Tiangong International Company Limited

天 工 國 際 有 限 公 司*

(incorporated in the Cayman Islands with limited liability)

(Stock Code: 826)

ANNOUNCEMENT OF THE INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2012

FINANCIAL HIGHLIGHTS

Revenue of the Group for the first half of 2012 totaled RMB1,727,010,000, representing an increase of 11.2% when compared with RMB1,553,550,000 for the same period in 2011.

The three main product segments of the Group grew in the first half of 2012. Revenue of High Speed Steel ("HSS"), HSS cutting tools and Die Steel ("DS") increased by approximately 25.4%, 4.8% and 16.9%, respectively, when compared with those for the same period in 2011.

Profit attributable to equity shareholders of the Company was RMB212,981,000 (1H2011: RMB150,473,000), representing an increase of 41.5% when compared with that for the same period in 2011.

The Board of Directors (the "Board") of Tiangong International Company Limited (the "Company") is pleased to announce the unaudited consolidated statement of comprehensive income of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2012 and the consolidated statement of financial position of the Group as at 30 June 2012 which have been reviewed by the Audit Committee of the Company, together with the comparative figures for the same period of 2011 as follows:

Consolidated statement of comprehensive income
for the six months ended 30 June 2012(unaudited)

		Six months ended 30 June	
		2012	2011
	Note	***RMB'000***	*RMB'000*
Revenue	4	**1,727,010**	1,553,550
Cost of sales		**(1,347,266)**	(1,248,576)
Gross profit		**379,744**	304,974
Other income	5	**13,504**	12,068
Distribution expenses		**(22,286)**	(17,867)
Administrative expenses		**(51,173)**	(30,696)
Other expenses		**(13,018)**	(13,858)
Result from operations		**306,771**	254,621
Finance income		**6,316**	1,523
Finance expenses		**(58,081)**	(75,904)
Net finance costs	6(a)	**(51,765)**	(74,381)
Share of profits of associates		**561**	270
Share of (losses)/profits of jointly controlled entities		**(1,099)**	762
Profit before income tax	6	**254,468**	181,272
Income tax expense	7	**(41,487)**	(30,799)
Profit for the period attributable to the equity shareholders of the Company		**212,981**	150,473
Other comprehensive income for the period			
Foreign currency translation differences -equity-accounted investees		**265**	—
Total comprehensive income for the period attributable to the equity shareholders of the Company		**213,246**	150,473
Earnings per share (RMB)			
Basic	8	**0.122**	0.090
Diluted		**0.119**	0.087

Consolidated statement of financial position
as at 30 June 2012 (unaudited)

	Note	At 30 June 2012 RMB'000	At 31 December 2011 RMB'000
Non-current assets			
Property, plant and equipment		**1,968,860**	1,793,278
Lease prepayments		**71,764**	72,555
Goodwill		**21,959**	21,959
Interest in associates		**44,533**	37,345
Interest in jointly controlled entities		**8,779**	5,835
Other financial assets		**10,000**	10,000
Deferred tax assets		**17,180**	12,721
		2,143,075	1,953,693
Current assets			
Inventories		**1,124,812**	1,177,805
Trade and other receivables	9	**1,593,975**	1,271,413
Pledged deposits		**408,450**	149,894
Time deposits		**330,000**	474,000
Cash and cash equivalents		**249,108**	103,089
		3,706,345	3,176,201
Current liabilities			
Interest-bearing borrowings		**1,744,604**	1,516,203
Trade and other payables	10	**1,261,685**	986,897
Income tax payables		**39,622**	31,403
Deferred income		**1,162**	1,162
		3,047,073	2,535,665
Net current assets		**659,272**	640,536
Total assets less current liabilities		**2,802,347**	2,594,229
Non-current liabilities			
Interest-bearing borrowings		**275,000**	427,000
Deferred income		**5,447**	6,028
Deferred tax liabilities		**24,739**	21,884
		305,186	454,912
Net assets		**2,497,161**	2,139,317
Capital and reserves			
Share capital		**34,541**	31,806
Reserves		**2,462,620**	2,107,511
Total equity		**2,497,161**	2,139,317

NOTES:

1. REPORTING ENTITY

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 interim financial report of the Company as at and for the six months ended 30 June 2012 comprises the Company and its subsidiaries (collectively referred to as the "Group") and the Group's interest in associates and jointly controlled entities.

