



CHINA ORIENTAL GROUP COMPANY LIMITED
中國東方集團控股有限公司*

(Incorporated in Bermuda with limited liability)

(在百慕達註冊成立的有限公司)

(Stock Code : 581)

(股份代號 : 581)



China Oriental Group Company Limited
中國東方集團控股有限公司

2006
ANNUAL REPORT
年 報

CONTENTS

2	Financial Highlights
3	Corporate Information
4	Chairman's Statement
10	Corporate Governance Report
17	Biographical Details of Directors and Senior Management
21	Directors' Report
31	Independent Auditor's Report
33	Consolidated Balance Sheet
35	Company Balance Sheet
36	Consolidated Income Statement
37	Consolidated Statement of Changes in Equity
38	Consolidated Cash Flow Statement
39	Notes to the Consolidated Financial Statements
95	Summary of Financial Information
97	Notice of Annual General Meeting

FINANCIAL HIGHLIGHTS

	For the year ended 31 December		
	2006	2005	Percentage of increase/ (decrease)
Sales volume (<i>thousand tonnes</i>)			
Billets	1,173	1,458	(19.5%)
Strips and strip products	2,202	1,848	19.2%
H-section steel products	250	N/A	N/A
Average selling price (net of value-added tax) per tonne (<i>RMB</i>)			
Billets	2,347	2,491	(5.8%)
Strips and strip products	2,600	2,917	(10.9%)
H-section steel products	2,917	N/A	N/A
Revenue (<i>RMB million</i>)	9,782	9,183	6.5%
Profit attributable to equity holders of the Company (<i>RMB million</i>)	1,033	847	22.0%
Basic earnings per share (<i>RMB</i>)	0.36	0.29	24.1%

CORPORATE INFORMATION

BOARD OF DIRECTORS

Executive Directors

Mr. Han Jingyuan

(Chairman and Chief Executive Officer)

Ms. Chen Ningning

(Vice Chairman)

Mr. Zhu Jun

Mr. Tang Chi Fai (resigned on 13 April 2007)

Mr. Liu Lei

Mr. Shen Xiaoling

Mr. Yu Jianshui (appointed on 14 April 2007)

Independent Non-executive Directors

Mr. Gao Qingju

Mr. Yu Tung Ho

Mr. Wong Man Chung, Francis

COMPANY SECRETARY AND QUALIFIED ACCOUNTANT

Mr. Lai Po Sing, *FCCA, FCPA (Practising)*

COMPANY'S WEBSITE

www.chinaorientalgroup.com

REGISTERED OFFICE

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Bermuda

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Wanchai, Hong Kong

BERMUDA PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Butterfield Fund Services (Bermuda) Limited

HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Tricor Investor Services Limited

AUDITORS

PricewaterhouseCoopers

PRINCIPAL BANKER

China Construction Bank

CHAIRMAN'S STATEMENT



CHAIRMAN'S STATEMENT



BUSINESS REVIEW

The audited consolidated revenue of the Group for the year 2006 was RMB9,782 million, representing an increase of 6.5% as compared to that of 2005, while the audited profit attributable to equity holders of the Company was RMB1,033 million, representing an increase of 22% from that of 2005. The audited basic earnings per share for the year 2006 was RMB0.36, representing an increase of 24.1% from that of 2005.

In 2006, the Group's total sales volume was 3,746,201 tonnes (2005: 3,335,805 tonnes), representing an increase of 12.3%. In 2006, billets, strips and strip-related products, H-section steel, cold rolled sheets and galvanised sheets accounted for 31.3%, 58.8%, 6.6%, 1.2% and 2.1% of the Group's total sales volume respectively (2005: accounted for 43.7%, 55.4%, N/A, 0.9% and N/A respectively), indicating further optimisation of the Group's sales mix.

The Group's average selling prices of billets and strips and strip-related products as well as H-section steel products (excluding value-added tax) were RMB2,347 per tonne, RMB2,600 per tonne and RMB2,917 per tonne respectively in 2006, representing decreases of 5.8%, 10.9% and N/A when compared to RMB2,491 per tonne, RMB2,917 per tonne and N/A in 2005. In February 2007, the unaudited average selling prices of billets and strips and strip-related products as well as H-section steel products (excluding value-added tax) were RMB2,505 per tonne, RMB2,750 per tonne and RMB3,195 per tonne respectively.

The average costs of sales of the Group's billets and strips and strip-related products as well as H-section steel products in 2006 were RMB1,963 per tonne, RMB2,155 per tonne and RMB2,629 per tonne respectively, representing decreases of 13.3%, 11.5% and N/A when compared with RMB2,264 per tonne, RMB2,436 per tonne and N/A in 2005 respectively. The decline in the average costs of sales per tonne was mainly due to lower average purchasing prices of iron powder and coke in 2006 when compared with those in 2005.

In 2006, gross profits of billets and strips and strip-related products as well as H-section steel products were RMB384 per tonne, RMB445 per tonne and RMB288 per tonne respectively (2005: RMB227 per tonne, RMB481 per tonne and N/A respectively).

Owing to the increase in total sales volume in 2006 and a relatively small decline in the selling price of billets, the gross profit in 2006 increased by 16.4% from that of 2005 to RMB1,424 million (2005: approximately RMB1,224 million).

CHAIRMAN'S STATEMENT

AWARDS TO THE COMPANY AND THE MANAGEMENT

Hebei Jinxi Iron and Steel Company Limited ("Jinxi Limited"), a subsidiary of the Group, and Mr. Han Jingyuan, the Chairman and the Chief Executive Officer of the Company, were named as the "2005 Top Ten Most Influential Brands in China" and "Top Ten Outstanding Entrepreneurs in Brand Building" respectively by the China Enterprise Culture Improvement Association, China Industrial Design Association and Market Daily of the People's Daily as well as China Quality and Brand Magazine in January 2006.

In May 2006, Jinxi Limited ranked 12th out of the top 100 enterprises in Hebei Province at the Sixth "Top 100 Enterprises" held in Hebei Province.

On 19 August 2006, the National Bureau of Statistics of China announced that Jinxi Limited ranked 168th out of the top 500 manufactures in the Chinese manufacturing industry.

Jinxi Limited was named as an "Enterprise with an AAA credit rating in quality" by China Product Quality Association and named as the "Enterprise Recognised for User Satisfaction in Hebei Province" by the Association for Quality of Hebei Province in November 2006.

In December 2006, the Ministry of Commerce of the People's Republic of China announced a list of the 500 largest foreign investment companies for the year 2005/2006. Jinxi Limited ranked 87th on the list, and was the second largest out of 14 enterprises from Hebei Province named on the list.

Mr. Han Jingyuan was also named the "Best Entrepreneurs in China" (Fifth Edition) by China Enterprise Confederation, China Enterprise Directors Association and other organisations in April 2006.

The Hebei Entrepreneur Association named Mr. Han Jingyuan as an "Excellent Private Entrepreneur in Hebei Province" on 18 August 2006.

HUMAN RESOURCE AND REMUNERATION POLICIES

As at 31 December 2006, the Group had a workforce of 6,052 (31 December 2005: 5,224) and temporary staff of 2,150 (31 December 2005: 1,906). Staff cost of the Group for the year 2006 was approximately RMB243 million (2005: approximately RMB169 million), representing an increase of 44.4%. The staff cost included basic salaries and benefits, as well as staff benefits such as discretionary bonus, medical and insurance plans, pension scheme, unemployment insurance plan, maternity insurance plan, fair value of share option etc. The Group's remuneration policies are designed to tie its employees' income to their productivity and/or sales volume, as well as to the extent they meet the Group's quality control and cost control targets. To enable the directors and employees of any of the Group's subsidiary or invested entity to have the opportunity for acquiring a shareholding in the Company and to encourage them to strive for enhancing the value of the Company and its shares for the benefit of the Company and its shareholders as a whole, the Company adopted a share option scheme on 23 June 2006. In order to improve the Group's productivity and further enhance the quality of its workforce, the Group provided continuing education and training programmes to both the management staff and factory workers.

CHAIRMAN'S STATEMENT

PRODUCTION CAPACITY

The annual production capacity of the Group as at the following dates was:

	31 December 2006 (tonnes)	31 December 2005 (tonnes)
Billets	4,000,000	4,000,000
Strips	1,600,000	800,000
Mid-width strips	1,200,000	1,000,000
H-section steel products	1,000,000	—
Cold rolled sheets and galvanised sheets	250,000 — 400,000	250,000 — 400,000

H-SECTION STEEL ROLLING LINE

The production line of H-section steel products, with an annual production capacity of 1 million tonnes of H-section steel products, commenced trial production in May 2006 and commercial production in late August 2006.

In 2006, the Group produced 473,164 tonnes of H-section steel products, with the sales volume of approximately 249,911 tonnes. The sales revenue and cost of sales generated from approximately 131,897 tonnes of H-section steel produced prior to the end of the trial production in late August 2006 had been recognised as the costs of H-section steel project in accordance with the relevant accounting standards.

The export sales of H-section steel in 2006 accounted for approximately 9.5% of the above-mentioned sales volume and the sales volume that had been carried over to project costs.

INVESTMENT IN FOSHAN JIN XI JIN LAN COLD ROLLED SHEET CO., LTD. ("FOSHAN JINXI")

In 2006, the Group sold 44,814 tonnes of cold rolled sheets and 76,869 tonnes of galvanised sheets respectively (2005: 30,578 tonnes and N/A respectively).

In 2006, the average selling prices of the Group's cold rolled sheets and galvanised sheets (excluding value-added tax) were RMB3,578 per tonne and RMB4,959 per tonne respectively (2005: RMB3,831 per tonne and N/A respectively).

In February 2007, the unaudited average selling prices of the Group's cold rolled sheets and galvanised sheets (excluding value-added tax) were RMB3,807 per tonne and RMB5,134 per tonne respectively.

Pursuant to prudent principles, the Group, during the year, made a provision for assets impairment of approximately RMB41.859 million for Foshan Jinxi's property, plant and equipment.

Due to a decline in the profit margin in the product market of Foshan Jinxi, intensified market competition and production, the audited annual loss, after taking into account of the above-mentioned provision for assets impairment, of Foshan Jinxi was approximately RMB91.252 million (2005: RMB51.613 million).

Following the commercial production of Foshan Jinxi's galvanised production line, with an annual capacity of 150,000 tonnes in August 2006, Foshan Jinxi's competitiveness and product mix will further be enhanced. Foshan Jinxi will continue to fine-tune its production process, improve its production efficiency and product mix as well as actively expand the market.

CHAIRMAN'S STATEMENT

DIVIDEND POLICY

The Company intends to distribute not less than 20% of the Group's distributable profit as dividend for the periods subsequent to its listing, but the actual amount of dividend and its percentage to the profit will be at the discretion of the Board and will depend upon the Company's future operation and earnings, capital requirement and surplus, general financial condition, contractual restrictions, and other factors that the Board deem relevant. In addition, pursuant to relevant PRC law, Jinxi Limited's distributable profit should not be higher than its net profit after allocations made to the statutory reserve as determined by the generally accepted accounting principles in the PRC.

CAPITAL STRUCTURE

The cash and bank balances (including restricted bank balances) of the Group as at 31 December 2006 was RMB530 million (31 December 2005: RMB1,725 million).

The current ratio was 1.55 as at the end of 2006 (31 December 2005: 1.22).

As at 31 December 2006, the Group's borrowings repayable within one year and borrowings repayable after one year amounted to approximately RMB573 million and RMB361 million respectively (31 December 2005: approximately RMB1,336 million and RMB294 million respectively).

The consolidated interest expenses in 2006 amounted to RMB50.387 million (2005: RMB74.189 million). The interest coverage was 25.5 times (2005: 14.5 times).

As at 31 December 2006, the ratio between total liabilities and total assets of the Group was 31.9% (31 December 2005: 42.0%).

To conclude, the financial position of the Group was healthy.

CAPITAL COMMITMENTS

As at 31 December 2006, the Group had capital commitments amounted to RMB2,070 million (31 December 2005: RMB256 million), which mainly consisted of the capital commitments to the construction of the H-section steel rolling line with annual production capacity of 1.2 million tonnes and other ancillary projects. Based on preliminary estimate, such capital commitments will be financed by the Group's internal resources and/or bank borrowings.

GUARANTEES AND CONTINGENT LIABILITIES

As at 31 December 2006, the Group's contingent liabilities amounted to RMB69 million (31 December 2005: RMB277 million), which mainly consisted of the guarantees for the letter of credit issued by an agent appointed by the Group to import machinery and equipment on behalf of the Group.

PLEDGE OF ASSETS

As at 31 December 2006, the net book value of the Group's property, plant and equipment amounting to approximately RMB1,088 million (31 December 2005: approximately RMB568 million), land use rights amounting to approximately RMB65 million (31 December 2005: approximately RMB67 million), inventories amounting to approximately RMB69 million (31 December 2005: approximately RMB32 million), notes receivable amounting to approximately RMB174 million (31 December 2005: approximately RMB67 million) and restricted bank balances amounting to approximately RMB95 million (31 December 2005: approximately RMB1,016 million) had been pledged as security for the Group's banking facilities.

CHAIRMAN'S STATEMENT

PLEDGE OF ASSETS *(Continued)*

As at 31 December 2006, Jinxi Limited pledged approximately RMB51 million of its notes receivable as security for providing guarantees so as to facilitate the issuing of letter of credit by a third party acting as its agent to import plant and equipment for Jinxi Limited (31 December 2005: approximately RMB248 million).

EXCHANGE RISKS

As at 31 December 2006, Renminbi, US dollar and HK dollar accounted for 75.9%, 23.7% and 0.4% of the Group's total bank balances (including restricted bank balances) respectively (31 December 2005: 28.9%, 71.0% and 0.1% respectively).

As majority of the sales, purchases of raw materials and bank loans committed by the Group were mainly in Renminbi in 2006 and 2005, the Group's exposure to foreign exchange risk remained relatively low. In light of the construction of the H-section steel rolling line, the Group had entered into project and equipment contracts in Euro Dollar of approximately Euro42.9 million. In 2005, the Group has entered into Euro Dollar forward contract to hedge against partial exchange rate risk exposure.

INTEREST RATE RISKS

The interest rates of the Group's certain borrowings are subject to variations. The risk of increasing interest rate will increase the interest costs of both new borrowings and existing borrowings. At present, the Group does not use any derivatives to hedge its interest rate risk exposure.

POST BALANCE SHEET EVENTS

Saved as disclosed in this report of the Group, there are no events to cause material impact on the Group from the balance sheet date to the date of this report.

PROSPECTS

In the coming year, with favourable factors including continuous economic growth in the PRC and the government's continued elimination

of backward capacity of iron and steel, the domestic price of iron and steel will continue to be supported by the relatively higher prices of iron and steel in overseas markets and surging raw material prices. However, increase in the supply of iron and steel in the industry as well as the uncertainty over the government's introduction of other macroeconomic austerity measures (for example, a further downward adjustment to export tax rebate) will rein in the rise in the price of iron and steel.

In the face of an intensified market competition, the Group will continue to keep an eye on the market and improve its product mix and enhance its production efficiency. Following the commercial production of the H-section steel rolling line and the strip production line with an annual production capacity of 600,000 tonnes in late August 2006, the Group will be able to further fine-tune its product mix.

With regard to raw material, the increase in production capacity in the iron and steel industry will drive the demand for both domestic and imported iron powder in the PRC. As such, it is expected that the price of iron powder will continue to fluctuate at a high level. In early March 2007, the purchasing price of domestic iron powder (including value-added tax) was approximately RMB780 per tonne.

On the front of coke, owing to the frequent accidents in coal mines, rise in coal price and strained railway transportation, the coke price will also fluctuate at a high level. In early March 2007, the purchasing price of coke (including value-added tax) was approximately RMB1,250 per tonne.

On Behalf of the Board
China Oriental Group Company Limited

Han Jingyuan
Chairman and Chief Executive Officer

Hong Kong, 3 April 2007

CORPORATE GOVERNANCE REPORT

(A) CORPORATE GOVERNANCE PRACTICES

The Company and the Board of Directors of the Company (the "Board") have applied the principles in the provisions of the Code on Corporate Governance Practices (the "Code") contained in Appendix 14 of the Rules Governing the Listing of Securities (the "Listing Rules") on The Stock Exchange of Hong Kong Ltd. (the "Stock Exchange") by adopting the Code by way of Board resolutions.

