V. MANAGEMENT DISCUSSION AND ANALYSIS

(1) Business review:

In accordance with IFRS, the Company recorded a profit attributable to shareholders of Rmb620,352,000 for the six months ended 30 June 2003, representing an increase of 218.73% over the same period last year. Basic earnings per share was Rmb0.210. In accordance with the PRC Accounting Rules and Regulations, the Company recorded a net profit of Rmb620,390,000 for the six months ended 30 June 2003, representing an increase of 224.95% over the same period last year. Earnings per share was Rmb0.209.

The first half of the year has seen positive developments in the PRC economy and an increase in demand for steel products. The prices of the Group's steel products generally increased by 28.77% compared with the prices in 2002, representing an increase of 39.50% compared with the same period last year.

In light of the above, the Company adopted a number of effective measures to increase its economic return:

1. Resources were utilized in a reasonable manner and the production structure was further improved. Through strengthening the centralised and unified management system, the production operations of the Company were further enhanced and the Company strove to maintain its production at a high standard. During the first half of the year, the Company produced 2,103,800 tonnes of steel products of which cold rolled sheets accounted for 827,300 tonnes; wire rods accounted for 253,300 tonnes; thick plates accounted for 547,000 tonnes; and large steel products accounted for 476,200 tonnes. The Steel Smelting Plant of the Company produced 1,324,800 tonnes of steel during the first half of the year.

2. Actively sought direct suppliers to jointly explore the market for the Company's products based on the principle of obtaining mutual benefits and achieving a win-win situation. During the first half of the year, the number of orders placed by direct suppliers increased by 8% over the same period last year. A comprehensive database relating to direct suppliers and key customers was set up so as to strengthen services provided to the direct suppliers.

   In the first half of the year, the Company sold 2,130,500 tonnes of steel products, representing a production to sales ratio of 101.27%.

3. Increased the focus on the research and development of products. The number of orders for specialized, distinctive and high quality products increased. Products were introduced to the market with a focus on their special features to explore their market position. With the continuous improvement on the quality and image of the cold-rolled sheet products of the Company in the market, the number of orders for the Company's specialized, distinctive and high quality products increased significantly by nearly 11% compared with the same period last year.

4. The strategy for producing exquisite products was implemented, the research and development of new products was strengthened and efficiency was improved with technological developments. The Company has set up 40 scientific and technological study projects this year, of which 25 have already commenced trial industrial production. In the first half of the year, the Company was able to produce high quality plate 05 which was used in manufacturing automobiles and domestic electrical appliances.

5. Active implementation of Enterprise Resource Planning (ERP). The implementation of ERP helped to improve the Company's management standard and production structure and increased corporate benefits. In the first half of the year, ERP was implemented in the sale, quality control, production and delivery of cold-rolled sheets and satisfactory results were achieved.

6. Improvement in the development process for projects under construction and sought to reach the output targets in respect of completed projects. Construction for the colour coating steel sheet project, the cold rolled sheet project and the large section plant project were completed. The Company will strive to carry out trial production relating to the above projects so as to achieve the output targets and benefits as soon as possible.

(2) During the reporting period, the profitability of the Group's principal activities was enhanced. The gross profit margin, based on financial statements prepared under IFRS, increased to 17.44% from 9.67%, representing an increase of 7.77% over the same period. The increase was mainly due to the rise in the prices of products and adjustment of product mix. There were no substantial changes in the profit constituents, principal activities and their structure from those of the previous reporting period.

(3) Steel products that accounted for 10% of the principal operating revenue or profit from principal activities of the Group were as follows (under IFRS):

Products	Income from principal activities *(Rmb'000)*	Cost of principal activities *(Rmb'000)*	Gross profit margin (%)	Percentage change of income from principal activities compared with previous year Increase (+) /decrease (-) (%)	Percentage change of cost of principal activities compared with previous year Increase (+) /decrease (-) (%)	Gross profit margin Increase (+) /decrease (-) (%)
Cold rolled sheets	3,076,398	2,633,511	14.40	77.51	58.77	235.66
Thick plates	1,757,685	1,295,438	26.30	56.43	22.58	342.02
Wire rods	568,443	500,062	12.03	-28.19	-35.02	332.73
Large steel products	1,339,572	1,096,858	18.12	10.83	22.08	-29.38
Including: connected transactions	721,702	662,553	8.20	11.97	16.27	-29.25

Pricing policy for connected transactions

Not less than the average of the selling prices between the Company and the independent third parties during the previous month.

Description on the necessity and continuity of connected transactions

Steel production requires a larger degree of continuity. The Company relies on Angang Holding and its subsidiaries for the supply of most of its raw materials and sells part of its products to Angang Holding and its subsidiaries. Therefore, such connected transactions will continue in the future production and operation of the Company.

