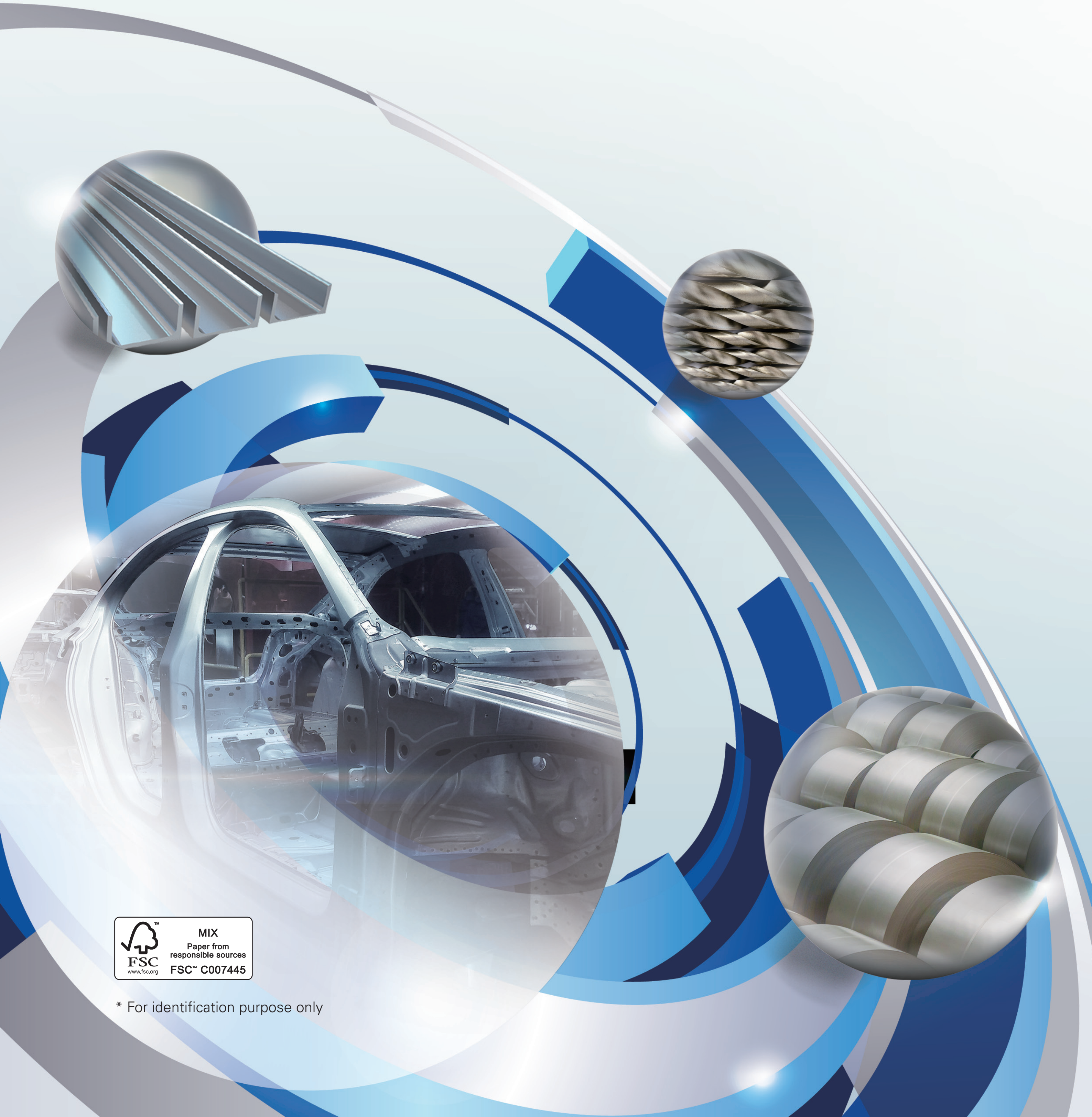
天工國際有限公司*

TIANGONG INTERNATIONAL COMPANY LIMITED

(incorporated in the Cayman Islands with limited liability)

Stock Code : 826

ANNUAL REPORT 2018



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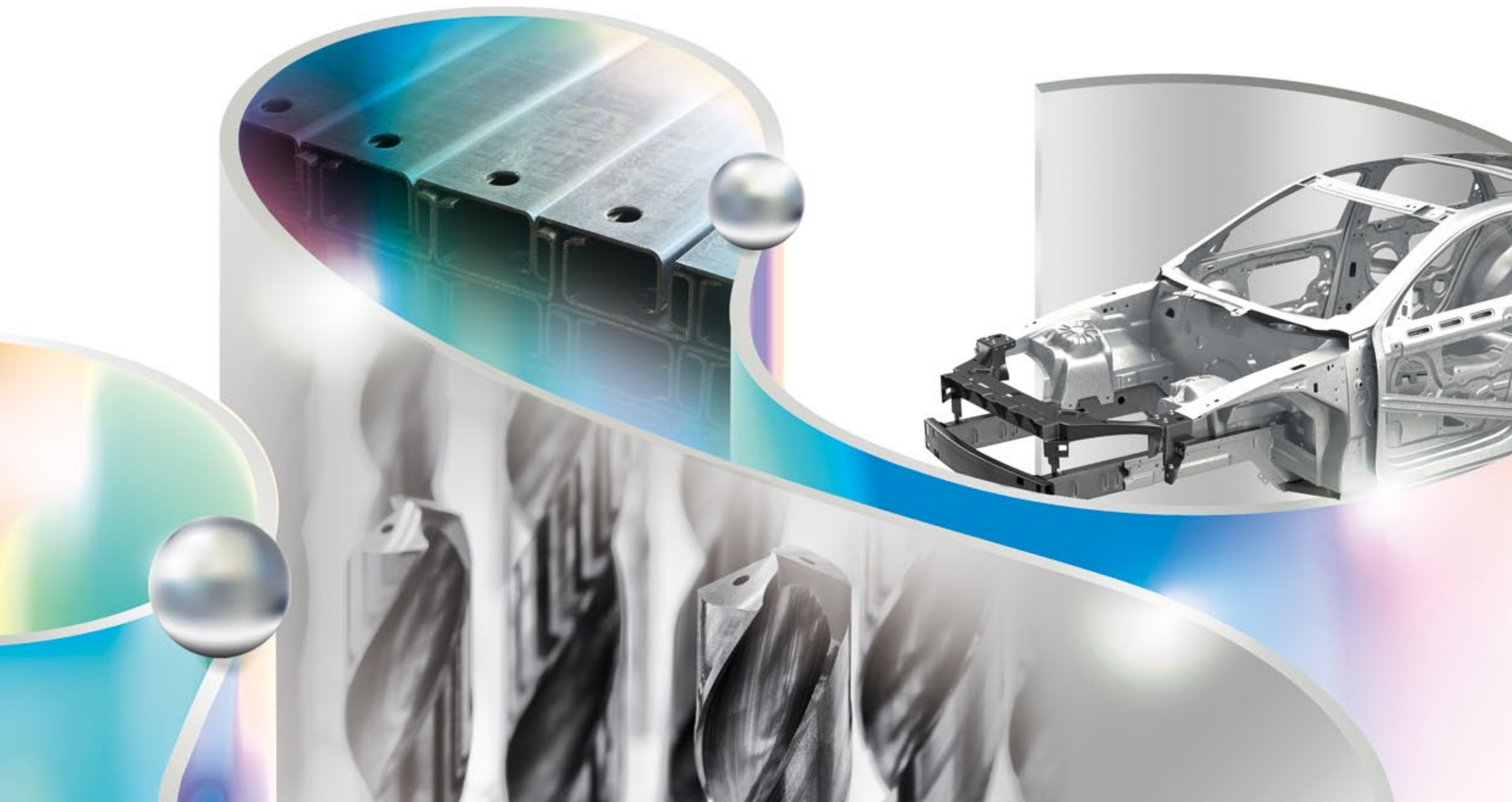
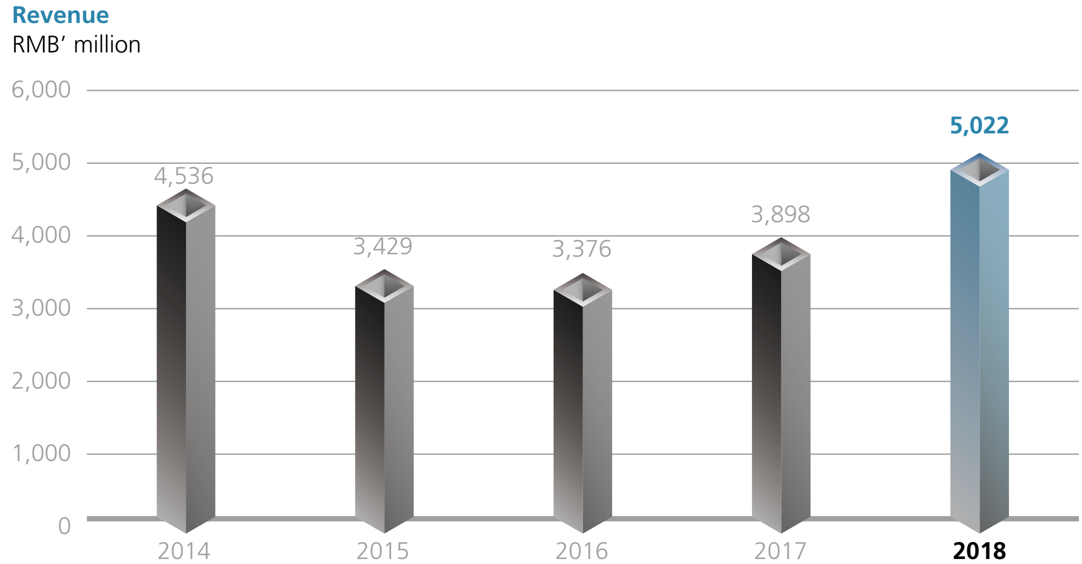
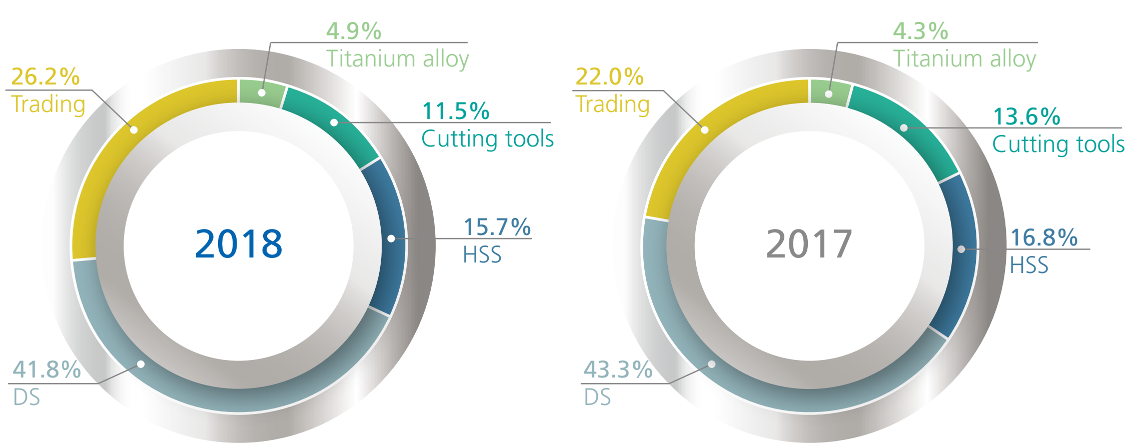


Financial Highlights

	2018	2017
Revenue (RMB'000)	**5,021,546**	3,898,443
Net profit for the year attributable to equity shareholders of the Company (RMB'000)	**258,835**	169,099
Basic earnings per share (RMB)	**0.106**	0.076
Proposed final dividend per share (RMB)	**0.0357**	0.0378



Revenue by Product Mix



Chairman's Statement

Leveraging on our dominating position in the market and advantage on costing and product range, we will strive to maintain growth and maximise returns to the shareholders of the Company.

Zhu Xiaokun *Chairman*

Dear Shareholders,

On behalf of the board of directors (the "Board") of Tiangong International Company Limited (the "Company", together with its subsidiaries, collectively the "Group"), I am pleased to present to you the annual results for the year ended 31 December 2018.

In respect of financial performance, the Group's annual revenue has exceeded RMB5 billion for the first time, reached RMB5.022 billion, representing an increase of 28.8% as compared to 2017. The increase was attributable to a growth of revenue in all segments of the Group. Comparing to that of 2018, gross profit has increased significantly by 32.6% to RMB661 million. Net profit attributable to equity shareholders of the Group has increased significantly by 53.1% to RMB259 million. The continuous growth of market demand, expansion in market share and the steady increase in selling price are the main contributors to the growth in gross profit margin. We believe that the Group's performance will further improve in the coming year.

During the year, National Bureau of Statistics has announced "Strategic Emerging Industries Key Products and Services Catalogue (2018)" with 39 types of advanced steel materials newly listed in the new materials category. High-performance die steel processing of the Group was ranked highly among the list. Since titanium alloy had also been included in the new materials category earlier, the established leading position of the Group in new materials field is strengthened. As the industry leader, the Group will uphold the spirit of craftsmanship to improve the qualities of products and achieve greater excellence.

To explore the international new materials market and develop powder metallurgy technology, the Group is intended to invest RMB500 million to establish the first domestic production line of die steel powder metallurgy, which aims at filling the gap in market and provides high-quality raw materials for automotive and aerospace industries. The first phase of the production line will be completed and operation will be commenced by December 2019. First phase of annual production capacity of powder metallurgy will reach up to 2,000 tons. With the trust and support of our customers, the Group has already received orders for related items.

The Group has also established the first Powder Metallurgy Institute in China with China Iron & Steel Research Institute Group. Funding will be devoted to research from specialist team and purchases of advance laboratory apparatus, in order to provide sufficient technical facilities and research capabilities to the development of powder metallurgy.

For overseas market, after the 15 months' review by the Department of Commerce of United States, the Group has become the only special steel export enterprise to receive a largely cut on countervailing duty from original 251% to 24.04%. This favorable ruling has further established the position of the Group's products in US and promoted the Group's competitiveness in international market. Furthermore, in order to keep pace with development of Belt and Road Initiative, the Group has established sales companies in countries and regions along the Belt and Road to promote quality products to more overseas markets.

Regarding the latest report of the leading global research centre, Steel & Metals Market Research, the Group is ranked third on global die steel producers, moving up one place from the previous report. Besides, the Group is ranked first globally for the 13th consecutive year and nationally for the 20th consecutive year in terms of annual production capacity of high-speed steel products

To strengthen and enhance the Group's competitiveness in the international market, the Group is actively exploring and preparing for the opportunities of acquisition of suitable overseas new materials enterprises. The Group is committed to acquiring local and overseas waste materials at low cost and improving production efficiency through sophisticated management to seek for further reduction on production cost.

In terms of marketing strategy, the Group will consistently increase the proportion of direct sales to minimise the dependence on distributors. On the other hand, the Group has set up online sales channel to sell own branded products to overseas consumers directly. Domestic online sales channels are also poised to launch. By establishing more direct sales channels, the intermediary cost could be reduced and leads to an improvement in the Group's gross profit margin.

Benefiting from the favorable policies from the government to manufacturing industry such as reduction on taxes and administrative fees, it is expected that the Group's profit margin will be further enhanced. Each business segment of the Group is clearly positioned and maturely developed. The Group will leverage our dominating position in the market and advantage on costing and product range, to strive for consistent growth and maximise the returns to the shareholders of the Company.

Finally, on behalf of the Board, I would like to express my sincere gratitude to our management and staff for their outstanding performance over the year, as their contribution was the key to the Group's success. I would also like to take this opportunity to cordially thank all shareholders, customers and business partners for their support and assistance.

Management Discussion and Analysis

Business and Market Review

Revenue

	For the year ended 31 December					
	2018		2017		Change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
DS	**2,098,110**	**41.8**	1,686,470	43.3	411,640	24.4
HSS	**782,015**	**15.6**	654,440	16.8	127,575	19.5
Cutting tools	**581,232**	**11.5**	530,212	13.6	51,020	9.6
Titanium alloy	**245,155**	**4.9**	168,164	4.3	76,991	45.8
Trading of goods	**1,315,034**	**26.2**	859,157	22.0	455,877	53.1
	5,021,546	**100.0**	3,898,443	100.0	1,123,103	28.8

DS — accounted for 41.8% of the Group's revenue in FY 2018

	For the year ended 31 December					
	2018		2017		Change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
DS						
Domestic	**944,542**	**45.0**	843,822	50.0	100,720	11.9
Export	**1,153,568**	**55.0**	842,648	50.0	310,920	36.9
	2,098,110	**100.0**	1,686,470	100.0	411,640	24.4

DS is manufactured using rare metals including molybdenum, chromium and vanadium, a type of high alloy special steel. DS is mainly used in die and mould casting as well as machining processing. Many different manufacturing industries require moulds, including automotive, high-speed railway construction, aviation and plastic product manufacturing industries.

During the year, revenue generated from DS segment increased by 24.4% to RMB2,098,110,000 (2017: RMB1,686,470,000). The Group's domestic revenue in DS increased by 11.9% to RMB944,542,000 (2017: RMB843,822,000) while export revenue increased by 36.9% to RMB1,153,568,000 (2017: RMB842,648,000).

The increase in revenue in DS segment was attributable to both an increase in market demand and the average selling prices of the products. Overall sales volume increased by 8.2% while average selling prices increased by 15.0%.

For the domestic market, an increase in average selling price was the main contributor to the increased revenue. Driven by the increased price of raw materials during the year, domestic average selling price recorded an increase of 11.4%.

For overseas markets, the continuous strong market demand stimulated an increase of 17.1% in sales volume. At the same time, average selling price increased by 17.0% due to (i) increased price of raw materials used by the Group; and (ii) ability to pass on raw material price increases to the Group's customers.

HSS — accounted for 15.6% of the Group's revenue in FY 2018

	For the year ended 31 December					
	2018		2017		Change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
HSS						
Domestic	**527,517**	**67.5**	456,089	69.7	71,428	15.7
Export	**254,498**	**32.5**	198,351	30.3	56,147	28.3
	782,015	**100.0**	654,440	100.0	127,575	19.5

HSS, manufactured using rare metals including tungsten, molybdenum, chromium, vanadium and cobalt, is characterised by greater hardness, heat resistance and durability. These attributes make HSS suited to such applications as cutting tools and in the manufacture of high-temperature bearings, high-temperature springs, internal-combustion engines and roll, with wide usage in specific industrial applications including automotive, machinery manufacturing, aviation, and electronics industries.

Both domestic and export revenue experienced an increase in 2018. The Group's domestic revenue increased by 15.7% to RMB527,517,000 (2017: RMB456,089,000), while export revenue increased by 28.3% to RMB254,498,000 (2017: RMB198,351,000).

Similar to DS, the increase in revenue in HSS was also attributable to both an increase in market demand and the average selling prices of the products. For HSS segment, the magnitude of the increase in average selling price is greater than that of the increase in market demand. The reason behind was that tungsten and cobalt are used in the production of HSS. The increase in price of tungsten and cobalt was more significant during the year. Overall sales volume increased by 5.0% while average selling prices increased by 13.8%.

For the domestic market, an increase of 3.2% was recorded in sales volume while the average selling price increased by 12.1%.

For overseas markets, market demand is relatively strong, which resulted in an increase of 11.1% in sales volume. Average selling price increased by 15.5% together with the increased price of raw materials used by the Group.

Cutting tools — accounted for 11.5% of the Group's revenue in FY 2018

	For the year ended 31 December					
	2018		2017		Change	
	RMB'000	%	RMB'000	%	RMB'000	%
Cutting tools						
Domestic	**219,871**	**37.8**	246,309	46.5	(26,438)	(10.7)
Export	**361,361**	**62.2**	283,903	53.5	77,458	27.3
	581,232	**100.0**	530,212	100.0	51,020	9.6

Cutting tools segment includes HSS and carbide cutting tools. HSS cutting tools products can be categorised into four major types — twist drill bits, screw taps, end mills and turning tools. All of these are used in industrial manufacturing. The two main types of HSS cutting tools manufactured by the Group are twist drill bits and screw taps. The Group's vertical integration extending from upstream HSS production to downstream HSS cutting tools production brought us a significant cost advantage over our peers. High end carbide tools manufactured by the Group mainly comprised of customised carbide tools.

Overall increase of 9.6% was recorded in the segment revenue of cutting tools. However, the domestic and overseas markets experienced a very different competition atmosphere.

The demand in the domestic market was mainly from the elementary products. Since the production technology was relatively simple, competition from small scale producers was strong. To prevent an unnecessary price war, the Group preferred to focus on the domestic mid-range market and overseas markets.

Domestic sales volume was reduced by 28.4% as a result of the change in the market focus policy. Since the product mix was shifted to mid-range products, the volume reduction was partially offset by an increase of 24.6% in average selling price.

In the overseas markets, since the demand was primarily from mid-range and higher end HSS and carbide cutting tools, production technology was crucial and competition was relatively less keen. The sales volume recorded an increase of 23.8%, which was the main contributor to the increase in export revenue of the segment.

Titanium alloy — accounted for 4.9% of the Group's revenue in FY 2018

	For the year ended 31 December					
	2018		2017		Change	
	RMB'000	**%**	RMB'000	%	RMB'000	%
Titanium alloy						
Domestic	**242,492**	**98.9**	165,990	98.7	76,502	46.1
Export	**2,662**	**1.1**	2,174	1.3	488	22.5
	245,155	**100.0**	168,164	100.0	76,991	45.8

The corrosion resistance nature of titanium alloy promoted the extensive applications of titanium alloy in various industries, including aerospace, chemical pipeline equipment, nuclear and ocean industries.

Demand for titanium products remained strong during the year. 37.8% increase in sales volume was recorded. At the same time, the price of sponge titanium increased during the year. As the major raw material of titanium alloy segment, the increased price of sponge titanium was passed on to our customers. Accordingly, average selling price also increased by 5.8% during the year. As a result, segment revenue increased by 45.8% to RMB245,155,000 (2017: RMB168,164,000).

Trading of goods

This segment involves the purchase and sales of general carbon steel products which were not within the Group's production scope. Instead of pursuing profitability, the Group intended to utilise their enriched sourcing resources in the supply chain to maintain the relationship with our existing customers.

Financial Review

Net profit attributable to equity shareholders of the Company increased by 53.1% from RMB169,099,000 in 2017 to RMB258,835,000 in 2018. The increase was mainly attributable to (i) increase in sales volume of the products of the Group's four core segments during the year ended 31 December 2018 due to increased market demand and market share; and (ii) the increased price of major raw materials used by the Group during the year ended 31 December 2018. Since the Group has the ability to pass on raw material price increases to its customers, there was an increase in the average selling price of the products of the Group's four core segments.

Revenue

Revenue of the Group for 2018 totalled RMB5,021,546,000, representing an increase of 28.8% as compared with RMB3,898,443,000 in 2017. All the segments of the Group experienced an increase during the year.

Cost of sales

The Group's cost of sales was RMB4,360,619,000 in 2018, representing an increase of 28.3% as compared with RMB3,399,980,000 in 2017, as a result of an increase in sales.

Gross margin

For 2018, the overall gross margin was 13.2% (2017: 12.8%). Set out below is the gross margin of our five segments in 2018 and 2017:

	2018	2017
DS	18.2%	16.3%
HSS	20.6%	19.1%
Cutting tools	13.9%	13.8%
Titanium alloy	15.2%	14.4%
Trading of goods	0.0%	0.2%

DS

The gross margin of DS increased from 16.3% in 2017 to 18.2% in 2018. During the year, the increase in the price of raw materials was passed on to our customers. Production utilisation was further enhanced by the increase in market demand. The Group was able to take advantage of the increase in selling price and cost savings. The gross margin was enhanced accordingly.

HSS

Similar to DS, the gross margin of HSS increased from 19.1% in 2017 to 20.6% in 2018. The increase was supported by improvements in both pricing and cost savings.

Cutting tools

The market for cutting tools is relatively mature and stable in recent years. The cutting tools segment retained a stable gross margin at 13.9% in 2018 (2017: 13.8%).

Titanium alloy

The gross margin of titanium alloy increased from 14.4% in 2017 to 15.2% in 2018. The improvement in gross margin of titanium alloy was mainly attributable to the combined effect of increased raw material prices passed on to customers and improved utilisation of production capacity.

Trading of goods

The gross margin of this segment remained stable at 0.0% (2017: 0.2%).

Other income

Other income decreased from RMB64,614,000 in 2017 to RMB42,467,000 in 2018. The main reason for the decrease was the reduced government grant. A total amount of RMB33,270,000, was received in 2018 (2017: RMB53,815,000).

Distribution expenses

Distribution expenses in 2018 were RMB105,000,000 (2017: RMB85,800,000), representing an increase of 22.4%. The increase was mainly attributable to the increase in sales volume and the increase in marketing and advertising expenditures. For 2018, distribution expenses as a percentage of revenue was 2.1% (2017: 2.2%).

Administrative expenses

Administrative expenses increased from RMB140,357,000 in 2017 to RMB155,475,000 in 2018. The increase was mainly due to the cost of the share-based payment expenses incurred during the year for the granting of 60,000,000 share options to the Directors and employees of the Group. For 2018, administrative expenses as a percentage of revenue was 3.1% (2017: 3.6%).

Other expenses

Other expenses increased significantly from RMB2,210,000 in 2017 to RMB40,755,000 in 2018. Due to the implementation of IFRS 9, the new "expected credit loss" model requires an ongoing measurement of credit risk associated with receivables and therefore recognises loss allowances earlier than that under the "incurred loss" model in IAS 39. Significant provision of loss allowance was recognised in 2018 which amounted to RMB35,374,000 (2017: RMB1,049,000). In addition, net foreign exchange losses of RMB2,471,000 was recognised by the Group in 2018 (2017: gain of RMB6,395,000 recognised in other income).

Net finance costs

The Group's finance income was RMB7,233,000 in 2018, representing an increase of RMB1,438,000, primarily due to an increase in the average bank deposit balance. The Group's finance expense was RMB142,071,000 in 2018, representing an increase of 20.2% from RMB118,205,000 in 2017. The increase was due to a higher level of average interest-bearing borrowing balances and increased average borrowing costs.

Income tax

As set out in Note 8 of the consolidated statement of profit or loss, the Group's income tax expense decreased by 68.7% from RMB43,396,000 in 2017 to RMB13,598,000 in 2018. The decrease in income tax expenses was mainly due to the exempted arrangement on withholding tax expenses on dividend distributed by the Group's PRC subsidiary in 2017 and 2018. Under new PRC tax rules, withholding tax expenses on dividends distributed by the Group's PRC subsidiary to foreign intermediate holding companies was temporarily exempted if the dividend distributed was reinvested to the PRC subsidiary.

Profit for the year attributable to equity shareholders of the Company

As a result of the factors set out above, the Group's share of profit increased by 53.1% from RMB169,099,000 in 2017 to RMB258,835,000 in 2018. The margin of profit attributable to equity shareholders of the Company increased from 4.3% in 2017 to 5.2% in 2018.

Total comprehensive income for the year attributable to equity shareholders of the Company

For 2018, total comprehensive income for the year attributable to equity shareholders of the Company was RMB247,228,000 (2017: RMB154,544,000) after taking into account foreign currency translation differences and fair value adjustments on equity investments.

During the year, the Group debited to other comprehensive income a foreign currency translation difference of RMB3,562,000 (2017: credited RMB4,825,000) related to translation of financial statements of Hong Kong subsidiaries and overseas equity accounted investees.

The Group also recognised a fair value loss in the consolidated statement of profit or loss and other comprehensive income of RMB8,045,000 (2017: loss of RMB19,380,000) on its equity investments.

Other financial assets

Other financial assets held by the Group included Bank of Jiangsu, Xiamen Chuangfeng Yizhi Investment Management Partnership, Nanjing Xiaomuma Technology Co., Ltd. and JM Digital Steel Inc. All of these investments were stated at their fair value as at 31 December 2018. The total fair value loss, net of tax, of RMB8,045,000 (2017: RMB19,380,000) was recorded in other comprehensive income during the year.

Trade and bills receivables

Trade and bills receivables increased from RMB1,708,023,000 in 2017 to RMB1,999,111,000 in 2018, which was mainly due to the expansion of sales. During the year, loss allowance of trade receivables increased by RMB67,509,000, which was mainly the result of adopting IFRS 9 where estimate of credit losses was required to be recognised earlier than that under IAS 39.

Outlook

Operating Environment

In the past year, although the China-US trade war has been raging, and some of the Group's products have been listed as dutiable items, the revenue of the Group's overseas markets had not been affected at all. The sales volume to the US has not gone down but up, which has fully reflected that the quality of the Group's products is internationally recognised and the Group has gained the trust and support from overseas customers. Therefore, despite the uncertainty in global economic environment, the demand of the customers is still steady.

Product Development Strategy

The Group strives to explore high-end markets to increase profits. After the restructuring of the factory area in Danyang, Jiangsu, the Group is fully committed to develop the powder metallurgy project. The first Powder Metallurgy Institute in Mainland China was established at the end of last year jointly by the Group and China Iron & Steel Research Institute Group. It aims to develop high-quality metal powder products comparable to international advanced level. The Group could enter the high-end market by setting up a powder metallurgy production line to improve the technical level of the Group's products and meet the high specification requirements of aerospace industry and 3D printing etc.

The competition in the high-end market is relatively moderate with fewer competitors. It is conducive to the increase of customers' reliance and the stability of the Group's sales base. By avoiding vicious price competition in the low-end market, the Group would be able to improve the gross profit margin.

With the focus on entering the high-end market, the Group has made efforts to automate its production systems in recent years. Apart from enhancing the precision of products, it also reduces labour cost and speeds up the production process.

Marketing Strategy

The Group has strengthened its direct sales channels to minimise the dependence on distributors used to be in this industry. During the year, the proportion of enterprise customers through direct sales increased. Increasing the direct sales channel would help reduce distribution costs and improve the Group's gross profit margin. Meanwhile, customers would enjoy lower purchase prices. This mutual beneficial cooperation with customers would achieve a win-win situation.

By eliminating the barrier of distributors, the Group could enhance its understanding of customer needs, such as the product specifications and requirements of post-processing. The Group would be able to adjust the products accordingly and ensure that the products would meet market needs. The financial stability of the direct sales customers and their reliance on suppliers are generally higher than distributors. It would be beneficial to the stability of the Group's business environment.

Raw Materials Supply Overview

With the supply-side reform proposed by the PRC government, the overcapacity in rare metals industry has been resolved and small-scale suppliers have been eliminated. By reducing the adverse price competition, the price of rare metals keeps rising steadily. Since the cost of special steel products which rare metals are used as raw material could be passed to customers, the Group would be able to adjust its price and improve the gross margin despite the upward pricing trend of raw materials.

Our Mission

The Group believes that innovation and advancements are the best way to remain competitive and to realise the true value of the Group's businesses.

Last but not least, we re-affirm that maximisation of shareholder value, whilst adhering to the highest standards of corporate governance is always our top priority.

Forward Looking Statements

This management discussion and analysis contains certain forward looking statements with respect to the financial condition, results of operations and business of the Group. These forward looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements.

Forward looking statements involve inherent risks and uncertainties. Readers including shareholders and investors should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward looking statement.

Placing and Use of Proceeds

The Group invited two strategic investors, BAIC Group Industrial Investment Co., Ltd. and Jiangsu Shagang Group Co., Ltd. to subscribe for an aggregate of 300,000,000 shares at the placing price of HK$1.60 per share. The placing of the 300,000,000 shares was completed on 11 May 2018 with the net proceeds of HK$477.8 million representing a net issue price of approximately HK$1.59 per share. The market price of the placing shares was HK$1.78 per share as quoted on the Stock Exchange of Hong Kong on 27 April 2018, the date when the terms of the placing agreement were fixed. The proceeds from the placing has been used as follows:

Intended use of proceeds from the placing		Actual use of proceeds (as at 31 December 2018)	Proposed use of the remaining unutilised proceeds (as at 31 December 2018)
(i)	Construction of powder metallurgy production facilities	HK$33.1 million was used in acquiring machinery for the metal metallurgy production line	The Group plans to fully utilise the balance of HK$23.6 million for the construction of powder metallurgy production facilities
(ii)	Replenishment of Group's working capital to procure raw materials and meet any cashflow requirements that may arise from the daily operations	HK$421.1 million was used as working capital and for daily operation, including payment of electricity, staff salaries and procurement of raw materials	The remaining unutilised proceeds was nil

Liquidity and Financial Resources

As at 31 December 2018, the Group's current assets included cash and cash equivalents of RMB583,235,000, inventories of RMB1,994,287,000, trade and other receivables of RMB2,351,841,000, pledged deposits of RMB464,500,000 and time deposits of RMB717,414,000. As at 31 December 2018, the interest-bearing borrowings of the Group were RMB3,183,779,000 (2017: RMB2,993,292,000), RMB2,284,602,000 of which was repayable within one year and RMB899,177,000 of which was repayable after more than one year. The Group's adjusted net debt-to-equity ratio, which is calculated based on adjusted net debt (defined as total interest-bearing borrowings plus unaccrued proposed dividends, less cash and cash equivalents) divided by adjusted capital (comprising all components of equity, less unaccrued proposed dividends) as at 31 December 2018, was 56.9% (2017: 67.8%).

The increase in borrowings was mainly attributable to the increased cash demand as a result of expansion of production and sales in the DS and HSS segments. As at 31 December 2018, borrowings of RMB2,112,000,000 were in RMB, USD56,705,916 were in USD, EUR66,712,271 were in EUR and HKD181,560,200 were in HKD. The borrowings of the Group were subject to interest payable at rates ranging from 0.90% to 5.22% per annum. There is no seasonality in borrowing requirements of the Group. The Group did not enter into any financial instruments to hedge itself against risks associated with interest rates and foreign currency exchange fluctuations.

During the year, net cash generated from operating activities was RMB810,899,000 (2017: RMB215,006,000). Better utilisation of bills payable enhanced the credit period obtained from the suppliers. The maturity period of the Group's bills payable were six months or twelve months from date of issuance. These lengthened credit periods and better credit control on trade receivables enhanced the net cash generated from operating activities for the year.

Cash Conversion Cycle

The cash conversion cycle, calculated as turnover days over inventory, plus turnover days over trade receivables, minus turnover days of trade payables, attempts to measure the amount of time each net input dollar is tied up in the production and sales process before it is converted into cash through sales to customers. It is important to manufacturers because it measures the efficiency of their capital chain management.

The Group's turnover days of inventory for 2018 was 163 days (2017: 204 days). The relatively long turnover days of inventory is common in the special steel industry due to the complex production process. The improved turnover days of inventory was mainly due to the more effective and efficient control over production cycle and improved technical skills to shorten some specified production processes.

The Group's turnover days of trade receivables for 2018 was 135 days (2017: 144 days). The improved turnover days of trade receivables was mainly due to the strengthened credit control and debts collection policy implemented by the Group during the year.

The Group's turnover days of trade payables for 2018 was 120 days (2017: 113 days). The lengthened turnover days of trade payables was due to the better utilisation of bills for trade payables.

Accordingly, the Group's cash conversion cycle for 2018 was 178 days (2017: 235 days). The improved cash conversion cycle was mainly due to the more effective and efficient control over the inventory production. Please note that the calculation of the aforesaid indexes may not be comparable with those measurement indexes published by other issuers.

Capital Expenditure and Capital Commitments

For 2018, the Group's net increase in property, plant and equipment amounted to RMB76,725,000, which was mainly expenditure on production line of powder metallurgy and were financed by a combination of our internal cash resources, operating cashflows and bank borrowings. As at 31 December 2018, capital commitments were RMB458,597,000 (2017: RMB435,362,000), of which RMB90,265,000 (2017: RMB25,362,000) were contracted for and RMB368,332,000 (2017: RMB410,000,000) were authorised but not contracted for. The majority of the capital commitments related to investment in the production line of powder metallurgy and intelligent facility for cutting tools and is expected to be funded by internal resources and operating cash flows of the Group.

