Tiangong International Company Limited
天 工 國 際 有 限 公 司*

(incorporated in the Cayman Islands with limited liability)

(Stock Code: 826)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2012

FINANCIAL HIGHLIGHTS

- Revenue for the Group for 2012 totaled RMB3,118 million, representing a slight increase as compared with RMB3,112 million in the previous year.
- Gross profit margin increased from 22.7% in 2011 to 23.4% in 2012.
- Profit attributable to equity shareholders of the Company increased by approximately 22% to RMB445 million (2011: RMB365 million).
- Basic earnings per share was RMB0.244 (2011: RMB0.218).
- The Board proposed a final dividend of RMB0.0461 per share for the year ended 31 December 2012.

The Board of Directors (the "Board") of Tiangong International Company Limited (the "Company") is pleased to announce the audited consolidated statement of comprehensive income of the Company and its subsidiaries (the "Group") for the year ended 31 December 2012 and the consolidated statement of financial position of the Group as at 31 December 2012, together with the comparative figures for the same period of 2011 as follows:

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2012

	Note	2012 RMB'000	2011 RMB'000
Revenue	4	**3,118,251**	3,111,763
Cost of sales		**(2,388,862)**	(2,405,000)
Gross profit		**729,389**	706,763
Other income	5	**78,944**	12,701
Distribution expenses		**(44,583)**	(36,890)
Administrative expenses		**(100,437)**	(85,924)
Other expenses		**(14,661)**	(34,057)
Profit from operations		**648,652**	562,593
Finance income		**10,588**	4,087
Finance expenses		**(118,538)**	(133,030)
Net finance costs	6(a)	**(107,950)**	(128,943)
Share of losses of associates		**(209)**	(221)
Share of (losses)/profits of jointly controlled entities		**(3,593)**	1,703
Profit before taxation	6	**536,900**	435,132
Income tax	7	**(92,008)**	(69,805)
Profit for the year attributable to equity shareholders of the Company		**444,892**	365,327
Other comprehensive income/(loss) for the year			
Exchange differences on translation of financial statements of overseas associates and jointly controlled entities		**677**	(3,715)
Total comprehensive income for the year attributable to equity shareholders of the Company		**445,569**	361,612
Earnings per share (RMB)	8		
Basic		**0.244**	0.218
Diluted		**0.240**	0.212

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at 31 December 2012

	Note	2012 RMB'000	2011 RMB'000
Non-current assets			
Property, plant and equipment		**2,143,725**	1,793,278
Lease prepayments		**70,972**	72,555
Goodwill		**21,959**	21,959
Interest in associates		**43,647**	37,345
Interest in jointly controlled entities		**6,637**	5,835
Other financial assets		**10,000**	10,000
Deferred tax assets		**12,336**	12,721
		2,309,276	1,953,693
Current assets			
Inventories		**1,426,003**	1,177,805
Trade and other receivables	9	**1,530,598**	1,271,413
Pledged deposits		**238,479**	149,894
Time deposits		**446,000**	474,000
Cash and cash equivalents		**150,499**	103,089
		3,791,579	3,176,201
Current liabilities			
Interest-bearing borrowings		**1,886,407**	1,516,203
Trade and other payables	10	**1,147,200**	986,897
Current taxation		**43,578**	31,403
Deferred income		**1,162**	1,162
		3,078,347	2,535,665
Net current assets		**713,232**	640,536
Total assets less current liabilities		**3,022,508**	2,594,229
Non-current liabilities			
Interest-bearing borrowings		**201,638**	427,000
Deferred income		**4,866**	6,028
Deferred tax liabilities		**28,721**	21,884
		235,225	454,912
Net assets		**2,787,283**	2,139,317
Capital and reserves			
Share capital		**35,803**	31,806
Reserves		**2,751,480**	2,107,511
Total equity		**2,787,283**	2,139,317

NOTES

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 2012 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group's interests in associates and jointly controlled entities. 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

The annual results set out in the announcement do not constitute the Group's financial statements for the year ended 31 December 2012 but are extracted from those financial statements.

The financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs"), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards ("IASs") and Interpretations issued by the International Accounting Standards Board ("IASB"). This announcement also complies with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). In addition, this announcement has been reviewed by the Company's Audit Committee.

The figures in respect of this announcement of the Group's results for the year ended 31 December 2012 have been compared by the Company's auditor, KPMG, Certified Public Accountants, to the amounts set out in the Group's financial statements for the year and the amounts were found to be in agreement. The work performed by KPMG in respect of this announcement was limited and did not constitute an audit, review or other assurance engagement and consequently no assurance has been expressed by the auditor on this announcement.

