

1. REVIEW OF OPERATIONS

The competition was fierce in the PRC steel market in 2005. Domestic steel enterprises were challenged by overcapacity, shortage of energy supply, rising prices of raw materials and declining prices of steel products.

Facing such adverse factors, the Company took active efforts in exploring market, strengthening research and development on market-oriented basis and reducing production cost to minimise adverse impacts and achieved the ever best records in its production, operation, innovation and renovation. Meanwhile, the Company substantially moved forward with assets restructuring, laying a solid foundation for its future development.

(1) Operating Results

In accordance with IFRSs, the Group recorded a net profit of Rmb2,117,397,000 for the year ended 31 December 2005, representing an increase of 17.79% as compared with the previous year, and basic earnings per share was Rmb0.715.

In accordance with PRC Accounting Rules and Regulations, the Group recorded a net profit of Rmb2,079,485,000 for the year ended 31 December 2005, representing an increase of 17.07% as compared with the previous year, and basic weighted average earnings per share was Rmb0.702.

(2) Analysis of the Group's Financial and Operational Status

Prepared in accordance with PRC Accounting Rules and Regulations

| Item | Unit: Rmb'000 | | |
|--|--------------------|------------|------------|
| | 2005 | 2004 | Change (%) |
| Total assets | 14,289,823 | 15,343,328 | (6.87) |
| Long-term liabilities | 604,013 | 1,244,548 | (51.47) |
| Shareholders' funds | 11,329,257 | 10,133,942 | 11.80 |
| Income from principal operations | 26,488,115 | 23,227,617 | 14.04 |
| Profit from principal operations | 3,755,332 | 3,363,488 | 11.65 |
| Net profit | 2,079,485 | 1,776,337 | 17.07 |
| Net (decrease) / increase in cash and cash equivalents | (2,185,794) | 141,157 | (1,648.48) |

1. REVIEW OF OPERATIONS (continued)

(2) Analysis of the Group's Financial and Operational Status (continued)

Prepared in accordance with IFRSs

| Item | 2005 | 2004 | Unit: Rmb'000 | |
|---|--------------------|------------|---------------|-------------------|
| | | | Change (%) | Reason for change |
| Total assets | 14,223,931 | 14,899,934 | (4.54) | A |
| Non-current liabilities | 604,013 | 1,244,548 | (51.47) | B |
| Total equity attributable to equity shareholders of the Company | 11,250,702 | 10,022,276 | 12.26 | C |
| Turnover | 26,488,115 | 23,227,617 | 14.04 | D |
| Gross profit | 3,724,184 | 3,372,351 | 10.43 | D |
| Profit for the year and attributable to equity shareholders of the Company | 2,117,397 | 1,797,587 | 17.79 | E |
| Net (decrease) / increase in deposit with banks and cash and cash equivalents | (2,185,794) | 141,157 | (1,648.48) | F |

Note:

- A. The decrease in total assets was attributable to repayment of bank loans and distribution of dividends;
- B. The decrease in non-current liabilities was attributable to transferral of bank loan mature within one year to current liabilities;
- C. The increase in total equity attributable to equity shareholders of the Company was attributable to the profit generated from operations;
- D. The increases in turnover and gross profit were mainly attributable to the increase in sales volume, the proportional increase in sales of high value-added products and the increased product prices;
- E. The increase in profit for the year and attributable to equity shareholders of the Company was mainly attributable to the increase in gross profit; and
- F. The decrease in deposit with banks balance and cash and cash equivalents was attributable to repayment of loans, payment of construction expenses and distribution of dividends.

1. REVIEW OF OPERATIONS (continued)

(3) Analysis of the changes of financial figures of the Group's assets and expenses (prepared in accordance with PRC Accounting Rules and Regulations)

Unit: Rmb'000

| Item of Balance Sheet | 31 December 2005 | | 31 December 2004 | | Increase/ (decrease) of percentage in total assets compared with previous year(%) |
|-----------------------------|------------------|--|------------------|--|---|
| | Amount | As a percentage in total assets (%) | Amount | As a percentage in total assets (%) | |
| Cash at bank and in hand | 562,339 | 3.94 | 2,748,133 | 17.91 | (13.97) |
| Receivables and Prepayments | 1,369,558 | 9.58 | 2,295,374 | 14.96 | (5.38) |
| Fixed assets, at cost | 11,438,201 | 80.04 | 11,146,973 | 72.65 | 7.39 |
| Accumulated depreciation | 4,905,493 | 34.33 | 4,067,194 | 26.51 | 7.82 |
| Construction in progress | 2,840,603 | 19.88 | 611,746 | 3.99 | 15.89 |
| Undistributed profit | 3,732,361 | 26.12 | 2,960,225 | 19.29 | 6.83 |

