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## Chairman's Statement

Dear Shareholders,

I am pleased to present the Annual Report of the Group for the year ended 31 December 2006 and extend my gratitude to all the shareholders on behalf of the Board of China Special Steel Holdings Company Limited.

### MARKET HIGHLIGHTS

06 | In 2006, the bearing steel market in PRC, from January to December, recorded a total production of approximately 2.07 million tonnes. Compared with that of 2005, the total production increased by approximately 100 thousand tonnes, representing a year-on-year increase of 5.2%. There was a slightly downward adjustment in average selling price during 2006 and the price became stable at the year end. With the impact of reduction in the rebate on export of some steel products, the overall momentum became moderate. On the other hand, stainless steel market performed well with strong momentum in price. According to the statistics from the China Special Steel Association of Enterprises, output of stainless steel billets has approached 5.3 million tonnes in 2006, representing a year-on-year increase of 68% which has exceeded that of Japan and become the highest in the world. Among the stainless steel products, 62.4% is nickel-chromium stainless steel series.

### SATISFACTORY RESULTS

In 2006, the Group's major products was still bearing steel. Although the growth in bearing steel market in PRC slowed down, the growth in Group's growth in sale volume still outperformed the market average. The Group's turnover increased by 5% from RMB837.5 million in 2005 to RMB879.8 million in 2006. When compared to 2005, the sales volume of special steel products increased by 13% to approximately 275,341 tonnes in year 2006. It was another successful year of creating value and strengthening the foundations for growth. We have continuously reduced the production cost and further improve the gross margin from 19% to 21% in 2006. Even though there was a suspension of production for two months in the first half of 2006 due to the equipment refinement project and additional expenses were incurred in the projects of production capacity enhancement, product development and other basic administration expenses for a listing company, we still maintain an operation profit before tax and other income similar to last year.

## **INCREASE IN CAPACITY**

Aiming at enhancing the production capacity and improvement in the production efficiency, the final stage of equipment refinement project has completed in July 2006. Furthermore, the major transactions of capital injection in Anyang Steel Group Luoyang Anlong Steel Company Limited ("Anlong Steel") were completed and Anlong has been formally renamed as Luoyang Yongan Special Steel Company Limited ("Yongan Special Steel") on 5 January 2007. The Group has gradually increased its designed annual production capacity for special steel from 500,000 tonnes to 800,000 tonnes and for iron-making from 400,000 tonnes to 700,000 tonnes. The synergy effect and increased capacity will allow the Group to further enhance the economy of scales through mass production.

## **PRODUCT DEVELOPMENT**

In view of the potential growth in demand for stainless steel and the highest added value of stainless steel among other special steel products, the Group has successfully produced stainless steel base material in 2006 after the arrangement, research and development in 2005. Stainless steel base material is a kind of purified nickel pig iron which is a base material for the production of stainless steel and has a higher profit margin than bearing steel and spring steel. To leverage on our expertise in the steel making, metallurgy and product development, we shall further develop other high margin special steel products in the future to meet the market needs.

## **PROSPECTS FOR 2007**

In the first quarter of 2007, with the existing production facilities of the Group, the Company starts to sell stainless steel base material to major stainless steel manufacturers, including Taiyuan Iron & Steel (Group) Company Ltd., Boashan Iron & Steel Co., Ltd. and POSCO. This will also be the Group's strategy to gain access to a stable supply of iron and nickel at a reasonable price and to rebalance the product mix in order to cope with the market trends, i.e. reallocating more resources from producing bearing steel to producing more stainless steel related products. This will result in an expansion in the Group's product-variety and in turn allowing the Group to enlarge its clientele and profit margin. The production and sales of the Group during the first quarter in 2007 was satisfactory. The ex-factory output of stainless steel base materials has reached 39,000 tonnes. In the first quarter, the average selling price, excluding VAT, of stainless steel base materials was RMB8,300 per tonne. Following the production of stainless steel materials with richer nickel content (over 3 per cent.) and the surging price of nickel, the latest selling price, excluding VAT, was nearly

RMB10,000 per tonne. Currently, the average monthly output of stainless steel base material exceeds 22,000 tonnes per month. The Group also plans to further increase the production capacity of the Group's facilities to meet the market demand and then further increasing turnover. All of these, will be beneficial to the Group's future business development.

Finally, I wish to thank all of those who contributed to the Group's successful implementation of corporate strategies and satisfactory result in 2006. I also wish all of our customers, shareholders and employees another prosperous and productive year in 2007.

**Dong Shutong**

*Chairman & CEO*

Hong Kong, 20 April 2007



# Dedication to Product Quality

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