3 CHANGES IN ACCOUNTING POLICIES

The IASB has issued certain amendments to IFRSs 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 REVENUE AND SEGMENT REPORTING

Revenue represents mainly the sales value of high alloy steel, including high speed steel ("HSS") and die steel ("DS"), HSS cutting tools, trading of goods and titanium alloy after eliminating intercompany transactions.

The Group has five 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* 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* The DS segment manufactures and sells die steel for the steel industry.

— *Trading of goods* The trading of goods segment sells aluminium and chemical goods (purified terepthatic acid).

— *Titanium alloy* The titanium alloy segment manufactures and sells titanium alloy for the titanium industry.

(a) Segment results, assets and liabilities

For the purposes of assessing segment performance and allocating resources between segments, the Chairman (the chief operating decision maker) 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 payable, 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 share of profits less losses of associates and jointly controlled entities and other head office or corporate administration costs.

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 used by the segments in their operations.

Information regarding the Group's reportable segments as provided to the Chairman (the chief operating decision maker) for the purposes of resource allocation and assessment of segment performance for the years ended 31 December 2012 and 2011 is set out below.

	Year ended and as at 31 December 2012					
	HSS	**HSS cutting tools**	**DS**	**Trading of goods**	**Titanium alloy**	**Total**
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenue from external customers	**1,092,587**	**567,297**	**1,038,826**	**386,076**	**33,465**	**3,118,251**
Inter-segment revenue	**255,988**	**—**	**—**	**—**	**—**	**255,988**
Reportable segment revenue	**1,348,575**	**567,297**	**1,038,826**	**386,076**	**33,465**	**3,374,239**
Reportable segment profit (adjusted EBIT)	**285,931**	**83,275**	**304,493**	**3,757**	**7,350**	**684,806**
Reportable segment assets	**1,684,968**	**805,351**	**2,427,432**	**90,113**	**144,000**	**5,151,864**
Reportable segment liabilities	**396,387**	**179,036**	**519,991**	**27,913**	**13,692**	**1,137,019**

	Year ended and as at 31 December 2011					
	HSS	HSS cutting tools	DS	Trading of goods	Titanium alloy	Total
	RMB'000	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*	*RMB'000*
Revenue from external customers	1,158,264	609,675	985,733	358,091	—	3,111,763
Inter-segment revenue	213,322	—	—	—	—	213,322
Reportable segment revenue	1,371,586	609,675	985,733	358,091	—	3,325,085
Reportable segment profit (adjusted EBIT)	266,700	88,696	308,671	5,806	—	669,873
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

	2012	2011
	RMB'000	*RMB'000*
Revenue		
Reportable segment revenue	**3,374,239**	3,325,085
Elimination of inter-segment revenue	**(255,988)**	(213,322)
Consolidated revenue	**3,118,251**	3,111,763

	2012	2011
	RMB'000	*RMB'000*
Profit		
Reportable segment profit	**684,806**	669,873
Net finance costs	**(107,950)**	(128,943)
Share of losses of associates	**(209)**	(221)
Share of (losses)/profits of jointly controlled entities	**(3,593)**	1,703
Unallocated head office and corporate expenses	**(36,154)**	(107,280)
Consolidated profit before taxation	**536,900**	435,132

	2012	2011
	RMB'000	*RMB'000*
Assets		
Reportable segment assets	**5,151,864**	4,324,566
Interest in associates	**43,647**	37,345
Interest in jointly controlled entities	**6,637**	5,835
Other financial assets	**10,000**	10,000
Deferred tax assets	**12,336**	12,721
Pledged deposits	**238,479**	149,894
Time deposits	**446,000**	474,000
Cash and cash equivalents	**150,499**	103,089
Unallocated head office and corporate assets	**41,393**	12,444
Consolidated total assets	**6,100,855**	5,129,894

	2012 *RMB'000*	2011 *RMB'000*
Liabilities		
Reportable segment liabilities	**1,137,019**	971,377
Interest-bearing borrowings	**2,088,045**	1,943,203
Current tax liabilities	**43,578**	31,403
Deferred tax liabilities	**28,721**	21,884
Unallocated head office and corporate liabilities	**16,209**	22,710
Consolidated total liabilities	**3,313,572**	2,990,577

(c) Geographical information

The Group's business is managed on a worldwide basis, but participates in four principal economic environments, the People's Republic of China (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.

