CHAIRMAN'S STATEMENT

Hebei Jinxi Iron and Steel Company Limited

Foshan Jin Xi Jin Lan Cold Rolled Sheet Company Limited

The Board is pleased to announce that the audited consolidated turnover of the Group for the year 2004 was RMB9,119 million, representing an increase of 72.8% as compared to that of 2003, while audited profit attributable to shareholders was RMB1,177 million, representing a growth of 9.4% when compared to that of 2003. Audited basic earnings per share for the year 2004 was RMB0.42, which represented a decrease of 17.6% from that of 2003.

BUSINESS REVIEW

Despite substantial fluctuations in the market prices of steel and raw materials in the first half of 2004 and the impact of the PRC's austerity measures, the overall performance in 2004 still improved from that of 2003 due to the reason that the steel market rebounded in the second half of 2004, the price of iron powder fell from that of the first half of 2004, as well as the change of the product mix of the Group and the staff's dedicated efforts.

In 2004, the Group sold approximately 2,006,000 tonnes of billets and 1,379,000 tonnes of strips, representing increases of 17.0% and 95.0% from approximately 1,714,000 tonnes of billets and 707,000 tonnes of strips in 2003 respectively. The average selling prices of billets and strips (net of value-added tax) were RMB2,599 per tonne and RMB2,808 per tonne respectively, representing increases of 23.2% and 21.2% from RMB2,109 per tonne and RMB2,316 per tonne in 2003 respectively.

Due to increases in the prices of iron powder and coke, the average cost of sales of the Group's billets and strips in 2004 were RMB2,270 per tonne and RMB2,341 per tonne respectively, representing increases of 37.2% and 37.9% when compared with RMB1,654 per tonne and RMB1,698 per tonne in 2003 respectively.

In 2004, gross profit of billets and strips were reduced to RMB329 per tonne and RMB467 per tonne respectively (2003: RMB455 per tonne and RMB618 per tonne respectively). The gross profit in 2004 increased by 6.4% to RMB1,311 million when compared to that of 2003 (2003: RMB1,232 million).

Awards to the Company and the Management

Hebei Jinxi Iron and Steel Company Limited ("Jinxi Limited"), a subsidiary of the Group, was named as the "Enterprise with Greatest Growth Potential" and as one of the "Top 500 Chinese Enterprises" by the China Enterprise Confederation and the China Enterprise Directors Association in January 2005 and August 2004 respectively. Jinxi Limited was also named as the "Large-Scale Industrial Enterprise in China" by the National Bureau of Statistics of China in August 2004.

In addition, Mr. Han Jingyuan, the Chairman and the Chief Executive Officer of the Company, received the "Outstanding Entrepreneur of Hebei Province" award from the Hebei Provincial Enterpriser Association in July 2004, and was named as "The Most Attention-grabbing Chinese Entrepreneur in 2004" by the China Enterprise Confederation and the China Enterprise Directors Association in January 2005.

Human Resources and Remuneration Policies

As at 31 December 2004, the Group had a workforce of 4,617 (31 December 2003: 4,462); and temporary staff of 1,792 (31 December 2003: 1,134). Staff cost of the Group for the year approximated to RMB146 million (2003: RMB106 million), representing an increase of 37.7%. The cost included basic salaries and benefits, as well as other staff benefits such as discretionary bonus, medical and insurance plans, pension scheme, unemployment insurance plan and maternity insurance plan. The Group's remuneration policies are designed to tie its employees' income to their production and/or sales volume, as well as to the extent that they meet the Group's quality control and cost control targets. In order to improve the Group's productivity and further enhance the quality of its workforce, the Group implemented continuing education and training programmes for both the management staff and factory workers.

