MANAGEMENT DISCUSSION AND ANALYSIS

REVIEW OF RESULTS

The turnover of the Group for the year was approximately RMB1,056,629,000, representing an increase of approximately 12.2% compared with approximately RMB941,577,000 for the last year while the net profit attributable to shareholders was approximately RMB308,000, representing a decrease of approximately 99.3% compared with approximately RMB41,229,000 for the last year.

BUSINESS REVIEW

Steel price roared to historical high in the first quarter, due to lower increase in new resources of steel in the PRC in the beginning of the year, as well as the expected impact of rising price of iron ore. Subsequently, following the escalating macro-economic control over the market, steel demand grew at a slower pace, in addition to the release of production capacity within the industry, new resources in the PRC increased substantially. Eventually, the prices of steel products have dropped significantly in the second half of 2005. The profitability of the Group's main business recorded a considerable shrink. Sales volume of steel products decreased 2.1% from approximately 142,000 tonnes for the last year to approximately 139,000 tonnes. Although the selling price of the Group's steel products increased by approximately 15.0% compared with that for the last year, the gross profit decreased and was mainly because of relatively lower growth rate of the selling prices of our steel products as compared to that of the purchasing costs of raw materials and fuels during the year.

PRODUCTION AND SALES

The revenue from domestic sales of steel products in the PRC during the year was approximately RMB120,095,000, representing an decrease of approximately 17.4% compared with approximately RMB145,406,000 last year.

The revenue from indirect export sales of steel products in the PRC during the year was approximately RMB919,835,000, representing an increase of approximately 16.5% compared with approximately RMB789,859,000 for the last year. The market for indirect export sales in the PRC continued to be the core market for the Group.

The revenue from direct export sales of steel products outside the PRC during the year was approximately RMB8,602,000 while it was approximately RMB6,312,000 for the last year. The Group will continue to develop and maintain a good momentum of the international market, especially the newly launched product (stainless steel pipes) which has been exported to countries such as the U.S. and Vietnam.

The revenue from export sales of aluminum forged wheel products outside Taiwan during the two months period since the Group's acquisition of Fullchamp Technologies Co., Ltd in October 2005 was approximately RMB8,097,000. The Group will put great effort on developing its marketing and sales channels in order to achieve a profitable economic of scale.

GROSS PROFIT

The Group recorded a gross profit of approximately RMB41,067,000 for the year, with a gross profit margin of approximately 3.9%, compared with the gross profit of approximately RMB99,378,000 and a gross profit margin of approximately 10.6% for the last year. This was mainly attributable to the lower growth rate of the selling prices of our products as compared to that of the purchasing costs of raw materials and fuels, coupled with tight supply of power and transport.

OPERATING EXPENSES

The total operating expenses of the Group for the year were approximately RMB57,769,000, of which approximately RMB9,853,000 in distribution costs, RMB30,558,000 in administrative expenses, RMB2,986,000 in other operating expenses and RMB14,372,000 in finance costs, accounting for approximately 0.9%, 2.9%, 0.3% and 1.4% of turnover respectively while the amounts for the last year were approximately RMB9,954,000, RMB28,124,000, RMB3,922,000 and RMB5,375,000 respectively, accounting for approximately 1.1%, 3.0%, 0.4% and 0.6% respectively.

FINANCIAL RESOURCES AND TREASURY POLICIES

The Group continues to adhere to prudent treasury policies. The gearing ratio (borrowings divided by shareholders' funds) as of 31 December 2005 was approximately 198.6% (2004: 100.7%). The total borrowings of the Group amounted to approximately RMB427,511,000 (2004: RMB230,807,000), mainly denominated in US dollars, HK dollars, Renminbi and new Taiwan dollars with floating interest rates. The Group's short term loans from banks accounted for approximately 43.4% of the total assets (2004: 42.6%).

The current ratio (current assets divided by current liabilities) as of 31 December 2005 was approximately 1.21 (2004: 1.74). The Group continued to insure against receivables in order to lower the risks of credit sales and to ensure that funds would be recovered on a timely basis, hence fulfilling the requirements for debt repayments and working capital commitments.

CASH FLOW

Net cash outflow of approximately RMB142,085,000 was used in operating activities for the year, mainly resulted from the increase of inventories level of the Group. Despite approximately RMB957,388,000 raised from bank borrowings, the net decrease in cash and cash equivalents amounted to approximately RMB75,687,000, as a result of net cash outflow of approximately RMB37,150,000 used for plant expansion and purchase of machinery and equipment and RMB12,000,000 dividend paid. Cash and cash equivalents as at 31 December 2005 amounted approximately RMB27,136,000, mainly denominated in Renminbi, US dollars, HK dollars and new Taiwan dollars.

EXCHANGE RATE EXPOSURES

As most of the Group's monetary assets and liabilities are denominated in US dollars, HK dollars, Renminbi and new Taiwan dollars and those currencies remained relatively stable during the year, the Group was not exposed to any significant exchange risk. Meanwhile, the Group is also studying and implementing various measures in relation to reducing any exchange impact from the revalued of Renminbi against US dollars and new Taiwan dollars.

PLEDGE OF ASSETS

As at 31 December 2005, property, plant and equipment and interest in leasehold land held for own use under an operating lease of the Group with net book value of approximately RMB159,791,000 and RMB8,860,000 respectively were pledged to secure bank borrowings.

CONTINGENT LIABILITIES

The Group did not have any significant contingent liabilities at the balance sheet date (2004: Nil). At 31 December 2005, the Company had provided corporate guarantees of RMB145,263,000 (2004: RMB173,808,000) in favour of certain banks for banking facilities granted to a subsidiary. These banking facilities had been utilised to the extent of approximately RMB96,983,000 at the balance sheet date (2004: RMB104,320,000).

EMPLOYMENT, TRAINING AND DEVELOPMENT

As at 31 December 2005, the Group had a total of 480 employees. Total staff costs for the year ended 31 December 2005 were approximately RMB18,640,000, including retirement benefits cost of approximately RMB1,474,000. Remuneration packages of the Group are maintained at a competitive level to attract, retain and motive employees and are reviewed on a periodic basis.

OUTLOOK

Under the macro-economic control policy, the growth rate will slow down in 2006. According to the "Strategy on the Development of the Steel Industry" promulgated by the State, the development of the steel industry will be directed towards controlled volume, technology upgrade, industrial layout and product mix adjustment, so as to combine the impact of an increase in new capacity with the phasing out of backward capacity. Following the completion of Phase III of our plant and the new installation of steel-cutting and pipe-making machines, the Group's future production capacity and market competitiveness would be enhanced to meet the steady but moderately fast growth of the national economy of the PRC. Moreover, the Group's new product (stainless pipes) has already been launched to the domestic market in the PRC as well as the international market, and has duly obtained the Hygiene Permit for Stainless Steel Pipes from the Guangdong Province Health Bureau, which would significantly help to promote the Group's new products in those markets.

Looking forward to 2006, the Group's management is confident that the Group will fully capitalize its extensive experience in cost management and achieve greater cost effectiveness, increased output of high value-added products and welcome to every investment opportunity which are beneficial to the Group, with an aim to generate the best return from investments and generate the best returns to our investors.