Foreign Exchange Exposure

The Group's revenues were denominated in RMB, USD and EUR, with RMB accounting for the largest portion of 64.7%. As such, 35.3% of total sales and operating profit were subject to exchange rate fluctuations. The Group has put in place measures such as monthly review of product pricing in the light of foreign exchange fluctuations and incentivising overseas customers to settle balances on a more timely basis to minimise the financial impact of exchange rate exposures.

Pledge of Assets

As at 31 December 2018, the Group pledged certain bank deposits amounting to RMB464,500,000 (2017: RMB241,380,000), certain trade receivables amounting to RMB151,780,000 (2017: RMB123,200,000) and other financial assets amounting to nil (2017: RMB73,500,000). The increase in pledged bank deposits was to support the increased banking facilities of the Group for issuance of bank acceptance bills.

Employees' Remuneration and Training

As at 31 December 2018, the Group employed 2,864 employees (2017: 2,951 employees). Total staff costs during the year amounted to RMB268,791,000 (2017: RMB243,619,000). The Group provided employees with remuneration packages comparable to market rates and employees are further rewarded based on their performance according to the framework of the Group's salary, incentives and bonus scheme. In order to enhance the Group's productivity, and further improve the quality of the Group's human resources, the Group provides compulsory continuous training for all of its staff on a regular basis.

Contingent Liabilities

Neither the Group, nor the Company, had any significant contingent liabilities at the end of the reporting period.

Principal Risks and Uncertainties

The main activities of the Group include production and sales of DS, HSS, cutting tools and titanium alloy. The Group is exposed to a variety of financial risks including credit risk, liquidity risk, currency risk and interest rate risk. Details of the above main risks and measures for risk reduction are set out in note 32 to the financial statements.

Apart from the financial risks mentioned above, the Group is exposed to certain operating risks and uncertainties including rare metal price volatility and market demand.

Risks and uncertainties arising from rare metal price volatility

Rare metals represented a significant portion in the cost of materials of the Group's products. The price of rare metals significantly affected the per unit production costs of the Group's products. In view of the risk of rare metal price volatility, the Group has already engaged with rare metal suppliers to obtain discounted prices for purchasing rare metal over a fixed period of time. Moreover, since the price of rare metal is publicly available market information, the Group was capable to partially transmit the effect of rare metal price volatility to downstream customers. However, because of the transparency of the rare metal price, in extreme situations where the rare metal price remained low, the Group could be under pressure to make downward pricing adjustments on our products.

Risks and uncertainties arising from market demand of the Group's products

The Group's business and profitability growth were affected by the uncertainties of global macroeconomic situations, which could materially affect the manufacturing industry. These uncertainties eventually affect the demand of the Group's products. To minimise the effect of global macroeconomic uncertainties, the Group continued to develop new markets all over the world. The Group believes that the best way to manage such risks and uncertainties is to avoid reliance on demand from a particular economy.

In Compliance with Laws and Regulations

As a company listed in Hong Kong, the Company is subject to the regulations of the Securities and Futures Commission of Hong Kong and The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Since the shares of Jiangsu Tiangong Technology Company Limited ("TG Tech"), a 74.03% owned subsidiary of the Company, are quoted on the National Equities Exchange and Quotations System (the "NEEQ System"), TG Tech is subject to the regulations of the NEEQ System. Also, various PRC government authorities, particularly the State Environmental Protection Administration, have the authority to issue and implement regulations governing various aspects of special steel production. The Group will constantly update and ensure compliance with new rules and regulations issued by these regulators.

As at 31 December 2018 and up to the date of this report, the Board was unaware of any non-compliance with the relevant laws and regulations that had a significant impact on the Group.

Relationships with Key Stakeholders

(i) Employees

The Group recognises human resources as assets important to the Group's development and growth. Most of the Group's employees were working at the manufacturing plant in Zhenjiang City, the PRC. The Group provided employees with remuneration packages comparable to the market rates and employees were further rewarded based on their performance according to the framework of the Group's salary, incentives and bonus scheme. In order to enhance the Group's productivity, and further improve the quality of the Group's human resources, the Group provided compulsory continuous training for all of its staff on a regular basis.

(ii) Suppliers

The Group's suppliers mainly supplied us with raw materials and utilities in the PRC. The Group developed longstanding and good relationships with its suppliers. Our procurement department conducted regular meetings with the suppliers of raw materials and utilities to ensure that raw materials supplied were in stable supply and of good quality.

(iii) Customers

The Group established long-term cooperation relationships with major customers. The sales team in domestic and overseas sales offices visit and discuss with customers regularly so as to keep us well-informed of market information and changes.

Environmental,
Social and Governance Report

Environmental, Social and Governance Report

About the Environmental, Social and Governance Report

This is the third Environmental, Social and Governance Report (hereafter referred to as "the ESG Report") published by Tiangong International Company Limited (hereafter referred to as "the Company") and its subsidiaries (collectively referred to as "the Group"). The ESG Report mainly covers the annual performance and progress of the Group's environmental, social and other sustainability issues in 2018, so as to respond to relevant expectations of stakeholders. It is to be read in conjunction with the "Corporate Governance Report" of *Tiangong International Company Limited Annual Report 2018* ("Annual Report 2018"), so as to have a comprehensive overview on the environmental, social and governance ("ESG") performance of the Group.

ESG Reporting Content and Period

Unless otherwise stated, the organizational scope of the ESG Report covers the Company and its major subsidiaries. Other subsidiaries and associates of the Group that are not directly engaged in production activities and therefore have minor impacts on the overall environmental and social performance of the Group, are not included in the reporting scope of the ESG Report. If their operation has greater impacts on the environmental and social performance of the Group in the future, the Group would consider incorporating those companies into the scope of ESG reports in future fiscal years. All information disclosed in the ESG Report was sourced from the Group's documents and statistics. The Group assures the truthfulness, accuracy and completeness of the ESG Report.

The reporting period of the ESG Report is consistent with that stated in the Annual Report 2018 of the Group, which is 1 January 2018 to 31 December 2018 ("reporting period"). Where necessary, some of the content goes beyond the aforesaid period so as to enhance the comparability of the ESG Report.

Reporting Guideline

The ESG Report was prepared based on the *Environmental, Social and Governance Reporting Guide* under Appendix 27 to the *Rules Governing the Listing of Securities* ("Listing Rules") issued by the Stock Exchange of Hong Kong Limited ("SEHK"). Moreover, it was prepared based on the principles of materiality, quantitative, balance and consistency to determine and disclose its contents, and is compliant with the "comply or explain" provision set out in the *Environmental, Social and Governance Reporting Guide* by SEHK.

Form of Publication

The ESG Report is published in two language versions — Traditional Chinese and English. If there is any inconsistency between the two versions, the Traditional Chinese version shall prevail. You are welcome to access the Traditional Chinese and English versions of the ESG Report in the PDF format through the Company's website, http://www.tggj.cn/, and SEHK's HKExnews website.

Comments and Feedback

Your feedback is immensely important for the Group to keep enhancing its environmental and social performance. If you have any comments or feedback, you are welcome to contact us by email at tiangong@biznetvigator.com.

1. Group Profile

Established in 1981, the Group is a manufacturer of die steel ("DS"), high speed steel ("HSS"), cutting tools and titanium alloy. The Group focuses on manufacturing special steel, cutting tools and titanium alloy with full business integrity and quality, and has become one of the China's top 500 private enterprises and private enterprises in manufacturing sector. After years of development, the Group has developed an integrated system of scientific researches, production and sales covering mining, special steel production and tool manufacturing equipping with cutting-edge production equipment and technology.

2. ESG Management

By implementing the value of "contributing to the society and bringing benefits to people" and upholding the mission of fulfilling corporate social responsibility, the Group continuously improving its ESG management and ESG-related systems regarding product quality, environmental protection, employee rights and benefits, health and safety, etc., to realize its sustainable development targets.

2.1 Responsibility Mechanism

As the market gradually transitioning to a lower-carbon economy, it may entail extensive policy, legal, technology, and market changes that pose different levels of risks to companies. For example, climate change motivates companies to pay more attention to their environmental measures to tackle the changes. Under this circumstance, the Group proactively responds to ESG risks by establishing proper and effective ESG risk management and internal control systems and gradually integrating them into the Group's risk management system[1]. The Board is responsible for evaluating and determining ESG risks and ensures that appropriate and effective ESG risk management and internal control systems are in place, and is responsible for the Group's ESG strategy and reporting.

In order to implement ESG management works effectively and systematically, the Group has built an ESG management system formed by the Company's senior management and each functional department with different responsibilities. The senior management of the Company takes responsibility for reviewing ESG topics, formulating corresponding action plans and reporting to the Board about the ESG works, which are coordinated and carried out by each functional department. To further enhance ESG management at the professional and systematic levels, the Group will proactively refer to the SEHK's guidelines and comments of the fulfillment of ESG responsibility of listed companies to gradually improve the ESG management system in the future, and to create an ESG working group which will be responsible for organizing, coordinating and consolidating ESG management works. By doing so, it is able to form a hierarchical ESG management system to continuously implement the Group's vision in social responsibility.

[1] For details of the Group's internal control and risk management system, please refer to the relevant content in the 2018 Annual Report.

2.2 Stakeholder Engagement

Shareholders and investors, government, customers, employees, suppliers and communities are all important stakeholders of the Group. Keeping a smooth communication with each stakeholder is an essential part for the Group to realize sustainable development. The Group could have a better understanding of each stakeholder's expectations by multi-dimensional and regular stakeholder engagement to make specific work plans and continuously improve itself.

Stakeholders	Expectations	Communication Methods	Frequency	Respond Actions
Shareholders and Investors	Investment returns Corporate governance Regular communication	General Meetings Company announcement Regular reports	Annual/quarterly/ irregular	• Continuously improving risk management and internal control system; • Enhancing information disclosure and communicating regularly
Government	Compliance with laws and regulations Paying tax according to laws	Supervision and assessments Information disclosure	Regular/irregular	• Strictly complying with national laws and regulations and implementing works to be compliant; • Proactively cooperating with regulatory departments; • Paying tax according to laws
Customers	High-quality products Quality management Service guarantee	Contracts and agreements Customer service Service feedback	Annual/quarterly/ irregular	• Continuously improving production management system; • Promoting scientific research innovation and elevating quality and efficiency in production
Employees	Employee rights and benefits Health and safety Promotion and trainings	Labor contracts Employee conferences Employee activities	Regular/irregular	• Strengthening human resource management system to ensure employee rights and benefits; • Implementing measures relating to employee's occupational health and safety; • Formulating training plans and broadening employee's development path
Suppliers	Being Fair and just Win-win cooperation	Contracts and agreements Supplier assessments	Annual/irregular	• Guaranteeing the bidding and procurement process to be fair and transparent; • Fulfilling contracts and agreements
Communities	Community development Environmental protection	Community communication Charitable contribution Eco-friendly events	Regular/irregular	• Engaging in the harmonious community development • Proactively holding charity donation events • Implementing environmental protection measures

2.3 Materiality Assessment

Based on the Group's development direction and stakeholders' focus points, the Group conducted a materiality assessment according to the "materiality" principle, and, therefore, it could report the material ESG performance of the Group and to respond to stakeholders' expectations more specifically.

There were mainly three steps of the materiality assessment, including reviewing the previous ESG works, identifying ESG topics, and verifying and reviewing ESG topics. First of all, the Group reviewed its previous ESG works and ESG Reports in 2016 and 2017. Following this, with reference to SEHK guidelines and other sustainability reporting guidelines, the Group identified ESG topics of this year by taking full consideration of the Group's business nature and development strategy together with stakeholders' expectation and industrial development trends. After ESG topics are identified, they were verified and reviewed by the Group for the determination of the topics to be disclosure and the content of the ESG Report.

The verified ESG topics are listed as follows. The ESG Report shows the ESG performance of the Group during the reporting period according to the topics and relevant reporting guidelines.

Aspects	Reported ESG topics
Environmental	Emission management Use of resources Environmental protection
Social	Employee rights and benefits Labor standards Health and safety Employee development and training Supplier management Product responsibility Scientific research and innovation Anti-corruption Community investment

3. Manufacturing with Excellent Craftsmanship, Operating with Pragmatic Attitude

The Group upholds the development concept of "building a well-established Tiangong with a reputable brand" and adheres to the spirit of excellent craftsman to manufacture high-quality products with great care and continuous improvement. The Group attaches great importance to innovation and keeps elevating product quality and production efficiency through innovations in technologies.

3.1 Quality of Tiangong

As a manufacturer of special steel, cutting tools and titanium alloy, the Group strictly complies with the relevant laws and regulations relating to health and safety, advertising, labelling and privacy matters relating to products and services provided and methods of redress, including but not limited to the *Work Safety Law of the People's Republic of China*, the *Recommendation Concerning Safety in the Use of Chemicals at Work*, the *Advertising Law of the People's Republic of China* and the *Trademark Law of the People's Republic of China*, etc. In addition, the Group has formulated and implemented quality control systems in accordance with the *Quality Management Systems — Requirements of National Standard of the People's Republic of China* (GB/T 19001-2016, identical to ISO 9001:2015, *Quality Management Systems — Requirements*) and has carried out measurement management of products according to ISO 10012:2003 *Measurement Management System* to guarantee its product quality in an all-around ways. Furthermore, to ensure production safety and the implementation of safety management of products and materials, the Group has formulated and implemented the responsibility system for production safety and safety commitment system. During the reporting period, the Group did not violate any laws and regulations relating to health and safety, advertising, labeling and privacy matters relating to products and services provided and methods of redress.

The Group meticulously and strictly manages the whole production process and has implemented various kinds of product quality control manual. A series of quality inspection is adapted to the production process from receipt of raw materials to the finished products. The Group examines the raw materials upon their arrival by taking samples for chemical tests to ensure their quality meets the specification. During the production process, physical and chemical analyses on the semi-finished products of each stage of production are done to ensure their production quality. In addition, the technology department and quality inspection department of the Group are responsible for the safety technology qualification of the design of new products, new techniques and equipment, and supervising the implementation of the safety technology operation regulations of the production safety procedure of each product, respectively, to ensure production safety. A series of quality tests is conducted by the Group for the finished products to guarantee that they meet relevant requirements regarding health and safety, labeling, environmental protection, etc., before entering into the market. During the reporting period, the Group was awarded the title of "China Industrial Model Enterprise" and became one of the enterprises in Jiangsu Province who is certified to be in compliance with Chinese Grade 1 Management and Measurement System, attributing to its persistence in maintaining high-quality of products.

The Group was awarded the title of "China Industrial Model Enterprise"

The Group attaches great importance to customers' feedback and provides pre-sales and after-sales service to them. The Group proactively responds to customers' comments and suggestions regarding the products and services of the Group, and timely arranges personal to give feedback according to the formulated customer service management measures. In addition, customers could identify the authenticity of products through the Group's product authenticity checking systems, including QR code, digital security query system and product sequence number system. The system not only protects the rights and benefits of customers to buy quality products, but also maintains the Group's business credit. Regarding the information of the Group and its clients, the Group strictly complies with the applicable record management measures and confidentiality rules to keep information and messages safe.

3.2 Driven by Innovation

2018 is a crucial year to continue to implement the "Thirteenth Five-Year Plan", which indicates that DS, HSS, titanium alloy and powder metallurgy products are included in the strategic emerging industry development plan. Moreover, in the "China Manufacturing 2025 Plan", DS and HSS, titanium alloy, and powder metallurgy are classified as distinct developing advanced basic materials, key strategic materials, and advanced new materials, respectively. Innovation is the primary driving force for the development of an enterprise. The Group firmly seizes the chance, and proactively renovates and improves its current products through its technical research and development. The Group not only greatly inspires and supports employees to be innovative and conduct scientific research and awards the group or individual for their achievements in innovation, but also proactively cooperates with external professional researchers and makes use of the Group's internal advanced equipment and external technology improvement to accelerate the research and development of advanced new materials.

By continuous exploration and research, the Group officially commenced the first establishment of powder metallurgy production line in China on 26 March 2018, which fills the domestic gaps of the research of large-scale production of powder metallurgy. On 18 November 2018, China Iron & Steel Research Institute Group and the Group jointly established the first powder metallurgy institute in China, which aims to satisfy the needs of the research and development and performance test of new products of powder metallurgy. The institute also provides technical support and reliable assurance to the mass production and research and development on the product types of powder metallurgy. The Group's researches and establishment in the powder metallurgy production line is an important step to move forwards to the field of new materials, and to focus its efforts in the world's leading advance technology and its high-end application.

On 18 November 2018, China Iron & Steel Research Institute Group and the Group jointly established the first powder metallurgy institute in China

The Group's 2018 Summing-up and Commending Conference for Technology Innovation

3.3 Supplier Management

Suppliers are important business partners of the Group and the Group hopes to cooperate with suppliers for mutual development. Hence, the Group has formulated and implemented the regulations for bidding and long-term management mechanisms of materials procurement, such as the *Regulation for Administration of Procurement of Supplies and Price Accounting* and the *Management Regulation of Bidding*, to standardize the Group's bidding and material procurement management system and to ensure the fair, just and transparent bidding. In addition, the Group has formulated supplier assessment systems, established a supplier list and assessed suppliers' environmental and social performance on a regular basis, including their management level, product quality, after-sale service, whether environmental and social management measures are in place, etc. By doing so, it is able to guarantee the quality of raw materials and equipment that the Group uses in production as well as to manage the environmental and social risks from suppliers in a better way.

The Group will have regular on-site assessments to evaluate suppliers' social responsibility performance. For instance, if suppliers have violations of labor regulations, including employment of child labor, forced labor, etc., the Group would immediately terminate the cooperation with them. Additionally, the Group would consider the operation location of suppliers and try to choose local suppliers to reduce the emissions of pollutants due to long-distance transportation.

3.4 Anti-corruption and Upholding Integrity

The Group implements the business philosophy of "business starts from being integrity" and strictly complies with the applicable laws and regulations relating to bribery, extortion, fraud and money laundering, including but not limited to the *Criminal Law of the People's Republic of China*, the *Regulations of the People's Republic of China for Suppression of Corruption*, Listing Rules and fair competition rules. The Group has formulated and implemented the disciplinary measures for employees according to the aforesaid laws and regulations. The Group would handle the employee who may be involved in corruption and bribery seriously. The cases shall be transferred to judicial authority with any serious circumstance. Moreover, the *Management Regulation of Bidding* has been formulated to regulate bidding and ensure its process is transparent and open. During the reporting period, the Group did not violate any laws and regulations relating to bribery, extortion, fraud and money laundering.

The Group requires that employees shall comply with national laws, regulations and policies and strictly implement every regulation, measure and fundamental practice of the Group. By implementing the reward and punishment measure, the Group encourages those who comply with laws and regulations, while punishes those who violate relevant regulations with reference to relevant regulations. Moreover, the Group requires that business partners shall comply with relevant regulations to ensure the implementation of legal governance, and the procurement employees shall not have any economic interests with suppliers and be honest in performing duties.

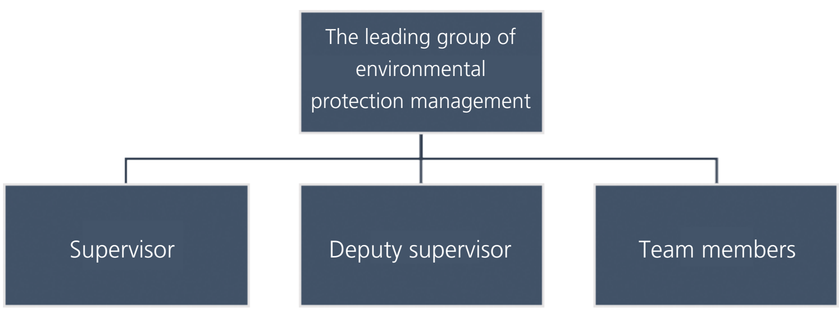
The appraisal results of the "2017 Integrity Enterprise" of China Hardware and Electromechanical Chamber of Commerce of All-China Federation of Industry and Commerce were announced during the reporting period and the Group was awarded the "2017 Integrity Enterprise".

4. Green Development, Protecting the Environment

The sustainable development of an enterprise could not be successful without implementing corresponding safety and environmental protection works. The Group thoroughly implements the principle of "production must be subject to safety, production must be subject to environmental protection, production must adhere to green development". The Group takes safety and environmental protection as the foundation and bottom line of all types of works so as to realize the Group's green and high-quality development.

4.1 Environmental Responsibility Management

As the works of ecological civilization construction continue to develop, China continues to enhance its environmental governance and revolves its governance regime in ecological and environmental areas. Moreover, the *Opinions of the Central Committee of the Communist Party of China and the State Council on Strengthening the Ecological and Environmental Protection in All Aspects and Firmly Winning the Battle of Preventing and Controlling Environmental Pollution* was published on 24 June 2018 and set out an overall plan for enhancing ecological and environmental protection and firmly winning the battle of preventing and controlling environmental pollution. Therefore, the Group has proactively responded to the national call of accelerating the reform of ecological civilization system and building a beautiful China by further enhancing safety and environmental protection works, implementing specific environmental protection management tasks, raising the awareness of safety and environmental protection laws, and proactively implementing energy saving and emission reduction. During the reporting period, the Group held a seminar for environmental protection management and established a leading group of environmental protection management, which is consisted of various cadres of the Group. By doing so, a management system has been built and formed by "supervisor-deputy supervisor-team members". This group upholds the central idea of green development and proactively promotes safety and environmental protection measures by comprehensively investigating dust, solid waste, spent oil, wastewater, noise and other potential pollutions. Improvement and corrective measures are formulated thereafter. The leading group of environmental protection management takes the responsibility for environmental protection management, which is implemented by the person-in-charge, such as building green facilities, equipment rectification and establishing waste inventory records. Hazards are investigated and eliminated in time to ensure relevant national, provincial and municipal standards have been met. The achievements of the fulfillment of environmental management responsibility of the Group during the reporting period have been disclosed in chapter 4.2 and 4.3.



4.2 Use of Resources

The Group strictly complies with relevant laws and regulations relating to the use of resources, such as the *Cleaner Production Promotion Law of the People's Republic of China, the Energy Conservation Law of the People's Republic of China*, etc. In addition, the Group has formulated and implemented water and electricity saving management measures and used resources and energy reasonably in accordance with the principle of reducing, reusing and recycling ("3R Principle"). By doing so, it is able to improve water and electricity utilization efficiency of the Group and save resources and energy.

The Group uses steel scrap and grinding swarfs, which are mainly sourced from the process of steel production, for steel smelting and production. Grinding swarfs are recycled and reused for steel production of the Group, which greatly increases the utilization rate of the raw materials. During the reporting period, the Group reused about 64,708.11 metric tons of grinding swarfs.

The Group advocates using electricity reasonably by implementing the *Management Measures of Saving Electricity* and using appropriate lighting fixtures according to the specific lighting needs, replacing energy consuming lights by energy-saving lights gradually. Furthermore, the Group requires to keep equipment from idling and wasting energy. Moreover, the Group holds water and electricity saving education events to raise employees' energy saving and environmental protection awareness and strengthens the supervision over water and electricity usage.

As for water sourcing, water used by the Group is mainly sourced from municipal fresh water supplies and wells. In order to increase water efficiency, a proportion of wastewater is reused as cooling water for production facilities after biochemical treatment in wastewater treatment plant. The Group also applies a water recycling system. During the reporting period, the amount of recycled water was approximately 110,867 metric tons.

As of the end of the reporting period, the major resources consumptions of the Group are listed as follows:

Indicators	Unit	2018	2017
Number of products (steel and titanium alloy)	Metric tons	**196,015.68**	159,658.56
Water consumption	Metric tons	**356,519.00**	170,593.00
Intensity of water consumption	Metric tons/ metric tons of products	**1.82**	1.07
Electricity consumption	Megawatt hours	**610,815.37**	515,675.13
Intensity of electricity consumption	Megawatt hours/ metric tons of products	**3.12**	3.23
Natural gas consumption	Ten thousand cubic meters	**3,549.80**	3,192.01
Intensity of natural gas consumption	Ten thousand cubic meters/ metric tons of products	**0.02**	0.02
Packaging materials used	Metric tons	**2,820.00**	Not reported

4.3 Emissions

The Group strictly abides by relevant laws and regulations relating to air and greenhouse gas ("GHG") emissions, discharges into water and land, and generation and disposal of waste, and complies with policies and management practices on minimizing the issuer's significant impact on the environment and natural resources, including but not limited to the *Environmental Protection Law of the People's Republic of China*, the *Atmospheric Pollution Prevention and Control Law of the People's Republic of China*, the *Water Pollution Prevention and Control Law of the People's Republic of China*, the *Law of the People's Republic of China on the Prevention and Control of Environmental Pollution by Solid Waste*, the *Law of the People's Republic of China on Prevention and Control of Pollution from Environmental Noise*, the *Environmental Protection Tax Law of the People's Republic of China and the Interim Measures of Jiangsu Province on Administration of Hazardous Wastes Management.* Moreover, for implementing the environmental protection management for production and operation, the Group has formulated the *Environmental Protection Management Measures* according to the applicable national laws and regulations relating to environmental protection listed above. The Group strictly complies with and implements the management measures relating to the prevention and control of water pollution, air pollution and noise, waste and the use of resources. During the reporting period, the Group did not violate any laws and regulations relating to air and GHG emissions, discharges into water and land, and generation and disposal of waste.

Moreover, the *Environmental Protection Tax Law of the People's Republic of China* has come into force since 1 January 2018 and requires that the enterprises and public institutions shall pay environmental pollution tax in accordance with the provision of the law to protect and improve the environment, and promote the ecological civilization construction. Therefore, the Group proactively and timely respond to the law by strictly fulfilling the responsibility of environmental protection and implementing environmental protection works as well as paying environmental pollution tax according to the law.

4.3.1 Exhaust Gas and GHG

The air emissions and GHG generated from the operation of the Group are primarily due to natural gas burning and electricity consumption. The Group has accomplished the renovation of boilers and furnaces, which replaced coal with natural gas as their fuel source and reduced air pollutant emissions during their operation. In addition, dust and oil mist are generated from the operation of the Group. High-efficient dust and oil mist collection devices have been installed on-site accordingly to reduce their impacts on the environment and employees' health. Regular maintenance has been conducted by the equipment maintenance department of each workshop to ensure the good operation of equipment and prevent fugitive emissions and extra energy consumption due to equipment malfunction. Furthermore, employees are required to operate equipment properly according to the operational guidelines to avoid equipment idling and reduce its energy consumption and GHG emissions. During the reporting period, the intensity of total GHG emissions of the Group decreased by 4.5% compared to that of previous reporting period.

During the reporting period, the Group enhanced dust treatment efficiency and reduced its environmental impact through the following practices:

1. Corrective measures are fully implemented to the dust removal equipment in workshops to improve dust removal efficiency;

2. Enclosing ash yards in workshops to prevent dust emission;

3. Investigating whether discharge outlets of exhaust gas and leak-proof measures meet environmental protection requirements;

4. Improving and renovating the exhaust system to elevate oil mist treatment efficiency.

As of the end of the reporting period, the major air pollutants and GHG emissions of the Group are listed as follows:

Indicators	Unit	2018[2]	2017[3]
Air pollutants[4]			
Sulfur oxides emissions	Metric tons	**0.51**	0.49
Nitrogen oxides emissions	Metric tons	**66.45**	59.72
GHG[5]			
Scope 1: direct emissions	Metric tons	**76,813.56**	69,017.28
Scope 2: indirect emissions	Metric tons	**429,708.61**	362,777.45
Total GHG emissions	Metric tons	**506,522.17**	431,794.74
Total GHG emissions intensity	Metric tons/ metric tons of products	**2.58**	2.70

4.3.2 Wastewater

The Group has formulated and implemented the *Administrative Procedures on Prevention and Control of Water Pollution*. All wastewater from production is collected and transferred to the wastewater treatment plant of the Group for treatment, which ensures that the discharge of treated wastewater reaches relevant standards. The supervision and monitoring of wastewater discharge are implemented by the Group in accordance with the *Implementation Procedure of Monitoring and Measurement*. Moreover, both of wastewater discharge pipeline and treatment facility have adopted seepage prevention measures to prevent wastewater leakage from causing impacts on the surrounding.

2 The data of 2018 were set out based on the consumption of natural gas, gasoline and electricity of the Group. The calculation scope is broader than the previous reporting period due to the inclusion of gasoline consumption in this year.

3 The data of 2017 were set out based on the consumption of natural gas and electricity.

4 The calculations of air pollutants were set out based on the *Pollution Generation and Discharge Coefficient Manual of Industrial Pollution Sources in the First National Census of Pollution Sources* and the *Road Vehicles Air Pollutant Emission Inventory Preparation Technical Guide (Trial)*. The data used in the calculation were sourced from the recorded data of the Group and conservative estimates were made based upon historical performance data or benchmarking with similar facilities.

5 The calculations of GHG emissions were set out based on the *Guideline of the Greenhouse Gas Emissions Accounting and Reporting for the Chinese Steel Production Enterprise (Trial)* and the *2011 and 2012 Chinese Regional Grid Average Carbon Dioxide Emission Factor* published by National Development and Reform Commission of the People's Republic of China. The data used in the calculation were sourced from the recorded data of the Group and conservative estimates were made based upon historical performance data or benchmarking with similar facilities. Among these, the datum of scope 2: indirect emission in 2017 was revised and shall be subject to the data listed here.

4.3.3 Solid Wastes

During operation, the solid wastes generated by the Group include non-hazardous wastes, such as melting slag, waste paper, etc., and hazardous wastes, such as spent oil (including spent lubricating oil and waste mineral oil), acidic and alkaline waste, etc. The Group has implemented environmental protection measures in accordance with relevant national and local environmental protection standards to ensure the solid waste treatment meets relevant requirements. Considering the complete data of hazardous waste were not disclosed in the previous reporting period, the Group enhanced its waste management during the reporting period by arranging specific personnel to handle wastes under the lead of the leading group of environmental protection management. Comprehensive waste inventory records have been established to improve the data collection system for waste. In addition, specific personnel is responsible for the implementation of anti-corrosive and leakage prevention measures to the waste storage areas and their compliance with relevant environmental requirements.

The Group follows the 3R principle to treat wastes. As for hazardous wastes, they are properly stored in strict compliance with dangerous good management regulations and are handed over to qualified third-parties for treatment. As for non-hazardous wastes, the Group divides them into recyclable and non-recyclable wastes. For instance, the metal in the smelting slag generated from production of the Group could be reused in steel production, while other parts could be transferred to brick factory and cement plant for brick and cement production. In addition, the spent lubricating oil produced from operation of the Group is reused after being treated in the spent lubricating oil treatment plant to reduce its generation. Domestic wastes are collected and treated by the third parties entrusted by the Group.

As of the end of the reporting period, the amount of solid wastes of the Group is listed as follows:

Indicators	**Unit**	**2018**
Non-hazardous wastes		
Melting slag	Metric tons	**34,604.86**
Waste paper	Metric tons	**36.86**
Total amount of non-hazardous wastes	Metric tons	**34,641.72**
Hazardous Wastes		
Acidic and alkaline wastes	Metric tons	**28,087.00**
Other hazardous wastes[6]	Metric tons	**26.28**
Total amount of hazardous wastes	Metric tons	**28,113.28**

4.3.4 Noise

The Group has formulated the *Administrative Procedures on Prevention and Control of Noise Pollution* and conducted noise assessment in the workshops. A series of measures to mitigate noise impact has been taken, such as taking priority in choosing quiet equipment, to ensure the noise from the production of the Group complies with the *Emission Standard for industrial Enterprises Noise at Boundary*. The Group shall arrange the operation with loud noise in the daytime as far as possible to avoid affecting residents' daily life in the evening.

[6] Including spent lubricating oil, waste mineral oil, oily sludge and other hazardous wastes.

5. Unified Tiangong, Forging ahead Together

The Group takes "enterprise develops prosperously and employees become wealthy" as its business management target to standardize human resource management and enhance team management skills. The Group strives to build a high-quality, united and hardworking team with strong cohesiveness to make progress with employees together.

5.1 Employees' Rights and Benefits

The Group strictly complies with relevant laws and regulations relating to compensation and dismissal, recruitment and promotion, working hours, rest periods, equal opportunity and other benefits and welfare, including but not limited to the *Labor Law of the People's Republic of China*, the *Labor Contract Law of the People's Republic of China*, the *Trade Union Law of the People's Republic of China* and the *Special Rules on the Labor Protection of Female Employees*. To further standardize the Group's human resource management, the Group has formulated and implemented the *Human Resources Management Rules of Tiangong International Company Limited*, the *Compensation Management Measures of Technical and Management Positions*, the *Work Attendance Regulation and Management Measures of Housing Provident Funds* and other human resource management policies. The Group has implemented reasonable working hours, sound labor contract system and recruitment system, comprehensive promotion mechanisms and remuneration and benefit policies, which enable employees to keep their mind on work. On the front of preventing child labor, the Group strictly complies with the applicable laws and regulations, such as the *Law of the People's Republic of China, on the Protection of Minors*, resolutely objecting to hire child labor under 16 years old as an employee. During the reporting period, the Group did not violate any laws and regulations relating to compensation and dismissal, recruitment and promotion, working hours, rest periods, equal opportunity, other benefits and welfare, prevention of child labor and forced labor.

The Group advocates equality and diversity in the employment policies, and it does not discriminate against employees because of race, nationality, color, gender and other conditions. The Group standardizes recruitment management according to the *Recruitment Policy*. The recruitment is conducted in various ways, such as online recruitment, job fair, etc., under the principle of "openness, fairness, competition, competitive selection and resource". During recruitments, the human resources department of the Group verifies the background of every candidate by checking his/her personal documents, such as identity card, diploma and so on to prevent hiring minors under 16 years old. The Group enters into individual employment contracts with its employees according to laws to cover wages, employee benefits and workplace safety and grounds for termination, etc. When a contract of employment is terminated, the termination follows relevant procedures according to the *Management Measures of Termination of Employment* and the labor contracts. In addition, the Group has paid the contributions to employees' social insurance funds (including medical insurance, unemployment insurance, pension insurance, work-related injuries insurance and childbirth insurance) and housing provident funds for its employees. The Group ensures that employees are legally entitled to take paid leaves and other public holidays by the people-oriented policies regarding employee leave, and they are also entitled to take marriage leaves, maternity leaves and bereavement leaves. In addition, the Group has formulated the attendance management system, which legally stipulates the working hours of employees and strictly prohibits the occurrence of forced labor.

In order to fully inspire every employee's motivation in different positions, and establish and enhance the qualification-based job management system and compensation system, the Group has formulated the *Compensation Management Regulations for Technical and Management Position* to stipulate the compensation structure and its adjustment standard of employee's position. Moreover, in order to seek and cultivate outstanding management personnel, the Group takes "character is the most important, performance is the basis, seniority is the supplement" as its employees' promotion principles to inspire employees' enthusiasm at the workplace.

Holding an employees' representatives conference is an effective way for the Group to continuously promote democratic management. In order to protect the rights and benefits of employees, the Group holds employees' representatives conference every year to proactively acquire the current comments of employees' representatives to the Group. On 31 March 2018, the Group held the first meeting of the second employees' representatives conference of Tiangong International and proactively communicates with employees' representatives to understand their thoughts and needs.

A group photo of the Second Employees' Representatives Conference of the Group

The meeting of the Second Employees' Representatives Conference of the Group

5.2 Health and Safety

The Group always upholds the safety production principle of "safety first, emphasizing prevention" and takes full responsibility for safety. The Group strictly complies with relevant national laws and regulations relating to work safety, providing a safe working environment and protecting employees from occupational hazards, such as the *Work Safety Law of the People's Republic of China*, the *Law of the People's Republic of China on the Prevention and Control of Occupational Diseases*, the *Special Equipment Safety Law of the People's Republic of China*, the *Standards Labor Protection Articles of Jiangsu Province*, the *Interim Provisions on the Inspection, Elimination and Control of Potential Work Safety Risk*, etc. In addition, the Group has formulated and implemented the occupational health and safety management systems, the plans for inspection, elimination and control of potential risks, the safety operation manuals for each equipment, and the emergency response plans. During the reporting period, the Group did not violate relevant laws and regulations in China relating to occupational health and safety.