2. BASIS OF PREPARATION

This interim financial report of Tiangong International Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard ("IAS") 34, Interim financial reporting, issued by the International Accounting Standards Board ("IASB"). It was authorised for issue on 20 August 2012.

The interim financial report has been prepared in accordance with the same accounting policies adopted in the 2011 annual financial statements, except for the accounting policy changes and adoptions that are expected to be reflected in the 2012 annual financial statements. Details of these changes and adoptions of accounting policies are set out in the following notes. The interim financial report has not been audited by the Company's auditors, but has been reviewed by the Company's Audit Committee.

The preparation of an interim financial report in conformity with IAS 34 requires management to make judgments, estimates and assumptions that affect the application of policies and report amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

This interim financial report contains condensed consolidated financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the 2011 annual financial statements. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with International Financial Reporting Standards ("IFRSs").

The financial information relating to the financial year ended 31 December 2011 that is included in the interim financial report as being previously reported information does not constitute the Company's annual financial statements for that financial year but is derived from those financial statements. Annual financial statements for the year ended 31 December 2011 are available from the Company's registered office. The auditor has expressed an unqualified opinion on those financial statements in the report dated 26 March 2012.

3. CHANGES IN ACCOUNTING POLICIES

The IASB has issued a few amendments to IASs that are first effective for the current accounting period of the Group and the Company. These include the amendments to IFRS 7, *Financial instruments: Disclosures — Transfers of financial assets* and the amendments to IAS 12, *Income taxes — Deferred tax: recovery of underlying assets*. None of the developments are relevant to the Group's financial statements and the Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

4. SEGMENT REPORTING

The Group has four reportable segments, as described below, which are the Group's product divisions. For each of the product divisions, the Chairman (the chief operating decision maker) reviews internal management reports on at least a monthly basis. No operating segments have been aggregated to form the following reportable segments.

The following summary describes the operations in each of the Group's 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.
- *Chemical goods* The chemical goods segment sells purified terepthatic acid and other chemicals.

(a) Segment results, assets and liabilities

	Six months ended and as at 30 June 2012				
	HSS	**HSS cutting tools**	**DS**	**Chemical goods**	**Total**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenue from external customers	**719,592**	**307,362**	**572,591**	**127,465**	**1,727,010**
Inter-segment revenue	**107,373**	**—**	**—**	**—**	**107,373**
Reportable segment revenue	**826,965**	**307,362**	**572,591**	**127,465**	**1,834,383**
Reportable segment profit (adjusted EBIT)	**178,083**	**41,604**	**136,443**	**1,328**	**357,458**
Reportable segment assets	**1,612,002**	**775,368**	**2,283,289**	**94,237**	**4,764,896**
Reportable segment liabilities	**364,635**	**261,590**	**443,074**	**88,928**	**1,158,227**

	Six months ended 30 June 2011				
	HSS	HSS cutting tools	DS	Chemical goods	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenue from external customers	573,672	293,215	489,990	196,673	1,553,550
Inter-segment revenue	121,992	—	—	—	121,992
Reportable segment revenue	695,664	293,215	489,990	196,673	1,675,542
Reportable segment profit (adjusted EBIT)	117,335	43,493	122,706	3,573	287,107

	As at 31 December 2011				
	HSS	HSS cutting tools	DS	Chemical goods	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Reportable segment assets	1,306,754	837,763	2,151,307	28,742	4,324,566
Reportable segment liabilities	305,063	160,100	506,202	12	971,377

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

Revenue	Six months ended 30 June **2012** *RMB'000*	 2011 *RMB'000*
Reportable segment revenue	**1,834,383**	1,675,542
Elimination of inter-segment revenue	**(107,373)**	(121,992)
Consolidated revenue	**1,727,010**	1,553,550