	2012 *RMB'000*	2011 *RMB'000*
Revenue		
The PRC	**1,792,322**	1,681,064
North America	**387,689**	410,634
Europe	**313,181**	367,143
Asia (other than the PRC)	**607,843**	633,610
Others	**17,216**	19,312
Total	**3,118,251**	3,111,763

5. OTHER INCOME

		2012 *RMB'000*	2011 *RMB'000*
Government grants	(i)	**50,075**	8,257
Dividend income from unlisted securities	(ii)	**800**	800
Reversal of provision for doubtful debts *(Note 9(b))*		**21,916**	—
Others		**6,153**	3,644
		78,944	12,701

(i) Jiangsu Tiangong Tools Company Limited ("TG Tools"), a wholly-owned subsidiary of the Company located in the PRC, received unconditional grants amounting to RMB48,913,000 (2011: RMB7,095,000) from the local government in Danyang to reward its contribution to local economy and encourage its innovation of technology and recognised amortisation of government grants related to assets of RMB1,162,000 (2011: RMB1,162,000) during the year ended 31 December 2012.

(ii) The Group received dividends totalling to RMB800,000 (2011: RMB800,000) from its unlisted equity investments during the year ended 31 December 2012.

6 PROFIT BEFORE TAXATION

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

(a) Net finance costs

	2012	2011
	RMB'000	*RMB'000*
Interest income	**(10,588)**	(4,087)
Finance income	**(10,588)**	(4,087)
Interest on bank loans	**144,751**	107,305
Less: interest expense capitalised into property, plant and equipment under construction*	**(26,213)**	(11,463)
Fair value recognised upon warrants issuance	**—**	42,754
Change in fair value of warrants	**—**	(5,566)
Finance expenses	**118,538**	133,030
Net finance costs	**107,950**	128,943

* The borrowing costs have been capitalised at a rate of 0.30%–9.80% per annum (2011: 0.30%–9.80%).

(b) Staff costs

	2012	2011
	RMB'000	*RMB'000*
Salaries, wages and other benefits	**158,980**	149,048
Contributions to defined contribution retirement plans	**10,631**	7,102
Equity-settled share-based payment expenses	**3,609**	6,469
	173,220	162,619

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.

(c) Other items

	2012	2011
	RMB'000	*RMB'000*
Cost of inventories*	**2,388,862**	2,405,000
Depreciation	**121,295**	113,386
Amortisation of lease prepayments	**1,583**	1,627
(Reversal)/provision for doubtful debts	**(21,916)**	11,081
Impairment loss on non-trade receivables	**1,595**	—
Auditor's remuneration	**2,350**	2,200
Provision/(reversal) for write-down of inventories	**773**	(2,941)
Operating lease charges	**1,315**	1,274

* Cost of inventories includes RMB240,526,000 (2011: RMB223,198,000) relating to staff costs, depreciation expenses and write-down of inventories which are also included in the respective total amounts disclosed separately above or in note 6(b) for each of these types of expenses.

7 INCOME TAX IN THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(a) Taxation in the consolidated statement of comprehensive income represents:

	2012	2011
	RMB'000	*RMB'000*
Current tax		
Provision for PRC income tax	**82,900**	67,558
Provision for Hong Kong profits tax	**1,886**	—
	84,786	67,558
Deferred tax		
Origination and reversal of temporary differences	**7,222**	2,247
	92,008	69,805

(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) 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 year ended 31 December 2012.

(iii) 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 were previously 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. Under the grandfathering rules introduced from 1 January 2008, enterprises that had not started to benefit from such tax holidays because they had not yet generated taxable profits, started the tax holiday from 1 January 2008. In accordance with these regulations, TG Tools and Tiangong Aihe 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 is qualified as High and New Technology Enterprise during the years from 2012 to 2014 and subject to a preferential income tax rate of 15% in 2012 (2011: 12.5%).

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

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

	2012	2011
	RMB'000	*RMB'000*
Profit before taxation	**536,900**	435,132
Notional tax on profit before taxation, calculated using the PRC statutory tax rate of 25% (2011: 25%)	**134,225**	108,783
Effect of preferential tax rates	**(51,358)**	(53,090)
Effect of different tax rates	**592**	9,948
Tax effect of non-deductible expenses	**1,235**	1,937
Withholding tax on undistributed profits of subsidiaries	**847**	3,332
Withholding tax on distributed dividends	**20,989**	—
Tax refund	**(14,522)**	(1,105)
Actual tax expense	**92,008**	69,805

8 EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB444,892,000 (2011: RMB365,327,000) and the weighted average of 1,822,304,110 ordinary shares (2011: 1,678,000,000 shares) in issue during the year, calculated as follows:

Weighted average number of ordinary shares

	2012	2011
Issued ordinary shares at 1 January	**1,678,000,000**	1,678,000,000
Effect of issuance of ordinary shares	**88,013,699**	—
Effect of exercise of warrants	**56,290,411**	—
Weighted average number of ordinary shares at 31 December	**1,822,304,110**	1,678,000,000

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB444,892,000 (2011: RMB365,327,000) and the weighted average number of ordinary shares of 1,857,187,430 shares (2011: 1,720,505,706 shares), calculated as follows:

Weighted average number of ordinary shares (diluted)

	2012	2011
Weighted average number of ordinary shares at 31 December	**1,822,304,110**	1,678,000,000
Effect of warrants	**30,010,314**	39,744,292
Effect of equity settled share-based transactions	**4,873,006**	2,761,414
Weighted average number of ordinary shares (diluted) at 31 December	**1,857,187,430**	1,720,505,706

9 TRADE AND OTHER RECEIVABLES

	2012 RMB'000	2011 RMB'000
Trade receivables	**1,152,150**	858,750
Bills receivable	**176,741**	273,752
Less: provision for doubtful debts	**(29,278)**	(51,194)
Net trade and bills receivable	**1,299,613**	1,081,308
Prepayments	**189,467**	173,768
Non-trade receivables	**43,113**	16,337
Less: impairment loss on non-trade receivables	**(1,595)**	—
Net prepayments and non-trade receivables	**230,985**	190,105
	1,530,598	1,271,413

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

(a) Ageing analysis

As of the end of the reporting period, the ageing analysis of trade debtors and bills receivable (which are included in trade and other receivables), based on the invoice date and net of provision for doubtful debts, is as follows:

	2012 RMB'000	2011 RMB'000
1 to 3 months	**967,658**	682,048
4 to 6 months	**226,152**	284,320
7 to 12 months	**99,159**	90,384
1 to 2 years	**6,438**	24,556
Over 2 years	**206**	—
	1,299,613	1,081,308

Trade debtors and bills receivable are due within 0 to 120 days from the date of billing.

(b) Impairment of trade and bills receivable

Impairment losses in respect of trade and bills receivable 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 receivable directly.

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

	2012 RMB'000	2011 RMB'000
At 1 January	**51,194**	40,113
(Reversal)/provision for doubtful debts recognised	**(21,916)**	11,081
At 31 December	**29,278**	51,194

(c) Trade and bills receivable that are not impaired

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

	2012	2011
	RMB'000	*RMB'000*
Neither past due nor impaired	**1,077,661**	809,438
Less than 3 months past due	**25,423**	19,256
More than 3 months but less than 6 months past due	**—**	54,268
More than 6 months past due	**—**	1,561
Amounts past due but not impaired	**25,423**	75,085
	1,103,084	884,523

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 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.

10 TRADE AND OTHER PAYABLES

	2012	2011
	RMB'000	*RMB'000*
Trade and bills payable	**978,009**	850,283
Non-trade payables and accrued expenses	**169,191**	136,614
	1,147,200	986,897

As of the end of the reporting period, the ageing analysis of trade creditors and bills payable (which are included in trade and other payables), based on the invoice date, is as follows:

	2012	2011
	RMB'000	*RMB'000*
1 to 3 months	**524,340**	608,724
4 to 6 months	**417,619**	197,834
7 to 12 months	**19,563**	26,316
1 to 2 years	**7,898**	10,217
Over 2 years	**8,589**	7,192
	978,009	850,283

11 DIVIDENDS

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

	2012	2011
	RMB'000	*RMB'000*
Dividend proposed after the end of the reporting period of RMB0.0461 per ordinary share (2011: RMB0.0480 per ordinary share)	**89,019**	80,544

The final dividend proposed after the end of the reporting period has not been recognised as a liability at the end of the reporting period.

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

	2012	2011
	RMB'000	*RMB'000*
Dividend in respect of the previous financial year, approved and paid during the year of RMB0.0480 per share (2011: RMB0.028125 per share)	**87,936**	47,194

In respect of the final dividend for the year ended 31 December 2011, there is a difference of RMB7,392,000 between final dividend disclosed in the 2011 annual financial statements and amounts approved and paid during the year which represents dividends attributable to shares issued upon the exercise of 29,000,000 warrants and issuance of 125,000,000 ordinary shares, before the closing date of the register of members.

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.

MARKET REVIEW

The global economy lost steam in 2012, when we saw a slowdown in China's economy, uncertainties in the United States and austerity measures in Europe, etc. The estimated global GDP growth retreated to 2.3%, while the global GDP growth achieved 2.8% in 2011.