Notes:

1. *Increase in income from cold rolled sheets (as principal operation) over the same period last year was mainly due to an increase in sales volume of cold rolled sheet, expansion in the proportion of high value-added products and a rise in the price of products. In the first half of 2003, sales volume of cold rolled sheets increased by 18.57% over the same period last year while the unit price of products increased by 52.25% over the same period last year;*

2. *Increase in income from thick plates (as principal operation) over the same period last year was mainly due to an increase in sales volume of thick plates, expansion in the proportion of high value-added products and a rise in the price of products. In the first half of 2003, sales volume of thick plates increased by 3.29% over the same period last year while the unit price of products increased by 52.06% over the same period last year;*

3. *Decrease in income from wire rods (as principal operation) over the same period last year was due to a decrease in the sales volume of the products as a result of the inspection and repair, and the restructuring of sales of different types of products;*

4. *Increase in costs of cold rolled sheets, thick plates and large steel products (as principal operation) over the same period last year was due to an increase in sales volume and a rise in the procurement costs of raw materials;*

5. *Increase in gross profit margins of cold rolled sheets, thick plates and wire rods over the same period last year was due to the increase in revenue from principal operations which was higher than the increase in costs of principal operations.*

(4) Investment of the Company

The Company issued 890,000,000 H Shares and 300,000,000 A Shares in July 1997 and November 1997, respectively, raising a total of approximately Rmb2,633,000,000. In March 2000, the Company issued convertible debentures of Rmb1,500,000,000, raising a total of Rmb1,480,000,000, in the PRC.

1. It was proposed that the proceeds shall be used in seven projects. The following five projects were completed and their operations have commenced:

   (1) Establishment of a steel smelting plant with a total investment of Rmb1,540,992,000;

   (2) Renovation of the combined pickling and continuous rolling line with a total investment of Rmb645,434,000;

   (3) Renovation of the cold rolling plant 1700 cross cutting lines with a total investment of Rmb60,000,000;

   (4) Expansion and renovation of cold rolling line with a total investment of Rmb1,409,600,000;

   (5) Cold rolling plant's renovation of No. 2 and 3 cross cutting lines with a total investment of Rmb32,960,000.

   The above five projects generated benefits amounting to Rmb150,000,000 during the reporting period.

2. The following two projects were under construction:

Unit: Rmb'000

Method of fund raising	Projects undertaken	Planned progress of projects	Total investment of project *(Rmb'000)*	Estimated yield rate or actual benefits	Actual investment amount *(Rmb'000)*	Actual progress of project
Issue of H shares and A shares	Construction by the jointly controlled entity of galvanised steel production line	Completion in the first half of 2000	Total investment of project: 1,494,000 Total investment of the Company: 250,000	15.51% (estimate)	248,305	Testing and adjustment commenced in mid-July 2003, trial production is expected to commence in late September 2003
Issue of convertible debentures	Distribution centre for the Cold Rolling Sheet Plant	Completion in July 2001	180,000	15.66% (estimate)	—	Preliminary work in progress.

3. Status of unused proceeds

Since 8 May 1997, the Company has raised proceeds of Rmb4,113,400,000, of which Rmb3,937,291,000 has been applied to relevant projects and the balance was deposited with banks.

4. Progress on uncompleted projects financed by proceeds

The joint venture between the Company and Thyssen Stahl AG for the construction and operation of the proposed galvanised steel production line was not established on schedule due to the following major factors: Thyssen Stahl AG was undergoing reorganisation with Krupp when the Company was negotiating with Thyssen Stahl AG; the difficulty and the time required for negotiations were beyond the Company's initial expectations and the time required for submission for approval took longer than expected. Testing and adjustment of the project commenced in mid-July 2003 and trial production is expected to commence in late September 2003. The new distribution centre for the Cold Rolling Plant was not completed on schedule as the implementation plan for the project is subject to further analysis.

5. Investment and progress of non-publicly raised funds

(1) For the setting up of the Company's galvanized steel sheet production line and colour coating steel sheet production line, the planned investment was Rmb2,640,000,000. As at 30 June 2003, Rmb1,026,433,000 had been invested. The colour coating steel sheet production line was completed in the first half of 2003. The galvanized steel sheet production line is expected to be completed by the end of the second half of 2003.

(2) For the alteration project for the Large Section Plant, the planned investment was Rmb789,000,000. The project was completed and came into operation. The actual total investment was Rmb746,082,000.

(3) For the renovation of the flattening machine of the Thick Plate Plant and alteration of the main power supply unit of the plant, the planned investment was Rmb370,000,000. The actual total investment was Rmb322,045,000 has been invested.

(5) Warning in respect of Substantial Movement in Net Profit

The Company anticipated a substantial increase of more than 50% in the Group's net profit (under the PRC accounting rules and regulations and IFRS) during the period between 1 January 2003 and 30 September 2003 as compared with the same period last year. The increase was mainly due to the adjustment of sales product mix, expansion in the proportion of high value-added products and a rise in the price of products over the same period last year.