Profit	Six months ended 30 June **2012** *RMB'000*	 2011 *RMB'000*
Reportable segment profit	**357,458**	287,107
Net finance costs	**(51,765)**	(74,381)
Share of profits of associates	**561**	270
Share of (losses)/profits of jointly controlled entities	**(1,099)**	762
Other unallocated head office and corporate expenses	**(50,687)**	(32,486)
Consolidated profit before income tax	**254,468**	181,272

Assets	**At** **30 June** **2012** *RMB'000*	At 31 December 2011 *RMB'000*
Reportable segment assets	**4,764,896**	4,324,566
Interest in associates	**44,533**	37,345
Interest in jointly controlled entities	**8,779**	5,835
Other financial assets	**10,000**	10,000
Deferred tax assets	**17,180**	12,721
Pledged deposits	**408,450**	149,894
Time deposits	**330,000**	474,000
Cash and cash equivalents	**249,108**	103,089
Other unallocated head office and corporate assets	**16,474**	12,444
Consolidated total assets	**5,849,420**	5,129,894

Liabilities	**At** **30 June** **2012** *RMB'000*	At 31 December 2011 *RMB'000*
Reportable segment liabilities	**1,158,227**	971,377
Interest-bearing borrowings	**2,019,604**	1,943,203
Income tax payables	**39,622**	31,403
Deferred tax liabilities	**24,739**	21,884
Other unallocated head office and corporate liabilities	**110,067**	22,710
Consolidated total liabilities	**3,352,259**	2,990,577

5. OTHER INCOME

		Six months ended 30 June	
		2012	2011
		RMB'000	*RMB'000*
Government grants	(i)	**12,266**	5,968
Dividend income from unlisted securities		**800**	—
Foreign exchange gain		**—**	5,965
Others		**438**	135
		13,504	12,068

(i) Jiangsu Tiangong Tools Company Limited ("TG Tools"), a wholly-owned subsidiary of the Company located in the People's Republic of China (the "PRC"), received unconditional grants amounting to RMB11,685,000 (six months ended 30 June 2011: RMB5,387,000) from the local government in Danyang mainly to reward its contribution to the local economy and encourage its innovation of technology. It also recognised amortisation of government grants related to assets of RMB581,000 (six months ended 30 June 2011: RMB581,000) during the six months ended 30 June 2012.

6. PROFIT BEFORE INCOME TAX

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

(a) Net finance costs

	Six months ended 30 June	
	2012	2011
	RMB'000	*RMB'000*
Interest income	**(6,316)**	(1,523)
Finance income	**(6,316)**	(1,523)
Interest on bank loans	**71,389**	49,575
Fair value recognised upon warrants issuance	**—**	42,754
Change in fair value of warrants	**—**	(5,566)
Less: interest expense capitalised into property, plant and equipment under construction	**(13,308)**	(10,859)
Finance expenses	**58,081**	75,904
Net finance costs	**51,765**	74,381

(b) Other items

	Six months ended 30 June	
	2012	2011
	RMB'000	*RMB'000*
Cost of inventories*	**1,347,266**	1,248,576
Depreciation	**61,135**	55,927
Amortisation of lease prepayments	**791**	663
Provision for impairment of doubtful debts	**7,651**	12,972
Provision/(Reversal) for write-down of inventories	**2,359**	(5,052)
Equity settled share-based transactions	**3,609**	2,937

* Cost of inventories includes RMB51,911,000 (six months ended 30 June 2011: RMB39,952,000) relating to depreciation expenses and write-down/(write-back) of inventories provision which amounts are also included in the respective total amounts disclosed separately above for each of these types of expenses.

7. INCOME TAX EXPENSE

	Six months ended 30 June	
	2012	2011
	RMB'000	*RMB'000*
Current tax		
Provision for PRC income tax	**42,528**	29,293
Provision for Hong Kong profits tax	**562**	—
	43,090	29,293
Deferred tax		
Origination and reversal of temporary differences	**(1,603)**	1,506
	41,487	30,799

(a) 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.

(b) 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.

The statutory corporate income tax rate of the Group's operating subsidiaries in the PRC is 25% (2011: 25%).

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 corporate 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 is calculated commencing from the year of 2008.