During the year, the Board has adopted and complied with the Code with the exception that the roles of the Chairman and the Chief Executive Officer of the Company are performed by Mr. Han Jingyuan.

The Board believes that there is no need to segregate the roles of the Chairman and the Chief Executive Officer of the Company because the role of the chief executive officer/general manager of the Company's major operating subsidiaries are performed by other persons and apart from acting as the listing vehicle of the Group, the Company has no real operating activities or business.

Depending on the future development of the operating activities or business of the Company, eventually the Board will actively consider the issue of replacing Mr. Han Jingyuan by an appropriate candidate as the Chief Executive Officer of the Company.

(B) DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors of the Company's (the "Directors") securities transactions on terms no less exacting than the required standard set out in the Model Code of Appendix 10 of the Listing Rules (the "Model Code").

The Company has made specific enquiry of all Directors and all Directors have confirmed with the Company that they have complied with the required standard set out in the Model Code and its code of conduct regarding Directors' securities transactions during the year.

(C) BOARD OF DIRECTORS

The directors of the Company during the year were as follows:

Executive Directors

Mr. Han Jingyuan (*Chairman and Chief Executive Officer*)

Ms. Chen Ningning (*Vice Chairman*)

Mr. Zhu Jun

Mr. Tang Chi Fai

Mr. Liu Lei

Mr. Shen Xiaoling

Independent non-executive Directors

Mr. Yu Tung Ho

Mr. Gao Qingju

Mr. Wong Man Chung, Francis

(with professional qualification in accordance with the Listing Rules)

CORPORATE GOVERNANCE REPORT

(C) BOARD OF DIRECTORS *(Continued)*

A total of 6 Board meetings were held during the year. The individual attendance of each Director was as follows:

Number of Attendance

Mr. Han Jingyuan	6
Ms. Chen Ningning	1
Mr. Zhu Jun	6
Mr. Tang Chi Fai	6
Mr. Liu Lei	6
Mr. Shen Xiaoling	6
Mr. Yu Tung Ho	6
Mr. Gao Qingju	6
Mr. Wong Man Chung, Francis	6

The Board operates and exercises its power in accordance with the Bye-laws of the Company. In addition, the Board has also specifically resolved that all transactions/contracts/other matters of the Group that are subject to the disclosure requirement in accordance with the Listing Rules should be approved by the Board in advance.

The Board considers all the independent non-executive Directors are independent during the year.

Save as disclosed in the section of "Biographical Details of Directors and Senior Management" in the annual report of the Company, there are no relationships (including financial, business, family or other material/relevant relationships) among members of the Board.

(D) CHAIRMAN AND CHIEF EXECUTIVE OFFICER

During the year, the roles of the Chairman and the Chief Executive Officer of the Company are performed by Mr. Han Jingyuan.

(E) INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Gao Qingju and Mr. Yu Tung Ho have service contracts for a period of one year commencing from 23 December 2006. Mr. Wong Man Chung, Francis has service contract for a period of one year commencing from 25 August 2006.

The annual fee specified in each of Mr. Gao Qingju, Mr. Yu Tung Ho and Mr. Wong Man Chung, Francis's existing service contracts are HK\$300,000, HK\$350,000 and HK\$300,000 respectively.

(F) REMUNERATION OF DIRECTORS

The role and function of the remuneration committee of the Company (the "Remuneration Committee") are as follows:

- (a) to make recommendations to the Board on the Company's policy and structure for all remuneration of Directors and senior management and on the establishment of a formal and transparent procedure for developing policy on such remuneration;

(F) REMUNERATION OF DIRECTORS

(Continued)

- (b) to have the delegated responsibility to determine the specific remuneration packages of all executive Directors and senior management, including benefits in kind, pension rights and compensation payments, including any compensation payable for loss or termination of their office or appointment, and make recommendations to the Board of the remuneration of non-executive Directors;
- (c) to review and approve performance-based remuneration by reference to corporate goals and objectives resolved by the Board from time to time;
- (d) to review and approve the compensation payable to executive Directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms and that such compensation is otherwise fair and not excessive for the Company;
- (e) to review and approve compensation arrangements relating to dismissal or removal of Directors for misconduct to ensure that such arrangements are determined in accordance with relevant contractual terms and that any compensation payment is otherwise reasonable and appropriate; and

- (f) to ensure that no Director or any of his/her associates is involved in deciding his/her own remuneration.

The basis of the emolument payable to the Directors is determined with reference to the range of prevailing directors' fee for Director of listed companies in Hong Kong and is subject to the approval of the Remuneration Committee. The Remuneration Committee will consider factors such as salaries paid by comparable companies, time commitment and responsibilities of the Directors, employment conditions elsewhere in the Group and desirability of performance-based remuneration.

The Chairman of the Remuneration Committee is Mr. Han Jingyuan. The remaining members are the three independent non-executive Directors, Mr. Gao Qingju, Mr. Yu Tung Ho and Mr. Wong Man Chung, Francis.

A total of 5 Remuneration Committee meetings were held during the year to discuss remuneration related matters. The individual attendance of each member was as follows:

Number of Attendance

Mr. Han Jingyuan	5
Mr. Gao Qingju	5
Mr. Yu Tung Ho	5
Mr. Wong Man Chung, Francis	5

CORPORATE GOVERNANCE REPORT

(F) REMUNERATION OF DIRECTORS

(Continued)

During the year, the work performed by the Remuneration Committee was as follows:

- reviewed and revised the Directors' fee;
- reviewed and approved the Directors and senior management's remuneration in the Company and subsidiaries of the Company; and
- reviewed and approved the granting of options to Directors and senior management of the Company.

(G) NOMINATION OF DIRECTORS

The Company did not have a nomination committee. The candidates for directorship during the year were selected by the senior management of the Company subject to the review and approval of the Board in accordance with the Bye-laws of the Company. The criteria adopted by the Board in selecting and approving candidates for directorship are based on whether the candidates are appropriate in term of experience and the potential contribution to the Group associated with the candidates' appointment.

(H) AUDITORS' REMUNERATION

The audit fee of the Group for 2006 was RMB3,300,000.

During the year, there were no significant non-audit service assignments being performed by the auditors of the Group.

(I) AUDIT COMMITTEE

The Company has set up an audit committee and the terms of reference adopted complied with the requirement of the Listing Rules.

The audit committee comprises all of the three independent non-executive Directors of the Company, Mr. Yu Tung Ho, Mr. Gao Qingju and Mr. Wong Man Chung, Francis. The chairman of the audit committee was elected by the members each time when it was held during the year.

The role and function of the audit committee are as follows:

- (a) to be primarily responsible for making recommendation to the Board on the appointment, reappointment and removal of the external auditor, and to approve the remuneration and terms of engagement of the external auditor, and any questions of resignation or dismissal of that auditor;
- (b) to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process in accordance with applicable standard. The audit committee should discuss with the auditor the nature and scope of the audit and reporting obligations before the audit commences;

CORPORATE GOVERNANCE REPORT

(I) AUDIT COMMITTEE *(Continued)*

- (c) to develop and implement policy on the engagement of an external auditor to supply non-audit services. The audit committee should report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken;
- (d) to monitor integrity of financial statements of the Company and the Company's annual report and accounts, half-year report and, if prepared for publication, quarterly reports, and to review significant financial reporting judgements contained in them;
- (e) members of the committee must liaise with the Board, senior management and the qualified accountant and the committee must meet, at least once a year, with the Company's auditors and the committee should consider any significant or unusual items that are, or may need to be, reflected in such reports and accounts and must give due consideration to any matters that have been raised by the Company's qualified accountants, compliance officer or auditors;
- (f) to review the Company's financial controls, internal control and risk management systems;
- (g) to discuss with the management the system of internal control and ensure that management has discharged its duty to have an effective internal control system;
- (h) to consider any findings of major investigations of internal control matters as delegated by the Board or on its own initiative and management's response;
- (i) where an internal audit function exists, to ensure co-ordination between the internal and external auditors, and to ensure that the internal audit function is adequately resourced and has appropriate standing within the Company, and to review and monitor the effectiveness of the internal audit function;
- (j) to review the Group's financial and accounting policies and practices;
- (k) to review the external auditor's management letter, any material queries raised by the auditor to management in respect of the accounting records, financial accounts or systems of control and management's response;
- (l) to ensure that the Board will provide a timely response to the issues raised in the external auditor's management letter;

CORPORATE GOVERNANCE REPORT

(I) AUDIT COMMITTEE *(Continued)*

- (m) to report to the Board on the matters set out in the above role and function; and
- (n) to consider other topics, as defined by the Board.

A total of 2 audit committee meetings were held during the year. The individual attendance of each member was as follows:

	Number of Attendance	Number of acting as chairman
Mr. Gao Qingju	2	1
Mr. Yu Tung Ho	2	0
Mr. Wong Man Chung, Francis	2	1

During the year, the work performed by the audit committee was mainly as follows:

- discussed and reviewed the interim and annual financial statements and internal control matters of the Group with senior management of the Company and the external auditors;
- communicated with the external auditors concerning the auditing procedures of the Group; and
- recommended to the Board on the reappointment of the external auditor, and to review and approve the remuneration and terms of engagement of the external auditor.

(J) DIRECTORS' RESPONSIBILITY IN PREPARING THE ACCOUNTS

The Directors acknowledge that they are responsible for the preparation of accounts which give a true and fair view of the Company and the Group.

(K) ANNUAL REVIEW OF THE EFFECTIVENESS OF THE INTERNAL CONTROL OF THE GROUP

The Directors have conducted a review of the effectiveness of the system of internal control of the Group during the year and have resolved that the system of internal control of the Group was effective during the year except for the following:

As stated in the announcement dated 11 April 2007, the Board announced that Hebei Jinxi Iron and Steel Company Limited ("Jinxi Limited") has signed a guarantee dated April 2006 to provide financial assistance in the form of guarantee to its fellow subsidiary, Foshan Jin Xi Jin Lan Cold Rolled Sheet Co., Ltd., which is a connected person (as defined in the Listing Rules) of the Group. Due to oversight and inadvertent misunderstanding of the Listing Rules by some of the management of the Group involved in the issuance of the guarantee, Jinxi Limited's entry into the guarantee and the provisions of the guarantee dated April 2006 was not being reported to the Company. As a result, the failures by the Company to notify the Stock Exchange and announce Jinxi Limited's entry into the guarantee and the provisions of the guarantee and to seek shareholders of the Company's approval as required under Chapter 14A of the Listing Rules constitutes a breach of Rule 14A.63 of the Listing Rules.

(K) ANNUAL REVIEW OF THE EFFECTIVENESS OF THE INTERNAL CONTROL OF THE GROUP *(Continued)*

Each of the Directors is aware and understands that each has undertaken to the Stock Exchange that in exercising each of their powers and duties as a director, each of them would comply to the best of his or her ability (and to procure the Company to comply) with the Listing Rules. However, in view of the facts surrounding the provision of the guarantee and in particular, the fact the Directors (other than the two executive Directors involved in issuing the guarantee, being Mr. Han and Mr. Shen) were not aware of Jinxi Ltd. entering into the guarantee, after discussion amongst the members of the Board, the Board considers that Mr. Han and Mr. Shen, as executive Directors of the Company and also more importantly as the directors and in respect of Mr. Shen only, deputy general manager of Jinxi Ltd. are mainly accountable for this breach of the Listing Rules.

In order to minimize the chance of breaching the Listing Rules by the Group in the future, the Company has adopted the following measures:

1. As preventive control, a letter has been issued by the Company to the general manager, deputy general manager and financial controller of subsidiaries of the Group to remind them to consult the financial controller and company secretary of the Company directly/indirectly for any possible transactions which may constitute notifiable transactions, connected transaction and/or other disclosures under the Listing Rules. In addition, they are urged to study

the previous training materials of the Listing Rules again and pay attention to the previous faxes/correspondence issued by the Company regarding compliance with the Listing Rules. Re-training of the Listing Rules will be given to the management who was involved in the granting of the existing guarantee so as to refresh their memory in due course.

2. In addition, the Board will, as soon as practicable and following further investigation and consideration of the Group's internal control needs, engage an appropriately experienced professional company to review and suggest ways to enhance the Group's overall internal control system.
3. As detective control, all subsidiaries of the Group are required to copy signed bank facilities agreement, guarantee agreement and asset pledge agreement to the Company for record unless waived by the Company.

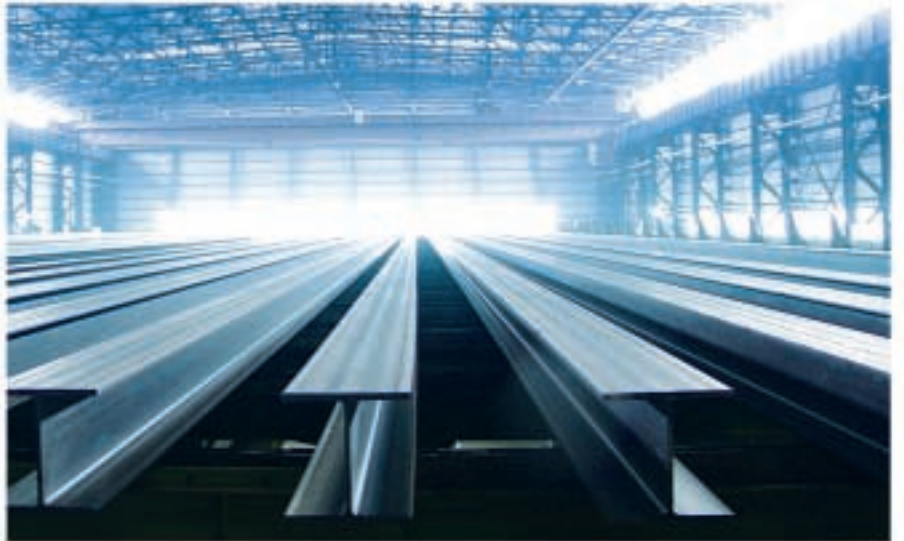
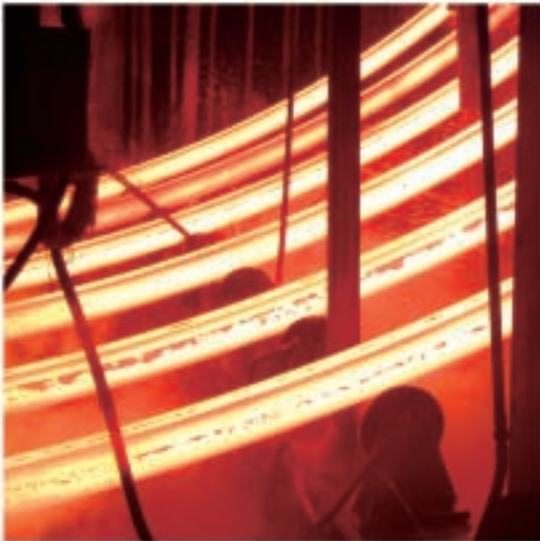
The Company has set up the internal audit department in October 2006 and it is expected that the internal audit department will further enhance and strengthen the internal control system of the Group.

On Behalf of the Board
China Oriental Group Company Limited

Han Jingyuan
Chairman and Chief Executive Officer

Hong Kong, 3 April 2007

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT



BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

DIRECTORS

Executive Directors

Han Jingyuan, 50, is the Chairman and Chief Executive Officer of the Company, and also serves as chairman of the board of Jinxi Limited and Foshan Jinxi. Mr. Han graduated from the People's University in 1994 with a degree in management. His experience in the steel industry began in 1984 when he was employed as a subdivision head of Han'erzhuang Iron Mine. In 1992, Mr. Han, then head of Han'erzhuang Iron Mine, joined Jinxi Iron Factory and served as a deputy head until 1997. In 1997, Mr. Han joined Tangshan Jinxi Group where he served as chairman of the board and general manager until 1999. Since Jinxi Limited was incorporated in December 1999, Mr. Han has been serving as the chairman of the board and general manager. In order to concentrate his effort on the future strategic development of the Group, Mr. Han resigned as general manager of Jinxi Limited in September 2004. Mr. Han has in-depth industry knowledge and 22 years of extensive operational and managerial experience in the iron and steel industry. In December 2003, Mr. Han was awarded the honorary title of "Top Ten Celebrities for China's Reform Programme in the New Century" (新世紀中國改革十大新聞人物) for 2003 by the Organising Committee for Nomination of Celebrities for China's Reform Programme (中國改革人物徵評活動組委會). Mr. Han is the director and the controlling shareholder of Wellbeing Holdings Limited, the controlling shareholder of the Group.

