Notes to Condensed Consolidated Interim Financial Statements

1. CORPORATION INFORMATION

China Special Steel Holdings Company Limited (the "Company") was incorporated as an exempted company with limited liability in the Cayman Islands on 11 March 2004 under the Companies Law, Chapter 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. The registered office of the Company is located at Century Yard, Cricket Square, Hutchins Drive, P.O. Box 2681GT, George Town, Grand Cayman, British West Indies. The principal place of business of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") is located at No. 4 Third Street, Jinshui District, Zhengzhou, Henan Province, the People's Republic of China (the "PRC"). The principal place of business of the Company is located at Room 3504, 35th Floor, China Merchants Tower, Shun Tak Centre, 168-200 Connaught Road Central, Hong Kong.

The principal activities of the Company are investment holding and the trading of iron ore. The Group is principally engaged in the manufacture and sale of special steel products in Mainland China.

The shares of the Company have been listed on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 19 May 2005.

In the opinion of the directors, Easyman Assets Management Limited ("Easyman"), a company incorporated in the British Virgin Islands and is wholly owned by Mr. Dong Shutong ("Mr. Dong"), is the ultimate holding company of the Group.

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES

Basis of preparation

The condensed consolidated interim financial statements have been prepared under the historical cost convention in accordance with International Accounting Standards 34 "Interim Financial Reporting" and the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules").

Notes to Condensed Consolidated Interim Financial Statements

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES (Continued)

Significant accounting policies

Except for the new and revised International Financial Reporting Standards ("IFRSs") effective from 1 January 2006, the accounting policies adopted in the preparation of the condensed consolidated interim financial statements are consistent with those followed in the preparation of the annual financial statements for the year ended 31 December 2005.

Impact of New and Revised International Financial Reporting Standards ("IFRSs")

The following new and revised IFRSs affect the Group and are adopted for the first time for the current period's interim financial statements.

IAS 19 Amendment	Actuarial Gains and Losses, Group Plans and Disclosures
IAS 21 Amendment	Net investment in a Foreign Operation
IAS 39 Amendment	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
IAS 39 Amendment	The Fair Value Option
IAS 39 & IFRS 4 Amendments	Financial Guarantee Contracts
IFRSs 1 & 6 Amendments	First-time Adoption of International Financial Reporting Standards and Exploration for and Evaluation of Mineral Resources
IFRS 6	Exploration for and Evaluation of Mineral Resources
IFRIC-Int 4	Determining Whether an Arrangement Contains a Lease
IFRIC-Int 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
IFRIC-Int 6	Liabilities arising from Participating in a Specific Market — Waste Electrical and Electronic Equipment (effective for accounting periods beginning on or after 1 December 2005)

The adoption of these new standards had no material impact on the accounting policies of the Group and the Company and the methods of computation in the Group's and the Company's financial statements during the six months ended 30 June 2006.

Notes to Condensed Consolidated Interim Financial Statements

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES (Continued)

Impact of Issued But Not Yet Effective IFRSs

The Group has not applied the following new and revised IFRSs, that have been issued but are not yet effective, in these financial statements. Unless otherwise stated, these IFRSs are effective for annual periods beginning on or after 1 January 2007:

IAS 1 Amendment	Capital Disclosures
IFRS 7	Financial Instruments: Disclosures
IFRIC-Int 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies (effective for accounting periods beginning on or after 1 March 2006)
IFRIC-Int 8	Scope of IFRS 2 (effective for accounting periods beginning on or after 1 May 2006)
IFRIC-Int 9	Reassessment of Embedded Derivatives (effective for accounting periods beginning on or after 1 June 2006)
IFRIC-Int 10	Interim Financial Reporting and Impairment (effective for accounting periods beginning on or after 1 November 2006)

The IAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

IFRS 7 requires disclosure relating to financial instruments and incorporates many of the disclosure requirements of IAS 32. This IFRS shall be applied for annual periods beginning on or after 1 January 2007.

Except as stated above, the Group expects that the adoption of the pronouncements listed above will not have any significant impact on the Group's financial statements in the period of initial application.

Notes to Condensed Consolidated Interim Financial Statements

3. REVENUE AND OTHER INCOME

Revenue represents the net invoiced value of goods sold, net of value-added tax, after allowances for returns, trade discounts and various types of government surcharges, where applicable.

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Sale of goods:		
Bearing steel	**338,690**	391,144
Spring steel	**32,905**	32,211
Carbon structure steel and gear steel	**3,275**	1,061
	374,870	424,416
Interest income	**2,614**	672
Reversal of unclaimed trade payable balances aged more than 3 years	**2,589**	—
Sale of scrap materials	**782**	401
Others	**323**	218
Other income	**6,308**	1,291
Total revenue	**381,178**	425,707

The principal activities of the Group are manufacture and sale of special steel products to customers in the PRC. The principal assets employed by the Group are located in the PRC. Accordingly, no segmental analysis by business or geographical segment is provided.