In order to ensure work safety of the Group and implementation of safety measures, and clarify the safety responsibilities for each position and implement the principle of "three no harms" at the on-site operation, the Group takes full consideration of relevant work safety regulations to build a occupational health and safety management system of the Group, which is formed by the formulated work safety responsibility system, safety management system, safety inspection system, labor equipment management system, fire control management system, protection regulation for female workers, potential hazards control measure, accident investigation and handling management measure and other safety management measures. According to the requirements of the safety education system, every employee is required to receive relevant safety education and enter into a work safety commitment after getting well known of all contents in it. Moreover, the Group has formulated safe operation regulations specifically for each equipment to instruct employees' safe operation, including safety regulations of electric works and furnace operation. Employees are required to operate in accordance with these regulations. In addition, comprehensive and reliable safety equipment is allocated in workshops by the Group. Occupational hazards warning signs are in place to strengthen workplace safety management.

The Group has also established work safety responsibility system to clarify each person's work safety responsibility and implement safety management. Other than holding meetings for safety management discussion, specific employees are in place for workplace safety inspection and eliminate workplace hazards or other problems by regular inspection and handling non-compliance. The Group has formulated hazards investigation work plans to discover and identify unsafe factors in production and prevent accidents from occurring. Various kinds of safety inspection, including comprehensive, professional, seasonal, inspection during holidays, and daily inspections, are implemented to protect employees' life and keep their property safe. Furthermore, the Group has formulated contingency and rescue plans according to the *Work Safety Law of the People's Republic of China* and the *Fire Protection Law of the People's Republic of China*. The work safety leading group of the Group takes the lead in the emergency and rescue response operations. In addition, regular fire drills are held to increase employees' emergency responsiveness.

The Group proactively improves the employees' working conditions, and provide personal protective equipment according to the needs to prevent occupational diseases. Physical examination and various safety trainings are organized by the Group to raise the safety awareness of its employees.

5.3 Talent Development

The Group further builds a better workforce to promote company development by continuously improving employee training mechanism, strengthening the basic and professional knowledge of employees and broadening their career development path.

The Group has formulated and implemented the *Orientation Training Plan for New Employee of Tiangong International Company Limited* and the *Interim Measures for "Master-apprentice" Programs* of to facilitate new employees to be familiar with and adapt to the culture, policies and code of conduct of the Group quicker and better, and to be capable of doing the job. The orientation training includes introductions to the Group's management philosophy and corporate culture, technology and application of tools, work safety management, quality management knowledge, safe operation rules and points to note, etc. Trainings are hosted by the Group's senior employees and invited external experts to make employees acquire professional knowledge and skills better.

In addition, the Group promotes employees' development and makes full use of the human resource in the Group by formulating the *Interim Measures of "Master-Apprentice" Program* in the way of "deliver, help and teach face to face" program. The "deliver, help and teach face to face" program, also called "master-apprentice" program, is a training program that the Group implemented. Under this program, a new employee is paired up with an experienced employee through a one-on-one apprenticeship agreement in which the experienced employee is obligated to deliver and share experiences and methods with new employees. The experienced employees take full responsibility of drawing up the "deliver, help and teach face to face" training plan according to actual circumstances and provide guidance and assistance to his/her apprentice. Both the master and apprentice could make progress together through discussion and working together.

Other than professional knowledge and skills training, the Group held general education and culture seminars on an irregular basis to enrich employees' mental health.

The Group held a general education and culture seminar on 10 April 2018 by inviting Professor Libo to share his views on the Chinese spirit in poetries

6. Community Communication, Harmonious Development for a Common Prosperity

The harmonious development of society needs enterprises' proactive participation. The Group keeps its social responsibility in mind and proactively communicates with the community. By organizing various kinds of culture and sports activities and contributing to community charity events, the Group contributes to education and public welfare.

6.1 Energetic Tiangong

The Group always cares about the physical and psychological health of employees. Various kinds of culture and sports events could fully inspire employees' motivation by promoting their sport spirit and making them stronger, as well as elevating their team cohesion.

The Ninth (2018) Employee Sports Competition of the Group

6.2 Charitable Contribution

A country's future counts on children. The Group is willing to help children in need and let them have a bright future. During the reporting period, the Group held a youth charity event named "Holding Children's Hand with Our Hand" to make a donation to the handicapped children.

The Group held a charity event of "Holding Children's Hand with Our Hand"

Furthermore, the Group participated in the Charity Night of Hong Kong Environmental Protection Practitioners Association Limited ("HKPAA") with the theme of "Uniting Grassroots and Serving the Society" on 18 January 2018, which was held by the Charity Organization of HKPAA and HKPAA, and donated 1 million Hong Kong dollars. The donation in this event will be used for the Charity Organization of HKPAA to provide emergency assistance, and scholarship and events to the members' children to the grassroots like environmental protection practitioners. Through this charity donation, the Group aimed to help grassroots and bring positive energy in the society.

The Group participated in the Charity Night of HKPAA

The Group donated RMB 500,000 to Nanjing Normal University Education Development Foundation during the reporting period in order to support and further promote the development of higher education and technology research.

7. SEHK Environmental, Social and Governance Reporting Guide Index

General Disclosures and KPIs	Description	Relevant Chapter(s) in the ESG Report or Explanation
Environmental		
Aspect A1: Emissions		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to air and greenhouse gas emissions, discharges into water and land, and generation of hazardous and non-hazardous waste	4.1, 4.3
KPI A1.1	The types of emissions and respective emissions data	4.3
KPI A1.2	Greenhouse gas emissions in total (in tonnes) and, where appropriate, intensity (e.g. per unit of production volume, per facility)	4.3
KPI A1.3	Total hazardous waste produced (in tonnes) and, where appropriate, intensity (e.g. per unit of production volume, per facility)	4.3
KPI A1.4	Total non-hazardous waste produced (in tonnes) and, where appropriate, intensity (e.g. per unit of production volume, per facility)	4.3
KPI A1.5	Description of measures to mitigate emissions and results achieved	4.3
KPI A1.6	Description of how hazardous and non-hazardous wastes are handled, reduction initiatives and results achieved	4.3
Aspect A2: Use of Resources		
General Disclosure	Policies on the efficient use of resources, including energy, water and other raw materials	4.2
KPI A2.1	Direct and/or indirect energy consumption by type (e.g. electricity, gas or oil) in total (kWh in '000s) and intensity (e.g. per unit of production volume, per facility)	4.2
KPI A2.2	Water consumption in total and intensity (e.g. per unit of production volume, per facility)	4.2
KPI A2.3	Description of energy use efficiency initiatives and results achieved	4.2
KPI A2.4	Description of whether there are any issues in sourcing water that is fit for purpose, water efficiency initiatives and results achieved	4.2
KPI A2.5	Total packaging material used for finished products (in tonnes) and, if applicable, with reference to per unit produced	4.2

General Disclosures and KPIs	Description	Relevant Chapter(s) in the ESG Report or Explanation
Aspect A3: Environment and Natural Resources		
General Disclosure	Policies on minimizing the issuer's significant impact on the environment and natural resources	4.1, 4.2
KPI A3.1	Description of the significant impacts of activities on the environment and natural resources and the actions taken to manage them	4.1, 4.2
Social		
Aspect B1: Employment		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to compensation and dismissal, recruitment and promotion, working hours, rest periods, equal opportunity, diversity, anti-discrimination, and other benefits and welfare	5.1
Aspect B2: Health and Safety		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to providing a safe working environment and protecting employees from occupational hazards	5.2
Aspect B3: Development and Training		
General Disclosure	Policies on improving employees' knowledge and skills for discharging duties at work. Description of training activities	5.3
Aspect B4: Labor Standards		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to preventing child and forced labor	5.1
Aspect B5: Supply Chain Management		
General Disclosure	Policies on managing environmental and social risks of the supply chain	3.3

General Disclosures and KPIs	Description	Relevant Chapter(s) in the ESG Report or Explanation
Aspect B6: Product Responsibility		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to health and safety, advertising, labeling and privacy matters relating to products and services provided and methods of redress	3.1, 3.2
Aspect B7: Anti-corruption		
General Disclosure	Information on: (a) the policies; and (b) compliance with relevant laws and regulations that have a significant impact on the issuer relating to bribery, extortion, fraud and money laundering	3.4
Aspect B8: Community Investment		
General Disclosure	Policies on community engagement to understand the needs of the communities where the issuer operates and to ensure its activities take into consideration the communities' interests	6

Directors & Senior Management

Executive Directors

Mr. ZHU Xiaokun, aged 62, is an Executive Director and the Chairman of the Company. He is responsible for the overall business development strategy of the Group and has over 30 years of experience in special steel and cutting tools industry. Mr. Zhu graduated from the Economic and Management Department of Jiangsu Open University. In 1984, he joined Danyang Houxiang Television Antenna Factory (the predecessor of Jiangsu Tiangong Group Company Limited ("TG Group")) as the general manager. He led the factory to transform from a television antenna factory to an enterprise of HSS cutting tools in 1987 and also subsequently to expand to include the production of HSS in 1992, the production of DS in 2005 and the production of titanium alloy in 2012. He has been acting as the Chairman of the Group since July 1997. In 1998, he was awarded as a National Township Factory Manager, named as a National Township Entrepreneur in 2004 by Ministry of Agriculture, awarded as Model of Work Force in the Jiangsu Province in 2006, Model of the National Steel Industry Work Force in 2008, Top Ten Annual Jiangsu Businessman in 2010, "Most Benevolent Model" on Charitable Donations in Jiangsu Province in 2011, awarded National Labor Medal in 2012, continuously awarded of "Most Honored Business Leader of the Twelfth Five-year Plan in Jiangsu" in 2013 to 2015 and awarded of "National Model Worker" in 2015. Mr. Zhu is the representative of the Thirteenth National People's Congress. Mr. Zhu is the father of the Chief Investment Officer of the Group, Mr. Zhu Zefeng.

Mr. WU Suojun, aged 46, is an Executive Director of the Company and the Chief Executive Officer of the Company. Mr. Wu joined the Group in 1993 as a workshop officer. He is in charge of the purchase, sales, production and operation management of HSS and DS. He is also responsible for the security and environmental works.

Mr. YAN Ronghua, aged 50, is an Executive Director of the Company. He graduated from the Economic and Management Department of the Jiangsu Open University. He joined the Group in 1994. He was appointed as the head of office administration and subsequently the assistant general manager, deputy general manager of the Group. Mr. Yan is currently in charge of external investment management, and monitoring and evaluation of the Group's accounting and warehousing function.

Mr. JIANG Guangqing, aged 54, is an Executive Director of the Company. He graduated from Aerospace Industry 061 Base Technical School (航天工業零六一基地技工學校), joined the Group in 1993 and currently is the special assistant of the general manager. He is in charge of the production, operation and management of cutting tools.

Independent Non-Executive Directors

Mr. GAO Xiang, aged 75, joined the Company in 2007 as an Independent Non-Executive Director. In July 1966, he graduated from Wuhan Institute of Mechanics, majoring in production craftsmanship of machines and equipment. He is a senior engineer. Under his leadership, the study of twist drill extrusion technology by Chengdu Tools Research Institute was honoured with Third Class Award of Technical Findings of the Ministry of Mechanics. His achievements are widely recognized in the industry, and he has been granted special government subsidy by the State Council since 1999 as a result of such achievements.

Mr. LEE Cheuk Yin, Dannis, aged 48, joined the Company as an Independent Non-executive Director in 2010. He obtained the Bachelor of Business Administration from Texas A & M University, the USA. He is an associate member of the Hong Kong Institute of Certified Public Accountants and a member of the American Institute of Certified Public Accountants. He possesses over 20 years of experience in accounting and auditing field. Mr. Lee is an independent non-executive director of Geely Automobile Holdings Limited (HK Stock Code: 175). He was an executive director of AMCO United Holding Limited (HK Stock Code: 630) (resigned in 2011), a non-executive director of Kam Hing International Holdings Limited (HK Stock Code: 2307) (resigned in 2011) and an independent non-executive director of U-Home Group Holdings Limited (HK Stock Code: 2327) (resigned in 2015).

Mr. WANG Xuesong, aged 47, joined the Company as an Independent Non-executive Director in 2016. He is a holder of a Bachelor's Degree in Electronic Engineering from the Tsinghua University and a Master's Degree of Business Administration from the Columbia University. Mr. Wang has been the project manager of Sun Microsystems, Inc., responsible for the development of the world's leading fourth and fifth generations of UltraSPARC CPU chips. He has been awarded the second class National Science Progress Award of the People's Republic of China with his development in 32-bit slot in CPU technology. He has over 10 years of management and engineering experience in various industries in Silicon Valley in the United States and in China. Further, Mr. Wang has nearly 20 years of operating and investment experience in the United States and China. He has been a principal of China Renaissance Capital Investment, where he was responsible for private equity investments. He has also been an executive director and a senior investment member of China Everbright Investment and Assets Management Co., Ltd. Mr. Wang was a co-founding partner of Everbright ReinFore in 2013 and is currently a member of the firm's Investment Committee.

Senior Management

Mr. WANG Gang, aged 35, is the Chief Financial Officer of the Group. He graduated with a master's degree from the Royal Institute of Technology, Sweden. He is a member of The Chinese Institute of Certified Public Accountants. Prior to joining the Group in August 2015, he worked in KPMG Hong Kong and KPMG China and was promoted to the position of audit manager of KPMG China. Mr. Wang then joined TG Group as chief accountant in 2014. He was appointed as a director and the financial controller of TG Tech from August 2015 and subsequently resigned from the position of financial controller in TG Tech in January 2017, in preparation for the appointment as the Chief Financial Officer of the Company. Mr. Wang has over 10 years of experience in the fields of finance, auditing, accounting and administration and is familiar with the business and operation of the Group.

Mr. LIAO Jun, aged 53, is the Chief Technology Officer of the Group. He graduated from the College of Materials Science and Engineering of Chongqing University and acquired an Executive MBA from Shanghai Jiao Tong University in 2008. Prior to joining the Company in July 2014 as head of innovation and technology department, he worked as deputy chief of technical section of Shanghai No. 5 Steel Co., Ltd. He then served as deputy head of technical center of China Bao Steel Group and director of its branch steel plant. He has over 30 years of experience in special steel production and technology innovation. Mr. Liao is taking the responsibility of the Company's technology advance and development in order to enhance the product grading, technical specification and quality control.

Mr. ZHU Zefeng, aged 36, is the Chief Investment Officer of the Group. He graduated with advanced diploma in Business Operation Management from the Durham College, Canada. He joined the Company as management trainee in January 2016 to acquire the relevant experience and knowledge of the manufacturing process of the Group's products. He also involved in investigation and investment project on downstream subcontractor. Prior to his joining, he worked for TopTech Tools Manufacturing Inc. as an operation manager, with over 7 years of experience in overlooking and integration of upstream and downstream operation of its special steel business. His prime focus is to execute the Group's future investment strategy, in particular, in the integration of upstream and downstream component of the supply chain of the Group's existing business, as approved by the Board from time to time. Mr. Zhu is the son of the Executive Director and Chairman of the Company, Mr. Zhu Xiaokun.

Mr. JIANG Rongjun, aged 50, is an Executive Director and the General Manager of Jiangsu Tiangong Technology Company Limited ("TG Tech"). He joined the Group in 1985 as a workshop officer. Mr. Jiang is currently in charge of the production, sales and management of titanium alloy plant.

Mr. LEE Johnly, aged 39, is the Financial Controller and Company Secretary of the Company. Mr. Lee joined the Group in July 2015 and has over 15 years of experience in the field of finance, auditing, accounting and administration, including working in the assurance and advisory business services department of Ernst & Young Certified Public Accountants. Mr. Lee graduated with a Bachelor's Degree in Accountancy from the Hong Kong Polytechnic University. He is a member of The Hong Kong Institute of Certified Public Accountants.

Corporate Governance Report

The Group strives to attain and maintain high standards of corporate governance and to apply the principles set out in the Corporate Governance Code (the "Code") set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") as it believes that good corporate governance practices are fundamental to the Group's development and essential for safeguarding shareholders' interests. To achieve this objective, the Group strengthens its internal policies and procedures, provides continuous training to its staff and increases the transparency of its operation and accountability to all shareholders. The Group is committed to improving this practice and maintaining an ethical corporate culture. Save as disclosed below, during the year ended 31 December 2018, the Group has complied with the applicable principles and code provisions set out in the Code.

The Board

The Board's primary role is to secure and enhance long-term shareholder value. It focuses on the Group's overall strategic policy and provides proper supervision to ensure effective management and to achieve sound returns for its shareholders. The Board has delegated the authority and responsibility for implementing business strategies and management of the daily operations of the Group's business to the management. The Board is mainly responsible for developing long term objectives and strategy of the Group, monitoring operation performance and results, monitoring performance of the management, establishing dividend policy and reviewing significant investment plans and decisions. The Board meets at least four times a year and additional meetings are held when required to discuss significant events and issues.

The Board is responsible for determining the policy for corporate governance of the Company and performing the corporate governance duties including:

(a) to develop and review the Company's policies and practices on corporate governance;

(b) to review and monitor the training and continuous professional development of Directors and senior management;

(c) to review and monitor the Company's policies and practices in compliance with legal and regulatory requirements;

(d) to develop, review and monitor the code of conduct and compliance manual (if any) applicable to employees and Directors; and

(e) to review the Company's compliance with the Code.

Corporate governance duties performed by the Board during the year were covered in the below sections of the corporate governance report.

The company secretary of the Company (the "Company Secretary") assists the Chairman in preparing the agenda for Board meetings and all Directors shall have access to the advice and services of the Company Secretary with a view to ensuring that Board procedures, and all applicable rules and regulations are followed. All Directors can give notice to the Chairman of the Board or the Company Secretary if they intend to include matters in the agenda for Board meetings. Regular board meetings are held with at least 14 days' advance notice, and all Directors would be served with an agenda with supporting papers at least 3 days before the intended date of a Board meeting, so as to ensure that there is timely access to relevant information. The Group ensures that all the Board members are informed of the Group's latest developments and thereby assists them in the discharge of their duties. Procedures have been agreed by the Board to enable the Directors to seek independent professional advice, at the Company's expense.

Number of Meetings and Directors' Attendance

	Attendance/Number of Board Meetings			
Name of Director	Board Meeting	Audit Committee	Remuneration Committee	Nomination Committee
Mr. Zhu Xiaokun *(Chairman)*	6/6	N/A	1/1	1/1
Mr. Wu Suojun *(Chief executive officer)*	6/6	N/A	N/A	N/A
Mr. Jiang Guangqing	6/6	N/A	N/A	N/A
Mr. Yan Ronghua	6/6	N/A	N/A	N/A
Mr. Gao Xiang	6/6	2/2	1/1	1/1
Mr. Lee Cheuk Yin Dannis	5/6	2/2	1/1	1/1
Mr. Wang Xuesong	5/6	2/2	1/1	1/1

General Meetings With Shareholders

The Company's annual general meeting provides a useful platform for direct communication between the Board and its shareholders. Separate resolutions are proposed on each substantially separate issue at the general meetings.

The annual general meeting ("AGM") was held on 14 May 2018. Mr. Zhu Xiaokun acted as the chairman of the AGM.

The attendance records of the Directors at the shareholders' meetings held in the year 2018 are set out below:

	AGM
Executive Directors	
Mr. Zhu Xiaokun *(Chairman)*	✓
Mr. Wu Suojun *(Chief executive officer)*	–
Mr. Jiang Guangqing	–
Mr. Yan Ronghua	–
Independent non-executive Directors	
Mr. Gao Xiang	–
Mr. Lee Cheuk Yin Dannis	✓
Mr. Wang Xuesong	✓

In respect of the code provision A.6.7 of the Code which requires that independent non-executive directors and other non-executive directors should attend general meetings, Mr. Gao Xiang, the Independent Non-executive Director, was unable to attend the AGM due to other business engagement.

Minutes of the Board and Board Committees which record in sufficient detail the matters considered by the Board and the Board Committees and their decisions reached, including any concerns raised by Directors or dissenting views expressed are taken by the Company Secretary. Such minutes of the Board and Board Committees, together with supporting papers, are open for inspection following reasonable notice by any Director. Draft and final versions of minutes were sent to all Directors for their comment and records within a reasonable time after the relevant meeting was held. The Company has arranged appropriate insurance cover on Directors' liabilities in respect of legal actions against them arising from corporate activities.

Composition of the Board

The Board comprises four Executive Directors (Mr. Zhu Xiaokun, Mr. Wu Suojun, Mr. Yan Ronghua and Mr. Jiang Guangqing), and three Independent Non-Executive Directors (Mr. Gao Xiang, Mr. Lee Cheuk Yin, Dannis and Mr. Wang Xuesong). Biographical details of the Directors as at the date of this report are set out on pages 43 to 45 of this annual report.

Independent Non-Executive Directors account for more than one-third of the members of the Board. The Independent Non-Executive Directors come either from the steel industry or have related professional background, bringing valuable expertise and experience that promotes the best interests of the Company and its shareholders. The role of the Independent Non-Executive Directors is to provide independent and objective opinions to the Board for its consideration, take the lead where potential conflicts of interests arise, serve on the audit, remuneration and nomination committees and scrutinise the Company's performance in achieving agreed corporate goals and objectives, and monitor the reporting of performance. The Company has received an annual confirmation of independence from each of the Independent Non-Executive Directors. The Company is of the view that all the Independent Non-Executive Directors meet the guidelines for assessing independence as set out in Rule 3.13 of the Listing Rules and considers each of them to be independent.

The Company had adopted a Board diversity policy aiming to set out the approach to achieve the diversity of the Board. The Company recognises and embraces the benefits of having a diverse Board to enhance the quality of its performance. It endeavours to ensure that the Board has a balance of skills, experience and diversity of perspectives appropriate to the requirements of the Company's business. All Board appointments will continue to be made on a merit basis with due regard for the benefits of diversity of the Board members.

The Nomination Committee will follow a range of diversified perspectives, including but not limited to gender, age, cultural and educational background, professional experience, skills, knowledge and length of service. The ultimate decision will be made upon the possible contribution that the selected candidates will bring to the Board.

The Nomination Committee considered that the current composition of the Board is balanced in terms of diversity and is able to meet the objectives of the Board. The Board's diversity provides the Company with experienced individuals and professionals with proven and extensive industry experience whose opinions and expertise are useful for the decision-making of the Board and the implementation of its business directives.

Directors and Company Secretary's Continuous Training and Development

Directors also participate in continuous professional development to develop and refresh their knowledge and skills. The Company has from time to time provided information and updates to the Directors on the latest developments regarding the Listing Rules and other applicable regulatory requirements so as to ensure the Directors are in compliance with good corporate governance practices.

During the year ended 31 December 2018, all Directors have been provided with and read seminar materials covering topics including the Code, the disclosure of inside information and updates relating to the latest development of the Listing Rules and other applicable regulatory requirements to refresh their knowledge and to facilitate the discharge of their responsibilities. Each of the Directors has provided to the Company his records of training received during the financial year ended 31 December 2018.

For the financial year ended 31 December 2018, the Company Secretary has taken no less than 15 hours of relevant professional training.

Chairman and Chief Executive Officer

The Chairman of the Board is Mr. Zhu Xiaokun, and the Chief Executive Officer is Mr. Wu Suojun. The Chairman's and the Chief Executive Officer's roles and responsibilities are clearly defined to ensure their independence and a balance of power and authority. The Chairman of the Board provides leadership for the Board and he is responsible for the overall management of the Board and monitoring the Group's business strategies, while the Chief Executive Officer is responsible for the Group's day-to-day management in accordance with the instructions issued by the Board and operating the business of the Group and implementing policies and strategies adopted by the Board. Save as disclosed in the directors & senior management section of this report, there is no relationship (including financial, business, family or other material/relevant relationship(s) among the Directors and in particular, between the Chairman and the Chief Executive Officer.

In 2018, the Chairman has held a meeting with the Independent Non-Executive Directors without the Executive Directors being present.

Appointment, Re-election and Removal of Directors

While there was no appointment of new Directors this year, a person may be appointed as a member of the Board at any time either by shareholders' resolutions in general meetings or by resolutions of the Board upon recommendation by the Nominations Committee of the Company. New Directors appointed by the Board during the year are required to retire and submit themselves for re-election at the first general meeting immediately following their appointments.

Each newly appointed Director is provided with induction material on the first occasion of his/her appointment, so as to ensure that he/she has an appropriate understanding of the business and operations of the Group and that he/she is sufficiently aware of his/her responsibilities and obligations under the Listing Rules, code of conduct and other relevant regulatory compliance requirements.

All Directors are required to retire by rotation at least once every three years at the annual general meeting, subject to re-election by the shareholders. All Non-Executive Directors (including Independent Non-Executive Directors) are appointed for a term of not more than three years.

Board Committees

The Board has established three Board Committees to oversee different aspects of the Company's affairs. These Board Committees include the Audit Committee, the Remuneration Committee and the Nomination Committee. The Board Committees have been structured to include a majority of Independent Non-Executive Directors as members in order to ensure that all relevant issues are reviewed independently and objectively. These Board Committees will report back to the Board on their decisions or recommendations. The terms of reference of the respective Board Committees have complied with the Code provisions and are available on the Company's website www.tggj.cn and the website of the Stock Exchange www.hkexnews.hk.

Audit Committee

The Audit Committee comprises three Independent Non-Executive Directors, namely, Mr. Lee Cheuk Yin, Dannis, Mr. Gao Xiang and Mr. Wang Xuesong. The Chairman of the Audit Committee, Mr. Lee Cheuk Yin, Dannis, possesses expertise in accounting, auditing and finance.

Under its terms of reference, the Audit Committee is mainly responsible for overseeing the Company's financial reporting system and internal procedures, reviewing the financial information of the Company and overseeing the relationship with external auditors. These include reviewing and recommending for the Board's approval the interim and the annual financial statements; reviewing the external auditors' independence, objectivity and the effectiveness of the audit process; and reviewing and recommending to the Board for approval of the external auditor's remuneration; reviewing and obtaining explanation from management and the external auditor on the results for the year, including causes of changes from the previous period, effects on the application of new accounting policies, compliance with the Listing Rules and relevant legislation, and any audit issues, before recommending their adoption by the Board; considering and proposing to the Board the re-appointment of the Company's external auditors; considering and approving the procedures and guidelines in employing the external auditor to perform non-audit assignments for the Company; receiving and reviewing the internal audit reports from the internal auditor; holding meetings with the external auditors in the absence of management to discuss any audit issues; holding meetings with the internal auditor in private to discuss internal audit issues; approving the internal audit program for the year; carrying out a review of the internal control and risk management systems of the Company during the year including the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programs and budget and review of the effectiveness of the internal control and risk management systems of the Group. The Audit Committee has been provided with sufficient resources to discharge its duties.

The Audit Committee had a meeting on 15 March 2019 to consider and review the 2018 annual report and annual financial statements of the Group and to give their opinion and recommendation to the Board. The Audit Committee considered that the 2018 annual report and annual financial statements of the Company have complied with the Listing Rules and the applicable accounting standards and the Company has made appropriate disclosure thereof.

The Audit Committee held two meetings in 2018 and one meeting to date in 2019.

The meetings were held together with the external auditors of the Company, the Chief Financial Officer, and the Financial Controller of the Company, to discuss auditing, risk management, internal control, internal audit functions and financial reporting matters which include the review of the interim and annual financial statements. Full minutes of the Audit Committee meetings were kept by the Company Secretary. Draft and final versions of such minutes were sent to all members of the Audit Committee for their comment and records respectively, in both cases within a reasonable time after the meeting. The Audit Committee has made recommendations to the Board on the reappointment of the external auditors and their remuneration and terms of engagement and reviewed their independence. No former partner of KPMG, the existing auditing firm of the Company, was acting as a member of the Audit Committee for a period of 1 year from the date of his ceasing to be a partner of the firm; or to have any financial interest in the firm.

Remuneration Committee

The Remuneration Committee comprises one Executive Director, namely, Mr. Zhu Xiaokun, and three Independent Non-Executive Directors, namely, Mr. Gao Xiang, Mr. Lee Cheuk Yin, Dannis and Mr. Wang Xuesong. Mr. Wang Xuesong is the Chairman of the Remuneration Committee.

The primary role of the Remuneration Committee is to make recommendation to the Board on the Company's policy and structure for remuneration of Directors and senior management and to ensure that their compensation arrangements are determined in accordance with relevant contractual terms. No Director and any of his associates has taken part in any discussion on his own remuneration. Details of the fees of the Directors are set out in note 10 to the financial statements. The Company's remuneration policy is to maintain fair and competitive remuneration packages based on business needs and market practice. Factors such as market rate, an individual's qualification, experience, performance and expected workload are taken into account during the remuneration package determination process. The Remuneration Committee has consulted the Chairman of the Board, Mr. Zhu Xiaokun or the Chief Executive Officer, Mr. Wu Suojun, about their proposals relating to the remuneration of other Executive Directors and have access to professional advice if considered necessary. The Remuneration Committee was provided with sufficient resources to discharge its duties.

The Remuneration Committee held one meetings in 2018 and one meeting to date in 2019.

The meetings were held to assess the performance of the Directors and senior management, approve the terms of executive Director's service contracts, discuss and review the overall remuneration policy and structure. Recommendations have been made to the Board on the remuneration packages of individual executive Directors and senior management.

For the year ended 31 December 2018, the remuneration of the senior management is listed as below by band:

Band of remuneration	No. of persons
RMB1,000,000 to RMB2,000,000	1
RMB0 to RMB1,000,000	11

Further details of the remuneration of Directors and the 5 highest paid employees have been set out in notes 10 and 11 to the financial statements.

Nomination Committee

The Nomination Committee comprises one Executive Director, namely, Mr. Zhu Xiaokun, and three Independent Non-Executive Directors, namely, Mr. Gao Xiang, Mr. Lee Cheuk Yin, Dannis and Mr. Wang Xuesong. Mr. Gao Xiang is the Chairman of the Nomination Committee.

The primary responsibility of the Nomination Committee is to make recommendations to the Board on matters relating to the appointment or re-appointment of Directors and succession planning for Directors, and assessing the independence of the Independent Non-Executive Directors. The Nomination Committee has been provided with sufficient resources to discharge its duties.

The Nomination Committee has adopted the terms of reference as outlined under the Code provisions regarding the selection, recommendation and nomination of candidates for directorship during the year. The current terms of reference of the Nomination Committee are available on the websites of the Company and the Stock Exchange.

The Nomination Committee held one meetings in 2018 and one meeting to date in 2019. The meetings were held to discuss and review the composition and structure of the Board and senior management and the re-appointment arrangement of the Directors in the Company's forthcoming annual general meeting. The Executive Directors were appointed based on their qualification and experience in relation to the Group's business. The Independent Non-Executive Directors were appointed based on their professional qualifications and experience in their respective areas.

Directors' Responsibility for the Financial Statements

The Directors are responsible for overseeing the preparation of financial statements on a going concern basis, with supporting assumptions or conditions as necessary, for each financial period with a view to ensuring that such financial statements give a true and fair view of the state of affairs of the Group and of the results and cash flow for that financial year. Management of the Company has provided such explanation and information to the Board to enable the Board to make an informed assessment of the financial and other information put before the Board for approval. The Company's accounts are prepared in accordance with the Listing Rules, the Companies Ordinance, all relevant statutory requirements and applicable accounting standards. The Company has selected appropriate accounting policies and has applied them consistently based on prudent and reasonable judgments and estimates.

The Directors endeavor to ensure a balanced, clear and understandable assessment of the Company's position and prospects in annual reports, interim reports, price-sensitive announcements and other disclosures required under the Listing Rules and other statutory requirements.

Internal Control and Risk Management

Sound internal control and risk management systems enhance the effectiveness and efficiency of operations, ensures compliance with laws and regulations and mitigates the Group's business risk. The Company has an internal audit function. The Board is responsible for the internal control and risk management systems of the Group and reviewing their effectiveness and adequacy. Such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board and the Group's management hold meetings on a regular basis to review and evaluate the Group's business operations, production processes and financial reporting processes, adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, their training programmes and budget in order to achieve reasonable assurance of the following:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations

To maintain effective internal control and risk management systems that helps The Group to achieve its business objectives and safeguard its assets, the Group has implemented measures including: (i) establishing written policies and work flow for major operations and production cycles; (ii) having in place appropriate segregation of duties; and (iii) setting proper authorisation levels.

The Group has established an internal control and monitoring department to perform the internal control review on every workshop and department and furnish opinions to the Board in respect of material matters or bring to the attention of the management the existence of any relevant risks to prevent internal control defects. This department is responsible for performing independent review of the adequacy and effectiveness of the risk management and internal control systems.

The Board also ensures timely publication of the Group's financial statements and aims to present a clear, balanced and understandable assessment of the Group's performance and position through all its publications and communications to the public and complies with the requirements under the applicable rules and regulations about timely disclosure of inside information.

The Board, through the Audit Committee, have conducted a review covering all material controls, including financial, operational and compliance controls and risk management functions of the Group for the year ended 31 December 2018. The Audit Committee and the Board were not aware of any areas of concern that would have a material impact on the Group's financial position or results of operations and, having taken into account of the adequacy of resources, staff qualifications and experience, training programs, internal audit and financial reporting functions, considered that effective and adequate internal control and risk management systems of the Group had been in place and had been functioning effectively.

External Auditors

KPMG was re-appointed as the external auditors of the Company by the shareholders at the AGM until the next annual general meeting. In order to maintain their independence, objectivity and effectiveness in performing the audit services, the Audit Committee pre-approved all audit services and discussed with KPMG the nature and scope of the audit services. KPMG is primarily responsible for providing audit services in connection with the annual consolidated financial statements.

During the year ended 31 December 2018, the total remuneration paid or payable to KPMG was RMB2,650,000, including RMB2,650,000 for consolidated financial statements audit service and nil for non-audit professional service.

The Model Code for Securities Transactions by Directors of Listed Issuers

The Group has adopted a code of conduct governing securities transactions by Directors in compliance with and on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules (the "Model Code"). All of the Directors have confirmed, following specific enquiry by the Company, that they have complied with the required standard set out in the Model Code and the Group's code of conduct governing securities transactions by Directors and employees who may possess or have access to price sensitive information or inside information during the year ended 31 December 2018.

Dividend Policy

The Group adopted the Dividend Policy on January 2019. It aims to manage its optimal capital efficiently and generate long-term sustainable value for shareholders, while balancing operational and regulatory requirements. It also aims to grow its dividend in line with business growth and to share the benefits of its success with its shareholders.

The Group may declare and distribute no less than 35% of the consolidated net profit after tax of the Group as dividends to its shareholders.

The declaration and payment of dividends shall remain to be determined at the sole discretion of the Board and subject to any applicable restrictions, laws, rules and regulations.

In proposing any dividend payout, the Board shall take into account of the following factors:

- the actual and expected financial performance of the Group;
- the general financial position of the Group;
- the working capital requirements, capital expenditure requirements and future development strategy of the Group;
- restrictions imposed by any debt covenants;
- the general market conditions;
- the business cycle of the Company's business; and
- any other factors that the Board deems appropriate.

Any final dividends declared by the Company must be approved by an ordinary resolution of the shareholders at an annual general meeting and must not exceed the amount recommended by the Board.

Shareholders' Rights

Set out below is a summary of certain rights of the shareholders of the Company as required to be disclosed pursuant to the Code:

Convening of extraordinary general meeting on requisition or putting forward proposals at general meetings by shareholders

In accordance with the section 79 of the Company's articles of association, general meetings may be convened on the written requisition of any two or more members of the Company deposited at the registered office of the Company in Hong Kong specifying the objects of the meeting and signed by the requisitionists, provided that such requisitionists held as at the date of deposit of the requisition not less than one tenth of the paid up capital of the Company which carries the right of voting at general meetings of the Company. General meetings may also be convened on the written requisition of any one member of the Company which is a recognised clearing house (or its nominee(s)) deposited at the registered office of the Company in Hong Kong specifying the objects of the meeting and signed by the requisitionist, provided that such requisitionist held as at the date of deposit of the requisition not less than one-tenth of the paid up capital of the Company which carries the right of voting at general meetings of the Company.

If the Board does not within 21 days from the date of deposit of the requisition proceed duly to convene the meeting to be held within a further 21 days, the requisitionists themselves or any of them representing more than one-half of the total voting rights of all of them, may convene the general meeting in the same manner, as nearly as possible, as that in which meetings may be convened by the Board provided that any meeting so convened shall not be held after the expiration of three months from the date of deposit of the requisition, and all reasonable expenses incurred by the requisitionists as a result of the failure of the Board shall be reimbursed to them by the Company.