Chen Ningning, 36, the Vice Chairman of the Company, obtained a master of business administration in management from New York Institute of Technology in 1994. Before returning to Asia to work for Pioneer Group, Ms. Chen worked as a fund manager with a US financial group in New York. Currently, Ms. Chen is the controlling shareholder and director of Pioneer Iron & Steel Group Company Limited. Ms. Chen has extensive experience and strong relationships with many key players in the Chinese steel industry. Besides her role in our Group, Ms. Chen currently serves as a non-executive director and

vice-chairman of Inner Mongolia Baotou Rare Earth Hi-Technology Company Limited, a Shanghai-listed mining company. Ms. Chen is also a director in Jinxi Limited and serves in a non-executive capacity as director of a number of Chinese logistics and trading companies. Ms. Chen is the director and the controlling shareholder of Smart Triumph Corporation, a substantial shareholder of the Group.

Zhu Jun, 43, is an executive Director of the Company and also serves as an executive director



of the board and the general manager of Jinxi Limited. Mr. Zhu graduated in 2001 from a graduate programme of the Communist Party School in Hebei Province with a diploma in management. Prior to working in the steel industry, Mr. Zhu worked for 10 years as deputy director of Qianxi County Chemical Fertilizer Factory which was based in Qianxi County. Mr. Zhu joined Jinxi Iron Factory in 1992 and later served as deputy director. Mr. Zhu has had 13 years of working experience in the iron and steel industry. He has served as Jinxi Limited's deputy general manager since December 1999 and as general manager since September 2004. Mr. Zhu was appointed to Jinxi Limited's board of directors in June 2000.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

DIRECTORS *(Continued)*

Executive Directors *(Continued)*

Tang Chi Fai, 41, is an executive Director of the Company and a director in Jinxi Limited. Mr. Tang graduated from Hong Kong Polytechnic with a diploma in accounting. Mr. Tang is also a fellow member of the Chartered Association of Certified Accountants and Hong Kong Institute of Certified Public Accountants. Previously, Mr. Tang worked as audit manager in the Hong Kong office of an international accounting firm for nearly 6 years and as financial controller for a red chip company listed in Hong Kong for over 7 years. Mr. Tang joined PMC in September 2003 as chief financial officer. Mr. Tang has over 13 years of experience on corporate finance, accounting and auditing in both Hong Kong and the PRC. Mr. Tang tendered a letter of resignation to resign as Director of the Company and all other positions within the Group with effect from 13 April 2007.

Liu Lei, 51, is an executive Director and the deputy general manager of the Company and a director of Foshan Jinxi. Mr. Liu has over 19 years of experience in management and industrial fields. Mr. Liu graduated in the area of Industrial Electrical Automation of Electrical Engineering Faculty of 河北工學院 (Hebei Industrial Academy) in July 1978. Mr. Liu was awarded the title of 河北省有突出貢獻的中青年專業技術人才 (Professional Technological Talent With Outstanding Contribution in Hebei Province) by Government of Hebei Province in April 1987. Mr. Liu was also granted the qualification of research fellow by 河北省自然研究高級評委會 (Senior Appraisal Committee of Zi Ran Yan Jiu of Hebei Province) in December 2000. Before joining the Group in June 2004, Mr. Liu was the Vice Chancellor of 河北省科學院 (Science Bureau of Hebei Province) from October 1999 to June 2004.

Shen Xiaoling, 46, is an executive Director of the Company and also serves as an executive director and deputy general manager of Jinxi Limited. He obtained a diploma in management from the Hebei Provincial Communist Party School in 2001. Before joining the Group, Mr.

Shen was head of China Construction Bank Luanxian Sub-branch. Mr. Shen also had 5 years of experience acting as head of China Construction Bank Qianxi Sub-branch and more than 6 years of experience as the deputy head of Bank of China Qianxi Sub-branch. Mr. Shen has been deputy general manager of Jinxi Limited since January 2002.

Independent non-executive Directors

Gao Qingju, 70, is an independent non-executive Director. Mr. Gao, a senior engineer, has been employed by Beijing Lianxingfa Industrial & Technical Co., Ltd. since 2000 and currently serves as both its general manager and director of the board. After completing his study in metallurgical machinery and equipment at the Beijing College of Iron & Steel (北京鋼鐵工業學校) in 1958, Mr. Gao joined the Ministry of Metallurgical Industry and worked there for nearly 40 years, during which he was once appointed as the head of a sub-division of the ministry's production department. During his tenure with this ministry, Mr. Gao worked as a researcher on high-temperature alloys at a research institution in Beijing and completed an economics training programme at the Beijing Communist Party School in 1988. Before taking his current position with Beijing Lianxingfa Industrial & Technical Co., Ltd., Mr. Gao became the secretary-general of the Association of National Local Steel Enterprises, and continues to hold this position.

Yu Tung Ho, 60, is an independent non-executive Director. Mr. Yu, who currently serves as both a Director and Chief Operating Officer for Asia Television Co., Ltd., has been in broadcasting for more than 36 years. His experience includes acting as executive vice president of Phoenix Satellite Television in Hong Kong and serving as chairman of the 12th and 13th Hong Kong Advertising Industry Association. Mr. Yu has also served as the deputy general manager of China Broadcasting Television International Economic and Technology Company. In his 36 years of experience, Mr. Yu has also served as chief of the Guangdong Province Broadcasting Station.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

DIRECTORS *(Continued)*

Independent non-executive Directors *(Continued)*

Wong Man Chung, Francis, 42, is an independent non-executive Director. Mr. Wong is a Certified Public Accountant (Practising) and has over 19 years of experience in auditing, taxation, management and financial advisory. Mr. Wong is currently an independent non-executive director of Digital China Holdings Limited, Yardway Group Limited and Wai Kee Holdings Limited whose shares are listed on the Main Board of the Stock Exchange. He was once the independent non-executive director of Sys Solutions Holdings Limited, a company listed on the Growth Enterprise Market of the Stock Exchange. Mr. Wong is a director of Union Alpha C.P.A. Limited (which incorporated Francis Wong C.P.A. Co. Limited). Previously, Mr. Wong worked for an international accounting firm for 6 years and the Hong Kong Securities Clearing Company Limited for 2 years. Mr. Wong is a fellow member of Hong Kong Institute of Certified Public Accountants, Taxation Institute of Hong Kong and Association of Chartered Certified Accountant of the United Kingdom. Mr. Wong is also an associate member of Institute of Chartered Accountants in England and Wales and a member of the Society of Chinese Accountants & Auditors, Hong Kong. Mr. Wong holds a Master Degree in Management conferred by Guangzhou Jinan University.

SENIOR MANAGEMENT

During the year, the senior management of the Group includes the executive Directors of the Company.

Zhu Jun (as disclosed above)

Yu Jianshui, 39, is the general manager of Foshan Jinxi. Mr. Yu was a metallurgy graduate at Hebei Polytechnic University. He joined the Group after graduation until May 2005. He had been served as the plant manager of sintering plant and iron smelting plant. He has 15 years of management experience in production and technological improvement. During the period, he received the awards of County Technological Selected Talent (縣科技拔尖人才), Ten Outstanding Youths in the County (縣十大傑出青年), Outstanding Youth in Post of Tangshan City (唐山市青年崗位能手), Workers' Model in Hebei Province (河北省勞動模範), The First Class Honour of Technological Improvement in Tangshan City, The Third Class Honour of Technological Improvement in Hebei Province. He was employed as the deputy general executive manager of Shanxi Province Xiaoyi City Chengcai Iron and Steel Company in May 2005. He joined Foshan Jinxi in April 2006. Mr. Yu was appointed as executive Director of the Company with effect from 14 April 2007.

COMPANY SECRETARY AND QUALIFIED ACCOUNTANT

Lai Po Sing, 40, is the Financial Controller and Company Secretary of the Company. Mr. Lai graduated from the Chinese University of Hong Kong with a Bachelor Degree in Business Administration. He also holds a degree of Master of Business Administration from the University of Manchester in the UK. He is a Certified Public Accountant (Practising) in Hong Kong and a fellow member of both Hong Kong Institute of Certified Public Accountants and the Association of Chartered Certified Accountants. He is also an associate member of Institute of Chartered Accountants in England and Wales. He has over 16 years' experience in internal auditing, external auditing, taxation, finance and accounting.

DIRECTORS' REPORT

The directors (the "Director") of China Oriental Group Company Limited (the "Company") herein present their annual report and the audited financial statements of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 31 December 2006.

REORGANISATION AND BASIS OF PREPARATION

The Company was incorporated as an exempted company with limited liability on 3 November 2003 under the Companies Act 1981 of Bermuda. Pursuant to the reorganisation (the "Reorganisation"), as disclosed in the prospectus of the Company dated 18 February 2004 (the "Prospectus"), to rationalise the structure of the Group in preparation for the listing of the Company's shares on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), the Company became the holding company of the then companies comprising the Group on 20 January 2004. The basis of preparation of the audited financial statements are set out in Notes 1 and 2 to the consolidated financial statements.

Following completion of the Reorganisation and the global offerings, the Company's shares were listed on the Stock Exchange on 2 March 2004.

PRINCIPAL ACTIVITIES

As at 31 December 2006, the Company's principal activity is investment holding. The principal activity of the Group is the manufacture and sales of iron and steel products. The nature of the principal activity has not changed during the year.

SEGMENT INFORMATION

Over 90% of the Group's consolidated sales and contribution to results are derived from the PRC and mainly from the production and sales of iron and steel products for the year ended 31 December 2006 and are set out in Note 5 to the consolidated financial statements.

RESULTS AND DIVIDENDS

The Group's consolidated income statement for the year ended 31 December 2006 and its consolidated balance sheet as at that date, together with the balance sheet of the Company as at 31 December 2006, are set out in the financial statements on pages 33 to 36.

At a meeting held on 3 April 2007, the Directors proposed a final dividend of HK\$133,630,000 (approximately RMB132,150,000), representing HK4.6 cents per ordinary share to the shareholders of the Company whose names appear on the register of members of the Company on 22 May 2007. Subject to the approval of the Company's shareholders at the Company's forthcoming annual general meeting to be held on 22 May 2007, the final dividend will be paid on 12 June 2007.

SUMMARY OF FINANCIAL INFORMATION

A summary of the consolidated financial results and assets, liabilities and minority interest of the Group for the last five financial years, is set out on page 95.

PROPERTY, PLANT AND EQUIPMENT

Details of movements in the property, plant and equipment of the Group and the Company during the year are set out in Note 7 to the consolidated financial statements.

DIRECTORS' REPORT

SHARE CAPITAL

Details of the movements in the Company's issued share capital during the year are set out in Note 17 to the consolidated financial statements.

RESERVES

Details of the movements in the reserves of the Group during the year are set out in Note 18 to the consolidated financial statements.

DISTRIBUTABLE RESERVES

At 31 December 2006, the Company's accumulated losses amounted to RMB39,643,000 (2005: RMB8,319,000).

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Bye-laws or the Companies Act 1981 of Bermuda, which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

MAJOR CUSTOMERS AND SUPPLIERS

The sales attributable to the five largest customers of the Group accounted for less than 30% of the total Group's consolidated revenue for the year.

The purchases attributable to the five largest suppliers of the Group accounted for less than 30% of the total Group's consolidated purchases for the year.

DIRECTORS

The Directors during the year and up to the date of this report were as follows:

Executive Directors

Mr. Han Jingyuan
Ms. Chen Ningning
Mr. Zhu Jun
Mr. Tang Chi Fai
Mr. Liu Lei
Mr. Shen Xiaoling

Independent non-executive Directors

Mr. Gao Qingju
Mr. Yu Tung Ho
Mr. Wong Man Chung, Francis

In accordance with Bye-law 87(1) of the Company and the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules"), Messrs Zhu Jun and Wong Man Chung, Francis will retire by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Pursuant to 13.51(2) of the Listing Rules, the annual fee specified in each of Messrs Zhu Jun, and Wong Man Chung, Francis's existing service contracts are HK\$300,000 and HK\$300,000 respectively. The basis of determining the Director's fee was based on the mutual negotiation between the Directors with reference to the range of prevailing directors' fee for directors of listed companies in Hong Kong. Mr. Zhu Jun owns approximately 2.82% of shares in Wellbeing Holdings Limited ("Wellbeing Holdings"), a controlling shareholder of the Company. Save as disclosed in this annual report, Messrs Zhu Jun and Wong Man Chung, Francis do not have any relationships with any directors, senior management or substantial or controlling shareholders of the Company.

DIRECTORS' REPORT

DIRECTORS *(Continued)*

The Company has received, from each of the independent non-executive Directors, an annual confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Company considers all of the independent non-executive Directors are independent.

DIRECTORS' INTERESTS IN CONTRACTS

Save as the transactions as disclosed in Note 35 to the consolidated financial statements, no director had a material interest in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party during the year.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the Directors and senior management of the Company are set out on pages 17 to 20 of the annual report.

DIRECTORS' SERVICE CONTRACTS

Two of the executive Directors have service contracts with the Company for a fixed term of three years commencing from 13 November 2006. Mr. Zhu Jun (an executive Director) has a service contract with the Company for a fixed term of three years commencing from 23 December 2006. Mr. Tang Chi Fai (an executive Director) has a service contract with the Company for a fixed term of one year commencing from 23 December 2006. The remaining two executive Directors have service contracts with the Company for a fixed term of 2 years commencing from 29 September 2006 and 3 years commencing from 1 July 2005, respectively. Each of these contracts may be terminated by either party giving not less than three months' notice in writing.

Two of the independent non-executive Directors have service contracts for a period of one year commencing from 23 December 2006. Mr. Wong Man Chung, Francis (an independent non-executive Director) has a service contract for a period of one year commencing from 25 August 2006.

Mr. Han Jingyuan, Mr. Zhu Jun and Mr. Shen Xiaoling (executive directors of the Company and its subsidiary) have service contracts with the Company's subsidiary on 9 June 2003 for a fixed term of five years commencing from 9 June 2003 which are exempted under the Listing Rules. Actual amount of salary was not specified in the service contracts other than the clause which stated that after probation, the employees will be paid according to the salary of the post. The service contracts may be terminated by the Company's subsidiary by paying compensation equivalent to the unfulfilled contract's salary and one month's salary for each year of service completed.

Save as disclosed above, no Director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' REPORT

DIRECTORS' INTERESTS AND SHORT POSITIONS IN SECURITIES

At 31 December 2006, the interests and short positions of the Directors, chief executives and their associates of the Company in the shares, underlying shares and debentures of the Company or any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, were as follows:

Number of shares held and nature of interest in the Company:

	Corporate Interest	Percentage of the Company's issued share capital	Long/ Short Position
Mr. Han Jingyuan	1,282,480,849 (Note 1)	44.15%	Long
Ms. Chen Ningning	817,519,151 (Note 2)	28.14%	Long

Notes:

1. At 31 December 2006, Mr. Han Jingyuan beneficially owned 60.69% of the issued share

capital of Wellbeing Holdings and held 16.09% of the issued share capital of Wellbeing Holdings on trust for the benefit of certain employees of the subsidiary of the Company. Wellbeing Holdings beneficially owned 1,230,728,124 shares or 42.37% of the issued shares of the Company. He is also the beneficial owner of 100% of the issued share capital of Chingford Holdings Limited which beneficially owned 51,752,725 shares or 1.78% of the issued shares of the Company at 31 December 2006.

2. At 31 December 2006, Ms. Chen Ningning beneficially owned 100% of the issued capital of Pioneer Iron & Steel Group Company Limited which in turn owned 100% of the issued share capital of Smart Triumph Corporation ("Smart Triumph"). Smart Triumph owned 817,519,151 shares or 28.14% of the issued shares of the Company.

Save as disclosed above and in the section of "Equity-settled share option scheme" below, at 31 December 2006, none of the directors and chief executives and their associates had any interest and short positions in the shares, underlying shares and debentures of the Company or any associated corporation (within the meaning of Part XV of SFO) as recorded in the register required to be kept under Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

DIRECTORS' REPORT

EQUITY-SETTLED SHARE OPTION SCHEME

The Company has a share option scheme for all directors and any employees of any company in the Group or any entity in which any member of the Group holds an equity interest. The purpose of the share option scheme is to provide the above persons with the opportunity to acquire proprietary interests in the Company and to encourage the above persons 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 option period is to be determined and notified by the board of directors of the Company (the "Board") to each grantee at the time of making an offer which shall not expire later than ten years from the date of grant. There are no minimum periods for which an option granted must be held and/or minimum performance targets that must be reached before the option can be exercised in whole or in part, unless the Board otherwise determines.