Due to the above-mentioned tax holiday, TG tools and Tiangong Aihe Special Steel Company Limited ("TG Aihe") are subject to the PRC corporate income tax rate at 50% of its applicable tax rate for 3 years from 2009 and 2010 respectively. In 2012, the applicable income tax rate of TG Aihe is 12.5% (2011: 12.5%).

TG tools was applying for renewal of its High and New Technology Enterprise status during the six months ended 30 June 2012 and if approved, it is eligible to enjoy a preferential income tax rate of 15%. TG tools was qualified as High and New Technology Enterprise during the years 2009 to 2011. Management is of the opinion that it is highly probable that this qualification will be renewed and approved by government before the end of year 2012 as it has met the conditions of qualification. In 2012, the estimated annual effective income tax rate of TG Tools to calculate the income tax expense is 15% (2011: 12.5%).

Danyang Tianfa Forging Company Limited ("Tianfa Forging"), Jiangsu Tiangong Titanium Technology Company Limited ("TG Titan") and Jiangsu Tiangong Mould Steel R&D Center Company Limited ("TG Mould") are all subject to the statutory income tax rate of 25%.

(c) Hong Kong profits tax has been provided at the rate of 16.5% (2011: Nil) on the estimated assessable profits arising in Hong Kong during the six months ended 30 June 2012.

8. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to equity shareholders of the Company of RMB212,981,000 during the period presented (six months ended 30 June 2011: RMB150,473,000) and the weighted average number of ordinary shares outstanding of 1,739,618,785 (six months ended 30 June 2011: 1,678,000,000).

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on the profit attributable to equity shareholders of the Company of RMB212,981,000 during the period presented (six months ended 30 June 2011: RMB150,473,000) and the weighted average number of potential ordinary shares outstanding of 1,791,814,846 (six months ended 30 June 2011: 1,721,317,781) for the six months ended 30 June 2012 after taking into account the potential dilutive effect of the warrants and equity settled share-based transactions.

9. TRADE AND OTHER RECEIVABLES

	At 30 June 2012 *RMB'000*	At 31 December 2011 *RMB'000*
Trade receivables	**1,305,309**	858,750
Bills receivable	**203,964**	273,752
Less: impairment provision for doubtful debts	**(58,845)**	(51,194)
Net trade and bills receivable	**1,450,428**	1,081,308
Prepayments	**126,988**	173,768
Non-trade receivables	**16,559**	16,337
	1,593,975	1,271,413

Included in trade and other receivables are debtors and bills receivable (net of allowance for doubtful debts) with the following ageing analysis:

	At 30 June 2012 *RMB'000*	At 31 December 2011 *RMB'000*
Current	**1,063,576**	809,438
Less than 3 months past due	**235,686**	169,559
More than 3 months but less than 6 months past due	**124,780**	88,579
More than 6 months but less than 12 months past due	**23,529**	8,040
More than 12 months but less than 24 months past due	**2,857**	5,692
Trade debtors and bills receivable, net of allowance for doubtful debts	**1,450,428**	1,081,308

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.

10. TRADE AND OTHER PAYABLES

Included in trade and other payables are trade creditors and bills payable with the following ageing analysis as at the date of the consolidated statement of financial position.

	At 30 June 2012 *RMB'000*	At 31 December 2011 *RMB'000*
Due within 3 months	**729,751**	653,175
Due after 3 months but within 6 months	**267,962**	185,580
Due after 6 months but within 12 months	**39,317**	6,066
Due after 1 year but within 2 years	**129**	3,424
Due after 2 years	**20**	2,038
Total trade creditors and bills payable	**1,037,179**	850,283
Non-trade payables and accrued expenses	**143,962**	136,614
Dividends payable	**80,544**	—
	1,261,685	986,897

11. CAPITAL, RESERVES AND DIVIDENDS

(a) Dividends payable to equity shareholders attributable to the previous financial year, approved but not paid during the interim period:

	Six months ended 30 June	
	2012	2011
	RMB'000	*RMB'000*
Dividend in respect of the previous financial year, approved but not paid during the interim period, of RMB0.048 per share (six months ended 30 June 2011: RMB0.028125 per share)	**80,544**	47,194

(b) Issuance of new ordinary shares

During the six months ended 30 June 2012, the Company issued 125,000,000 new ordinary shares of HKD1.87 each. Total proceeds of RMB182,483,000, net of share issuance expenses, were raised of which RMB1,976,000 was credited to share capital and the balance of RMB180,507,000 was credited to the share premium account.