Shareholders may also make use of the above mechanism in putting forward proposals at a general meeting. In order to allow shareholders to make an informed decision at the relevant general meeting, requisitionists are requested to provide contact details to the Board at the time of deposition of the requisition in case further information is required to be included in the notice of meeting.

Shareholders should note that the Company is required to give notice of an extraordinary meeting of not less than 10 clear business days (pursuant to Listing Rules requirements) and not less than 14 days (pursuant to the articles of association of the Company).

Procedures for directing shareholders' enquiries to the Board

Shareholders may at any time send their enquiries and concerns to the Board of the Company in writing through the Company Secretary whose contact details are as follows:

The Company Secretary
Tiangong International Company Limited
Unit 1303, 13/F Jubilee Center
18 Fenwick Street, Wanchai, Hong Kong
Email: tiangong@biznetvigator.com
Tel No.: (852) 3102-2386
Fax No.: (852) 3102-2331

The Company Secretary shall forward the shareholders' enquiries and concerns to the Board and/or relevant Board Committees of the Company, where appropriate, to answer the shareholders' questions.

Investor Relationship and Communication

The Board and senior management recognize the importance of communication with shareholders and accountability to shareholders. Annual and interim reports offer comprehensive operational and financial performance information to shareholders and the annual general meetings provide a forum for shareholders to make comments and raise concerns to the Board directly. The Group's senior management also maintains close communication with investors, analysts and the media by other channels including roadshows, briefings and individual meetings. The Group has set up its own website www.tggj.cn, which is updated on a regular basis, as a means to provide updated information on the Company to investors. Shareholders are encouraged to attend the forthcoming annual general meeting of the Company for which at least 20 clear business days' notice (pursuant to Listing Rules requirements) and not less than 21 days' notice (pursuant to the articles of association of the Company) is given. At the meeting, the Chairman of the Board, the Chairman of the Board Committees (or their respective committee members) and the Directors are available to answer questions on the Group's business. There was no change in the Company constitutional documents during the year.

Report of the Directors

The Directors are pleased to submit the annual report together with the audited financial statements for the year ended 31 December 2018.

Principal Place of Business

The Company is a company incorporated and domiciled in Cayman Islands and has its principal place of business at Zhenjiang City, Jiangsu Province, the PRC.

Principal Activities

The principal activities of the Company are the production and sales of DS, HSS, cutting tools and titanium alloy. The principal activities and other particulars of the subsidiaries are set out in note 16 to the financial statements.

Financial Statements

The results of the Group for the year ended 31 December 2018 are set out in the consolidated statement of profit or loss and the consolidated statement of profit or loss and other comprehensive income on page 80 and 81.

The financial position of the Group as at 31 December 2018 is set out in the consolidated statement of financial position of the Group on pages 82 to 83. The financial position of the Company as at 31 December 2018 is set out in note 35 to the financial statement on page 175.

The cash flows of the Group for the year ended 31 December 2018 are set out in the consolidated cash flow statement on pages 85 to 86.

Results and Appropriations

The Board proposed a final dividend payment of RMB0.0357 per share for the financial year ended 31 December 2018 (2017: RMB0.0378).

Charitable Donations

Charitable donations made by the Group during the year amounted to RMB1,317,000 (2017: RMB500,000).

Property, Plant and Equipment

Details of the movements in the property, plant and equipment of the Group during the year are set out in note 13 to the financial statements.

Reserves

Details of movements in the reserves of the Company and of the Group during the year are set out in note 31 to the financial statements and in the consolidated statements of changes in equity, respectively.

Distributable Reserves

Distributable reserves of the Company as at 31 December 2018, calculated in accordance with the Companies Law (Cap. 22) (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, amounted to RMB1,513,695,000 (2017: RMB1,169,404,000).

Pre-emptive Rights

There is no provision for pre-emptive rights under the Company's articles of association and there is no restriction against such rights under the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

Share Capital

Details of the movements in share capital of the Company during the year are set out in note 31 to the financial statements.

Business Review

A review of the business of the Group during the year and a discussion on the Group's future business development are provided in the management discussion and analysis and the Chairman's statement of this annual report. Descriptions of possible risks and uncertainties that the Group may be facing and an analysis of the Group's performance during the year using financial key performance indicators is provided on pages 5 to 15 of this annual report. Particulars of important events affecting the Group that have occurred since the end of the financial year are provided in note 38 to the financial statements.

In addition, further information of the Company's environmental protection policies and compliance with relevant laws and regulations which have a significant impact on the Group are provided in the ESG Report and in the management discussion and analysis of this annual report. An account of the Company's relationships with its key stakeholders are disclosed in the section heading "Relationships with key stakeholders" on page 15 of the management discussion and analysis of this annual report.

Directors

The Directors during the financial year were:

Executive Directors

Mr. Zhu Xiaokun
Mr. Wu Suojun
Mr. Yan Ronghua
Mr. Jiang Guangqing

Independent Non-Executive Directors

Mr. Gao Xiang
Mr. Lee Cheuk Yin, Dannis
Mr. Wang Xuesong

Directors will retire by rotation in accordance with the requirement of the Listing Rules and the articles of association of the Company in the annual general meetings.

The Independent Non-Executive Directors are appointed for periods of one year. The Company considers that Mr. Gao Xiang, Mr. Lee Cheuk Yin, Dannis and Mr. Wang Xuesong are independent pursuant to the criteria set out in the Listing Rules and that a confirmation of independence has been received from each of them.

Directors' Interests and Short Positions in Shares, Underlying Shares and Debentures

As at 31 December 2018, the interests, long positions or short positions of the Directors and chief executive of the Company in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were recorded in the register required to be kept under Section 352 of the SFO, or which were notified to the Company and the Stock Exchange pursuant to the Model Code (set out in Appendix 10 of the Listing Rules) were as follows:

(a) Interests in the Company

Director's name	Interests	Ordinary shares held	Approximate attributable interests (%)
Zhu Xiaokun[1 and 2]	Interests of controlled corporations	817,190,000(L)	32.18
	Beneficial owner	3,800,000(L)	0.15
	Beneficial owner[3]	500,000(L)	0.02
			32.35
Wu Suojun	Beneficial owner	800,000(L)	0.03
	Beneficial owner[3]	2,467,000(L)	0.10
Yan Ronghua	Beneficial owner	500,000(L)	0.02
	Beneficial owner[3]	1,300,000(L)	0.05
Jiang Guangqing	Beneficial owner	300,000(L)	0.01
	Beneficial owner[3]	900,000(L)	0.04
Gao Xiang	Beneficial owner[3]	300,000(L)	0.01
Lee Cheuk Yin, Dennis	Beneficial owner[3]	300,000(L)	0.01
Wang Xuasong	Beneficial owner[3]	300,000(L)	0.01

Notes:

As at 31 December 2018,

(1) Tiangong Holdings Company Limited ("THCL") held 743,458,000 ordinary shares. THCL was held as to 89.02% and 10.98% by Zhu Xiaokun and Yu Yumei, the spouse of Zhu Xiaokun, respectively. Zhu Xiaokun is deemed to be interested in the 773,258,000 shares held by THCL.

(2) Silver Power (HK) Limited, which was wholly-owned by Zhu Xiaokun, held 43,932,000 ordinary shares.

(3) Options granted under Share Option Scheme of the Company.

(L) Represents long position.

(b) Interests in the shares of associated corporations

Name of Director	Name of associated corporation	Nature of interests and capacity	Total number of shares	Approximate percentage of interests (%)
Mr. Zhu Xiaokun	THCL	Beneficial owner	44,511(L)	89.02
		Spousal interest[1]	5,489(L)	10.98
Mr. Zhu Xiaokun	TG Tech	Beneficial owner	10,000,000(L)[2]	2.47

Notes:

(1) Ms. Yu Yumei, the spouse of Mr. Zhu Xiaokun held 5,489 shares in THCL. Mr. Zhu Xiaokun is deemed to be interested in such 5,489 shares in THCL.

(2) Mr. Zhu Xiaokun has acquired the shares in TG Tech in the Second Placing.

(L) Represents long position.

Save as disclosed above, as at the end of the reporting period, as far as the Directors are aware, none of the Directors and chief executive had any other interests, long positions or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations.

Substantial Shareholders' Interests

As at 31 December 2018, save for the Directors or chief executives as disclosed above, the following persons have an interest or short position in the shares or the underlying shares or debentures of the Company and its associated corporations which are required to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, which were recorded in the register required to be kept under Section 336 of the SFO:

(a) Interests in the Company

Substantial shareholders' name	Nature of interests and capacity	Ordinary shares	Approximate attributable interest (%)	Approximate attributable interest (%) (diluted)[6]
Yu Yumei[1]	Spousal interest[2]	821,490,000(L)	32.35	32.07
THCL[1]	Beneficial owner	773,258,000(L)	30.45	30.19
Zhu Zefeng	Interests of controlled corporations[3]	578,352,521(L)	22.78	22.58
	Beneficial owner	500,000(L)	0.02	0.02
	Beneficial owner	1,000,000(L)[4]	0.04	0.04
			22.84	22.64

Substantial shareholders' name	Nature of interests and capacity	Ordinary shares	Approximate attributable interest (%)	Approximate attributable interest (%) (diluted)[6]
Niu Qiu Ping	Spousal interest[5]	579,852,521(L)	22.84	22.64
Sky Greenfield Investment Limited	Beneficial owner[3]	578,352,521(L)	22.78	22.58
Liu Yang	Interests of controlled corporations[7]	155,492,000(L)	6.12	6.07
Atlantis Capital Holdings Limited	Interests of controlled corporations[7]	155,492,000(L)	6.12	6.07
Atlantis Investment Management Limited	Beneficial owner[7]	155,492,000(L)	6.12	6.07
Atlantis Investment Management (Ireland) Limited	Beneficial owner[7]	20,492,000(L)	0.81	0.80
Riverwood Asset Management (Cayman) Ltd.	Investment Manager[8]	135,000,000(L)	5.32	5.27
北京汽車集團產業投資有限公司 (Beijing Automobile Group Industrial Investment Co., Ltd.*)	Interests of controlled corporations[9]	150,000,000(L)	5.91	5.86
深圳市安鵬股權投資基金管理有限公司 (Shenzhen An Peng Equity Investment Fund Management Co., Ltd*)	Beneficial owner	150,000,000(L)	5.91	5.86
諾安基金管理有限公司 一 諾安彩虹十五號資產管理計劃 (BOC-Lion Rainbow No. 15 Fund*)	Trustee[10]	150,000,000(L)	5.91	5.86
Jiangsu Shagang Group Co., Ltd	Interests of controlled corporations[11]	150,000,000(L)	5.91	5.86
Shagang International (Hong Kong) Co., Limited	Beneficial owner	150,000,000(L)	5.91	5.86

(L) Represents long position.

Notes:

(1) THCL is owned as to 89.02% by Mr. Zhu Xiaokun and 10.98% by his spouse, Madam Yu Yumei.

(2) Ms. Yu Yumei is the spouse of Mr. Zhu Xiaokun and is deemed to be interested in the shares of the Company held by Mr. Zhu Xiaokun. For information in relation to shares of the Company held by Mr. Zhu Xiaokun, please refer to the paragraph headed "Directors' Interests and Short Positions in Shares, Underlying Shares and Debentures — (a) Interests in the Company".

(3) Zhu Zefeng controlled 100% of Sky Greenfield Investment Limited.

(4) Options granted under Share Option Scheme of the Company.

(5) Ms. Niu Qiu Ping is the spouse of Mr. Zhu Zefeng and is deemed to be interested in the shares of the Company held by Mr. Zhu Zefeng.

(6) As at the date of 31 December 2018, 22,147,000 ordinary shares may be issued pursuant to the outstanding share options granted under the 2007 Share Option Scheme.

(7) Atlantis Investment Management (Ireland) Limited and Atlantis Investment Management (Hong Kong) Limited are wholly-owned by Atlantis Capital Holdings Limited which is in turn wholly-owned by Liu Yang.

(8) Riverwood Asset Management (Cayman) Ltd. is wholly-owned by Liu Yang.

(9) 深圳市安鵬股權投資基金管理有限公司 Shenzhen An Peng Equity Investment Fund Management Co., Ltd ("An Peng Fund") is a wholly-owned company of 北京汽車集團產業投資有限公司 (Beijing Automobile Group Industrial Investment Co., Ltd*).

(10) 諾安基金管理有限公司 — 諾安彩虹十五號資產管理計劃 Lion Rainbow No. 15 Fund is a single client asset management scheme invested and established by An Peng Fund with 諾安基金管理有限公司 Lion Fund Management Co., Ltd.* as the asset manager.

(11) Shagang International (Hong Kong) Co., Limited, is a wholly-owned company of Jiangsu Shagang Group Co., Ltd.

* For identification purpose only

(b) Interests in the shares of associated corporation

Substantial shareholder's name	Name of associated corporation	Nature of interests and capacity	Total number of shares	Approximate percentage of interests (%)
Ms. Yu Yumei	THCL	Beneficial owner	5,489(L)	10.98
		Spousal interest(1)	44,511(L)	89.02
Ms. Yu Yumei	TG Tech	Spousal interest(1)	10,000,000(L)	2.47
Guo Guangchang	TG Tech	Interests of controlled corporations(2)	72,697,000(L)	17.95
南京鋼鐵集團有限公司工會委員會 (Labour Union Committee of Nanjing Iron & Steel Group Co., Ltd.*)	TG Tech	Interests of controlled corporations(3)	72,697,000(L)	17.95
南京新工投資集團有限責任公司 (Nanjing Xingong Investment Group Co., Ltd.*)	TG Tech	Interests of controlled corporations(4)	72,697,000(L)	17.95

(L) Represents long position.

Notes:

(1) Ms. Yu Yumei is the spouse of Mr. Zhu Xiaokun and is deemed to be interested in the shares of the associated corporations of the Company held by Mr. Zhu Xiaokun. For information in relation to shares of associated corporations of the Company held by Mr. Zhu Xiaokun, please refer to the paragraph headed "Directors' Interests and Short Positions in Shares, Underlying Shares and Debentures — (b) Interests in the shares of associated corporation".

(2) Guo Guangchang was deemed to hold a total of 72,697,000 shares (long position) in TG Tech directly held by 南京鋼鐵股份有限公司 (Nanjing Iron & Steel Co., Ltd.) by virtue of his control over numerous corporations:

(a) Guo Guangchang controlled 85.29% of Fosun International Holdings Ltd.

(b) Fosun International Holdings Ltd. controlled 100% of 復星控股有限公司 (Fosun Holdings Limited).

(c) 復星控股有限公司 (Fosun Holdings Limited) controlled 70.72% of 復星國際有限公司 (Fosun International Ltd.).

(d) 復星國際有限公司 (Fosun International Ltd.) controlled 100% of 上海復星高科技(集團)有限公司 (Shanghai Fosun High Technology (Group) Co., Ltd.).

(e) 上海復星高科技(集團)有限公司 (Shanghai Fosun High Mainland China Technology (Group) Co., Ltd.) controlled 100% of 上海復星產業投資有限公司 (Shanghai Fosun Industrial Investment Co., Ltd.) and 30% of 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.).

(f) 上海復星產業投資有限公司 (Shanghai Fosun Industrial Investment Co., Ltd.) controlled 100% of 上海復星工業技術發展有限公司 (Shanghai Fosun Industrial Technology Development Co., Ltd.) and 20% of 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.).

(g) 上海復星工業技術發展有限公司 (Shanghai Fosun Industrial Technology Development Co., Ltd.) controlled 10% of 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.).

(h) 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.) controlled 100% of 南京鋼鐵聯合有限公司 (Nanjing Iron & Steel United Co., Ltd.) and 40.60% of 南京鋼鐵股份有限公司 (Nanjing Iron & Steel Co., Ltd.).

(i) 南京鋼鐵聯合有限公司 (Nanjing Iron & Steel United Co., Ltd.) controlled 2.74% of 南京鋼鐵股份有限公司 (Nanjing Iron & Steel Co., Ltd.).

(3) 南京鋼鐵集團有限公司工會委員會 (Labour Union Committee of Nanjing Iron & Steel Group Co., Ltd.*) was deemed to hold a total of 72,697,000 shares (long position) in TG Tech directly held by 南京鋼鐵股份有限公司 (Nanjing Iron & Steel Co., Ltd.) by virtue of its control over numerous corporations:

(a) 南京鋼鐵集團有限公司工會委員會 (Labour Union Committee of Nanjing Iron & Steel Group Co., Ltd.*) controlled 36.07% of 南京鋼鐵創業投資有限公司 (Nanjing Iron & Steel Business Investment Co., Ltd.*).

(b) 南京鋼鐵創業投資有限公司 (Nanjing Iron & Steel Business Investment Co., Ltd.*) controlled 51% of 南京鋼鐵集團有限公司 (Nanjing Iron & Steel Group Co., Ltd.*).

(c) 南京鋼鐵集團有限公司 (Nanjing Iron & Steel Group Co., Ltd.*) controlled 40% of 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.).

(d) 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.) in turn controlled various corporations set out in note 2 (h) and (i) above.

(4) 南京新工投資集團有限責任公司 (Nanjing Xingong Investment Group Co., Ltd.*) was deemed to hold a total of 72,697,000 shares (long position) in TG Tech directly held by 南京鋼鐵股份有限公司 (Nanjing Iron & Steel Co., Ltd.) by virtue of its control over numerous corporations:

(a) 南京新工投資集團有限責任公司 (Nanjing Xingong Investment Group Co., Ltd.*) controlled 49% of 南京鋼鐵集團有限公司 (Nanjing Iron & Steel Group Co., Ltd.*).

(b) 南京鋼鐵集團有限公司 (Nanjing Iron & Steel Group Co., Ltd.*) controlled 40% of 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.).

(c) 南京南鋼鋼鐵聯合有限公司 (Nanjing Nangang Iron & Steel United Co., Ltd.) in turn controlled various corporations set out in note 2(h) and (i) above.

* For identification purpose only

Arrangements to Acquire Shares or Debentures

Save as disclosed in this report (note Share Option Scheme below), at no time during the year was the Company or any of its subsidiaries, holding companies or fellow subsidiaries a party to any arrangements to enable a Director to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

Biographical Details of Directors and Senior Management

Brief biographical details of the Directors and the senior management are set out on pages 43 to 45.

Final Dividend and Closure of Register of Members

The register of members of the Company will be closed from 21 May 2019 to 24 May 2019 (both days inclusive), for the purpose of determining shareholders' entitlement to attend and vote at the forthcoming annual general meeting of the Company (the "Annual General Meeting") on 24 May 2019, during which period no transfer of shares of the Company will be registered. In order to qualify for attending and voting at the Annual General Meeting, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th Floor, Hopewell Centre, No. 183 Queen's Road East, Wan Chai, Hong Kong, for registration by no later than 4:30 p.m. on 20 May 2019.

The Board has resolved on 18 March 2019 to recommend the payment of a final dividend of RMB0.0357 per share for the year ended 31 December 2018 (2017: RMB0.0378) to shareholders of the Company whose names appear on the register of members of the Company on 29 May 2019. The register of members will be closed from 30 May 2019 to 3 June 2019, both days inclusive, and the proposed final dividend is expected to be paid on or before 14 June 2019. The payment of dividends shall be subject to the approval of the shareholders of the Company at the Annual General Meeting expected to be held on 24 May 2019. In order to qualify for the proposed dividend, shareholders of the Company should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's branch share registrar, Computershare Hong Kong Investor Services Limited, at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, for registration by no later than 4:30 p.m. on 29 May 2019.

Share Option Scheme

The Company adopted a share option scheme (the "2007 Share Option Scheme") on 7 July 2007 and expired on 6 July 2017. A total of 35,170,000 shares have been allotted and issued pursuant to the 2007 Share Option Scheme, 34,764,000 options granted under the 2007 Share Option Scheme were cancelled and lapsed and 22,147,000 options granted under the 2007 Share Option Scheme remained outstanding and exercisable until 18 August 2019 according to the terms of grant, notwithstanding the expiry of the 2007 Share Option Scheme. The options were accepted by certain Directors and employees of the Company in respect of their services to the Group. These share options were vested on 19 August 2014 and have an initial exercise price of HKD1.78 per share of USD0.0025 each and an exercise period ranging from 19 August 2014 to 18 August 2019. The closing price of the Company's shares at the date of grant was HKD1.78 per share of USD0.0025 each.

The Company has a new share option scheme (the "Share Option Scheme") which was adopted on 26 May 2017.

The Share Option Scheme of the Company was approved by the Company in the Annual General Meeting held on 26 May 2017.

The purpose of the Share Option Scheme is to provide participants with the opportunity to acquire proprietary interests in the Company and to encourage participants to work towards enhancing the value of the Company and its shares for the benefit of the Company and its Shareholders as a whole. The Share Option Scheme will provide the Company with a flexible means of either retaining, incentivising, rewarding, remunerating, compensating and/or providing benefits to participants. The major terms of the Share Option Scheme are as follows:

1. The Directors may, at their discretion, invite any directors (including executive directors, non-executive directors and independent non-executive directors) and employees of any member of the Group and any advisers, consultants, distributors, contractors, contract manufacturers, suppliers, agents, customers, business partners, joint venture business partners, service providers of any member of the Group who the Board considers, in its sole discretion, have contributed or will contribute to the Group (the "Participants") to participate in the Share Option Scheme.

2. The maximum number of shares over which options may be granted under the Share Option Scheme must not exceed 222,008,000 shares of nominal value USD0.0025 each in the capital of the Company. As at the date of this report, options in respect of 222,008,000 shares may be granted, representing approximately 9.9% of the issued share capital of the Company as at the date of this report.

3. The total number of shares of the Company issued and to be issued upon exercise of the options granted to each Participant (including both exercised, cancelled and outstanding options) under the Scheme in any 12 month period must not exceed 1% of the shares in issue. Any further grant of options which would result in the number of shares issued as aforesaid exceeding the said 1% limit must be subject to prior shareholders' approval with the relevant Participant and his associates abstaining from voting.

4. The period within which the options must be exercised will be specified by the Company at the time of grant.

   This period must expire no later than 10 years from the relevant date of grant (being the date on which the Board resolves to make an offer of option to the relevant grantee).

5. At the time of grant of the options, the Company may specify any minimum period(s) for which an option must be held before it can be exercised. The Scheme does not contain any such minimum period.

6. The amount payable on acceptance of an option is HKD1.00.

7. The subscription price for the shares, the subject of the options, shall be no less than the higher of (i) the closing price of the shares as stated in the daily quotations sheet issued by the Stock Exchange on the date of grant; (ii) the average closing price of the shares as stated in the daily quotations sheets issued by the Stock Exchange for the five Stock Exchange business days immediately preceding the date of grant; and (iii) the nominal value of a share on the date of grant. The subscription price will be established by the Board at the time the option is offered to the Participants.

8. The Share Option Scheme shall be valid and effective till 24 May 2027.

On 11 January 2018, options entitled holders to subscribe for a total of 60,000,000 shares of USD0.0025 each were granted to and accepted by certain Directors, employees and consultants of the Company in respect of their services to the Group. 50% of these share options will be vested on 31 March 2019 if the consolidated audited net profit of the Company for the year ended 31 December 2018 represents an increase of 50% or more as compared to that of the year ended 31 December 2017. The remaining 50% of these share options will be vested on 31 March 2020 if the consolidated audited net profit of the Company for the year ending 31 December 2019 represents an increase of 50% or more as compared to that of the year ended 31 December 2018. All these options have an initial exercise price of HKD1.50 per share of USD0.0025 each and an exercise period commencing from the relevant vesting date and ending on 31 December of the same year as the vesting date. The closing price of the Company's shares at the date of grant was HKD1.29 per share of USD0.0025 each. As there was an increase in audited consolidated net profit of 53.1% in 2018, options in relation to 30,000,000 shares will vested on 31 March 2019.

	No. of options outstanding at the beginning of the year	No. of options granted during the year	No. of shares acquired on exercise of options during the year	No. of shares cancelled/ lapsed/ forfeited during the year	No. of options outstanding at the end of the year	Date granted	Period during which options are exercisable	Exercise price per share	Market value per share at date of grant of options*	Market value per share on exercise of options*
Directors										
Mr. Zhu Xiaokun	500,000	–	–	–	500,000	18 August 2014	19 August 2014 to 18 August 2019	HKD1.78	HKD1.78	–
Mr. Wu Suojun	867,000	–	–	–	867,000	18 August 2014	19 August 2014 to 18 August 2019	HKD1.78	HKD1.78	–
	–	800,000	–	–	800,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	800,000	–	–	800,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Mr. Yan Ronghua	300,000	–	–	–	300,000	18 August 2014	19 August 2014 to 18 August 2019	HKD1.78	HKD1.78	–
	–	500,000	–	–	500,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	500,000	–	–	500,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Mr. Jiang Guangqing	300,000	–	–	–	300,000	18 August 2014	19 August 2014 to 18 August 2019	HKD1.78	HKD1.78	–
	–	300,000	–	–	300,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	300,000	–	–	300,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Mr. Gao Xiang	–	150,000	–	–	150,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	150,000	–	–	150,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Mr. Lee Cheuk Yin, Dannis	–	150,000	–	–	150,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	150,000	–	–	150,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Mr. Wang Xuesong	–	150,000	–	–	150,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	150,000	–	–	150,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
Employees	20,180,000	–	–	–	20,180,000	18 August 2014	19 August 2014 to 18 August 2019	HKD1.78	HKD1.78	–
	–	27,950,000	–	–	27,950,000	11 January 2018	01 April 2019 to 31 December 2019	HKD1.50	HKD1.29	–
	–	27,950,000	–	–	27,950,000	11 January 2018	01 April 2020 to 31 December 2020	HKD1.50	HKD1.29	–
	22,147,000	60,000,000	–	–	82,147,000					

The options granted to the Directors are personal to the Directors and registered under the names of the respective Directors as beneficial owners.

* being the weighted average closing price of the Company's ordinary shares immediately before the dates on which the options were granted or exercised, as applicable.

Information on the accounting policy for share options granted and the weighted average value per option is provided in note 3(n)(ii) and note 29 to the financial statements respectively.

Apart from the foregoing, at no time during the year was the Company, or any of its holding company or subsidiaries a party to any arrangement to enable the Directors to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

Directors' and Controlling Shareholders' Interests in Contracts

Save as disclosed under the heading "Continuing Connected Transactions" below and "Material related party transactions" in note 34 to the financial statements, there is no contract of significance to the business of the Group between the Company, or any of its subsidiary companies, or a controlling shareholder or any of its subsidiaries during the year. During the year, no contract of significance for the provision of services to the Group by a controlling shareholder or any of its subsidiaries was made. There is no transaction, arrangement or contract of significance to the Group subsisting during or at the end of the year in which any Director or any entity connected with a Director is or was materially interested, either directly or indirectly.

Directors' Service Contracts

No Director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries, which is not determinable by the employing company within one year without payment of compensation (other than statutory compensation).

Permitted indemnity provision

During the year ended 31 December 2018, there was no permitted indemnity provision in force for the benefit of one or more (existing or former) directors of the Company or of its associated companies or such directors' associated companies.

Purchase, Sales or Redemption of Shares

During the year ended 31 December 2018, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's shares.

Issue of Shares or Debentures

Save as disclosed in this annual report, during the year ended 31 December 2018, neither the Company nor any of its subsidiaries has issued any shares or debentures.

Corporate Governance

The Company has, so far where applicable, adopted and complied with the principles and code provisions set out in the Corporate Governance Code (the "CG Code") in Appendix 14 of the Listing Rules during the year ended 31 December 2018, except for the following deviation:

Code Provision A.6.7

Code provision A.6.7 of the CG Code stipulates that independent non-executive directors ("INEDs") and other non-executive directors should also attend general meetings. One of the INEDs, Gao Xiang was unable to attend the annual general meeting of the Company held on 14 May 2018 due to other business engagement.

Audit Committee

The Audit Committee comprises three INEDs. The Audit Committee held a meeting on 15 March 2019 to consider and review the 2018 annual report and annual financial statements of the Group and to give their opinion and recommendation to the Board. The Audit Committee considered that the 2018 annual report and annual financial statements of the Company have complied with the applicable accounting standards and the Company has made appropriate disclosure thereof.

Defined contribution pension funds

The Group participates in defined contribution pension funds managed by the PRC local government authorities as disclosed in note 8(b) to the financial statements.

The PRC subsidiaries of the Group participate in defined contribution retirement benefit schemes (the "Schemes") organised by the PRC municipal and provincial government authorities whereby the PRC subsidiaries are required to make contributions at the rate of 19% starting from 1 July 2016 (before 1 July 2016: 20%) of the eligible employees' salary rate to the Schemes. The Group has accrued for the required contributions which are remitted to the respective local government authorities when the contributions become due. The local government authorities are responsible for the pension obligations payable to the retired employees covered under the Schemes.

Forfeited contributions could not be used by the Group to reduce the existing level of contributions.

Major Customers and Suppliers

The information in respect of the Group's sales and purchases attributable to major customers and suppliers during the financial year ended 31 December 2018 is as follows:

	Percentage of the Group's total	
	Sales	**Purchases**
The largest customer/supplier	25%	20%
Five largest customers/suppliers in aggregate	42%	55%

At no time during the year had the Directors, their close associates or any shareholder of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interest in these major customers and suppliers.

A majority of the domestic customers were granted credit for a term of 90 days, depending on the sales order volumes and the creditworthiness of individual customers. Beyond the normal credit term, a 90-day extension was also granted to key and credit-worthy customers subject to specific approval from management.

Overseas customers were generally granted Letter of Credit ("L/C") of 90 days, and a longer term-up L/C up to 120 days was allowed to customers with steady and high sales volumes.

The Group accepted bills from customers as settlement of trade receivables. The maturity period of bills ranges from three to twelve months.

Continuing Connected Transactions

Connected transactions relating to daily operation:

Description of the event	**Enquiry index**
On 16 April 2018, TG Tech, an indirectly owned subsidiary of the Company and 江蘇偉建工具科技有限公司 (Jiangsu Weijian Tools Technology Co., Ltd.#) ("Weijian Tools") entered into the Framework Titanium Coil Supply Agreement, pursuant to which TG Tech agreed to supply and Weijian Tools agreed to purchase titanium coil in 2018. The total amount of goods supplied under the aforementioned agreement was expected not to exceed RMB26 million.	For details, please refer to the announcement on the continuing connected transactions published by the Company on 16 April 2018 on the websites of the Stock Exchange at www.hkexnews.hk.
On 16 April 2018, 江蘇天工工具有限公司 (Jiangsu Tiangong Tools Co.,Ltd.#) ("TG Tools"), an indirect wholly-owned subsidiary of the Company and Weijian Tools entered into the Framework HSS Coil Supply Agreement pursuant to which TG Tools agreed to supply and Weijian Tools agreed to purchase HSS coil in 2018. The total amount of goods supplied under the aforementioned agreement was expected not to exceed RMB50 million.	For details, please refer to the announcement on the continuing connected transactions published by the Company on 16 April 2018 on the websites of the Stock Exchange at www.hkexnews.hk.

\# for identification purpose only, English name is not the official name of the entity

Note: In respect of the above connected transactions, Weijian Tools is a company owned as to 75% by Mr. Zhu Zefeng, a substantial shareholder of the Company. Mr. Zhu Zefeng is a substantial shareholder holding approximately 22.84% of the issued share capital of the Company and the chief investment officer of the Company.

Save for the above, the continuing connected transactions of the Group on leases from controlling shareholders disclosed in note 34 to the financial statements fall under the de minimis provision set forth in Rule 14A.76 (1) of the Listing Rules and are therefore exempt from reporting, announcement and independent shareholders' approval.

The independent non-executive Directors have reviewed the continuing connected transactions and confirmed that they have been entered into in the ordinary and usual course of business of the Group on normal commercial terms and according to the agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

Further, the Company has notified KPMG of the information relating to the continuing connected transactions to be disclosed in the 2018 annual report of the Company. KPMG has reviewed the information relating to such connected transactions and has issued a letter to the board of directors to confirm that such connected transactions:

(1) have been approved by the board of directors of the Company;

(2) were conducted in all material aspects in accordance with the Group's pricing policy (if such transactions involved the provision of goods or services by the Group);

(3) were conducted in all material aspects in accordance with the terms of relevant agreements governing such transactions; and

(4) have not exceeded the caps as disclosed in the previous announcements.

Pledge of Assets

As at 31 December 2018, the Group pledged certain bank deposits amounting to approximately RMB464,500,000 (31 December 2017: RMB241,380,000). The Group also pledged certain trade receivables amounting to approximately RMB151,780,000 (31 December 2017: RMB123,200,000) and other financial assets amounting to nil (31 December 2017: RMB73,500,000).

Financial Information Summary

A summary of the published results and assets, liabilities and non-controlling interests of the Group for the last five financial years, as extracted from the audited financial statements, is set out on page 179. This summary does not form part of the audited financial statements.

Directors' Interests in Competing Business

During the year and up to the date of this annual report, none of the Directors are considered to have interests in any business which competes or is likely to compete, either directly or indirectly, with the businesses of the Group, pursuant to the Listing Rules.

Management Contracts

No contracts concerning the management and/or administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

Sufficiency of Public Float

Based on the information that is publicly available to the Company and within the knowledge of the Directors of the Company, as at the date of this annual report, the Company has maintained sufficient public float as required under the Listing Rules.

Auditors

KPMG will retire and, being eligible, will offer themselves for re-appointment. A resolution for the re-appointment of KPMG as auditors of the Company is to be proposed at the forthcoming Annual General Meeting. There has been no change in the Company's auditors in any of the preceding three years.

By order of the Board

Tiangong International Company Limited
Zhu Xiaokun
Chairman
Hong Kong, 18 March 2019

Independent Auditor's Report

Independent auditor's report to the shareholders of
Tiangong International Company Limited
(Incorporated in the Cayman Islands with limited liability)

Opinion

We have audited the consolidated financial statements of Tiangong International Company Limited ("the Company") and its subsidiaries ("the Group") set out on pages 80 to 178, which comprise the consolidated statement of financial position as at 31 December 2018, the consolidated statement of profit or loss, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2018 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board ("IASB") and have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ("HKSAs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report. We are independent of the Group in accordance with the HKICPA's Code of Ethics for Professional Accountants ("the Code") together with any ethical requirements that are relevant to our audit of the consolidated financial statements in the Cayman Islands, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Revenue recognition

Refer to Note 5 to the consolidated financial statements and the accounting policies on page 105.

The Key Audit Matter	How the matter was addressed in our audit
The Group's revenue principally comprises sales of die steel, high speed steel, cutting tools and titanium alloy products to distributors and manufacturers and the trading of general carbon steel. Contracts for different products with different types of customers have a variety of different terms. Such terms may affect the timing of the recognition of sales to these customers. Management evaluates the terms of each contract in order to determine the appropriate timing of revenue recognition. Revenue from domestic and overseas direct sales is recognised when the control of the goods have been transferred to customers, which is generally when the goods leave the Group's warehouses, when the goods are delivered at the customers' premises and when the goods are loaded on board, respectively in accordance with the terms of the sales contracts. Revenue under consignment arrangements is generally recognised when the goods are sold to end customers.	Our audit procedures to assess the recognition of revenue included the following: • obtaining an understanding of and assessing the design, implementation and operating effectiveness of management's key internal controls in relation to revenue recognition; • inspecting key customer contracts to identify performance obligations and terms and conditions relating to transfer of control of the goods and assessing the Group's timing of recognition of revenue with reference to the requirements of the prevailing accounting standards; • comparing revenue transactions recorded during the current year, on a sample basis, with invoices, sales contracts and other underlying documents to assess whether the related revenue was recognised in accordance with the Group's revenue recognition accounting policies; • comparing, on a sample basis, specific revenue transactions recorded before and after the financial year end date with underlying documentation, which included goods delivery notes, goods acceptance notes, consignment statements and customs declaration forms, to assess whether revenue has been recognised in accordance with the terms of the sales contracts and in the correct financial year;

Revenue recognition

Refer to Note 5 to the consolidated financial statements and the accounting policies on page 105.

