 Amount USD '000
Ordinary shares of USD0.01 each	**1,000,000**	**10,000**	1,000,000	10,000

Ordinary shares issued and fully paid:

	2009 No. of Shares ('000)	2009 Amount USD '000	2009 RMB equivalent '000	2008 No. of Shares ('000)	2008 Amount USD '000	2008 RMB equivalent '000
At 1 January and at 31 December	**419,500**	**4,195**	**31,806**	419,500	4,195	31,806

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

(d) Nature and purpose of reserves

(i) Share premium

The application of the share premium account is governed by the Companies Law of the Cayman Islands. Under the Companies Law of the Cayman Islands, the funds in the share premium account are distributable to shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to repay its debts as they fall due in the ordinary course of business.

(ii) Capital reserve

The capital reserve comprises the waived payables due to TG Group in connection with the acquisition of land use rights and plant in 2007. These waivers of liabilities by TG Group were regarded as equity transactions and recorded in the capital reserve account.

29 Capital, reserves and dividends (continued)

(d) Nature and purpose of reserves (continued)

(iii) Merger reserve

The merger reserve comprises the excess amount, arising from the Group's reorganisation of Group entities under common control in 2006 and 2007, of its share of the net identifiable assets acquired in these subsidiaries over the consideration paid. The reorganisation transactions were regarded as equity transactions and the excess of the share of the net identifiable assets over the consideration paid was transferred to the merger reserve in the consolidated financial statements.

(iv) PRC statutory reserve

Transfers from retained earnings to the following PRC statutory reserves were made in accordance with the relevant PRC rules and regulations and the articles of association of the Company's subsidiaries incorporated in the PRC and were approved by the respective boards of directors.

General reserve fund

The subsidiaries in the PRC are required to transfer at least 10% of their profit after taxation, as determined under the PRC accounting regulations, to the general reserve fund until the reserve balance reaches 50% of their respective registered capital. The transfer to this reserve must be made before any distribution of dividends to shareholders.

The general reserve fund can be used to make good losses and convert into share capital by the issue of new shares to shareholders in proportion to their existing equity holdings, provided that the balance after such conversion is not less than 25% of their registered capital.

Enterprise expansion fund

The enterprise expansion fund can be used to convert into share capital and to develop business.

(e) Distributability of reserves

At 31 December 2009, the aggregate amount of reserves available for distribution to equity holders of the Company was RMB894,902,000 (2008: RMB903,768,000).

(f) Capital management

The Group's primary objectives when managing capital are to maintain investor, creditor and market confidence and to sustain future development of the business. The board of directors monitors the return on capital, which the Group defines as net operating income divided by total shareholders' equity, excluding non-controlling interest. The board of directors also monitors the level of dividends to ordinary shareholders.

The Group actively and regularly reviews and manages its capital structure to maintain a balance between the higher shareholder returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

The Group monitors its capital structure closely, and adjusts its level of interest-bearing borrowings, trade and other payables and dividend payments to safeguard the Group's ability to continue as a going concern.

The gearing ratio of the Group for the year ended 31 December 2009 is 99% (2008: 87%). The gearing ratio is calculated by dividing total borrowings by total equity.

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

30 Financial risk management and fair values

Exposure to credit, liquidity, currency and interest rate risks arises in the normal course of the Group's business. The Group's exposure to these risks and the financial risk management policies and practices used by the Group to manage these risks are described below.

(a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

The Group's credit risk is primarily attributable to trade and other receivables. Management has a credit policy in place and the exposures to these credit risks are monitored on an ongoing basis.

The maximum exposure to credit risk without taking into account any collateral held is represented by the carrying amount of each financial asset in the balance sheet after deducting any impairment allowance.

(i) Trade and other receivables

In respect of trade and other receivables, individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and taking into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. The Group's customers are normally granted credit terms of 0 to 150 days depending on the creditworthiness of individual customers. Normally, the Group does not obtain collateral from customers.

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer rather than the industry or country in which the customers operate and therefore significant concentrations of credit risk primarily arise when the Group has significant exposure to individual customers. At the balance sheet date, 7% (2008: 3%) and 20% (2008: 17%) of the total trade and other receivables were due from the Group's largest customer and the five largest customers respectively.

Further quantitative disclosures in respect of the Group's exposure to credit risk arising from trade and other receivables are set out in Note 20.

(ii) Investments

The Group limits its exposure to credit risk by only investing in liquid securities and/or only with counterparties that have a credit rating equal to or better than the Group. Management does not expect any counterparty to fail to meet its obligations.