Production Capacity

The annual production capacity of the Group is as follows:

	31 December 2004 ***Tonnes***	31 December 2003 *Tonnes*
Billets	**3,500,000**	3,100,000
Narrow-width strips	**800,000**	730,000
Mid-width strips	**1,000,000**	—

H-section Steel Rolling Line

As at 31 December 2004, the Group has entered into equipment and projects contracts amounting to approximately RMB765.2 million. Site construction had already commenced. Production of the entire project will commence in the second quarter of 2006. The project is expected to have an annual production capacity of 1 million tonnes of H-section steel.

Investment in Foshan Jin Xi Jin Lan Cold Rolled Sheet Co., Ltd.

The Group owns 60% of the equity interests in Foshan Jin Xi Jin Lan Cold Rolled Sheet Co., Ltd. (the "Joint Venture") following its entering into an equity transfer and capital increase agreement with the original investors on 28 December 2004. From January to February 2005, the Group has already injected US$17.88 million as registered capital into the Joint Venture. In March 2005, the Company provided US$10 million as security deposit for bank loans granted to the Joint Venture for the purpose of providing financial support to its full-scale operation.

The Joint Venture, with annual production capacity of 400,000 tonnes of cold rolled sheets and 180,000 tonnes of galvanized sheets, is expected to commence production in April 2005.

Dividend Policy

The Company intends to distribute not less than 20% of the Group's distributable profit as dividend for the periods subsequent to its listing, but the actual amount of dividend and its percentage to the profit will be at the discretion of the board of directors and will depend upon the Company's future operation and earnings, capital requirement and surplus, general financial condition, contractual restrictions, and other factors that the board of directors deem relevant. In addition, pursuant to relevant PRC law, Jinxi Limited's distributable profit should not be higher than its net profit after allocations made to the statutory reserve and welfare funds as determined by PRC generally accepted accounting principles.

Capital Structure

After taking into account the proceeds from the listing of the Group, the cash and bank balances of the Group as at 31 December 2004 substantially increased to RMB2,926 million (31 December 2003: RMB189 million).

The current ratio had improved significantly from 0.96 at the end of 2003 to 1.69 as at 31 December 2004.

As at 31 December 2004, the Group's loans repayable within one year and loans repayable after one year amounted to RMB1,458 million and RMB459 million respectively (31 December 2003: RMB322 million and RMB683 million respectively). The major reason for the increase in bank loans was that the Company used part of the proceeds from the listing as security for the bank loans of RMB1,200 million granted to Jinxi Limited. That banking facility will be utilised to finance/re-finance the capital expenditure and for general corporate purposes of the Group.

The consolidated interest expenses in 2004 amounted to RMB64.27 million (2003: RMB30.796 million). The interest coverage was 19.3 times (2003: 38.1 times), which remained at a healthy level.

As at 31 December 2004, the ratio between total liabilities and total assets of the Group was 46.5%, representing an improvement on the same ratio of 75.0% as at 31 December 2003.

To conclude, the financial position of the Group was further strengthened when compared to that of 2003.

Use of Proceeds from Global Offering

In March 2004, the Company issued 805,000,000 shares at HK$2.75 per share by way of the global offering and the over-allotment. The net proceeds after deducting the relevant expenses were approximately HK$2,107 million.

During the period from the date of listing to 31 December 2004, the use of net proceeds from the listing as stated in the Prospectus was as follows:

	RMB million
Construction of mid-width strip rolling line	86.1
Coal powder blowing technique	2.0
Energy recycling for power generation	8.1
Construction of the H-section steel rolling line	122.8
Demolition of three 120 m^3 blast furnaces to construct a 530 m^3 blast furnace *(note 1)*	8.7
General corporate purposes (Including working capital and repayment of loans)	351.8
	579.5

Note 1: To enhance production efficiency, the plan to expand to a 450 m^3 blast furnace as disclosed in the Prospectus had been changed to the construction of a 530 m^3 blast furnace.

As at 31 December 2004, the proceeds not yet utilised were placed in banks as short-term deposits, of which US$164 million (approximate RMB1,359 million) was placed in commercial banks as deposits or security deposits as collateral for newly-added banking facilities granted to Jinxi Limited.