(c) Issuance of share upon exercise of warrants

During the six months ended 30 June 2012, a total of 48,000,000 warrants were exercised at an aggregated price paid of RMB39,050,000. Following the exercise of warrants, the share capital and share premium accounts of the Company have been increased by RMB759,000 and RMB52,237,000, respectively. Included in the amounts is RMB13,946,000 which has been transferred from the capital reserve to the share premium account.

MANAGEMENT DISCUSSION AND ANALYSIS

Market Review

In the first half of 2012, the global economy continued to deteriorate. Worse still, the Chinese economy showed signs of cooling down after years of continuous growth. Unlike the generic steel industry, high speed steel (HSS) and die steel are specialized products and their production required rare metals and complicated technology. As they are widely applied in many different industrial machineries; hence, demands remain firm and prices being relatively stable. The Group, being the largest HSS manufacturer and a leading die steel manufacturers in China, has strong competitive advantages over both foreign and most domestic competitors. These advantages have facilitated the Group in capturing greater market shares even under the adverse macro environment:

Competitive advantages:

1. *Sizable production scale*

   The Group is the dominant player in HSS industry with an annual production capacity of approximately 50,000 tons.

2. *Significant cost advantages over foreign competitors*

   China has the world's largest reserves of rare metals such as tungsten, molybdenum and vanadium, which are essential raw materials for high grade HSS and die steel production. In recent years, China has imposed strict quotes as well as hefty levies on "direct" exports of rare metals. This has led to foreign competitors suffering from higher raw material costs and unstable supply.

3. *Tight credit environment squeezes out small-scale players and speeds up market consolidation*

   To combat inflationary pressure, Chinese government has tightened monetary and credit conditions since 2010. Consequently, small-scale domestic players have been forced to close down. This market consolidation actually led to an increased market share for the Group.

Business Review

In the first half of 2012, the Group's revenue achieved substantial growth to RMB1,727,010,000, representing an increase of approximately 11.2% year-on-year. Core product segments including HSS, HSS cutting tools and die steel recorded an encouraging year-on-year growth of approximately 25.4%, 4.8% and 16.9% respectively.

	For the six months ended 30 June					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS	**719,592**	**41.7**	573,672	36.9	145,920	25.4
HSS cutting tools	**307,362**	**17.8**	293,215	18.9	14,147	4.8
Die Steel	**572,591**	**33.1**	489,990	31.5	82,601	16.9
Chemical goods	**127,465**	**7.4**	196,673	12.7	(69,208)	(35.2)
Total	**1,727,010**	**100.0**	1,553,550	100.0	173,460	11.2

During the period, the Group has achieved significant improvement in profitability with profit attributable to the equity shareholders of the Company surged by approximately 41.5% year-on-year. Gross profit margin of the Group was approximately 22.0% (1H2011: 19.6%) while net profit margin increased remarkably to approximately 12.3% (1H2011: 9.7%). The profit enhancement was mainly attributable to the improving production efficiency and curbing production wastage. The Group has invested heavily in advanced forging machineries and automating HSS and die steel production facilities over the past few years. Such measures have significantly enhanced yield rate and alleviate the pressure brought by soaring labor cost.

HSS — accounted for 42% of the Group's revenue in 1H2012

HSS is a widely used alloy in specific industrial applications including automotive, machinery manufacturing, aviation and electronic industries. Its production involves various rare metals, such as tungsten, molybdenum, chromium, vanadium and other raw materials.

During the period under review, HSS continued to be the greatest revenue contributor of the Group. Revenue from HSS grew by approximately 25.4% to RMB719,592,000 (1H2011: RMB573,672,000).

