

Notes to Financial Statements

(Prepared under PRC Accounting Standards)

31 December 2006

I. CORPORATE AFFILIATION

Maanshan Iron & Steel Company Limited (the “Company”), a joint stock limited liability company incorporated after the reorganisation of a state-owned enterprise known as Maanshan Iron and Steel Company (the “Original Magang”, now named as Magang (Group) Holding Company Limited (“Holding”)), was incorporated in Maanshan City, Anhui Province, the People’s Republic of China (the “PRC”) on 1 September 1993. The registration number of the Company’s business licence is Qi Gu Wan Zong Zi No. 000970. The Company’s A shares and H shares were issued and listed in Shanghai Stock Exchange and Hong Kong Stock Exchange respectively. The Company together with its subsidiaries (the “Group”) are principally engaged in the manufacture and sale of iron and steel products and related by-products.

II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED OF FINANCIAL STATEMENTS

The principal accounting policies, accounting estimates and the preparation of consolidated financial statements, based upon which the financial statements are prepared, were selected in accordance with Accounting Standards for Business Enterprises and “Accounting System for Business Enterprises” and other related standards, regulations and rules as issued by the Ministry of Finance of the PRC.

1. Accounting system

The Group has implemented Accounting Standards for Business Enterprises and “Accounting System for Business Enterprises”.

2. Financial year

The financial year of the Group is from 1 January to 31 December of each calendar year.

3. Reporting currency

Except for overseas subsidiaries which use their respective local currencies for recording purposes, Renminbi (“RMB”) is used as the Group’s reporting currency.

4. Basis of accounting and measurement basis

The Group’s accounts have been prepared on an accrual basis. Assets are valued at actual cost when they are acquired. Subsequently, following regular inspection, the Group provides impairment provisions in accordance with “Accounting System for Business Enterprises”.

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5. Foreign currency transaction

Foreign currency transactions are translated into the reporting currency at the exchange rates quoted by the People's Bank of China prevailing on the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Renminbi at the applicable rates of exchange ruling at the balance sheet date as quoted by the People's Bank of China. The consequential exchange gains or losses are dealt with in the current period's income statement. Foreign currency translation differences relating to funds borrowed to finance the acquisition or construction of fixed assets are accounted for according to the requirements relating to the capitalisation of borrowing costs.

6. Foreign currency translation

All assets and liabilities are translated to Renminbi at the exchange rates prevailing at the balance sheet date; shareholders' equity, with the exception of retained profits, are translated at the exchanged rates prevailing at the transaction date; retained profits are recorded based on the amount stated on the statement of income and profit appropriation after translation adjustments; exchange differences arising from the difference between total translated assets and the sum of total translated liabilities and translated shareholders' equity are dealt with in the exchange fluctuation reserve as a separate allocation of retained profits. All statement of income and profit appropriation items are translated at the average exchange rates during the year. All cash flow statement items are translated at the average exchange rates during the year. All opening balances and last year actual amounts are stated at last year translated amounts.

7. Cash equivalents

Cash equivalents represent short term highly liquid investments which are readily convertible into known amounts of cash, subject to an insignificant risk of changes in value and which are within three months of maturity when acquired.

8. Short term investments

The Group's short term investments refer to those investments that can be realised at any time and that are intended to be held for less than one year. They include stocks, bonds and funds. Short term investments are recorded at the initial price paid on acquisition less cash dividends that are declared but not received, and interest on bonds due but not received.

Cash dividends and interest on short term investments declared by investee company during the holding period are net off against the book value of the investment when received, except for those recorded as receivables when acquired. Upon disposal of short term investments, the difference between the book value of the short term investments and the proceeds on disposal are recorded as a gain or loss on disposal of investments for the current period. The cost of the investments is determined using the weighted average method.

Short term investments, using the individual comparison method, are stated at the lower of cost and market value at the end of the period. Provision for decline in value of short term investments is made for any reduction of cost to market value, and charged to the income statement in the period in which they arise.

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

9. Bad debts provision

Recognition criteria for bad debts:

- (i) the irrecoverable amount of a bankrupt or deceased debtor who has insufficient assets or estate to repay the debt;
- (ii) the irrecoverable amount, supported by evident characteristics, of a debtor who is unable to comply with the repayment obligation after the debt fell due.

Bad debts provision is made using the provision method and is offset against the corresponding trade and other receivables when those bad debts are approved by directors.

The Group adopted the provision method under which specific and general provisions were made to account for bad debt losses on trade and other receivables. A specific provision refers to an amount that is provided based on management's assessment of the recoverability of an individual receivable. A general provision is set up on the remaining balances of trade and other receivables based on the ageing analysis. Full provision is made for those trade and other receivables that have been specifically identified as irrecoverable, while general provision is made for the remaining balance after taking into account the ageing analysis. The general provision was determined in accordance with the financial and cash flow status of the debtor, using the percentages below:

Ageing	Bad debts general provision percentage (Net of post balance sheet date settlement)	
	Trade receivables	Other receivables
1 to 6 months	–	–
7 to 12 months	10%	–
13 to 24 months	25%	40%
25 to 36 months	50%	60%
over 36 months	100%	100%

10. Inventories

Inventories include raw materials, work in progress, construction contract, finished goods and spare parts. Inventories are finished goods or merchandise held by an enterprise for sale in the ordinary course of business, or work in progress in the process of production for such sale, or in the form of materials or supplies to be consumed in the production process or in the rendering of services. Inventories are stated at actual cost of acquisition. Raw materials are stated at cost of purchase. Cost of work in progress and finished goods comprise direct materials, direct labor and an appropriate proportion of production overheads. Cost of spare parts are charged to the income statement when issued for production as production cost for the period and hence included in the cost of finished goods sold. Inventories, other than spare parts, are determined on weighted average basis. Inventories are accounted for using perpetual inventory system.

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. Inventories (continued)

Contract costs incurred comprise direct materials, direct labour, utilization expenses of equipment, other direct costs and an appropriate proportion of variable construction overheads. Contract costs records the portion that the aggregate amount of costs incurred and aggregate recognised gross profits (or recognised loss) to date exceeds the amount of progress billings and the balance is represented as unsettled projects on financial statement. Provision of impairment for construction contract is assessed at year end. When it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as current expenses immediately.

Provision is made for those inventories which cannot be recovered due to them being damaged, wholly or partly obsolete, or having their selling prices lower than cost. Provision is determined as the excess of carrying value of the inventories over its net realisable value on an individual basis. Net realisable value is the estimated selling prices in the ordinary course of business less any estimated costs of completion and estimated selling expenses.

11. Long term investments

Long term investments include long term equity investments and long term debt investments.

Long term equity investments are recorded at initial cost on acquisition. The equity method is then applied when the Company holds 20% or more of the voting capital, or less than 20% but with significant influence, while cost method is then applied for all other equity investments when the Company holds less than 20% of the voting capital, or has 20% or above but without significant influence.

When the equity method is adopted, the amount of initial cost of the investment in excess of the investor's share of the owner's equity in the investee company is regarded as an equity investment difference and amortised according to the investment period specified in the contract. If the investment period is not specified in the contract, the difference is amortised over a period of not more than 10 years (including 10 years). The amount of initial cost of the investment fall short of the investor's share of the owner's equity in the investee company is credited to the capital reserve.

When the equity method is adopted, the Group should, after the acquisition of the equity investment, adjust the carrying amount of the investment according to its attributable share of the investee enterprise's net profit or loss and recognised as investment income or loss for the current period accordingly. It recognises net losses incurred by the investee enterprise to the extent that the carrying amount of the investment is reduced to zero.

When the cost method is adopted, profits or cash dividends declared to be distributed by the investee enterprise should be recognised as investment income in the current period after the investment acquired by the Group. The excess should be treated as a recovery of investment cost.

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

11. Long term investments (continued)

Long term debt investments are recorded at the initial cost on acquisition. Interest income is computed based on the par value and par interest rate over the period. The premium and discount on long term debt investments is amortised over the period in which the investment is held and the relevant bond interest is recognised.

If the recoverable amount of any investment is lower than the carrying amount of that investment as a result of a continuing decline in market value or changes in operating conditions of the investee company, the difference between the recoverable amount and the carrying amount of the investment should be recognised as an impairment of a long term investment and an investment loss in the current period.

12. Fixed assets

Fixed assets represent tangible assets held for the purposes of production of products, provision of services, leasing or operational use. They are of relatively high value and have useful lives exceeding 1 year.

Fixed assets are recorded at cost of acquisition. The cost of fixed assets which is purchased separately comprise its purchase price, value added tax, import duties and other related taxes, and any directly attributable expenditures for bringing the asset to its working condition for its intended use, such as transportation and installation costs. Interest and exchange differences arising from specific borrowings that are incurred in bringing the fixed asset to its working condition are capitalised. If the future economic benefits brought about by the incurrence of subsequent overhaul and technical improvement costs are greater than those originally estimated, then such costs will be capitalised as fixed assets. In the prior years, furnace relining costs were accrued, using the straight line method, over the period between relinings. Under the PRC Accounting Standards issued in 2002, repair and maintenance costs incurred on fixed assets should be charged to the income statement as and when incurred. Hence, from 1 January 2002 onwards, the Company no longer accrued for the provision for furnace relining costs on a straight-line basis. As prescribed by the standard, a prior year adjustment has not been made for the balance of provision for furnace relining costs as at 31 December 2001 as the balance will be net off against future furnace relining costs to be actually incurred. Expenditure on repair and maintenance of fixed assets are charged to the income statement as and when incurred. Gains or losses arising from the disposal, damage, obsolescence or physical counting of fixed assets are accounted for as non-operating expenses or income in the current period.

Depreciation is provided on fixed assets using the straight-line method. The depreciation rates are determined based on the cost, the estimated useful lives and estimated residual value (3% of original cost) of each category of fixed assets as follows:

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

12. Fixed assets (continued)

Category	Estimated useful life	Annual depreciation rate
Buildings and structures	10 to 20 years	4.9%-9.7%
Plant, machinery and equipment	10 years	9.7%
Transportation vehicles and equipment	5 years	19.4%

The useful life of land use rights included in buildings and structures exceeded the estimated useful life of buildings. The corresponding amount is treated as residual value.

Fixed assets are depreciated on a monthly basis from the month following that in which the assets are used in operation. For fixed assets that are no longer used in operation, depreciation ceases from the month following that in which the assets cease to be used.

At the end of the accounting period, fixed assets are carried at the lower of book value and recoverable amount. A provision for impairment of fixed assets is made for any difference between the book value and the lower recoverable amount and charged to the current period's income statement. The recoverable amount of the fixed assets is the greater of the net selling price and the value in use. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

13. Construction materials

Construction materials include preparation materials for construction projects, equipment that needs to be installed and prepayment for large-scale equipment. Construction materials are recorded at actual cost.

14. Construction in progress

Construction in progress includes all costs incurred during the preparation period before commencement of construction and until the asset is ready for its intended use. These costs include direct materials, direct labour, equipment for installation, construction and installation charges, management fees, gain or loss on trial run production and borrowing costs which are qualified for capitalisation. Construction in progress is transferred to fixed assets when the asset is ready for its intended use.

The impairment provisions are made against those projects which have been suspended for a long period of time and the construction of which is not expected to resume within three years, and which have been considered obsolete in terms of its technology and functionality and where there exists significant uncertainty as to whether it will bring future economic benefits to the Company, and hence causing their recoverable amounts to be lower than their carrying values. The difference between the recoverable amount and the carrying value of the construction in progress is recognised as an impairment provision and charged to the current period's income statement.

Notes to Financial Statements (Continued)

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

15. Borrowing costs

Borrowing costs include interest, amortisation of discounts or premiums, ancillary expenses and exchange differences arising from foreign currency borrowings of the Group. The specific borrowings are the borrowings especially for the acquisition or construction of a fixed asset, and the costs of which are capitalised and recorded in the fixed asset's cost when:

- (i) expenditures for the assets are incurred;
- (ii) borrowing costs are incurred;
- (iii) the acquisition and construction activities that are necessary to bring the assets to their expected usable conditions have commenced.

The capitalisation of borrowing costs is suspended during the period in which the acquisition or construction of a fixed asset is abnormally interrupted, and the interruption period is more than 3 months. Borrowing costs during the period are then treated as an expense of the current period until the acquisition or construction is resumed.

The capitalisation of borrowing costs ceases when the fixed asset being acquired or constructed is substantially ready for its intended use and borrowing costs incurred thereafter are recorded as financial expenses in the period in which they are incurred.

The capitalised borrowing costs for each accounting period are computed based on the accumulated weighted average expenditure incurred for the acquisition or construction of fixed assets up to the end of the period, using the related weighted average interest rate, subject to the actual borrowing costs and amortisation of discounts and premiums thereof. Exchange difference and significant specific ancillary borrowing expenses of foreign specific borrowing will be capitalised at its actual cost.

Expenses incurred in other borrowings should be recognised as financial expenses in the period in which they are incurred.

16. Intangible assets

The Group's intangible assets represent land use rights and iron ore mining rights, which are stated at cost less accumulated amortisation. Amortisation is calculated on a straight-line basis to write off the cost over the estimated useful life.

