IV. Business Review and Analysis

In the first half of the year, the domestic demand of steel products increased following the growth in the domestic economy. This resulted in the substantial increase in the domestic output of steel and iron products. In addition, the amount of steel products imported also increased when compared to the same period in the previous year. The domestic demand and supply of steel products was roughly in balance, and the prices basically remained stable. On the other hand, the international steel product market continued to remain weak, resulting in the downward adjustment of price level. For the raw materials and energy resources, their supply was smaller than the previous year, pushing their prices to rise considerably. The prices for imported ore, electricity supply and coal rose by approximately 4%, 5% and 3% respectively. In respect of other costs of the Company, in the past year, a considerable number of projects were transferred to fixed assets, resulting in the increase of approximately RMB50,000,000 in the current period's depreciation as compared to the same period in the previous year. Furthermore, staff cost was duly increased. In the above circumstance, the Group (the Company and its subsidiaries) worked out its strategy of "Accelerating Development and Improving Effectiveness". Taking into account the market changes and the equipment production capacity, the Group focused on enhancing its production capacity and, at the same time, taking full advantage of economies of scale. The increase in the Company's profit for the first half of the year was mainly attributable to the increase in sales amount and sales quantity as compared to the same period in the previous year. The production costs had decreased even raw materials cost increased. Nevertheless, the profit increase percentage was narrowed since provisions for impairment of construction in progress and fixed assets were made. In the latter half of the year, the Group will further improve its management and enhance financial operations in accordance with its pre-set policy.

In the first half of the year, the Group registered an increase in sales revenues and cash collection period. As a result, cash inflow recorded an increase. In addition, no growth was noted in funds allocated for inventories, thus accelerating the funds turnover rate. The Company had improved liquidity position. Short-term and long-term bank borrowings dropped by RMB243,000,000 and RMB95,000,000 respectively as compared to the end of the previous year. Trade receivables and long term investments had no significant fluctuations.

The Group's capital mainly comprised shareholders' funds and bank borrowings, the majority of which was in Renminbi with a small amount in U.S. dollar. The fixed interest rate required by the State applied to all the borrowings. The Group adopted a conservative financial policy to manage financial and operational risks. In the first half of the year, the financial indices of the Group were improved, and a reasonable current ratio and quick ratio were achieved.

In terms of market expansion, in the first half of the year, the Company focused on the promotion and development of H-shaped steel products. A total of 240,000 tons of H-shaped steel was sold, of which some were exported to overseas markets and some were sold in the domestic market. A majority of the steel sold in the domestic market was used on key projects of the State like bridges, highways, construction projects and power plants. In the first half of the year, the Group also developed a total of 270,000 tons of new products.

They were high-tech products which improved the market competitiveness of the Company's products.

The Group attached importance to the improving of technologies and upgrading of equipment. The Group aimed to realize production structure and product mix adjustment through the said two channels. In the first half of 2001, the Group's no. 1 steel-making plant electric arc furnace was completed and came into operations, marking an end to the previous steel-making method of MASC.L. The No. 4 high gas boiler of the heat and electricity supply plant and the new ball-shaped iron-ore production lines started commercial production in 18 July 2001 and 28 July 2001 respectively. All these were expected to further improve the integrated benefits of production and operations.

Year 2001 to 2005 is the period marked for the tenth "Five Year Plan" of the State, as well as a crucial period for the development of MASC.L. In 2001, the Group started to implement its own tenth five-year structural adjustment plan in the principal steel and iron business of MASC.L. The development strategies of MASC.L. in the period are: to focus on market demands, phase out outdated technologies, adjust product mix, and develop the production scale to a due extent; to increase high-tech elements, produce short-supplied products with extra values added, and improve the quality and grades of all products in an effort to achieve better cost-effectiveness. Major projects focus on the establishment of a production line for casting and rolling thin billet plates and another production line for rolling thin plates. To accompany the operations of the two new production lines, the output of iron and steel will also be improved. With the implementation of the tenth five-year plan, the product mix of MASC.L. will be improved, and the products' technological level and extra values will be enhanced. The four major product lines of thin plate, H-shaped steel, train wheel and wire rod will be produced in product series and as complements to major projects. The series cover major construction materials and construction complements, with the plate covering ratio expected to reach 41%. At that time, the risk-bearing ability and market competitiveness of MASC.L. products will be improved substantially. The tenth five-year plan is mainly funded by bank borrowings and the Company's own capital. The plan was included into the Directors' work report, and examined and approved by the Annual General Meeting convened on 26 June 2001.

As at the end of June 2001, the employee number of the Group was 45,566. Staff salary was mainly determined under the principle of "Income in proportion to Results". The Company set up a benchmark system, conducted assessments accordingly and determined salaries in accordance with the assessment results. The annual salary system continued to apply to the management of the Company. The income of middle management was pegged to their responsibilities and the said benchmark, and was worked out at the end of the year. The option scheme of the Group was still under development and not yet implemented.

As at 30 June 2001, under PRC accounting standards, the total assets of the Group amounted to RMB17,196,730,000 and net assets (shareholders' equity) to 11,895,090,000. The Group's gearing ratio was 30.83% (total liability/total asset). None of the Group's assets were mortgaged or pledged. The Group had no material contingency liability.