The Key Audit Matter	How the matter was addressed in our audit
We identified the recognition of revenue as a key audit matter because revenue is one of the key performance indicators of the Group and therefore there is an inherent risk of manipulation of the timing of recognition of revenue by management to meet specific targets or expectations.	• inspecting underlying documentation for manual journal entries relating to revenue which were recorded during the year and the closing period and which were considered to be material or met other specific risk- based criteria; • confirming, on a sample basis, the value of sales transactions for the year ended 31 December 2018 directly with customers and inspecting underlying documentation relating to reconciling differences between the transactions confirmed by customers and the Group's accounting records to assess whether the related revenue had been recognised in the correct financial year; and • inquiring of management as to the reasons for sales credits issued subsequent to the year end and inspecting relevant underlying documentation in order to assess whether the sales credits were completely and accurately accounted for in the correct financial year.

Loss allowance for trade receivables

Refer to Note 22 to the consolidated financial statements and the accounting policies on page 93.

The Key Audit Matter	How the matter was addressed in our audit
At 31 December 2018, the Group's gross trade receivables totalled RMB1,194 million, against which loss allowance of RMB106 million was recorded. Management measured loss allowance at an amount equal to lifetime expected credit loss, based on ageing of the receivables and loss rate, for receivables that existed during the reporting periods in which IFRS 9 "Financial Instruments" was applicable. According to the past experience of the Group, the loss patterns for overseas and domestic customers are significantly different. Therefore, when calculating the loss allowance based on ageing information, the receivables are segmented into overseas and domestic customer bases. We identified loss allowance for trade receivables as a key audit matter because trade receivables and loss allowance are material to the Group and because the recognition of expected credit losses is inherently subjective and requires the exercise of significant management judgement.	Our audit procedures to assess the loss allowance for trade receivables included the following: • obtaining an understanding of and assessing the design, implementation and operating effectiveness of management's key internal controls relating to credit control, segmentation of trade receivables, estimate of expected credit losses and making related allowances; • obtaining an understanding of the key data and assumptions of the expected credit loss model adopted by management, including the basis of the segmentation of the trade receivables based on credit risk characteristics, the historical default data, and the assumptions involved in management's estimated loss rate; • assessing the reasonableness of management's loss allowance estimates by examining the information used by management to form such judgements, including testing the accuracy of the historical default data and evaluating whether the historical loss rates are appropriately adjusted based on current economic conditions and forward-looking information; • assessing whether items were correctly categorised in the trade receivables ageing report by comparing a sample of individual items with the underlying goods delivery notes, sales invoices and other relevant underlying documentation; and • comparing, on a sample basis, cash receipts from customers subsequent to the financial year end relating to trade receivable balances at 31 December 2018 with bank-in slips and other relevant underlying documentation.

Valuation of inventories

Refer to Note 21 to the consolidated financial statements and the accounting policies on page 101.

The Key Audit Matter	How the matter was addressed in our audit
At 31 December 2018, the Group's gross inventories totalled RMB2,009 million, against which provisions for inventories of RMB15 million were recorded. The Group's inventories are valued at the lower of cost and net realisable value. The Group's provisions for inventories to write down the cost of inventories to their net realisable value is determined by management on an individual item basis by taking into account the estimated selling prices of the Group's products, the estimated costs of completion of work-in-progress at the reporting date and the estimated costs necessary to make the sales. The selling prices of the Group's special steel products are subject to market price volatility of the main raw materials, which include steel and alloys. Certain steel products are produced to meet the specific needs of downstream customers, the demand for which may change significantly from time to time. We identified the valuation of inventories as a key audit matter because of the significant management judgment involved in assessing the level of provisions for inventories, particularly in respect of slow moving inventories and inventories where the net realisable value may be less than the recorded cost.	Our audit procedures to assess the valuation of inventories included the following: • obtaining an understanding of and assessing the design, implementation and operating effectiveness of management's key internal controls over making provisions for inventories; • assessing the assumptions and estimates made by management in making provisions for inventories by performing a retrospective review of the historical accuracy of these estimates, discussing any significant variances with management and considering the impact of these variances on the current year's assumptions and estimates; • evaluating whether items were correctly categorised in the finished goods inventory ageing report by comparison with production records, on a sample basis; • recalculating the Group's inventory provision with reference to the sales prices achieved after the year end date, where available, and the latest market prices for the Group's products; • comparing year end inventory levels of individual products, on a sample basis, with procurement plans agreed with customers in order to assess the residual risk of the inventories' realisability; and • inspecting the inventory ageing report to identify any slow moving and obsolete inventory items and critically assessing whether appropriate provisions had been established for slow moving and obsolete items, for which there has been a lack of recent sales transactions.

Information other than the consolidated financial statements and auditor’s report thereon

The directors are responsible for the other information. The other information comprises all the information included in the annual report, other than the consolidated financial statements and our auditor’s report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the consolidated financial statements

The directors are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with IFRSs issued by the IASB and the disclosure requirements of the Hong Kong Companies Ordinance and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The directors are assisted by the Audit Committee in discharging their responsibilities for overseeing the Group’s financial reporting process.

Auditor’s responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. This report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, related safeguards.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Chan Ting Yuen.

KPMG
Certified Public Accountants
8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

18 March 2019

Consolidated Statement of Profit or Loss

For the year ended 31 December 2018

(Expressed in Renminbi ("RMB"))

	Note	**2018 RMB'000**	2017 RMB'000 (Note)
Revenue	5	**5,021,546**	3,898,443
Cost of sales		**(4,360,619)**	(3,399,980)
Gross profit		**660,927**	498,463
Other income	6	**42,467**	64,614
Distribution expenses		**(105,000)**	(85,800)
Administrative expenses		**(155,475)**	(140,357)
Other expenses	7	**(40,755)**	(2,210)
Profit from operations		**402,164**	334,710
Finance income		**7,233**	5,795
Finance expenses		**(142,071)**	(118,205)
Net finance costs	8(a)	**(134,838)**	(112,410)
Share of profits/(losses) of associates	17	**2,349**	(4,805)
Share of profits of joint ventures	18	**10,893**	602
Profit before taxation	8	**280,568**	218,097
Income tax	9	**(13,598)**	(43,396)
Profit for the year		**266,970**	174,701
Attributable to:			
Equity shareholders of the Company		**258,835**	169,099
Non-controlling interests		**8,135**	5,602
Profit for the year		**266,970**	174,701
Earnings per share *(RMB)*	12		
Basic		**0.106**	0.076
Diluted		**0.106**	0.076

Note: The Group has initially applied IFRS 15 and IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. See Note 4.

The notes on pages 87 to 178 form part of these financial statements. Details of dividends payable to equity shareholders of the Company attributable to the profit for the year are set out in Note 31(b).

Consolidated statement of profit or loss and other comprehensive income

For the year ended 31 December 2018

(Expressed in Renminbi ("RMB"))

	2018 RMB'000	2017 RMB'000 (Note(i))
Profit for the year	**266,970**	174,701
Other comprehensive income for the year (after tax and reclassification adjustment)		
Items that will not be reclassified to profit or loss:		
Equity investments at fair value through other comprehensive income		
– net movement in fair value reserve (net of tax of RMB841,000) (non-recycling)	**(8,045)**	–
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of:		
– financial statements of entities with functional currencies other than RMB	**(3,562)**	4,825
Available-for-sale securities: net movement in the fair value reserve (net of nil tax) (2017: net of tax of RMB3,420,000) (recycling) (Note(ii))	**–**	(19,380)
Other comprehensive income for the year	**(11,607)**	(14,555)
Total comprehensive income for the year	**255,363**	160,146
Attributable to:		
Equity shareholders of the Company	**247,228**	154,544
Non-controlling interests	**8,135**	5,602
Total comprehensive income for the year	**255,363**	160,146

Notes:

(i) The Group has initially applied IFRS 15 and IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. See Note 4.

(ii) This amount arose under the accounting policies applicable prior to 1 January 2018. As part of the opening balance adjustments as at 1 January 2018, the balance of this reserve has been reclassified to fair value reserve (non-recycling) and will not be reclassified to profit or loss in any future periods. See Note 4(b).

The notes on pages 87 to 178 form part of these financial statements.

Consolidated Statement of Financial Position

As at 31 December 2018

(Expressed in Renminbi ("RMB"))

	Note	2018 RMB'000	2017 RMB'000 (Note)
Non-current assets			
Property, plant and equipment	13	**3,597,069**	3,520,344
Lease prepayments	14	**93,628**	70,875
Goodwill	15	**21,959**	21,959
Interest in associates	17	**51,905**	49,372
Interest in joint ventures	18	**33,813**	26,263
Other financial assets	19	**100,024**	88,900
Deferred tax assets	30(b)	**25,195**	23,954
		3,923,593	3,801,667
Current assets			
Trading securities	20	**1,482**	–
Inventories	21	**1,994,287**	1,896,864
Trade and other receivables	22	**2,351,841**	2,044,171
Pledged deposits	23	**464,500**	241,380
Time deposits	24	**717,414**	500,000
Cash and cash equivalents	25	**583,235**	219,798
		6,112,759	4,902,213
Current liabilities			
Interest-bearing borrowings	26	**2,284,602**	2,170,279
Trade and other payables	27	**1,911,451**	1,302,982
Current taxation	30(a)	**117**	4,164
Deferred income	28	**5,279**	5,499
		4,201,449	3,482,924
Net current assets		**1,911,310**	1,419,289
Total assets less current liabilities		**5,834,903**	5,220,956

The notes on pages 87 to 178 form part of these financial statements.

Consolidated Statement of Financial Position

As at 31 December 2018
(Expressed in Renminbi ("RMB"))

	Note	**2018 RMB'000**	2017 RMB'000 (Note)
Non-current liabilities			
Interest-bearing borrowings	26	**899,177**	823,013
Deferred income	28	**50,498**	37,777
Deferred tax liabilities	30(c)	**62,268**	57,201
		1,011,943	917,991
Net assets		**4,822,960**	4,302,965
Capital and reserves			
Share capital	31(a)/(c)	**45,242**	40,477
Reserves	31(d)	**4,626,262**	4,119,167
Total equity attributable to equity shareholders of the Company		**4,671,504**	4,159,644
Non-controlling interests		**151,456**	143,321
Total equity		**4,822,960**	4,302,965

Approved and authorised for issue by the board of directors on 18 March 2019.

Zhu Xiao Kun
Directors

Yan Rong Hua
Directors

Note: The Group has initially applied IFRS 15 and IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. See Note 4.

The notes on pages 87 to 178 form part of these financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2018

(Expressed in Renminbi ("RMB"))

	Note	Attributable to equity shareholders of the Company										Non-controlling interests RMB'000	Total equity RMB'000
		Share capital RMB'000 (Note31(c)(i))	Share premium RMB'000 (Note31(d)(i))	Capital redemption reserve RMB'000 (Note31(d)(i))	Capital reserve RMB'000 (Note31(d)(ii))	Merger reserve RMB'000 (Note31(d)(iii))	Exchange reserve RMB'000 (Note31(d)(iv))	Fair value reserve (recycling) RMB'000 (Note31(d)(v))	Fair value reserve (non-recycling) RMB'000 (Note31(d)(vi))	PRC statutory reserve RMB'000 (Note31(d)(vii))	Retained earnings RMB'000		
Balance at 31 December 2017		40,477	1,602,218	492	70,595	91,925	(57,076)	53,975	-	566,221	1,790,817	143,321	4,302,965
Impact on initial application of IFRS 9	4	-	-	-	-	-	-	(53,975)	53,975	-	(31,897)	-	(31,897)
Balance at 1 January 2018		40,477	1,602,218	492	70,595	91,925	(57,076)	-	53,975	566,221	1,758,920	143,321	4,271,068
Changes in equity for the year 2018													
Profit for the year		-	-	-	-	-	-	-	-	-	258,835	8,135	266,970
Other comprehensive income		-	-	-	-	-	(3,562)	-	(8,045)	-	-	-	(11,607)
Total comprehensive income		-	-	-	-	-	(3,562)	-	(8,045)	-	258,835	8,135	255,363
Dividends approved in respect of the previous year	31(b)(ii)	-	-	-	-	-	-	-	-	-	(100,183)	-	(100,183)
Transfer to reserve	31(d)(vii)	-	-	-	-	-	-	-	-	32,577	(32,577)	-	-
Shares allotment	31(c)(ii)	4,765	381,884	-	-	-	-	-	-	-	-	-	386,649
Issuance of share options	31(c)(iii)	-	-	-	10,063	-	-	-	-	-	-	-	10,063
Balance at 31 December 2018		45,242	1,984,102	492	80,658	91,925	(60,638)	-	45,930	598,798	1,884,995	151,456	4,822,960

	Note	Attributable to equity shareholders of the Company									Non-controlling interests RMB'000	Total equity RMB'000
		Share capital RMB'000 (Note31(c)(i))	Share premium RMB'000 (Note31(d)(i))	Capital redemption reserve RMB'000 (Note31(d)(i))	Capital reserve RMB'000 (Note31(d)(ii))	Merger reserve RMB'000 (Note31(d)(iii))	Exchange reserve RMB'000 (Note31(d)(iv))	Fair value reserves (recycling) RMB'000 (Note31(d)(v))	PRC statutory reserve RMB'000 (Note31(d)(vii))	Retained earnings RMB'000		
Balance at 1 January 2017		40,167	1,590,760	492	72,848	91,925	(61,901)	73,355	544,538	1,665,531	137,719	4,155,434
Changes in equity for 2017												
Profit for the year		–	–	–	–	–	–	–	–	169,099	5,602	174,701
Other comprehensive income		–	–	–	–	–	4,825	(19,380)	–	–	–	(14,555)
Total comprehensive income		–	–	–	–	–	4,825	(19,380)	–	169,099	5,602	160,146
Dividends approved in respect of the previous year	31(b)(ii)	–	–	–	–	–	–	–	–	(22,130)	–	(22,130)
Transfer to reserve	31(d)(vii)	–	–	–	–	–	–	–	21,683	(21,683)	–	–
Exercise of share options	31(c)(iii)	310	11,458	–	(2,253)	–	–	–	–	–	–	9,515
Balance at 31 December 2017		40,477	1,602,218	492	70,595	91,925	(57,076)	53,975	566,221	1,790,817	143,321	4,302,965

The notes on pages 87 to 178 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2018

(Expressed in Renminbi ("RMB"))

	Note	2018 RMB'000	2017 RMB'000 (Note)
Operating activities			
Cash generated from operations	25(b)	**818,390**	244,177
PRC taxes paid		**(7,428)**	(27,790)
Hong Kong Profits Tax paid		**(63)**	(1,381)
Net cash generated from operating activities		**810,899**	215,006
Investing activities			
Payment for purchase of property, plant and equipment		**(307,235)**	(299,586)
Payment for purchase of other financial assets		**(20,010)**	(15,400)
Payment for lease prepayments		**(24,607)**	–
Proceeds from disposal of property, plant and equipment		**6,476**	3,105
(Payment for)/proceeds from time and pledged deposits, net		**(440,534)**	80,580
Interest received	8(a)	**7,233**	5,795
Dividends received from an associate		**488**	–
Dividends received from investment in securities	6	**1,800**	–
Proceeds from disposal of trading securities		**–**	4,505
Payment for trading securities		**(2,429)**	(3,960)
Payment for capital injection in associates		**–**	(6,500)
Net cash used in investing activities		**(778,818)**	(231,461)

The notes on pages 87 to 178 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2018
(Expressed in Renminbi ("RMB"))

	Note	2018 RMB'000	2017 RMB'000 (Note)
Financing activities			
Proceeds from interest-bearing borrowings		**4,937,670**	5,042,507
Repayment of interest-bearing borrowings		**(4,747,183)**	(4,938,127)
Interest paid		**(142,193)**	(118,407)
Dividends paid to equity shareholders of the Company	31(b)(ii)	**(100,183)**	(22,130)
Proceeds from shares allotment		**386,649**	9,515
Net cash generated from/(used in) financing activities		**334,760**	(26,642)
Net increase/(decrease) in cash and cash equivalents		**366,841**	(43,097)
Cash and cash equivalents at 1 January		**219,798**	259,546
Effect of foreign exchange rate changes		**(3,404)**	3,349
Cash and cash equivalents at 31 December		**583,235**	219,798

Note: The Group has initially applied IFRS 15 and IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. See Note 4.

The notes on pages 87 to 178 form part of these financial statements.

Notes to the Financial Statements

(Expressed in Renminbi ("RMB") unless otherwise indicated)

1 Reporting entity

Tiangong International Company Limited (the "Company") was incorporated in the Cayman Islands on 14 August 2006 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961 as consolidated and revised) of the Cayman Islands. The Company's shares have been listed on the Main Board of the Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 26 July 2007.

The Company and its subsidiaries are collectively referred to as the "Group".

2 Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs"), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards ("IASs") and Interpretations issued by the International Accounting Standards Board ("IASB"). These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out in Note 3.

The IASB has issued certain new and revised IFRSs that are first effective or available for early adoption for the current accounting period of the Group and the Company. Note 4 provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statements.

(b) Basis of measurement

The consolidated financial statements of the Group as at and for the year ended 31 December 2018 comprise the Company and its subsidiaries and the Group's interests in associates and joint ventures.

The measurement basis used in the preparation of the financial statements is the historical cost basis except as set out in the accounting policies hereunder.

(c) Accounting estimates and judgements

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

2 Basis of preparation (continued)

(c) Accounting estimates and judgements (continued)

Judgements made by management in the application of IFRSs that have significant effect on the financial statements and major sources of estimation uncertainty are set out in Note 36.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, and have been applied consistently by the Group entities, except as explained in Note 4, which addresses changes in accounting policies.

(a) Subsidiaries and non-controlling interests

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. When assessing whether the Group has power, only substantive rights (held by the Group and other parties) are considered.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-Group balances, transactions and cash flows and any unrealised profits arising from intra-Group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-Group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Non-controlling interests represent the equity in a subsidiary not attributable directly or indirectly to the Company, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. For each business combination, the Group can elect to measure any non-controlling interests either at fair value or at the non-controlling interests' proportionate share of the subsidiary's net identifiable assets.

Non-controlling interests are presented in the consolidated statement of financial position within equity, separately from equity attributable to the equity shareholders of the Company. Non-controlling interests in the results of the Group are presented on the face of the consolidated statement of profit or loss and other comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the Company. Loans from holders of non-controlling interests and other contractual obligations towards these holders are presented as financial liabilities in the consolidated statement of financial position in accordance with Notes 3(l) and (k) depending on the nature of the liability.

Changes in the Group's interests in a subsidiary that do not result in a loss of control are accounted for as equity transactions, whereby adjustments are made to the amounts of controlling and non-controlling interests within consolidated equity to reflect the change in relative interests, but no adjustments are made to goodwill and no gain or loss is recognised.

3 Significant accounting policies (continued)

(a) Subsidiaries and non-controlling interests (continued)

When the Group loses control of a subsidiary, it is accounted for as a disposal of the entire interest in that subsidiary, with a resulting gain or loss being recognised in profit or loss. Any interest retained in that former subsidiary at the date when control is lost is recognised at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see Note 3(d)) or, when appropriate, the cost on initial recognition of an investment in an associate or joint ventures (see Note 3(b)).

In the Company's statement of financial position, an investment in a subsidiary is stated at cost less impairment losses (see Note 3(g)), unless the investment is classified as held for sale (or included in a disposal group that is classified as held for sale).

(b) Associates and joint ventures

An associate is an entity in which the Group or Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

A joint venture is an arrangement whereby the Group or Company and other parties contractually agree to share control of the arrangement, and have rights to the net assets of the arrangement.

An investment in an associate or a joint venture is accounted for in the consolidated financial statements under the equity method, unless it is classified as held for sale (or included in a disposal group that is classified as held for sale). Under the equity method, the investment is initially recorded at cost, adjusted for any excess of the Group's share of the acquisition-date fair values of the investee's identifiable net assets over the cost of the investment (if any). The cost of the investment includes purchase price, other costs directly attributable to the acquisition of the investment, and any direct investment into the associate or joint venture that forms part of the Group's equity investment. Thereafter, the investment is adjusted for the post acquisition change in the Group's share of the investee's net assets and any impairment loss relating to the investment (see Notes 3(c) and (g)). Any acquisition-date excess over cost, the Group's share of the post-acquisition, post-tax results of the investees and any impairment losses for the year are recognised in the consolidated statement of profit or loss, whereas the Group's share of the post-acquisition post-tax items of the investees' other comprehensive income is recognised in the consolidated statement of profit or loss and other comprehensive income.

When the Group's share of losses exceeds its interest in the associate or the joint venture, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee. For this purpose, the Group's interest is the carrying amount of the investment under the equity method together with any other long-term interests that in substance form part of the Group's net investment in the associate or the joint venture.

3 Significant accounting policies (continued)

(b) Associates and joint ventures (continued)

Unrealised profits and losses resulting from transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the investee, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in profit or loss.

If an investment in an associate becomes an investment in a joint venture or vice versa, retained interest is not remeasured. Instead, the investment continues to be accounted for under the equity method.

In all other cases, when the Group ceases to have significant influence over an associate or joint control over a joint venture, it is accounted for as a disposal of the entire interest in that investee, with a resulting gain or loss being recognised in profit or loss. Any interest retained in that former investee at the date when significant influence or joint control is lost is recognised at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see Note 3(d)).

In the Company's statement of financial position, investments in associates and joint ventures are stated at cost less impairment losses (see Note 3(g)), unless classified as held for sale (or included in a disposal Group that is classified as held for sale).

(c) Goodwill

Goodwill represents the excess of

(i) the aggregate of the fair value of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the Group's previously held equity interest in the acquiree; over

(ii) the net fair value of the acquiree's identifiable assets and liabilities measured as at the acquisition date.

When (ii) is greater than (i), then this excess is recognised immediately in profit or loss as a gain on a bargain purchase.

Goodwill is stated at cost less accumulated impairment losses. Goodwill arising on a business combination is allocated to each cash-generating unit, or Groups of cash generating units, that is expected to benefit from the synergies of the combination and is tested annually for impairment (see Note 3(g)).

On disposal of a cash generating unit during the year, any attributable amount of purchased goodwill is included in the calculation of the profit or loss on disposal.

3 Significant accounting policies (continued)

(d) Other investments in equity securities

The Group's policies for investments in equity securities, other than investments in subsidiaries, associates and joint ventures, are as follows:

Investments in equity securities are recognised/derecognised on the date the Group commits to purchase/sell the investment. The investments are initially stated at fair value plus directly attributable transaction costs, except for those investments measured at fair value through profit or loss (FVPL) for which transaction costs are recognised directly in profit or loss. For an explanation of how the Group determines fair value of financial instruments, see Note 32(f). These investments are subsequently accounted for as follows, depending on their classification.

(A) Policy applicable from 1 January 2018

Equity investments

An investment in equity securities is classified as FVPL unless the equity investment is not held for trading purposes and on initial recognition of the investment the Group makes an irrevocable election to designate the investment at FVOCI (non-recycling) such that subsequent changes in fair value are recognised in other comprehensive income. Such elections are made on an instrument-by-instrument basis, but may only be made if the investment meets the definition of equity from the issuer's perspective. Where such an election is made, the amount accumulated in other comprehensive income remains in the fair value reserve (non-recycling) until the investment is disposed of. At the time of disposal, the amount accumulated in the fair value reserve (non-recycling) is transferred to retained earnings. It is not recycled through profit or loss. Dividends from an investment in equity securities, irrespective of whether classified as at FVPL or FVOCI, are recognised in profit or loss as other income in accordance with the policy set out in Note 3(q)(ii).

(B) Policy applicable prior to 1 January 2018

The Group's investments in equity securities are classified as available-for-sale financial assets. At the end of each reporting period the fair value is remeasured, with any resultant gain or loss being recognised in other comprehensive income and accumulated separately in equity in the fair value reserve. As an exception to this, investments in equity securities that do not have a quoted price in an active market for an identical instrument and whose fair value cannot otherwise be reliably measured are recognised in the statement of financial position at cost less impairment losses (see Note 3(g)). Dividend income from equity securities calculated using the effective interest method are recognised in profit or loss in accordance with the policies set out in Note 3(q)(ii).

When the investments are derecognised or impaired (see Note 3(g)), the cumulative gain or loss recognised in equity is reclassified to profit or loss. Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments or they expire.

3 Significant accounting policies (continued)

(e) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses (see Note 3(g)).

The cost of self-constructed items of property, plant and equipment includes the cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads and borrowing costs (see Note 3(s)).

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognised in profit or loss on the date of retirement or disposal.

Depreciation is calculated to write-off the cost of items of property, plant and equipment, less their estimated residual value, if any, using the straight line method over their estimated useful lives as follows:

–	Plant and buildings	20–40 years
–	Machinery	10–20 years
–	Motor vehicles	8 years
–	Office equipment and others	5 years

Where parts of an item of property, plant and equipment have different useful lives, the cost of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reviewed annually.

Construction in progress represents plant and buildings under construction and equipment pending installation, and is stated at cost less impairment losses (see Note 3(g)). Cost comprises direct costs of construction as well as interest charges during the year of construction and installation. Capitalisation of these costs ceases and the construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use, notwithstanding any delays in the issue of the relevant commissioning certificates by the relevant authorities in the People's Republic of China (the "PRC").

No depreciation is provided in respect of construction in progress until it is substantially complete and ready for its intended use.

3 Significant accounting policies (continued)

(f) Leased assets

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if the Group determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made based on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

(i) Classification of assets leased to the Group

Assets that are held by the Group under leases which transfer to the Group substantially all the risks and rewards of ownership are classified as being held under finance leases. Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases.

(ii) Operating lease charges

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to profit or loss in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognised in profit or loss as an integral part of the aggregate net lease payments made. Contingent rentals are charged to profit or loss in the accounting period in which they are incurred.

Lease prepayments in the consolidated statement of financial position represent the cost of land use rights paid to the PRC land bureau. Land use rights are carried at cost less accumulated amortisation and accumulated impairment losses (see Note 3(g)). Amortisation is charged to the consolidated statement of profit or loss on a straight-line basis over the respective periods of the rights.

(g) Credit losses and impairment of assets

(i) Credit losses from financial instruments

(A) Policy applicable from 1 January 2018

The Group recognises a loss allowance for expected credit losses (ECLs) on the following items:

– financial assets measured at amortised cost (including cash and cash equivalents, time deposits, pledged deposits and trade and other receivables);

Financial assets measured at fair value, including equity securities measured at FVPL and equity securities designated at FVOCI (non-recycling), are not subject to the ECL assessment.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(A) Policy applicable from 1 January 2018 (continued)

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of all expected cash shortfalls (i.e. the difference between the cash flows due to the Group in accordance with the contract and the cash flows that the Group expects to receive).

The expected cash shortfalls are discounted using the following discount rates where the effect of discounting is material:

– fixed-rate financial assets and trade and other receivables: effective interest rate determined at initial recognition or an approximation thereof;

– variable-rate financial assets: current effective interest rate;

The maximum period considered when estimating ECLs is the maximum contractual period over which the Group is exposed to credit risk.

In measuring ECLs, the Group takes into account reasonable and supportable information that is available without undue cost or effort. This includes information about past events, current conditions and forecasts of future economic conditions.

ECLs are measured on either of the following bases:

– 12-month ECLs: these are losses that are expected to result from possible default events within the 12 months after the reporting date; and

– lifetime ECLs: these are losses that are expected to result from all possible default events over the expected lives of the items to which the ECL model applies.

Loss allowance for trade receivables are always measured at an amount equal to lifetime ECLs. ECLs on these financial assets are estimated using a provision matrix based on the Group's historical credit loss experience, adjusted for factors that are specific to the debtors and an assessment of both the current and forecast general economic conditions at the reporting date.

For all other financial instruments, the Group recognises a loss allowance equal to 12-month ECLs unless there has been a significant increase in credit risk of the financial instrument since initial recognition, in which case the loss allowance is measured at an amount equal to lifetime ECLs.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(A) Policy applicable from 1 January 2018 (continued)

Significant increases in credit risk

In assessing whether the credit risk of a financial instrument has increased significantly since initial recognition, the Group compares the risk of default occurring on the financial instrument assessed at the reporting date with that assessed at the date of initial recognition. In making this reassessment, the Group considers that a default event occurs when (i) the debtor is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held); or (ii) the financial asset is 1 year past due. The Group considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available without undue cost or effort.

In particular, the following information is taken into account when assessing whether credit risk has increased significantly since initial recognition:

– failure to make payments of principal or interest on their contractually due dates ;

– an actual or expected significant deterioration in a financial instrument's external or internal credit rating (if available);

– an actual or expected significant deterioration in the operating results of the debtor; and

– existing or forecast changes in the technological, market, economic or legal environment that have a significant adverse effect on the debtor's ability to meet its obligation to the Group.

Depending on the nature of the financial instruments, the assessment of a significant increase in credit risk is performed on either an individual basis or a collective basis. When the assessment is performed on a collective basis, the financial instruments are grouped based on shared credit risk characteristics, such as past due status and credit risk ratings.

ECLs are remeasured at each reporting date to reflect changes in the financial instrument's credit risk since initial recognition. Any change in the ECL amount is recognised as an impairment gain or loss in profit or loss. The Group recognises an impairment gain or loss for all financial instruments with a corresponding adjustment to their carrying amount through a loss allowance account, except for investments in debt securities that are measured at FVOCI (recycling), for which the loss allowance is recognised in other comprehensive income and accumulated in the fair value reserve (recycling).

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(A) Policy applicable from 1 January 2018 (continued)

Basis of calculation of interest income

Interest income recognised in accordance with Note 3(q)(iii) is calculated based on the gross carrying amount of the financial asset unless the financial asset is credit-impaired, in which case interest income is calculated based on the amortised cost (i.e. the gross carrying amount less loss allowance) of the financial asset.

At each reporting date, the Group assesses whether a financial asset is credit-impaired. A financial asset is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable events:

– significant financial difficulties of the debtor;

– a breach of contract, such as a default or delinquency in interest or principal payments;

– it becoming probable that the borrower will enter into bankruptcy or other financial reorganisation;

– significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor; or

– the disappearance of an active market for a security because of financial difficulties of the issuer.

Write-off policy

The gross carrying amount of a financial asset, lease receivable or contract asset is written-off (either partially or in full) to the extent that there is no realistic prospect of recovery. This is generally the case when the Group determines that the debtor does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off.

Subsequent recoveries of an asset that was previously written-off are recognised as a reversal of impairment in profit or loss in the period in which the recovery occurs.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(B) Policy applicable prior to 1 January 2018

Prior to 1 January 2018, an "incurred loss" model was used to measure impairment losses on financial assets not classified as at FVPL (e.g. trade and other receivables, available-for-sale investments and held-to-maturity debt securities). Under the "incurred loss" model, an impairment loss was recognised only when there was objective evidence of impairment. Objective evidence of impairment included:

– significant financial difficulties of the debtor;

– a breach of contract, such as a default or delinquency in interest or principal payments;

– it becoming probable that the debtor will enter bankruptcy or other financial reorganisation;

– significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor; or

– a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost.

If any such evidence existed, an impairment loss was determined and recognised as follows:

– For trade and other receivables and other financial assets carried at amortised cost, impairment loss was measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate, where the effect of discounting was material. This assessment was made collectively where these financial assets shared similar risk characteristics, such as similar past due status, and had not been individually assessed as impaired. Future cash flows for financial assets which were assessed for impairment collectively were based on historical loss experience for assets with credit risk characteristics similar to the collective Group.

  If in a subsequent period the amount of an impairment loss decreased and the decrease could be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss was reversed through profit or loss. A reversal of an impairment loss was only recognised to the extent that it did not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(B) Policy applicable prior to 1 January 2018 (continued)

When the recovery of a trade debtor or other financial assets carried at amortised cost was considered doubtful but not remote, associated impairment losses were recorded using an allowance account. When the Group was satisfied that recovery was remote, the amount considered irrecoverable was written off against the gross carrying amount of those assets directly. Subsequent recoveries of amounts previously charged to the allowance account were reversed against the allowance account. Other changes in the allowance account and subsequent recoveries of amounts previously written off directly were recognised in profit or loss.

– For available-for-sale investments, the cumulative loss that had been recognised in the fair value reserve (recycling) was reclassified to profit or loss. The amount of the cumulative loss that was recognised in profit or loss was the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

  Impairment losses recognised in profit or loss in respect of available-for-sale equity securities were not reversed through profit or loss. Any subsequent increase in the fair value of such assets was recognised in other comprehensive income.

  Impairment losses recognised in profit or loss in respect of available-for-sale debt securities were reversed if the subsequent increase in fair value could be objectively related to an event occurring after the impairment loss was recognised. Reversals of impairment losses in such circumstances were recognised in profit or loss.

– If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through profit or loss. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

– For available-for-sale securities, the cumulative loss that has been recognised in the fair value reserve is reclassified to profit or loss. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(i) Credit losses from financial instruments (continued)

(B) Policy applicable prior to 1 January 2018 (continued)

– Impairment losses recognised in profit or loss in respect of available-for-sale equity securities are not reversed through profit or loss. Any subsequent increase in the fair value of such assets is recognised in other comprehensive income.

– Impairment losses in respect of available-for-sale debt securities are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognised. Reversals of impairment losses in such circumstances are recognised in profit or loss.

Impairment losses are written-off against the corresponding assets directly, except for impairment losses recognised in respect of trade debtors and bills receivable included within trade and other receivables, whose recovery is considered doubtful but not remote. In this case, the impairment losses for doubtful debts are recorded using an allowance account. When the Group is satisfied that recovery is remote, the amount considered irrecoverable is written-off against trade debtors and bills receivable directly and any amounts held in the allowance account relating to that debt are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other changes in the allowance account and subsequent recoveries of amounts previously written-off directly are recognised in profit or loss.

(ii) Impairment of other non-current assets

Internal and external sources of information are reviewed at the end of each reporting period to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognised no longer exists or may have decreased:

– property, plant and equipment;

– prepayments for leasehold land classified as being held under an operating lease;

– goodwill; and

– investments in subsidiaries, associates and joint venture in the Company's statement of financial position.

3 Significant accounting policies (continued)

(g) Credit losses and impairment of assets (continued)

(ii) Impairment of other non-current assets (continued)

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually whether or not there is any indication of impairment:

– *Calculation of recoverable amount*

The recoverable amount of an asset is the greater of its fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

– *Recognition of impairment losses*

An impairment loss is recognised in profit or loss if the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs of disposal (if measurable) or value in use (if determinable).

– *Reversals of impairment losses*

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the year in which the reversals are recognised.

(iii) Interim financial reporting and impairment

Under the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited, the Group is required to prepare an interim financial report in compliance with IAS 34, *Interim financial reporting*, in respect of the first six months of the financial year. At the end of the interim period, the Group applies the same impairment testing, recognition, and reversal criteria as it would at the end of the financial year (see Notes 3(g)(i) and 3(g)(ii)).

Impairment losses recognised in an interim period in respect of goodwill are not reversed in a subsequent period. This is the case even if no loss, or a smaller loss, would have been recognised had the impairment been assessed only at the end of the financial year to which the interim period relates.

3 Significant accounting policies (continued)

(h) Inventories

Inventories are assets which are held for sale in the ordinary course of business, 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 carried at the lower of cost and net realisable value.

Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised.

The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(i) Contract assets and contract liabilities

A contract asset is recognised when the Group recognises revenue (see Note 3(q)) before being unconditionally entitled to the consideration under the payment terms set out in the contract. Contract assets are assessed for expected credit losses (ECL) in accordance with the policy set out in Note 3(g)(i) and are reclassified to receivables when the right to the consideration has become unconditional (see Note 3(j)).

A contract liability is recognised when the customer pays non-refundable consideration before the Group recognises the related revenue (see Note 3(q)). A contract liability would also be recognised if the Group has an unconditional right to receive non-refundable consideration before the Group recognises the related revenue. In such cases, a corresponding receivable would also be recognised (see Note 3(j)).

For a single contract with the customer, either a net contract asset or a net contract liability is presented. For multiple contracts, contract assets and contract liabilities of unrelated contracts are not presented on a net basis.

3 Significant accounting policies (continued)

(i) Contract assets and contract liabilities (continued)

Policy prior to 1 January 2018

In the comparative period, amounts received before the related goods were delivered were presented as "advances received" under "trade and other payables". These balances has been reclassified on 1 January 2018 as shown in Note 27 (see Note 4(c)(iv)).