(iii) Guarantees

The Group's policy is to provide financial guarantees only to wholly-owned subsidiaries. At 31 December 2009 no guarantees were outstanding (2008: nil).

(iv) Deposits with bank

Substantially all of the bank deposits are deposited with Chinese state-owned banks and local commercial banks. The management does not expect any losses arising from non-performance of these financial institutions.

30 Financial risk management and fair values (continued)

(b) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's policy is to regularly monitor its liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and readily realisable marketable securities and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

Typically the Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of 60 days, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. In addition, as at 31 December 2009, total banking and borrowing facilities available to the Group amounted to RMB3,230,000,000 of which RMB1,708,664,000 had been utilised.

The following table details the remaining contractual maturities at the balance sheet dates of the Group's and the Company's non-derivative financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and the earliest date the Group and the Company can be required to pay. At the balance sheet dates, the Group did not have any derivative financial liabilities.

The Group

	2009				
	Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	**More than 1 year but less than 2 years RMB'000**	**More than 2 years but less than 3 years RMB'000**	**Total RMB'000**	**Balance sheet carrying amount RMB'000**
Non-derivative financial liabilities					
Interest-bearing borrowings	**1,414,592**	**184,197**	**–**	**1,598,789**	**1,556,700**
Trade and other payables	**645,124**	**–**	**–**	**645,124**	**645,124**
Income tax payables	**14,964**	**–**	**–**	**14,964**	**14,964**
	2,074,680	**184,197**	**–**	**2,258,877**	**2,216,788**

	2008				
	Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 3 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000
Non-derivative financial liabilities					
Interest-bearing borrowings	1,138,716	154,025	42,988	1,335,729	1,283,865
Trade and other payables	442,257	–	–	442,257	442,257
Income tax payables	13,383	–	–	13,383	13,383
	1,594,356	154,025	42,988	1,791,369	1,739,505

30 Financial risk management and fair values (continued)

(b) Liquidity risk (continued)

The Company

	2009				
	Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 3 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000
Non-derivative financial liabilities					
Trade and other payables	**3,297**	**–**	**–**	**3,297**	**3,297**
	3,297	**–**	**–**	**3,297**	**3,297**

	2008				
	Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 3 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000
Non-derivative financial liabilities					
Interest-bearing borrowings	179,536	–	–	179,536	170,865
Trade and other payables	10,055	–	–	10,055	10,055
	189,591	–	–	189,591	180,920

(c) Currency risk

The Group is exposed to currency risk primarily through sales, purchases and borrowings which give rise to receivables, payables, borrowings and cash balances that are denominated in a foreign currency, i.e. a currency other than the functional currency of the operations to which the transactions relate. The currencies giving rise to this risk are primarily United States dollars (USD), Euros (EUR), HKD and Sterling (GBP).

RMB is not freely convertible into foreign currencies. All foreign exchange transactions involving RMB must take place through the People's Bank of China or other institutions authorised to buy and sell foreign exchange. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the People's Bank of China.

The following table details the Group's and the Company's exposure at the balance sheet date to currency risk arising from recognised assets or liabilities denominated in a currency other than the functional currency of the entity to which they relate. For presentation purposes, the amounts of the exposure are shown in RMB, translated using the spot rate at the year end date.

30 Financial risk management and fair values (continued)

(c) Currency risk (continued)

(i) Exposure to currency risk

The Group

	2009 Exposure to foreign currencies (expressed in RMB)			
	USD RMB'000	**EUR RMB'000**	**HKD RMB'000**	**GBP RMB'000**
Trade and other receivables	**99,070**	**18,348**	**—**	**358**
Cash and cash equivalents	**14,432**	**3,172**	**97**	**—**
Trade and other payables	**(41,456)**	**—**	**—**	**—**
Balance sheet net exposure	**72,046**	**21,520**	**97**	**358**

	2008 Exposure to foreign currencies (expressed in RMB)			
	USD RMB'000	EUR RMB'000	HKD RMB'000	GBP RMB'000
Trade and other receivables	114,827	38,009	—	3,707
Cash and cash equivalents	1,561	570	3,543	—
Trade and other payables	(6,059)	—	—	—
Interest-bearing borrowings	(170,865)	—	—	—
Balance sheet net exposure	(60,536)	38,579	3,543	3,707

The Company

	2009 Exposure to foreign currencies (expressed in RMB)			
	USD RMB'000	**EUR RMB'000**	**HKD RMB'000**	**GBP RMB'000**
Cash and cash equivalents	**1,674**	**—**	**98**	**—**
Balance sheet net exposure	**1,674**	**—**	**98**	**—**

	2008 Exposure to foreign currencies (expressed in RMB)			
	USD RMB'000	EUR RMB'000	HKD RMB'000	GBP RMB'000
Cash and cash equivalents	492	—	3,249	—
Trade and other payables	(6,059)	—	—	—
Interest-bearing borrowings	(170,865)	—	—	—
Balance sheet net exposure	(176,432)	—	3,249	—

30 Financial risk management and fair values (continued)

(c) Currency risk (continued)

(ii) Sensitivity analysis

The following table indicates the instantaneous change in the Group's profit after tax (and retained profits) that would arise if foreign exchange rates to which the Group has significant exposure at the balance sheet date had changed at that date, assuming all other risk variables remained constant.