Category	Estimated useful life
Land use rights	50 years
Iron ore mining rights	25 years

At the end of the accounting period, intangible assets are carried at the lower of book value and recoverable amounts. If the recoverable amount is lower than the book value, a provision for impairment on intangible assets is made for the difference, and charged to the income statement in the current period.

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

17. Bonds payable

The bonds issued are recorded under the par value. Any premium or discount arising from the difference between issue price and par value is amortised in the same time when such interest is accrued over the duration of bonds according to effective interest rate method.

18. Specific payables

Government subsidies for specific construction projects are recognised as specific payables on actual receipt of the subsidies. Upon completion of the subsidised construction projects, the costs incurred are recognised as fixed assets and the utilised portion of specific payables thereof are transferred to the capital reserve.

19. Revenue recognition

Revenue from the sale of goods is recognised when the significant risks and rewards in relation to ownership of the goods have been transferred to the buyer, the Group retains neither continuing management nor effective control over the goods sold; and when it is probable that the economic benefits associated with the transaction will flow to the Group; and the relevant amounts of revenue and costs can be measured reliably.

If an afforded service commences and accomplishes in the same financial year, related revenue is recognised when the service accomplishes; if an afforded service accomplishes in the financial year other than that of the service commences, when the outcome of the afforded service can be estimated reliably, the related revenue is recognised by reference to the percentage of completion method at the balance sheet date; otherwise, the related revenue is recognized only to the extent of recoverable service costs incurred.

When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract should be recognised as revenue and expenses respectively by reference to the percentage of completion method at the balance sheet date. When the outcome of a construction contract cannot be estimated reliably, contract revenue should be recognised only to the extent of recoverable contract costs incurred.

Revenue from the sale of goods is determined according to the invoiced value of goods sold, and excludes value added tax ("VAT"). Sales returns and allowances are recorded as a reduction of revenue in the period in which the returns and allowances occur. Cash discounts are recognised as expenses in the period in which they are incurred.

Interest income is recognised using the matching principle and after taking into account the principal outstanding and the effective interest rate applicable.

20. Income tax

The Company uses tax payable method to account for income tax.

Notes to Financial Statements (Continued)

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II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND BASIS OF CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

21. Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control or jointly control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control. Related parties may be individuals or corporate entities.

22. Preparation of consolidated financial statements

The Group's consolidated financial statements are prepared according to the rules of directive No. 1995(11) issued by the Ministry of Finance. The consolidated financial statements include companies in which the Group has over 50% of the equity voting rights, or companies in which the Group has less than 50% of the equity voting rights, but is able to control its financial and operating policies.

The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. All inter-group transactions and balances are eliminated on consolidation, including the unrealised profits and losses incurred.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

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III. TAX

The principal kinds of taxes and the related rates are as follows:

1. VAT

According to national tax regulation, the Company adopted the "Exempt, Offset, Refund" arrangements for VAT in export sales. Before September 2006, the refunds rate was 11%-13%, but was adjusted to 8% since then. The output VAT rate of the domestic sale is 17%. VAT payable is the net difference between output VAT and deductible input VAT.

A subsidiary of the Company adopted the "Levy first, refund afterwards" arrangements for VAT in its own export sales.

2. Business tax

Payable based on 3%-5% of the service income.

3. City construction and maintenance tax

Payable based on 7% of the net VAT and business tax to be paid.

4. Education surcharge

Payable based on 3% of the net VAT and business tax to be paid.

5. Local education surcharge

Payable based on 1% of the net VAT and business tax to be paid.

6. Flood prevention fund

Payable based on 0.06% of last year's sales or operating income.

7. Real estate tax

Payable based on certain percentage of the cost of real estate with legal title in accordance with relevant regulations.

8. Corporate income tax

The corporate income tax of the Company and its subsidiaries is calculated at 15% to 33%, on their estimated assessable profits for the year based on existing legislation, interpretations and practice in respect thereof. Certain subsidiaries of the Company are foreign investment enterprises and their corporate income taxes have been provided at the rate of 15% to 30% and are entitled to enjoy "Two years exempted and subsequent three years with 50% reduction" tax holidays. Profits tax of overseas and Hong Kong subsidiaries have been provided at the rate of 17.5%-30% on their estimated assessable profits which were earned in or derived from overseas and Hong Kong during the year.

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES

The consolidated financial statements include the subsidiaries below, which was same with prior year excluding those listed in Notes i and ii:

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Subsidiaries							
Ma Steel International Trade and Economic Corporation ("Ma Steel International Trade Corp.")	Anhui, PRC	Import of machinery and raw materials and export of steel products	RMB50,000,000	RMB50,000,000	50,000,000	100	—
Design & Research Institute of Maanshan Iron & Steel Company Limited ("Design & Research Institute")	Anhui, PRC	Planning and design of metallurgical, construction and environmental protection projects, construction supervision and contract service	RMB50,000,000	RMB50,000,000	7,500,000	58.96	7.86
MG Control Technique Company Limited ("MG Control Technique")	Anhui, PRC	Design of automation systems; purchase, installation and repairs of automation, computers and communication systems	RMB8,000,000	RMB8,000,000	7,500,000	93.75	4.18

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Subsidiaries (continued)							
Anhui Masteel K. Wah New Building Materials Co., Ltd. ("Anhui Masteel K. Wah")	Anhui, PRC	Production, sale and transportation of slag products and provision of related consultation services	US\$4,290,000	US\$4,290,000	24,854,930	70	–
Ma Steel (Wuhu) Processing and Distribution Co., Ltd. ("Ma Steel (Wuhu)")	Anhui, PRC	Processing and sale of metallic products; processing of motor vehicle spare parts and sale of construction materials and chemical products (except dangerous products)	RMB35,000,000	RMB35,000,000	8,225,885	70	30
Ma Steel (Cihu) Processing and Distribution Co., Ltd. ("Ma Steel (Cihu)")	Anhui, PRC	Production, processing and sale of steel plates, steel wires and steel sections; provision of storage and after-sales services	RMB30,000,000	RMB30,000,000	–	–	92

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Subsidiaries (continued)							
Ma Steel (Guangzhou) Processing and Distribution Co., Ltd. ("Ma Steel (Guangzhou)")	Guangdong, PRC	Production, processing and sale of steel plates, steel wires and steel sections and provision of storage, transportation and after-sales services	RMB120,000,000	RMB120,000,000	80,000,000	66.67	—
Maanshan Iron & Steel (HK) Limited ("Ma Steel (HK)")	Hong Kong, PRC	Trading of steel and iron ores, and provision of steel trading agency services and transportation services	HK\$4,800,000	HK\$4,800,000	4,101,688	80	20
Anhui Masteel Holly Industrial Co. ("Holly Industrial")	Anhui, PRC	Production and sale of packing materials for steel and other products; provision of on-site packing service; research & development, production and sale of vehicle spare parts, electronic engineering products, macromolecular compound materials; processing and sale of metallic products	RMB30,000,000	RMB30,000,000	21,478,316	71	—

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IV. SUBSIDIARIES, JOINT CONTROL ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Subsidiaries (continued)							
Maanshan Masteel Huayang Equipment Inspection & Engineering Co., Ltd ("Huayang Equipment")	Anhui, PRC	Provision of equipment inspection technique consultancy services, equipment services and equipment inspection work	RMB1,000,000	RMB1,000,000	900,000	90	—
Ma Steel (Jinhua) Processing and Distribution Co., Ltd. ("Ma Steel (Jinhua)")	Zhejiang, PRC	Production, processing and sale of steel plates, steel wires and steel sections and provision of storage, transportation and after-sales services	RMB120,000,000	RMB120,000,000	90,000,000	75	—
MG Trading and Development GmbH ("MG Trading")	Germany	Trading of equipment, iron and steel products and provision of technology services	EUR153,388	EUR153,388	1,573,766	100	—
Maanshan Iron & Steel (Australia) Proprietary Limited ("Ma Steel (Australia))	Australia	Production and sales of iron ore through an unincorporated joint venture	AUD21,737,900	AUD21,737,900	126,312,415	100	—

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IV. SUBSIDIARIES, JOINT CONTROL ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Subsidiaries (continued)							
Ma Steel (Hefei) Iron & Steel Co., Ltd. ("Ma Steel (Hefei)") (note i)	Anhui, PRC	Smelting and processing of ferrous metals and sale of the products and by-products; production and sale of coke, coke chemical products and power; processing of iron and steel products and production and sale of metallic products; iron and steel technological services and related businesses; dock operation, storage, transportation, construction services.	RMB500,000,000	RMB334,495,000	237,495,000	71	—
Ma Steel (Hefei) Processing and Distribution Co., Ltd. ("MS (Hefei) Processing") (note i)	Anhui, PRC	Processing and sale of hot rolled and cold rolled steel thin plate for vehicles, home appliances and engineering industries, construction steel framework products; provision of storage and transportation services	RMB120,000,000	RMB91,000,000	73,200,000	61	28
Ma Steel (Yangzhou) Processing and Distribution Co., Ltd. ("MS (Yangzhou) Processing") (note ii)	Jiangsu, PRC	Production, processing and sale of steel plates, steel wires and steel sections; provision of after-sales and storage services (except of dangerous products)	USD20,000,000	USD10,000,000	61,651,010	71	—

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Associates							
濟源市金馬焦化有限公司 ("濟源市金馬焦化")	Henan, PRC	Production and sale of coke, tar, benzene and coal gas	RMB200,000,000	RMB200,000,000	80,000,000	40	—
滕州盛隆煤焦化有限公司 ("滕州盛隆煤焦化")	Shandong, PRC	Production and sale of coke, tar, coal gas and coke chemical products; provision of logistics services	RMB208,800,000	RMB208,800,000	66,776,000	32	—
上海大宗鋼鐵電子交易中心有限公司 ("上海鋼鐵電子")	Shanghai, PRC	Set-up of iron & steel e-commerce and related services; provision of iron & steel e-commerce technology and information services	RMB20,000,000	RMB20,000,000	4,000,000	20	—
馬鞍山港口(集團)有限責任公司 ("馬鞍山港口公司")	Anhui, PRC	Loading/unloading, cargo forwarding agency service, storage, transmitting of cargo and division or merge of cargo in containers; provision of general services to ships, repairing and manufacturing of spare parts	RMB250,000,000	RMB250,000,000	112,500,000	45	—

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Associates (continued)							
安徽奧馬特汽車變速系統有限公司 ("奧馬特變速系統") (note i)	Anhui, PRC	Development, production, and sales of vehicle automatic transmission product and related spare parts; provision of related design technique, equipment production and transportation services	RMB50,000,000	RMB13,471,500	—	—	31.95
安徽馬鋼立體智能停車設備有限公司 ("馬鋼智能停車") (note ii)	Anhui, PRC	Development, production installation, and sales of automatic parking equipments, storage equipments, engineering and related steel frame, decoration materials, electronic spare parts, instruments and meters and provision of related integration and consulting services	USD2,500,000	USD2,500,000	—	—	25

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IV. SUBSIDIARIES, JOINTLY-CONTROLLED ENTITY AND ASSOCIATES (CONTINUED)

Name of investee company	Place of incorporation and registration	Principal activities	Registered capital	Paid-up capital	Investment cost of the Company RMB	Percentage of equity held by the Company	
						directly %	indirectly %
Jointly-controlled entity ("JCE")							
Ma' anshan BOC-Ma Steel Gases Company Limited ("BOC-Ma Steel") (Note iii)	Anhui, PRC	Manufacture and sale of air products (hydrogen, oxygen, argon and other gases) in gas and liquid states and other industrial gases, provision of products related sales and supply work and technical services and other related services	RMB468,000,000	RMB468,000,000	234,000,000	50	—
Total					<u>1,292,069,010</u>		

Note i: Newly incorporated during the year

Note ii: Newly acquired during the year

Note iii: BOC-Ma Steel is jointly controlled by BOC (China) Investment Company Limited and the Company, and hence proportionate consolidation should be applied. Since BOC-Ma Steel is still at pre-operating stage and has not commenced its commercial production as at 31 December 2006, no income statement has been reported. Its net assets did not exceed 2% of the Group's net assets. Having considered materiality, equity method of accounting is adopted by the Company to account for BOC-Ma Steel. This treatment complies with the new Accounting Standards for Business Enterprises which became effective on 1 January 2007.

The names of certain PRC subsidiaries in English are direct translations of their registered names in Chinese.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS

1. Cash and balances with financial institutions

	31 December 2006			31 December 2005		
	Original currency	Exchange rate	RMB	Original currency	Exchange rate	RMB
Cash on hand	RMB200,631	1.0000	200,631	RMB179,223	1.0000	179,223
Balances with financial institutions (Note 2)	RMB3,306,174,722	1.0000	3,306,174,722	RMB2,387,389,191	1.0000	2,387,389,191
	HK\$305,323	1.0047	306,691	HK\$3,696,567	1.0403	3,859,056
	US\$19,946,528	7.8087	155,789,281	US\$27,105,931	8.0702	218,803,290
	EUR3,209,257	10.2665	32,947,833	EUR50,884,207	9.5797	487,455,441
	JPY1,030,670,853	0.0656	67,642,928	JPY21,825,153	0.0687	1,499,733
	AUD9,702,434	6.1579	59,746,618	AUD1,257,644	5.9219	7,447,641
Other balances with financial institutions	RMB526,197,697 (Note)	1.0000	526,197,697	RMB135,897,049	1.0000	135,897,049
	US\$1,000,184 (Note)	7.8087	7,838,098	US\$1,221,978	8.0702	9,905,749
	EUR363,170	10.2665	3,728,484	EUR269,246	9.5797	2,579,297
	JPY2,007,165	0.0656	131,731	JPY112	0.0687	7
Total			4,160,704,714			3,255,015,677

Note: Included in the balances were US\$1,000,000 and RMB523,300,000 which have been pledged as securities for the provision of banking facilities and issue of bank bills to the Company's subsidiaries. The deposits were not readily available for payment.