Notes to Condensed Consolidated Interim Financial Statements

4. PROFIT BEFORE INCOME TAX

The Group's profit before income tax is arrived at after charging/(crediting):

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Cost of inventories recognised as an expense	**288,354**	338,416
Interest on loans and discounted bills	**10,012**	10,853
Bank charges and other finance costs	**166**	331
Finance costs	**10,178**	11,184
Staff costs (including directors' and senior executives' emoluments):		
Salaries and other staff costs	**10,585**	8,728
Retirement costs:		
Defined contribution retirement fund	**1,630**	967
Equity-settled share-based payments	**1,579**	—
Total staff costs	**13,794**	9,695
Research and development costs	**215**	247
Auditors' remuneration	**1,080**	893
Depreciation of property, plant and equipment	**22,688**	22,880
Amortisation of prepaid land lease payments	**154**	153
Provision for impairment of trade receivables	**432**	—
Gain on disposal of property, plant and equipment	**(17)**	(4)
Minimum lease payments under operating leases in respect of land and buildings	**464**	480

Notes to Condensed Consolidated Interim Financial Statements

5. INCOME TAX EXPENSES

Hong Kong profits tax has been provided at the rate of 17.5% (six months ended 30 June 2005: 17.5%) on the estimated assessable profits of the Company arising in Hong Kong during the six months ended 30 June 2006. Hence, the applicable Hong Kong corporate income tax rate of the Company which operates in Hong Kong is 17.5% based on existing legislation. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the jurisdictions in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

No provision for Hong Kong profits tax has been made as the Group had no assessable profits arising in Hong Kong for the six-month periods ended 30 June 2006 and 2005.

The applicable income tax rate of Zhengzhou Yongtong Special Steel Co., Ltd. ("Yongtong Special Steel") and Gongyi Yongtong Scrap Steel Co., Ltd. ("Yongtong Scrap Steel"), subsidiaries of the Group, was 33% for the six-month periods ended 30 June 2006 and 2005.

Yongtong Special Steel was re-registered as a wholly-foreign-owned company on 10 November 2003. In accordance with the relevant tax laws and regulations in the PRC and pursuant to the approval from the local tax authority dated 4 June 2004, with effect from 1 January 2004, Yongtong Special Steel was exempted from corporate income tax of the PRC for the years ended 31 December 2004 and 2005, and is entitled to a 50% reduction in corporate income tax of the PRC for the years ending 31 December 2006, 2007 and 2008. Accordingly, Yongtong Special Steel was subject to PRC corporate income tax at an applicable income tax rate of 15% for the six months ended 30 June 2006.

Notes to Condensed Consolidated Interim Financial Statements

5. INCOME TAX EXPENSES (Continued)

Major components of income tax expense are as follows:

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Provision for income tax in respect of profit for the period:		
Current		
— charge for the period	**9,177**	—
Deferred	**(1,045)**	—
Tax expense	**8,132**	—

A reconciliation of the income tax expense applicable to profit before tax using the statutory rate to the income tax expense at the effective tax rate is as follows:

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Accounting profit	**53,193**	63,363
Loss of group companies not offset against taxable profit	**5,781**	1,901
	58,974	65,264

Notes to Condensed Consolidated Interim Financial Statements

5. INCOME TAX EXPENSES (Continued)

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Tax at an applicable tax rate of 33%	**19,461**	21,537
Tax effect of:		
Tax exemption	**(10,622)**	(21,497)
Tax loss utilized	**—**	(40)
Temporary differences not previously recognised	**(707)**	—
Income tax expense before minority interests	**8,132**	—

6. EARNINGS PER SHARE

The calculation of basic earnings per share for the current period is based on the profit attributable to the shareholders of the Company of RMB45,091,000 (six months ended 30 June 2005: RMB63,356,000), and the weighted average of 526,000,000 (six months ended 30 June 2005: 360,000,000) ordinary shares in issue during the period.

The calculation of diluted earnings per share amounts is based on the net profit for the six months ended 30 June 2006 attributable to shareholders of the Company. The weighted average number of ordinary shares used in the calculation is the ordinary shares in issue during the current period, as used in the basic earnings per share calculation and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise of all dilutive potential ordinary shares into ordinary shares.