The Group

	2009		2008	
	Increase/ (decrease) in foreign exchange rates	**Increase/ (decrease) on profit after tax and retained profits RMB'000**	Increase/ (decrease) in foreign exchange rates	Increase/ (decrease) on profit after tax and retained profits RMB'000
USD	**5%**	**3,165**	5%	(3,027)
	(5)%	**(3,165)**	(5)%	3,027
EUR	**5%**	**942**	10%	3,858
	(5)%	**(942)**	(10)%	(3,858)
HKD	**5%**	**5**	5%	177
	(5)%	**(5)**	(5)%	(177)
GBP	**5%**	**16**	10%	371
	(5)%	**(16)**	(10)%	(371)

Results of the analysis as presented in the above table represent an aggregation of the instantaneous effects on each of the Group entities' profit after tax and equity measured in the respective functional currencies, translated into RMB at the exchange rate ruling at the balance sheet date for presentation purposes.

The sensitivity analysis assumes that the change in foreign exchange rates had been applied to re-measure those financial instruments held by the Group which expose the Group to foreign currency risk at the balance sheet date. The analysis is performed on the same basis for 2008.

30 Financial risk management and fair values (continued)

(d) Interest rate risk

The Group's interest rate risk arises primarily from interest-bearing borrowings, pledged deposits and time deposits.

Pledged bank deposits are not held for speculative purposes but are placed to satisfy conditions for issuance of bank acceptance bills and other banking facilities granted to the Group.

Interest-bearing borrowings issued at variable rates and at fixed rates expose the Group to cash flow interest rate risk and fair value interest rate risk respectively. The interest rates and terms of repayment of the interest-bearing borrowings of the Group are disclosed in Note 25.

(i) Interest rate profile

The following table details the interest rate profile of the Group's and the Company's interest-bearing financial instruments at the balance sheet date:

The Group

	2009		2008	
	Effective interest rate %	**RMB'000**	Effective interest rate %	RMB'000
Fixed rate instruments				
Interest-bearing borrowings	**2.4%–5.31%**	**(816,700)**	4.78%–6.72%	(592,865)
Pledged deposits	**1.17%**	**119,358**	0.36%–3.78%	63,600
Time deposits	**1.98%**	**192,000**	1.98%–3.24%	115,000
		(505,342)		(414,265)
Variable rate instruments				
Interest-bearing borrowings	**3.51%–5.76%**	**(740,000)**	3.51%–7.47%	(691,000)

The Company

	2009		2008	
	Effective interest rate %	**RMB'000**	Effective interest rate %	RMB'000
Fixed rate instruments				
Interest-bearing borrowings	**–**	**–**	5.07%–5.10%	(170,865)

30 Financial risk management and fair values (continued)

(d) Interest rate risk (continued)

(ii) Sensitivity analysis

At 31 December 2009, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would have decreased/increased the Group's profit after tax and retained profits by approximately RMB6,525,000 (2008: RMB6,910,000).

The sensitivity analysis above indicates the instantaneous change in the Group's profit after tax (and retained profits) that would arise assuming that the change in interest rates had occurred at the balance sheet date and had been applied to re-measure those financial instruments held by the Group which expose the Group to fair value interest rate risk at the balance sheet date. In respect of the exposure to cash flow interest rate risk arising from floating rate non-derivative instruments held by the Group at the balance sheet date, the impact on the Group's profit after tax (and retained profits) is estimated as an annualised impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis for 2008.

(e) Fair values

Available-for-sale financial assets are stated at cost less impairment losses as there is no quoted market price in an active market for these assets. Further disclosures in respect of these assets are set out in Note 18.

Except for available-for-sale financial assets, all financial instruments measured at other than fair value are carried at amounts not materially different from their fair values as at 31 December 2009 and 2008 due to either the short maturities of these financial instruments or variable market interest rates for long-term bank borrowings.