(j) Trade and other receivables

A receivable is recognised when the Group has an unconditional right to receive consideration. A right to receive consideration is unconditional if only the passage of time is required before payment of that consideration is due. If revenue has been recognised before the Group has an unconditional right to receive consideration, the amount is presented as a contract asset (see Note 3(i)).

Receivables are stated at amortised cost using the effective interest method less allowance for credit losses (see Note 3(g)(i)).

(k) Interest-bearing borrowings

Interest-bearing borrowings are measured initially at fair value less transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method. Interest expense is recognised in accordance with the Group's accounting policy for borrowing costs (see Note 3(s)).

(l) Trade and other payables

Trade and other payables are initially recognised at fair value and subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(m) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the consolidated cash flow statement. Cash and cash equivalents are assessed for expected credit losses (ECL) in accordance with the policy set out in Note 3(g)(i).

3 Significant accounting policies (continued)

(n) Employee benefits

(i) Short-term employee benefits and contributions to defined contribution retirement plans

Salaries, annual bonuses, paid annual leave, contributions to defined contribution retirement plans and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Share-based payments

The fair value of share options granted to employees is recognised as an employee cost with a corresponding increase in a capital reserve within equity. The fair value is measured at grant date using the binomial lattice model, taking into account the terms and conditions upon which the options were granted. Where the employees have to meet vesting conditions before becoming unconditionally entitled to the options, the total estimated fair value of the options is spread over the vesting period, taking into account the probability that the options will vest.

During the vesting period, the number of share options that is expected to vest is reviewed. Any resulting adjustment to the cumulative fair value recognised in prior years is charged/credited to the profit or loss for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognised as an expense is adjusted to reflect the actual number of options that vest (with a corresponding adjustment to the capital reserve) except where forfeiture is only due to not achieving vesting conditions that relate to the market price of the Company's shares. The equity amount is recognised in the capital reserve until either the option is exercised (when it is included in the amount recognised in share capital and share premium for the shares issued) or the option expires (when it is released directly to retained profits).

(o) Income tax

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to items recognised in other comprehensive income or directly in equity, in which case the relevant amounts of tax are recognised in other comprehensive income or directly in equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

3 Significant accounting policies (continued)

(o) Income tax (continued)

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria is adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination), and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the end of the reporting period. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at the end of each reporting period and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

Additional income taxes that arise from the distribution of dividends are recognised when the liability to pay the related dividends is recognised.

3 Significant accounting policies (continued)

(o) Income tax (continued)

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or

- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  - the same taxable entity; or

  - different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

(p) Provisions and contingent liabilities

Provisions are recognised when the Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(q) Revenue and other income

Income is classified by the Group as revenue when it arises from the sale of goods in the ordinary course of the Group's business.

Revenue is recognised when control over a product is transferred to the customer, at the amount of promised consideration to which the Group is expected to be entitled, excluding those amounts collected on behalf of third parties. Revenue excludes value added tax or other sales taxes and is after deduction of any trade discounts.

Further details of the Group's revenue and other income recognition policies are as follows:

3 Significant accounting policies (continued)

(q) Revenue and other income (continued)

(i) Sales of goods

Revenue is recognised when the the goods are shipped from the Group's warehouses, delivered at the customers' premises, or loaded on board. If the products are a partial fulfilment of a contract covering other goods, then the amount of revenue recognised is an appropriate proportion of the total transaction price under the contract, allocated between all the goods promised under the contract on a relative stand-alone selling price basis.

Revenue from sales of goods was recognised on a similar basis in the comparative period under IAS 18.

(ii) Dividends

– Dividend income from unlisted investments is recognised when the shareholder's right to receive payment is established.

– Dividend income from listed investments is recognised when the share price of the investment goes ex-dividend.

(iii) Interest income

Interest income is recognised as it accrues under the effective interest method using the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to the gross carrying amount of the financial asset. For financial assets measured at amortised cost that are not credit-impaired, the effective interest rate is applied to the gross carrying amount of the asset. For credit-impaired financial assets, the effective interest rate is applied to the amortised cost (i.e. gross carrying amount net of loss allowance) of the asset (see Note 3(g)(i)).

(iv) Government grants

Government grants are recognised in the statement of financial position initially when there is reasonable assurance that they will be received and that the Group will comply with the conditions attaching to them. Grants that compensate the Group for expenses incurred are recognised as income in profit or loss on a systematic basis in the same periods in which the expenses are incurred. A government grant related to an asset is recognised initially as deferred income and amortised to profit or loss on a straight-line basis over the useful life of the asset.

3 Significant accounting policies (continued)

(r) Translation of foreign currencies

Foreign currency transactions during the year are translated at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the end of the reporting period. Exchange gains and losses are recognised in profit or loss, except those arising from foreign currency borrowings used to hedge a net investment in a foreign operation which are recognised in other comprehensive income.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. The transaction date is the date on which the Group initially recognises such non-monetary assets or liabilities. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was measured.

The results of foreign operations are translated into Renminbi ("RMB") at the exchange rates approximating the foreign exchange rates ruling at the dates of the transactions. Statement of financial position items are translated into RMB at the closing foreign exchange rates at the end of the reporting period. The resulting exchange differences are recognised in other comprehensive income and accumulated separately in equity in the exchange reserve.

On disposal of a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation is reclassified from equity to profit or loss when the profit or loss on disposal is recognised.

(s) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset. Other borrowing costs are expensed in the period in which they are incurred.

The capitalisation of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalisation of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

3 Significant accounting policies (continued)

(t) Related parties

(a) A person, or a close member of that person's family, is related to the Group if that person:

(i) has control or joint control over the Group;

(ii) has significant influence over the Group; or

(iii) is a member of the key management personnel of the Group or the Group's parent.

(b) An entity is related to the Group if any of the following conditions applies:

(i) The entity and the Group are members of the same Group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a Group of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group.

(vi) The entity is controlled or jointly controlled by a person identified in (a)(i).

(vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(viii) The entity, or any member of a Group of which it is a part, provides key management personnel services to the Group or to the Group's parent.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.

3 Significant accounting policies (continued)

(u) Segment reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the Chairman (the chief operating decision maker) for the purposes of allocating resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of products and services, the nature of production processes, the type or class of customers, the methods used to distribute the products or provide the services, and the nature of the regulatory environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

4 Changes in accounting policies

(a) Overview

The IASB has issued a number of new IFRSs and amendments to IFRSs that are first effective for the current accounting period of the Group. Of these, the following developments are relevant to the Group's financial statements:

- IFRS 9, *Financial instruments*
- IFRS 15, *Revenue from contracts with customers*
- IFRIC 22, *Foreign currency transactions and advance consideration*

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period, except for the amendments to IFRS 9, *Prepayment features with negative compensation* which have been adopted at the same time as IFRS 9.

4 Changes in accounting policies (continued)

(b) IFRS 9, *Financial instruments*, including the amendments to IFRS 9, *Prepayment features with negative compensation*

IFRS 9 replaces IAS 39, *Financial instruments: recognition and measurement*. It sets out the requirements for recognising and measuring financial assets, financial liabilities and certain contracts to buy or sell non-financial items.

The Group has applied IFRS 9 retrospectively to items that existed at 1 January 2018 in accordance with the transition requirements. The Group has recognised the cumulative effect of initial application as an adjustment to opening equity at 1 January 2018. Therefore, comparative information continues to be reported under IAS 39.

The following is a summary of the impact of transition to IFRS 9 on retained earnings and reserves and the related tax impact at 1 January 2018.

	RMB'000
Retained earnings	
Recognition of additional expected credit losses:	
– Interest in associates	(409)
– Interest in joint ventures	(2,083)
– Trade and other receivables	(34,871)
Related tax	5,466
Net decrease in retained earnings at 1 January 2018	(31,897)
Fair value reserve (recycling)	
Transferred to fair value reserve (non-recycling) relating to equity securities now measured at FVOCI and decrease in fair value reserve (recycling) at 1 January 2018	(53,975)
Fair value reserve (non-recycling)	
Transferred from fair value reserve (recycling) relating to equity securities now measured at FVOCI and increase in fair value reserve (non-recycling) at 1 January 2018	53,975

4 Changes in accounting policies (continued)

(b) IFRS 9, *Financial instruments*, including the amendments to IFRS 9, *Prepayment features with negative compensation* (continued)

Further details of the nature and effect of the changes to previous accounting policies and the transition approach are set out below:

(i) Classification of financial assets and financial liabilities

IFRS 9 categories financial assets into three principal classification categories: measured at amortised cost, at fair value through other comprehensive income (FVOCI) and at fair value through profit or loss (FVPL). These supersede IAS 39's categories of held-to-maturity investments, loans and receivables, available-for-sale financial assets and financial assets measured at FVPL. The classification of financial assets under IFRS 9 is based on the business model under which the financial asset is managed and its contractual cash flow characteristics.

The following table shows the original measurement categories for each class of the Group's financial assets under IAS 39 and reconciles the carrying amounts of those financial assets determined in accordance with IAS 39 to those determined in accordance with IFRS 9.

	IAS 39 carrying amount at 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount at 1 January 2018
	RMB'000	RMB'000	RMB'000	RMB'000
Financial assets carried at amortised cost				
Trade and other receivables	2,044,171	–	(34,871)	2,009,300
Pledged deposits	241,380	–	–	241,380
Time deposits	500,000	–	–	500,000
Cash and cash equivalents	219,798	–	–	219,798
	3,005,349	–	(34,871)	2,970,478
Financial assets measured at FVOCI (non-recyclable)				
Equity securities not held for trading (Note)	–	88,900	–	88,900
Financial assets classified as available-for-sale under IAS 39 (Note)	88,900	(88,900)	–	–

4 Changes in accounting policies (continued)

(b) IFRS 9, *Financial instruments*, including the amendments to IFRS 9, *Prepayment features with negative compensation* (continued)

(i) Classification of financial assets and financial liabilities (continued)

Note: Under IAS 39, equity securities not held for trading were classified as available-for-sale financial assets. These equity securities are classified at FVPL under IFRS 9, unless they are eligible for and designated at FVOCI by the Group. At 1 January 2018, the Group designated its investment in Bank of Jiangsu, Xiamen Chuangfeng Yizhi Investment Management Partnership and Nanjing Xiaomuma Technology Co., Ltd. at FVOCI (non-recycling), as the investments are held for strategic purposes.

For an explanation of how the Group classifies and measures financial assets and recognises related gains and losses under IFRS 9, see respective accounting policy notes in Notes 3(d), (g)(i), (j) and (m).

The measurement categories for all financial liabilities remain the same. The carrying amounts for all financial liabilities (including financial guarantee contracts) at 1 January 2018 have not been impacted by the initial application of IFRS 9.

The Group did not designate or de-designate any financial asset or financial liability at FVPL at 1 January 2018.

(ii) Credit losses

IFRS 9 replaces the "incurred loss" model in IAS 39 with the "expected credit loss" (ECL) model. The ECL model requires an ongoing measurement of credit risk associated with a financial asset and therefore recognises ECLs earlier than under the "incurred loss" accounting model in IAS 39.

The Group applies the new ECL model to the following items:

– financial assets measured at amortised cost (including cash and cash equivalents, pledged deposits, time deposits and trade and other receivables)

For further details on the Group's accounting policy for accounting for credit losses, see Note 3(g)(i).

The following table reconciles the closing loss allowance for trade and other receivables determined in accordance with IAS 39 as at 31 December 2017 with the opening loss allowance determined in accordance with IFRS 9 as at 1 January 2018.

	RMB'000
Loss allowance at 31 December 2017 under IAS 39	38,359
Additional credit loss recognised at 1 January 2018 on:	
– Trade and other receivables	34,871
Loss allowance at 1 January 2018 under IFRS 9	73,230

4 Changes in accounting policies (continued)

(b) IFRS 9, *Financial instruments*, including the amendments to IFRS 9, *Prepayment features with negative compensation* (continued)

(iii) Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below:

- Information relating to comparative periods has not been restated. Differences in the carrying amounts of financial assets resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 continues to be reported under IAS 39 and thus may not be comparable with the current period.

- The following assessments have been made on the basis of the facts and circumstances that existed at 1 January 2018 (the date of initial application of IFRS 9 by the Group):

  - the determination of the business model within which a financial asset is held; and

  - the designation of certain investments in equity instruments not held for trading to be classified as at FVOCI (non-recycling).

- If, at the date of initial application, the assessment of whether there has been a significant increase in credit risk since initial recognition would have involved undue cost or effort, a lifetime ECL has been recognised for that financial instrument.

(c) IFRS 15, *Revenue from contracts with customers*

IFRS 15 establishes a comprehensive framework for recognising revenue and certain costs from contracts with customers. IFRS 15 replaces IAS 18, *Revenue*, which covered revenue arising from sale of goods and rendering of services, and IAS 11, *Construction contracts*, which specified the accounting for construction contracts.

IFRS 15 also introduces additional qualitative and quantitative disclosure requirements which aim to enable users of the financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

The Group has elected to use the cumulative effect transition method and no material cumulative effect of initial application shall be recognised as an adjustment to the opening balance of equity at 1 January 2018. Therefore, comparative information has not been restated and continues to be reported under IAS 18.

Further details of the nature and effect of the changes on previous accounting policies are set out below:

4 Changes in accounting policies (continued)

(c) IFRS 15, *Revenue from contracts with customers* (continued)

(i) Timing of revenue recognition

Previously, revenue arising from construction contracts and provision of services was recognised over time, whereas revenue from sale of goods was generally recognised at a point in time when the risks and rewards of ownership of the goods had passed to the customers.

Under IFRS 15, revenue is recognised when the customer obtains control of the promised good or service in the contract. This may be at a single point in time or over time. IFRS 15 identifies the following three situations in which control of the promised good or service is regarded as being transferred over time:

A. When the customer simultaneously receives and consumes the benefits provided by the entity's performance, as the entity performs;

B. When the entity's performance creates or enhances an asset (for example work in progress) that the customer controls as the asset is created or enhanced;

C. When the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.

If the contract terms and the entity's activities do not fall into any of these 3 situations, then under IFRS 15 the entity recognises revenue for the sale of that good or service at a single point in time, being when control has passed. Transfer of risks and rewards of ownership is only one of the indicators that is considered in determining when the transfer of control occurs.

The adoption of IFRS 15 does not have a material impact on when the Group recognises revenue from sales of goods.

(ii) Significant financing component

IFRS 15 requires an entity to adjust the transaction price for the time value of money when a contract contains a significant financing component, regardless of whether the payments from customers are received significantly in advance of revenue recognition or significantly deferred.

Previously, the Group only applied such a policy when payments were significantly deferred, which was not common in the Group's arrangements with its customers. The Group did not apply such a policy when payments were received in advance.

This change in accounting policy had no material impact on opening balances as at 1 January 2018.

4 Changes in accounting policies (continued)

(c) IFRS 15, *Revenue from contracts with customers* (continued)

(iii) Sales commissions payable related to sales contracts

The Group previously recognised sales commissions payable related to sales contracts as distribution expenses when they were incurred. Under IFRS 15, the Group is required to capitalise these sales commissions as costs of obtaining contracts when they are incremental and are expected to be recovered, unless the expected amortisation period is one year or less from the date of initial recognition of the asset, in which case the sales commissions can be expensed when incurred. Capitalised commissions are charged to profit or loss when the revenue from the related sale is recognised and are included as distribution expenses at that time.

This change in accounting policy had no material impact on opening balances as at 1 January 2018.

(iv) Presentation of contract assets and liabilities

Under IFRS 15, a receivable is recognised only if the Group has an unconditional right to consideration. If the Group recognises the related revenue before being unconditionally entitled to the consideration for the promised goods and services in the contract, then the entitlement to consideration is classified as a contract asset. Similarly, a contract liability, rather than a payable, is recognised when a customer pays consideration, or is contractually required to pay consideration and the amount is already due, before the Group recognises the related revenue. For a single contract with the customer, either a net contract asset or a net contract liability is presented. For multiple contracts, contract assets and contract liabilities of unrelated contracts are not presented on a net basis (see Note 3(i)).

Previously, contract liabilities relating to sales contracts were presented in the consolidated statement of financial position under "trade and bills payables" included in trade and other payables. To reflect these changes in presentation, the Group has made the following adjustment at 1 January 2018, as a result of the adoption of IFRS 15:

– Advances received amounting to RMB36,717,000, which were previously recorded under "trade and bills payables" are now presented under "contract liabilities" included in trade and other payables (Note 27)

(d) IFRIC 22, *Foreign currency transactions and advance consideration*

This interpretation provides guidance on determining "the date of the transaction" for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) arising from a transaction in which an entity receives or pays advance consideration in a foreign currency.

The Interpretation clarifies that "the date of the transaction" is the date on initial recognition of the non-monetary asset or liability arising from the payment or receipt of advance consideration. If there are multiple payments or receipts in advance of recognising the related item, the date of the transaction for each payment or receipt should be determined in this way.

The adoption of IFRIC 22 does not have any material impact on the financial position and the financial result of the Group.

5 Revenue and segment reporting

(a) Revenue

Revenue represents mainly the sales value of high alloy steel, (including die steel ("DS") and high speed steel ("HSS")), cutting tools, titanium alloy and trading of goods after eliminating intercompany transactions. Further details regarding the Group's revenue are disclosed in Note 5(b).

(i) Disaggregation of revenue

Disaggregation of revenue from contracts with customers by products divisions is as follows:

	2018 **RMB'000**	2017 RMB'000 (Note)
DS	**2,098,110**	1,686,470
HSS	**782,015**	654,440
Cutting tools	**581,232**	530,212
Titanium alloy	**245,155**	168,164
Trading of goods	**1,315,034**	859,157
	5,021,546	3,898,443

Note: The Group has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated and was prepared in accordance with IAS 18 (see Note 4(c)).

The Group's revenue from contracts with customers was recognised at point in time. Disaggregation of revenue from contracts with customers by geographic markets is disclosed in Note 5(b)(iii).

The Group's customer base is diversified and includes only one customer (2017: one customer) with whom transactions have exceeded 10% of the Group's revenue. In 2018 revenue from trading of goods to these customers, amounted to RMB1,272,964,000 (2017: RMB841,500,000) and arose in the PRC in which trading of goods segment is active. Details of concentrations of credit risk arising from this customer are set out in Note 32(a).

(ii) Revenue expected to be recognised in the future arising from contracts with customers in existence at the reporting date

As at 31 December 2018, the Group has applied the practical expedient in paragraph 121 of IFRS 15 to its sales contracts for goods such that information about revenue expected to be recognised in the future is not disclosed in respect of revenue that the Group will be entitled to when it satisfies the remaining performance obligations under the contracts for sales of goods that had an expected duration of one year or less.

5 Revenue and segment reporting (continued)

(b) Segment reporting

The Group has five reportable segments, as described below, which are the Group's product divisions. For each of the product divisions, the Chairman (the chief operating decision maker) reviews internal management reports on at least a monthly basis. No operating segments have been aggregated to form the following reportable segments. The following summary describes the operations in each of the Group's reportable segments:

– *DS* The DS segment manufactures and sells materials that are used in the die set manufacturing industry.

– *HSS* The HSS segment manufactures and sells materials that are used in the tools manufacturing industry.

– *Cutting tools* The cutting tools segment manufactures and sells HSS and carbide cutting tools to the tooling industry.

– *Titanium alloy* The titanium alloy segment manufactures and sells titanium alloys to the titanium industry.

– *Trading of goods* The trading of goods segment sells general carbon steel products that are not within the Group's production scope.

5 Revenue and segment reporting (continued)

(b) Segment reporting (continued)

(i) Segment results, assets and liabilities

For the purposes of assessing segment performance and allocating resources between segments, the Chairman (the chief operating decision maker) monitors the results, assets and liabilities attributable to each reportable segment on the following basis:

Segment assets include all tangible, intangible assets and current assets with the exception of interest in associates, interest in joint ventures, other financial assets, pledged deposits, time deposits, cash and cash equivalents, deferred tax assets and other head office and corporate assets. Segment liabilities include bills payable, trade and non-trade payables, deferred income and accrued expenses attributable to the manufacturing and sales activities of the individual segments with the exception of interest-bearing borrowings, current taxation, deferred tax liabilities and other head office and corporate liabilities.

Revenue and expenses are allocated to the reportable segments with reference to sales generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

The measure used for reporting segment profit is "adjusted EBIT", i.e. "adjusted earnings before interest and taxes", where "interest" is regarded as net finance costs. To arrive at adjusted EBIT, the Group's earnings are further adjusted for items not specifically attributed to individual segments, such as share of profits less losses of associates and joint ventures and other head office or corporate administration costs.

In addition to receiving segment information concerning adjusted EBIT, management is provided with segment information concerning revenue (including inter-segment revenue) generated by the segments in their operations. Inter-segment revenue is priced with reference to prices charged to external parties for similar orders.

5 Revenue and segment reporting (continued)

(b) Segment reporting (continued)

(i) Segment results, assets and liabilities (continued)

Information regarding the Group's reportable segments as provided to the Chairman (the chief operating decision maker) for the purposes of resource allocation and assessment of segment performance for the years ended 31 December 2018 and 2017 is set out below.

	Year ended and as at 31 December 2018					
	DS RMB'000	**HSS RMB'000**	**Cutting tools RMB'000**	**Titanium alloy RMB'000**	**Trading of goods RMB'000**	**Total RMB'000**
Revenue from external customers	**2,098,110**	**782,015**	**581,232**	**245,155**	**1,315,034**	**5,021,546**
Inter-segment revenue	**–**	**242,524**	**–**	**–**	**–**	**242,524**
Reportable segment revenue	**2,098,110**	**1,024,539**	**581,232**	**245,155**	**1,315,034**	**5,264,070**
Reportable segment profit (adjusted EBIT)	**283,514**	**145,499**	**64,823**	**35,743**	**327**	**529,906**
Reportable segment assets	**3,895,601**	**2,182,621**	**1,369,391**	**562,837**	**31**	**8,010,481**
Reportable segment liabilities	**1,343,658**	**363,104**	**179,345**	**56,315**	**–**	**1,942,422**

	Year ended and as at 31 December 2017 (Note)					
	DS RMB'000	HSS RMB'000	Cutting tools RMB'000	Titanium alloy RMB'000	Trading of goods RMB'000	Total RMB'000
Revenue from external customers	1,686,470	654,440	530,212	168,164	859,157	3,898,443
Inter-segment revenue	–	109,355	–	–	–	109,355
Reportable segment revenue	1,686,470	763,795	530,212	168,164	859,157	4,007,798
Reportable segment profit (adjusted EBIT)	216,646	112,469	58,584	23,623	1,824	413,146
Reportable segment assets	3,234,273	2,302,430	1,404,979	543,472	10	7,485,164
Reportable segment liabilities	786,721	308,703	176,268	52,702	–	1,324,394

Note: The Group has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated and was prepared in accordance with IAS 18 (see Note 4(c)).

5 Revenue and segment reporting (continued)

(b) Segment reporting (continued)

(ii) Reconciliations of reportable segment revenue, profit or loss, assets and liabilities

	2018 RMB'000	2017 RMB'000
Revenue		
Reportable segment revenue	**5,264,070**	4,007,798
Elimination of inter-segment revenue	**(242,524)**	(109,355)
Consolidated revenue (Note 5(a))	**5,021,546**	3,898,443

	2018 RMB'000	2017 RMB'000
Profit		
Reportable segment profit	**529,906**	413,146
Net finance costs	**(134,838)**	(112,410)
Share of profits/(losses) of associates	**2,349**	(4,805)
Share of profits of joint ventures	**10,893**	602
Unallocated head office and corporate expenses	**(127,742)**	(78,436)
Consolidated profit before taxation	**280,568**	218,097

5 Revenue and segment reporting (continued)

(b) Segment reporting (continued)

(ii) Reconciliations of reportable segment revenue, profit or loss, assets and liabilities (continued)

	2018 RMB'000	2017 RMB'000
Assets		
Reportable segment assets	**8,010,481**	7,485,164
Interest in associates	**51,905**	49,372
Interest in joint ventures	**33,813**	26,263
Other financial assets	**100,024**	88,900
Deferred tax assets	**25,195**	23,954
Trading securities	**1,482**	–
Pledged deposits	**464,500**	241,380
Time deposits	**717,414**	500,000
Cash and cash equivalents	**583,235**	219,798
Unallocated head office and corporate assets	**48,303**	69,049
Consolidated total assets	**10,036,352**	8,703,880

	2018 RMB'000	2017 RMB'000
Liabilities		
Reportable segment liabilities	**1,942,422**	1,324,394
Interest-bearing borrowings	**3,183,779**	2,993,292
Current taxation	**117**	4,164
Deferred tax liabilities	**62,268**	57,201
Unallocated head office and corporate liabilities	**24,806**	21,864
Consolidated total liabilities	**5,213,392**	4,400,915

5 Revenue and segment reporting (continued)

(b) Segment reporting (continued)

(iii) Geographical information

The Group's business is managed on a worldwide basis, but participates in four principal economic geographies, the PRC, North America, Europe and Asia (other than the PRC).

In presenting geographical information, segment revenue is based on the geographical location of customers. Substantially all of the Group's assets and liabilities are located in the PRC and accordingly, no geographical analysis of segment assets, liabilities and capital expenditure is provided.

	2018	2017
	RMB'000	RMB'000
Revenue		
The PRC	**3,249,457**	2,571,367
North America	**548,031**	404,171
Europe	**882,839**	672,417
Asia (other than the PRC)	**299,530**	226,063
Others	**41,689**	24,425
Total	**5,021,546**	3,898,443

6 Other income

	Notes	2018 RMB'000	2017 RMB'000
Government grants	(i)	**33,270**	53,815
Sales of scrap materials		**3,239**	256
Net foreign exchange gain		**–**	6,395
Dividend income from listed securities	(ii)	**1,800**	1,780
Disposal gain from trading securities		**–**	545
Net gain on disposal of property, plant and equipment		**1,639**	496
Others		**2,519**	1,327
		42,467	64,614

Note:

(i) The subsidiaries of the Group, including Jiangsu Tiangong Tools Company Limited ("TG Tools"), Tiangong Aihe Company Limited ("TG Aihe") and Jiangsu Tiangong Technology Company Limited ("TG Tech"), located in the PRC, collectively received unconditional grants amounting to RMB27,771,000 (2017: RMB47,375,000) from the local government to reward their contribution to the local economy and encourage technology innovation. TG Tools and TG Tech also recognised amortisation of government grants related to assets of RMB5,499,000 (2017: RMB6,440,000) during the year ended 31 December 2018 (see Note 28).

(ii) The Group received dividends totalling RMB1,800,000 (2017: RMB1,780,000) from a listed equity investment (see Note 19).

7 Other expenses

	Notes	2018 RMB'000	2017 RMB'000
Provision of loss allowance for trade receivables	32(a)	**35,374**	1,049
Net foreign exchange losses		**2,471**	–
Charitable donations		**1,317**	–
Net realised and unrealised losses on trading securities		**947**	–
Others		**646**	1,161
		40,755	2,210

8 Profit before taxation

Profit before taxation is arrived at after charging/(crediting):

(a) Net finance costs

	2018 RMB'000	2017 RMB'000
Interest income	**(7,233)**	(5,795)
Finance income	**(7,233)**	(5,795)
Interest on bank loans	**171,386**	145,860
Less: interest expense capitalised into property, plant and equipment under construction*	**(29,315)**	(27,655)
Finance expenses	**142,071**	118,205
Net finance costs	**134,838**	112,410

* The borrowing costs have been capitalised at a rate of 5.11% per annum (2017: 5.02%).

(b) Staff costs

	2018 RMB'000	2017 RMB'000
Salaries, wages and other benefits	**224,866**	213,726
Contributions to defined contribution retirement plans	**33,862**	29,893
Equity-settled share-based payment expenses (Note 29)	**10,063**	–
	268,791	243,619

The Group participates in defined contribution pension funds managed by the PRC local government authorities. According to the respective pension fund regulations, the Group is required to pay annual contributions determined by the respective authorities in the PRC. The Group remits all the pension fund contributions to the respective social security offices, which are responsible for the payments and liabilities relating to the pension funds. The Group has no obligation for payment of retirement and other post-retirement benefits of employees other than the contributions described above.

8 Profit before taxation (continued)

(c) Other items

	Notes	2018 RMB'000	2017 RMB'000
Cost of inventories*		**4,360,619**	3,399,980
Depreciation of property, plant and equipment	13	**225,673**	220,167
Amortisation of lease prepayments	14	**1,854**	1,749
Provision of loss allowance for trade receivables	32(a)	**35,374**	1,049
Provision/(reversal) of write-down of inventories	21	**1,002**	(16,804)
Operating lease charges		**1,059**	1,367
Auditor's remuneration			
– audit services		**2,650**	2,500
– other services		**–**	100

* Cost of inventories includes RMB364,341,000 (2017: RMB327,223,000) relating to staff costs, depreciation expenses and write-down of inventories which are also included in the respective total amounts disclosed separately above or in Note 8(b) for each of these types of expenses.

9 Income tax in the consolidated statement of profit or loss

(a) Taxation in the consolidated statement of profit or loss represents:

	2018 RMB'000	2017 RMB'000
Current tax		
Provision for PRC taxes (Note 30(a))	**3,199**	31,775
Provision for Hong Kong Profits Tax (Note 30(a))	**245**	–
	3,444	31,775
Deferred tax		
Reversal of temporary differences	**10,154**	11,621
	13,598	43,396

(i) Pursuant to the rules and regulations of the Cayman Islands and British Virgin Islands, the Group is not subject to any income tax in the Cayman Islands or British Virgin Islands.

9 Income tax in the consolidated statement of profit or loss (continued)

(a) Taxation in the consolidated statement of profit or loss represents: (continued)

(ii) The provision for PRC Income Tax is based on the respective corporate income tax rates applicable to the subsidiaries located in the PRC as determined in accordance with the relevant income tax rules and regulations of the PRC.

TG Tools, TG Aihe and TG Tech are subject to a preferential income tax rate of 15% in 2018 available to enterprises which qualify as a High and New Technology Enterprise (2017: 15%).

The statutory corporate income tax rate applicable to the Group's other operating subsidiaries in the PRC is 25% (2017: 25%).

The income tax law of the PRC and its relevant regulations also impose withholding tax at 10%, unless reduced by a tax treaty/arrangement, on dividend distributions made out of the PRC from earnings accumulated from 1 January 2008. Undistributed earnings generated prior to 1 January 2008 are exempted from such withholding tax.

(iii) Hong Kong Profits Tax has been provided for Tiangong Development Hong Kong Company Limited ("TG Development") at the rate of 16.5% (2017: 16.5%) on the estimated assessable profits arising in Hong Kong for the year ended 31 December 2018.

(b) Reconciliation between tax expense and accounting profit at applicable tax rates:

	2018 **RMB'000**	2017 RMB'000
Profit before taxation	**280,568**	218,097
Notional tax on profit before taxation, calculated using the PRC statutory tax rate of 25% (2017: 25%)	**70,142**	54,524
Effect of preferential tax rates	**(16,601)**	(20,396)
Effect of different tax rates	**(1,872)**	(1,266)
Tax effect of non-deductible expenses	**1,075**	1,300
Tax effect of non-taxable income	**(3,586)**	(555)
(Refund)/provision of withholding tax on distributed dividends	**(22,222)**	22,222
Tax effect of bonus deduction for research and development expenses	**(13,670)**	(6,338)
Reversal of previously over-recognised deductible temporary differences	**–**	2,112
Under/(over)-provision in respect of prior year	**332**	(8,207)
Actual tax expense	**13,598**	43,396

10 Directors' emoluments

Directors' emoluments disclosed pursuant to section 383(1) of the Hong Kong Companies Ordinance and Part 2 of the Companies (Disclosure of Information about Benefits of Directors) Regulation are as follows:

Year ended 31 December 2018

	Directors' fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Contributions to retirement benefit schemes RMB'000	Bonuses RMB'000	Share-based payments RMB'000 (Note)	Total RMB'000
Executive directors						
Zhu Xiaokun	–	277	15	–	–	292
Wu Suojun	–	162	15	360	268	805
Yan Ronghua	–	159	15	120	168	462
Jiang Guangqing	–	112	15	90	101	318
Independent non-executive directors						
Wang Xuesong	81	–	–	–	50	131
Gao Xiang	36	–	–	–	50	86
Lee Cheuk Yin, Dannis	81	–	–	–	50	131
Total	198	710	60	570	687	2,225

10 Directors' emoluments (continued)

Year ended 31 December 2017

	Directors' fees RMB'000	Salaries, allowances and benefits in kind RMB'000	Contributions to retirement benefit schemes RMB'000	Bonuses RMB'000	Share-based payments RMB'000 (Note)	Total RMB'000
Executive directors						
Zhu Xiaokun	–	169	14	7,500	–	7,683
Wu Suojun	–	175	14	159	–	348
Yan Ronghua	–	149	14	101	–	264
Jiang Guangqing	–	109	14	97	–	220
Independent non-executive directors						
Wang Xuesong	80	–	–	–	–	80
Gao Xiang	36	–	–	–	–	36
Lee Cheuk Yin, Dannis	80	–	–	–	–	80
Total	196	602	56	7,857	–	8,711

Note:

These represent the estimated value of share options granted to the directors under the Company's share option scheme. The value of these share options is measured according to the Group's accounting policies for share-based payment transactions as set out in Note 3(n)(ii).

The details of these benefits in kind, including the principal terms and number of options granted, are disclosed under the paragraph "Share option scheme" in the directors' report and Note 29.

11 Individuals with highest emoluments

Of the five individuals with the highest emoluments, one (2017: two) is a director whose emoluments are disclosed in Note 10. The aggregate of the emoluments in respect of the other four (2017: three) individuals are as follows:

	2018 **RMB'000**	2017 RMB'000
Salaries, allowances and benefits in kind	**1,854**	1,387
Share-based payments	**604**	–
Bonuses	**502**	121
Contributions to retirement benefit schemes	**45**	42
	3,005	1,550

	2018 **Number of** **individuals**	2017 Number of individuals
HKD nil to HKD1,000,000	**3**	2
HKD1,000,001 to HKD2,000,000	**1**	1

(Expressed in Renminbi ("RMB") unless otherwise indicated)

12 Earnings per share

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB258,835,000 (2017: RMB169,099,000) and the weighted average of 2,431,907,143 ordinary shares (2017: 2,220,546,288 ordinary shares) in issue during the year:

Weighted average number of ordinary shares

	2018	2017
Issued ordinary shares at 1 January	**2,239,050,000**	2,220,080,000
Effect of shares allotment	**192,857,143**	–
Effect of exercise of share options	**–**	466,288
Weighted average number of ordinary shares at 31 December	**2,431,907,143**	2,220,546,288

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB258,835,000 (2017: RMB169,099,000) and the weighted average number of ordinary shares of 2,435,421,765 shares (2017: 2,226,347,577 shares), calculated as follows:

Weighted average number of ordinary shares (diluted)

	2018	2017
Weighted average number of ordinary shares at 31 December	**2,431,907,143**	2,220,546,288
Effect of equity settled share-based transactions (Note 29)	**3,514,622**	5,801,289
Weighted average number of ordinary shares (diluted) at 31 December	**2,435,421,765**	2,226,347,577

The calculation of diluted earnings per share for the year ended 31 December 2018 did not include the potential effects of 22,147,000 (2017: 22,147,000) share options during the year as they have anti-dilutive effects on the basic earnings per share for the year.