	For the six months ended 30 June					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS						
Domestic	**632,420**	**87.9**	524,512	91.4	107,908	20.6
Export	**87,172**	**12.1**	49,160	8.6	38,012	77.3
	719,592	**100.0**	573,672	100.0	145,920	25.4

HSS Cutting Tools — accounted for 18% of the Group's revenue in 1H2012

HSS cutting tool products can be categorized into four major types — twist drill bits, screw taps, end mills and turning tools, which are mainly used in industrial manufacturing. The Group's vertical integration from upstream HSS production to downstream HSS cutting tool production brought us significant cost advantage over our peers.

In 1H2012, revenue generated from HSS cutting tools increased to RMB307,362,000 (1H2011: RMB293,215,000), representing a 4.8% year-on-year growth.

	For the six months ended 30 June					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS Cutting Tools						
Domestic	**126,518**	**41.2**	108,617	37.0	17,901	16.5
Export	**180,844**	**58.8**	184,598	63.0	(3,754)	(2.0)
	307,362	**100.0**	293,215	100.0	14,147	4.8

Die Steel — accounted for 33% of the Group's revenue in 1H2012

Die steel, used in die and mould casting and machining processing, is mainly applied in sectors such as automotive industry, high-speed railway construction, aviation and plastic product manufacturing. Its production involves various rare metals.

Revenue generated from die steel in 1H2012 reached RMB572,591,000 (1H2011: RMB489,990,000), representing a 16.9% increase.

	For the six months ended 30 June					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
Die steel						
Domestic	**355,114**	**62.0**	257,415	52.5	97,699	38.0
Export	**217,477**	**38.0**	232,575	47.5	(15,098)	(6.5)
	572,591	**100.0**	489,990	100.0	82,601	16.9

Titanium Alloy

Titanium alloy is lighter and stronger with higher corrosion resistance as compared to aluminum alloy. Thus, it is mainly applied in aviation, marine engineering, medical and chemical industry. Its production involves sponge titanium and various rare metals.

With an initial production capacity of 1,500–2,000 tons, the titanium production line commenced production at the end of 2011. During the period, titanium alloy contributed approximately RMB18 million to the Group's revenue. The Group started by producing titanium ingots and rods in the first phase, and will gradually extend to higher margin products such as titanium pipes and flat sheets in the near future.

Titanium alloy segment is currently in the market development stage and satisfactory results have been achieved. Aerospace, chemical processing, military and other industrial application are the main sectors consuming titanium alloy. The Group has been actively seeking business opportunities in different potential areas. The Group aims to offer a broader range of products with higher grades and specifications to meet demands from various industries. It is expected that titanium will soon become another pillar revenue source for the Group in the future.

Outlook

The Group remains optimistic towards the second half of 2012 with focuses on further containing costs and advancing into new markets. During the period, the Group introduced a new production line for high speed steel and die steel production. Our consistent margin improvement has been a testimony for the success of all these cost reduction measures. Apart from that, the Group has expanding its footprint to emerging economies since 2011. A jointly controlled entity has been set up in India in June this year and another one is planning to be set up in Brazil in the future. As emerging economies are furious in urbanization and industrial development, which will subsequently fuel the demand of HSS, HSS cutting tools and die steel, hence, the Group believes that advancing into these markets will broaden our revenue base and generate promising return.

Other than our HSS, HSS cutting tools and die steel business, the Group is confident that our recently developed titanium alloy business will be a growth engine in the near future. Although titanium is often more expensive than other competing metals; however, it is a better alternative in industrial and aerospace application because of its strength, durability and overall performance. Through research & development and technology enhancement, we will continue to venture into the new material industry and create long term value for our shareholders.

Financial review

As a result of the increase penetration in the market share of the Group's products, revenue of all of the Group's main businesses increased. The net profit attributable to equity shareholders of the Company increased by approximately 41.5% to RMB212,981,000 in the first half of 2012 from RMB150,473,000 for the first half of 2011 was also due to the one-off fair value change of warrants amounting to RMB37,188,000 incurred in the prior year.

Revenue

Revenue of the Group for the first half of 2012 totalled RMB1,727,010,000, representing an increase of approximately 11.2% when compared with RMB1,553,550,000 in first half of 2011. The increase was mainly attributable to the increase in sales volume of the products of the Group.