31 Commitments

(a) Capital commitments

Capital commitments outstanding at the year end not provided for in the consolidated financial statements were as follows:

	The Group	
	2009	2008
	RMB'000	RMB'000
Contracted for		
— Land and buildings	**4,650**	23,915
— Equipment	**61,855**	101,571
	66,505	125,486
Authorised but not contracted for		
— Equipment	**170,310**	185,056

31 Commitments (continued)

(b) Operating leases commitments

At 31 December 2009 and 2008, the total future minimum lease payments under non-cancellable operating leases were payable as follows:

	The Group		The Company	
	2009	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 1 year	**1,069**	1,323	**—**	145
After 1 year but within 5 years	**7**	34	**—**	—
	1,076	1,357	**—**	145

The Group leases certain properties located in the PRC and Hong Kong as the Group's offices under operating leases. The leases run for an initial period of 1-2 years.

32 Related party transactions

The Group has transactions with TG Group. The following is a summary of principal related party transactions carried out by the Group with TG Group.

Particulars of significant transactions between the Group and TG Group are as follows:

(a) Significant Related Party Transactions-Recurring

	2009	2008
	RMB'000	RMB'000
Lease expense to:		
TG Group	**1,000**	1,000

Pursuant to two lease agreements entered into between the Group and TG Group on 28 February 2007 and 7 July 2007, the Group is required to pay RMB 600,000 per annum for the lease of office premises from TG Group effective from 1 January 2007 to 31 December 2009, and to pay RMB 400,000 per annum for the lease of amenity facilities from TG Group effective from 1 July 2007 to 31 December 2009.

(b) Amounts due to related parties

	2009	2008
	RMB'000	RMB'000
TG Group	**1,000**	1,000

32 Related party transactions (continued)

(c) Transactions with key management personnel

Remuneration for key management personnel of the Group, including amounts paid to the Company's directors as disclosed in Note 10 and certain of the highest paid employees as disclosed in Note 11, is as follows:

	2009 RMB'000	2008 RMB'000
Short-term employee benefits	**5,714**	4,845
Post-employment benefits	**99**	109
	5,813	4,954

Total remuneration is included in "staff costs" (see Note 8(ii)).

33 Accounting estimates and judgements

Key sources of estimation uncertainty are as follow:

(a) Impairment losses on trade and other receivables

Impairment losses for trade and other receivables are assessed and provided based on the directors' regular review of ageing analysis and evaluation of collectibility. A considerable level of judgement is exercised by the directors when assessing the creditworthiness and past collection history of each individual customer. Any increase or decrease in the impairment losses for bad and doubtful debts would affect the consolidated statement of comprehensive income in future years.

(b) Depreciation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives, after taking into account the estimated residual value. The Group reviews annually the useful life of an asset and its residual value, if any. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

(c) Net realisable value of inventories

Net realisable value of inventories is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses. These estimates are based on the current market condition and the historical experience of distributing and selling products of a similar nature. They could change significantly as a result of competitor actions in response to severe industry cycles or other changes in market condition. Management reassess the estimations at each balance sheet date.

(d) Income taxes

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. The Group carefully evaluates the tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislation. Deferred tax assets are recognised for temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax credits can be utilised, management's judgement is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

33 Accounting estimates and judgements (continued)

(e) Estimated carrying amounts of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating units and a suitable discount rate in order to calculate the present value. Details of the recoverable amount calculation are disclosed in Note 16.

34 Parent and ultimate controlling party

At 31 December 2009, the directors consider the immediate parent and ultimate controlling party of the Group to be Tiangong Holdings Company Limited, which is incorporated in British Virgin Islands. This entity does not produce financial statements available for public use.

35 Non-adjusting subsequent events

(a) Subsequent to the balance sheet date, the Group has reached an agreement with Taisun International Co., Ltd. to invest in a joint venture registered in the Republic of Korea named TGT Special Steel Company Limited ("TGT"). The registered capital of TGT is USD1,000,000. The Group has completed its full capital contribution in January 2010.

(b) Subsequent to the balance sheet date, the Group is in the process of establishing a new subsidiary in the PRC named Jiangsu Tiangong Titanium Technology Co., Ltd ("TG Titan"). The registered capital of TG Titan is RMB300,000,000 of which TG Tools and Tianfa Forging holds 90% and 10% interests respectively. The Group has made initial capital contribution in January 2010. Up to the date of this report, the registration of TG Titan was not completed.

(c) After the balance sheet date, the directors proposed a final dividend of RMB0.0534 per ordinary share on 13 April 2010. Further details are disclosed in Note 29(b).