2. Balances with financial institutions

The balances with financial institutions included the following overdue Hong Kong dollar fixed deposit principal amounts with three non-bank financial institutions (31 December 2005: four), aggregating approximately HK\$119 million (31 December 2005: approximately HK\$123 million).

	Notes	31 December 2006 HK\$'000	31 December 2005 HK\$'000
China Venturetech Investment Corporation ("China Venturetech")	(i)	–	3,491
Guangdong International Trust & Investment Corporation ("GITIC")	(ii)	23,317	23,317
CITIC Ningbo Inc. ("Ningbo CITIC")	(iii)	48,000	48,000
SEG International Trust & Investment Corporation ("SEG")	(iii)	48,125	48,125
		119,442	122,933

Based on legal advice, the directors are satisfied that the Company's deposits with the above non-bank financial institutions are valid fixed deposits.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

2. Balances with financial institutions (continued)

- (i) China Venturetech was in liquidation since 1998 and the Company has registered its debts with 中國人民銀行關閉中國新技術創業投資公司清算組 (the liquidator of China Venturetech). On 23 January 2006, the liquidator of China Venturetech declared that all the assets have been liquidated. On 14 February 2006, the Company received the last instalment of repayment of RMB3,632,000. As at 31 December 2006, the overdue fixed deposit in China Venturetech had been fully settled.
- (ii) GITIC was declared bankrupt by the Shenzhen Intermediate People's Court of Guangdong Province on 16 January 1999. On 28 February 2003, the People's High Court of Guangdong Province declared an end to the bankruptcy proceeding in relation to the GITIC bankruptcy case but the liquidation process will remain in progress. During the period from year 2000 to 2004, the Company received three repayments amounting to approximately RMB7.1 million in aggregate. During the year, no allocation of assets was made by the liquidator of GITIC.
- (iii) Ningbo CITIC is now in liquidation and the Company has registered its debts with the liquidator. SEG is currently in the process of business suspension and rectification under the supervision of the People's Bank of China. The recovery of the relevant deposit and interest can only be proceeded when the business suspension and rectification has been completed. Up to the approval date of the financial statements, no repayments have been received from Ningbo CITIC and SEG.

As at the date on which these financial statements were approved, the directors are unable to estimate the principal amount of the outstanding deposits the Company will be able to recover. Based on the above factors, the directors maintain the full provision made for the overdue fixed deposits.

3. Short term investments

Item	31 December 2006		31 December 2005	
	Investment cost RMB	Provision for decline in value RMB	Investment cost RMB	Provision for decline in value RMB
Equity investment	—	—	13,568,593	—

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

3. Short term investments (continued)

As at 31 December 2006, all the short term investments held by the Group had been disposed.

The movement of provision for decline in value of short term investments for the year 2006 is disclosed in the supplementary information of the financial statements.

4. Bills receivable

	31 December 2006 RMB	31 December 2005 RMB
Bank bills	<u>681,137,717</u>	<u>1,931,609,265</u>

As at the balance sheet date, the Group does not hold any discounted bills with recourse yet to mature.

The decrease in the Group's bills receivables by 65% was mainly attributable to the increase in endorsement of bank bills to customers for materials purchase in the current year.

The balance of bills receivable does not contain any amount due from a shareholder who holds 5% or above of the Company's equity interest.

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5. Trade receivables

Trade receivables ageing analysis:

	31 December 2006				31 December 2005			
	Balance	Ratio	Provision for bad debts	Ratio	Balance	Ratio	Provision for bad debts	Ratio
Within one year	569,139,754	91	(377,185)	1	270,498,124	81	-	-
One to two years	11,991,603	2	(2,625,603)	22	17,486,861	5	(4,908,558)	28
Two to three years	7,842,899	1	(3,550,504)	45	8,259,890	3	(7,853,396)	95
Over three years	34,385,996	6	(34,385,996)	100	36,536,094	11	(36,536,094)	100
Total	623,360,252	100	(40,939,288)		332,780,969	100	(49,298,048)	

	31 December 2006				31 December 2005			
	Balance	Ratio	Provision for bad debts	Ratio	Balance	Ratio	Provision for bad debts	Ratio
Within one year	529,392,156	91	(307,111)	1	204,374,088	77	-	-
One to two years	9,061,019	2	(2,265,254)	25	15,723,061	6	(3,300,034)	21
Two to three years	6,963,324	1	(3,481,662)	50	8,259,890	3	(7,853,396)	95
Over three years	34,385,996	6	(34,385,996)	100	36,536,094	14	(36,536,094)	100
Total	579,802,495	100	(40,440,023)		264,893,133	100	(47,689,524)	

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

5. Trade receivables (continued)

An analysis of the amount of bad debts provision written off in the current year:

Reason	Group and Company	
	2006 RMB	2005 RMB
Bankrupt or liquidated debtors	307,795	–
Debtors with age greater than 3 years and demonstrated by sufficient evidence that they were irrecoverable	–	357,613
Total	<u>307,795</u>	<u>357,613</u>

The five largest trade receivables of the Group and the Company both amounted to RMB148,859,842, which accounted for 24% and 26% of the gross trade receivables of the Group and the Company respectively.

Except for those as stated in Note VII point 6, the balance of trade receivables does not contain any amount due from a shareholder who holds 5% or above of the Company's equity interest.

The movement of bad debts provision for trade receivables for the year 2006 is disclosed in the supplementary information of the financial statements.

(Prepared under PRC Accounting Standards)
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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

6. Other receivables

Other receivables ageing analysis:

	31 December 2006				31 December 2005			
	Balance	Ratio	Provision for bad debts	Ratio	Balance	Ratio	Provision for bad debts	Ratio
	RMB	%	RMB	%	RMB	%	RMB	%
Within one year	159,246,588	85	-	-	174,855,093	85	-	-
One to two years	676,445	1	(215,947)	32	2,925,579	2	(509,854)	17
Two to three years	2,197,702	1	(1,318,621)	60	2,361,612	1	(2,250,672)	95
Over three years	24,689,111	13	(24,638,179)	100	25,302,728	12	(23,412,221)	93
Total	186,809,846	100	(26,172,747)		205,445,012	100	(26,172,747)	

	31 December 2006				31 December 2005			
	Balance	Ratio	Provision for bad debts	Ratio	Balance	Ratio	Provision for bad debts	Ratio
	RMB	%	RMB	%	RMB	%	RMB	%
Within one year	48,777,104	64	-	-	18,061,977	37	-	-
One to two years	648,433	1	(215,947)	33	2,905,638	6	(509,854)	18
Two to three years	2,197,702	3	(1,318,621)	60	2,361,612	5	(2,250,672)	95
Over three years	24,638,179	32	(24,638,179)	100	25,251,796	52	(23,412,221)	93
Total	76,261,418	100	(26,172,747)		48,581,023	100	(26,172,747)	

The five largest other receivables of the Group and the Company amounted to RMB9,284,396 and RMB7,848,658 respectively, which accounted for 5% and 10% of the gross other receivables of the Group and the Company respectively.

The balance of other receivables does not contain any amount due from a shareholder who holds 5% or above of the Company's equity interest.

The movement of bad debts provision for other receivables for the year 2006 is disclosed in the supplementary information of the financial statements.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

7. Prepayments

Prepayments ageing analysis:

	31 December 2006			31 December 2005		
	Balance RMB	Ratio %	Reason of outstanding	Balance RMB	Ratio %	Reason of outstanding
Within one year	517,690,362	85	N/A	297,726,499	79	N/A
One to two years	11,517,780	2	Note	20,432,951	5	Note
Two to three years	20,000,000	3	Note	59,741,931	16	Note
Over three years	59,508,163	10	Note	–	–	N/A
Total	608,716,305	100		377,901,381	100	

Note: Prepayment aged over one year was mainly attributable to the delay in raw materials supply.

The increase in the Group's prepayment by 61% was mainly attributable to the increase in prepayment for coal purchase.

Except for those as stated in Note VII point 6, the balance of prepayments does not contain any amount due from a shareholder who holds 5% or above of the Company's equity interest.

(Prepared under PRC Accounting Standards)
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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

8. Inventories

	31 December 2006		31 December 2005	
	Balance RMB	Provision RMB	Balance RMB	Provision RMB
Raw materials	3,593,290,386	–	2,973,683,772	–
Work in progress	538,136,776	–	641,585,619	(3,000,000)
Construction contract	51,118,889	–	31,002,486	–
Finished goods	665,523,682	(4,840,000)	407,365,707	(46,838,109)
Spare parts	1,783,832,105	(86,929,889)	1,266,795,977	(71,121,783)
Total	<u>6,631,901,838</u>	<u>(91,769,889)</u>	<u>5,320,433,561</u>	<u>(120,959,892)</u>

Included in the Group's inventories were finished goods amounting to RMB121,914,383 which have been pledged to banks as securities for issue of bank bills for the Company's subsidiaries.

The movement of provision for impairment of inventories for the year 2006 is disclosed in the supplementary information of the financial statements.

9. Long term investments

Items	Group			
	At 1 January 2006 RMB	Increase during the year RMB	Decrease during the year RMB	At 31 December 2006 RMB
Long term equity investments				
Interests in a JCE (ii)	234,000,000	–	–	234,000,000
Interests in associates (iii)	268,059,681	61,454,724	–	329,514,405
Other equity investments (iv)	16,817,035	–	–	16,817,035
	<u>518,876,716</u>	<u>61,454,724</u>	<u>–</u>	<u>580,331,440</u>
Long term debt investment				
Other debt investment (v)	10,918,870	–	(2,660,000)	8,258,870
Total	<u>529,795,586</u>	<u>61,454,724</u>	<u>(2,660,000)</u>	<u>588,590,310</u>

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. Long term investments (continued)

Items	Company			At 31 December 2006 RMB
	At 1 January 2006 RMB	Increase during the year RMB	Decrease during the year RMB	
Long term equity investments				
Interests in subsidiaries (i)	654,682,848	597,167,738	(69,367,583)	1,182,483,003
Interests in a JCE (ii)	234,000,000	–	–	234,000,000
Interests in associates (iii)	268,059,681	47,954,724	–	316,014,405
Other equity investments (iv)	16,817,035	–	–	16,817,035
	<u>1,173,559,564</u>	<u>645,122,462</u>	<u>(69,367,583)</u>	<u>1,749,314,443</u>
Long term debt investment				
Other debt investment (v)	10,918,870	–	(2,660,000)	8,258,870
Total	<u>1,184,478,434</u>	<u>645,122,462</u>	<u>(72,027,583)</u>	<u>1,757,573,313</u>

The total of long term investments of the Group amounted to RMB588,590,310, which represented 3% of the Group's net assets.

According to the directors' opinion, there is no material restriction on realisation of investments as at the balance sheet date.

The increase in the Company's long term investments by 48% was mainly attributable to the increase in investments in subsidiaries and associates.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. Long term investments (continued)

(i) Interests in subsidiaries

Name of investee company	Investment period	Percentage of equity held		Investment cost				Adjustment for gain or loss				
		by the Company	Initial investment cost	Opening balance	Increase during the year	Decrease during the year	Closing balance	Current year's			Closing balance	
								share of profit/(loss)	Dividend received/ receivable	Accumulated increase/ (decrease)		
												Opening balance
%	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB	RMB		
Ma Steel International Trade Corp.	NA	100	50,000,000	50,000,000	—	—	50,000,000	81,143,778	19,071,649	—	100,215,427	150,215,427
Design & Research Institute	NA	58.96	7,500,000	7,500,000	—	—	7,500,000	34,369,669	24,902,601	(8,818,400)	50,453,870	57,953,870
MG Control Technique	NA	93.75	7,500,000	7,500,000	—	—	7,500,000	2,535,653	388,217	—	2,923,870	10,423,870
Anhui Masteel K. Wah	30 years	70	24,854,930	24,854,930	—	—	24,854,930	3,551,381	4,973,467	(1,988,773)	6,536,075	31,391,005
Ma Steel (Wuhu)	30 years	70	8,225,885	8,225,885	—	—	8,225,885	35,855,286	11,352,697	(12,927,276)	34,280,707	42,506,592
Ma Steel (Guangzhou)	50 years	66.67	80,000,000	80,000,000	—	—	80,000,000	17,994,823	22,272,810	(14,394,600)	25,873,033	105,873,033
Ma Steel (HK)	NA	80	4,101,688	4,101,688	—	—	4,101,688	25,130,015	10,481,399	—	35,611,414	39,713,102
MG Trading	NA	100	1,573,766	1,573,766	—	—	1,573,766	(275,961)	750,014	—	474,053	2,047,819
Holly Industrial	20 years	71	21,478,316	21,478,316	—	—	21,478,316	53,760,988	53,083,196	(31,182,916)	75,661,268	97,139,584
Huayang Equipment	20 years	90	900,000	900,000	—	—	900,000	556,188	1,679,823	(55,618)	2,180,393	3,080,393
Ma Steel (Jinhua)	50 years	75	90,000,000	63,000,000	27,000,000	—	90,000,000	6,203	6,253,381	—	6,259,584	96,259,584
Ma Steel (Australia)	NA	100	126,312,415	126,312,415	—	—	126,312,415	4,607,825	27,722,857	—	32,330,682	158,643,097
Ma Steel (Hefei)	100 years	71	355,000,000	—	237,495,000	—	237,495,000	—	14,284,464	—	14,284,464	251,779,464
MS (Hefei) Processing	50 years	61	73,200,000	—	73,200,000	—	73,200,000	—	(12,043)	—	(12,043)	73,187,957
MS (Yangzhou) Processing	20 years	71	61,651,010	—	61,651,010	—	61,651,010	—	617,196	—	617,196	62,268,206
Total			395,447,000	399,346,010	—	794,793,010	259,235,848	197,821,728	(69,367,583)	387,689,993	1,182,483,003	