The above-mentioned three projects including mid-width strip rolling line, coal powder blowing technique and energy recycling for power generation were completed during the year of 2004. As at 31 December 2004, the total expenditures of these three projects were approximately RMB431.6 million, which were mostly financed by the Group's internal resources.

The expected utilisation of the listing proceeds in three completed projects as disclosed in the Prospectus was RMB280 million. After the deduction of approximately RMB96.2 million of actual utilisation during 2004 and approximately RMB21.8 million of the estimated payment in 2005 of the outstanding construction fees of the projects from the above-mentioned expected utilisation of the listing proceeds, the remaining balance will be approximately RMB162 million. In order to achieve higher efficiency of the listing proceeds, the remaining balance will be reallocated to the expected utilisation of the listing proceeds for the construction of the H-section steel rolling line as disclosed in the Prospectus, which will be increased from RMB800 million to RMB962 million.

Capital Commitments

As at 31 December 2004, the Group had capital commitments amounting to RMB1,445 million (31 December 2003: RMB820 million) which mainly consisted of the construction of the H-section steel rolling line. Such capital commitments will be financed by the listing proceeds and the Group's internal resources.

Guarantees and Contingent Liabilities

As at 31 December 2004, the Group's contingent liabilities amounted to RMB395.88 million (31 December 2003: RMB27 million), which mainly consisted of the guarantees for the letter of credit issued by an agent (appointed by the Group to import machinery and equipment on behalf of the Group) to the supplier.

Pledge of Assets

As at 31 December 2004, the net book value of the Group's buildings and machinery pledged as security for the Group's bank loans amounted to approximately RMB494 million (31 December 2003: RMB212 million).

Exchange Risks

As at 31 December 2004, Renminbi, US dollar and HK dollar accounted for 26.3%, 73.3% and 0.4% of the Group's total bank balance respectively (31 December 2003: 97.4%, 0% and 2.6% respectively).

As majority of the sales, purchases of raw materials and bank loans committed by the Group were mainly in Renminbi in 2004 and 2003, and the exchange rates of Renminbi to HK dollar and US dollar were relatively stable, the Group's exposure to foreign exchange risk remained relatively low. In light of the construction of H-section steel rolling line, the Group had entered into project and equipment contracts of Euro 44.19 million approximately. Hence, in March 2005, the Group has already entered into future forward contract for Euro to hedge partial exchange rate risk exposure and is actively exploring ways to hedge its exchange rate risk exposure to Euro.

Interest Rate Risks

The interest rates of the Group's loans are subject to variations. The risk of increasing interest rate will increase the interest costs of both new loans and existing loans. At present, the Group has not used any derivatives to hedge its interest rate risk exposure.

Prospects

Although the steel market will face the increase in the production capacity of the steel industry, the uncertainties over whether the austerity measures will further deepen and whether the interest rate will rise in the PRC in 2005, the continuous economic growth in the PRC will mitigate, to a certain extent, the adverse impact of the above-mentioned factors.

With respect to the major raw materials, it is expected that the price of iron powder will remain hovering at high levels as a result of the rise in the price of iron ore in the international market. As the proportion of the imported iron ore used by the Group was approximately 15% to 20%, the impact of rising price of imported iron ore on the Group will be limited. On the coke front, it is estimated that the supply of coke will be greater than its demand in the domestic market and competition amongst the coke enterprises will be intensified. As such, the price of coke is expected to basically remain at similar levels as the previous year or sustain a slight increase.

In view of growing competition in the steel industry, the Group will continue to optimise its product mix and put more efforts in new product development. In terms of capacity, strips will account for 51% of the total steel production volume in 2005. In addition, the production of cold rolled steel sheets will commence in April 2005, which is expected to make contribution to the Group.

On Behalf of the Board
CHINA ORIENTAL GROUP COMPANY LIMITED

Han Jingyuan
Chairman and Chief Executive Officer

Hong Kong, 31 March 2005