36 Comparative figures

As a result of the application of IAS 1 (revised 2007), *Presentation of financial statements*, and IFRS 8, *Operating segments*, certain comparative figures have been adjusted to conform to current period's presentation and to provide comparative amounts in respect of items disclosed for the first time in 2009. Further details of these developments are disclosed in Note 4.

	Year ended 31 December				
	2009	2008	2007	2006	2005
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Revenue	**1,323,752**	1,993,269	1,735,763	1,303,987	1,094,711
Profit before income tax	**119,320**	115,112	181,357	147,111	92,140
Income tax expense	**(7,242)**	(2,602)	(437)	(50,507)	(33,255)
Profit for the year	**112,078**	112,510	180,920	96,604	58,885
Attributable to:					
Equity holders of the Company	**112,078**	114,643	180,172	91,729	47,940
Minority interests	**—**	(2,133)	748	4,875	10,945
Earnings per Share					
Basic (RMB)	**0.27**	0.27	0.51	0.31	0.16

	Year ended 31 December				
	2009	2008	2007	2006	2005
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets					
Non-current assets	**1,452,915**	1,228,276	834,225	513,368	421,008
Current assets	**2,349,310**	2,002,804	1,668,262	1,187,972	1,069,770
Total assets	**3,802,225**	3,231,080	2,502,487	1,701,340	1,490,778
Liabilities					
Non-current liabilities	**193,553**	203,446	84,900	137,900	—
Current liabilities	**2,040,950**	1,549,505	1,033,223	957,980	1,009,395
Total liabilities	**2,234,503**	1,752,951	1,118,123	1,095,880	1,009,395
Equity					
Total equity	**1,567,722**	1,478,129	1,384,364	605,460	481,383

Note:

The results of the Group for the three financial years ended 31 December 2005, 2006 and 2007 and its assets and liabilities were extracted from the Prospectus and previous annual report, which also set forth the details of the basis of presentation of the combined accounts.

Registered Name

Tiangong International Company Limited

Chinese Name

天工國際有限公司

Stock Code

Hong Kong Stock Exchange 826

Board Of Directors

Executive Directors

Mr. Zhu Xiaokun *(Chairman)*

Mr. Zhu Zhihe *(Chief Executive Officer)*

Mr. Zhu Mingyao

Mr. Yan Ronghua

Non-executive Director

Mr. Thong Kwee Chee

Independent Non-executive Directors

Mr. Li Zhengbang

Mr. Gao Xiang

Mr. Lau Siu Fai

Company Secretary

Mr. Leung Wai Yip

Authorized Representatives

Mr. Lau Siu Fai

Mr. Leung Wai Yip

Audit Committee

Mr. Lau Siu Fai *(Chairman)*

Mr. Gao Xiang

Mr. Thong Kwee Chee

Remuneration Committee

Mr. Li Zhengbang *(Chairman)*

Mr. Zhu Xiaokun

Mr. Gao Xiang

Mr. Lau Siu Fai

Mr. Thong Kwee Chee

Nomination Committee

Mr. Gao Xiang *(Chairman)*

Mr. Zhu Xiaokun

Mr. Li Zhengbang

Mr. Lau Siu Fai

Mr. Thong Kwee Chee

Registered Office in the Cayman Islands

P.O. Box 309

G.T. Ugland House

South Church Street, George Town

Grand Cayman, Cayman Islands

Registered Office in Hong Kong

Unit 1303

13/F Jubilee Centre

18 Fenwick Street

Wanchai

Hong Kong

Principal Place of Business

Houxiang Town

Danyang City

Jiangsu Province

The PRC

Compliance Adviser

BNP Paribas Capital (Asia Pacific) Limited

59th–63rd Floors

Two International Finance Centre

8 Finance Street

Central

Hong Kong

Auditors

KPMG

Certified Public Accountants

8th Floor

Prince's Building

10 Chater Road

Central

Hong Kong

Hong Kong Legal Adviser

Richards Butler

20th Floor, Alexandra House

16–20 Chater Road

Central

Hong Kong

Principal Share Registrar and Transfer Office

Butterfield Fund Services (Cayman) Limited

Butterfield House, 68 Fort Street

P.O. Box 705

Grand Cayman KY1-1107

Cayman Islands

Hong Kong Branch Share Registrar and Transfer Office in Hong Kong

Computershare Hong Kong Investor Services Limited

Shops 1712–1716, 17th Floor

Hopewell Center

183 Queen's Road East

Wanchai

Hong Kong

Principal Bankers

China Construction Bank Corporation

Industrial and Commercial Bank of China Limited

Bank of China Limited

Agricultural Bank of China