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. Long term investments (continued)

(ii) Interests in a JCE

Name of investee company	Investment period	Percentage of equity held by the Company	Group and Company									
			Initial investment cost	Investment cost			Adjustment for gain or loss				Closing balance	
				Opening balance	Increase during the year	Decrease during the year	Closing balance	Current year's share of profit	Dividend received/receivable	Accumulated increase/(decrease)		
												RMB
BOC-Ma Steel	18 Years	50	234,000,000	234,000,000	-	-	234,000,000	-	-	-	-	234,000,000

(iii) Interests in associates

Name of investee company	Investment period	Percentage of equity held by the Group	Group									
			Initial investment cost	Investment cost			Adjustment for gain or loss				Closing balance	
				Opening balance	Increase during the year	Decrease during the year	Closing balance	Current year's share of profit	Dividend received/receivable	Accumulated increase/(decrease)		
												RMB
濟源市金馬焦化	50 years	40	80,000,000	80,000,000	-	-	80,000,000	11,081,594	18,035,266	-	29,116,860	109,116,860
滕州盛隆煤焦化	50 years	32	66,776,000	66,776,000	-	-	66,776,000	(837,635)	10,896,216	-	10,058,581	76,834,581
上海鋼鐵電子	N/A	20	4,000,000	4,000,000	-	-	4,000,000	(683,589)	4,888,026	-	4,204,437	8,204,437
馬鞍山港口公司	20 years	45	112,500,000	104,831,800	7,668,200	-	112,500,000	2,891,511	6,467,016	-	9,358,527	121,858,527
奧馬特變速系統	20 years	45	9,000,000	-	9,000,000	-	9,000,000	-	-	-	-	9,000,000
馬鋼智能停車	20 years	25	4,500,000	-	4,500,000	-	4,500,000	-	-	-	-	4,500,000
Total				255,607,800	21,168,200	-	276,776,000	12,451,881	40,286,524	-	52,738,405	329,514,405

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. Long term investments (continued)

(iii) Interests in associates (continued)

Name of investee company	Investment period	Percentage of equity held by the Company	Initial investment cost	Investment cost			Adjustment for gain or loss			Closing balance			
				Opening balance	Increase during the year	Decrease during the year	Opening balance	Current year's share of profit	Dividend received/receivable		Accumulated increase/(decrease)		
												Company	
												RMB	RMB
濟源市金馬焦化	50 years	40	80,000,000	80,000,000	-	-	80,000,000	11,081,594	18,035,266	-	29,116,860	109,116,860	
滕州盛隆煤焦化	50 years	32	66,776,000	66,776,000	-	-	66,776,000	(837,635)	10,896,216	-	10,058,581	76,834,581	
上海鋼鐵電子	N/A	20	4,000,000	4,000,000	-	-	4,000,000	(683,589)	4,888,026	-	4,204,437	8,204,437	
馬鞍山港口公司	20 years	45	112,500,000	104,831,800	7,668,200	-	112,500,000	2,891,511	6,467,016	-	9,358,527	121,858,527	
Total			255,607,800	255,607,800	7,668,200	-	263,276,000	12,451,881	40,286,524	-	52,738,405	316,014,405	

(iv) Other equity investments

Equity investments accounted for using the cost method:

Name of investee company	Nature of investments	Number of shares held	Percentage of equity held by the Company	Investment cost
			%	RMB
河南龍宇能源股份有限公司	Legal person shares	6,500,138	0.66	10,000,000
Tangshan Iron and Steel Company Limited	Circulating share with sales restriction	1,003,200	0.04	4,559,109
Shanghai Chlor-Alkali Chemical Company Limited	Circulating share with sales restriction	164,578	0.01	807,926
Others				1,450,000
Total				16,817,035

Notes to Financial Statements (Continued)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

9. Long term investments (continued)

(v) Other debt investment

Debtor	Principal amount RMB	Annual interest rate %	Maturity date	Interest for the year RMB	Accumulated interest received/receivable RMB	Carrying value RMB
安徽省電力 開發總公司	<u>8,258,870</u>	Nil	2007-2009	<u>-</u>	<u>-</u>	<u>8,258,870</u>

The movement of impairment provision for long term investments for the year 2006 is disclosed in the supplementary information of the financial statements.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

10. Fixed assets

	Buildings and structures RMB	Plant, machinery and equipment RMB	Transportation vehicles and equipment RMB	Total RMB
Cost				
At 1 January 2006	8,697,233,073	18,806,495,387	415,790,295	27,919,518,755
Additions	62,770,641	30,144,811	3,396,706	96,312,158
Acquisition of a subsidiary (Note 45)	34,567,612	16,793,913	666,897	52,028,422
Minority shareholder contribution (Note 46)	212,656,812	385,748,243	3,882,583	602,287,638
Transferred from construction in progress (Note 11)	315,818,982	1,713,783,325	12,530,224	2,042,132,531
Reclassifications	172,523,886	(179,247,185)	6,723,299	-
Disposal	(39,171,289)	(217,465,520)	(47,859,002)	(304,495,811)
At 31 December 2006	9,456,399,717	20,556,252,974	395,131,002	30,407,783,693
Accumulated depreciation				
At 1 January 2006	2,748,009,347	6,428,411,270	234,659,664	9,411,080,281
Provided during the year	512,645,677	1,761,811,454	50,941,736	2,325,398,867
Acquisition of a subsidiary (Note 45)	1,422,359	1,407,743	86,377	2,916,479
Reclassifications	43,074,508	(43,883,151)	808,643	-
Disposal	(20,967,459)	(173,742,589)	(38,004,178)	(232,714,226)
At 31 December 2006	3,284,184,432	7,974,004,727	248,492,242	11,506,681,401
Net book value				
At 31 December 2006				
Net book value	6,172,215,285	12,582,248,247	146,638,760	18,901,102,292
Less: Impairment provision	(5,252,400)	(85,423,244)	-	(90,675,644)
Net book value, net of impairment provision	<u>6,166,962,885</u>	<u>12,496,825,003</u>	<u>146,638,760</u>	<u>18,810,426,648</u>
At 31 December 2005				
Net book value	5,949,223,726	12,378,084,117	181,130,631	18,508,438,474
Less: Impairment provision	(10,391,900)	(106,664,944)	-	(117,056,844)
Net book value, net of impairment provision	<u>5,938,831,826</u>	<u>12,271,419,173</u>	<u>181,130,631</u>	<u>18,391,381,630</u>

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

10. Fixed assets (continued)

The cost of fully depreciated fixed assets which are still in use amounted to approximately RMB1.8 billion.

As at the balance sheet date, certain of the Group's equipments with a net book value of approximately RMB28 million were pledged to secure a loan granted by Profit Access Investments Limited. Further details of the transaction are included in Note 24 to the financial statements.

At the balance sheet date, certificates of ownership in respect of the Group's buildings with a net book value of RMB70.2 million had not been issued by the relevant government authorities. The directors represent that the Group is in the process of obtaining the relevant certificates.

The movement of provision for impairment of fixed assets for the year 2006 is disclosed in the supplementary information of the financial statements.

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

11. Construction in progress

Construction in progress represents the following major projects which remained uncompleted as at 31 December 2006:

Name of project	Budget cost	1 January 2006	Minority shareholder contribution (Note 46)	Addition during the year	Transferred to fixed assets (Note 10)	Other transfer out	At 31 December 2006	Source of fund	Percentage of completion
	RMB'000	RMB	RMB	RMB	RMB	RMB	RMB		%
1. Blast Furnaces Project	5,715,560	761,803,243	-	2,914,116,638	(38,825,293)	-	3,637,094,588	Internally generated funds	21-100
<i>Including borrowing costs capitalised:</i>		11,765,964	-	169,246,148	-	-	181,012,112	and loans from financial institution	
2. Converters Project	3,491,500	475,136,663	-	2,429,219,373	(61,253,940)	-	2,843,102,096	Internally generated funds	82-100
<i>Including borrowing costs capitalised:</i>		3,026,339	-	54,035,221	-	-	57,061,560	and loans from financial institution	
3. Wheel Line Project	524,330	158,473,675	-	302,903,186	(436,198,628)	-	25,178,233	Internally generated funds	84-100
4. Construction Steel Lines Project	16,842,710	1,379,445,445	-	6,211,839,258	(743,547,500)	-	6,847,737,203	Internally generated funds	25-100
<i>Including borrowing costs capitalised:</i>		43,118,129	-	265,189,590	(23,465,500)	-	284,842,219	and loans from financial institution	
5. Coking Stoves Project	2,697,000	279,910,490	-	1,298,851,178	(49,983,497)	-	1,528,778,171	Internally generated funds	43-100
<i>Including borrowing costs capitalised:</i>		8,784,000	-	60,739,740	-	-	69,523,740	and loans from financial institution	
6. Public Auxiliary Utilities Project	4,781,794	1,237,039,767	-	2,267,971,488	(99,087,037)	-	3,405,924,218	Internally generated funds	7-100
<i>Including borrowing costs capitalised:</i>		1,247,190	-	54,489,705	-	-	55,736,895	and loans from financial institution	

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

11. Construction in progress (continued)

Name of project	Budget cost RMB'000	1 January 2006 RMB	Minority shareholder contribution (Note 46) RMB	Addition during the year RMB	Transferred to fixed assets (Note 10) RMB	Other transfer out RMB	At 31 December 2006 RMB	Source of fund	Percentage of completion %
7. Energy-saving and Environment Protection Project	107,730	33,036,296	-	38,341,100	(33,817,606)	-	37,559,790	Internally generated funds	22-100
8. Other Projects <i>Including borrowing costs capitalised:</i>	N/A	477,056,170 15,108,480	640,000 -	700,199,425 -	(579,419,030) -	(64,508,540) -	533,968,025 15,108,480	Internally generated funds and loans from financial institution	N/A
		4,801,901,749	640,000	16,163,441,646	(2,042,132,531)	(64,508,540)	18,859,342,324		
Less: Impairment provision		(74,000,000)	-	-	-	74,000,000	-		
		<u>4,727,901,749</u>	<u>640,000</u>	<u>16,163,441,646</u>	<u>(2,042,132,531)</u>	<u>9,491,460</u>	<u>18,859,342,324</u>		

The increase in the Group's construction in progress by 299% was mainly attributable to the constructions for the "Eleventh Five Year Plan" in 2006.

The capitalisation rates of interest are 1.4%-5.832% per annum.

The movement of provision for impairment of construction in progress for the year 2006 is disclosed in the supplementary information of the financial statements.

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31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

12. Intangible assets

	Method of acquisition	Original amount	Accumulated amortisation	At 1 January 2006	Additions during the year	Amortisation during the year	Transfer to construction in progress	At 31 December 2006	Remaining years of amortisation
		RMB	RMB	RMB	RMB	RMB	RMB	RMB	
Mine Participation right (Note i)	Purchase	110,150,400	(1,115,704)	109,034,696	8,953,168	(4,481,358)	-	113,506,506	24 years
Land use rights (Note ii)	Purchase	1,092,429,840	(231,318,487)	861,111,353	436,227,094	(23,379,892)	(33,808,464)	1,240,150,091	36 to 50 years
Land use rights	Acquisition of a subsidiary (Note 45)	-	-	-	13,447,882	(14,583)	-	13,433,299	48 years
Land use rights	Minority shareholder contribution (Note 46)	-	-	-	154,104,000	(4,491,200)	-	149,612,800	29 years
Total		<u>1,202,580,240</u>	<u>(232,434,191)</u>	<u>970,146,049</u>	<u>612,732,144</u>	<u>(32,367,033)</u>	<u>(33,808,464)</u>	<u>1,516,702,696</u>	

Note i: One subsidiary of the Company, Ma Steel (Australia), has 10% interest in an Australian unincorporated joint venture, in which Ma Steel (Australia) does not have joint control or is not in a position to exercise significant influence. During 2005, together with the other participants of this joint venture, Ma Steel (Australia) purchased a mine participation right in Australia in the form of sub-lease for 25 years.

Note ii: As at the balance sheet date, the net book value of land use right leased out is approximately RMB3.56 million (2005: RMB1.24 million).