13 Property, plant and equipment

	Plant and buildings RMB'000	Machinery RMB'000	Motor vehicles RMB'000	Office equipment and others RMB'000	Construction in progress RMB'000	Total RMB'000
Cost:						
Balance at 1 January 2017	966,308	3,000,272	11,187	40,609	541,968	4,560,344
Additions	1,098	53,394	4,096	7,581	232,787	298,956
Transfers from construction in process	2,150	206,584	–	–	(208,734)	–
Disposals	–	(769)	(4,523)	(2)	–	(5,294)
Balance at 31 December 2017	969,556	3,259,481	10,760	48,188	566,021	4,854,006
Additions	74,192	87,891	–	4,068	141,084	307,235
Transfers from construction in process	189,147	49,295	–	–	(238,442)	–
Disposals	(245)	(26,239)	(923)	(148)	–	(27,555)
Balance at 31 December 2018	1,232,650	3,370,428	9,837	52,108	468,663	5,133,686
Accumulated depreciation:						
Balance at 1 January 2017	(245,289)	(829,782)	(4,899)	(36,210)	–	(1,116,180)
Charge for the year	(39,743)	(176,372)	(1,179)	(2,873)	–	(220,167)
Written back on disposals	–	322	2,361	2	–	2,685
Balance at 31 December 2017	(285,032)	(1,005,832)	(3,717)	(39,081)	–	(1,333,662)
Charge for the year	(40,476)	(180,727)	(1,217)	(3,253)	–	(225,673)
Written back on disposals	136	21,628	825	129	–	22,718
Balance at 31 December 2018	(325,372)	(1,164,931)	(4,109)	(42,205)	–	(1,536,617)
Net book value:						
At 31 December 2018	907,278	2,205,497	5,728	9,903	468,663	3,597,069
At 31 December 2017	684,524	2,253,649	7,043	9,107	566,021	3,520,344

13 Property, plant and equipment (continued)

All plant and buildings are located in the PRC.

Pursuant to the renewed lease agreements entered into between the Group and Jiangsu Tiangong Group Company Limited ("TG Group") on 1 January 2017, the Group is required to pay RMB600,000 per annum for the lease of office premises from TG Group effective from 1 January 2017 to 31 December 2019, and to pay RMB400,000 per annum for the lease of amenity facilities from TG Group effective from 1 January 2017 to 31 December 2019 (see Note 34(b)).

14 Lease prepayments

	RMB'000
Cost:	
At 1 January 2017 and 31 December 2017	89,647
Charge for the year	24,607
At 31 December 2018	114,254
Accumulated amortisation:	
At 1 January 2017	(17,023)
Charge for the year	(1,749)
At 31 December 2017	(18,772)
Charge for the year	(1,854)
At 31 December 2018	(20,626)
Net book value:	
At 31 December 2018	93,628
At 31 December 2017	70,875

The amortisation charge for the year is included in "administrative expenses" in the consolidated statement of profit or loss.

15 Goodwill

	2018 RMB'000	2017 RMB'000
Cost:		
Balance at 1 January and 31 December	**21,959**	21,959
Accumulated impairment losses:		
Balance at 31 December	**–**	–
Carrying amount:		
At 31 December	**21,959**	21,959

For the purpose of impairment testing, goodwill is allocated to the Group's operating divisions which represent the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Goodwill is allocated to the Group's CGUs identified according to the reportable segments as follows:

	2018 RMB'000	2017 RMB'000
DS	**21,959**	21,959

The recoverable amounts of the CGU was determined based on value-in-use calculations. The key assumptions for the value-in-use calculations are those regarding the discount rate, growth rate of revenue and gross margin. The Group prepared cash flow forecasts derived from the two-year financial budgets and extrapolated cash flows for the following thirteen years based on an estimated growth rate of revenue of 5% – 10% (2017: 5% – 15%), a pre-tax discount rate of 10.1% (2017: 11.6%) and a gross margin of 15% – 20% (2017: 15% – 20%). The growth rate used does not exceed the long-term average growth rate for the business in which the CGU operates.

Management determined the budgeted gross margin and growth rate of revenue based on past performance and its expectation for market development. The discount rate used is pre-tax and reflects specific risks relating to the relevant segments.

The recoverable amounts of the CGUs are higher than their carrying amounts based on value-in-use calculations. Accordingly, no impairment of goodwill is recognised in the consolidated statement of profit or loss.

(Expressed in Renminbi ("RMB") unless otherwise indicated)

16 Interests in subsidiaries

The following list contains only the subsidiaries which principally affected the results, assets or liabilities of the Group. The class of shares held is ordinary shares unless otherwise stated.

Name of company	Note	Place and date of incorporation	Proportion of ownership interest		Issued and fully paid-up/ registered capital	Principal activity
			Direct	Indirect		
China Tiangong Company Limited		British Virgin Islands, 14 August 2006	100%	–	USD-/USD50,000	Investment holding
TG Tools	(i)	The PRC, 7 July 1997	–	100%	RMB2,148,128,000/ RMB2,148,128,000	Manufacture and sale of high speed steel and cutting tools
TG Aihe	(ii)	The PRC, 5 December 2003	–	100%	RMB723,038,000/ RMB723,038,000	Manufacture and sale of die steel
Danyang Tianfa Forging Company Limited ("Tianfa Forging")	(ii)	The PRC, 11 October 2000	–	100%	USD18,600,000/ USD18,600,000	Precision forging and sale of high speed steel
China Tiangong (Hong Kong) Company Limited ("CTCL (HK)")		Hong Kong, 13 June 2008	–	100%	HKD1/HKD1	Investment holding
TG Tech	(iii)	The PRC, 27 January 2010	–	74.03%	RMB405,000,000/ RMB405,000,000	Manufacture and sale of titanium-related products
TG Development		Hong Kong, 15 February 2012	–	100%	USD5,500,000/ USD5,500,000	Trading of alloy steel and cutting tools
Jiangsu Tiangong Mould Steel R&D Center Company Limited ("TG R&D")	(iii)	The PRC, 5 March 2012	–	100%	RMB5,000,000/ RMB5,000,000	Research and development of alloy and steel products
Jiangsu Tiangong International Trading Company Limited ("International Trading")	(iii)	The PRC, 6 March 2014	–	100%	RMB20,000,000/ RMB50,000,000	Trading of goods
Jurong Tiangong New Materials Technology Company Limited ("TG New Materials")	(iii)	The PRC, 29 July 2015	–	100%	RMB300,000,000/ RMB300,000,000	Research and development, manufacture and sale of high speed steel, and die steel related products
Jiangsu Tiangong Precision Tools Company Limited ("Precision Tools")	(iv)	The PRC, 25 January 2016	–	100%	HKD-/ HKD10,000,000	Research and development, manufactory and sale of cutting tools related products
Danyang Taifeng Precision Machinery Tools Company Limited ("Taifeng Precision")	(iii)	The PRC, 5 February 2016	–	100%	RMB-/ RMB8,000,000	Research and development, manufacture, distribution and sale of cutting tools related products
Jiangsu Tiangong Investment Management Company Limited ("TG Investment")	(v)	The PRC, 9 March 2017	–	100%	HKD15,000,000/ HKD35,000,000	Investment management and advisory related services

16 Interests in subsidiaries (continued)

Note:

(i) TG Tools is a wholly foreign-owned enterprise incorporated in the PRC.

(ii) TG Aihe and Tianfa Forging are incorporated in the PRC as sino-foreign equity joint ventures.

(iii) TG Tech, TG R&D, International Trading, TG New Material and Taifeng Precision are incorporated in the PRC as domestic companies.

(iv) Precision Tools (formerly known as Danyang Tianjia Tools Technology Company Limited) is a wholly foreign-owned enterprise incorporated in the PRC.

(v) On 9 March 2017, CTCL (HK) established a wholly owned subsidiary, TG Investment, which is engaged in investment management and advisory related services. As at 31 December 2018, CTCL (HK) had injected capital totaling HKD15,000,000.

The following table lists out information relating to TG Tech, the only subsidiary of the Group which has a material non-controlling interest ("NCI"). The summarised financial information presented below represents the amounts before any inter-company elimination.

	2018 **RMB'000**	2017 RMB'000
NCI percentage	**25.97%**	25.97%
Current assets	**468,461**	419,419
Non-current assets	**174,979**	185,679
Current liabilities	**(36,464)**	(29,446)
Non-current liabilities	**(23,777)**	(23,777)
Net assets	**583,199**	551,875
Carrying amount of NCI	**151,457**	143,321
Revenue	**272,893**	188,867
Profit for the year	**31,324**	21,573
Total comprehensive income	**31,324**	21,573
Profit allocated to NCI	**8,135**	5,602
Dividend paid to NCI	**–**	–
Cash flows from operating activities	**31,774**	(39,494)
Cash flows from investing activities	**(7,144)**	(2,852)
Cash flows from financing activities	**–**	–

(Expressed in Renminbi ("RMB") unless otherwise indicated)

17 Interest in associates

The following list contains the particulars of associates, all of which are unlisted corporate entities whose market price is not available:

					Proportion of ownership interest			
Name of associate	Note	Form of business structure	Place of incorporation and business	Issued and fully paid-up/ registered capital	Group's effective interest	Held by the Company	Held by a subsidiary	Principal activity
Jiangsu Tianrun Huafa Logistics Company Limited ("Tianrun Huafa")	(i)	Incorporated	The PRC	RMB5,000,000/ RMB5,000,000	40%	–	40%	Logistics and freight
Xinzhenggong Company Limited ("XZG")	(ii)	Incorporated	Taiwan	TWD200,000,000/ TWD200,000,000	25%	–	25%	Sale of special steel related products
SB Specialty Metals Holdings LLC ("SBSMH")	(iii)	Incorporated	United States of America	USD8,625,000/ USD8,625,000	19.8%	19.8%	–	Sale of special steel related products
Fusion TG Canada Inc ("TGC")	(iv)	Incorporated	Canada	CAD6,000,000/ CAD6,000,000	10%	10%	–	Sale of special steel related products
Jiangsu Ningxing Tiangong Mould technology Company Limited ("JS NXTG")	(v)	Incorporated	The PRC	RMB10,000,000/ RMB10,000,000	30%	–	30%	Sale of special steel related products
Shenzhen 51 Mocai Technology Company Limited ("51 Mocai")	(vi)	Incorporated	The PRC	RMB50,000,000/ RMB50,000,000	10%	–	10%	Sale of special steel related products
Aceros T&C Company Limited ("ATC")	(vii)	Incorporated	Mexico	–/ CUP100,000	15%	–	15%	Sale of special steel related products

Note:

(i) Tianrun Huafa is a transportation agency of the Group in the PRC.

(ii) XZG is the sole distributor of the Group's products in Taiwan.

(iii) SBSMH, a distributor of special steel products in the USA, enables the Group to have exposure to this market through local experience.

(iv) TGC is the sole distributor of the Group's products in Canada.

(v) JS NXTG, a distributor of special steel products in the PRC, enables the Group to increase its exposure to the East of China. During 2017, TG Aihe injected capital totaling RMB1,500,000 and fully paid up the registered capital.

(vi) 51 Mocai, a distributor of special steel products in the PRC, enables the Group to increase its exposure to the South of China. During 2017, TG Aihe injected capital totaling RMB5,000,000 and fully paid up the registered capital. The Group has a right to appoint one director to the Board of 51 Mocai in accordance with the investment agreement, therefore the Directors consider that 51 Mocai is an associate of the Group.

(vii) As at 22 November 2016, TG Tools formed an associate, ATC, with Citma Metals Co. Ltd, in Mexico. The associate is principally engaged in sale of special steel related products. As at 31 December 2017, TG Tools had not contributed any capital into ATC. All inventories of ATC are supplied by the Group. The Directors consider that the Group can exercise significant influence over ATC and therefore ATC is accounted for as an associate of the Group.

All of the above associates are accounted for using the equity method in the consolidated financial statements.

17 Interest in associates (continued)

Aggregate information of associates that are not individually material:

	At 31 December 2018 RMB'000	At 1 January 2018 RMB'000	At 31 December 2017 RMB'000
Aggregate carrying amount of individually immaterial associates in the consolidated financial statements	**51,905**	48,963	49,372

	2018 RMB'000	2017 RMB'000
Aggregate amounts of the Group's share of those associates'		
– Profit/(loss) from continuing operations	**2,349**	(4,805)
– Other comprehensive income	**1,081**	1,193
Total comprehensive income	**3,430**	(3,612)

(Expressed in Renminbi ("RMB") unless otherwise indicated)

18 Interest in joint ventures

Details of the Group's interest in joint ventures as at 31 December 2018, which are accounted for using the equity method in the consolidated financial statements, are set out below:

Name of joint venture	Note	Form of business structure	Place of incorporation and business	Particulars of issued and paid up capital and securities	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by a subsidiary	Principal activity
TGT Special Steel Company Limited ("TGT")	(i)(vi)	Incorporated	The Republic of Korea	1,000,000 shares of USD1 each	70%	–	70%	Sale of special steel related products
TGK Special Steel PVT Limited ("TGK")	(ii)	Incorporated	India	2,000,000 shares of USD1 each	50%	–	50%	Sale of special steel related products
Czechtools and Materials S.R.O. ("CTM")	(iii)	Incorporated	Czech Republic	26,140,000 shares of CZK1 each	50%	–	50%	Sale of special steel related products
Five Star Special Steel Europe S.R.L ("FSS")	(iv)(vi)	Incorporated	Italy	100,000 shares of EUR1 each	60%	–	60%	Sale of special steel related products
TG Middle East Celik San Ltd. ("TGME")	(v)	Incorporated	Turkey	1,000,000 shares of EUR1 each	50%	–	50%	Sale of special steel related products

Note:

(i) TGT is the sole distributor of the Group's special steel products in Korea.

(ii) TGK is the sole distributor of the Group's special steel products in India.

(iii) CTM is the sole distributor of the Group's special steel products in the Czech Republic.

(iv) FSS is the sole distributor of the Group's special steel products in Italy.

(v) TGME is the sole distributor of the Group's special steel products in Turkey.

(vi) According to TGT's and FSS's joint venture agreements, no single shareholder is in a position to control the shareholders' meeting nor no single director appointed by either shareholder is in a position to control the Board of Directors. Therefore, although the Group holds more than 50% of equity interests in TGT and FSS, management of the Group consider that the Group does not have the ability to use its power over TGT and FSS to affect its returns through its involvement and deem them to be joint ventures of the Group rather than subsidiaries.

18 Interest in joint ventures (continued)

Aggregate information of joint ventures that are not individually material:

	At 31 December 2018 RMB'000	At 1 January 2018 RMB'000	At 31 December 2017 RMB'000
Aggregate carrying amount of individually immaterial joint ventures in the consolidated financial statements	**33,813**	24,180	26,263

	2018 RMB'000	2017 RMB'000
Aggregate amount of the Group's share of those joint ventures'		
– Profit from continuing operations	**10,893**	602
– Other comprehensive income	**(1,260)**	318
Total comprehensive income	**9,633**	920

19 Other financial assets

	Note	**At 31 December 2018 RMB'000**	At 1 January 2018 RMB'000	At 31 December 2017 RMB'000
Equity securities designated at FVOCI (non-recycling)	(iii)			
– Listed in the PRC	(i)	**80,959**	73,500	–
– Unlisted equity securities	(ii)	**19,065**	15,400	–
Available-for-sale financial assets	(iii)			
– Listed in the PRC		**–**	–	73,500
– Unlisted equity securities		**–**	–	15,400
		100,024	88,900	88,900

19 Other financial assets (continued)

Note:

(i) The listed equity securities are shares in Bank of Jiangsu Co., Ltd., a company listed on the Mainboard of the Shanghai Stock Exchange and shares in JM Digital Steel Inc., a company listed on the National Equities Exchange and Quotations System. The Group designated these investments at FVOCI (non-recycling), as the investments are held for strategic purposes. Dividends of RMB1,800,000 were received from these investments during the year ended 31 December 2018 (2017: RMB1,780,000).

(ii) The unlisted equity securities are shares in Xiamen Chuangfeng Yizhi Investment Management Partnership, a company incorporated in the PRC and shares in Nanjing Xiaomuma Technology Co., Ltd., a company incorporated in the PRC. The Group designated these investments at FVOCI (non-recycling), as the investments are held for strategic purposes. No dividends were received from these investments during the year ended 31 December 2018 (2017: nil).

(iii) Available-for-sale financial assets were reclassified to equity securities designated at FVOCI (non-recycling) upon the initial application of IFRS 9 at 1 January 2018 (see Note 4(b)(i)).

20 Trading securities

	2018 **RMB'000**	2017 RMB'000
Listed equity securities at FVPL (Note 32(f)(i))		
– in Hong Kong	**1,482**	–

21 Inventories

(a) Inventories in the consolidated statement of financial position comprise:

	2018 **RMB'000**	2017 RMB'000
Raw materials	**76,244**	61,493
Work in progress	**863,034**	768,618
Finished goods	**1,055,009**	1,066,753
	1,994,287	1,896,864

(b) The analysis of the amount of inventories recognised as an expense and included in profit or loss is as follows:

	2018 **RMB'000**	2017 RMB'000
Carrying amount of inventories sold	**4,359,617**	3,416,784
Provision/(reversal) of write-down of inventories	**1,002**	(16,804)
	4,360,619	3,399,980

22 Trade and other receivables

	At 31 December 2018 RMB'000	At 1 January 2018 RMB'000	At 31 December 2017 RMB'000
Trade receivables	**1,193,506**	1,019,779	1,019,779
Bills receivables	**911,473**	726,603	726,603
Less: loss allowance (Note)	**(105,868)**	(73,230)	(38,359)
Net trade and bills receivables	**1,999,111**	1,673,152	1,708,023
Prepayments	**250,879**	231,444	231,444
Non-trade receivables	**101,851**	104,704	104,704
Less: loss allowance	**–**	–	–
Net prepayments and non-trade receivables	**352,730**	336,148	336,148
	2,351,841	2,009,300	2,044,171

Note: Upon the adoption of IFRS 9, an opening adjustment as at 1 January 2018 was made to recognise additional ECLs on trade receivables (see Note 4(b)).

Substantially all of the trade and other receivables are expected to be recovered or recognised as an expense within one year.

Trade receivables of RMB151,780,000 (2017: RMB123,200,000) have been pledged to a bank as security for the Group's bank loans as disclosed in Note 26.

The Group's exposure to credit risks and foreign currency risks related to trade and other receivables are disclosed in Note 32.

22 Trade and other receivables (continued)

Ageing analysis

As of the end of the reporting period, the ageing analysis of trade and bills receivables (which are included in trade and other receivables), based on the invoice date and net of loss allowance, is as follows:

	2018 RMB'000	2017 RMB'000
Within 3 months	**1,592,295**	1,521,338
4 to 6 months	**177,310**	117,972
7 to 12 months	**52,609**	44,940
1 to 2 years	**152,084**	13,457
Over 2 years	**24,813**	10,316
	1,999,111	1,708,023

Trade and bills receivables are due from 90 to 180 days from the date of billing. Further details on the Group's credit policy and credit risk arising for trade and bills receivable are set out in Note 32(a).

23 Pledged deposits

As at 31 December 2018, bank deposits of RMB464,500,000 (2017: RMB241,380,000) have been pledged to banks as security for the Group to issue bank acceptance bills and other banking facilities (as described in Note 26). The pledge in respect of the bank deposits will be released upon the settlement of the related bills by the Group and the termination of related banking facilities.

The Group's exposure to credit risks and interest rate risks are disclosed in Note 32.

24 Time deposits

As at 31 December 2018, time deposits of RMB717,414,000 (2017: RMB500,000,000) in the consolidated statement of financial position represent bank deposits that are over 3 months of maturity at acquisition.

The Group's exposure to credit risks and interest rate risks are disclosed in Note 32.

25 Cash and cash equivalents

(a) Cash and cash equivalents comprise:

As at 31 December 2017 and 2018, all of the Group's cash and cash equivalents in the consolidated statement of financial position and the consolidated cash flow statement represented cash at bank and cash on hand.

	2018 RMB'000	2017 RMB'000
Cash at bank and on hand	**583,235**	219,798

25 Cash and cash equivalents (continued)

(b) Reconciliation of profit before taxation to cash generated from operations:

	Note	**2018 RMB'000**	2017 RMB'000 (Note)
Profit before taxation		**280,568**	218,097
Adjustments for:			
Depreciation	8(c)	**225,673**	220,167
Amortisation of lease prepayments	8(c)	**1,854**	1,749
Interest income	8(a)	**(7,233)**	(5,795)
Interest on bank loans	8(a)	**142,071**	118,205
Gains on disposal of property, plant and equipment	6	**(1,639)**	(496)
Dividends received from listed securities	6	**(1,800)**	(1,780)
Disposal gains from trading securities	6	**–**	(545)
Revaluation losses from trading securities	7	**947**	–
Provision of loss allowance on trade and other receivables	8(c)	**35,374**	1,049
Share of (profits)/losses of associates	17	**(2,349)**	4,805
Share of profits of joint ventures	18	**(10,893)**	(602)
Equity-settled share-based payment expenses	8(b)	**10,063**	–
Operating profit before changes in working capital		**672,636**	554,854
Change in inventories		**(97,423)**	4,911
Change in trade and other receivables		**(377,915)**	(469,837)
Change in trade and other payables		**608,591**	160,689
Change in deferred income		**12,501**	(6,440)
Net cash generated from operations		**818,390**	244,177

Note: The Group has initially applied IFRS 15 and IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. See Note 4.

25 Cash and cash equivalents (continued)

(c) Reconciliation of liabilities arising from financing activities:

The table below details changes in the Group's liabilities from financing activities, including both cash and non-cash changes. Liabilities arising from financing activities are liabilities for which cash flows were, or future cash flows will be, classified in the Group's consolidated cash flow statement as cash flows from financing activities.

	Interest-bearing borrowings RMB'000
At 1 January 2017	2,888,912
Proceeds from interest-bearing borrowings	5,042,507
Repayment of interest-bearing borrowings	(4,938,127)
Changes from financing cash flows	104,380
At 31 December 2017 and 1 January 2018	2,993,292
Proceeds from interest-bearing borrowings	4,937,670
Repayment of interest-bearing borrowings	(4,747,183)
Changes from financing cash flows	190,487
At 31 December 2018	3,183,779

26 Interest-bearing borrowings

	Note	2018 RMB'000	2017 RMB'000
Current			
Secured bank loans	(i)	**332,765**	291,990
Unsecured bank loans	(ii)	**1,205,365**	1,506,547
Current portion of non-current secured bank loans		**–**	46,400
Current portion of non-current unsecured bank loans		**746,472**	325,342
		2,284,602	2,170,279
Non-current			
Secured bank loans	(iii)	**–**	46,400
Unsecured bank loans	(iv)	**1,645,649**	1,148,355
Less: Current portion of non-current secured bank loans		**–**	(46,400)
Current portion of non-current unsecured bank loans		**(746,472)**	(325,342)
		899,177	823,013
		3,183,779	2,993,292

Note:

(i) The current secured bank loans were secured by certain trade receivables and sales contracts at annual interest rates ranging from 0.90% to 4.20% (2017: 0.90% to 3.50%) per annum.

(ii) Current unsecured bank loans carried interest at annual rates ranging from 1.55% to 5.22% (2017: 2.00% to 5.22%) per annum, and were all repayable within one year.

(iii) Non-current secured bank loans were pledged against equity securities at interest rate of nil (2017: 5.5%) per annum.

(iv) Non-current unsecured bank loans carried interest at annual rates ranging from 2.65% to 5.13% (2017: 2.34% to 5.13%) per annum.

26 Interest-bearing borrowings (continued)

The current portion and non-current portion of the Group's non-current bank loans were repayable as follows:

	2018 **RMB'000**	2017 RMB'000
Within 1 year	**746,472**	371,742
Over 1 year but less than 2 years	**899,177**	790,342
Over 2 years but less than 3 years	**–**	32,671
	1,645,649	1,194,755

As at 31 December 2017 and 2018, the Group's banking facility with one bank is subject to the fulfilment of a covenant relating to certain of the Group's balance sheet ratios, as are commonly found in lending arrangements with financial institutions. If the Group were to breach the covenants the drawn down facilities would become payable on demand. The Group regularly monitors its compliance with these covenants. Further details of the Group's management of liquidity risk are set out in Note 32(b).

More information about the Group's exposure to interest rate, foreign currency and liquidity risks is disclosed in Note 32.

27 Trade and other payables

	At 31 December 2018 **RMB'000**	At 1 January 2018 RMB'000	At 31 December 2017 RMB'000 (Note)
Trade and bills payables	**1,740,593**	1,138,428	1,138,428
Contract liabilities	**32,434**	36,717	–
Non-trade payables and accrued expenses	**138,424**	127,837	164,554
	1,911,451	1,302,982	1,302,982

Note: As a result of the adoption of IFRS 15, advances received are included and disclosed in contract liabilities (see Note 3(i)).

The Group's exposure to liquidity and foreign currency risks related to trade and other payables is disclosed in Note 32.

27 Trade and other payables (continued)

As of the end of the reporting period, the ageing analysis of trade and bills payables (which are included in trade and other payables), based on the invoice date, is as follows:

	2018 **RMB'000**	2017 RMB'000
Within 3 months	**1,022,521**	474,445
4 to 6 months	**375,682**	334,821
7 to 12 months	**291,150**	286,691
1 to 2 years	**19,427**	14,793
Over 2 years	**31,813**	27,678
	1,740,593	1,138,428

28 Deferred income

Deferred income consists of conditional government grants received for completion of certain construction projects. During 2018, the Group received RMB18,000,000 conditional government grants (2017: RMB nil) to support capital investments of the Group. As at 31 December 2018, the carrying amount of deferred income in respect of government grants after amortisation (Note 6(i)) amounted to RMB55,777,000 (2017: RMB43,276,000) of which RMB50,498,000 (2017: RMB37,777,000) was classified as non-current deferred income.

29 Equity settled share-based transactions

The Group has a share option scheme which was adopted on 7 July 2007 and expired on 6 July 2017 and has adopted a new share option scheme on 26 May 2017, whereby the directors of the Company are authorised, at their discretion, to invite employees of the Group, including directors of any company in the Group, to take up options to subscribe for shares of the Company. Each option gives the holder the right to subscribe for one ordinary share in the Company.

(Expressed in Renminbi ("RMB") unless otherwise indicated)

29 Equity settled share-based transactions (continued)

(a) The terms and conditions of the grants are as follows:

	Number of instruments	Vesting conditions	Contractual life of options
Options granted to directors:			
– on 18 August 2014	1,967,000	Immediately on 19 August 2014	5 years and expires at close of business on 18 August 2019
– on 11 January 2018	2,550,000	On 31 March 2019 and subject to performance conditions (Note)	1.97 years and expires at close of business on 31 December 2019
– on 11 January 2018	2,550,000	On 31 March 2020 and subject to performance conditions (Note)	2.97 years and expires at close of business on 31 December 2020
Options granted to employees:			
– on 18 August 2014	20,180,000	Immediately on 19 August 2014	5 years and expires at close of business on 18 August 2019
– on 11 January 2018	27,450,000	On 31 March 2019 and subject to performance conditions (Note)	1.97 years and expires at close of business on 31 December 2019
– on 11 January 2018	27,450,000	On 31 March 2020 and subject to performance conditions (Note)	2.97 years and expires at close of business on 31 December 2020
Total share options granted	82,147,000		

Note:

The share options granted on 11 January 2018 shall be vested when the following performance conditions are satisfied:

- If the consolidated audited net profit of the Company for the year ended 31 December 2018 represents an increase of 50% or more as compared to that of the year ended 31 December 2017, the vesting date will be 31 March 2019 for the 50% of the total share options granted.
- If the consolidated audited net profit of the Company for the year ended 31 December 2019 represents an increase of 50% or more as compared to that of the year ending 31 December 2018, the vesting date will be 31 March 2020 for the rest of the total share options granted.

(Expressed in Renminbi ("RMB") unless otherwise indicated)

29 Equity settled share-based transactions (continued)

(b) The number and weighted average exercise prices of share options are as follows:

		2018		2017	
	Note	**Weighted average exercise price**	**Number of options**	Weighted average exercise price	Number of options
Outstanding at the beginning of the year		**HKD1.780**	**22,147,000**	HKD1.236	41,117,000
Granted during the year	31(c)(iii)	**HKD1.500**	**60,000,000**	–	–
Exercised during the year	31(c)(iii)	**–**	**–**	HKD0.600	(18,970,000)
Outstanding at the end of the year		**HKD1.575**	**82,147,000**	HKD1.780	22,147,000
Exercisable at the end of the year		**HKD1.780**	**22,147,000**	HKD1.780	22,147,000

The weighted average share price at the date of exercise for share options exercised during the year was not applicable (2017: HKD0.600).

The options outstanding as at 31 December 2018 had an exercise price of HKD1.780 or HKD1.575 (2017: HKD1.780) and average remaining contractual life of 1.25 years (2017: 1.66 years).

(Expressed in Renminbi ("RMB") unless otherwise indicated)

29 Equity settled share-based transactions (continued)

(c) Fair values of share options and assumptions:

The fair values of services received in return for share options granted is measured by reference to the fair value of share options granted. The estimate of the fair value of the share options granted is measured based on a binomial lattice model. The contractual life of the share option is used as an input into this model. Expectations of early exercise are incorporated into the binomial lattice model.

	Share options granted on 18 August 2014	**Share options granted on 11 January 2018 (Lot A)**	**Share options granted on 11 January 2018 (Lot B)**
Fair value at grant date	HKD0.59 per share option	HKD0.23 per share option	HKD0.34 per share option
Grant date share price	HKD1.78 per share	HKD1.29 per share	HKD1.29 per share
Exercise price	HKD1.78 per share	HKD1.50 per share	HKD1.50 per share
Expected volatility	48.17%	44.31%	49.44%
Contractual option life	5 years	1.97 years	2.97 years
Dividend yield	3.04%	1.76%	1.76%
– Risk-free interest rate	1.22%	1.29%	1.51%
Exercise multiple			
– Directors:	2.800	1.788	1.788
– Management:	2.800	–	–
– Employees:	2.200	1.768	1.768

The expected volatility is based on the historical volatility of the Company over the contractual life of the options as at the date of valuation. Expected dividend yield is based on historical dividend yield. Changes in the subjective input assumptions could materially affect the fair value estimate.

Share options were granted under service conditions. The conditions have not been taken into account in the grant-date fair value measurement of the services received. There were no market conditions associated with the share option granted.

30 Income tax in the consolidated statement of financial position

(a) Current taxation in the consolidated statement of financial position represents:

	2018 **RMB'000**	2017 RMB'000
At the beginning of the year	**4,164**	1,560
Provision for PRC taxes for the year	**3,199**	31,775
Provision for Hong Kong Profits Tax for the year	**245**	–
Hong Kong Profits Tax paid	**(63)**	(1,410)
PRC taxes paid	**(7,428)**	(27,761)
At the end of the year	**117**	4,164

(b) Deferred tax assets recognised

The components of the deferred tax assets recognised in the consolidated statement of financial position and the movements during the year are as follows:

Deferred tax arising from:	**Deductible tax losses** RMB'000	**Unrealised profits** RMB'000	**Loss allowance for trade and other receivables** RMB'000	**Write-down of inventories** RMB'000	**Depreciation differences** RMB'000	**Total** RMB'000
At 1 January 2017	14,877	2,901	5,598	4,658	2,112	30,146
(Charged)/credited to profit or loss	(2,838)	1,015	121	(2,339)	(2,112)	(6,153)
Charged to reserves	(39)	–	–	–	–	(39)
At 31 December 2017	12,000	3,916	5,719	2,319	–	23,954
Impact of initial application of IFRS 9 (Note 4(b))	–	–	5,466	–	–	5,466
At 1 January 2018	12,000	3,916	11,185	2,319	–	29,420
(Charged)/credited to profit or loss	(10,699)	1,228	4,489	736	–	(4,246)
Credited to reserves	21	–	–	–	–	21
At 31 December 2018	1,322	5,144	15,674	3,055	–	25,195

30 Income tax in the consolidated statement of financial position (continued)

(b) Deferred tax assets recognised (continued)

In accordance with the accounting policy set out in Note 3(o), the Group has not recognised deferred tax assets in respect of cumulative tax losses of RMB12,112,000 (2017: RMB4,880,000) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdiction and entity. The tax losses incurred by subsidiaries in the PRC expire within 5 years from the year when such losses were incurred under current tax legislation.

(c) Deferred tax liabilities recognised and not recognised

The components of deferred tax liabilities recognised in the consolidated statement of financial position and the movements during the year are as follows:

Deferred tax arising from:	**Undistributed profits of subsidiaries**	**Deductible capitalised borrowing costs**	**Revaluation of equity securities**	**Total**
	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2017	4,704	37,504	12,945	55,153
Charged to profit or loss	–	5,468	–	5,468
Credited to reserves	–	–	(3,420)	(3,420)
At 31 December 2017	4,704	42,972	9,525	57,201
Charged to profit or loss	–	5,908	–	5,908
Credited to reserves	–	–	(841)	(841)
At 31 December 2018	4,704	48,880	8,684	62,268

As at 31 December 2018, deferred tax liabilities of RMB4,704,000 (2017: RMB4,704,000) were recognised in respect of tax that would be payable on the distribution of the retained profits of the Group's PRC subsidiaries in the foreseeable future. Deferred tax liabilities of RMB115,325,000 (2017: RMB116,740,000) have not been recognised, as the Group controls the timing of the reversal of temporary differences associated with undistributed profits of these subsidiaries and it has been determined that it is probable that the undistributed profits earned by the Group's PRC subsidiaries will not be distributed in the foreseeable future.

31 Capital, reserves and dividends

(a) Movements in components of equity

The reconciliation between the opening and closing balances of each component of the Group's consolidated equity is set out in the consolidated statement of changes in equity. Details of the changes in the Company's individual components of equity between the beginning and the end of the year are set out below:

	Note	Share capital RMB'000 Note31(c)(i)	Share premium RMB'000 Note31(d)(i)	Capital redemption reserve RMB'000 Note31(d)(i)	Capital reserve RMB'000 Note31(d)(ii)	Exchange reserve RMB'000 Note31(d)(iv)	Accumulated losses	Total
Balance at 1 January 2017		40,167	1,590,760	492	15,850	–	(317,989)	1,329,280
Changes in equity for 2017:								
Total comprehensive income for the year		–	–	–	–	5,880	(92,695)	(86,815)
Dividends approved in respect of the previous year	31(b)(ii)	–	–	–	–	–	(22,130)	(22,130)
Exercise of share options		310	11,458	–	(2,253)	–	–	9,515
Balance at 31 December 2017 and 1 January 2018		40,477	1,602,218	492	13,597	5,880	(432,814)	1,229,850
Total comprehensive income for the year		–	–	–	–	(31)	62,590	62,559
Dividends approved in respect of the previous year	31(b)(ii)	–	–	–	–	–	(100,183)	(100,183)
Shares allotment	31(c)(ii)	4,765	381,884	–	–	–	–	386,649
Issuance of share options	31(c)(iii)	–	–	–	10,063	–	–	10,063
Balance at 31 December 2018		45,242	1,984,102	492	23,660	5,849	(470,407)	1,588,938

31 Capital, reserves and dividends (continued)

(b) Dividends

(i) Dividends payable to equity shareholders of the Company in respect of the year:

	2018 **RMB'000**	2017 RMB'000
Dividend proposed after the end of the reporting period of RMB0.0357 per ordinary share (2017: RMB0.0378 per ordinary share)	**90,592**	84,550

The final dividend proposed after the end of the reporting period has not been recognised as a liability at the end of the reporting period.

(ii) Dividends payable to equity shareholders of the Company in respect of the previous financial year, approved and paid during the year:

	2018 **RMB'000**	2017 RMB'000
Dividend in respect of the previous financial year, approved and paid during the year of RMB0.0378 per ordinary share (2017: RMB0.0100 per ordinary share)	**100,183**	22,130

In respect of the final dividend for the year ended 31 December 2017, there is a difference of RMB15,633,000 (2016: RMB16,000) between the final dividend disclosed in the 2017 annual financial statements and amounts approved and paid during the year, which is mainly due to share allotments during 2018 and the RMB/HKD exchange rate difference between the fixed middle average exchange rate on the date of the 2017 annual result announcement and the actual exchange rate applied on the date of payment.

