



Management Discussion and Analysis

BUSINESS REVIEW

For the year ended 31 December 2005, the Group posted a record high turnover of approximately HK\$4,570.0 million, representing an encouraging increase of approximately 38.9% as compared to approximately HK\$3,289.6 million for the previous year. Net profit attributable to shareholders amounted to approximately HK\$305.0 million, representing an increase of HK\$25.7 million over the previous year. The strong growth in turnover and profit was the combined positive result of the Group's further investments in the steel manufacturing business and the organic growth of its core business during the year.

The following discussions and analysis should be read in conjunction with our consolidated financial statements together with the accompanying notes, included elsewhere in the report.

Manufacture and sale of steel products

The Group operates in this business segment through a wholly-owned subsidiary, Qinhuangdao Shougang Plate Mill Co., Ltd. ("Qinhuangdao Plate Mill") and a 96% owned subsidiary (previously an associate), Qinhuangdao Shouqin Metal Materials Co., Ltd. ("Shouqin").

At the beginning of the year, the Group held an effective interest of 51% in Shouqin (27% held by the Group directly and 24% held by Qinhuangdao Plate Mill). As mentioned in the Company's 2005 Interim Report, the Group acquired a further direct interest of 45% in Shouqin during the year, the transaction of which was completed as of November 2005, making up a total effective interest of 96% in Shouqin.



Qinhuangdao Plate Mill achieved a good performance for 2005. Its turnover recorded a new height of HK\$2,914.8 million (before elimination of intersegment sales) for the year, representing an increase of HK\$497.3 million from HK\$2,417.5 million (before elimination of intersegment sales) in 2004. This significant growth in turnover was driven by both favourable volume variance and favourable price variance.

During the year, Qinhuangdao Plate Mill increased the sales of its major steel products by approximately 114,000 metric tonnes to approximately 689,000 metric tonnes, with an increase of average price of HK\$25 per metric tonne. Similar to last year, by virtue of increased production and economies of scale in the procurement of raw materials, Qinhuangdao Plate Mill successfully lessened the adverse effects of a general rise in the price of raw materials. Accordingly, net profit of Qinhuangdao Plate Mill and its intermediate holding companies attributable to the Group (excluding the result for Shouqin, which will be described below) was HK\$161.8 million for the year ended 31 December 2005, showing an impressive increase in profit of HK\$44.2 million over that in 2004.



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Shouqin recorded a turnover of HK\$3,136.3 million for the year. As it only commenced production in mid 2004, turnover of last year was HK\$1,378.2 million. Approximately 1,099,000 metric tonnes of steel slabs were sold in 2005, representing an increase of 633,000 metric tonnes as compared to approximately 466,000 metric tonnes sold in 2004. Despite the apparent decline in steel product price in the fourth quarter which caused a negative impact on sales revenue and earnings, Shouqin's full year operation in 2005 was deemed satisfactory. For the year ended 31 December 2005, net profit attributable to the Group from Shouqin amounted to HK\$36.1 million, versus a profit contribution of HK\$38.9 million for last year.



Shipping operations

Shougang Concord Shipping Holdings Limited and its subsidiaries ("Shougang Shipping Group") was mainly engaged in the time charter business for the year ended 31 December 2005. During the year, the adjustment of freight rates in the market has caused a decline of HK\$45.3 million in charter hire income, from HK\$270.8 million in 2004 to HK\$225.5 million in 2005. Against this background, the time charter

business achieved an operating profit of HK\$68.9 million for the year, as compared to an operating profit of HK\$112.4 million for 2004. Shougang Shipping Group also conducted a floating crane business with operating profit of HK\$3.2 million for the year ended 31 December 2005, which increased moderately from a profit of HK\$2.7 million for the year ended 31 December 2004. For the year ended 31 December 2005, Shougang Shipping Group reported a net profit attributable to shareholders of HK\$70.6 million, a decrease of HK\$39.9 million from a net profit attributable to shareholders of HK\$110.5 million in 2004.