Cost of sales

The Group's cost of sales increased by RMB98,690,000 from RMB1,248,576,000 for the first half of 2011 to RMB1,347,266,000 for the first half of 2012, representing an increase of approximately 7.9%. The increase was due to the increase in revenue during the period. As a percentage of total revenue, the Group's cost of sales decreased from approximately 80.4% in the first half of 2011 to approximately 78.0% in the first half of 2012.

Gross margin

For the first half of 2012, the gross margin was approximately 22.0% (1H2011: 19.6%). Set out below is the gross margin for our four products for the first half of 2011 and 2012:

	For the period ended 30 June	
	2012	2011
HSS	**25.8%**	21.3%
HSS cutting tools	**15.0%**	16.2%
Die steel	**25.7%**	26.8%
Chemical goods	**1.0%**	1.8%

HSS

The HSS gross margin increased from 21.3% in the first half of 2011 to 25.8% in the same period in 2012, which was mainly due to the benefit from the operating leverage as a result from the increase in production volume.

HSS cutting tools

In the first half of 2012, the gross margin of HSS cutting tools decreased slightly to 15.0% (1H2011: 16.2%) as a result of the decrease in average selling price.

Die steel

The gross margin of die steel decreased slightly from 26.8% in the first half of 2011 to 25.7% in the first half of 2012. The decrease was mainly due to the increase in the sales of hot die steel which had a lower gross profit margin as compared with cold die steel.

Other income

The Group's other income totalled RMB13,504,000 in the first half of 2012, representing an increase of RMB1,436,000 from RMB12,068,000 in the first half of 2011. The increase was mainly attributable to the increase in government grants received from the government.

Distribution expenses

The Group's distribution expenses was RMB22,286,000 (1H2011: RMB17,867,000), representing an increase of approximately 24.7%. The increase was mainly attributable to the increase in transportation expenses as a result of the increase in shipping charges. For the first half of 2012, the distribution expenses as a percentage of revenue was 1.3% (1H2011: 1.2%).

Administrative expenses

For the first half of 2012, the Group's administrative expenses increased by RMB20,477,000 to RMB51,173,000 (1H2011: RMB30,696,000) primarily due to the increase in the share option costs and the increase of social security fund to the employees for the first half of 2012, the administrative expenses as a percentage of revenue was 3.0% (1H2011: 2.0%).

Net finance cost

The Group's finance income was RMB6,316,000 for the first half of 2012, representing an increase of RMB4,793,000 when compared with the RMB1,523,000 for the first half of 2011. The increase was mainly due to the increase in time deposit as well as a higher bank deposit rate in the first half of 2012. The Group's finance expenses were RMB58,081,000 for the first half of 2012, representing a decrease of 23.5% when compared with the RMB75,904,000 for the first half of 2011. The decrease was attributable to the net effect of the recognition of the one-off fair value change of warrants amounting to RMB37,188,000 during the first half of 2011 and the increase in interest-bearing borrowings in 2012 compared with the same period last year.

Income tax expense

The Group's income tax expense increased by RMB10,688,000 from RMB30,799,000 in the first half of 2011 to RMB41,487,000 in the first half of 2012. Such increase was mainly due to the increase in sales and net profits.

Profit for the period

As a result of the factors discussed above, the Group's profit increased by approximately 41.5% to RMB212,981,000 for the first half of 2012 from RMB150,473,000 for the first half of 2011. The Group's net profit margin increased remarkably from 9.7% in the first half of 2011 to 12.3% in the same period of 2012 mainly due to the effect of the operating leverage.