The total number of shares of the Company issued and to be issued upon exercise of the options granted and to be granted to each of the above persons in any 12-month period must not exceed 1% of the shares of the Company in issue without the approval of the shareholder of the Company. Where any grant of options to a substantial shareholder or an independent non-executive Director of the Company, or any of their respective associates, would result in the shares issued and to be issued upon exercise of all options already granted and to be granted to such person in the 12-month period up to and including the date of such grant:

(i) representing in aggregate over 0.1% of the shares of the Company in issue; and

(ii) having an aggregate value, based on the closing price of the shares of the Company on the date of grant, in excess of HK\$5 million,

such grant of options shall be approved by shareholders of the Company.

Upon acceptance of the offer, HK\$1 should be paid by each of the above persons to the Company as consideration for the options granted.

The subscription price shall be such price determined by the Directors of the Company at its absolute discretion and shall be no less than the highest of: (a) the closing price of the shares of the Company on the date of grant; (b) the average closing price of the shares of the Company for the 5 business days immediately preceding the date of grant; and (c) the nominal value of a share on the date of grant.

The above share option scheme shall be valid and effective for a period of 10 years commencing on 23 June 2006 and ending on 22 June 2016 (both days inclusive).

At 31 December 2006 and 3 April 2007, the number of shares to be issued upon exercise of the options which had been granted and remained outstanding under the stock option scheme was 24,200,000, representing 0.8% of the issued share capital at those dates.

At 31 December 2006 and 3 April 2007, the number of shares available for issue under the scheme (excluding the above options which had been granted and remained outstanding) was 266,300,000 shares, representing 9.2% of the issued share capital at those dates.

DIRECTORS' REPORT

EQUITY-SETTLED SHARE OPTION SCHEME (Continued)

Details of the share options outstanding during the year were as follows:

	No. of options outstanding at 1 January 2006	No. of options granted during the year	Date of grant	Exercisable period	No. of options exercised/ cancelled/ lapsed during the year	No. of options outstanding at 31 December 2006	Exercise price per share HK\$	Closing price per share immediately before the date of grant HK\$
Mr. Han Jingyuan	—	2,800,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,800,000	1.76	1.74
Ms. Chen Ningning	—	2,600,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,600,000	1.76	1.74
Mr. Zhu Jun	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Tang Chi Fai	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Liu Lei	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Shen Xiaoling	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Yu Tung Ho	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Gao Qingju	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Mr. Wong Man Chung, Francis	—	2,400,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,400,000	1.76	1.74
Employee	—	2,000,000	30 June 2006	30 June 2006 to 29 June 2016	—	2,000,000	1.76	1.74

Note 1: All the above Directors' interests in share options are personal and in long position.

Note 2: All of the above share options granted on 30 June 2006 can be exercised immediately upon acceptance of the offer by the grantee and there were no vesting conditions/period.

DIRECTORS' REPORT

EQUITY-SETTLED SHARE OPTION SCHEME *(Continued)*

The fair value of share options granted on 30 June 2006 was HK\$16,266,974 (approximately RMB16,745,000) which was calculated by using the Binomial option pricing model. The Group recognized the above fair value as expenses during the year. The model inputs were the share price at grant date of HK\$1.76, exercise price of HK\$1.76, expected volatility of 43.0%, expected dividend yield of 3.68%, contractual life of 10 years, and an annual risk-free interest rate of 4.84%. To allow for the effects of early exercise, it was assumed that the grantee would exercise the share options when the share price of the Company was twice the exercise price (the "Early Exercise Multiple"). The expected volatility was determined by using the annualized standard deviation of the historical share price of the Company since its listing on 2 March 2004 and other comparable listed companies for the last five years. To consider the expected life of expiration, the Company made reference to both the employee turnover rate and the early exercise multiple. The employee turnover rate is based on the historical turnover record of Directors and senior management of the Company. As the Company's share listed on the Stock Exchange in Hong Kong since 2004, the Company cannot solely rely on the historical employee turnover rate due to its short track record period. Alternatively, the Company determined the expected life of expiration by applying the Early Exercise Multiple.

As the Binomial option pricing model requires the input of highly subjective assumptions, including the volatility of share prices, changes in subjective input assumptions can materially affect the fair value estimate.

The accounting policy for equity-settled share options is stated in note 2.20 to the consolidated financial statements.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Save as disclosed above, at no time during the year were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate granted to any Director or their respective spouses or children under 18 years of age, or were any such rights exercised by them; or were the Company or any of its holdings companies, fellow subsidiaries and subsidiaries a party to any arrangement to enable the Company's Directors, their respective spouses or children under 18 years of age to acquire such rights in any other body corporate.

CONTRACTS OF SIGNIFICANCE

Save as disclosed above and the transactions as disclosed in Note 35 to the consolidated financial statements, no controlling shareholder or any of its subsidiaries have any contract of significance with the Company or its subsidiary during the year.

DIRECTORS' REPORT

SUBSTANTIAL SHAREHOLDERS

At 31 December 2006, the interests or short positions of every person, other than a Director or chief executive of the Company, in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company under Section 336 of the SFO are as follows:

Name	Number of shares held	Percentage of the Company's issued share capital	Long/Short Position
Wellbeing Holdings	1,230,728,124	42.37%	Long
Pioneer Iron & Steel Group Company Limited	817,519,151 (Note 1)	28.14%	Long
Smart Triumph	817,519,151 (Note 1)	28.14%	Long

Note 1: At 31 December 2006, Ms. Chen Ningning beneficially owned 100% of the issued capital of Pioneer Iron & Steel Group Company Limited which in turn owned 100% of the issued share capital of Smart Triumph. Smart Triumph owned 817,519,151 shares or 28.14% of the issued shares of the Company.

Save as disclosed above, at 31 December 2006, no person, other than a Director or chief executive of the Company, had interests or short positions in the shares and underlying shares of the Company required to be kept in the register by the Company under Section 336 of the SFO.

RELATED PARTY AND CONNECTED TRANSACTIONS

Details of significant related party and connected transactions of the Group under the Listing Rules are set out as below and in note 35 to the consolidated financial statements.

The purchases of raw material by Foshan Jin Xi Jin Lan Cold Rolled Sheet Co., Ltd. ("Foshan Jinxi"), an indirect non-wholly owned subsidiary of the Company from Hebei Jinxi Iron and Steel Company Limited ("Jinxi Limited."), an indirect non-wholly owned subsidiary of the Company have constituted continuing connected transactions under the Listing Rules. The shareholders of the Company have approved the above continuing connected transactions and the related annual cap for a period of three years ending 31 December 2007 on 4 February 2005. During the year ended 31 December 2006, the purchase of raw material (excluding value-added tax) by Foshan Jinxi from Jinxi Limited amounted to approximately RMB105.2 million.

In the opinion of the independent non-executive Directors of the Company, the purchases of raw material by Foshan Jinxi from Jinxi Limited for the year ended 31 December 2006 were entered into:

- (i) in the ordinary and usual course of business of the Group;
- (ii) on normal commercial terms;
- (iii) in accordance with the relevant agreement governing such transactions on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; and

DIRECTORS' REPORT

RELATED PARTY AND CONNECTED TRANSACTIONS *(Continued)*

- (iv) within the relevant annual cap amounts as approved by the shareholders of the Company on 4 February 2005.

The board of Directors confirms that the auditors of the Company have confirmed the matters stated in Rule 14A.38 of the Listing Rules in connection with the above continuing connected transactions.

On 12 December 2005, the Company announces that it and Foshan Jin Lan will issue guarantees to a PRC financial institution to secure the loan obligation of Foshan Jinxi on a several basis and in proportion to their equity interest. The guarantee will expire when the loan obligation and other relevant interest and expenses under the loan contract are repaid fully. The loan facility granted by the PRC financial institution is RMB150 million with a period of 3 years. The maximum liability under the guarantee of the Company will be RMB90 million and the related outstanding interest and expenses (if any). The guarantee was approved by the shareholders of the Company and was issued on 19 January 2006.

On 12 December 2005, the Company announces that Accordpower Investments Limited, a wholly-owned subsidiary of the Company, will provide shareholder's advances of US\$18.5 million to Foshan Jinxi. The non-interest bearing advances are US\$11.3 million while the interest bearing advances are US\$7.2 million. The interest rate of the interest bearing advances are based on 90% of the standard RMB loan interest rate of five years issued by the People's Bank of China. The duration of the advances will be 5 years. The shareholder's advances agreements were approved by the shareholders of the Company and signed on 19 January 2006.

Jinxi Limited has issued a guarantee dated April 2006 to a PRC bank to secure the master bank facility of RMB150 million granted to Foshan Jinxi by a PRC bank. The master bank facility's period is from 30 May 2006 to 30 May 2007. The maximum liability under the guarantee of Jinxi Limited will be RMB150 million plus the related outstanding interest and expenses (if any). The obligations of Jinxi Limited under the guarantee in respect of each individual facility granted under the master bank facility will expire two years after the expiry date of each individual facility being granted under the master bank facility. Foshan Jinxi will pay a guarantee fee of RMB900,000 for the year ended 30 May 2007 (plus any accrued interest), which is equivalent to 0.6% of the amount under the guarantee. Due to oversight and inadvertent misunderstanding of the Listing Rules by some of the management of the Group involved in the issuance of the guarantee, Jinxi Limited's entry into the guarantee and the provision of the guarantee was not reported to the Company. As a result, the failures by the Company to notify the Stock Exchange and announce Jinxi Limited's entry into the guarantee and the provisions of the guarantee and to seek shareholders of the Company's approval as required under Chapter 14A of the Listing Rules constitutes a breach of Rule 14A.63 of the Listing Rules.

DIRECTORS' REPORT

RELATED PARTY AND CONNECTED TRANSACTIONS *(Continued)*

Each of the Directors is aware and understands that each has undertaken to the Stock Exchange that in exercising each of their powers and duties as a director, each of them would comply to the best of his or her ability (and to procure the Company to comply) with the Listing Rules. However, in view of the facts surrounding the provision of the guarantee and in particular, the fact the Directors (other than the two executive Directors involved in issuing the guarantee, being Mr. Han and Mr. Shen) were not aware of Jinxi Ltd. entering into the guarantee, after discussion amongst the members of the Board, the Board considers that Mr. Han and Mr. Shen, as executive Directors of the Company and also more importantly as the directors and in respect of Mr. Shen only, deputy general manager of Jinxi Ltd. are mainly accountable for this breach of the Listing Rules.

Mr. Zhou Weijie, is a director of Foshan Jinxi and Foshan Jin Lan Aluminium Co., Ltd. (a company which is controlled by Mr. Zhou Weijie) has 40% of the equity interest in Foshan Jinxi. Therefore, Foshan Jinxi is a connected person of the Group in accordance with the Listing Rules.

Save as disclosed above and in Note 36 (i) to the consolidated financial statements, there were no other transactions required to be disclosed as non-exempt connected transactions in accordance with the Listing Rules.

SUFFICIENCY OF PUBLIC FLOAT

The Company has maintained a sufficient public float throughout the year ended 31 December 2006.

PURCHASE, SALES OR REDEMPTION OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities during the years ended 31 December 2006 and 2005.

SUBSEQUENT EVENTS

Details of the significant post balance sheet events are set out in Note 36 to the consolidated financial statements.

AUDITORS

PricewaterhouseCoopers retired and a resolution for their reappointment as auditors of the Company will be proposed at the forthcoming annual general meeting.

On Behalf of the Board

China Oriental Group Company Limited

Han Jingyuan

Chairman and Chief Executive Officer

Hong Kong, 3 April 2007

INDEPENDENT AUDITOR'S REPORT



羅兵咸永道會計師事務所

PricewaterhouseCoopers
22nd Floor Prince's Building
Central, Hong Kong

Independent Auditor's Report **To the Shareholders of China Oriental Group Company Limited** *(incorporated in Bermuda with limited liability)*

We have audited the consolidated financial statements of China Oriental Group Company Limited (the "Company") and its subsidiaries (hereafter collectively referred to as the "Group") set out on pages 33 to 94, which comprise the consolidated and company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with Section 90 of the Companies Act 1981 of Bermuda and for no other purpose. We do not assume responsibility towards or accept liability to any person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

INDEPENDENT AUDITOR'S REPORT

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 3 April 2007

CONSOLIDATED BALANCE SHEET

As at 31 December 2006
(All amounts in Renminbi ("RMB") thousands unless otherwise stated)

	Note	As at 31 December 2006	2005
ASSETS			
Non-current assets			
Property, plant and equipment	7	4,675,308	4,236,071
Leasehold land and land use rights	6	78,092	79,569
Investment properties	8	20,428	20,911
Intangible assets	9	18,289	9,547
Investments in an associate	11	7,897	8,881
Deferred income tax assets	22	—	2,327
		4,800,014	4,357,306
Current assets			
Inventories	12	1,407,898	1,103,374
Trade receivables	13	998,828	714,184
Other current assets		2,591	2,524
Prepayments, deposits and other receivables	15	481,734	185,555
Financial assets at fair value through profit or loss	14	135	64,633
Restricted bank balances	16	95,262	1,015,416
Bank and cash balances	16	434,905	709,870
		3,421,353	3,795,556
Total assets		8,221,367	8,152,862
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Ordinary shares	17	309,340	309,340
Share premium	17	2,151,035	2,151,035
Other reserves	18	984,296	735,325
Retained earnings		2,034,456	1,397,752
		5,479,127	4,593,452
Minority interest		122,322	138,643
Total equity		5,601,449	4,732,095

CONSOLIDATED BALANCE SHEET (Continued)

As at 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

	Note	As at 31 December 2006	2005
LIABILITIES			
Non-current liabilities			
Borrowings	21	360,770	294,230
Long-term advances from customers		—	15,000
Deferred income tax liabilities	22	290	—
Amounts due to related parties	35(c)	55,529	—
		416,589	309,230
Current liabilities			
Trade payables	19	516,368	632,439
Accruals, advances from customers and other current liabilities	20	998,236	1,014,908
Amounts due to related parties	35(c)	56,674	64,400
Current income tax liabilities		58,225	53,862
Current portion of long-term advances from customers		—	10,000
Borrowings	21	573,230	1,335,900
Dividends payable		596	28
		2,203,329	3,111,537
Total liabilities		2,619,918	3,420,767
Total equity and liabilities		8,221,367	8,152,862
Net current assets		1,218,024	684,019
Total assets less current liabilities		6,018,038	5,041,325

Chen Ningning
Vice Chairman and Director

Liu Lei
Director

The notes on pages 39 to 94 are an integral part of this financial statement.