Note:

- 1) The decrease in the percentage of cash at bank and in hand in total assets was attributable to repayment of loans, payment of construction expenses and distribution of dividends.
- 2) The decrease in accounts receivables and prepayments was mainly attributable to the decrease in bills receivable, which was due to the decrease in working capital as a result of repayment of loans, payment of construction expenses and distribution of dividends, discounting of bills of Rmb200,000,000 and endorsement of bills of Rmb589,000,000.
- 3) The increase in fixed assets at cost was attributable to completion of certain technological renovation projects which were transferred to fixed assets during the reporting period.
- 4) The increase in accumulated depreciation was attributable to provision for depreciation during the reporting period.
- 5) The increase in construction in progress was attributable to the increase in project expenses for the 2130 cold rolling production line and other project expenses.
- 6) The increase in undistributed profit was attributable to the net profit generated from operations during the reporting period.

1. REVIEW OF OPERATIONS (continued)

(3) Analysis of the changes of financial figures of the Group's assets and expenses (prepared in accordance with PRC Accounting Rules and Regulations) (continued)

Unit: Rmb'000

| Item of Income Statement | 2005 | 2004 | Increase / (decrease) compared with previous year% |
|--------------------------|----------------|---------|---|
| Operating expenses | 462,875 | 423,192 | 9.38 |
| Administrative expenses | 348,542 | 281,900 | 23.64 |
| Financial expenses | 64,038 | 120,840 | (47.01) |
| Income tax | 902,969 | 856,406 | 5.44 |

Note:

- 1) The increase in operating expenses was attributable to the rise in selling costs from the increased sales volume and the rise in export operating expenses from the increased exports volume.
- 2) The increase in administrative expenses was mainly attributable to the expenses arising from the Company's acquisition of the entire equity interests in ANSI.
- 3) The decrease in financial expenses was attributable to repayment of bank loans and the decrease in interest expenses as a result of the decreased loans.
- 4) The increase in income tax was attributable to the increased total profit.

1. REVIEW OF OPERATIONS *(continued)*

(4) Analysis of components of cash flow generated from the Group's operating activities, investing activities and financing activities (prepared in accordance with PRC Accounting Rules and Regulations)

Unit: Rmb'000

| Item | 2005 | 2004 | Main reason for change |
|--|-------------|-----------|---|
| Net cash flows from operating activities | 2,553,120 | 1,594,803 | The increase in net cash inflow from operating activities was mainly due to the increase in net profit from operations and the decreases in both operating receivables and the increment of inventories |
| Net cash flows from investing activities | (2,655,508) | (836,358) | The increase in net cash outflows from investing activities was due to acquisition of fixed assets and the increase in construction expenses. |
| Net cash flows from financing activities | (2,096,443) | (593,128) | The increase in net cash outflows from financing activities was mainly due to the year-on-year increases in repayment of loans and payment of dividends. |

(5) Number of Employees of the Company, Employees' Qualifications, Salary Policy and Training Programmes of the Company

As of 31 December 2005, the Company had 6,092 employees, among whom 3,855 were in production, 37 in sales, 450 in technology, 54 in accounting and 454 in administration. Of the Company's employees, 1,002 had bachelor or higher degrees, representing 16.4% of the total number of the employees, 1,117 had diplomas, representing 18.3% of the total number of the employees and 252 had secondary education, representing 4.1% of the total number of the employees.

In 2005, the Company provided variegated training programmes to address different needs of its employees. During the year, the Company organised various training programmes to a total of 20,214 participants, of whom, 665 from management, 2,162 from administration and technology teams and 17,387 from production and services.

1. REVIEW OF OPERATIONS *(continued)*

(5) Number of Employees of the Company, Employees' Qualifications, Salary Policy and Training Programmes of the Company *(Continued)*

The Company adopted position-linked and liability-linked annual remuneration packages for the senior management; position-linked remuneration and new product incentive packages for scientific research personnel; sales profit-linked remuneration package for sales personnel; and position-linked remuneration packages for other personnel.

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

With effect from 21 July 2005, the PRC adopted a managed floating exchange rate system subject to adjustment with reference to the basket of currencies based on market supply and demand. The Company exports some of its products and also imports certain equipment and spare parts. As the Company had adopted a foreign exchange risk control while entering into contracts for such import and export, the changes in the exchange rates had no material impacts on the Company.