Notes to Condensed Consolidated Interim Financial Statements

6. EARNINGS PER SHARE (Continued)

The calculations of basic and diluted earnings per share are based on:

	For the six months ended 30 June	
	2006	2005
	(Unaudited)	(Unaudited)
	RMB'000	RMB'000
Net profit for the period attributable to shareholders of the Company	**45,091**	63,356

	Note	Number of shares For the six months ended 30 June	
		2006	2005
		(Unaudited)	(Unaudited)
Weighted average number of ordinary shares in issue during the period used in the basic earnings per share calculation	(a)	**525,566,667**	360,000,000
Weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise of all share options outstanding during the period		**10,609,267**	—
Weighted average number of ordinary shares used in the diluted earnings per share calculation		**536,175,934**	360,000,000

Note:

(a) The weighted average number of ordinary shares used in the calculation of basic earnings per share for the six months ended 30 June 2005 is based on the assumption that the 320,000,000 shares issued as at 2 May 2005 had been in issue throughout the six months ended 30 June 2005.

Notes to Condensed Consolidated Interim Financial Statements

7. DIVIDENDS

Pursuant to a directors' resolution of the Company dated 10 April 2006, the Company declared a final dividend of HK$0.042 per ordinary share, totalling approximately HK$21,000,000 (equivalent to approximately RMB21,689,000) pertaining to 2005 for payment in 2006. The proposed final dividend was approved by the Company's shareholders at the Extraordinary General Meeting held on 30 June 2006.

Pursuant to the directors' resolution of the Company dated 18 September 2006, the Board declared an interim dividend of HK$0.02 per share.

8. RETIREMENT BENEFITS

As stipulated by the PRC state regulations, Yongtong Special Steel and Yongtong Scrap Steel participate in a defined contribution retirement plan. All employees are entitled to an annual pension equal to a fixed proportion of the average basic salary amount within the geographical area of their last employment at their retirement date. Yongtong Special Steel and Yongtong Scrap Steel are required to make contributions to the local social security bureau at 20% of the previous year's average basic salaries within the geographical area where the employees are under employment with Yongtong Special Steel and Yongtong Scrap Steel. The Group has no obligations for the payment of pension benefits beyond the annual contributions as set out above.

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance for those employees working in Hong Kong who are eligible to participate in the MPF Scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to the income statement as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme.

Notes to Condensed Consolidated Interim Financial Statements

9. PROPERTY, PLANT AND EQUIPMENT

	Buildings RMB'000	Plant and machinery RMB'000	Office equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
Cost:					
As at 1 January 2006	109,755	580,814	4,993	12,114	707,676
Additions	—	1,728	840	1,129	3,697
Transferred from construction in progress — note 10	197	19,434	—	—	19,631
Disposals	(35)	(61)	—	(142)	(238)
As at 30 June 2006	109,917	601,915	5,833	13,101	730,766
Accumulated depreciation:					
As at 1 January 2006	20,674	125,297	3,429	7,310	156,710
Charge for the period	2,444	18,866	391	987	22,688
Disposals	—	—	—	(96)	(96)
As at 30 June 2006	23,118	144,163	3,820	8,201	179,302
Impairment loss:					
As at 1 January 2006	—	3,058	—	—	3,058
Charge for the period	—	—	—	—	—
As at 30 June 2006	—	3,058	—	—	3,058
Net carrying amount:					
As at 30 June 2006	86,799	454,694	2,013	4,900	548,406
As at 31 December 2005	89,081	452,459	1,564	4,804	547,908

As at 30 June 2006, land use rights, certain buildings and plant and machinery of the Group with a net book value of RMB415,120,000 (31 December 2005: RMB422,001,000) in aggregate were pledged to banks to secure bank loans and notes payable amounting to RMB175,000,000 and RMB125,000,000, respectively (31 December 2005: RMB135,000,000 and RMB92,917,000), as set out in notes 16(a) and 18(a).

Notes to Condensed Consolidated Interim Financial Statements

10. CONSTRUCTION IN PROGRESS

	Six months ended 30 June 2006 (Unaudited) RMB'000	Year ended 31 December 2005 (Audited) RMB'000
At beginning of period/year	**119,036**	4,709
Additions	**54,816**	114,820
Transferred to property, plant and equipment — note 9	**(19,631)**	(493)
At end of period/year	**154,221**	119,036

Notes to Condensed Consolidated Interim Financial Statements

11. PREPAID LAND LEASE PAYMENTS

	Six months ended 30 June 2006 (Unaudited) RMB'000	Year ended 31 December 2005 (Audited) RMB'000
Cost:		
At beginning of period/year	**6,160**	6,160
Additions	**—**	—
At end of period/year	**6,160**	6,160
Accumulated amortisation:		
At beginning of period/year	**473**	168
Provided for the period/year	**154**	305
At end of period/year	**627**	473
Less: Current portion reclassified to prepayments, deposits and other receivables	**305**	305
Net book value:	**5,228**	5,382

Prepaid land lease payments represent expenditures in respect of land use rights for three pieces of land located in Didong Village, Gongyi City, for an estimated tenure of 20 years. As at 30 June 2006, land use rights and certain buildings of the Group were pledged to a bank to secure bank loans. Refer to note 18 for further details of the bank loans.