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

13. Short term loans

Type	Annual interest rate %	Maturity date	31 December 2006 RMB	31 December 2005 RMB
Unsecured loans	5.022-5.58	1/2007 ~6/2007	380,000,000	112,372,660
Trust receipt loans	4.60-4.66	2/2007	19,018,506	–
			399,018,506	112,372,660

The increase in the Group's short term loans by 255% was mainly attributable to the increase in working capital loans borrowed for purchase of raw materials and fuel.

14. Bills payable

	31 December 2006 RMB	31 December 2005 RMB
Bank bills	1,346,880,982	655,567,000

The increase in the Group's bills payable by 105% was mainly attributable to the increase in use of bank bills for payments of materials purchase.

Balances with financial institutions amounting to USD1 million, RMB523.3 million and inventories amounting to RMB121,914,383 have been pledged to banks as securities for issue of bank bills by the Company's subsidiaries, and were not readily available for payment or sale.

The balance of bills payable does not contain any amount due from a shareholder who holds 5% or above of the Company's equity interest.

15. Short term commercial papers

Name	Interest payable during the year RMB	Accumulated interest payable RMB	31 December 2006 RMB	31 December 2005 RMB
Short term commercial papers	–	–	–	2,000,000,000

The short-term commercial papers represented 20,000,000 3.19% per annum short-term commercial papers with a nominal value of RMB100 issued by the Company at par on 29 December 2005. These short-term commercial papers were redeemed on 28 December 2006.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

16. Accounts payable

The increase in the Group's accounts payable by 45% was mainly attributable to the increase of payables for equipments purchases under the "Eleventh Five-year Plan" constructions.

Certain of the Group's accounts payable amounting to RMB5,900,000 are aged over three years as a result of delay in settlement of construction fee.

Except for those as stated in Note VII point 6, the balance of accounts payable does not contain any amount due to a shareholder who holds 5% or above of the Company's equity interest.

17. Deposits received

The ageing of deposits received is within one year.

Except for those as stated in Note VII point 6, the balance of deposits received does not contain any amount due to a shareholder who holds 5% or above of the Company's equity interest.

18. Wages payable

The increase in the Group's wages payable by 41% was mainly due to the increase of bonus payable for the year 2006.

The closing balance included RMB500,175 which was performance-related wages brought forward from prior years.

19. Dividends payable

	31 December 2006 RMB	31 December 2005 RMB
Dividends of 2005 due to Holding	400,000,000	–
Dividends of 2005 due to minority shareholders	8,654,914	–
Dividends of 2004 due to minority shareholders	<u>–</u>	<u>8,643,954</u>
Total	<u>408,654,914</u>	<u>8,643,954</u>

The increase in the Group's dividends payable by 46 times was mainly attributable to the increase in dividends payable to Holding.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

20. Taxes payable

	31 December 2006 RMB	31 December 2005 RMB
Corporate income tax	93,109,562	118,021,576
VAT	100,355,879	330,870,312
Business tax	1,849,836	1,673,353
City construction and maintenance tax	31,132,303	7,377,600
Other taxes	27,462,697	35,846,914
Total	<u>253,910,277</u>	<u>493,789,755</u>

The decrease in the Group's taxes payable by 49% was mainly due to the decrease in VAT payable of 2006.

The basis of calculations and the applicable tax rates are disclosed in Note III to the financial statements.

21. Other taxes payable

	31 December 2006 RMB	31 December 2005 RMB
Flood prevention fund	26,909,152	13,484,963
Education surcharge	13,344,540	5,079,358
Other taxes	5,459,200	1,743,556
Total	<u>45,712,892</u>	<u>20,307,877</u>

The increase in the Group's other taxes payable by 125% was mainly attributable to the increase in flood prevention fund and education surcharge payables.

The basis of calculations and the applicable tax rates are disclosed in Note III to the financial statements.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

22. Other payables

	31 December 2006 RMB	31 December 2005 RMB
Construction, maintenance and inspection fee	229,605,094	154,804,749
Payables to a minority shareholder	168,620,150	–
Sales benefits	151,517,642	116,044,016
Payroll related charges	145,714,652	154,084,470
Direct issue cost of bonds with warrants	64,350,000	–
Others	67,555,614	55,149,346
Total	827,363,152	480,082,581

The increase in the Group's other payables by 72% was mainly attributable to the increase of the payable to a minority shareholder and direct issue cost of bonds with warrants.

Certain of the Group's other payables amounting to RMB5,400,000 are aged over three years as a result of delay in settlement of certain service fees.

The balance of other payables does not contain any amount due to a shareholder who holds 5% or above of the Company's equity interest.

23. Accrued charges

	31 December 2006 RMB	31 December 2005 RMB
Loan interests	57,072,832	58,712,708
Maintenance fee	11,580,000	4,862,311
Retirement benefits payable to early retired employees	7,440,372	10,773,268
Others	14,411,488	24,769,361
Total	90,504,692	99,117,648

Notes to Financial Statements (Continued)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

24. Long term loans due within a year

Lenders	31 December 2006			31 December 2005			Maturity date	Annual interest rate %	Conditions of borrowings
	Currency type	Original currency amount	RMB	Currency type	Original currency amount	RMB			
Industrial and Commercial Bank of China	-	-	-	RMB	260,000	260,000	N/A	N/A	N/A
China Construction Bank (Note i)	RMB	13,200,000	13,200,000	RMB	13,200,000	13,200,000	12/2007	2.4	Unsecured
	USD	3,986,329	31,128,044	USD	7,972,657	64,340,936	4/2007	LIBOR (6 months) +0.5	Guaranteed by Holding
Agricultural Bank of China	RMB	90,000,000	90,000,000	-	-	-	5/2007-8/2007	5.49	Guaranteed by Holding
Bank of China	RMB	32,000,000	32,000,000	-	-	-	3/2007-5/2007	5.76	Guaranteed by Holding
	EUR	123,947	1,272,499	EUR	123,947	1,187,373	3/2007-9/2007	0.25	Guaranteed by Sinosteel Trading Company
The Export-import Bank Of China	RMB	200,000,000	200,000,000	-	-	-	6/2007	5.265	Unsecured
	RMB	15,000,000	15,000,000	-	-	-	8/2007	3.78	Guaranteed by Holding
Huishang Bank	RMB	19,000,000	19,000,000	-	-	-	6/2007-8/2007	5.49	Unsecured
Profit Access Investment Company Limited (Note ii)	USD	260,000	2,151,994	-	-	-	6/2007	5.49	Unsecured
	USD	726,000	6,000,000	-	-	-	8/2007	5.49	Secured
Total			<u>409,752,537</u>						<u>78,988,309</u>

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

24. Long term loans due within a year (continued)

Note i: LIBOR represents London Interbank Offered Rate.

Note ii: Profit Access Investments Limited holds a 30% equity interests in Anhui Masteel K. Wah and is a minority shareholder of Anhui Masteel K. Wah. Profit Access Investments Limited granted foreign exchange loans to Anhui Masteel K. Wah. The loans bear interest at a rate of 5.49% per annum (with reference to RMB loan interest rate of Huishang Bank). Certain of the loans are secured by the pledge of certain of the Anhui Masteel K. Wah's equipment with an aggregate net book value of approximately RMB28 million as at 31 December 2006.

25. Long term loans

Lenders	31 December 2006			31 December 2005			Maturity date	Annual interest rate %	Conditions of borrowings
	Currency type	Original currency amount	RMB	Currency type	Original currency amount	RMB			
Industrial and Commercial Bank of China	RMB	1,700,000,000	1,700,000,000	RMB	2,057,000,000	2,057,000,000	4/2008 — 9/2008	Central Bank benchmark rate less 10%	Guaranteed by Holding
	RMB	900,000,000	900,000,000	—	—	—	2/2010 — 6/2010	5.022	Unsecured
China Construction Bank	RMB	1,377,000,000	1,377,000,000	RMB	1,117,000,000	1,117,000,000	1/2010 — 9/2011	Central Bank benchmark rate less 10%	Guaranteed by Holding
	RMB	1,000,000,000	1,000,000,000	RMB	600,000,000	600,000,000	1/2010 — 6/2010	4.86, 5.022	Unsecured
	—	—	—	USD	20,000,000	161,404,000	N/A	N/A	N/A
	—	—	—	USD	3,986,329	32,170,471	N/A	N/A	N/A

Notes to Financial Statements (Continued)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

25. Long term loans (continued)

Lenders	31 December 2006			31 December 2005			Maturity date	Annual interest rate %	Conditions of borrowings
	Currency type	Original currency amount	RMB	Currency type	Original currency amount	RMB			
Bank of China	RMB	1,930,000,000	1,930,000,000	RMB	212,000,000	212,000,000	2/2008— 8/2011	5.76, Central Bank benchmark rate less 10%	Guaranteed by Holding
	RMB	900,000,000	900,000,000	RMB	110,000,000	110,000,000	2/2010— 6/2010	4.76, 5.022	Unsecured
	EUR	1,487,361	15,269,994	EUR	1,611,308	15,435,846	3/2008— 9/2019	0.25	Guaranteed by Sinosteel Trading Company
	—	—	—	USD	66,000,000	532,633,200	N/A	N/A	N/A
Agricultural Bank of China	RMB	2,220,000,000	2,220,000,000	RMB	894,000,000	894,000,000	1/2008— 10/2011	5.265, 5.508, 5.76	Guaranteed by Holding
	RMB	600,000,000	600,000,000	RMB	600,000,000	600,000,000	9/2008	5.184	Unsecured
Huishang Bank	—	—	—	RMB	169,000,000	169,000,000	N/A	N/A	N/A
	RMB	360,000,000	360,000,000	RMB	360,000,000	360,000,000	9/2008	5.184	Guaranteed by Holding
China CITIC Bank	RMB	400,000,000	400,000,000	RMB	400,000,000	400,000,000	8/2008	4.32	Unsecured
	USD	50,000,000	390,435,000	USD	50,000,000	403,510,000	8/2008	LIBOR(6 months) +0.4	Unsecured
China Merchants Bank	RMB	400,000,000	400,000,000	RMB	400,000,000	400,000,000	10/2008— 11/2008	Central Bank benchmark rate less 10%	Unsecured
	USD	50,000,000	390,435,000	USD	50,000,000	403,510,000	10/2008— 11/2008	LIBOR(6 months) +0.4	Unsecured
The Export-import Bank Of China	RMB	580,000,000	580,000,000	RMB	95,000,000	95,000,000	3/2008— 8/2012	3.78	Guaranteed by Holding

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

25. Long term loans (continued)

Lenders	31 December 2006			31 December 2005			Maturity date	Annual interest rate %	Conditions of borrowings
	Currency type	Original currency amount	RMB	Currency type	Original currency amount	RMB			
Bank of Communications	RMB	1,000,000,000	1,000,000,000	—	—	—	4/2009 — 9/2011	Central Bank benchmark rate less 10%	Guaranteed by Holding
	RMB	500,000,000	500,000,000	—	—	—	6/2010	5.022	Unsecured
Industrial Bank	RMB	300,000,000	300,000,000	—	—	—	6/2011 — 7/2011	Central Bank benchmark rate less 10%	Unsecured
Shanghai Pudong Development Bank	RMB	600,000,000	600,000,000	—	—	—	6/2009 — 6/2010	5.022, Central Bank benchmark rate less 10%	Unsecured
Shenzhen Development Bank	RMB	150,000,000	150,000,000	—	—	—	11/2009	Central Bank benchmark rate less 10%	Guaranteed by Holding
Profit Access Investment Company Limited	—	—	—	USD	986,000	8,151,994	N/A	N/A	N/A
Total		<u>15,713,139,994</u>			<u>8,570,815,511</u>				

The increase in the Group's long term loans by 83% was mainly attributable to the increase in the long term loans drawdown to finance the constructions under the "Eleventh Five-year Plan".

Notes to Financial Statements (Continued)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

26. Bonds payable

Name	Life	Issue date	Nominal Amount RMB	Interest payable during the year RMB	Accumulated interest payable RMB	31 December 2006 RMB	31 December 2005 RMB
Bonds with warrants	5 years	13 November 2006	5,500,000,000	13,050,950	13,050,950	5,513,050,950	-

On 13 November 2006, the Company issued 55,000,000 bonds with warrants with a nominal value of RMB100 each, amounting to RMB5.5 billion in total. The bonds with warrants are listed on the Shanghai Stock Exchange. The bonds with warrants are guaranteed by Holding and have a 5-year life from the date of issuance, and will be fully repaid in November 2011. The subscribers of each bond have been entitled to receive 23 warrants at nil consideration, and in aggregate, 1,265,000,000 warrants have been issued. The warrants have a life of 24 months from the date of listing and every warrant can be converted into one A share at a conversion price of RMB3.4. The holders of the warrants are entitled to exercise the warrants 10 trading days prior to the 12-month and 24-month of the listing of the warrants. Exercise in full of the warrants would have resulted in the issue of 1,265,000,000 A shares.

The bonds with warrants are interest-bearing at a rate of 1.4% per annum payable in arrears on 12 November each year.

Up to 31 December 2006, no warrant was exercised.

27. Specific payables

	31 December 2006 RMB	31 December 2005 RMB
Government subsidies for specific construction projects	116,566,523	3,200,000

The increase by 35 times was attributable to the increase in government subsidies received for the constructions under the "Eleventh Five-year Plan".