There was no material impacts on the changes of tax rate and exchange rates on the Company when comparing the figures of 2005 and that of 2004.

3. INVESTMENT OF THE COMPANY

(1) External Investments

The Company's external investment for 2005 amounted to Rmb2,479,000, representing a decrease of 94.69% from Rmb46,664,000 in the last year.

The 23rd meeting of the third Board was held on 1 December 2005, at which the Company's acquisition of 6% interests (equivalent to Rmb2,479,000) in TKAS (Changchun) Tailored Blanks Ltd held by Wuhan Zhongren Ruizhong Auto Parts Industry Co., Ltd was considered and approved.

3. INVESTMENT OF THE COMPANY (continued)

(2) Use of Proceeds

In March 2000, the Company issued convertible debentures at the total par value of Rmb1,500,000,000, raising a total of Rmb1,480,000,000, in the PRC.

Unit: Rmb'000

| | |
|---------------------------------------|-----------|
| Total proceeds | 1,480,000 |
| Total use of proceeds during the year | 0 |
| Total accumulated use of proceeds | 1,480,000 |

| Projects undertaken | Proposed investment | Changes in use of proceeds | Actual investment | Actual (estimated) benefits | Whether progressing as scheduled and estimated return |
|--|---------------------|----------------------------|-------------------|-----------------------------|---|
| Renovation of cold rolling line | 1,950,000 | No | 1,585,710 | 313,809 | Yes |
| Cold Rolling Plant's renovation of No. 2 and 3 cross cutting lines | 100,000 | No | 32,960 | 31,098 | Yes |
| Cutting and Distribution centre for the Cold Rolling Plant | 180,000 | No | 0 | 15.66% (estimated) | No |
| Total | 2,230,000 | — | 1,618,670 | — | — |

Reason for the failure keeping in line with the schedule and estimated return

The delay in completion of the cutting and distribution centre for the cold rolling plant was due to the further analysis required with respect to the Company's operation plans.

3. INVESTMENT OF THE COMPANY (continued)

(3) Progress of investment of non-publicly raised funds

| Item | Estimated amount <i>(Rmb'000)</i> | Progress | Return |
|-----------------------------------|---|--------------------|--------|
| 2130 cold rolling production line | 2,640,000 | Under construction | — |
| Total | 2,640,000 | — | — |

4. LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE OF THE GROUP (PREPARED IN ACCORDANCE WITH IFRSs)

As at 31 December 2005, the Group had long-term loans of Rmb604 million (exclusive of loans due within one year) with annual interest rates ranging from 5.76% to 6.12%. Under the term of 2 to 9 years, the loans will expire in the period from 2007 to 2014. The loans are mainly used for technological renovation. The Group's bank loans due within one year amounted to Rmb758 million. With good creditability and high profitability of products, the Group has sufficient cash to repay the existing liabilities falling due in the future.

As at 31 December 2005, the Group's deposits with banks and cash and cash equivalents decreased by Rmb2,186 million to Rmb562 million from Rmb2,748 million in the previous year, which was mainly due to payment of construction expenses, repayment of loans and distribution of dividends.

As at 31 December 2005, the Group's total assets less current liabilities amounted to Rmb11.855 billion, as compared with Rmb11.267 billion as at 31 December 2004. The shareholders' fund of the Group amounted to Rmb11.251 billion in 2005, as compared with Rmb10.022 billion as at 31 December 2004.

5. ASSET PLEDGED

ANSC-TKS Galvanizing Co., Ltd ("ANSC-TKS") pledged its trade receivables, land use rights, construction in progress, properties, buildings and machinery and equipment to the Bank of China as security for its loans from the Bank of China. In addition, the Company pledged its 50% equity interests in ANSC-TKS to the Bank of China.

6. CAPITAL COMMITMENTS AND CONTINGENT LIABILITIES

As at 31 December 2005, the Group had capital commitment of Rmb21.457 billion, which were primarily the expenditures for the acquisition of the entire equity interests in ANSI and construction projects.

As at 31 December 2005, the Group did not have any contingent liabilities.

7. FOREIGN EXCHANGE RISK

Save for certain product exports, the Company's sales of products and purchases of equipment, raw materials and spare parts are mainly denominated in Renminbi. Therefore, there is no material exposure to foreign exchange risks in the Company's transactions.

8. GEARING RATIO

In accordance with IFRSs, the shareholders' funds to liabilities ratio of the Group as at 31 December 2005 was 3.78 times, compared with 2.05 times as at 31 December 2004.