Notes to Condensed Consolidated Interim Financial Statements

12. INVENTORIES

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Raw materials	**63,747**	37,269
Work in progress	**21,305**	21,606
Finished goods	**20,157**	28,521
Spare parts and consumables	**52,376**	15,493
	157,585	102,889
Less: Provision against obsolete inventories	**(2,009)**	(2,009)
	155,576	100,880

Notes to Condensed Consolidated Interim Financial Statements

13. TRADE AND NOTES RECEIVABLES

An aged analysis of the trade receivables and notes receivables as at the balance sheet date, based on the due date, is as follows:

	30 June 2006			31 December 2005		
	Trade receivables (Unaudited) RMB'000	**Notes receivable (Unaudited) RMB'000**	**Total (Unaudited) RMB'000**	Trade receivables (Audited) RMB'000	Notes receivable (Audited) RMB'000	Total (Audited) RMB'000
Outstanding balances aged:						
Within 90 days	**65,227**	**6,428**	**71,655**	66,469	3,172	69,641
91–180 days	**2,172**	**16,723**	**18,895**	85	15,114	15,199
181–270 days	**1,100**	**—**	**1,100**	2,104	—	2,104
271–365 days	**26**	**—**	**26**	78	—	78
1–2 years	**609**	**—**	**609**	113	—	113
2–3 years	**170**	**—**	**170**	499	—	499
Over 3 years	**579**	**—**	**579**	461	—	461
	69,883	**23,151**	**93,034**	69,809	18,286	88,095
Less: provision for bad and doubtful debts	**(824)**	**—**	**(824)**	(813)	—	(813)
	69,059	**23,151**	**92,210**	68,996	18,286	87,282

The above trade and notes receivables balances are unsecured, interest-free and generally have credit terms of 30 to 60 days.

Notes to Condensed Consolidated Interim Financial Statements

14. PREPAYMENTS AND OTHER RECEIVABLES

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Prepayments to suppliers	**101,921**	87,922
Other prepayments	**1,620**	8,130
Other receivables	**7,252**	6,601
Current portion reclassified from prepaid land lease payments	**305**	305
	111,098	102,958

The above balances are unsecured and interest-free and have no fixed terms of repayment.

15. CASH AND CASH EQUIVALENTS AND PLEDGED TIME DEPOSITS

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Cash and bank balances	**182,205**	15,232
Time deposits	**162,446**	153,217
	344,651	168,449
Less: Pledged time deposits for notes payable	**(162,446)**	(153,217)
	182,205	15,232

Notes to Condensed Consolidated Interim Financial Statements

15. CASH AND CASH EQUIVALENTS AND PLEDGED TIME DEPOSITS (Continued)

The above time deposits as at 30 June 2006 were pledged to banks to secure notes payable of RMB208,600,000 (31 December 2005: RMB202,917,000) as set out in note 16(a).

The pledged time deposits bear interest at a rate of 2.07% (2005: 2.07%) per annum.

16. TRADE AND NOTES PAYABLES

An aged analysis of the trade payables and notes payables as at the balance sheet date, based on the due date, is as follows:

	30 June 2006			31 December 2005		
	Trade payables (Unaudited) RMB'000	**Notes payable (Unaudited) RMB'000**	**Total (Unaudited) RMB'000**	Trade payables (Audited) RMB'000	Notes payable (Audited) RMB'000	Total (Audited) RMB'000
		(a)			(a)	
Outstanding balances aged:						
Within 90 days	**64,346**	**75,000**	**139,346**	58,968	76,217	135,185
91–180 days	**10,054**	**133,600**	**143,654**	12,710	126,700	139,410
181–270 days	**7,141**	**—**	**7,141**	3,465	—	3,465
271–365 days	**1,918**	**—**	**1,918**	1,192	—	1,192
1–2 years	**2,453**	**—**	**2,453**	4,182	—	4,182
2–3 years	**865**	**—**	**865**	2,166	—	2,166
Over 3 years	**1,080**	**—**	**1,080**	2,952	—	2,952
	87,857	**208,600**	**296,457**	85,635	202,917	288,552

Trade payables are unsecured, interest-free and generally have credit terms of 30 to 60 days.