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

28. Other long term liabilities

	31 December 2006 RMB	31 December 2005 RMB
Payables to Holding	400,000,000	400,000,000
Accrued charges for furnace relining	74,499,299	74,499,299
Retirement benefits payable to early retired employees	22,044,660	29,485,032
Total	<u>496,543,959</u>	<u>503,984,331</u>

The payables to Holding are interest-free, unsecured and contractually repayable after 1 January 2008.

29. Minority interests

The increase in the minority interests in consolidated balance sheet by 125% was mainly attributable to the capital injection made by minority shareholders and the increase in profits of certain non-wholly owned subsidiaries during the year.

The increase in the minority interest in consolidated statement of income by 42% was mainly attributable to the increase in profits of certain non-wholly owned subsidiaries during the year.

Notes to Financial Statements (Continued)

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

30. Share capital

The Company had registered, issued and fully paid share capital amounting to RMB6,455,300,000, with each share having a face value of RMB1. The types and structure of share capital are as follows:

	1 January 2006		Group and Company Increase/(decrease) during the year Transfer of shares under State Share Reform	31 December 2006	
	RMB	Ratio		RMB	Ratio
A. Shares with sales restriction					
1. State-owned shares	4,034,560,000	62.50	(204,000,000)	3,830,560,000	59.34
2. Other domestically owned shares	87,810,000	1.36	–	87,810,000	1.36
Including:					
Shares owned by domestic legal persons	87,810,000	1.36	–	87,810,000	1.36
Shares owned by domestic natural persons	–	–	–	–	–
Sub-total	4,122,370,000	63.86	(204,000,000)	3,918,370,000	60.70
B. Shares without sales restriction					
1. A shares	600,000,000	9.29	204,000,000	804,000,000	12.45
2. H shares	1,732,930,000	26.85	–	1,732,930,000	26.85
Sub-total	2,332,930,000	36.14	204,000,000	2,536,930,000	39.30
C. Total	6,455,300,000	100.00	–	6,455,300,000	100.00

On 17 March 2006, all relevant approvals for converting all the Company's unlisted and non-circulating Shares ("Non-circulating Shares") into listed and circulating A shares ("Circulating A Shares") (the "State Share Reform") have been obtained. The then Non-circulating Shares have been entitled to be listed and become Circulating A shares since 31 March 2006 (the "Listing Date"). In accordance with the execution arrangement, Holding offered 3.4 of its shares to each original Circulating A Shares' shareholder for every 10 Circulating A Shares they held. The number of shares held by Holding decreased by 204 million shares whereas the number of shares held by the original Circulating A Shares' shareholders increased by 204 million shares. The total number of issued share of the Company remained unchanged.

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V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

30. Share capital (continued)

After the implementation of the State Share Reform, all the shares held by Holding and the legal person A shares held by other domestic legal persons are not listed for trading or transferred within 12 months from the Listing Date and the State-owned shares held by Holding are also not listed for trading and transferred in the following 24 months. However, so far as it is permitted under the scope of prevailing policies, Holding may carry out incentive stock option plan(s) or share transfer to particular investor(s). Target(s) of the incentive stock option plan(s) should hold the shares for such period as prescribed under the relevant policies and the particular investor(s) should, after acquiring the shares from Holding, continue to hold such shares for the same period as undertaken by Holding.

31. Capital reserve

	Group and Company			
	At 1 January 2006	Increase during the year	Decrease during the year	At 31 December 2006
	RMB	RMB	RMB	RMB
Share premium	4,864,975,395	–	–	4,864,975,395
Specific payables transferred in	585,369,700	3,200,000	–	588,569,700
Total	<u>5,450,345,095</u>	<u>3,200,000</u>	<u>–</u>	<u>5,453,545,095</u>

The addition in the capital reserve of the Group and the Company during the year represented the transfer-in of government subsidies from specific payables upon the completion of certain subsidised construction projects.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

32. Surplus reserves

	Group			At 31 December 2006 RMB
	At 1 January 2006 RMB	Increase during the year RMB	Decrease during the year RMB	
Statutory reserve	1,179,972,207	1,415,801,706	–	2,595,773,913
Statutory public welfare fund	1,178,385,368	–	(1,178,385,368)	–
Reserve fund	11,112,647	11,934,321	–	23,046,968
Enterprise expansion fund	10,677,774	7,661,545	–	18,339,319
Total	<u>2,380,147,996</u>	<u>1,435,397,572</u>	<u>(1,178,385,368)</u>	<u>2,637,160,200</u>

	Company			At 31 December 2006 RMB
	At 1 January 2006 RMB	Increase during the year RMB	Decrease during the year RMB	
Statutory reserve	1,166,669,675	1,397,992,215	–	2,564,661,890
Statutory public welfare fund	1,166,669,675	–	(1,166,669,675)	–
Total	<u>2,333,339,350</u>	<u>1,397,992,215</u>	<u>(1,166,669,675)</u>	<u>2,564,661,890</u>

In accordance with the Company Law of the PRC and the articles of associations, the Company and certain of its subsidiaries are required to allocate 10% of their profit after tax, as determined in accordance with PRC accounting standards and regulations applicable to these companies, to the statutory reserve (the "SR") until such reserves reach 50% of the registered capitals of these companies. Part of the SR may be capitalised as these companies' share capitals, provided that the remaining balances after the capitalisation are not less than 25% of the registered capitals of these companies.

In previous years, the Company and certain of its subsidiaries are required to transfer 5% to 10% of their profit after tax, as determined in accordance with PRC accounting standards and regulations applicable to these companies, to the statutory public welfare fund (the "PWF"). According to the Company Law of the People's Republic of China (2005 revised) that took effect as of 1 January 2006, and the modified articles of associations, the Company and certain of its subsidiaries were not required to allocate any profit to the PWF starting from 2006. The balance of PWF as at 31 December 2005 was transferred to the SR.

(Prepared under PRC Accounting Standards)
31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

32. Surplus reserves (continued)

Certain of the Company's subsidiaries are Chinese-foreign equity joint ventures. In accordance with the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures and their respective articles of associations, these subsidiaries are required to allocate certain of their profit after tax as determined in accordance with PRC accounting standards and related regulations to the enterprise expansion fund, the reserve fund and the employee bonus and welfare fund. The allocation rates are determined by their respective boards of directors.

Subsequent to the balance sheet date, the directors determined that the Company should transfer RMB231,322,540 (2005: RMB278,666,301) to the SR. This represents 10% of the Company's profit after tax of RMB2,313,225,397 (2005: RMB2,786,663,009) determined in accordance with PRC accounting standards and regulations.

During the year, the share of subsidiaries' current year appropriations to each of the SR, the reserve fund and the enterprise expansion fund, in accordance with percentage of investment held by the Group, were RMB6,093,798 (2005: RMB8,146,210), RMB11,934,321 (2005: RMB7,632,717) and RMB7,661,545 (2005: RMB5,542,898), respectively.

The Group's and the Company's surplus reserves increased by 11% and 10% respectively were attributable to the profit appropriation for the year 2006.

33. Retained profits

	Note	Group RMB
Retained profits at beginning of year		4,595,922,817
Add: the consolidated net profit for the year		2,276,585,903
Less: Transfer to SR		(237,416,338)
Transfer to reserve fund		(11,934,321)
Transfer to enterprise expansion fund		(7,661,545)
Transfer to employee bonus and welfare fund		(6,546,881)
Ordinary share dividend payable		(1,032,848,000)
Retained profits at end of year		<u>5,576,101,635</u>
Including: Cash dividend proposed by directors	42	<u>839,189,000</u>

In accordance with the PRC relevant regulations, the retained profits of the Company for the purpose of profit distribution are deemed to be the lower of the amount determined in accordance with PRC accounting standards and regulations, and the amount determined in accordance with generally accepted accounting principles in Hong Kong.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

33. Retained profits (continued)

As at 31 December 2006, the Company had retained profits of approximately RMB5.55 billion (31 December 2005: approximately RMB4.54 billion), as determined in accordance with the lower of the amount determined under PRC accounting standards and regulations and the amount determined under generally accepted accounting principles in Hong Kong, available for distribution by way of cash or kind.

As at 31 December 2006, in accordance with the Company Law of the PRC, an amount of approximately RMB5.45 billion (31 December 2005: approximately RMB5.45 billion) standing to the credit of the Company's capital reserve account, as determined under PRC accounting standards and regulations, was available for distribution by way of future capitalisation issue. At the same date, the Company did not have any capitalisation issue.

34. Principal operating income, cost of sales and profit from principal operating activities

Category	2006			Group		
	Operating income	Cost of sales	Profit from operating activities	Operating income	Cost of sales	Profit from operating activities
	RMB	RMB	RMB	RMB	RMB	RMB
Sale of steel products	32,315,572,592	28,529,075,512	3,786,497,080	30,143,438,308	25,853,648,022	4,289,790,286
Sale of steel billets	545,925,914	488,023,868	57,902,046	479,308,861	406,276,901	73,031,960
Sale of coke by-products	523,437,134	347,290,381	176,146,753	371,127,636	313,134,277	57,993,359
Sale of pig iron	657,460	516,726	140,734	793,112	629,353	163,759
Others	934,281,052	565,364,651	368,916,401	1,088,428,093	720,818,084	367,610,009
Total	34,319,874,152	29,930,271,138	4,389,603,014	32,083,096,010	27,294,506,637	4,788,589,373

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

34. Principal operating income, cost of sales and profit from principal operating activities (continued)

Category	Company					
	2006			2005		
	Operating income RMB	Cost of sales RMB	Profit from operating activities RMB	Operating income RMB	Cost of sales RMB	Profit from operating activities RMB
Sale of steel products	32,301,046,955	28,700,830,117	3,600,216,838	30,143,438,308	25,853,648,022	4,289,790,286
Sale of steel billets	545,925,914	488,023,868	57,902,046	479,308,861	406,276,901	73,031,960
Sale of coke by-products	523,437,134	348,277,129	175,160,005	371,127,636	313,134,277	57,993,359
Sale of pig iron	657,460	516,726	140,734	793,112	629,353	163,759
Others	897,559,475	747,915,702	149,643,773	1,003,920,997	938,471,716	65,449,281
Total	34,268,626,938	30,285,563,542	3,983,063,396	31,998,588,914	27,512,160,269	4,486,428,645

Sales to the five largest customers of the Group and the Company for the year amounted to RMB4,203,430,165 and RMB4,054,038,407, which accounted for 12% of the Group's and the Company's total sales amounts respectively.

35. Taxes and surcharges

	2006 RMB	2005 RMB
City construction and maintenance tax	142,411,681	131,303,393
Education surcharge	61,033,577	56,272,883
Local education surcharge	20,344,526	18,757,628
Other taxes	16,603,258	12,773,111
Total	240,393,042	219,107,015

The calculation bases of the Group's taxes and surcharges and the related tax rates are disclosed in Note III to the financial statements.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

36. Other operating profit

The decrease in the Group's other operating profit by 56% was mainly attributable to the decrease in the trading of iron ore.

37. Administrative expenses

	2006 RMB	2005 RMB
Staff cost	385,519,205	282,614,051
Welfare and support services	95,845,003	95,795,830
Removal compensation and demolition expenses	61,661,513	76,990,800
Taxes and duties	58,019,901	55,109,722
Depreciation and amortisation charge	55,271,900	42,326,809
Joint office expenses	52,260,851	46,767,059
Safeguard fee	51,496,378	42,120,051
Flood prevention fee	32,460,658	17,277,444
Environmental protection fee	26,076,536	34,574,233
Inventory provision	(26,190,003)	75,464,166
Others	171,873,626	160,598,909
Total	<u>964,295,568</u>	<u>929,639,074</u>

38. Financial expenses

	2006 RMB	2005 RMB
Interest expenses	296,225,738	362,470,045
Less: Interest income	(34,258,808)	(22,103,475)
Exchange loss	79,056,338	46,862,358
Less: Exchange gain	(23,184,103)	(201,605,652)
Others	24,931,084	23,858,875
Total	<u>342,770,249</u>	<u>209,482,151</u>

The increase in the Group's financial expenses by 64% was mainly attributable to the decrease in foreign exchange gain and increase in foreign exchange loss.

(Prepared under PRC Accounting Standards)
31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

39. Investment income

	Group		Company	
	2006 RMB	2005 RMB	2006 RMB	2005 RMB
Share of profits of subsidiaries	–	–	197,821,728	168,737,203
Share of profit of associates	40,286,524	13,464,093	40,286,524	13,464,093
Other equity investment income	19,277,921	5,281,238	19,300,121	5,281,238
Total	59,564,445	18,745,331	257,408,373	187,482,534

The increase in the Group's investment income by 218% was mainly attributable to the increase in the share of profits of associates and gain on disposal of short-term investment during the year.

As at the balance sheet date, no significant restriction was imposed upon the transfer of the Group's investment income.

40. Subsidies income

	2006 RMB	2005 RMB
Fiscal subsidies	5,850,001	1,992,600

41. Non-operating expenses

The decrease in the Group's non-operating expenses by 164% was mainly attributable to the reversal of fixed assets impairment during the year.