COMPANY BALANCE SHEET

As at 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

	Note	As at 31 December	
		2006	2005
ASSETS			
Non-current assets			
Property, plant and equipment	7	13,501	15,458
Investment properties	8	20,428	20,911
Investments in subsidiaries	10(a)	224,017	224,017
Loans to subsidiaries	10(b)	2,050,529	1,181,917
		2,308,475	1,442,303
Current assets			
Prepayments, deposits and other receivables	15	1,637	5,140
Financial assets at fair value through profit or loss	14	135	64,633
Amounts due from related parties		7,809	—
Restricted bank balances	16	47,962	887,722
Bank and cash balances	16	73,666	53,724
		131,209	1,011,219
Total assets		2,439,684	2,453,522
EQUITY			
Capital and reserves attributable to the Company's equity holders			
Share capital	17	2,460,375	2,460,375
Other reserves		16,745	—
Accumulated losses		(39,643)	(8,319)
Total equity		2,437,477	2,452,056
LIABILITIES			
Current liabilities			
Accruals and other current liabilities		1,810	1,438
Amounts due to related parties		345	—
Dividends payable		52	28
Total liabilities		2,207	1,466
Total equity and liabilities		2,439,684	2,453,522
Net current assets		129,002	1,009,753
Total assets less current liabilities		2,437,477	2,452,056

Chen Ningning
Vice Chairman and Director

Liu Lei
Director

The notes on pages 39 to 94 are an integral part of this financial statement.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

	Note	Year ended 31 December	
		2006	2005
Revenue	5	9,782,116	9,182,693
Cost of sales	25	(8,357,880)	(7,958,870)
Gross profit		1,424,236	1,223,823
Other income	24	4,149	4,286
Distribution costs	25	(13,084)	(6,954)
Administrative expenses	25	(170,443)	(152,036)
Other expenses	25	(10,620)	(3,262)
Other gains/(losses) — net	23	31,439	(47,749)
Operating profit		1,265,677	1,018,108
Finance income	27	18,930	62,596
Finance costs	27	(50,387)	(74,189)
Finance costs — net		(31,457)	(11,593)
Share of loss of an associate	11	(984)	(2,319)
Profit before income tax		1,233,236	1,004,196
Income tax expense	28	(210,886)	(157,081)
Profit for the year		1,022,350	847,115
Attributable to:			
Equity holders of the Company		1,032,754	846,585
Minority interest		(10,404)	530
		1,022,350	847,115
Earnings per share for profit attributable to equity holders of the Company during the year (expressed in RMB per share)			
— basic	30	RMB0.36	RMB0.29
— diluted	30	RMB0.36	Not applicable
Dividends	31	161,879	136,044

The notes on pages 39 to 94 are an integral part of these consolidated financial statements

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

	Note	Attributable to equity holders of the Company			Total	Minority interest	Total equity
		Share capital	Other reserves	Retained earnings			
Balance at 1 January 2005		2,460,375	559,183	865,782	3,885,340	115,524	4,000,864
Profit for the year		—	—	846,585	846,585	530	847,115
Profit appropriation to statutory reserves	18	—	172,084	(172,084)	—	—	—
Cash flow hedges:							
— Fair value loss in the year	18	—	(3,370)	—	(3,370)	—	(3,370)
— Transfer to property, plant and equipment	18	—	3,370	—	3,370	—	3,370
Dividends relating to 2004		—	—	(142,531)	(142,531)	(3,534)	(146,065)
Minority shareholder's injection		—	—	—	—	25,478	25,478
Liquidation of a subsidiary		—	—	—	—	(500)	(500)
Others	18	—	4,058	—	4,058	1,145	5,203
		—	176,142	531,970	708,112	23,119	731,231
Balance at 31 December 2005		<u>2,460,375</u>	<u>735,325</u>	<u>1,397,752</u>	<u>4,593,452</u>	<u>138,643</u>	<u>4,732,095</u>
Balance at 1 January 2006		<u>2,460,375</u>	<u>735,325</u>	<u>1,397,752</u>	<u>4,593,452</u>	<u>138,643</u>	<u>4,732,095</u>
Profit for the year		—	—	1,032,754	1,032,754	(10,404)	1,022,350
Profit appropriation to statutory reserves	18	—	230,276	(230,276)	—	—	—
Employee share options scheme:							
— Value of employee services	18	—	16,745	—	16,745	—	16,745
Dividends relating to 2005		—	—	(136,044)	(136,044)	(3,581)	(139,625)
Dividends relating to 2006		—	—	(29,730)	(29,730)	(2,353)	(32,083)
Acquisition from a minority shareholder		—	—	—	—	(40)	(40)
Others	18	—	1,950	—	1,950	57	2,007
		—	248,971	636,704	885,675	(16,321)	869,354
Balance at 31 December 2006		<u>2,460,375</u>	<u>984,296</u>	<u>2,034,456</u>	<u>5,479,127</u>	<u>122,322</u>	<u>5,601,449</u>

The notes on pages 39 to 94 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

	Note	Year ended 31 December	
		2006	2005
Cash flows from operating activities			
Cash generated from operations	32	480,570	624,480
Interest received		16,515	60,299
Dividends received from financial assets at fair value through profit or loss		1,061	3,728
Interest paid		(54,585)	(119,085)
Income tax paid		(203,906)	(243,799)
		239,655	325,623
Cash flows from investing activities			
Purchase of property, plant and equipment	32	(586,511)	(853,939)
Proceeds from disposal of property, plant and equipment	32	8,069	4,013
Decrease in loan receivables		—	50,000
Purchase of investment properties		—	(21,356)
Dividends received		—	3,522
Increase in investment in an associate		—	(2,800)
Acquisition of minority interest		(40)	—
		(578,482)	(820,560)
Net cash used in investing activities		(578,482)	(820,560)
Net cash used before financing activities		(338,827)	(494,937)
Cash flows from financing activities			
Proceeds from current borrowings		779,090	1,651,718
Proceeds from borrowings from related parties		31,000	13,000
Repayment of current borrowings		(1,515,990)	(1,900,818)
Repayment of borrowings from related parties		—	(20,704)
Proceeds from non-current borrowings		215,770	—
Repayment of non-current borrowings		(165,000)	(38,000)
Dividends paid		(165,751)	(146,266)
Capital injection by a minority shareholder		—	1,900
Liquidation of a subsidiary		—	(500)
Decrease in restricted bank balances pledged as security for current bank borrowings		887,722	471,279
		66,841	31,609
Net cash generated from financing activities		66,841	31,609
Net decrease in cash and cash equivalents		(271,986)	(463,328)
Effect of foreign exchange rate changes		(2,979)	(44,858)
Cash and cash equivalents, beginning of the year		709,870	1,218,056
Cash and cash equivalents, end of the year	16	434,905	709,870

The notes on pages 39 to 94 are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

1. GENERAL INFORMATION

China Oriental Group Company Limited (the "Company") was incorporated in Bermuda on 3 November 2003 as an exempted company with limited liability under the Companies Act 1981 of Bermuda as a result of a group reorganisation (the "Reorganisation").

The address of the Company's registered office is Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda.

Following the completion of the global offering, the Company's shares were listed on The Stock Exchange of Hong Kong Limited on 2 March 2004.

The Company together with its subsidiaries are hereinafter collectively referred to as the Group. The Group is mainly engaged in the manufacture and sales of iron and steel products. The Group has manufacturing plants in Hebei Province and Guangdong Province of the People's Republic of China (the "PRC") and sells mainly to customers located in the PRC.

These consolidated financial statements are presented in thousands of units of RMB, unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 3 April 2007.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards (the "HKFRS"). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

(a) *Standards, amendments and interpretations to standards effective in 2006*

- HKFRS 6, "Exploration for and evaluation of mineral resources", is mandatory for the Group's accounting periods beginning on or after 1 January 2006. HKFRS 1 Amendment — First-time Adoption of Hong Kong Financial Reporting Standards and HKFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources, is mandatory for the Group's accounting periods beginning on or after 1 January 2006.

HKFRS 6 permits an entity to develop an accounting policy for exploration and evaluation assets without specific consideration of certain requirements of HKAS 8. Amendments to HKFRS 1 exempt the requirement to present comparative information for HKFRS 6. The Group has reviewed related operation and identified no material exploration and evaluation assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

(a) **Standards, amendments and interpretations to standards effective in 2006** *(Continued)*

- HKAS 39 and HKFRS 4 (Amendment), Financial Guarantee Contracts, is mandatory for the Group's accounting periods beginning on or after 1 January 2006.

This amendment requires issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, to be initially recognised at their fair value, and subsequently measured at the higher of (a) the unamortised balance of the related fees received and deferred, and (b) the expenditure required to settle the commitment at the balance sheet date.

The Group has concluded that the amendment was relevant to the Group's operation. The impact of adopting the amendment is described in Note 2.27.

- Amendment to HKAS 21, Amendment "Net investment in a foreign operation", is mandatory for the Group's accounting periods beginning on or after 1 January 2006.

The amendment relates to intragroup loans that fund foreign operations, addressing concerns raised by constituents that the definition of a net investment was too restrictive and unclear in the previous version of the standards.

The Group has reviewed the amendment and concluded that the amendment was relevant to the Group's operation. The impact of adopting the amendment is described in Note 2.4.

- HK(IFRIC)-Int 4, "Determining whether an arrangement contains a lease", is mandatory for the Group's accounting periods beginning on or after 1 January 2006.

The Group has reviewed its contracts and believed that the Group did not have relevant arrangements that might be affected by this interpretation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

(b) Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following standards and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 May 2006 or later periods that the Group has not early adopted:

- HKFRS 7, "Financial instruments: Disclosures", effective for annual periods beginning on or after 1 January 2007. HKAS 1, "Amendments to capital disclosures", effective for annual periods beginning on or after 1 January 2007. The Group assessed the impact of HKFRS 7 and the amendment to HKAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and capital disclosures required by the amendment of HKAS 1. The Group will apply HKFRS 7 and the amendment to HKAS 1 from annual periods beginning 1 January 2007;
- HKFRS 8, "Operating segments", effective for annual periods beginning on or after 1 January 2009. This standard supersedes HKAS 14 Segment Reporting, under which segments were identified and reported on risk and return analysis. Items were reported on the accounting policies used for external reporting. Under HKFRS 8, segments are components of an entity regularly reviewed by an entity's chief operating decision-maker. Items are reported based on the internal reporting. Management is currently assessing the impact of HKFRS 8 on the Group's operations. The Group will apply HKFRS 8 with effect from 1 January 2009;
- HK(IFRIC)-Int 8, Scope of HKFRS 2 (effective for annual periods beginning on or after 1 May 2006). HK(IFRIC)-Int 8 requires consideration of transactions involving the issuance of equity instruments — where the identifiable consideration received is less than the fair value of the equity instruments issued — to establish whether or not they fall within the scope of HKFRS 2. The Group will apply HK(IFRIC)-Int 8 from 1 January 2007, but it is not expected to have any impact on the Group's consolidated financial statements;
- HK(IFRIC)-Int 9, Reassessment of embedded derivatives (effective for annual periods beginning on or after 1 June 2006). HK(IFRIC)-Int 9 requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. Management believes that this interpretation should not have a significant impact on the reassessment of embedded derivatives as the Group has already assessed whether embedded derivative should be separated using the principles that are consistent with HK(IFRIC)-Int 9;

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.1 Basis of preparation *(Continued)*

(b) Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group *(Continued)*

- HK(IFRIC)-Int 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). HK(IFRIC)-Int 10 prohibits the impairment losses recognised in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. The Group will apply HK(IFRIC)-Int 10 from 1 January 2007; and
- HK(IFRIC)-Int 11, HKFRS 2-Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007). It clarifies the application of share-based payment to certain share-based payment arrangements involving the entity's own equity instruments and to arrangements involving equity instruments of the entity's parent. The Group will apply HK(IFRIC)-Int 11 from 1 January 2008.

(c) Interpretations to existing standards that are not yet effective and not relevant for the Group's operations

The following interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 May 2006 or later periods but are not relevant for the Group's operations:

- HK(IFRIC)-Int 7, Applying the Restatement Approach under HKAS 29, Financial Reporting in Hyperinflationary Economies (effective from 1 March 2006); and
- HK(IFRIC)-Int 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008).

(d) Amendments and interpretations to standards effective in 2006 but not relevant for the Group's operations

The following amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Group's operations:

- HKAS 19 Amendment — Employee Benefits;
- HKAS 39 Amendment — Cash Flow Hedge Accounting of Forecast Intragroup Transactions;
- HKAS 39 Amendment — The fair value option;
- HK(IFRIC)-Int 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds; and
- HK(IFRIC)-Int 6, Liabilities arising from Participating in a Specific Market — Waste Electrical and Electronic Equipment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.2 Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiaries made up to 31 December.

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Except for those companies composing the Group upon the Reorganisation, which have been accounted for on the merger basis, the results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group except for those subsidiaries composing the Group upon the Reorganisation. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less provision for impairment losses (Note 2.9). The results of subsidiaries are accounted by the Company on the basis of dividends received and receivable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.2 Consolidation *(Continued)*

(b) Transactions with minority interest

The Group applies a policy of treating transactions with minority interest as transactions with parties external to the Group. Disposals to minority interest result in gains and losses for the Group that are recorded in the consolidated income statement. Purchases from minority interest result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

(c) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

2.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

2.4 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Renminbi, which is the functional and presentation currency of the Company and its subsidiaries.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.4 Foreign currency translation *(Continued)*

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges or qualifying net investment hedges.

(c) Net investment in foreign operation

The Company and some subsidiaries have some monetary item that is receivable for or payable to a foreign operation within the Group. An item for which settlement is neither planned nor likely to occur in the foreseeable future is, in substance, a part of the entity's net investment in that foreign operation. Such monetary items include long-term receivables or loans, which do not include trade receivables and trade payables.

Exchange differences arising on a monetary item that forms a part of the Group's net investment in a foreign operation is recognised in profit or loss in the separate financial statements of the reporting entity or the individual financial statements of the foreign operation, as appropriate. In the financial statements that include the foreign operation and the reporting entity (consolidated financial statements when the foreign operation is a subsidiary), such exchange differences, if appropriate, is recognised initially in a separate component of equity and recognised in profit or loss on disposal of the net investment.

2.5 Property, plant and equipment

Property plant and equipment, comprising buildings, machinery, furniture and fixtures, leasehold improvements and vehicles are stated at cost less accumulated depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged in the income statement during the financial period in which they are incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.5 Property, plant and equipment *(Continued)*

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate their costs or revalued amounts to their residual values over their estimated useful lives (*Note 4.1*), as follows:

	Estimated useful life
Buildings	10-20 years
Machinery	5-10 years
Furniture and fixtures	5-10 years
Vehicles	5-10 years
Leasehold improvements	2-5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (*Note 2.9*).

Gains and losses on disposals are determined by comparing proceeds with the carrying amount and are recognised within other gains/(losses) — net, in the income statement.

Construction-in-progress ("CIP") represents buildings, plant and machinery under construction or pending installation and is stated at cost less accumulated impairment losses, if any. Cost includes the costs of construction and acquisition. No provision for depreciation is made on CIP until such time as the relevant assets are completed and available for intended use. When the assets concerned are ready for their intended use, the costs are transferred to property, plant and equipment and depreciated in accordance with the policy as stated above.

2.6 Leasehold land and land use rights

All land in the PRC is state-owned or collectively-owned and no individual land ownership right exists. The Group acquired the right to use certain land. The premiums paid for such right are treated as prepayment for operating lease and recorded as leasehold land and land use rights, which are amortised over the lease periods using the straight-line method.

2.7 Investment properties

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies in the consolidated Group, is classified as investment property.

Investment property is measured initially at its cost, including related transaction costs.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.7 Investment properties *(Continued)*

After initial recognition, investment property is carried at depreciated cost less accumulated impairment.

Fair value is determined and disclosed based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are reviewed annually by the directors. Changes in fair values are not recognised in the income statement.

Depreciation of investment properties is calculated using the straight-line method to allocate cost to their residual value over their estimated useful lives of 20 years.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its carrying amount at the date of reclassification becomes its cost for accounting purposes. Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified and subsequently accounted for as investment property.

If an item of property, plant and equipment becomes an investment property because its use has changed, the transfer does not change the carrying amount of the property transferred, nor does it change the cost of that property for measurement or disclosure purposes.

2.8 Intangible assets

Intangible assets mainly comprised iron ore mining licenses purchased, which are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of licences over their estimated useful lives (3-5 years).

Intangible assets should be derecognised on disposal or when no future economic benefits are expected from its use or disposal.

The gain or loss arising from the derecognition of an intangible asset should be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It should be recognised in profit or loss when the asset is derecognised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.9 Impairment of investments in subsidiaries, associates and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation, and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.10 Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity financial assets, and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determine the classification of its financial assets at initial recognition.

(a) *Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Derivatives are also classified as held for trading unless they are designated as hedges. Assets in this category are classified as current assets.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets.

(c) *Held-to-maturity financial assets*

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. If the Group were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available-for-sale. Held to maturity financial assets are included in non-current assets, except for those with maturities less than 12 months from the balance sheet date; these are classified as current assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.10 Financial assets *(Continued)*

(d) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

During the years ended 31 December 2006 and 2005, the Group has no financial assets categorised as held-to-maturity or available-for-sale financial assets.

Regular purchases and sales of financial assets are recognised on the trade-date — the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are presented in the income statement within other (losses)/gains — net, in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognised in the income statement as part of other income when the Group's right to receive payment is established.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Impairment testing of trade receivables is described in Note 2.13.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.11 Derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designed as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either:

- (1) hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge);
- (2) hedges of a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedges); or
- (3) hedges of net investments in foreign operations (net investment hedge).

A hedge of the foreign currency risk of a firm commitment is accounted for either as a cash flow hedge or as a fair value hedge.

The Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Except for the cash flow hedge disclosed in Note 18, the Group has no other hedging activities during the years ended 31 December 2006 and 2005. The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedge item is more than 12 months, and as a current asset or liability, if the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as a current asset or liability.

