

# Management Discussion and Analysis

## 1. REVIEW OF OPERATIONS

China continued to experience rapid economic development in 2003, which resulted in an increase in demand for steel products. During 2003, the Company took full advantage of market opportunities and made effective use of its production resources. The Company actively adjusted product structure and optimized its production organization to achieve a higher level of production output. The average selling price of the Company's steel products increased by 27.11% in 2003 over 2002. However, upstream products prices also increased. The price of raw materials of the Company generally increased in 2003 by 21.64% over 2002.

### (i) Operating Results

In accordance with IFRS, the Group recorded a net profit of Rmb1,433,002,000 for the year ended 31 December 2003, representing an increase of 139.51% as compared with the previous year, and basic weighted average earnings per share was Rmb0.484.

In accordance with PRC Accounting Rules and Regulations, the Group recorded a net profit of Rmb1,432,579,000 for the year ended 31 December 2003, representing an increase of 140.94% as compared with the previous year, and basic weighted average earnings per share was Rmb0.484.

### (ii) Analysis of the Group's Financial and Operational Status (In accordance with PRC Accounting Rules and Regulations)

Item	Unit: RMB'000		
	2003	2002	Change (%)
Total assets	<b>15,011,870</b>	12,425,350	20.82
Long-term liabilities	<b>1,898,337</b>	1,473,121	28.86
Shareholders' fund	<b>8,948,268</b>	7,805,448	14.64
Income from			
principal operations	<b>14,520,736</b>	10,771,077	34.81
Profit from principal			
operations	<b>2,299,052</b>	1,272,680	80.64
Net profit	<b>1,432,579</b>	594,588	140.94
Net increase in cash			
and cash equivalents	<b>904,925</b>	940,822	-3.82

# Management Discussion and Analysis *(Continued)*

## 1. REVIEW OF OPERATIONS *(continued)*

### (ii) Analysis of the Group's Financial and Operational Status (in accordance with IFRS)

	2003	2002	Change (%)	Reasons for change
Total assets	<b>14,845,674</b>	12,293,565	20.76	A
Long-term liabilities	<b>1,898,002</b>	1,472,264	28.92	B
Shareholders' funds	<b>8,815,385</b>	7,674,255	14.87	C
Turnover	<b>14,482,148</b>	10,746,477	34.76	D
Profit from principal operations	<b>2,276,228</b>	1,265,561	79.86	E
Net profit	<b>1,433,002</b>	598,316	139.51	F
Net increase in bank deposits, cash and cash equivalents	<b>904,925</b>	940,822	-3.82	G

*Unit: Rmb'000*

*Notes:*

- A. Increase in total assets was due to the net profit generated from operation and the increase in cash and other assets generated from operating activities and fund-raising activities;
- B. Increase in long-term debt was due to the borrowings of Rmb850,000,000 for new projects and transfer of current liabilities of Rmb420,000,000;
- C. Increase in shareholders' interests was due to the net profit generated from operations and shares issued upon conversion of convertible debentures;
- D. Increase in turnover was due to the improvement in product selling structure, the expansion of the selling ratio of high value-added products and the rise of product price;
- E. Increase in profit from principal operations was due to the improvement in product selling structure and the increase in product price which was higher than the increase in costs;
- F. Increase in net profit was due to the increase in profit from principal operations and the decrease of income tax for the Company in 2003 as a result of the preferential taxation policy;
- G. Decrease in the increased amount of cash and cash equivalents over the previous year was due to the decrease in cash flow generated by fund-raising activities in the year over the previous year.

# Management Discussion and Analysis *(Continued)*

## 1. REVIEW OF OPERATIONS *(continued)*

### (iii) Number of Employees of the Company, Employees' Qualifications, Salary Policy and Training

As at 31 December 2003, the Company had 7,720 employees, of whom 5,257 were involved in production, 52 were sales personnel, 345 were technicians, 49 were accounting personnel, 544 were administrative personnel. Among them, 773 had bachelor or higher degrees, representing 10.01% of the total number of the employees; 920 had technical diplomas, representing 11.92% of the total number of the employees; 271 had secondary education, representing 3.51% of the total number of the employees. As at the end of the year, the Company had to bear the retirement cost for 1,365 staff members.

In 2003, the Company firmly focused on its production operations and reforms, and carried out training for its staff which included training for the projects which integrated the projects of the expansion and renovation of cold rolled steel, galvanized rods, color coating renovation, thick plates renovation, and deployed the staff technical grading training and production staff training which enhanced staff's operation level. A total of more than 3,000 employees have been trained.

## 2. IMPACT OF TAX RATE, EXCHANGE RATE AND INTEREST RATES

The tax rate applicable to the Company did not change in 2003 as compared with the previous year. However, the Company has enjoyed two significant preferential taxation policies in the year. First, the application of domestic equipment in technological renovation projects granted concessions in income tax resulting in the reduction of income tax amounted to Rmb219,000,000. Second, technological development leading to the production of new products granted concessions in income tax amounted to Rmb62,000,000. The lending rate applicable to the Company did not have any material change in the year as compared with the previous year.

## 3. THE INVESTMENT OF THE COMPANY

### 1. External Investments

In 2003, the Company, Angang New Steel and Iron Company Limited ("ANSI") and Angang International Trading (Group) Company ("AITG") jointly contributed capital of Rmb48,000,000 for the establishment of 鞍鋼瀋陽鋼材加工配送有限公司 (Angang Shenyang Steel Product Processing & Distribution Company Limited) (the "Processing Company"), of which Rmb14,400,000 was contributed by the Company, representing 30% of the investment, Rmb14,400,000 by ANSI, representing 30% and Rmb19,200,000 by AITG, representing 40%. The "Processing Company" is principally engaged in the processing, sale, warehousing and delivery of steel products.

