MANAGEMENT DISCUSSION AND ANALYSIS

Operating Results

In the first half of 2001, the Group continued to grip the market opportunity so as to increase sales, to reduce costs, and to achieve better operating results. For the six months ended 30th June 2001, the Group's turnover was Rmb1,881,704,000; profit attributable to shareholders was Rmb123,685,000; and earnings per share were Rmb0.116.

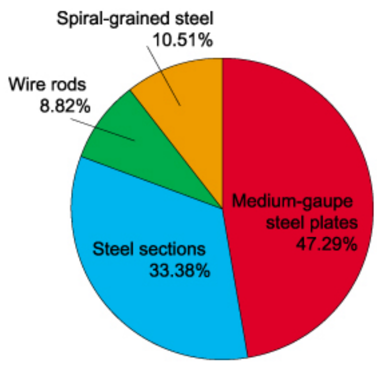
1. Significant Increase in Sales

The domestic steel product market recorded a recovery since April 2000 and until June 2001 when a downturn was registered. In general, the market condition in the first half of the current year remained stable and no significant fluctuation was noted as compared to the second half of the previous year. The Group has capitalised on its well established sales network and its reputation on quality. The Group made a breakthrough in its results by boosting its sales volume and maintaining its prices.

In the first half of 2001, the average selling price of the Group's steel products was Rmb2,277 per ton, representing an increase of 10.59% over the same period of last year thereby increasing the profit contribution by approximately Rmb160,000,000. The average selling prices of medium-gauge steel plate, steel sections, wire rods and spiral-grained steel were Rmb2,402 per ton, Rmb2,209 per ton, Rmb1,990 per ton and Rmb2,168 per ton respectively, representing an increase of 15.04%, 4.92%, 4.57% and 8.08% respectively over the same period of previous year.

In the first half of 2001, the Group delivered 788,200 tons of steel products, representing 100% achievements on both production-to-sale ratio and accounts receivable collection rate. The sales volume amounted to 755,800 tons (comprising 357,400 tons of medium-gauge steel plates, 252,300 tons of steel sections, 66,700 tons of wire rods and 79,400 tons of spiral-grained steel), representing an increase of 104,000 tons over the same period of last year. Since steel billets produced by the Group were all used for its rolled steel production, the volume of continuously cast billets exports decreased by 132,700 tons as compared with the same period of last year.

Sales Analysis of Principal Products for the First Half of 2001



2. Costs under Control

The Group asserts its belief of applying technology to production process and maintaining its competitiveness on cost control, and positions the current year as the "Year of Cost Management". The Group has commenced a broad range of activities in the "Year of Cost Management" which primarily focus on technological improvements and the strengthening of management. Preliminary achievement on cost reduction was noted.

Although the Group's production in the first half of 2001 was hindered by the limitation of supply of coking coal and billets and the fact that certain equipment are operating beyond their expected operating lives, the outputs of coking coal, pig iron, steel and steel products have all achieved historically high records, representing respective increase of 6.30%, 10.98%, 14.02% and 24.03% over the same period of last year. Fixed costs were reduced by approximately Rmb30,000,000. 14 technological and economic performance indices achieved historically high records. The aggregate energy consumption rate per ton was 885 kg of standard coal and, iron and steel wastage per ton was 1,079 kg, representing a decrease of 5.14% and 0.74% from the same period of last year. As a result of the improvements in the technological and economic performance indices, production costs were reduced by approximately Rmb20,000,000.

Due to the large number of equipment repairs works undertaken and the special repair for certain equipment during the first half of 2001, repair expenses increased by approximately Rmb23,353,000 as compared with the same period of last year. Salary expenses were increased by approximately Rmb32,671,000 as compared with the same Period of last year as a result of a general salary increment approved during the period. Provision for slow-moving inventories was increased by Rmb29,800,000 as a result of change in age profile.

3. Increase and Decrease in Other Expenses

In the first half of 2001, due to the increase in wage surcharges and bad debt provisions, administrative expenses of the Group amounted to approximately Rmb82,956,000, representing an increase of approximately Rmb21,271,000 as compared with the same period of last year. A provision of approximately Rmb26,400,000 for impairment losses was made in respect of certain fixed assets that have been left idle. Accordingly, other operating expenses were increased by approximately Rmb22,072,000 as compared with the same period of last year.

The selling costs in the first half of 2001 amounted to approximately Rmb38,706,000, representing a decrease of approximately Rmb18,052,000 as compared with the same period of last year. The decrease was mainly attributable to the export expenses of approximately Rmb21,000,000 incurred in the first half of the previous year in relation to the export of 154,000 tons of steel billets while steel billets were all sold in the domestic market during the first half of the year.

Financial Status

In the first half of 2001, the Group maintained healthy cash flows and sound financial position such as a higher accounts receivable collection rate, sufficient raw materials and abundant cash balances.

1. As at 30th June 2001, the total assets of the Group amounted to approximately Rmb4,202,667,000; total liabilities amounted to approximately Rmb2,066,955,000; The Group's gearing ratio (Total liabilities (excluding minority interests) /Total assets x 100%) was 49.18%, representing a decrease of 1.2% from the beginning of the year. Due to the increase in current liabilities, liquidity ratio (Current assets /Current liabilities x 100%) dropped to 97.80%, representing a decrease of 10.06% from the beginning of the year.

2. As at 30th June 2001, bank balances and cash of the Group amounted to approximately Rmb296,532,000, representing a decrease of approximately Rmb35,757,000 from the beginning of the year. The decrease was mainly attributable to the large investments on technological improvement projects and the distribution of dividends. All deposits were placed with state-owned commercial banks. The Group had no designated deposit.

3. As at 30th June 2001, the Group's bank loans amounted to Rmb981,200,000, representing a net decrease of Rmb6,000,000 from the beginning of the year. Among the bank loans, amounts repayable within one year amounted to Rmb661,200,000, and Rmb517,000,000 of which are repayable in the second half of the current year. Interest is charged at rates ranging from 3.24% to 6.534% (2000:3.24% to 6.435%) per annum.

4. In the first half of the year, the Group's capital expenditure on projects such as spherical furnace, desulfurization and dehydrogenation of coking coal, blast furnace coal blower and Jingxing Dolomite Mine amounted to approximately Rmb179,500,000. At the end of June 2001, the spherical furnace has commenced operation. The aggregate expenditure for construction in progress amounted to approximately Rmb196,300,000.

Charges on Assets and Contingent Liabilities

The Group pledges its assets to secure its bank loans. As at 30th June 2001, the total carrying value of assets pledged was Rmb319,600,000 (31st December 2000: Rmb203,232,000).

As at 30th June 2001, the Group had no contingent liabilities (31st December 2000: nil).