Despite a lackluster macro environment, the Group still managed to achieve a moderate growth in its operating results and recorded over 20% growth year-on-year for profit attributable to the equity shareholders of the Group. The increase was mainly attributable to the following reasons:

(1) The Group's unparalleled market leadership in HSS industry

According to China Special Steel Enterprise Association (the "CSSEA"), the Group remained China's largest HSS manufacturer by volume in 2012. Its unique business model features vertically integrated production process and the use of recycled materials, leading to greater efficiency and lower production costs. Moreover, the production processes of HSS and die steel are complementary to each other; hence their production lines can be operated more efficiently with increased productivity. The Group's annual production capacity in HSS is approximately 50,000 tons.

(2) Significant cost advantages over foreign competitors

Foreign competitors suffered from competitive disadvantages due to substantially higher material costs resulting from China's hefty levies on "direct" exports of rare metals as well as higher labour costs. 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, it has imposed strict quotas as well as hefty levies on "direct" exports of rare metals. Foreign competitors have thus suffered from higher raw material costs and unstable supply.

(3) Peripheral domestic players were squeezed out in the tight credit environment

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

(4) Benefited from banks' support for more efficient private enterprises with strong cash flows

Notwithstanding the overall tight credit conditions, the Group, as one of the largest enterprises in Danyang Municipality, has not encountered any problem in renewing its standby credit facility with the local banks because of its leading market position in China and strong cash inflow. As at 31 December 2012, the Group's available standby credit line reached RMB5.6 billion, of which only approximately RMB2.6 billion was utilized.

BUSINESS REVIEW

Despite the adverse macro backdrop, the Group achieved moderate growth in its operating results for the year under review, which clearly reflects the Group's unparalleled leadership in the industry as well as the competitiveness and high quality of its products. During the period, the Group remained the largest manufacturer of HSS as well as a leading manufacturer of HSS cutting tools and die steel in China.

The Group's core products were widely recognized by its strategic partners spread across different sectors both in China and overseas. Moreover, we acquired a company that produces cutting tools in the auto sector in early 2013, which marked a milestone for the Group's successful penetration into China's auto sector and should give a strong boost to the Group's production of cutting tools and HSS products. As to the die steel segment, some of the die-steel products have been sold to auto manufacturers in Europe through distributors, which again showcases our international competitiveness. On the HSS segment, the Group recently developed a new key account in Russia in 2013 with expected annual HSS demand of 1,000 tons.

During the period under review, the Group continued to improve efficiency by expanding production lines and enhancing automation. Expansion of its taps production line was completed and commenced production. Its total investment amounted to RMB42 million. With an annual capacity of 12 million pieces, it is now one of the largest taps production lines in China.

The Group adhered to a low-carbon, green and sustainable development strategy. In 2012, it built an environmental-friendly natural gas heating system and to dismantle all chimneys. In addition, it spent over RMB6.5 million on a large-scale sewage project. The Group has made continuous efforts in environmental protection.

In 2012, all product segments achieved healthy and stable performance. For HSS and die steel, we saw increases by sales volume of approximately 12% and 19%, respectively, which showcased the Group's strong influence in the markets. Nevertheless, the increase in sales volume was offset by the decrease of average selling price impacted by decline of raw materials prices as well as a change in product mix to lower value products. For HSS cutting tools, there was an increase in domestic demand but was offset by the decrease in export sales.

	For the year ended 31 December					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS	**1,092,587**	**35.0**	1,158,264	37.2	(65,677)	(5.7)
HSS cutting tools	**567,297**	**18.2**	609,675	19.6	(42,378)	(7.0)
Die steel	**1,038,826**	**33.3**	985,733	31.7	53,093	5.4
Titanium alloy	**33,465**	**1.1**	—	—	33,465	N/A
Trading of goods	**386,076**	**12.4**	358,091	11.5	27,985	7.8
	3,118,251	**100.0**	3,111,763	100.0	6,488	0.2

HSS — accounted for 35% of the Group's revenue in FY2012

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

HSS operation was the greatest revenue contributor for the Group during the year under review. Revenue from HSS decreased by 5.7% to RMB1,092,587,000 (2011: RMB1,158,264,000). Despite a slowdown in China's industrial output, HSS sales to domestic market remained resilient, reflecting the Group's leadership in home market and sound operation model. The increase in sales quantity of HSS was partly offset by a decrease in overall average selling price.