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

42. Cash dividend proposed by directors

	Group and Company	
	2006 RMB	2005 RMB
Proposed final cash dividend – RMB13 cents (2005: RMB16 cents) per ordinary share	<u>839,189,000</u>	<u>1,032,848,000</u>

Proposed ordinary share dividend is determined based on the profit appropriation plan for the year ended 2006 as approved by the board of directors after the balance sheet date. Dividend proposed for legal person shares, A shares and H shares amounted to RMB509,388,100, RMB104,520,000 and RMB225,280,900 respectively. The proposed dividend is subject to approval by the shareholders at the annual general meeting.

43. Cash paid relating to other operating activities

	2006 RMB	2005 RMB
Welfare and support services	95,845,003	95,795,830
Removal compensation and demolition expenses	61,661,513	76,990,800
Taxes and duties	58,019,901	55,109,722
Safeguard fee	51,496,378	42,120,051
Flood prevention fee	32,460,658	17,277,444
Environmental improvement fee	26,076,536	34,574,233
Repair and maintenance expenses	24,228,949	13,797,253
Packing fee	19,227,486	19,118,316
Export related costs	17,606,395	8,392,268
Loading expenses	15,159,614	17,249,060
Rental fee	4,700,356	6,345,554
Others	10,408,762	75,151,562
Total	<u>416,891,551</u>	<u>461,922,093</u>

(Prepared under PRC Accounting Standards)
31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

44. Cash received relating to other investing activities

	2006 RMB	2005 RMB
Government subsidies for specific construction projects	<u>116,566,523</u>	<u>6,700,000</u>

45. Acquisition of businesses/a subsidiary

On 26 November 2006, the Company acquired a 71% of equity interest in 寶威鋼板制品(揚州)有限公司 (“Burwill (Yangzhou)”) from Burwill Times Industrial Limited at a cash consideration of RMB61,651,010. Burwill (Yangzhou) is mainly engaged in high value-added steel coils processing and distribution in the PRC. Upon completion of the acquisition, Burwill (Yangzhou) will be renamed as Ma Steel (Yangzhou) Processing and Distribution Co., Ltd. (“MS (Yangzhou) Processing”). The consideration was determined with reference to the net assets value, which was valued by 江蘇天衡會計事務所.

The net assets of MS (Yangzhou) Processing at the date of transfer were set out below:

	Notes	RMB
Cash and balances with financial institutions		12,487,491
Trade receivables		11,882,851
Other receivables		2,016,761
Prepayments		7,258
Inventories		354,141
Fixed assets cost	10	52,028,422
Less: Accumulated depreciation	10	(2,916,479)
Net book value		49,111,943
Intangible assets	12	13,447,882
Accounts payable		(1,533,881)
Taxes payable		(632,990)
Other payables		(303,032)
Other accrued charges		(6,015)
Minority interests		(25,181,399)
Net assets		61,651,010
Cash consideration paid		57,404,685
Unpaid portion of cash consideration		<u>4,246,325</u>

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

45. Acquisition of businesses/a subsidiary (continued)

Analysis of net outflow of cash and cash equivalents in respect of the acquisition of a subsidiary:

	RMB
Cash consideration paid	57,404,685
Cash and balances with financial institutions	(12,487,491)
	<hr/>
Net outflow of cash and cash equivalents in respect of the acquisition of a subsidiary	<u>44,917,194</u>

The operating results of MS (Yangzhou) Processing are not material since the date of acquisition.

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

45. Acquisition of businesses/a subsidiary (continued)

On 28 April 2005, the Company entered into an acquisition agreement (the "Acquisition Agreement") with Magang Holding Construction Co. Ltd. ("Construction Company"), a wholly-owned subsidiary of Holding, to acquire its steel structure manufacturing and installation business and electrical and mechanical equipment installation business (the "Businesses"). The acquisition price, which amounted to approximately RMB150 million, was determined by reference to an asset appraisal report issued by an independent assets valuer, Jiangsu Talent Certified Public Accountants. In accordance with the terms of the Acquisition Agreement, for the period from 1 February 2005 to the effective date of the Acquisition Agreement, the Businesses were entrusted to the Construction Company for management and the profit and loss was assumed by the Company, which was not significant.

Net assets acquired:

	RMB
Bills receivable	100,000
Trade receivables	76,007,671
Other receivables	7,693,900
Prepayments	13,130,991
Inventories	152,240,510
Fixed assets cost	71,854,377
Less: Accumulated depreciation	(17,458,303)
Net book value	54,396,074
Construction materials	120,000
Construction in progress	49,735,199
Accounts payable	(113,420,805)
Deposits received	(82,241,475)
Staff welfare payable	(3,810,465)
Taxes payable	(1,228,776)
Other taxes payable	(41,673)
Other payables	(2,907,567)
	<u>149,773,584</u>
Cash paid	<u>149,773,584</u>

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

46. Non-cash assets and liabilities contributed by a minority shareholder

On 28 April 2006, the Company and Hefei Investment Holding Company Limited (“Hefei Investment Holding”) entered into a Venturers’ Agreement for the establishment of Ma Steel (Hefei) Iron & Steel Co. Ltd. (“Ma Steel (Hefei)”). Pursuant to the Venturers’ Agreement, the Company and Hefei Investment Holding hold 71% and 29% of equity interests in Ma Steel (Hefei), respectively.

On 10 May 2006, Ma Steel (Hefei) was established with a registered capital of RMB500,000,000. Pursuant to the articles and memorandum of Ma Steel (Hefei), its registered capital will be paid up by the Company and Hefei Investment Holding in two installments. Up to the balance sheet date, the Company has contributed cash of RMB237,495,000 to Ma Steel (Hefei) and Hefei Investment Holding has also contributed cash of RMB299,312,595 and certain assets (including certain prepaid land premiums and production equipment located in Hefei City used for the manufacture of iron and steel products) and liabilities amounting to a net liability value of RMB202,312,595 to Ma Steel (Hefei).

Details of the net liability value of RMB202,313,000 injected into Ma Steel (Hefei) by Hefei Investment Holding are as follows:

	Notes	RMB
Prepayments		26,635,700
Inventories		115,342,635
Fixed assets	10	602,287,638
Construction in progress	11	640,000
Intangible assets	12	154,104,000
Short term loan		(476,620,150)
Bills payable		(219,200,000)
Accounts payable		(290,311,383)
Deposits received		(102,410,482)
Accrued charges		(12,780,553)
		<u>(202,312,595)</u>

(Prepared under PRC Accounting Standards)
31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

47. Differences in financial statements prepared under PRC and Hong Kong Accounting Standards

Ernst & Young is responsible for the audit of financial statements prepared under Hong Kong Accounting Standards.

Effects on net profit and the shareholders' equity arising from the material differences between the consolidated financial statements prepared under PRC and Hong Kong Accounting Standards are summarised as follows:

	Notes	2006 RMB'000	2005 RMB'000
Net profit			
Net profit from ordinary activities attributable to shareholders under Hong Kong Accounting Standards		2,394,652	2,909,943
Add back:			
Employee bonus and welfare fund	(ii)	6,547	4,616
Deduct:			
Deferred tax income	(i)	(74,861)	(18,441)
Recognition of deferred income	(iii)	(49,752)	(48,498)
Net profit from ordinary activities attributable to shareholders under PRC Accounting Standards		2,276,586	2,847,620

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

47. Differences in financial statements prepared under PRC and Hong Kong Accounting Standards (continued)

	Notes	31 December 2006 RMB'000	31 December 2005 RMB'000
Shareholders' equity			
Shareholders' equity under Hong Kong Accounting Standards		20,461,771	18,514,504
Add back:			
Deferred tax liabilities	(i)	754	–
Deferred income	(iii)	588,569	585,369
Deduct:			
Deferred tax assets	(i)	–	(53,175)
Recognition of deferred income	(iii)	(140,235)	(90,483)
Provision for furnace relining costs	(iv)	(74,499)	(74,499)
Recognition of equity component of bonds with warrants	(v)	(733,019)	–
Direct issue cost of bonds with warrants recognised as deduction from equity component	(v)	18,766	–
Shareholders' equity under PRC Accounting Standards		20,122,107	18,881,716

(i) Deferred tax

Under PRC accounting standards and regulations, the Company adopted the tax payable method in which the current year's tax payable represents the current year's income tax expense and does not recognise the effect of timing differences on income tax. Thus, no deferred tax was recognised as at 31 December 2005 and 31 December 2006.

Under HKAS 12, deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Accordingly, deferred tax liabilities recognised as at 31 December 2006 amounted to approximately RMB0.75 million (2005: deferred tax assets approximately RMB53.2 million). The movement in the deferred tax resulted in a deferred tax income of approximately RMB74.9 million in the current year (2005: approximately RMB18.4 million).

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

47. Differences in financial statements prepared under PRC and Hong Kong Accounting Standards (continued)

(ii) Employee bonus and welfare fund

Pursuant to the articles of association and the resolutions of the boards of directors of certain subsidiaries of the Company, these subsidiaries have to make appropriations to the employee bonus and welfare fund. During the year, the Group's share of the appropriation of these subsidiaries in respect of the employee bonus and welfare fund amounted to approximately RMB6.5 million (2005: approximately RMB4.6 million).

Under PRC accounting standards and regulations, it is an appropriation of profit and is deducted from net profit for the year.

Under Hong Kong Accounting Standards, the appropriation to the employee bonus and welfare fund is accounted for as staff cost and is charged to the current year's income statement.

(iii) Deferred income

Government grants for specific construction projects are accounted for as specific payables under PRC Accounting Standards, whereas under Hong Kong Accounting Standards, such grants are accounted for as deferred income.

Under PRC accounting standards and regulations, upon completion of the subsidised construction projects, the costs incurred are recognised as property, plant and equipment and the utilised portion of specific payables thereof is transferred to the capital reserve. As at 31 December 2006, accumulated specific payables transferred to the capital reserve amounted to approximately RMB589 million (31 December 2005: approximately RMB585 million).

Under Statement of Standard Accounting Practice No. 20, *Accounting for government grants and disclosure of assistance* ("HKSSAP 20"), upon completion of the subsidised construction projects, deferred income is released to the income statement over the expected useful lives of the relevant assets by equal annual instalments. During the year, certain subsidised construction projects, with government grants of approximately RMB3.2 million received in the current and prior year, were completed. As at 31 December 2006, accumulated deferred income amounting to approximately RMB589 million (31 December 2005: approximately RMB585 million) should be released to the income statement over the expected useful lives of the relevant assets. Deferred income of approximately RMB49.8 million (2005: approximately RMB48.5 million) was released to the current year's income statement. As at 31 December 2006, the accumulated deferred income released amounted to approximately RMB140.2 million (31 December 2005: approximately RMB90.5 million).

Notes to Financial Statements (Continued)

(Prepared under PRC Accounting Standards)

31 December 2006

V. MAJOR NOTES TO FINANCIAL STATEMENTS (CONTINUED)

47. Differences in financial statements prepared under PRC and Hong Kong Accounting Standards (continued)

(iv) Furnace relining costs

Under the PRC Accounting Standard *Fixed Assets* issued on 1 January 2002, repair and maintenance costs incurred on property, plant and equipment should be charged to the income statement as and when incurred. Hence, from 1 January 2002 onwards, the Company no longer accrued for the provision for furnace relining costs. The balance of provision for furnace relining costs, amounting to approximately RMB120.3 million as at 31 December 2001, will be utilised when furnace relining costs are actually incurred. During the year, no furnace relining costs were incurred (2005: Nil), and the remaining provision as at 31 December 2006 amounted to approximately RMB74.5 million (2005: approximately RMB74.5 million).

Under HKAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, furnace relining costs are recognised as and when incurred starting from 1 January 2001. The balance of provision for furnace relining costs of approximately RMB124 million as at 31 December 2000 was derecognised retrospectively by a prior year adjustment.

(v) Bonds with warrants

Under the PRC accounting standard and regulations, bonds with warrants were recorded as bonds payable at a nominal value of RMB5,500 million at the issue date. Besides, the direct issue cost of bonds with warrants was capitalised in construction in process.

Under HKAS 32, *Financial instruments: Disclosure and Presentation*, the bonds with warrants are determined as a compound financial instrument and should be separately classified as financial liability component and equity component. At the issue date, the carrying amount of the liability component was determined to be approximately RMB4,767 million by measuring the fair value of a similar liability that does not have an associated equity component, and the equity component is then determined to be approximately RMB733 million by deducting the fair value of the financial liability from the fair value of the compound financial instrument as a whole of RMB5,500 million. Besides, the direct issue cost of the bonds with warrants was allocated between the separate components and the amount recognised as deduction from equity is approximately RMB18.8 million.

(Prepared under PRC Accounting Standards)

31 December 2006

VI. SEGMENT INFORMATION

No business segment information is presented as over 90% of the Group's revenue is derived from one business segment, which is the manufacture and sale of iron and steel products and related by-products.

Geographical segmental analysis is presented based on the geographical location of customers. The Group's assets and liabilities are almost entirely situated in the PRC and accordingly, no information on geographical segment assets, liabilities and capital expenditure is provided.