Profit attributable to equity shareholders of the Company

For the first half of 2012, profit attributable to equity shareholders of the Company was RMB212,981,000 (1H2011: RMB150,473,000), representing an increase of 41.5%.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2012, the Group's current assets mainly included cash and cash equivalents of approximately RMB249,108,000, inventories of approximately RMB1,124,812,000, trade and other receivables of RMB1,593,975,000, time deposits of RMB330,000,000 and pledged deposits of RMB408,450,000. As at 30 June 2012, the interest-bearing borrowings of the Group were RMB2,019,604,000, RMB 1,744,604,000 of which were repayable within one year and RMB275,000,000 of which were repayable over one year. The Group's gearing ratio (calculated based on the total outstanding interest-bearing debt divided by the total equity) was 80.9%, lower than 90.8% as at 31 December 2011. The decrease was mainly attributable to the placement of new shares which generated approximately RMB182 million of capital during the period. As at 30 June 2012, borrowings of RMB1,934,300,000 were in RMB, USD11,744,831 were in USD and EUR1,400,000 were in EUR. The majority of the borrowings of the Group were subject to interests payable at the rates ranging from 0.30% to 7.87%. 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 the first half of 2012, the Group's net increase in fixed assets amounted to RMB175,582,000, which were mainly for the rod and wire rolling production line. As at 30 June 2012, capital commitments were RMB268,924,000, of which RMB59,700,000 was contracted and RMB209,224,000 was authorised but not contracted for. The majority of the capital commitments was related to the acquisition of production equipment.

FOREIGN EXCHANGE EXPOSURE

The Group's revenues were denominated in RMB, US dollars and Euros, with RMB accounting for the largest portion (approximately 58%). Approximately 42% of the total sales and the Group's costs and operating profit were subject to exchange rate fluctuations. The Group did not enter into any financial instrument to hedge against foreign exchange risk. 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 30 June 2012, the Group pledged certain bank deposits amounting to approximately RMB408,450,000 (31 December 2011: RMB149,894,000). Details are set out in the notes to the financial statements.

EMPLOYEE'S REMUNERATION AND TRAINING

As at 30 June 2012, the Group employed 3,962 employees (31 December 2011: 3,910). 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 education and training for all of its staff on a regular basis.

CONTINGENT LIABILITIES

The Company had no material contingent liabilities as at 30 June 2012.

INTERIM DIVIDEND

The Directors do not recommend the payment of an interim dividend for the period (no interim dividend for the six months period ended 30 June 2011).

SHARE OPTIONS SCHEME

The Company adopted a share options scheme (the "Scheme") in July 2007. On 28 January 2011, options entitled holders to subscribe for a total of 4,970,000 shares of USD0.01 each were granted to certain of the directors and employees of the Company in respect of their services to the Group. These share options had vested on 1 July 2012 and have an initial exercise price of HKD5.10 per share of USD0.01 each and an exercise period ranging from 1 July 2012 to 30 June 2016. The closing price of the Company's shares at the date of grant was HKD5.10 per share of USD0.01 each. Due to the implementation of Share Subdivision on 23 May 2011, the maximum aggregate number of shares which may be issued under the share option scheme was adjusted to 19,880,000 shares of USD0.0025 each at an exercise price of HKD1.275.

PURCHASE, SALES OR REDEMPTION OF SHARES

During the six months ended 30 June 2012, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of its securities.

CORPORATE GOVERNANCE

During the six months ended 30 June 2012, the Company has, so far where applicable, complied with 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 three independent non-executive directors. The Audit Committee held a meeting on 20 August 2012 to consider and review the interim report and interim financial statements of the Group and to give their opinion and recommendation to the Board. The Audit Committee considers that the 2012 interim report and interim financial statements of the Company have complied with the applicable accounting standards and the Company has made appropriate disclosure thereof.

THE MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS OF LISTED ISSUERS

The Company has adopted a code of conduct regarding directors' securities transactions on terms no less exacting than the required standard set out in the "Model Code for Securities Transactions by Directors of Listed Issuers" as set out in Appendix 10 of the Listing Rules. Having made specific enquiry of all directors of the Company, all directors of the Company have complied with the required standard set out in the Model Code and the Company's code of conduct regarding directors' securities transactions.

APPRECIATION

The board of Directors would like to take this opportunity to express gratitude to our shareholders, customers, the management and employees for their unreserved support to the Group.

By Order of the Board
Tiangong International Company Limited
Zhu Xiaokun
Chairman

Hong Kong, 20 August 2012

As at the date of this announcement, the directors of the Company are:

Executive Directors: ZHU Xiaokun, ZHU Zhihe, YAN Ronghua and WU Suojun

Independent non-executive Directors: LI Zhengbang, GAO Xiang and LEE Cheuk Yin, Dannis

* *For identification purpose*