	For the year ended 31 December					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS						
Domestic	**877,638**	**80.3**	944,118	81.5	(66,480)	(7.0)
Export	**214,949**	**19.7**	214,146	18.5	803	0.4
	1,092,587	**100.0**	1,158,264	100.0	(65,677)	(5.7)

HSS Cutting Tools — accounted for 18% of the Group's revenue in FY 2012

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

In 2012, revenue generated from HSS cutting tools declined by approximately 7% to RMB567,297,000 (2011: RMB609,675,000). With a limited life span, HSS cutting tools are effectively "consumables" in industrial production and hence their demand is relatively inelastic even during market downturns. Export sales, which accounted for 60% of the segment revenue, decreased by 16%. On the domestic market, the Group retained the growth momentum and achieved a sales growth of 11%.

	For the year ended 31 December					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
HSS Cutting Tools						
Domestic	**228,459**	**40.3**	205,842	33.8	22,617	11.0
Export	**338,838**	**59.7**	403,833	66.2	(64,995)	(16.1)
	567,297	**100.0**	609,675	100.0	(42,378)	(7.0)

Die Steel — accounted for 33% of the Group's revenue in FY 2012

Die steel is mainly used in die and mould casting as well as machining processing. Many different manufacturing industries require moulds including automotive industry, high-speed railway construction, aviation and plastic product manufacturing. Similar to HSS, its production involves the addition of various rare metals such as molybdenum, vanadium and chromium.

Revenue generated from die steel rose by 5.4% to RMB1,038,826,000 (2011: RMB985,733,000). 56% of the segment revenue was derived from domestic market while export sales accounted for the remaining 44%.

	For the year ended 31 December					
	2012		2011		Change	
	RMB'000	*%*	*RMB'000*	*%*	*RMB'000*	*%*
Die Steel						
Domestic	**582,543**	**56.1**	531,103	53.9	51,440	9.7
Export	**456,283**	**43.9**	454,630	46.1	1,653	0.4
	1,038,826	**100.0**	985,733	100.0	53,093	5.4

Titanium Alloy

Titanium alloy is lighter, stronger and has a higher corrosion resistance compared to aluminum alloy. Thus, it finds applications in aviation, marine engineering and the medical industries. Its production involves sponge titanium as well as various other rare metals.

With an initial annual 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 RMB33 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. Nevertheless, satisfactory results have been achieved from this segment. 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 alloy will soon become another pillar revenue source for the Group in the future.

The production of titanium and titanium alloy is both capital and technology intensive. Thus, it is an industry with high entry barrier. Currently, only a limited number of companies in China are engaged in titanium alloy production.

FINANCIAL REVIEW

Net profit attributable to equity shareholders of the Company increased significantly by approximately 21.8% from RMB365,327,000 in 2011 to RMB444,892,000 in 2012. The increase was mainly attributable to the Group's increase of gross margin, receipts of more government grants and due to the one-off fair value change of warrants amounting to RMB37,188,000 incurred in the prior period.

Revenue

Revenue for the Group for 2012 totaled RMB3,118,251,000, representing a slight increase as compared with RMB3,111,763,000 in the previous year.

Cost of sales

The Group's cost of sales was RMB2,388,862,000 in 2012, representing a slight decrease as compared with RMB2,405,000,000 in 2011. As a percentage of total revenue, the Group's cost of sales decreased slightly to 76.6% during the period (2011: 77.3%).

Gross margin

For 2012, the overall gross margin was approximately 23.4% (2011: 22.7%). Set out below is the gross margin of our five products segments in 2012 and 2011:

	2012	2011
HSS	**27.3%**	23.1%
HSS cutting tools	**16.4%**	16.0%
Die steel	**31.2%**	34.1%
Titanium alloy	**22.0%**	N/A
Trading of goods	**1.0%**	1.6%

HSS

Gross margin of HSS increased from 23.1% in 2011 to 27.3% in 2012. The increase was due to the benefit from the operating leverage as a result from the increase in production volume and was due to the decrease in raw material costs such as rare metals in the second half of the year.

HSS cutting tools

In 2012, the gross margin of HSS cutting tools remained stable at 16.4% (2011: 16.0%).

Die steel

The gross margin of die steel decreased from 34.1% in 2011 to 31.2% in 2012. The decrease was due to the change in product mix as compared with last year.

Titanium alloy

The Company started the production and selling of titanium alloys during the year. The major products produced were titanium ingot and titanium rods.

Trading of goods

This segment involves the purchase and sales of aluminum and chemicals which mainly comprises purified terephthalic acid. Purified terephthalic acid is mainly used for the production of household building materials such as blinds and covers. In 2012, trading of goods accounted for approximately 12% (2011: 11%) of the Group's revenue.

