

PROSPECTS

With the effects of the PRC's macroeconomic control and gradual on-streaming of projects under construction, the second half of 2005 is expected to see a steady growth in domestic steel production. However, there remains a challenge from the declining steel product prices, especially the obvious oversupply of steel products for construction. As such, the Company will taking full use of market changes, keep a close eye on specialized market demand, continuously to explore right path of sales, high valued added by-products, expand market share of profitable products and stick to its production scheduling tactics as planned to secure output for a maximum utilisation of production capacity. Meanwhile, procurement management will be further reinforced for quality enhancement of raw and auxiliary materials as well as the reduction in procurement cost. The Company will put efforts in energy saving and consumption reduction to cut down workflow costs. The Company expects to stabilise and refine its product quality. The Company is committed to technological renovations to achieve the production and operating target for the year.

MANAGEMENT DISCUSSION AND ANALYSIS

During the first half of 2005, the Company had leverage the opportunity of great demand for domestic steel and achieved the expected target through adjustment of structure, cultivation of potential and expanding production, saving energy and lowering consumption and strengthening of management. For the six months ended 30th June 2005, the Company's turnover amounted to RMB4,705,291,000, representing an increase of 9.7% as compared with the same period of last year. Profit before taxation amounted to RMB462,216,000, representing a decrease of 13.83% as compared with the same period of last year. Earnings per share amounted to RMB0.369, representing a decrease of 20.82% as compared with the same period of last year.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN REVENUE

In the first half year of 2005, the Company's turnover amounted to RMB4,705,290,000, of which RMB4,454,270,000 was derived from the sales of steel products, accounted for 94.67% of the total revenue and representing an increase of 9.58% over the same period of last year, and RMB251,020,000 was derived from the sales of non-steel products such as water granulated slag, coking and smelting by-products, cutting steel leftover and hydroelectricity, which accounted for 5.33% of the total revenue and represented an increase of 11.84% over the same period of last year.

Turnover	First half of 2005		First half of 2004		As compared with the first half of 2004
	Amount		Amount		Increase/ decrease
	RMB0'000	Percentage (%)	RMB0'000	Percentage (%)	(%)
Steel plates	240,837	51.18	198,176	46.20	21.53
Steel sections	84,149	17.88	105,255	24.54	-20.05
Wire rods	50,276	10.68	48,600	11.33	3.45
Steel billets	62,939	13.38	54,448	12.70	15.59
Cold rolled thin plates	7,226	1.55	—	—	Unapplicable
Sub-total	445,427	94.67	406,479	94.77	9.58
Others	25,102	5.33	22,445	5.23	11.84
Total	470,529	100	428,924	100	9.70

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN REVENUE (CONTINUED)

During the first half of 2005, the Company's sales revenue of the steel products increased by RMB389,480,000 as compared with the same period of last year, of which:

1. During the first half of 2005, the sales volume of the steel products (billets) amounted to 1,168,700 tonnes, representing a decrease of 0.35% over the same period of last year. As there was change in structure, revenue from sales increased by RMB41,210,000.

	First half of 2005 0'000 tonnes	First half of 2004 0'000 tonnes	As compared with the first half of 2004	
			Increase/ decrease(%)	Increase in revenue (RMB0'000)
Steel plates	54.98	50.71	8.42	16,687
Steel sections	25.30	32.99	-23.31	-24,539
Wire rod	15.91	16.22	-1.91	-929
Steel billets	19.17	17.36	10.43	5,676
Cold rolled thin plates	1.51	—	unapplicable	7,226
Total	<u>116.87</u>	<u>117.28</u>	<u>-0.35</u>	<u>4,121</u>

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

I. INCREASE IN REVENUE (CONTINUED)

2. During the first half of 2005, the average selling price of steel products (billets) amounted to RMB3,811 per tonne, representing an increase of 9.95% over the same period of last year. Revenue from sales increased by RMB34,778,000.

Selling price	First half of 2005 (RMB/tonne)	First half of 2004 (RMB/tonne)	As compared with the first half of 2004	
			Increase/ decrease(%)	Increase in revenue (RMB'000)
Steel plates	4,380	3,908	12.08	25,951
Steel sections	3,326	3,191	4.23	3,416
Wire rod	3,160	2,997	5.44	2,593
Steel billets	3,283	3,136	4.69	2,818
Cold rolled thin plates	4,785	—	unapplicable	—
Total	<u>3,811</u>	<u>3,466</u>	<u>9.95</u>	<u>34,778</u>

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

II. DECREASE IN PROFIT

Profit before taxation amounted to RMB462,216,000 for the first half of 2005, representing a decrease of RMB74,172,000 as compared with the same period of last year, which included:

1. Gross profit amounted to RMB723,927,000, representing a decrease of RMB14,490,000 over the same period of last year due to the decrease in gross profit rate.

Although the average selling price of steel products for the first half of the year of the Company increased by 9.95% as compared with the same period last year, as there was significant increase in purchase prices raw material such as of ore, coal, pig iron and scrap iron, the increase in cost exceeded the rise in selling price which resulted in the decrease of overall gross profit ratio for the first half of this year of the Company from 17.22% of the same period last year to 15.39%.

2. Other revenues amounted to RMB9,178,000, representing a decrease of RMB5,339,000 as compared with the same period of last year.
3. Distribution costs amounted to RMB71,128,000, representing an increase of RMB3,223,000 as compared with the same period of last year, which was mainly attributable to an increase in ship inspection costs.
4. Administrative expenses amounted to RMB123,539,000, representing an increase of RMB21,244,000 as compared with the same period of last year, which was mainly attributable to the increased surcharges such as social insurance as a result of the increased wages.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

II. DECREASE IN PROFIT (CONTINUED)

5. Other operating expenses amounted to RMB25,779,000, representing an increase of RMB20,006,000 as compared with the same period of last year. This was mainly attributable to the disposal of fixed assets with the improving technology.
6. Finance costs amounted to RMB50,443,000, representing an increase of RMB9,870,000 as compared with the same period of last year. This was mainly attributable to an increase in loans interest.

III. SOUND FINANCIAL POSITION

1. As of 30th June 2005, total assets and total liabilities of the Company amounted to RMB8,084,927,000 and RMB4,007,242,000 respectively. The gearing ratio was 49.56%. Current assets and current liabilities amounted to RMB3,346,253,000 and RMB3,204,197,000 respectively. The current ratio was 104.43%.
2. In the first half of 2005, upon net cash inflow from operating activities of RMB479,290,000 and together with the net cash inflow from financing activities of RMB411,460,000, deducted net expense of investment activities of RMB698,217,000 (mainly innovation of coke furnace and optimized production facilities and innovation for medium plate rolling machine and steel sections rolling machine, construction of blast furnace of 1,350m³ etc.), the cash and cash equivalents increased by RMB192,530,000. As at 30th June 2005, the cash and cash equivalents of the Company amounted to RMB988,830,000.