Notes to Condensed Consolidated Interim Financial Statements

16. TRADE AND NOTES PAYABLES (Continued)

Note:

(a) As at 30 June 2006, notes payable of RMB208,600,000 (31 December 2005: RMB202,917,000) were secured by time deposits amounting to RMB162,446,000 (31 December 2005: RMB153,217,000) as set out in note 15.

As at 30 June 2006, notes payable of the Group of RMB125,000,000 (31 December 2005: RMB92,917,000) were secured by fixed charges over the Group's land use rights, certain buildings, plant and machinery with a net book value of RMB415,120,000 (31 December 2005: RMB422,001,000) in aggregate as set out in note 9.

17. ACCRUED LIABILITIES AND OTHER PAYABLES

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Advance from customers	**4,834**	7,025
Payables related to purchases of property, plant and equipment	**11,934**	10,264
Value-added tax payables	**26,981**	27,560
Accrued interest expenses	**350**	265
Payroll payable	**2,675**	2,662
Other payables	**5,503**	5,017
	52,277	52,793

Other payables and accruals are unsecured, interest-free and have no fixed terms of repayment.

Notes to Condensed Consolidated Interim Financial Statements

18. INTEREST-BEARING LOANS AND OTHER BORROWINGS

	Notes	**30 June 2006 (Unaudited) RMB'000**	31 December 2005 (Audited) RMB'000
Bank loans			
Secured	(a)	**175,000**	142,425
Unsecured	(b)	**47,544**	30,000
Total		**222,544**	172,425
Repayable:			
Within one year		**222,544**	172,425
Portion classified as current liabilities		**(222,544)**	(172,425)
Long term portion		**—**	—

Notes:

(a) As at 30 June 2006, bank loans of the Group of RMB175,000,000 (31 December 2005: RMB135,000,000) with an interest rate of 5.58% per annum (31 December 2005: 5.58%) were secured by fixed charges over the Group's land use rights, certain buildings, plant and machinery with a net book value of RMB415,120,000 (2005: RMB422,001,000) in aggregate as set out in note 9.

As at 31 December 2005, a trust receipt bank loan of US$920,000 (equivalent to RMB7,425,000) with an interest rate of 7.90% per annum was secured by a lien over the Group's raw materials of RMB8,623,000.

(b) As at 30 June 2006, these unsecured bank loans denominated in US$ bore interest at 2% over and above London Inter Bank Offered Rate per annum and are repayable by October and November 2006.

Notes to Condensed Consolidated Interim Financial Statements

19. DEFERRED TAXATION

	Six months ended 30 June 2006 (Unaudited) RMB'000	Year ended 31 December 2005 (Audited) RMB'000
At beginning of period/year	**(2,343)**	(2,343)
Credited during the period/year	**1,045**	—
At end of period/year	**(1,298)**	(2,343)

The principal components of the Group's deferred income tax assets are as follows:

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Deferred tax liabilities:		
Capitalised financial interest	**(2,286)**	(2,343)
Deferred tax assets:		
Decelerated depreciation for tax purposes	**988**	—
Net deferred tax liabilities	**(1,298)**	(2,343)

Notes to Condensed Consolidated Interim Financial Statements

20. ISSUED CAPITAL

	Notes	Six months ended 30 June 2006 Number of ordinary shares	Six months ended 30 June 2006 RMB'000	Year ended 31 December 2005 Number of ordinary shares	Year ended 31 December 2005 RMB'000
Authorised:					
At beginning of period/year		**1,000,000,000**	**106,000**	3,800,000	403
Increase during period/year	(a)	**—**	**—**	996,200,000	105,597
At end of period/year		**1,000,000,000**	**106,000**	1,000,000,000	106,000
Issued and fully paid:					
At beginning of period/year		**500,000,000**	**53,000**	1	—
For the acquisition of the entire issued share capital of Infonics, issuing and allotting of ordinary shares of HK$0.10 each, credited as fully paid	(b)	**—**	**—**	69,999,999	7,420
Capitalisation issue	(c)	**—**	**—**	250,000,000	26,500
New issue on an initial public offering	(d)	**—**	**—**	180,000,000	19,080
New placement	(e)	**78,000,000**	**8,058**	—	—
At end of period/year		**578,000,000**	**61,058**	500,000,000	53,000

Notes:

(a) Pursuant to a directors' resolution of the Company dated 29 April 2005, the authorised share capital of the Company increased from HK$380,000, divided into 3,800,000 shares of HK$0.10 each, to HK$100,000,000, divided into 1,000,000,000 shares of HK$0.10 each.

(b) On 29 April 2005, Mr. Dong transferred his 10,001 shares of US$1 each in Infonics to the Company in consideration of the Company's allotting and issuing, credited as fully paid, 69,999,999 new shares to Easyman, a company wholly owned by Mr. Dong. Immediately following the transfer of the entire share capital of Infonics to the Company, the Company became the ultimate holding company of the Group.