Other income

Other income totaled RMB78,944,000 in 2012, representing an increase of RMB66,243,000 from RMB12,701,000 in 2011. The increase was mainly attributable to the increase in government grants of RMB41,818,000 and a reversal of provision for doubtful debts of RMB21,916,000.

Distribution expenses

Distribution expenses in 2012 were RMB44,583,000 (2011: RMB36,890,000), representing an increase of approximately 21%. The increase was mainly attributable to the increase in transportation expenses as a result of the increase in shipping charges. For 2012, the distribution expenses as a percentage of revenue was 1.4% (2011: 1.2%).

Administrative expenses

Administrative expenses increased from RMB85,924,000 in 2011 to RMB100,437,000 this year. The increase was mainly due to the increase in personnel costs and other operating expenses due to implementation of various initiatives by the Group. For 2012, administrative expenses as a percentage of revenue was 3.2% (2011: 2.8%).

Net finance costs

The Group's finance income was RMB10,588,000 for 2012, representing an increase of RMB6,501,000 primarily due to the increase in average bank deposits in 2012. The Group's finance expense was RMB118,538,000 in 2012, representing a decrease of 10.9% from RMB133,030,000 in 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 in 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 over 32% from RMB69,805,000 in 2011 to RMB92,008,000 in 2012. The increase was mainly due to the increase in profits tax as operating profit increased and increase in tax rate of TG Tools from 12.5% in 2011 to 15% in 2012.

Profit for the year

As a result of the factors discussed above, the Group's profit significantly increased by approximately 21.8% from RMB365,327,000 in 2011 to RMB444,892,000 in 2012. The net profit margin increased from 11.7% in 2011 to 14.3%.

Total comprehensive income attributable to equity shareholders of the Company

For 2012, total comprehensive income attributable to equity shareholders of the Company was RMB445,569,000 (2011: RMB361,612,000) after taking into account foreign currency translation differences.

Trade receivables

The trade and bills receivable increased from RMB1,081,308,000 in 2011 to RMB1,299,613,000 in 2012 which was mainly due to the increase in sales in the fourth quarter in 2012 as compared with the fourth quarter sales in 2011. Approximately 81% of the trade and bills receivable were neither past due nor impaired. During the year, the Group also made more effort on collecting long outstanding receivables and reduced the provision for doubtful debts balance by RMB21,916,000 in 2012.

OUTLOOK

Our healthy and stable financial performance in 2012 amid an adverse macro backdrop is a testimony to our unrivalled leadership in the HSS industry and effective internal cost control derived from our unique vertically-integrated business model.

The Group remains optimistic towards 2013 and will push ahead with its business expansion and focus on penetrating into different industries and exploring new markets. It aims to further expand its footprint on other countries such as Russia, Italy, South Africa and Brazil by setting up sales representative offices. In those countries, we see accelerating urbanization and industrial development, which will subsequently fuel the demand of HSS, HSS cutting tools and die steel. The Group believes that advancing into these markets will broaden our revenue base and generate promising return.

Apart from the traditional core segments, 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, it is a better alternative in industrial and aerospace applications because of its strength, durability and overall performance. Through research and development as well as technology enhancement, we will continue to develop the new material industry in a prudent manner with a focus on titanium alloy pipes.

FORWARD LOOKING STATEMENTS

This management discussion and analysis contains certain forward looking statements with respect to the financial condition, results of operations and business of the Group. These forward looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements.

Forward looking statements involve inherent risks and uncertainties. Readers should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward looking statement.

LIQUIDITY AND FINANCIAL RESOURCES

As at 31 December 2012, the Group's current assets mainly included cash and cash equivalents of approximately RMB150,499,000, inventories of approximately RMB1,426,003,000, trade and other receivables of RMB1,530,598,000, pledged deposits of RMB238,479,000 and time deposits of RMB446,000,000. As at 31 December 2012, the interest-bearing borrowings of the Group were RMB2,088,045,000, RMB1,886,407,000 of which were repayable within one year and RMB201,638,000 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 equity) was 75%, significantly lower than the 91% as at 31 December 2011.

The increase in borrowing was mainly attributable to the increase in investment in production equipment. As at 31 December 2012, borrowings of RMB1,317,000,000 were in RMB, USD107,770,000 were in USD, and EUR11,260,000 were in EUR. The borrowings of the Group were subject to interest payable at rates ranging from 0.30% to 7.22%. The Group did not enter into any interest rate swaps to hedge itself against the risks associated with interest rates.

During the year, the net cash generated from operating activities was RMB373,257,000 (2011: RMB652,157,000).