31 Capital, reserves and dividends (continued)

(c) Share capital

(i) Issued and fully paid share capital

Authorised:

	2018 and 2017	
	No. of Shares ('000)	**Amount USD '000**
Ordinary shares of USD0.0025 each (2017: USD0.0025)	4,000,000	10,000

Ordinary shares issued and fully paid:

	2018			2017		
	No. of shares ('000)	**Amount USD '000**	**RMB equivalent '000**	No. of shares ('000)	Amount USD '000	RMB equivalent '000
At 1 January	**2,239,050**	**5,597**	**40,477**	2,220,080	5,550	40,167
Shares allotment	**300,000**	**750**	**4,765**	–	–	–
Exercise of share options	**–**	**–**	**–**	18,970	47	310
At 31 December	**2,539,050**	**6,347**	**45,242**	2,239,050	5,597	40,477

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

(ii) Shares allotment

On 11 May 2018, an aggregate of 300,000,000 new ordinary shares of HKD1.60 each were allotted to certain professional, institutional or corporate investors pursuant to a subscription agreement dated 28 April 2018. Total proceeds of HKD480,000,000 (equivalent to RMB388,440,000), net of direct share issuance expense of HKD2,214,000 (equivalent to RMB1,791,000), were raised, of which RMB4,765,000 was credited to share capital and the balance of RMB381,884,000 was credited to the share premium account.

31 Capital, reserves and dividends (continued)

(c) Share capital (continued)

(iii) Shares issued under share option scheme

On 11 January 2018, 60,000,000 share options to subscribe for ordinary shares of USD0.0025 each in the capital of the Company were granted to employees of the Company in two tranches under the Company's employee share option scheme adopted on 26 May 2017 (no share options were granted during the year ended 31 December 2017). Each option gives the holder the right to subscribe for one ordinary share of the Company. These share options will vest on 31 March 2019 and 2020 subject to certain performance conditions (Note 29(a)), and then be exercisable until 31 December 2019 and 2020 respectively. The payable on acceptance per grant is HKD1.00. The exercise price is HKD1.50. Each share option in two tranches was valued at approximately HKD0.23 and HKD0.34 by an external appraiser, respectively.

On 18 August 2014, the Company granted an aggregate of 22,147,000 share options to employees of the Company to subscribe for ordinary shares of USD0.0025 each in the capital of the Company under its share option scheme adopted on 7 July 2007. The holders of the share options shall have the right to subscribe for ordinary shares during the period from 19 August 2014 to 18 August 2019 at an exercise price of HKD1.78 per share, which was equal to the market price of the ordinary shares on the date of grant. The amount payable on acceptance per grant is HKD1.00. Each share option was valued at approximately HKD0.59 by an external appraiser. No options were exercised during the year ended 31 December 2018 (2017: 18,970,000 shares were exercised).

When the options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in capital reserve will be transferred to retained earnings.

(d) Nature and purpose of reserves

(i) Share premium and capital redemption reserve

The share premium represents the difference between the par value of the shares of the Company and the proceeds received from the issuance of shares or the consideration paid for the repurchased shares of the Company. Under the Companies Law of the Cayman Islands, the share premium account is distributable to shareholders of the Company provided that immediately following the date on which the dividend is proposed to be distributed, the Company will be in a position to repay its debts as they fall due in the ordinary course of business.

Capital redemption reserve represents the par value of shares repurchased by the Company pursuant to section 37 of the Cayman Islands Companies Law.

31 Capital, reserves and dividends (continued)

(d) Nature and purpose of reserves (continued)

(ii) Capital reserve

The capital reserve comprises the following:

- Waived payables due to TG Group in connection with the acquisition of land use rights and plant in 2007. These waivers of liabilities by TG Group were regarded as equity transactions and recorded in the capital reserve account;

- The portion of the grant date fair value of unexercised share options granted to employees of the Group that has been recognised in accordance with the accounting policy adopted for share-based payments in Note 3(n)(ii); and

- Consideration received from issuance of warrants in accordance with the terms of warrant placing agreements entered into by the Company and the subscribers net of direct expenses.

(iii) Merger reserve

The merger reserve comprises the excess amount, arising from the Group's reorganisation of Group entities under common control in 2006 and 2007, of its share of the net identifiable assets acquired in these subsidiaries over the consideration paid. The reorganisation transactions were regarded as equity transactions and the excess of the share of the net identifiable assets over the consideration paid was transferred to the merger reserve in the consolidated financial statements.

(iv) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of Hong Kong subsidiaries and overseas equity-accounted investees. The reserve is dealt with in accordance with the accounting policies set out in Notes 3(a), 3(b) and 3(r).

(v) Fair value reserve (recycling)

The fair value reserve (recycling) comprises the cumulative net change in the fair value of debt securities measured at FVOCI under IFRS 9 held at the end of the reporting period (see Note 4(b)). Prior to 1 January 2018, this reserve included the cumulative net change in the fair value of available-for-sale financial assets held at the end of the reporting period in accordance with IAS 39. This amount has been reclassified to fair value reserve (non-recycling) upon the initial adoption of IFRS 9 at 1 January 2018 (see Note 4(b)).

(vi) Fair value reserve (non-recycling)

The fair value reserve (non-recycling) comprises the cumulative net change in the fair value of equity investments designated at FVOCI under IFRS 9 that are held at the end of the reporting period (see Note 4(b)).

31 Capital, reserves and dividends (continued)

(d) Nature and purpose of reserves (continued)

(vii) PRC statutory reserves

Transfers from retained earnings to the following PRC statutory reserves were made in accordance with the relevant PRC rules and regulations and the Articles of Association of the Company's subsidiaries incorporated in the PRC and were approved by the respective boards of directors.

General reserve fund

The subsidiaries in the PRC are required to transfer at least 10% of their profit after taxation, as determined under the PRC accounting regulations, to the general reserve fund until the reserve balance reaches 50% of their respective registered capital. The transfer to this reserve must be made before any distribution of dividends to shareholders.

The general reserve fund can be used to make good losses or be converted into share capital by the issuance of new shares to shareholders in proportion to their existing equity holdings, provided that the balance after such conversion is not less than 25% of these subsidiaries' registered capital.

Enterprise expansion fund

The enterprise expansion fund can be used to convert into share capital and to develop business.

(e) Distributability of reserves

As at 31 December 2018, the aggregate amount of reserves available for distribution to equity shareholders of the Company was RMB1,513,695,000 (2017: RMB1,169,404,000). After the end of the reporting period, the directors proposed a final dividend of RMB0.0357 per ordinary share (2017: RMB0.0378), amounting to RMB90,592,000 (2017: RMB84,550,000). This dividend has not been recognised as a liability at the end of the reporting period.

(f) Capital management

The Group's primary objectives when managing capital are to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, by pricing products and services commensurately with the level of risk and by securing access to finance at a reasonable cost.

The Group actively and regularly reviews and manages its capital structure to maintain a balance between the higher shareholder returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

The Group monitors its capital structure on the basis of an adjusted net debt-to-capital ratio. For this purpose, adjusted net debt is defined as total debt (which includes interest-bearing loans and borrowings) plus unaccrued proposed dividends, less cash and cash equivalents. Adjusted capital comprises all components of equity, less unaccrued proposed dividends.

31 Capital, reserves and dividends (continued)

During 2018, the Group's strategy was to maintain a stable adjusted net debt-to-capital ratio. In order to maintain or adjust the ratio, the Group may adjust the amount of dividends paid to shareholders, issue new shares, return capital to shareholders, raise new debt financing or sell assets to reduce debt.

The Group's adjusted net debt-to-capital ratios at 31 December 2018 and 2017 were as follows:

	Note	**2018** **RMB'000**	2017 RMB'000
Current liabilities:			
Interest-bearing borrowings	26	**2,284,602**	2,170,279
Non-current liabilities:			
Interest-bearing borrowings	26	**899,177**	823,013
Total debt		**3,183,779**	2,993,292
Add: Proposed dividends	31(b)	**90,592**	84,550
Less: Cash and cash equivalents	25	**(583,235)**	(219,798)
Adjusted net debt		**2,691,136**	2,858,044
Total equity		**4,822,960**	4,302,965
Less: Proposed dividends	31(b)	**(90,592)**	(84,550)
Adjusted capital		**4,732,368**	4,218,415
Adjusted net debt-to-capital ratio		**57%**	68%

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

32 Financial risk management and fair values of financial instruments

Exposure to credit, liquidity, interest rate and currency risks arises in the normal course of the Group's business. The Group is also exposed to equity price risk arising from its equity investments in other entities and movements in its own equity share price.

The Group's exposure to these risks and the financial risk management policies and practices used by the Group to manage these risks are described below.

(a) Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the Group. The Group's credit risk is primarily attributable to trade receivables. The Group's exposure to credit risk arising from cash and cash equivalents, time deposits, pledged deposits and bills receivable is limited because the counterparties are reputable financial institutions with high credit standing, for which the Group considers to have low credit risk.

The Group does not provide any guarantees which would expose the Group to credit risk.

Trade receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer rather than the industry or country in which the customers operate and therefore significant concentrations of credit risk primarily arise when the Group has significant exposure to individual customers. At the end of the reporting period, 0% (2017: 0%) and 6% (2017: 7%) of the total trade receivables was due from the Group's largest customer and the five largest customers respectively within DS, HSS and trading of goods segments.

Individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and take into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. Trade receivables are due within 90 – 180 days from the date of billing. Normally, the Group does not obtain collateral from customers.

The Group measures loss allowance for trade receivables at an amount equal to lifetime ECLs, which is calculated using a provision matrix.

32 Financial risk management and fair values of financial instruments (continued)

(a) Credit risk (continued)

Trade receivables (continued)

The following table provides information about the Group's exposure to credit risk and ECLs for trade receivables as at 31 December 2018:

	Expected loss rate %	Gross carrying amount RMB'000	Loss allowance RMB'000
Current (not past due)	1.0%	687,787	6,966
1 – 3 months past due	4.0%	187,471	7,454
4 – 6 months past due	7.4%	52,979	3,942
7 – 12 months past due	10.0%	119,931	12,034
1 – 2 years past due	36.0%	109,083	39,217
More than 2 years past due	100%	36,255	36,255
		1,193,506	105,868

Expected loss rates are based on actual loss experience over the past years. These rates are adjusted to reflect differences between economic conditions during the period over which the historic data has been collected, current conditions and the Group's view of economic conditions over the expected lives of the receivables.

32 Financial risk management and fair values of financial instruments (continued)

(a) Credit risk (continued)

Comparative information under IAS 39

Prior to 1 January 2018, an impairment loss was recognised only when there was objective evidence of impairment (see note 3(g)(i) – policy applicable prior to 1 January 2018). At 31 December 2017, trade receivables of RMB38,359,000 were determined to be impaired. The ageing analysis of trade debtors that were not considered to be impaired was as follows:

	2017 RMB'000
Neither past due nor impaired	1,521,338
Less than 3 months past due	67,915
3 to 6 months past due	13,814
Over 6 months past due	19,291
	101,020
	1,622,358

Receivables that were neither past due nor impaired related to a wide range of customers for whom there was no recent history of default.

32 Financial risk management and fair values of financial instruments (continued)

(a) Credit risk (continued)

Comparative information under IAS 39 (continued)

Receivables that were past due but not impaired related to a number of independent customers that had a good track record with the Group. Based on past experience, management believed that no impairment allowance was necessary in respect of these balances as there had been no significant change in credit quality and the balances were still considered fully recoverable.

Movement in the loss allowance account in respect of trade receivables during the year is as follows:

	2018 **RMB'000**	2017 RMB'000
Balance at 31 December 2017 under IAS 39	**38,359**	37,310
Impact on initial application of IFRS 9 (Note 4(b))	**34,871**	–
Balance at 1 January	**73,230**	37,310
Amounts written-off during the year	**(2,736)**	–
Loss allowance recognised during the year	**35,374**	1,049
Balance at 31 December	**105,868**	38,359

The following significant changes in the gross carrying amounts of trade receivables contributed to the increase in the loss allowance during 2018:

– origination of new trade receivables net of those settled resulted in an decrease in loss allowance of RMB9,366,000;

– increase in days past due resulted in an increase in loss allowance of RMB44,740,000; and

– a write-off of trade receivables with a gross carrying amount of RMB2,736,000 resulted in a decrease in loss allowance of RMB2,736,000.

32 Financial risk management and fair values of financial instruments (continued)

(b) Liquidity risk

Individual operating entities within the Group are responsible for their own cash management, including the short term investment of cash surpluses and the raising of loans to cover expected cash demands, subject to approval by the parent company's board when the borrowings exceed certain predetermined levels of authority. The Group's policy is to regularly monitor its liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and readily realisable marketable securities and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

The following tables show the remaining contractual maturities at the end of the reporting period of the Group's financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the end of the reporting period) and the earliest date the Group can be required to pay:

		2018 Contractual undiscounted cash outflow				
	Note	**Within 1 year or on demand RMB'000**	**More than 1 year but less than 2 years RMB'000**	**More than 2 years but less than 3 years RMB'000**	**Total RMB'000**	**Carrying amount at 31 December RMB'000**
Interest-bearing borrowings	26	**2,360,256**	**919,552**	**–**	**3,279,808**	**3,183,779**
Trade and other payables	27	**1,911,451**	**–**	**–**	**1,911,451**	**1,911,451**
		4,271,707	**919,552**	**–**	**5,191,259**	**5,095,230**

		2017 Contractual undiscounted cash outflow				
	Note	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 3 years RMB'000	Total RMB'000	Carrying amount at 31 December RMB'000
Interest-bearing borrowings	26	2,233,448	803,815	33,054	3,070,317	2,993,292
Trade and other payables	27	1,302,982	–	–	1,302,982	1,302,982
		3,536,430	803,815	33,054	4,373,299	4,296,274

32 Financial risk management and fair values of financial instruments (continued)

(c) Foreign currency risk

The Group is exposed to currency risk primarily through sales, purchases and borrowings which give rise to receivables, payables, borrowings and cash balances that are denominated in a foreign currency, i.e. a currency other than the functional currency of the entity to which the transactions relate. The currencies giving rise to this risk are primarily United States dollars (USD), Euros (EUR) and Hong Kong dollars (HKD).

RMB is not freely convertible into foreign currencies. All foreign exchange transactions involving RMB must take place through the People's Bank of China or other institutions authorised to buy and sell foreign exchange. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the People's Bank of China.

(i) Exposure to currency risk

The following table details the Group's exposure at the end of the reporting period to currency risk arising from recognised assets or liabilities denominated in a currency other than the functional currency of the entity to which they relate. For presentation purposes, the amounts of the exposures are shown in RMB, translated using the spot rate at the year end date. Differences resulting from the translation of the financial statements of foreign equity-accounted investees into the Group's presentation currency are excluded.

	2018 Exposure to foreign currencies (expressed in RMB)			2017 Exposure to foreign currencies (expressed in RMB)		
	USD RMB'000	**EUR RMB'000**	**HKD RMB'000**	USD RMB'000	EUR RMB'000	HKD RMB'000
Trade and other receivables	**339,531**	**414,522**	**–**	71,352	369,701	–
Cash and cash equivalents	**50,221**	**65,312**	**6,886**	10,597	9,576	12,086
Pledged deposits	**–**	**617**	**–**	–	–	–
Trade and other payables	**(115,318)**	**–**	**–**	(6,238)	(866)	–
Interest-bearing borrowings	**(389,184)**	**(523,511)**	**(159,083)**	(389,301)	(458,691)	–
Net exposure arising from recognised assets and liabilities	**(114,750)**	**(43,060)**	**(152,197)**	(313,590)	(80,280)	12,086

32 Financial risk management and fair values of financial instruments (continued)

(c) Foreign currency risk (continued)

(ii) Sensitivity analysis

The following table indicates the instantaneous change in the Group's profit after tax (and retained profits) that would arise if foreign exchange rates to which the Group has significant exposure at the end of the reporting period had increased at that date, assuming all other risk variables remained constant.

	2018		2017	
	Increase in foreign exchange rates	**Increase/ (decrease) in profit after tax and retained profits RMB'000**	Increase in foreign exchange rates	Increase/ (decrease) in profit after tax and retained profits RMB'000
USD	**5%**	**(5,772)**	5%	(14,639)
EUR	**5%**	**(3,693)**	5%	(3,487)
HKD	**5%**	**(6,661)**	5%	600

Decrease in foreign exchange rates would have had the equal but opposite effect to the amounts shown above, on the basis that all other variables remained constant.

Results of the analysis as presented in the above table represent an aggregation of the instantaneous effects on each of the Group entities' profit after tax and equity measured in the respective functional currencies, translated into RMB at the exchange rate ruling at the end of the reporting period for presentation purposes.

The sensitivity analysis assumes that the change in foreign exchange rates had been applied to re-measure those financial instruments held by the Group which expose the Group to foreign currency risk at the end of the reporting period. The analysis excludes differences that would result from the translation of the financial statements of foreign equity-accounted investees into the Group's presentation currency. The analysis is performed on the same basis as for 2017.

32 Financial risk management and fair values of financial instruments (continued)

(d) Interest rate risk

The Group's interest rate risk arises primarily from interest-bearing borrowings, pledged deposits and time deposits.

Pledged bank deposits are not held for speculative purposes but are placed to satisfy conditions for the Group to issue bank acceptance bills and other banking facilities.

Interest-bearing borrowings issued at variable rates and at fixed rates expose the Group to cash flow interest rate risk and fair value interest rate risk respectively. The interest rates and terms of repayment of the interest-bearing borrowings of the Group are disclosed in Note 26.

(i) Interest rate profile

The following table details the interest rate profile of the Group's interest-bearing financial instruments at the end of the reporting period:

	2018		2017	
	Effective interest rate %	**RMB'000**	Effective interest rate %	RMB'000
Fixed rate instruments				
Interest-bearing borrowings	**0.90% – 5.22%**	**(590,185)**	0.90% – 5.22%	(987,005)
Pledged deposits	**1.15% – 1.75%**	**464,500**	1.15% – 1.75%	241,380
Time deposits	**1.10% – 1.50%**	**717,414**	1.10% – 1.50%	500,000
		591,729		(245,625)
Variable rate instruments				
Interest-bearing borrowings	**2.00% – 5.13%**	**(2,593,594)**	2.00% – 5.50%	(2,006,287)

32 Financial risk management and fair values of financial instruments (continued)

(d) Interest rate risk (continued)

(ii) Sensitivity analysis

As at 31 December 2018, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would have decreased/increased the Group's profit after tax and retained profits by approximately RMB22,188,000 (2017: RMB20,139,000).

The sensitivity analysis above indicates the instantaneous change in the Group's profit after tax (and retained profits) that would arise assuming that the change in interest rates had occurred at the end of the reporting period and had been applied to floating rate non-derivative instruments held by the Group, which expose the Group to cash flow interest rate risk at the end of the reporting period. The impact on the Group's profit after tax (and retained profits) is estimated as an annualised impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis as for 2017.

(e) Equity price risk

The Group is mainly exposed to equity price changes arising from equity investments held for non-trading purposes (see Note 19).

The Group's equity investment listed on the Stock Exchange of Shanghai (the "SESH") and the National Equities Exchange and Quotations System (the "NEEQ") that are not held for trading purposes have been chosen based on their longer term growth potential and are monitored regularly for performance against expectations. The portfolio is diversified in terms of industry distribution, in accordance with the limits set by the Group.

Except for the trading securities, all of the Group's equity investments are held for long term strategic purposes. Their performance is assessed at least bi-annually against performance of similar listed entities, based on the limited information available to the Group, together with an assessment of their relevance to the Group's long term strategic plans.

32 Financial risk management and fair values of financial instruments (continued)

(e) Equity price risk (continued)

At 31 December 2018, it is estimated that an increase/(decrease) of 10% (2017: 10%) in the relevant equity price as applicable, with all other variables held constant, would have increased/(decreased) fair value reserve (non-recycling) of consolidated equity as follows:

	2018		2017	
		Effect on equity RMB'000		Effect on equity RMB'000
Changes in the relevant equity price risk variable:				
Increase	**10%**	**8,099**	10%	7,403
Decrease	**(10%)**	**(8,099)**	(10%)	(7,403)

The sensitivity analysis indicates the instantaneous change in the Group's fair value reserve (non-recycling) of consolidated equity that would arise assuming that the changes in the stock market index or other relevant risk variables had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Group which expose the Group to equity price risk at the end of the reporting period. It is also assumed that the Group's equity investments would change in accordance with the historical correlation with the relevant stock market index or the relevant risk variables, and that all other variables remain constant. The analysis is performed on the same basis for 2017.

(f) Fair value measurement

(i) Financial assets measured at fair value

The following presents the fair value of the Group's financial instruments measured at the end of the reporting period on a recurring basis, categorised into the three-level fair value hierarchy as defined in IFRS 13, Fair value measurement. The level into which a fair value measurement is classified is determined with reference to the observability and significance of the inputs used in the valuation technique as follows:

- Level 1 valuations: Fair value measured using only Level 1 inputs i.e. unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date.

- Level 2 valuations: Fair value measured using Level 2 inputs i.e. observable inputs which fail to meet Level 1, and not using significant unobservable inputs. Unobservable inputs are inputs for which market data is not available.

- Level 3 valuations: Fair value measured using significant unobservable inputs.

32 Financial risk management and fair values of financial instruments (continued)

(f) Fair value measurement (continued)

(i) Financial assets measured at fair value (continued)

Analysis on fair value measurement of derivative financial instruments as at 31 December 2017 and 2018 are as follows:

	Fair value at 31 December 2018	**Fair value measurement at 31 December 2018 categorised into**		
	RMB'000	**Level 1**	**Level 2**	**Level 3**
Recurring fair value measurement				
Other financial assets:				
– Listed equity securities – SESH	**59,700**	**59,700**	**–**	**–**
– Listed equity securities – NEEQ	**21,259**	**–**	**–**	**21,259**
– Unlisted equity securities	**19,065**	**–**	**–**	**19,065**
Trading securities:				
– Listed equity securities	**1,482**	**1,482**	**–**	**–**

	Fair value at 31 December 2017	Fair value measurement at 31 December 2017 categorised into		
	RMB'000	Level 1	Level 2	Level 3
Recurring fair value measurement				
Other financial assets:				
– Listed equity securities -SESH	73,500	73,500	–	–

32 Financial risk management and fair values of financial instruments (continued)

(f) Fair value measurement (continued)

(i) Financial assets measured at fair value (continued)

Fair value of the equity securities listed on the NEEQ, which do not have quoted price in active markets, and that of unlisted equity securities mentioned in Note 19 is determined using the price/earning or price/book value ratios of comparable listed companies adjusted for lack of marketability discount. The fair value measurement is negatively correlated to the discount for lack of marketability.

The movements during the period in the balance of these Level 3 fair value measurements are as follows:

	2018 RMB'000
Unquoted equity securities:	
At 1 January	15,400
Payment for purchases	20,010
Net unrealised gains recognised in other comprehensive income during the year	4,914
At 31 December	40,324

From 1 January 2018, any gains or losses arising from the remeasurement of the Group's listed equity securities held for strategic purposes are recognised in the fair value reserve (non-recycling) in other comprehensive income. Upon disposal of the equity securities, the amount accumulated in other comprehensive income is transferred directly to retained earnings. Prior to 1 January 2018, any gains arising from the disposal of the listed equity securities were presented in the "Other income" line item in the consolidated statement of profit or loss.

(ii) Financial assets and liabilities carried at other than fair value

Except for equity securities mentioned in Note 19 and trading securities mentioned in Note 20, all financial instruments measured at other than fair value are carried at cost or amortised cost that were not materially different from their fair values as at 31 December 2018 and 31 December 2017.

33 Commitments

(a) Capital commitments outstanding as at 31 December 2018 not provided for in the consolidated financial statements were as follows:

	2018 RMB'000	2017 RMB'000
Contracted for	**90,265**	25,362
Authorised but not contracted for	**368,332**	410,000
	458,597	435,362

(b) As at 31 December 2018, the total future minimum lease payments under non-cancellable operating leases were payable as follows:

	2018 RMB'000	2017 RMB'000
Within 1 year	**1,516**	1,021
After 1 year but within 5 years	**1,301**	1,000
	2,817	2,021

The Group leases certain properties located in the PRC and Hong Kong as the Group's offices under operating leases. The leases run for initial periods of 1 – 3 years.

34 Material related party transactions

(a) Key management personnel remuneration

Key management personnel remuneration represents amounts paid to the Company's directors as disclosed in Note 10 and the highest paid employees as disclosed in Note 11.

(b) Transactions with related companies

The Group has transactions with a company controlled by the controlling shareholder ("controlling shareholder's company"), controlling shareholder's family member's company, associates and joint ventures. The following is a summary of principal related party transactions carried out by the Group with these related parties for the years presented.

34 Material related party transactions (continued)

(b) Transactions with related companies (continued)

(i) Significant related party transactions

	2018 RMB'000	2017 RMB'000
Sale of goods to:		
Joint ventures	**222,190**	250,898
Associates	**395,609**	363,974
Controlling shareholder's family member's company*	**26,511**	11,772
	644,310	626,644
Freight expenses to:		
Associates	**615**	677
Lease expenses to:		
Controlling shareholder's company	**1,000**	1,000

* The controlling shareholder's family member became a connected person and the sales first became a connected transaction on 17 November 2017.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the ordinary course of business and on normal commercial terms or in accordance with the terms of the agreements governing such transactions.

34 Material related party transactions (continued)

(b) Transactions with related companies (continued)

(ii) Significant related party balances

	2018 RMB'000	2017 RMB'000
Trade and other receivables due from		
Joint ventures	**305,802**	295,685
Associates	**49,542**	29,370
Controlling shareholder's family member's company	**3,534**	1,923
	358,878	326,978
Trade and other payables due to		
Associates	**2,374**	7,004

(c) Applicability of the Listing Rules relating to connected transactions

The related party transactions in respect of lease expenses paid to the controlling shareholder's company and goods sold to controlling shareholder's family member's company mentioned in Note 34(b) above constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Listing Rules. The disclosures required by Chapter 14A of the Listing Rules are provided under the section "Continuing Connected Transactions" in the Report of Directors. The lease expenses paid to the controlling shareholder's company are continuing connected transactions but are exempted from these disclosure requirements as they are below the de minimis threshold under Rule 14A.76(1). Apart from these transactions, none of the other related party transactions mentioned in Note 34 fall under the definition of a connected transaction or continuing connected transactions as defined in Chapter 14A of the Listing Rules.

35 Company-level statement of financial position

	Note	2018 RMB'000	2017 RMB'000
Non-current assets			
Property, plant and equipment		**11**	11
Investments in subsidiaries		**1,700,428**	1,368,029
Interest in associates		**28,582**	25,403
		1,729,021	1,393,443
Current assets			
Cash and cash equivalents		**6,929**	12,583
		6,929	12,583
Current liabilities			
Interest-bearing borrowings		**112,014**	78,052
Trade and other payables		**682**	111
		112,696	78,163
Net current liabilities		**(105,767)**	(65,580)
Total assets less current liabilities		**1,623,254**	1,327,863
Non-current liabilities			
Interest-bearing borrowings		**34,316**	98,013
		34,316	98,013
Net assets		**1,588,938**	1,229,850
Capital and reserves			
Share capital	31(a)/(c)	**45,242**	40,477
Reserves	31(a)	**1,543,696**	1,189,373
Total equity		**1,588,938**	1,229,850

Approved and authorised for issue by the board of directors on 18 March 2019.

Zhu Xiao Kun *Directors*

Yan Rong Hua *Directors*

36 Accounting estimates and judgements

Note 15, 29(c) and 32(e) contain information about the assumptions and their risk factors relating to goodwill impairment, fair value of share options granted and financial instruments. Other judgements made by management in the application of IFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment are as follows:

(a) Impairment losses on trade and other receivables

Group estimates the amount of loss allowance for ECLs on trade and other receivables that are measured at amortised cost based on the credit risk of the respective financial instruments. The loss allowance amount is measured as the asset's carrying amount and the present value of estimated future cash flows with the consideration of expected future credit loss of the respective financial instrument. The assessment of the credit risk of the respective financial instrument involves a high degree of estimation and uncertainty. When the actual future cash flows are less than expected or more than expected, a material impairment loss or a material reversal of impairment loss may arise, accordingly.

(b) Depreciation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives, after taking into account the estimated residual value. The Group reviews annually the useful life of an asset and its residual value, if any. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

(c) Net realisable value of inventories

Net realisable value of inventories is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses. These estimates are based on current market conditions and historical experience of distributing and selling products of a similar nature. They could change significantly as a result of competitor actions in response to severe industry cycles or other changes in market conditions. Management reassess the estimations at each end of the reporting period.

(d) Income taxes

Determining income tax provisions involves judgement regarding the future tax treatment of certain transactions. The Group carefully evaluates the tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislation. Deferred tax assets are recognised for temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax credits can be utilised, management's judgement is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

(Expressed in Renminbi ("RMB") unless otherwise indicated)

37 Immediate and ultimate controlling party

At 31 December 2018, the directors consider the immediate parent and ultimate controlling party of the Group to be Tiangong Holdings Company Limited, which is incorporated in British Virgin Islands. This entity does not produce financial statements available for public use.

38 Non-adjusting events after the reporting period

(a) After the end of the reporting period the directors proposed a final dividend of RMB0.0357 per ordinary share on 18 March 2019. Further details are disclosed in Note 31(b).

(b) Subsequent to end of the reporting period the Group reached an agreement with the controlling shareholder's company to acquire the land and buildings situated at Danyang, Jiangsu, the PRC at a cash consideration of RMB100,000,000 on 15 January 2019. The consideration was arrived at after arm's length negotiations between the parties with reference to the valuation report issued by an independent valuer. No adjustments are required to be made to these financial statements as a result of the asset acquisition.

39 Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2018

Up to the date of issue of these financial statements, the IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended 31 December 2018 and which have not been adopted in these financial statements. These include the following which may be relevant to the Group.

	Effective for accounting periods beginning on or after
IFRS 16, *Leases*	1 January 2019
IFRIC 23, *Uncertainty over income tax treatments*	1 January 2019
Annual Improvements to IFRSs 2015–2017 Cycle	1 January 2019
Amendments to IAS 28, *Long-term interest in associates and joint ventures*	1 January 2019

The Group is in the process of making an assessment of what the impact of these amendments and new standards is expected to be in the period of initial application. So far the Group has identified some aspects of the new standards which may have a significant impact on the historical financial information. Further details of the expected impacts are discussed below. The Group may also change its accounting policy elections, including the transition options, until the standards are initially applied in that financial report.

39 Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 December 2018 (continued)

IFRS 16 Leases

As disclosed in Note 3(f), currently the Group classifies leases into finance leases and operating leases and accounts for the lease arrangements differently, depending on the classification of the lease. The Group enters into some leases as the lessor and others as the lessee.

IFRS 16 is not expected to impact significantly on the way that lessors account for their rights and obligations under a lease. However, once IFRS 16 is adopted, lessees will no longer distinguish between finance leases and operating leases. Instead, subject to practical expedients, lessees will account for all leases in a similar way to current finance lease accounting, i.e. at the commencement date of the lease the lessee will recognise and measure a lease liability at the present value of the minimum future lease payments and will recognise a corresponding "right-of-use" asset. After initial recognition of this asset and liability, the lessee will recognise interest expense accrued on the outstanding balance of the lease liability, and the depreciation of the right-of-use asset, instead of the current policy of recognising rental expenses incurred under operating leases on a systematic basis over the lease term. As a practical expedient, the lessee can elect not to apply this accounting model to short-term leases (i.e. where the lease term is 12 months or less) and to leases of low-value assets, in which case the rental expenses would continue to be recognised on a systematic basis over the lease term.

IFRS 16 will primarily affect the Group's accounting as a lessee of leases for properties, plant and equipment which are currently classified as operating leases. The application of the new accounting model is expected to lead to an increase in both assets and liabilities and to impact on the timing of the expense recognition in the statement of profit or loss over the period of the lease. As disclosed in Note 33(b), at 31 December 2018 the Group's future minimum lease payments under non-cancellable operating leases amount to RMB2,817,000 for properties and other assets respectively, the majority of which is payable either within 1 year or between 1 and 5 years after the reporting date. Some of these amounts may therefore need to be recognised as lease liabilities, with corresponding right-of-use assets, once IFRS 16 is adopted. Since the Group's non-cancellable operating lease commitment is not material as at 31 December 2018, the Group expects that the adoption of IFRS 16 will not have significant impact on the financial position and financial performance of the Group. The Group will need to perform a more detailed analysis to determine the amounts of new assets and liabilities arising from operating lease commitments on adoption of IFRS 16, after taking into account the applicability of the practical expedient and adjusting for any leases entered into or terminated between now and the adoption of IFRS 16 and the effects of discounting.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. The standard offers different transition options and practical expedients, including the practical expedient to grandfather the previous assessment of which existing arrangements are, or contain, leases. If this practical expedient is chosen, the Group will apply the new definition of a lease in IFRS 16 only to contracts that are entered into on or after the date of initial application. If the practical expedient is not chosen, the Group will need to reassess all of its decisions about which existing contracts are, or contain, leases, using the new definition. Depending on whether the Group elects to adopt the standard retrospectively or follow a modified retrospective method of recognising a cumulative-effect adjustment to the opening balance of equity at the date of initial application, the Group may or may not need to restate comparative information for any changes in accounting resulting from the reassessment. The Group has not yet decided whether it will choose to take advantage of this practical expedient, and which transition approach to be taken.

Financial Information Summary

		Year ended 31 December			
	2018	2017	2016	2015	2014
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Revenue	**5,021,546**	3,898,443	3,376,134	3,429,397	4,535,670
Profit before taxation	**280,568**	218,097	130,916	85,205	544,168
Income tax	**(13,598)**	(43,396)	(14,920)	(13,074)	(81,421)
Profit for the year	**266,970**	174,701	115,996	72,131	462,747
Other comprehensive (loss)/income for the year	**(11,607)**	(14,555)	45,713	(27,787)	(1,404)
Attributable to:					
Equity shareholders of the Company	**247,228**	154,544	156,284	44,836	462,062
Non-controlling interests	**8,135**	5,602	5,425	(492)	(719)
Earnings per share (RMB)					
Basic (RMB)	**0.106**	0.076	0.050	0.033	0.230

		As at 31 December			
	2018	2017	2016	2015	2014
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets					
Non-current assets	**3,923,593**	3,801,667	3,737,020	3,432,974	3,168,657
Current assets	**6,112,759**	4,902,213	4,558,884	4,950,998	5,196,180
Total assets	**10,036,352**	8,703,880	8,295,904	8,383,972	8,364,837
Liabilities					
Non-current liabilities	**1,011,943**	917,991	309,029	578,292	689,801
Current liabilities	**4,201,449**	3,482,924	3,831,441	3,929,393	3,745,215
Total liabilities	**5,213,392**	4,400,915	4,140,470	4,507,685	4,435,016
Equity					
Total equity	**4,822,960**	4,302,965	4,155,434	3,876,287	3,929,821

Note: The results of the Group for the four financial years ended 31 December 2014, 2015, 2016 and 2017 and its assets and liabilities were extracted from previous annual reports, which also set forth the details of the basis of presentation of the combined accounts.

Corporate Information

Registered Name
Tiangong International Company Limited

Chinese Name
天工國際有限公司

Stock Code
Hong Kong Stock Exchange: 826

Board of Directors
Executive Directors
Mr. Zhu Xiaokun *(Chairman)*
Mr. Wu Suojun *(Chief Executive Officer)*
Mr. Yan Ronghua
Mr. Jiang Guangqing

Independent Non-executive Directors
Mr. Gao Xiang
Mr. Lee Cheuk Yin, Dannis
Mr. Wang Xuesong

Company Secretary
Mr. Lee Johnly

Authorized Representatives
Mr. Lee Cheuk Yin, Dannis
Mr. Lee Johnly

Audit Committee
Mr. Lee Cheuk Yin, Dannis *(Chairman)*
Mr. Gao Xiang
Mr. Wang Xuesong

Remuneration Committee
Mr. Wang Xuesong *(Chairman)*
Mr. Zhu Xiaokun
Mr. Gao Xiang
Mr. Lee Cheuk Yin, Dannis

Nomination Committee
Mr. Gao Xiang *(Chairman)*
Mr. Zhu Xiaokun
Mr. Wang Xuesong
Mr. Lee Cheuk Yin, Dannis

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Hong Kong Branch Share Registrar and Transfer Office in Hong Kong
Computershare Hong Kong Investor Services Limited
Shops 1712–1716, 17th Floor
Hopewell Center
183 Queen's Road East
Wanchai
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Principal Bankers
China Construction Bank Corporation
Industrial and Commercial Bank of China Limited
Bank of China Limited
Agricultural Bank of China Limited
The Export-import Bank of China
The Hong Kong and Shanghai Banking Corporation Limited

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