(c) Upon the approval of the Company's listing on the Stock Exchange and pursuant to the resolution passed on 29 April 2005, the Company issued 250,000,000 ordinary shares of HK$0.10 each to the then existing shareholder. The issued share capital of RMB26,500,000 was offset against the share premium arising from the public listing.

Notes to Condensed Consolidated Interim Financial Statements

20. ISSUED CAPITAL (Continued)

Notes: (Continued)

(d) On 19 May 2005, 180,000,000 ordinary shares of HK$0.10 each were issued at a price of HK$1.48 per ordinary share for a total cash consideration, before related issue expenses, of HK$266,400,000 (equivalent to RMB282,384,000) through an initial public offering by way of placing and public offer.

(e) On 3 May 2006, 78,000,000 ordinary shares of HK$0.10 each were issued at a price of HK$2.175 per ordinary share for a total cash consideration, before related issue expenses, of HK$169,650,000 (equivalent to RMB175,265,000) by way of private placing.

21. OTHER RESERVES

The movements in the reserves of the Group are set out in the condensed consolidated statement of changes in equity of the condensed consolidated financial statements.

Contributed surplus

The contributed surplus of the Group represents the difference between the aggregate of the nominal value of the paid-up capital of Infonics acquired pursuant to the Group Reorganisation on 29 April 2005 over the nominal value of the Company's shares issued in exchange therefor.

Share premium

On 19 May 2005, 180,000,000 ordinary shares of HK$0.10 each were issued at a price of HK$1.48 per ordinary share for a total cash consideration, before related issue expenses of RMB30,567,000, of HK$266,400,000 (equivalent to RMB282,384,000).

On 3 May 2006, 78,000,000 ordinary shares of HK$0.10 each were issued at HK$2.175 per ordinary share for a total cash consideration, before related issue expenses of RMB5,576,000, of HK$169,650,000 (equivalent to RMB175,265,000).

Under the Companies Law (2001 Second Revision) of the Cayman Islands, the share premium and contributed surplus are distributable to the shareholders of the Company, provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to pay off its debts as and when they fall due in the ordinary course of business.

Notes to Condensed Consolidated Interim Financial Statements

21. OTHER RESERVES (Continued)

Capital reserve

The capital reserve is non-distributable. It represents the additional contribution by the shareholder in 2003 amounting to RMB37,147,000, the capitalisation of payable to the shareholder amounting to RMB85,000,000 in which Mr. Dong waived his rights and benefit in respect of the debts owing to him by Yongtong Special Steel in 2004 and the reversal of unclaimed trade payables outstanding more than three years amounting to RMB2,589,000 in 2006.

Share option reserve

The Company has a share option scheme under which options to subscribe for the Company's shares have been granted to certain directors and senior employees as set out in note 22.

Statutory surplus reserve and statutory reserve fund

In accordance with the Company Law of the PRC and the Articles of Association of Yongtong Special Steel and Yongtong Scrap Steel, Yongtong Special Steel and Yongtong Scrap Steel are each required to allocate 10% of their profit after tax, as determined in accordance with PRC GAAP, to the statutory surplus reserve (the "SSR") until such reserve reaches 50% of the registered capital of Yongtong Special Steel and Yongtong Scrap Steel.

Subsequent to the re-registration of Yongtong Special Steel as a wholly-foreign-owned company on 10 November 2003, allocation to the SSR is no longer required. According to the relevant PRC regulations applicable to wholly-foreign-owned companies, Yongtong Special Steel is required to allocate certain portion (not less than 10%) of its profit after tax in accordance with PRC GAAP to the statutory reserve fund (the "SRF") until such reserve reaches 50% of its registered capital.

The SSR and SRF are non-distributable other than in the event of liquidation and, subject to certain restrictions set out in the relevant PRC regulations, can be used to offset accumulated losses or can be capitalised as paid-up capital.

Notes to Condensed Consolidated Interim Financial Statements

21. OTHER RESERVES (Continued)

Statutory public welfare fund

According to the Company Law of the PRC and the Articles of Association of Yongtong Special Steel and Yongtong Scrap Steel, Yongtong Special Steel and Yongtong Scrap Steel are each required to transfer 5% to 10% of their profit after tax to, as determined in accordance with PRC GAAP, to the statutory public welfare fund (the "PWF") which is a non-distributable reserve other than in the event of liquidation of Yongtong Special Steel and Yongtong Scrap Steel. The fund must be used for capital expenditure on staff welfare facilities. Although such facilities are for staff use, they are owned by Yongtong Special Steel and Yongtong Scrap Steel.