CAPITAL EXPENDITURE AND CAPITAL COMMITMENTS

For 2012, the Group's net increase in fixed assets amounted to RMB350,447,000, which were mainly for the production plant and facilities for HSS and were financed by a combination of our internal cash resources and operating cash flows and bank borrowing. As at 31 December 2012, capital commitments were RMB537,922,000, of which RMB135,828,000 were contracted and RMB402,094,000 were authorised but not contracted for. The majority of the capital commitments were related to investment to completion production equipment installation and will also be financed by a combination of our internal cash resources and operating cash flows and bank borrowing.

FOREIGN EXCHANGE EXPOSURE

The Group's revenues were denominated in RMB, US dollars and Euros, with RMB accounting for the largest portion (approximately 57.5%). Approximately 42.5% 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 the light of foreign exchange fluctuations 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 2012, the Group pledged certain bank deposits amounting to approximately RMB238,479,000 (2011: RMB149,894,000) and certain trade receivables amounting to approximately RMB143,618,000 (2011: Nil).

EMPLOYEES' REMUNERATION AND TRAINING

As at 31 December 2012, the Group employed around 3,928 employees (31 December 2011: around 3,910 employees). Total staff costs during the year amounted to RMB173,220,000 (2011: RMB162,619,000). 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

As at the end of the reporting period, TG Tools has issued a guarantee to a bank in respect of a bank facility granted to TGT Special Steel Company Limited ("TGT"), a jointly controlled entity of the Group, which expires on 27 July 2013. As at the end of the reporting period, the directors do not consider it probable that a claim will be made against the Group under the guarantee. The maximum liability of the Group at the end of the reporting period under the guarantee issued is the outstanding amount of the facility drawn down by TGT of RMB15,049,000 (2011: RMB24,258,000). Included in bank deposits RMB11,500,000 (2011: RMB30,300,000) was pledged for the bank facility granted to TGT.

FINAL DIVIDEND AND CLOSURE OF REGISTER OF MEMBERS

The Register of Members of the Company will be closed from 24 May 2013 to 29 May 2013 (both days inclusive), for the purpose of determining shareholders' entitlement to attend and vote at the forthcoming annual general meeting of the Company (the "Annual General Meeting") on 29 May 2013, during which period no transfer of shares of the Company will be registered. In order to qualify for attending and voting at the Annual General Meeting, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712-1716, 17th Floor, Hopewell Centre, No.183 Queen's Road East, Wan Chai, Hong Kong, for registration by no later than 4:30 p.m. on 23 May 2013.

The Board has resolved to recommend the payment of a final dividend of RMB0.0461 per share for the year ended 31 December 2012 (2011: RMB0.0480) to shareholders of the Company whose names appear on the Register of Members of the Company on 7 June 2013. The Register of Members will be closed from 5 June 2013 to 7 June 2013, both days inclusive, and the proposed final dividend is expected to be paid on or before 30 July 2013. The payment of dividends shall be subject to the approval of the shareholders of the Company at the Annual General Meeting expected to be held on 29 May 2013. In order to qualify for the proposed dividend, shareholders of the Company should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, for registration by no later than 4:30 p.m. on 4 June 2013.

SHARE OPTIONS SCHEME

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 were 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 year ended 31 December 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 for the titanium production facilities and general working capital.

During the year ended 31 December 2012, all of the 128,000,000 warrants were exercised at an aggregated price paid of HKD128,000,000.

Save for disclosed above, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's shares during the year.

CORPORATE GOVERNANCE

During the year ended 31 December 2012, the Company has, so far where applicable, adopted and complied with the principles and code provisions set out in the Code on Corporate Governance Practices (effective until 31 March 2012) and the Code (effective from 1 April 2012) contained in Appendix 14 of the Listing Rules with no material non-compliance.

AUDIT COMMITTEE

The Audit Committee comprises three Independent Non-executive Directors. The Audit Committee held a meeting on 25 March 2013 to consider and review the 2012 annual report and annual financial statements of the Group and to give their opinion and recommendation to the Board. The Audit Committee considered that the 2012 annual report and annual 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 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"). All of the Directors have confirmed, following specific enquiry by the Company, that they have 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 year ended 31 December 2012.

The Group has also adopted a code of conduct governing securities transactions by employees who may possess or have access to price sensitive information or inside information (with effect from 1 January 2013).

PUBLICATION OF ANNUAL REPORT ON THE STOCK EXCHANGE WEBSITE

The Company's 2012 annual report will be submitted to the Stock Exchange for uploading onto the Stock Exchange's website (www.hkex.com.hk) as well as the Company's website (www.tggj.cn) in due course.

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, 26 March 2013

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*