(a) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement within other gains/(losses) — net.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.11 Derivative financial instruments and hedging activities *(Continued)*

(a) Cash flow hedge *(Continued)*

Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item affects profit or loss (for example, when the forecast sale that is hedged takes place). The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognised in the income statement within finance costs. The gain or loss relating to the effective portion of forward foreign exchange contracts hedging export sales is recognised in the income statement within sales. The gain or loss relating to the ineffective portion is recognised in the income statement within other gains/(losses) — net. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory or fixed assets), the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognised in cost of goods sold in case of inventory, or in depreciation in case of fixed assets.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement within other gains/(losses) — net.

(b) Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting and are accounted for at fair value through profit or loss. Changes in the fair value of these derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement within other gains/(losses) — net.

2.12 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method. The cost of finished goods and work in progress comprises design costs, raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.13 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within selling and marketing costs. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against selling and marketing costs in the income statement.

2.14 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

2.15 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.16 Trade and other payables

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.17 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings at nil or low interest rates from government are regarded as government assistant and recognised initially at the cost of consideration received.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.18 Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

2.19 Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of any qualifying asset that necessarily takes a substantial period of time to get ready for its intended use or sales are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the income statement in the period in which they are incurred.

2.20 Employee benefits

(a) Pension obligations

The Group has arranged for its Hong Kong employees to join the Mandatory Provident Fund Scheme (the "MPF Scheme"). Under the MPF Scheme, the Group and its Hong Kong employees make monthly contributions to the scheme at 5% of the employees' earnings as defined under the Mandatory Provident Fund legislation, subject to a cap of Hong Kong dollar 1,000 per person per month and any excess contributions are voluntary.

In accordance with the rules and regulations in the PRC, the Group has arranged for its PRC employees to join a defined contribution retirement benefit plan organised by PRC government. The PRC government undertakes to assume the retirement benefit obligations of all existing and future retired employees payable under the plan as set out in Note 26. The assets of this plan are held separately from those of the Group in an independent fund managed by the PRC government.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.20 Employee benefits *(Continued)*

(a) Pension obligations (Continued)

The Group's contributions to the defined contribution retirement benefit plan are charged to the income statement as incurred.

(b) Share-based compensation

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

2.21 Provisions

Provisions for environmental restoration, restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

2.22 Government grants

A government grant in the form of subsidy or financial refund is recognised when there is a reasonable assurance that the Group will comply with the conditions attached to the grant and that the grant will be received.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.22 Government grants *(Continued)*

Grants relating to income are deferred and recognised in the income statement over the period necessary to match them with the costs they are intended to compensate.

Grants relating to the purchase of property, plant and equipment are included in non-current liabilities and recognised in the income statement over the life of a depreciable asset by way of a reduced depreciation charge.

2.23 Revenue recognition

(a) *Sales of goods produced*

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

(b) *Interest income*

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

(c) *Dividend income*

Dividend income is recognised when the right to receive payment is established.

(d) *Rental income*

Rental income is recognised on an accruals basis in accordance with the substance of the relevant agreements.

2.24 Operating leases as a lessee

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged in the income statement on a straight-line basis over the period of the lease.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

2.25 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably. A contingent liability is not recognised but is disclosed in the notes to the consolidated accounts. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group. Contingent assets are not recognised but are disclosed in the notes to the consolidated accounts when an inflow of economic benefits is probable. When inflow is virtually certain, an asset is recognised.

2.26 Dividends distribution

Dividends distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

2.27 Financial guarantee liabilities

Financial guarantee liabilities are recognised in respect of the financial guarantee contract issued by the Group to the contract holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Financial guarantee liabilities are recognised initially at fair value plus transaction costs that are directly attributable to the issue of the financial guarantee contract. After initial recognition, such contracts are measured at the higher of the present value of the best estimate of the expenditure required to settle the present obligation and the amount initially recognised less cumulative amortisation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

3. FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: interest rate risk, credit risk, liquidity risk and foreign exchange risk. The Group's overall risk management program focuses on the unpredictability of financial market and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain foreign exchange risk.

(a) *Interest rate risk*

The Group's income and operating cash flows are substantially independent of changes in market interest rates as the Group has no significant interest-bearing assets. The Group's exposure to changes in interest rates is mainly attributable to its non-current borrowings. Non-current borrowings at variable rates expose the Group to cash flow interest-rate risk. Details of the Group's borrowings have been disclosed in Note 21.

The Group has not used any interest rate swaps to hedge its exposure to interest rate risk.

(b) *Credit risk*

The Group has no significant concentrations of credit risk. The carrying amounts of bank and cash balances, trade receivables, and other receivables represent the Group's maximum exposure to credit risk in relation to financial assets. The Group's credit policy for the sales of products is mainly delivery either on cash or upon receipt of bank acceptance notes with maturity dates within six months.

(c) *Liquidity risk*

The liquidity risk of the Group is controlled by maintaining sufficient cash and cash equivalents, together with adequate banking facilities.

(d) *Foreign exchange risk*

The Group mainly operates in the PRC with most of the transactions denominated and settled in RMB. However, the Group has certain bank deposits and financial assets that are denominated in foreign currencies, mainly United States Dollars (the "US\$"), Euros and Hong Kong Dollars (the "HK\$"), which are exposed to foreign currency translation risk. Details of the Group's bank and cash balances are disclosed in Note 16.

Payables for certain equipment imported by the Group were denominated in Euro. During the year ended 31 December 2006 the Group has not used any foreign exchange rate swaps to hedge its exposure to foreign exchange risk.

3.2 Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

3. FINANCIAL RISK MANAGEMENT *(Continued)*

3.2 Fair value estimation *(Continued)*

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date.

The nominal value less impairment provision of trade and other receivables and payables approximates their fair values.

The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experiences and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 Critical accounting estimates and assumptions

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal to the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) *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 the current market condition as at the balance sheet date and the historical experience of manufacturing and selling products of similar nature.

(b) *Impairment of property, plant and equipment*

The Group reviews property, plant and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, in accordance with the accounting policy stated in Note 2.9. The recoverable amount of cash-generating unit has been determined based on higher of value-in-use and fair value less costs to sell.

The Group determined that there was an impairment indication relating to a production line of a subsidiary which manufactures galvanised and cold rolled sheets. This production line was identified as a cash-generating unit.

The Group measured the value in use and fair value less costs to sell by discounting the future estimated cash flow deriving from the production line. These calculations required the Group to estimate the expected future cash flows from the cash-generating unit and also to apply a suitable discount rate in order to calculate the present value of those cash flows.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

4.1 Critical accounting estimates and assumptions (Continued)

(b) Impairment of property, plant and equipment (Continued)

As at 31 December 2006, the value in use and fair value less costs of sell approximated to RMB245.3 million and RMB240.4 million respectively. The Group considered that the recoverable amount was the higher of value in use and fair value less costs of sell. The recoverable amount of the production line was lower than its carrying amount by RMB41.9 million approximately (Note 7).

If the estimated gross margin in all forecast years had been 10% lower or higher than the management's estimates at 31 December 2006 (for example, 18% or 22% instead of 20%), the Group would have recognised the impairment as follows:

	2006	
	10% Lower	10% Higher
Impairment of property, plant and equipment	<u>75,956</u>	<u>—</u>

If the estimated pre-tax discount rate applied to the discounted cash flows had been 10% (for example, 9% or 11% instead of 10%) lower or higher than management's estimates, the Group would have recognised the impairment as follows:

	2006	
	10% Lower	10% Higher
Impairment of property, plant and equipment	<u>10,065</u>	<u>59,097</u>

(c) Useful life of the property, plant and equipment

Useful life is the period over which an asset is expected to be available for use by an entity. The depreciable amount of an asset is allocated on a systematic basis over its useful life (Note 2.5).

The following factors are considered in determining the useful life of an asset:

- (i) Expected usage of the asset
- (ii) Expected physical wear and tear
- (iii) Technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset
- (iv) Legal or similar limits on the use of the asset,

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS *(Continued)*

4.1 Critical accounting estimates and assumptions *(Continued)*

(c) Useful life of the property, plant and equipment *(Continued)*

The useful life of an asset is reviewed at each financial year-end and, if expectations differ from previous estimates, the change will be accounted for as a change in an accounting estimate in accordance with HKAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

4.2 Critical judgements in applying the entity's accounting policies

(a) Borrowing costs eligible for capitalisation

The borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made. It may be difficult to identify a direct relationship between particular borrowings and a qualifying asset and to determine the borrowings that could otherwise have been avoided. Such a difficulty occurs, for example, when the financing activity of an entity is co-ordinated centrally. As a result, the determination of the amount of borrowing costs that are directly attributable to the acquisition of a qualifying asset is difficult and the exercise of judgement is required.

Borrowing costs capitalised into property, plant and equipment are shown in Note 7.

(b) Distinction between investment properties and owner-occupied properties

The Group determines whether a property qualifies as investment property. In making its judgement, the Group considers whether the property generates cash flows largely independently of the other assets held by the Group. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for administrative purposes. If these portions can be sold separately, the Group accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for administrative purposes. Judgement is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Group considers each property separately in making its judgement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

5. SALES AND SEGMENT INFORMATION — GROUP

(a) Sales

The Group is principally engaged in the manufacture and sales of iron and steel products. Sales recognised for the years ended 31 December 2006 and 2005 were as follows:

	2006	2005
Sales:		
Gross sales, less discounts and returns		
— billets	2,752,589	3,631,593
— strips and strip products	5,723,391	5,389,347
— H section steel products	728,933	—
— galvanised sheets	381,209	—
— cold rolled sheets	160,332	117,159
— others	35,662	44,594
	9,782,116	9,182,693

(b) Segment information

No business segment information is presented as over 90% of the Group's sales and operating profit are earned from the sales of iron and steel products.

No geographical segment information is presented as over 90% of the Group's sales and operating profit are earned within the PRC and over 90% operating assets of the Group are located in the PRC, which is considered as one geographic location with similar risks and returns.

6. LEASEHOLD LAND AND LAND USE RIGHTS — GROUP

The Group's interests in leasehold land and land use rights represent the prepaid operating lease payments and their net book value are analysed as follows:

	2006	2005
Opening	79,569	55,239
Additions	—	25,644
Amortisation of prepaid operating lease payment (Note 25, 32)	(1,477)	(1,314)
	78,092	79,569

As at 31 December 2006, the net book value of leasehold land and land use rights pledged as security for the Group's borrowings amounted to approximately RMB65 million (2005: RMB67 million) (Note 21).

The Group's leasehold land and land use rights are located in the PRC and the remaining lease period is between 46 years to 49 years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

7. PROPERTY, PLANT AND EQUIPMENT

The Group

	Buildings	Machinery	Furniture and fixtures	Vehicles	Leasehold improve- ments	CIP	Total
At 1 January 2005							
Cost	749,256	1,555,561	13,702	35,506	577	402,711	2,757,313
Accumulated depreciation	(91,280)	(300,807)	(4,759)	(11,138)	(261)	—	(408,245)
Net book amount	<u>657,976</u>	<u>1,254,754</u>	<u>8,943</u>	<u>24,368</u>	<u>316</u>	<u>402,711</u>	<u>2,349,068</u>
Year ended 31 December 2005							
Opening net book amount	657,976	1,254,754	8,943	24,368	316	402,711	2,349,068
Additions	51,414	17,578	10,504	10,612	760	2,044,372	2,135,240
Transfers	166,513	688,162	8,354	302	—	(863,331)	—
Transfer to CIP for repairment	(7,710)	(2,159)	—	—	—	9,869	—
Disposals (Note 32)	(17,155)	(18,602)	(4,537)	(209)	—	—	(40,503)
Depreciation (Note 25, 32)	(37,250)	(158,698)	(4,962)	(6,473)	(351)	—	(207,734)
Closing net book amount	<u>813,788</u>	<u>1,781,035</u>	<u>18,302</u>	<u>28,600</u>	<u>725</u>	<u>1,593,621</u>	<u>4,236,071</u>
At 31 December 2005							
Cost	929,675	2,194,045	22,945	43,460	1,337	1,593,621	4,785,083
Accumulated depreciation	(115,887)	(413,010)	(4,643)	(14,860)	(612)	—	(549,012)
Net book amount	<u>813,788</u>	<u>1,781,035</u>	<u>18,302</u>	<u>28,600</u>	<u>725</u>	<u>1,593,621</u>	<u>4,236,071</u>
Year ended 31 December 2006							
Opening net book amount	813,788	1,781,035	18,302	28,600	725	1,593,621	4,236,071
Additions	9,543	15,995	2,952	7,308	—	787,387	823,185
Transfers	411,025	1,733,268	2,413	25	—	(2,146,731)	—
Disposals (Note 32)	(2,688)	(12,415)	(209)	(86)	—	—	(15,398)
Depreciation (Note 25, 32)	(49,772)	(265,923)	(3,157)	(7,668)	(171)	—	(326,691)
Impairment (Note 25, 32)	(9,060)	(32,150)	(450)	(199)	—	—	(41,859)
Closing net book amount	<u>1,172,836</u>	<u>3,219,810</u>	<u>19,851</u>	<u>27,980</u>	<u>554</u>	<u>234,277</u>	<u>4,675,308</u>
At 31 December 2006							
Cost	1,346,713	3,924,966	28,063	50,121	1,337	234,277	5,585,477
Accumulated depreciation and impairment	(173,877)	(705,156)	(8,212)	(22,141)	(783)	—	(910,169)
Net book amount	<u>1,172,836</u>	<u>3,219,810</u>	<u>19,851</u>	<u>27,980</u>	<u>554</u>	<u>234,277</u>	<u>4,675,308</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

7. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Group *(Continued)*

Depreciation expenses have been charged to the consolidated income statements as follows:

	2006	2005
Cost of sales	318,204	199,647
Administrative expenses	8,487	8,087
	326,691	207,734

- (a) As at 31 December 2006, the net book value of buildings and machinery pledged as security for the Group's current and non-current borrowings amounted to approximately RMB1,088 million (2005: RMB568 million) (*Note 21*).

During the year ended 31 December 2006, borrowing costs amounting to approximately RMB6 million were capitalised into the cost of property, plant and equipment (2005: approximately RMB25 million) at an average capitalisation rate of 5% approximately.

- (b) As at 31 December 2006, the Directors considered that certain production line in relation to production of galvanised and cold rolled sheets belonging to a subsidiary was carried at more than its recoverable amount (*Note 4.1*).

Impairment of the Group's property, plant and equipment has been charged to the consolidated income statement as follow:

	2006	2005
Cost of sales	41,859	—

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

7. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The Company

	Buildings	Furniture and fixtures	Vehicles	Leasehold improve- ments	Total
At 1 January 2005					
Cost	—	374	1,468	577	2,419
Accumulated depreciation	—	(65)	(245)	(261)	(571)
Net book amount	—	309	1,223	316	1,848
Year ended 31 December 2005					
Opening net book amount	—	309	1,223	316	1,848
Additions	12,399	303	1,189	760	14,651
Disposals	—	—	—	—	—
Depreciation	(258)	(91)	(341)	(351)	(1,041)
Closing net book amount	12,141	521	2,071	725	15,458
At 31 December 2005					
Cost	12,399	677	2,657	1,337	17,070
Accumulated depreciation	(258)	(156)	(586)	(612)	(1,612)
Net book amount	12,141	521	2,071	725	15,458
Year ended 31 December 2006					
Opening net book amount	12,141	521	2,071	725	15,458
Additions	365	2	46	—	413
Disposals	—	—	(1,082)	—	(1,082)
Depreciation	(646)	(130)	(341)	(171)	(1,288)
Closing net book amount	11,860	393	694	554	13,501
At 31 December 2006					
Cost	12,764	679	1,513	1,337	16,293
Accumulated depreciation	(904)	(286)	(819)	(783)	(2,792)
Net book amount	11,860	393	694	554	13,501

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

8. INVESTMENT PROPERTIES — GROUP AND COMPANY

The investment properties are located in the PRC and their net book value are analysed as follows:

At 1 January 2005

Cost	—
Accumulated depreciation	—
	<hr/>
Net book amount	—
	<hr/> <hr/>

Year ended 31 December 2005

Opening net book amount	—
Additions	21,356
Depreciation (Note 25, 32)	(445)
	<hr/>
Closing net book amount	20,911
	<hr/>

At 31 December 2005

Cost	21,356
Accumulated depreciation	(445)
	<hr/>
Net book amount	20,911
	<hr/> <hr/>

Year ended 31 December 2006

Opening net book amount	20,911
Additions	629
Depreciation (Note 25, 32)	(1,112)
	<hr/>
Closing net book amount	20,428
	<hr/>

At 31 December 2006

Cost	21,985
Accumulated depreciation	(1,557)
	<hr/>
Net book amount	20,428
	<hr/> <hr/>

During the year ended 31 December 2006, the rental income arising from investment properties approximately amounted to RMB1.26 million (2005: RMB0.14 million) (Note 24).