	2006			2005		
	PRC RMB'000	Overseas RMB'000	Total RMB'000	PRC RMB'000	Overseas RMB'000	Total RMB'000
Principal operating income	<u>30,800,297</u>	<u>3,519,577</u>	<u>34,319,874</u>	<u>30,035,284</u>	<u>2,047,812</u>	<u>32,083,096</u>
Profit from principal operating activities	<u>3,546,077</u>	<u>603,133</u>	<u>4,149,210</u>	<u>4,363,466</u>	<u>206,016</u>	<u>4,569,482</u>

VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS

1. Related party involving control relationship

Name	Registered address	Principal activities	Relationship with the Company	Nature	Legal representative
Holding	Maanshan City, Anhui Province	Mining & sorting of mineral products; construction engineering design; construction; property development; integrated technology service; domestic trading; food & beverages; production services; mechanical & electrical equipment manufacturing and metal products manufacturing	Ultimate holding company	Limited company	Gu Jianguo

As at 31 December 2006, Holding owned 60.08% of the Company's total share capital. Thus all subsidiaries of Holding become the Company's related parties.

2. Registered capital of related party involving control relationship and related changes

Name	At 1 January 2006 RMB'000	Increase during the year RMB'000	Decrease during the year RMB'000	At 31 December 2006 RMB'000
Holding	<u>6,298,290</u>	<u>—</u>	<u>—</u>	<u>6,298,290</u>

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

3. Stock or equity interest held by related party who could control the Company and the changes

Name	At 1	Ratio	Increase	Ratio	Decrease	Ratio	At 31	Ratio
	January		during		during		December	
	2006	%	the year	%	the year	%	2006	%
	RMB'000		RMB'000		RMB'000		RMB'000	
Holding	4,082,330	63.24	-	-	(204,000)	(3.16)	3,878,330	60.08

4. Related parties without control relationship

Information on related parties who carried out related party transactions with the Company but do not involve any control relationship:

Name	Relationship with the Company
馬鋼集團建設有限責任公司	Subsidiary of Holding
馬鋼集團建築路橋有限責任公司	Subsidiary of Holding
馬鋼集團南山礦業有限責任公司	Subsidiary of Holding
馬鋼集團姑山礦業有限責任公司	Subsidiary of Holding
馬鋼(集團)控股有限公司桃冲礦業公司	Subsidiary of Holding
馬鋼集團設計研究院有限責任公司	Subsidiary of Holding
馬鋼集團康泰置地發展有限公司	Subsidiary of Holding
馬鋼集團康泰建安實業有限公司	Subsidiary of Holding
馬鋼集團力生有限責任公司	Subsidiary of Holding
馬鋼集團實業發展有限責任公司	Subsidiary of Holding
馬鋼神馬冶金有限責任公司	Subsidiary of Holding
馬鋼集團鋼渣綜合利用有限責任公司	Subsidiary of Holding
馬鋼實業生興爐料加工有限責任公司	Subsidiary of Holding
安徽馬鋼比亞西焊網有限公司	Subsidiary of Holding
馬鋼運動用品有限責任公司	Subsidiary of Holding
馬鞍山市聯營乙炔廠	Subsidiary of Holding
馬鞍山馬鋼永固螺絲製品有限公司	Subsidiary of Holding
馬鋼集團動力機電安裝有限責任公司	Subsidiary of Holding
馬鋼(集團)控股有限公司再就業勞務分公司	Subsidiary of Holding
馬鋼(集團)控股有限公司有線電視中心	Subsidiary of Holding
馬鋼(集團)控股有限公司通訊技術服務部	Subsidiary of Holding
馬鋼(集團)控股有限公司馬鋼日報社	Subsidiary of Holding
馬鋼(集團)控股有限公司安冶機械廠	Subsidiary of Holding
馬鞍山馬鋼嘉華商品混凝土有限公司	Subsidiary of Holding

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

4. Related parties without control relationship (continued)

Information on related parties who carried out related party transactions with the Company but do not involve any control relationship (continued):

Name	Relationship with the Company
馬鞍山市華鑫軋鋼廠	Subsidiary of Holding
深圳粵海馬鋼實業有限公司	Subsidiary of Holding
馬鞍山博力建設監理有限公司	Subsidiary of Holding
馬鋼(集團)控股有限公司高級技工學校	Subsidiary of Holding
馬鋼(集團)控股有限公司醫院	Subsidiary of Holding
馬鋼(集團)控股有限公司安徽冶金科技職業技術學院	Subsidiary of Holding
馬鋼(集團)控股有限公司黨校	Subsidiary of Holding
濟源市金馬焦化	Associate of the Group
滕州盛隆煤焦化	Associate of the Group
馬鞍山港口公司	Associate of the Group
馬鋼智能停車	Associate of the Group
BOC-Ma Steel	Jointly control entity of the Group

5. (1) The following is a summary of the significant transactions carried out between the Group and its related parties during the year:

	Notes	2006 RMB	2005 RMB
Transactions with Holding and its subsidiaries:			
Purchases of iron ore	(i)	1,631,201,228	1,408,067,891
Fees paid for welfare, support services and other services	(ii), (iii)	194,496,697	206,210,276
Rental expenses	(iii)	36,250,000	36,250,000
Agency fee paid	(iii)	4,092,780	3,784,137
Purchases of fixed assets and construction services	(iii)	295,468,496	266,777,687
Fees received for the supply of utilities, services and other consumable goods	(iii)	(23,220,822)	(27,496,787)
Sale of steel products and related by-products	(iii)	(8,950,704)	(8,478,679)
Acquisition of businesses	(iv)	—	149,773,584
Transactions with associates of the Group:			
Purchases of coke	(v)	1,085,124,812	598,732,282
Loading expenses	(v)	75,036,389	40,076,344
Transactions with a JCE of the Group:			
Rental income	(vi)	(1,250,000)	(1,250,000)
Construction fee income	(vi)	(2,925,929)	(7,440,000)

Notes to Financial Statements (Continued)

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

5. (1) The following is a summary of the significant transactions carried out between the Group and its related parties during the year (continued):

- (i) The terms for the purchases of iron ore from Holding were conducted in accordance with an agreement dated 9 October 2003 entered into between the Company and Holding.
 - (ii) The terms for the provision of certain services, including on-the-job training, food and sanitary services, environmental and hygiene services and maintenance of roads and landscaping services were conducted in accordance with a services agreement dated 9 October 2003 entered into between the Company and Holding.
 - (iii) The other transactions with Holding and its subsidiaries were conducted on terms mutually agreed between the Company and the related parties.
 - (iv) The Company acquired the steel structure manufacturing and installation business and the electrical and mechanical equipment installation business from a wholly-owned subsidiary of Holding for a cash consideration of approximately RMB150 million in 2005, as further detailed in Note V point 45 to the financial statements.
 - (v) These transactions were made between the Group and 濟源市金馬焦化, 滕州盛隆煤焦化, 馬鞍山港口公司 and 馬鋼智能停車 and were conducted in accordance with the terms mutually agreed between them.
 - (vi) These transactions were made between the Group and BOC-Ma Steel and were conducted in accordance with the terms mutually agreed between them.
- (i), (ii), (iii), (v) and (vi) of the above transactions were carried out in the normal course of business of the Group.

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

- (2) Holding has guaranteed certain bank loans of the Group and bonds with warrants up to approximately RMB15 billion (2005: approximately RMB4.8 billion) as at the balance sheet date at nil consideration, as further detailed in Note V point 24, 25 and 26 to the financial statements.
- (3) Further details on balances with Holding and its subsidiaries, and the Group's associates are set out in Note VII point 6.

6. Receivable from/payable to related parties

	31 December 2006 RMB	31 December 2005 RMB	Details
Prepayments:			
馬鋼集團建設有限責任公司	26,328,100	2,467,871	Trade and construction fee
Others	1,018,542	581,147	
Total	27,346,642	3,049,018	

Notes to Financial Statements (Continued)

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

6. Receivable from/payable to related parties (continued)

	31 December 2006 RMB	31 December 2005 RMB	Details
Accounts payable:			
Holding	136,339,089	106,906,075	Construction fee, Payment for iron ore, supporting service fee and retirement fund
馬鋼集團建設有限責任公司	21,610,018	29,168,313	Construction and maintenance fees
馬鋼集團建築路橋有限責任公司	25,938,446	17,219,156	Construction and maintenance fees
馬鋼集團康泰建安實業有限公司	568,153	678,295	Construction fee
馬鋼集團力生有限責任公司	1,943,127	3,557,418	Construction fee
馬鋼集團實業發展有限責任公司 潤滑油分公司	2,954,930	3,049,623	Trade
馬鋼集團鋼渣綜合利用有限責任公司	232,785	9,904	Trade
馬鞍山市聯營乙炔廠	22,736	218,729	Processing fee
馬鋼集團南山礦業有限責任公司	1,117,338	3,800,806	Trade
馬鋼集團姑山礦業有限責任公司	-	2,920,165	Trade
馬鋼(集團)控股有限公司桃冲礦業公司	2,255,132	-	Trade
滕州盛隆煤焦化	368,571	150,771	Trade
濟源市金馬焦化	469,100	92,788	Trade
馬鞍山港口公司	6,524,273	8,234,474	Loading expenses
Others	4,472,961	3,322,360	
Total	<u>204,816,659</u>	<u>179,328,877</u>	

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VII. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (CONTINUED)

6. Receivable from/payable to related parties (continued)

	31 December 2006 RMB	31 December 2005 RMB	Details
Trade receivables:			
馬鋼集團建設有限責任公司	6,406,519	27,325,799	Trade and electricity fee
馬鋼集團康泰置地發展有限公司	–	1,048,877	Trade
馬鞍山馬鋼嘉華商品混凝土有限公司	3,063,581	3,217,616	Trade
Others	<u>963,912</u>	<u>772,495</u>	
Total	<u><u>10,434,012</u></u>	<u><u>32,364,787</u></u>	
Deposits received:			
Holding	44,200,000	–	Construction fee
馬鋼集團建設有限責任公司	9,144,804	–	Construction fee
馬鋼集團姑山礦業有限責任公司	59,156,440	55,662,819	Trade
安徽馬鋼比亞西焊網有限公司	5,652,992	9,106,633	Trade
Others	<u>1,595,861</u>	<u>2,622,943</u>	
Total	<u><u>119,750,097</u></u>	<u><u>67,392,395</u></u>	
Dividends payable:			
Holding	<u><u>400,000,000</u></u>	–	Dividend
Other long term liability:			
Holding	<u><u>400,000,000</u></u>	<u><u>400,000,000</u></u>	Dividend

Except for other long term liability due to Holding which is interest-free, unsecured and contracted to be repaid after 1 January 2008, the balances with related parties are interest-free, unsecured and have no fixed terms of repayment.

Notes to Financial Statements (Continued)

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VIII. CONTINGENT LIABILITIES

As at 31 December 2006, the Company had granted guarantees amounting to approximately RMB7,728 million (31 December 2005: approximately RMB7,795 million) to banks in connection with facilities granted to its subsidiaries.

Save as aforesaid, the Group and the Company had no significant contingent liabilities as at the balance sheet date.

IX. COMMITMENTS

Capital commitments

- (1). The commitments for capital expenditure for buildings and structures, plant and equipment as at the balance sheet date were as follows:

	Group		Company	
	31 December 2006 RMB'000	31 December 2005 RMB'000	31 December 2006 RMB'000	31 December 2005 RMB'000
Authorised, but not contracted for	5,217,641	11,044,413	4,469,724	11,042,318
Contracted, but not provided for	4,093,227	9,835,947	4,051,077	9,828,677
Total	<u>9,310,868</u>	<u>20,880,360</u>	<u>8,520,801</u>	<u>20,870,995</u>

- (2). The commitments for capital contributions at the balance sheet date were as follows:

	Group		Company	
	31 December 2006 RMB'000	31 December 2005 RMB'000	31 December 2006 RMB'000	31 December 2005 RMB'000
Contracted, but not provided for	<u>13,500</u>	<u>7,668</u>	<u>172,947</u>	<u>34,668</u>

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IX. COMMITMENTS (CONTINUED)

Capital commitments (continued)

- (3). The Group's and Company's share of the capital commitments of the Jointly Control Entity, which is not included in note (1) above, in respect of capital expenditure for buildings and structures, plant and equipment at the balance sheet date were as follows:

	Group and Company	
	31 December	31 December
	2006	2005
	RMB'000	RMB'000
Authorised, but not contracted for	10,952	31,202
Contracted, but not provided for	39,351	148,218
	50,303	179,420

- (4). The Group's and Company's share of other commitments of the Jointly Control Entity:

	Group and Company	
	31 December	31 December
	2006	2005
	RMB'000	RMB'000
Contracted, but not provided for	5,000	–

Notes to Financial Statements (Continued)

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X. POST BALANCE SHEET EVENTS

- (1). The Company proposed to issue 20,000,000 short term commercial papers with a nominal value of RMB100 each, amounting to RMB2 billion in total. The short term commercial papers will be issued at par and have a maturity of one year from the date of issuance. The proceeds from the issue will be used to finance the working capital of the Company.

The proposal of issuance has been approved in the extraordinary general meeting held on 1 February 2007. Up to reporting date, the proposal is pending for approval of the People's Bank of China.

- (2). During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law ("the New Corporate Income Tax Law") was approved and will become effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. Since the detailed implementation and administrative rules and regulations have not yet been announced, the future financial impact of the New Corporate Income Tax Law to the Group cannot be reasonably estimated at this stage.

XI. COMPARATIVE AMOUNTS

Certain comparative amounts have been reclassified to conform with the current year's presentation.

XII. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved by the board of directors on 17 April 2007.