

## BUSINESS REVIEW

In the first quarter of 2006, steel prices maintained the growth momentum in 2005 with persisting slump of steel products market. Meanwhile, in April, the price of imported iron ore in April rose by 19%, resulting in increasing cost and shrinking profitability of steel and iron production, leaving a tough situation for the Company. Seizing the market opportunity, the Company adjusted its sales strategy and rollout strengthen the implementation of cost reduction of process and procurement to ameliorate the unfavorable situation. Due to the substantial decrease in steel prices, the Company recorded sales revenue as RMB4,420,430,000 and profit before taxation as RMB35,040,000 in the second half of the year, representing a decrease of 6.05% and 92.42% respectively compared with the same period of 2005.

### 1. STRENGTHENING PRODUCTION PLAN TO FULLY EXPLORE PRODUCTION CAPACITY

In the first half of the year, the Company conducted activities of the "Implementation Year" seriously, focusing on achieving goals of production and operation, strengthening production management and expanding production scale. In the first half, the Company produced 640,400 tonnes of coking coal, 1,245,000 tonnes of pig iron, 1,431,700 tonnes of steel and 1,348,700 tonnes of steel products (billets), representing a rise of 14.14%, 13.70%, 11.83% and 16.35% respectively over the same period of last year. The production scale saw a significant increase over the same period of last year, hitting a historical record level.



## BUSINESS REVIEW (CONTINUED)

### 2. SEIZING MARKET INFORMATION TO STRENGTHEN MARKETING

In response to the slump of steel products market and falling price of steel products, the Company has established an early warning mechanism. After improving its market research and keeping a close eye on the changing steel products market, the Company was more able to predict and capture the market change and made timely adjustment to product prices in order to maximize the efficiency. Meanwhile, the Company enhanced the improvement of its capability to hedge business risks by maintaining a strategic relationship with the 16 customers. In the first half, the Company sold 1,380,400 tonnes of steel products (billets), representing a rise of 18.12% compared with the same period of last year. The collection rate of accounts receivable was 104.19%, with an increase of 1.5% over the same period of last year.



## BUSINESS REVIEW (CONTINUED)

### 3. IMPROVING PRODUCT QUALITY STEADILY TO SECURE REPUTATION

In the first half of the year, the Company further strengthened supervision and management of production process, improved the early warning system of abnormal information on quality and established a management system of quality inspection. For 40 indicators of quality appraisal established at the beginning of the year, the Company recorded a plan-completion ratio of 100%. According to 38 indicators, which are comparable to last year, the ratio of stability improvement was 86.84%. The overall quality of products output remained stable and no claims on poor quality was recorded. The ratio of the Company's products having accredited the fame as the Famous Brands in Chongqing reached 70.47%, representing a growth of 7.66% over the same period of last year. The Company has applied for registration for its steel plates for shipbuilding and pressure vessel plates for boilers as "the Famous Brand in China".

## BUSINESS REVIEW (CONTINUED)

### 4. SAVING COSTS TO IMPROVE TECHNICAL AND ECONOMIC INDICATORS

In the first half of 2006, the Company improved its policy of public bidding purchase, strictly enforced the terms of the contracts, increased the purchase volume of ore exploited in China and controlled the purchase cost of raw fuel material. The Company made an effort in deploying “benchmark review” and cost reduction of production process. Among the 45 comparable technical and economic indicators, 22 or 48.8% of them recorded a breakthrough in historical standards; while 40 or 80% of them showed noticeable year-on-year improvement. Energy consumption of iron-smelting and steel rolling process dropped by 8.96% and 3.54% respectively over the same period of last year, while the aggregate energy consumption of steel per tonne saw a decrease of 7.43% over the same period of last year. The production cost of the Company's products decreased by 11.9% over the same period of last year.

### 5. ADJUSTING PRODUCT STRUCTURE AND ACTIVELY DEVELOPING NEW PRODUCTS

After closely monitoring the change of market demand, the Company made efforts on the development of profitable products. In the first half of the year, four products were successfully developed, namely, Q370qd, Q420qd steel plates for bridge building, Q460C high strength steel plate and 20# angle steel. The output of new products and products with special requirement reached 299,600 tonnes, realizing an output value of RMB911,000,000, leading to an increase of 66.44% and 31.28% respectively over the same period of last year.



## PROSPECTS

In the second half of 2006, the imbalance of supply and demand of steel products will persist and the price of steel products will remain at a low level albeit China's economy will continue to grow steadily and rapidly. As a result, the Company will face the pressure of profit decrease. As such, the Company will carry out activities of the "Implementation Year", strengthen management and achieve a scale of mass production. The product structure will be adjusted to expand the market share of profitable products. The Company will further enhance the management of purchase of raw ancillary materials to optimize the resource allocation and lower the purchase cost. Meanwhile, the Company will enhance new products development and increase the output of profitable products.

## MANAGEMENT DISCUSSION AND ANALYSIS

In face of the austere steel market environment in the first half of 2006, the Company proactively adjusted its marketing strategies to promote and increase sales and production as well as reduce consumption and costs. However, due to the considerable decrease in steel prices, the Company's profit decreased. For the six months ended 30th June 2006, the Company recorded a turnover of RMB4,420,430,000, a decrease of 6.05% over the same period last year. Profit before taxation amounted to RMB35,040,000, a decrease of 92.42% over the same period last year.