Subsequent to the re-registration of Yongtong Special Steel as a wholly foreign-owned company on 10 November 2003, Yongtong Special Steel is no longer required to provide for the PWF.

22. SHARE OPTION SCHEME

On 2 May 2005, the Company approved a share option scheme (the "Share Option Scheme") under which the directors may, at their discretion, grant options to the directors and employees of the Company to subscribe for shares in the Company. At the Company's directors' meeting held on 30 July 2005, the Company granted certain employees under the Share Option Scheme a total of 25,000,000 share options to subscribe for the Company's shares of HK$0.1 each, at an exercise price of HK$1.07 per share, which was determined with reference to the average closing price of the Company's shares as quoted on the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant. Share options do not confer rights on the holders to dividends or vote at shareholders' meetings.

The exercise period of the option will be from the date of acceptance of the option (i.e. 16 August 2005) up to 30 July 2015, both dates inclusive, which is in compliance with the terms of the Share Option Scheme, subject to the following conditions.

The option will have a vesting schedule of 5 years whereby only 20% of the option shall be exercisable 12 months after 30 July 2005 and an additional 20% may be exercised by the grantee in each subsequent year until 30 July 2010 when 100% of the option may be exercised.

Notes to Condensed Consolidated Interim Financial Statements

22. SHARE OPTION SCHEME (Continued)

The fair value of the equity-settled share options granted was estimated as at the date of grant using a binomial model, taking into accounts the terms and conditions upon which the options were granted. The fair value of the share options granted was RMB7,700,000.

As at 30 June 2006, the Company had 22,450,000 share options outstanding under the Share Option Scheme, which represented approximately 3.9% of the Company's shares in issue as at 30 June 2006. The exercise in full of the remaining share options would, under the present capital structure of the Company, result in the issue of 22,450,000 additional ordinary shares of the Company and an additional share capital of HK$2,245,000 and share premium of HK$21,777,000 before share issue expenses.

23. FINANCIAL INSTRUMENTS

The Group's principal financial instruments, other than derivatives, comprise bank loans, other interest-bearing loans, and cash and short term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations.

It is, and has been throughout the six months under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main financial risks faced by the Group are cash flow interest rate risk, raw materials' price risk and credit risk. The Group does not hold or issue derivative financial instruments either for hedging or for trading purposes.

Interest rate risk

The Group's exposure to interest rate risk relates primarily to its interest-bearing loans and borrowings.

The Group does not hedge interest rate fluctuations.

In the opinion of the directors, the Group has no significant interest rate risk due to the short maturity of the Group's interest-bearing loans and other borrowings.

Notes to Condensed Consolidated Interim Financial Statements

23. FINANCIAL INSTRUMENTS (Continued)

Raw materials' price risk

Raw materials accounted for approximately 56% of the total cost of sales for the six months ended 30 June 2006 (2005: 62%). The Group's operation is exposed mainly to the volatility of the price of raw materials, which mainly included iron ore, scrap steel and coke. The price of these raw materials may be influenced by numerous factors and events which are beyond the Group's control. These factors and events include world demand and supply, forward selling activities and other macro-economic factors such as expectations regarding inflation, interest rates, currency exchange rates as well as general global economic conditions. These factors and events may have an adverse effect on the Group's operational activities.

The Group is not involved in any hedging transactions or any alternative measures to manage the potential raw materials' price risk.

Credit risk

Credit risk arising from the inability of a counterparty to meet the terms of a financial instrument contract of the Group is generally limited to the amounts, if any, by which the counterparty's obligations exceed the obligations of the Group. The Group minimises its exposure to credit risk by only dealing with counterparties with acceptable credit ratings.

Concentration of credit risk exists when changes in economic, industrial or geographic factors similarly affect groups of counterparties whose aggregate credit exposure is significant in relation to the Group's total credit exposure. The Group has significant sales transactions with manufacturers of automobiles and hence has a significant concentration of credit risk in this regard. The Group's sales to its top five customers accounted for approximately 64% (2005: 43%) of its total sales for the six months ended 30 June 2006. Failure to secure continued demand from these principal customers would adversely affect the Group's financial position.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral.

Foreign currency risk

The Group's exposure to foreign currency risk relates primarily to the Group's operations in Mainland China.

Notes to Condensed Consolidated Interim Financial Statements

23. FINANCIAL INSTRUMENTS (Continued)

Foreign currency risk (Continued)

The Group has foreign currency risk as certain of its payables to suppliers and interest-bearing loans are denominated in foreign currencies, principally United States dollars. Fluctuations in the exchange rates of RMB against foreign currencies could affect the Group's results of operations.