Electricity generation

Beijing Shougang Firstlevel Power Company Limited ("Beijing Power Plant") reported a turnover of HK\$411.0 million for the year ended 31 December 2005, representing an increase of HK\$29.6 million from HK\$381.4 million achieved in 2004. The total quantity of electricity generated and sold by Beijing Power Plant was approximately 1,171 million Kwh with a sales revenue of HK\$354.5 million for 2005, a rise of approximately 43 million Kwh and HK\$26.1 million as compared with the sales quantity of approximately 1,128 million Kwh and sales revenue of HK\$328.4 million in 2004. Sales revenues for steam and hot water for 2005 also increased by HK\$2.0 million and HK\$1.5 million, to HK\$33.1 million and HK\$23.4 million respectively. The higher output and enhanced revenue for the year have fully offset the impact of surging prices for major fuel sources including coal, coal gas, water and other ancillary materials. As a result, the Group's share of Beijing Power Plant's net profit has increased moderately to HK\$28.8 million in 2005 from HK\$26.6 million in 2004.



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Manufacture of steel cord for radial tyres

For the year ended 31 December 2005, turnover of Shougang Concord Century Holdings Limited and its subsidiaries (“Shougang Century Group”) reached a new height of HK\$592.9 million, representing a growth rate of 38.6% from HK\$427.9 million for that of last year. During the year, the strong growth in turnover was mainly driven by its core business of manufacture of steel cord for radial tyres, which grew by 50.6% to HK\$401.4 million for the current year due to expansion of production capacity since mid 2004.

In spite of the increase in sales volume, the radial tyres business faced strong price competition during the year, which has caused Shougang Century Group’s gross profit to decline by HK\$16.8 million to HK\$95.9 million. However, Shougang Century Group successfully continued to maintain its expenditure at a satisfactory level during the year. As a result, the net profit contributed by Shougang Century Group to the Group only declined slightly by HK\$0.3 million to HK\$17.1 million for the year ended 31 December 2005.

Trading of steel products; manufacture and installation of kitchen and laundry equipment

Following the efforts of the management to streamline its operations and to strengthen the steel trading business last year, Shougang Concord Steel Holdings Limited and its subsidiaries (“Shougang Steel Group”) achieved a further improvement in performance in 2005, both in terms of sales growth and profitability. It reported a turnover of HK\$1,163.4 million for the year ended 31 December 2005, representing an increase of HK\$910.2 million as compared to HK\$253.2 million for last year. Turnover of the steel trading business amounted to HK\$1,086.3 million, whereas the turnover of the kitchen and laundry equipment business also reached HK\$77.1 million during the year. In terms of profitability, Shougang Steel Group achieved a net profit of HK\$19.4 million for the year, a substantial growth of HK\$18.1 million from HK\$1.3 million earned in 2004.

LIQUIDITY AND FINANCIAL RESOURCES

The Group normally financed its operations by cash generated from its business activities and banking facilities provided by its bankers. For the year ended 31 December 2005, the Company obtained extra source of funding in the sum of HK\$9.9 million by the issue of 25.1 million new ordinary shares of the Company to certain employees upon their exercise of share options of the Company.

As at 31 December 2005, the Group had aggregate banking facilities of HK\$245.5 million and RMB2,762.0 million with banking institutions in Hong Kong and in the PRC, respectively. These banking facilities were utilized to the extent of HK\$44.5 million and RMB2,732.0 million respectively as at 31 December 2005. The banking facilities in Hong Kong were secured by certain properties and prepaid lease rentals of HK\$18.4 million in total, and those in the PRC were secured by certain plant and machinery with an aggregate net book value of RMB329.3 million and corporate guarantees from Shougang Corporation of RMB2,562.0 million.



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Due to consolidation of Shouqin's accounts, the Group's current assets as at the current year amounted to HK\$1,858.4 million, an increase of HK\$703.6 million from last year end's level of HK\$1,154.8 million (restated). The Group's current liabilities also increased from HK\$696.6 million to HK\$3,698.8 million, representing an increase of HK\$3,002.2 million for the year. Hence, the Group's working capital showed a net current liabilities position of HK\$1,840.4 million by end of 2005 from net current assets of HK\$458.2 million by end of 2004. The Group's current ratio, defined as current assets divided by current liabilities, accordingly decreased to 0.50 times as at 31 December 2005 from 1.66 times as at end of last year. The Group's gearing ratio which is defined as total debts divided by equity increased to 2.23 times as at 31 December 2005 as compared to 0.51 times as at 31 December 2004. In order to hedge against foreign currency risks, the Group had entered into some forward exchange contracts for certain normal business transactions during the year. By the end of 2005, the outstanding forward exchange contracts were denominated in United States Dollars ("USD"), Renminbi, Euro ("EUR") and Switzerland Francs ("CHF"), for which the Group sold USD 11 million against Renminbi, sold HK\$85 million against Renminbi, bought EUR249,581.73 against Hong Kong Dollars and bought CHF103,275 against Hong Kong Dollars.