# Management Discussion and Analysis *(Continued)*

## 3. THE INVESTMENT OF THE COMPANY *(continued)*

### 2. Use of proceeds

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. The Company has raised a total amount of Rmb4,113,000,000.

*Unit: Rmb'000*

Projects undertaken	Proposed investment	Changes in use of proceeds	Actual investment	Actual/ (estimated) benefits	Whether progressing as scheduled and estimated return
Construction of steel smelting plant	2,400,000	No	1,540,992	105,000	Yes
Renovation of the combined pickling and continuous rolling line	700,000	No	645,434	95,000	Yes
Construction of the jointly invested galvanised steel production line	Total project investment: 1,494,000 The Company's total investment: 250,000	No	Total project investment: 1,000,000 The Company's total investment: 248,305	15.51% (Estimated)	No
Renovation of the Cold Rolling Plant 1700 cross cutting lines	60,000	No	60,000	15,000	Yes
Renovation of cold rolling line	1,950,000	No	1,629,562	92,000	Yes
Cold Rolling Plant's renovation of No. 2 and 3 cross cutting lines	100,000	No	32,960	32,000	Yes
Distribution centre for Cold Rolling Plant	180,000	No	0	15.66% (Estimated)	No
<b>Total</b>	<b>5,640,000</b>		<b>4,157,253</b>		

The Company used proceeds of Rmb469,131,000 in 2003. To date, the Company's proceeds of Rmb4,113,400,000 have been completely applied in the relevant projects.

# Management Discussion and Analysis *(Continued)*

## **3. THE INVESTMENT OF THE COMPANY** *(continued)*

### **3. Progress on uncompleted projects financed by proceeds**

The major reason for the delayed completion of the cutting and distribution center in the Cold Rolled Plant was that the project's operation plans required further analysis.

### **4. Progress of investment 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, a substantial part of the production line has been completed and put into operations. As at 31 December 2003, Rmb1,305,486,000 had been invested.
2. The alteration project for the Large Section Plant has been completed. As at 31 December 2003, Rmb785,560,000 had been invested. An earning of Rmb90,000,000 was generated from this project in the year.
3. The renovation of the flattening machine of the Thick Plate Plant and alteration of the main power supply unit of the plant have been completed. As at 31 December 2003, Rmb400,972,000 had been invested. An earning of Rmb62,410,000 was generated from this project in the year.

# Management Discussion and Analysis *(Continued)*

## **4. THE IMPACT OF THE OPERATING ENVIRONMENT, MACROECONOMIC POLICY AND CHANGES IN LAWS AND REGULATIONS ON THE COMPANY**

1. On 4 December 2003, the US government announced the removal of trade protection measures on iron and steel products. On 6 December 2003, the European Union announced the removal of trade protection measures on iron and steel products. On 25 December 2003, the Chinese government announced the cancellation of similar measures. To date, iron and steel trade protection measures in three major markets that impact the world's iron and steel market have all been removed.

The implementation of protection measures on iron and steel products by China had a vital impact on maintaining the normal order of the import and export trade of iron and steel products as well as the healthy development of domestic iron and steel market. It also facilitated the development of the Company's operations.

At present, with the strong market for steel products in China and the international market, as well as the positive trend of increasing steel prices, the removal of trade protection measures should not have a material impact in the short-term for the Company. In the long run, the removal of such protection measures will encourage increased importation of steel products into China, and the extent of its impact will mainly depend on the continuing growth of the international market.

2. On 13 January 2004, the Ministry of Commerce published announcement (2003) No. 75 which stated that from 14 January 2004, importers of cold rolled sheets from Russia, Korea, Ukraine and Kazakhstan as well as the Taiwan region shall pay corresponding anti-dumping duty to the PRC government. This ruling will have a positive impact on maintaining a normal market order, and also will generate positive impact on the operations of the Company.

## **5. LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE OF THE GROUP (IN ACCORDANCE WITH IFRS)**

As at 31 December 2003, the Group had long term loans of Rmb1,893,000,000 with annual interest rates of 5.49% and 5.76%. The term of the loans range from 2 to 11 years and the loans were mainly used for plant construction.

As at 31 December 2003, the Group had cash, cash equivalents and bank deposits of Rmb2,607 million, which increased by Rmb905 million from Rmb1,702 million from the previous year. It was attributable to an increase in cash received from sales of products and financing activities.

In 2003, the total assets less current liabilities of the Group amounted to Rmb10,713 million, compared with Rmb9,147 million in 2002. The shareholders' fund of the Group amounted to Rmb8,815 million in 2003, compared with Rmb7,674 million by the end of 2002.

# Management Discussion and Analysis *(Continued)*

## **6. ASSETS PLEDGED**

The Company's jointly controlled entity 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 had pledged the 50% equity interests held by it in the jointly controlled entity to the Bank of China.

## **7. COMMITMENTS AND CONTINGENT LIABILITIES**

As at 31 December 2003, the Group had capital commitment of Rmb1,649,000,000, which was primarily the expenses of construction projects.

As at 31 December 2003, the Group did not have any contingent liabilities.

## **8. FOREIGN EXCHANGE RISK**

The Company does not have any significant foreign currency risk exposure arising from its sales and purchases of raw materials 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.

## **9. GEARING RATIO**

In accordance with IFRS, the shareholders' funds to liabilities ratio of the Group in 2003 was 1.46 times, compared with 1.66 times in 2002.