(6) Analysis of the Group's financial position

Prepared under IFRS (unaudited)

1. Items of income statements and cash flow statements

Unit: Rmb'000

Items	**For the six months ended 30 June** **2003**	2002	Increase/ Decrease(%)
Turnover	**6,947,111**	5,012,114	38.61
Cost of principal operation	**5,735,614**	4,527,618	26.68
Profit from principal operations	**1,211,497**	484,496	150.05
Profit attributable to shareholders	**620,352**	194,630	218.73
Net increase of cash and cash equivalents	**-22,041**	348,835	-106.32

Notes:

(1) Increase in turnover was due to the adjustment of sales product mix and a rise in the sales unit price of products;

(2) Increase in the cost of principal operations was due to the change in sales product mix and a rise in the cost of raw materials;

(3) Increase in the profit of principal operations was due to the increase in gross profit margin of principal operations;

(4) Increase in profit attributable to shareholders was due to the increase in the profit of principal operations;

(5) Decrease in the increased amount of cash and cash equivalents was due to the increase in project expenses.

2. Items of balance sheets

Unit: Rmb'000

Items	At 30 June 2003	At 31 December 2002	Increase/ Decrease(%)
Total assets	**13,019,359**	12,293,565	5.90
Shareholders' funds	**8,000,571**	7,674,255	4.25
Long-term loans	**1,963,000**	1,463,000	34.18
Cash at banks and in hand	**1,680,010**	1,702,051	-1.29
Bills receivable	**1,982,730**	1,719,474	15.31
Inventories	**1,144,386**	1,217,049	-5.97
Construction in progress	**3,178,906**	2,327,558	36.58
Bills payable	**1,504,930**	1,525,791	-1.37
Short-term bank loans	**100,000**	65,000	53.85

Notes:

(1) Increase in total assets was due to the net profit generated from operating activities, the increase in borrowings for construction projects from fund-raising activities and increase in project expenses;

(2) Increase in long-term loan was due to the borrowings of Rmb600 million for technological improvement during the period;

(3) Increase in bills receivable was due to the increase in turnover and customers' increase in the use of bills for settlement;

(4) Increase in construction in progress was due to the increase in expenses on technological improvement project;

(5) Increase in short-term bank loans was due to the repayment of a loan of Rmb100 million to Industrial and Commercial Bank of China which would be due on 30 June 2004. In the period, ANSC-TKS Galvanizing Co. Ltd. repaid a short-term loan of Rmb65,000,000.

(7) Business plan for the second half of 2003

1. To strengthen overall corporate management and promote innovativeness of management. To strengthen budget management, work out budget breakdown, step up budget control and increase management standard. To speed up the establishment of an information network and integrate information management in procurement, production, equipment, technology, finance and human resources;

2. To continue with the stepping up of reform, advance and establish new structures in respect of staffing and the distribution system in line with market competition;

3. To focus on technological improvements so as to achieve output targets and improve efficiency, implement technological renovation and develop new profit growth centres. To focus on the development of the large section plant renovation project, cold rolled sheet renovation and expansion project, galvanizing production line and colour coating projects so as to achieve target output and utilization as soon as possible;

4. To strengthen market research, make accurate prediction of changes in the market and formulate production and operation policies based on gathered market information. To strive to develop relationship with direct suppliers and maintain stable sales to direct suppliers by establishing long-term supply and demand relationship with them and maintain a stable sales network;

5. To strengthen the development of new products, continue the adjustment of product mix, increase the proportion of specialized, distinctive and high quality products and further reform and improve technological innovation structure;

6. To further improve the centralized and unified management system for production, strive to expand production scale and increase the economic benefits of the Company.

(8) Liquidity, financial resources and capital structure of the Group (in accordance with IFRS)

1. As at 30 June 2003, the Group had long term bank loans of Rmb1,963 million, which were mainly for technological improvement. The terms of the loans range from three to eleven years. The annual interest rate for the loan of Rmb1,763 million is 5.49% while the remaining Rmb200 million is 5.76%.

2. As at 30 June 2003, the Group had cash and cash equivalents and assets of Rmb1.68 billion. They amounted to Rmb1.702 billion as at the end of 2002.

   As at 30 June 2003, the total assets less current liabilities of the Group amounted to Rmb9,971 million, compared with Rmb9,147 million at the end of 2002. The shareholders' funds of the Group amounted to Rmb8,000 million as at 30 June 2003, compared with Rmb7,674 million as at the end of 2002.

(9) Assets pledged

ANSC-TKS Galvanizing Co. Ltd. ("ANSC-TKS"), the Company's jointly controlled entity, was pledged certain of its land use rights, construction in progress, properties, buildings, machinery and equipment to Bank of China as securities for a loan. The Company has pledged the 50% equity interests held by it in ANSC-TKS to Bank of China.

(10) Commitments and contingent liabilities

As at 30 June 2003, the Group had capital commitment of Rmb1,778 million for financing the construction costs of projects.

(11) As at 30 June 2003, the Group did not have any contingent liabilities.

(12) Foreign currency risk

The Company does not have any significant foreign currency risk exposure arising from its sales and raw materials purchases for production as these transactions are mainly carried out in Renminbi, with the exception of a small portion of export sales conducted in foreign currencies.

(13) Gearing ratio

In accordance with IFRS, the shareholders' funds to liabilities ratio of the Group as at 30 June 2003 was 1.59 times, compared with 1.66 times as at 31 December 2002.