Capital Structure

At the beginning of the current year, the issued share capital of the Company was HK\$927.5 million, represented by 4,637,251,215 ordinary shares at par value of HK\$0.20 each. During the year, certain option holders of the Group exercised the granted options, pursuant to which 25,146,000 new ordinary shares were issued at the exercise prices range of HK\$0.295 to HK\$0.41 per share. In addition, a wholly-owned subsidiary of the Company entered into agreements with third parties in August 2005 to acquire a total of 45% interest in Shouqin for a consideration of RMB467.5 million (equivalent to HK\$448.2 million). According to the terms of the agreements, 40% of the said consideration which amounted to HK\$179.3 million, would be satisfied by the issue of 271,659,999 new ordinary shares of the Company at HK\$0.66 per share. The said transaction was completed during the year. As a result of the aforesaid events, the issued share capital of the Company increased to HK\$986.8 million, represented by 4,934,057,214 ordinary shares as at 31 December 2005.

Subsequent to the balance sheet date, the Company entered into a share subscription agreement on 13 February 2006 with an independent investor, Carlo Tassara International S. A. (the "Subscriber"), pursuant to which the Subscriber would subscribe for 929,000,000 new ordinary shares of the Company at HK\$0.53 per share. Details of the said share subscription were described in the Company's announcement dated 14 February 2006 and the transaction was completed in early March 2006.



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As described in our circular to the shareholders dated 20 May 2005 and the special resolution of which was duly approved by the shareholders at the extraordinary general meeting held on 13 June 2005, the Company sought to cancel the share premium account and the capital reserve account (the "Cancellation") in writing off its accumulated losses, to the extent permitted by the High Court of Hong Kong (the "High Court"). The High Court made an order confirming the Cancellation on 1 September 2005, which was duly registered with the Companies Registry in Hong Kong on 1 September 2005. Accordingly, the Cancellation became effective on the same day. As a result, the share premium account of the Company has been reduced by HK\$1,412,855,741.98 and the capital reserve account of the Company has been reduced by HK\$1,800,000,000.00. An amount of HK\$2,920,201,029.67 arising from such reduction has been applied towards the elimination of the accumulated losses of the Company and the remaining balance of HK\$292,654,712.31 has been credited to the Company's special capital reserve account. Against this background, the Company will consider distributing dividends in the future.

CONTINGENT LIABILITIES

The Company has provided guarantees for the due and punctual performance and observance by a wholly-owned subsidiary of the Company of each and every of its obligations, undertakings and liabilities under two time charter hires, through which the Group leases certain of its vessels. The time charter hires commenced on 26 September 1997 with a lease period of 15 years, plus two months more or less in the Group's option. The daily rates of the time charter hires increase by US\$250 every half year until December 2007, and thereafter the daily rates will increase by US\$125 every half year.

EMPLOYEES AND REMUNERATION POLICIES

The Group had a total of approximately 3,500 employees as at 31 December 2005.

The remuneration policies of the Group are to ensure the fairness and competitiveness of total remuneration in order to motivate and retain existing employees as well as to attract potential employees. Remuneration packages are structured in a way that takes into account local practices under various geographical locations in which the Group operates.

The remuneration packages of Hong Kong employees include salary payments, discretionary bonuses on a performance basis, medical subsidies and a hospitalisation scheme. All of the subsidiaries of the Group located in Hong Kong provide pension schemes for their Hong Kong employees as part of their staff benefits. The remuneration packages of certain employees in the PRC include salary payments, discretionary bonuses on a performance basis, medical subsidies and welfare fund as part of their staff benefits.



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PROSPECTS

With the further acquisition of interest in Shouqin, our enlarged Group is empowered to step up its efforts to strengthen the growth and profitability potentials. The Group will also proactively identify suitable investment opportunities to further develop its long-term growth. We will focus on opportunities which are most beneficial to the Group and can strengthen our value chain.

Given the bright prospects of the PRC's economy and the competitive market position enjoyed by the Group, the Group is in excellent position to capture good business opportunities with an objective to maximize shareholders' return in the long run.