The Group does not enter into any hedging transactions to manage the potential fluctuation in foreign currency exchange rate as the directors consider that the Group's exposure to foreign currency risk is not significant.

Fair values

The fair values of the Group's financial instruments are not materially different from their carrying amounts. Fair value estimates are made at a specific point in time and are based on the relevant market information and information about the financial instruments. These estimates are subjective in nature, involve uncertainties and matters of significant judgement and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

24. RELATED PARTY TRANSACTIONS

In addition to the transactions and balances detailed elsewhere in these financial statements, the Group had the following material transactions with a related party:

		For the six months ended 30 June	
		2006 (Unaudited) RMB'000	2005 (Audited) RMB'000
Name of related party	**Nature of transactions**		
East Grow Management Limited ("East Grow") (note 1)	Purchases of materials from the related party (note 2)	**11,241**	—

Notes to Condensed Consolidated Interim Financial Statements

24. RELATED PARTY TRANSACTIONS (Continued)

Notes:

(1) East Grow is a company controlled by Mr. Dong, an executive director and a substantial shareholder of the Company.

(2) According to the master agreement entered into between East Grow and the Company (the "Master Agreement") on 13 December 2005 in connection with the sourcing of iron ore, East Grow agreed to supply iron ore to the Group from 1 January 2006 to 31 December 2008. According to the Master Agreement, the prices for these continuing connected transactions are set on the basis of 90% of the market price, at the maximum, and these transactions will be entered into in the usual and ordinary course of business of the Group. The annual cap for these transactions for years ending 31 December 2006, 2007 and 2008 will not exceed HK$318 million, HK$438 million and HK$588 million, respectively.

In the opinion of the directors, all the transactions above were conducted in the ordinary and usual course of the Group's business.

25. COMMITMENTS

Capital commitments

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Capital commitments in respect of property, plant and equipment:		
Authorised, but not contracted for	**—**	—
Contracted, but not provided for	**13,993**	24,155
	13,993	24,155

Notes to Condensed Consolidated Interim Financial Statements

25. COMMITMENTS (Continued)

Operating lease commitments

At the balance sheet date, the Group had future minimum lease payments under non-cancellable operating leases in respect of equipment and land and buildings falling due as follows:

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Within one year	**155**	576
In the second to fifth years, inclusive	**—**	—
	155	576

26. CONTINGENT LIABILITIES

As at 30 June 2006, the Group had the following contingent liabilities:

	30 June 2006 (Unaudited) RMB'000	31 December 2005 (Audited) RMB'000
Bills discounted with recourse	**119,802**	73,897
Bills endorsed with recourse	**186,725**	74,043
	306,527	147,940

Notes to Condensed Consolidated Interim Financial Statements

27. SUBSEQUENT EVENTS

The Company, through its indirect wholly-owned subsidiary, Yongtong Special Steel, entered into Capital Injection Agreement on 11 June 2006 with Anyang Steel Group Company Limited (the "ASG"), Luoyang State-owned Asset Committee and Anyang Steel Group Luoyang Anlong Steel Company Limited (the "Anlong Steel") pursuant to which (i) Yongtong Special Steel conditionally agreed to inject an aggregate amount of RMB171,730,000 (equivalent to approximately HK$166,728,000) by way of contribution to the registered capital of Anlong Steel and (ii) Luoyang State-owned Asset Committee conditionally agreed to make additional capital contribution of RMB75,000,000 in the form of the Luoyang Land to increase the registered capital of Anlong Steel from RMB90,000,000 to RMB336,730,000. Upon completion of the Capital Injection, each of Yongtong Special Steel, Luoyang State-owned Asset Committee and ASG will be interested in approximately 51%, 30.29% and 18.71% of the enlarged registered capital of Anlong Steel respectively. Out of the RMB171,730,000 capital to be contributed by Yongtong Special Steel to Anlong Steel, approximately RMB46,563,000 shall be deemed to have been injected by Yongtong Special Steel by way of set-off against the prepayments. The remaining sum of approximately RMB125,167,000 shall be paid in cash in four installments within 2 years after the date of the new business licence of Anlong Steel pursuant to the capital injection and will be financed by internal resources and bank borrowings of the Group. Upon Completion, the name of Anlong Steel will be changed to "Luoyang Yongan Special Steel Company Limited".

The shareholders approved the Capital Injection Agreement at the Extraordinary General Meeting held on 18 September 2006.

Pursuant to the directors' resolution of the Company dated 18 September 2006, the Board declared an interim dividend of HK$0.02 per share.

23. APPROVAL OF THE INTERIM FINANCIAL STATEMENTS

The interim financial statements were approved and authorised for issue by the Board on 18 September 2006.