As at 31 December 2006, the Directors of the Company assessed the fair value of the investment properties to be approximately RMB25.8 million based on the prices in an active market (2005: RMB22.5 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

9. INTANGIBLE ASSETS — GROUP

	Iron ore mining licenses
At 1 January 2005	
Cost	—
Accumulated amortisation	—
Net book amount	<u>—</u>
Year ended 31 December 2005	
Opening net book amount	—
Additions	10,229
Amortisation charge (<i>Note 25, 32</i>)	(682)
Closing net book amount	<u>9,547</u>
At 31 December 2005	
Cost	10,229
Accumulated amortisation	(682)
Net book amount	<u>9,547</u>
Year ended 31 December 2006	
Opening net book amount	9,547
Additions	36,822
Deduction	(24,498)
Amortisation charge (<i>Note 25, 32</i>)	(3,582)
Closing net book amount	<u>18,289</u>
At 31 December 2006	
Cost	22,418
Accumulated amortisation	(4,129)
Net book amount	<u>18,289</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

10. INVESTMENTS IN AND LOANS TO SUBSIDIARIES — COMPANY

(a) Investments in subsidiaries

	2006	2005
Unlisted investments, at cost	224,017	224,017

The particular subsidiaries at 31 December 2006 and 2005 were as follows:

Name	Place and date of incorporation	Legal status	Percentage of equity interest attributable to the Group	Issued and fully paid capital	Authorised capital	Principal activities
Gold Genesis Development Limited ("Gold Genesis")	British Virgin Islands ("BVI") 21 February 2003	Limited liability company	100% (Directly held)	US\$1	US\$50,000	Investment holding
Good Lucky Enterprises Limited ("Good Lucky")	BVI 21 February 2003	Limited liability company	100% (Directly held)	US\$1	US\$50,000	Investment holding
First Glory Services Limited ("First Glory")	BVI 16 October 2003	Limited liability company	100% (Directly held)	US\$2	US\$50,000	Investment holding
Accordpower Investments Limited ("Accordpower")	BVI 30 November 2004	Limited liability company	100% (Directly held)	US\$2	US\$50,000	Investment holding
Fullhero Investments Limited	BVI 3 May 2005	Limited liability company	100% (Directly held)	US\$2	US\$50,000	Investment holding
Hebei Jinxi Iron and Steel Company Limited ("Jinxi Limited")	PRC 24 December 1999	Joint stock company with limited liability	97.6% (Indirectly held)	RMB 228,635,573	RMB 228,635,573	Manufacture and sales of iron and steel products
Foshan Jin Xi Jin Lan Cold Rolled Sheet Company Limited ("Foshan Jinxi")	PRC 26 December 2003	Limited liability company	60% (Indirectly held)	US\$ 29,800,000	US\$ 29,800,000	Manufacture and sales of steel products
Jinxing Charging Company Limited ("Jinxing Charging")	PRC 2 August 2005	Limited liability company	62% (Indirectly held)	RMB 5,000,000	RMB 5,000,000	Manufacture and sales of lime products
Oriental Fullhero Leasing (Shenzhen) Co., Ltd ("Shenzhen Leasing")	PRC 23 September 2005	Limited liability company	100% (Indirectly held)	US\$ 65,000,000	US\$ 65,000,000	Leasing and financial leasing
Tangshan Jinxi Mining Company Limited ("Jinxi Mining") (i)	PRC 20 December 2004	Limited liability company	100% (Indirectly held)	RMB 2,000,000	RMB 2,000,000	Management service for mining rights

(i) Jinxi Limited entered into an equity acquisition agreement with Mr. Wang Shujun on 5 September 2006 to acquire 2% equity shares of Jinxi Mining held by Mr. Wang Shujun. The total consideration is RMB0.04 million in the form of cash. With completion of the transaction, Jinxi Mining has been a wholly owned subsidiary of Jinxi Limited.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

10. INVESTMENTS IN AND LOANS TO SUBSIDIARIES — COMPANY *(Continued)*

(b) Loans to subsidiaries

Loans to subsidiaries forms a part of the Company's net investment in foreign subsidiaries.

The loans to Jinxi Limited amounting to approximately US\$106.7 million (RMB833.2 million equivalent), are unsecured, interest-free and with a repayment term of 20 years.

Except for the loans to Jinxi Limited as disclosed above, the loans to subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

11. INVESTMENTS IN AN ASSOCIATE — GROUP

	2006	2005
Beginning of the year	8,881	12,474
Share of loss <i>(Note 32)</i>	(984)	(2,319)
Dividends	—	(4,074)
Capital injection to the associate	—	2,800
End of the year	7,897	8,881

The information of the unlisted associated company is as follows:

Name	Place and date of incorporation	Percentage of equity interest attributable to the Group	Assets	Liabilities	Revenues	Net loss
Qianxi County Zhongxing Iron Mine Co., Ltd. ("Zhongxing Iron Mine")	PRC 21 May 2002	35% (indirectly held)	36,083	13,885	64,272	(2,810)

12. INVENTORIES — GROUP

	2006	2005
Raw materials and materials in-transit	1,048,220	894,832
Work-in-progress	193,053	122,459
Finished goods	166,625	86,083
	1,407,898	1,103,374

As at 31 December 2006, the net book value of inventories pledged as security for the Group's notes payable and current borrowings amounted to approximately RMB69 million *(Note 19 and 21)*.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

12. INVENTORIES — GROUP *(Continued)*

As at 31 December 2005, the net book value of inventories pledged as security for the Group's notes payable amounted to approximately RMB32 million (*Note 19*).

The cost of inventories recognised as expense and included in cost of sales and administrative expenses amounted to RMB7,312 million and 6 million respectively (2005: RMB7,069 million and 7 million respectively) (*Note 25*).

13. TRADE RECEIVABLES — GROUP

	2006	2005
Accounts receivable	34,795	23,369
Notes receivable (a)	964,033	690,815
	998,828	714,184

(a) As at 31 December 2006 and 2005, notes receivable were all bank acceptance notes, approximately of which:

- (i) RMB10 million was pledged as security for issuing notes payable (2005: RMB67 million) (*Note 19*);
- (ii) RMB51 million was pledged as security in favour of a third party for issuing letters of credit (2005: RMB248 million) (*Note 33*);
- (iii) RMB29 million was pledged as security for the Group's current borrowings (2005: nil) (*Note 21*);
- (iv) RMB135 million was pledged as security for issuing letters of credit (2005: nil).

As at 31 December 2006 and 2005, the carrying amount of the Group's trade receivables approximated their fair value.

As at 31 December 2006 and 2005, the ageing analysis of trade receivables was as follows:

	2006	2005
Within 3 months	998,828	714,184

The credit policy usually adopted by the Group for the sales of products to customers is to deliver goods either upon receipt in cash or upon receipt of bank acceptance notes with maturity dates within six months.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

14. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS — GROUP AND COMPANY

	2006	2005
Liquid Reserve Fund — Euro, quoted	130	52,479
Liquid Reserve Fund — US dollars, quoted	5	12,154
	<u>135</u>	<u>64,633</u>

The above financial assets were acquired principally for the purpose of selling in the short term.

15. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

The Group

	2006	2005
Prepayments	441,044	107,899
Deposits and other receivables	40,690	77,656
	<u>481,734</u>	<u>185,555</u>

The Company

	2006	2005
Prepayments	310	801
Deposits and other receivables	1,327	4,339
	<u>1,637</u>	<u>5,140</u>

16. BANK AND CASH BALANCES AND RESTRICTED BANK BALANCES

The Group

	2006	2005
Bank and cash balances	434,905	709,870
Restricted bank balances	95,262	1,015,416
	<u>530,167</u>	<u>1,725,286</u>

As at 31 December 2006, the restricted bank balances were composed of the following items:

- The restricted bank balances amounting to approximately RMB41 million were pledged as security for issuing notes payable of the Group (2005: RMB128 million) (Note 19).
- The restricted bank balances of a subsidiary amounting to approximately RMB6 million were pledged as security for issuing notes payable to a fellow subsidiary (2005: nil).
- The restricted bank balances amounting to approximately US\$6 million (RMB48 million equivalent) were pledged as security for issuing letters of credit (2005: nil).

As at 31 December 2005, restricted bank balances, amounting to approximately US\$110 million (RMB888 million equivalent) were pledged as security for current borrowings of the Group (Note 21).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

16. BANK AND CASH BALANCES AND RESTRICTED BANK BALANCES *(Continued)*

The Group *(Continued)*

The carrying amounts of the bank and cash balances and restricted bank balances are denominated in the following currencies:

	2006	2005
RMB	402,482	499,004
US dollar	125,778	1,224,787
Hong Kong dollar	1,900	1,493
Euro	7	2
	530,167	1,725,286

The Company

	2006	2005
Bank and cash balances	73,666	53,724
Restricted bank balances	47,962	887,722
	121,628	941,446

As at 31 December 2006, restricted bank balances amounting to approximately US\$6 million (RMB48 million equivalent) (2005: nil) were pledged as security for issuing letters of credit.

As at 31 December 2005, restricted bank balances amounting to approximately US\$110 million (RMB888 million equivalent) were pledged as security for current borrowings of the Group *(Note 21)*.

The carrying amounts of the bank and cash balances and restricted bank balances are denominated in the following currencies:

	2006	2005
US dollar	118,975	935,129
Hong Kong dollar	1,881	1,474
RMB	768	4,843
Euro	4	—
	121,628	941,446

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

17. SHARE CAPITAL — GROUP AND COMPANY

	Number of shares (thousands)	Amount		
		Ordinary shares	Share premium	Total
At 1 January 2005	2,905,000	309,340	2,151,035	2,460,375
At 31 December 2005	<u>2,905,000</u>	<u>309,340</u>	<u>2,151,035</u>	<u>2,460,375</u>
At 31 December 2006	<u>2,905,000</u>	<u>309,340</u>	<u>2,151,035</u>	<u>2,460,375</u>

As at 31 December 2006 and 2005, the total number of authorised ordinary shares is 5,000,000,000 shares with a par value of HK\$0.1 per share.

As at 31 December 2006 and 2005, the number of issued and fully paid ordinary shares is 2,905,000,000 shares.

18. OTHER RESERVES — GROUP

	Merger reserve (a)	Capital surplus	Statutory reserve (b)	Hedging Reserve (c)	Options (d)	Total
Balance at 1 January 2005	(599)	13,136	546,646	—	—	559,183
Cash flow hedges:						
— Fair value loss in the year	—	—	—	(3,370)	—	(3,370)
— Transfer to property, plant and equipment	—	—	—	3,370	—	3,370
Profit appropriation	—	—	172,084	—	—	172,084
Others	—	4,058	—	—	—	4,058
Balance at 31 December 2005	(599)	17,194	718,730	—	—	735,325
Employee share options scheme:						
— Value of employee services (Note 32)	—	—	—	—	16,745	16,745
Profit appropriation	—	—	230,276	—	—	230,276
Others	—	1,950	—	—	—	1,950
Balance at 31 December 2006	<u>(599)</u>	<u>19,144</u>	<u>949,006</u>	<u>—</u>	<u>16,745</u>	<u>984,296</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

18. OTHER RESERVES — GROUP *(Continued)*

(a) Merger reserve

The merger reserve of the Group represents the difference between the nominal value of the shares of the subsidiaries that had been acquired and the nominal value of the Company's shares issued in exchange therefore pursuant to the Reorganisation.

(b) Statutory reserve

(i) *Statutory surplus reserves*

In accordance with the PRC regulations and the Articles of the Association of the subsidiaries registered in PRC ("PRC subsidiaries"), before distributing the net profit of each year, the PRC subsidiaries are required to set aside 10% of their statutory net profit for the year after offsetting any prior year's losses as determined under the PRC accounting regulations to the statutory surplus reserve fund. When the balance of such reserve reaches 50% of the share capital, any further appropriation is optional. The statutory surplus reserve fund can be utilised to offset prior years' losses or to issue bonus shares. However, such statutory surplus reserve fund must be maintained at a minimum of 25% of the entity's share capital after such issuance.

(ii) *Discretionary reserves*

The appropriation of discretionary reserve fund is proposed by board of directors of the PRC subsidiaries, and approved by the shareholder's meeting. The discretionary reserve fund can be utilised to offset prior years' losses or increase share capital.

(iii) *Statutory public welfare*

During the year ended 31 December 2005, the PRC subsidiaries are required to set aside 5% to 10% of their statutory net profit for the year to the statutory public welfare fund. The statutory public welfare fund is to be utilised to build or acquire capital items for the entity's employees and cannot be used to pay off staff welfare expense. These capital items belong to the PRC subsidiaries.

Pursuant to the relevant regulation issued by the Ministry of Finance of the PRC in the year 2006, the PRC subsidiaries do not set aside their statutory net profit to the statutory public welfare fund from 1 January 2006 onwards. The balance of such fund as at 31 December 2005 has been transferred to and used as statutory surplus reserve fund accordingly.

(c) Hedging reserve

The hedging reserve represents the gain or loss of the hedging instrument that are determined to be effective hedge.

The hedging reserve was removed from equity and included in the initial cost or other carrying amount of the asset or liability which was designated as hedged items when the hedge of a firm commitment subsequently resulted in the recognition of a non-financial asset or a non-financial liability.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

18. OTHER RESERVES — GROUP (Continued)

(d) Employee share option scheme

As approved by the Board of Directors and Shareholders' meeting, the share options were granted to the directors and an employee on 30 June 2006 ("Date of Grant"), in an aggregate to 24,200,000 shares. The options are exercisable at any time during the period no later than ten years from the Date of Grant with the exercise price of HK\$1.76 per share. The Group has no legal or constructive obligation to repurchase or settle the options in cash.

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

	31 December 2006	
	Average exercise price in HK\$ per share	Options (thousands)
At 1 January	—	—
Granted	1.76	24,200
At 31 December	1.76	<u>24,200</u>

Share options outstanding at 31 December 2006 will expire on 30 June 2016.

The fair value of options granted during the period, determined by using the Binomial valuation model, was HK\$16.267 million (approximately to RMB16.745 million). The significant inputs into the model were share price of HK\$1.76, at the grant date, exercise price shown above, volatility of 43.0%, expected dividends paid out rate of 3.68% and annual risk-free interest rate of 4.84%. The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of daily share prices of the Company and other comparable companies over the last five years.

19. TRADE PAYABLES — GROUP

	2006	2005
Accounts payable	425,268	430,159
Notes payable (a)	91,100	202,280
	516,368	<u>632,439</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

19. TRADE PAYABLES — GROUP *(Continued)*

(a) As at 31 December 2006, the notes payable represented bank acceptance notes, RMB32.1 million of which were secured by certain notes receivable (*Note 13*), certain restricted bank balances (*Note 16*), and bank acceptance notes issued by a subsidiary amounting to RMB8 million approximately, and RMB59 million of which were secured by certain inventories (*Note 12*), certain restricted bank balances (*Note 16*) and guaranteed by Jinxi Limited.

As at 31 December 2005, the notes payable represented bank acceptance notes secured by certain inventories (*Note 12*), certain notes receivable (*Note 13*) and certain restricted bank balances (*Note 16*).

As at 31 December 2006 and 2005, the ageing analysis of the trade payables was as follows:

	2006	2005
Within 3 months	478,916	546,684
4-6 months	30,703	82,623
7-9 months	2,795	640
10-12 months	219	815
Above 1 year	3,735	1,677
	516,368	632,439

20. ACCRUALS, ADVANCES FROM CUSTOMERS AND OTHER CURRENT LIABILITIES — GROUP

	2006	2005
Accruals	9,356	10,108
Advances from customers	387,518	275,835
Value-added tax payable	58,431	55,838
Other taxes payables	2,553	1,883
Other payables (a)	540,378	671,244
	998,236	1,014,908

(a) The breakdown of other payables as at 31 December 2006 and 2005 were as follows:

	2006	2005
Pension payables and other social welfare payables	104,424	99,431
Payables for purchase of property, plant and equipment	278,549	418,555
Customer deposits	91,671	76,920
Employee deposits	15,716	15,308
Salary payables	19,972	15,513
Others	30,046	45,517
	540,378	671,244

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

21. BORROWINGS — GROUP

	2006	2005
Non-current		
Bank borrowings, secured (i)	215,770	149,230
Other borrowings, unsecured (iii)	145,000	145,000
	360,770	294,230
Current		
Bank borrowings—		
Secured (i)	573,230	1,205,900
Guaranteed (ii)	—	130,000
	573,230	1,335,900
Total borrowings	934,000	1,630,130

- (i) As at 31 December 2006, secured borrowings amounting to RMB630 million, out of total secured borrowings amounting to RMB789 million, were secured by certain bank acceptance notes issued by third parties (Note 13), certain property, plant and equipment (Note 7), certain leasehold land and land use rights (Note 6) of the Group and certain bank acceptance notes issued by a subsidiary, amounting to approximately RMB7 million.

As at 31 December 2006, secured borrowings amounting to RMB9 million were secured by certain inventories (Note 12) and guaranteed by Jinxi Limited.

As at 31 December 2006, except for the secured borrowings disclosed above, current secured borrowings amounting to RMB150 million were secured by certain property, plant and equipment (Note 7), certain leasehold land and land use rights (Note 6) and guaranteed by the Company and Foshan Jin Lan Aluminum Company Limited ("Foshan Jin Lan") (a shareholder of Foshan Jinxi) collectively pursuant to the below agreement.

In January 2006, the Company and Foshan Jin Lan granted a guarantee in favour of Foshan Jinxi for bank borrowing facilities amounting to RMB150 million. In accordance with the guarantee contract, the Company and Foshan Jin Lan shall bear 60% and 40% of the guarantee obligation respectively.

As at 31 December 2005, secured borrowings were secured by certain restricted bank balances (Note 16) certain property, plant and equipment (Note 7) and certain leasehold land and land use rights (Note 6) of the Group.

- (ii) As at 31 December 2005, the guaranteed current borrowings were guaranteed by two third parties amounting to RMB30 million and RMB100 million respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

21. BORROWINGS — GROUP (Continued)

- (iii) Other unsecured borrowing represented a borrowing from the local county government amounting to RMB145 million which will be repaid from 1 January 2008 onwards at an amount of RMB20 million per annum. Interest is charged at the RMB bank deposit rate for 1 year fixed deposit.

As at 31 December 2006 and 2005, the Group's borrowings were repayable as follows:

	Bank borrowings		Other borrowings	
	2006	2005	2006	2005
Within 1 year	573,230	1,335,900	—	—
Between 1 and 2 years	—	149,230	20,000	—
Between 2 and 5 years	215,770	—	60,000	60,000
Over 5 years	—	—	65,000	85,000
	<u>789,000</u>	<u>1,485,130</u>	<u>145,000</u>	<u>145,000</u>

The effective interest rates at the balance sheet date were as follows:

	2006	2005
Bank borrowings	5.58%-7.15%	5.02%-7.15%
Other borrowings	2.52%	2.25%

The carrying amounts and fair value of the non-current borrowings are as follows:

	Carrying amounts		Fair value	
	2006	2005	2006	2005
Bank borrowings	215,770	149,230	215,770	149,230
Other borrowings	145,000	145,000	123,476	119,309
	<u>360,770</u>	<u>294,230</u>	<u>339,246</u>	<u>268,539</u>

The carrying amounts of short-term borrowings approximated their fair value.

The carrying amounts of the borrowings are all denominated in RMB.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

21. BORROWINGS — GROUP *(Continued)*

Interest rates of the bank borrowings denominated in RMB are reset periodically according to the primary rate announced by the People's Bank of China. The exposure of the Group's bank borrowings to interest-rate changes and the contractual repricing dates are as follows:

	2006	2005
6 months or less	393,230	1,152,130
6-12 months	395,770	333,000
	<u>789,000</u>	<u>1,485,130</u>

22. DEFERRED INCOME TAX — GROUP

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

	2006	2005
Deferred tax assets:		
— Deferred tax asset to be recovered within 12 months	—	2,327
Deferred tax liabilities:		
— Deferred tax liabilities to be settled within 12 months	(290)	—
	<u>(290)</u>	<u>2,327</u>

The gross movement on the deferred income tax account is as follows:

	2006	2005
Beginning balance of the year	2,327	—
(Charged)/credited to consolidated income statement <i>(Note 28 (a))</i>	(2,617)	2,327
Ending balance of the year	<u>(290)</u>	<u>2,327</u>

Deferred taxation is calculated on temporary differences under the liability method using the tax rate and the tax base that are consistent with the expected manner of recovery or settlement for the year ended 31 December 2006.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

22. DEFERRED INCOME TAX — GROUP *(Continued)*

The movement in deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction is as follows:

Deferred tax liabilities:

	Unrealised losses on inventories
At 1 January 2005	—
At 31 December 2005	—
Charged to consolidated income statement	(290)
At 31 December 2006	<u>(290)</u>

Deferred tax assets:

	Losses on disposal of property, plant and equipment	Others	Total
At 1 January 2005	—	—	—
Credited to consolidated income statement	<u>1,877</u>	<u>450</u>	<u>2,327</u>
At 31 December 2005	1,877	450	2,327
Charged to consolidated income statement	<u>(1,877)</u>	<u>(450)</u>	<u>(2,327)</u>
At 31 December 2006	<u>—</u>	<u>—</u>	<u>—</u>

The amount of unused tax losses for which no deferred tax asset recognised in the balance sheet approximately amounted to RMB95.2 million (2005: RMB53.3 million). In accordance with the relevant tax laws and regulations in the PRC, the loss can be carried forward for 5 years since the year the loss was generated.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

23. OTHER GAINS/(LOSSES) — NET — GROUP

	2006	2005
Other gains/(losses) — net:		
Sales of raw materials and by-products	37,423	27,267
Gain on disposal of intangible assets (Note 32)	85	—
Loss on disposal of property, plant and equipment (Note 32)	(7,329)	(36,490)
Foreign exchange loss, net (Note 32)	(2,979)	(44,858)
Others	4,239	6,332
Total	<u>31,439</u>	<u>(47,749)</u>

24. OTHER INCOME — GROUP

	2006	2005
Subsidy income	—	345
Dividend income on financial assets at fair value through profit or loss (Note 32)	1,061	3,728
Rental income arising from investment properties (Note 8)	1,261	141
Others	1,827	72
Total	<u>4,149</u>	<u>4,286</u>

25. EXPENSES BY NATURE — GROUP

	2006	2005
Employee benefit expense (Note 26)	243,483	168,608
Costs of inventories (Note 12)	7,318,352	7,076,396
Amortisation of leasehold land and land use rights (Note 6, 32)	1,477	1,314
Depreciation of property, plant and equipment (Note 7, 32)	326,691	207,734
Amortisation of intangible assets (Note 9, 32)	3,582	682
Impairment of property, plant and equipment (Note 7, 32)	41,859	—
Depreciation of investment properties (Note 8, 32)	1,112	445
Operating lease rental in respect of land use rights	4,503	3,368
Reversal of impairment provision for receivables (Note 7, 32)	(600)	—
(Reversal of)/provision for write-down of inventories (Note 32)	(10,754)	12,632
Auditors' remuneration	<u>3,300</u>	<u>3,000</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

26. EMPLOYEE BENEFIT EXPENSE — GROUP

	2006	2005
Staff costs (including directors' emoluments)		
— Salaries and welfare	203,184	144,062
— Pension costs — defined contribution plans (a)	23,554	24,546
— Share options granted to directors and an employee	16,745	—
	<u>243,483</u>	<u>168,608</u>

(a) Pensions — defined contribution plans

The employees of the subsidiaries of the Group that are incorporated in the PRC participate in a defined contribution retirement benefit plan organised by the relevant provincial government. For the year ended 31 December 2006 and 2005, the Group is required to make monthly defined contributions to these plans at rates from 20.5% to 28%, with the base of their total salary subject to a certain ceiling.

The Group has no other obligations for the payment of retirement and other post-retirement benefits of employees or retirees other than the payments disclosed in the above note.

(b) Directors' and senior management's emoluments

The emoluments of every director for the year ended 31 December 2006 and 2005, on a named basis, are set out as below:

Name of Director	Fees	Salaries and allowances	Bonus	Fair value of employee share options granted	Pension costs — defined contribution plans	Total
2006						
Mr. Han Jingyuan	638	3,948	—	1,936	12	6,534
Mr. Zhu Jun	306	520	480	1,661	20	2,987
Mr. Liu Lei	376	596	—	1,661	12	2,645
Mr. Shen Xiaoling	306	322	278	1,661	20	2,587
Ms. Chen Ningning	256	—	—	1,799	12	2,067
Mr. Yu Tung Ho	307	—	—	1,661	—	1,968
Mr. Tang Chi Fai	256	—	—	1,661	12	1,929
Mr. Wong Man Chung, Francis	256	—	—	1,661	—	1,917
Mr. Gao Qingju	256	—	—	1,661	—	1,917
	<u>2,957</u>	<u>5,386</u>	<u>758</u>	<u>15,362</u>	<u>88</u>	<u>24,551</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

26. EMPLOYEE BENEFIT EXPENSE — GROUP (Continued)

(b) Directors' and senior management's emoluments (Continued)

Name of Director	Fees	Salaries and allowances	Bonus	Fair value of employee share options granted	Pension costs — defined contribution plans	Total
2005						
Mr. Han Jingyuan	246	1,393	105	—	5	1,749
Mr. Zhu Jun	164	1,050	—	—	15	1,229
Mr. Shen Xiaoling	105	650	—	—	10	765
Mr. Liu Lei	167	436	58	—	5	666
Mr. Yu Tung Ho	263	—	—	—	—	263
Ms. Chen Ningning	244	—	—	—	7	251
Mr. Tang Chi Fai	214	—	—	—	7	221
Mr. Wong Man Chung, Francis	210	—	—	—	—	210
Mr. Gao Qingju	164	—	—	—	—	164
	<u>1,777</u>	<u>3,529</u>	<u>163</u>	<u>—</u>	<u>49</u>	<u>5,518</u>

None of the directors waived or agreed to waive any remuneration during the years 2006 and 2005. The emoluments of the independent non-executive directors during the year are RMB5.8 million approximately (2005: RMB0.64 million).

(c) Five highest paid individuals

The five highest paid individuals consisted of:

	2006	2005
Number of directors	<u>4</u>	4
Number of employees	<u>1</u>	1
	<u>5</u>	<u>5</u>

The five individuals whose emoluments were the highest in the Group for the year include four (2005: four) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining one (2005: one) individuals during the year are as follows:

	2006	2005
Salaries and allowances	<u>716</u>	737
Bonuses	—	58
Fair value of employee share options granted	<u>1,383</u>	—
Pension costs-defined contribution plans	<u>12</u>	13
	<u>2,111</u>	<u>808</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

26. EMPLOYEE BENEFIT EXPENSE — GROUP *(Continued)*

(c) Five highest paid individuals *(Continued)*

During the years ended 31 December 2006 and 2005, no emoluments were paid by the Group to any of the directors or the five highest paid individuals as inducement to join or upon joining the Company or as compensation for loss of office.

The remuneration of the five highest paid individuals during the years ended 31 December 2006 and 2005 fell within the following bands:

	Number of individuals	
	2006	2005
Nil to RMB1,000,000 (approximately to HK\$1,000,000)	—	3
RMB1,000,001 to RMB2,000,000 (approximately HK\$1,000,001 to HK\$2,000,000)	—	2
RMB2,000,001 to RMB3,000,000 (approximately HK\$2,000,001 to HK\$3,000,000)	4	—
RMB6,000,001 to RMB7,000,000 (approximately HK\$6,000,001 to HK\$7,000,000)	1	—
	1	—

27. FINANCE INCOME AND COSTS — GROUP

	2006	2005
Interest expenses		
— borrowings	(48,615)	(70,071)
— amount due to related parties <i>(Note 35 (b)(ii))</i>	(1,633)	(2,764)
— discount of notes receivable	(139)	(1,354)
Finance costs <i>(Note 32)</i>	(50,387)	(74,189)
Finance income		
— interest income on bank deposits <i>(Note 32)</i>	18,930	62,596
Finance costs, net	(31,457)	(11,593)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

28. TAXATION — GROUP

(a) Taxation represents:

	2006	2005
Current income tax		
— PRC enterprise income tax (the "EIT")	208,269	159,408
Deferred income tax (Note 22)	2,617	(2,327)
	<u>210,886</u>	<u>157,081</u>

The Company was incorporated in Bermuda as an exempted company with limited liability under the Companies Act 1981 of Bermuda and, accordingly, is exempted from payment of Bermuda income tax.

The subsidiaries directly held by the Company were incorporated in BVI with limited liability under the International Business Companies Act Chapter 291 and, accordingly, are exempted from payment of BVI income tax.

Hong Kong profits tax has not been provided as there is no estimated assessable profit for the year ended 31 December 2006 (2005: nil).

The PRC EIT is calculated based on the statutory profit of subsidiaries incorporated in the PRC in accordance with the PRC tax laws and regulations, after adjustments on certain income and expense items, which are not assessable or deductible for income tax purposes.

The PRC state enterprise income tax rate of the indirect subsidiary of the Company, Jinxi Limited, is 30% and the local income tax rate is 3%. Therefore, an aggregate tax rate of 33% was applicable for income tax filing purpose.

Effective from 25 December 2002, Jinxi Limited was approved to be a foreign-invested joint stock company. In accordance with the relevant tax laws and regulations in the PRC and a local tax authority approval dated 20 January 2003, effective from 1 January 2003, Jinxi Limited was entitled to a two-year full exemption followed by a three-year 50% tax deduction from the PRC state EIT.

Approved by local tax authority at 22 July 2004, Jinxi Limited was entitled to a five-year full exemption followed by a five-year 50% tax deduction from the local income tax started from 1 January 2003. Accordingly, the effective tax rate of Jinxi Limited was 15% for the year ended 31 December 2006 (2005: 15%).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

28. TAXATION — GROUP *(Continued)*

(a) Taxation represents *(Continued)*:

Foshan Jinxi qualified as a foreign investment production enterprise and was established in a coastal economic development zone. Accordingly, the applicable enterprise income tax rate is 24% and the local tax rate is 3%, resulting in an aggregate tax rate of 27%. As at 31 December 2006, Foshan Jinxi was in a cumulative tax loss position. Accordingly, the effective tax rate is nil (2005: nil).

(b) The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the weight average tax rate of 35.29% (2005: 33%) to profits of the consolidated entities for the years ended 31 December 2006 and 2005 as follows:

	2006	2005
Profit before taxation	<u><u>1,233,236</u></u>	<u><u>1,004,196</u></u>
Taxation calculated at statutory tax rate	435,181	331,385
Effect of tax exemption of Jinxi Limited	(251,861)	(196,590)
Tax losses for which no deferred income tax asset was recognised	25,977	21,015
Effect of other non-taxable income	(9)	(988)
Effect of non-deductible expenses	1,598	2,259
	<u><u>210,886</u></u>	<u><u>157,081</u></u>

29. PROFIT ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE COMPANY

The profit attributable to the equity holders of the Company is dealt with in the accounts of the Company to the extent of approximately RMB134.45 million (2005: RMB124.79 million).

30. EARNINGS PER SHARE

Basic

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	2006	2005
Profit attributable to equity holders of the Company	<u><u>1,032,754</u></u>	846,585
Weighted average number of ordinary shares in issue (thousands)	2,905,000	2,905,000
Basic earnings per share (RMB per share)	<u><u>0.36</u></u>	<u><u>0.29</u></u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

30. EARNINGS PER SHARE *(Continued)*

Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares: share options. For the share options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) during the period based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

The average market price of ordinary shares during the year ended 31 December 2006 did not exceed the exercise price, HK\$1.76 per share. The share options are antidilutive and are ignored in the calculation of the diluted earnings per share.

31. DIVIDENDS

	2006	2005
Interim, paid (a)	29,730	—
Final, proposed (b, c)	132,149	136,044
	161,879	136,044

- (a) At a meeting held on 30 August 2006, the directors declared an interim dividends of HK\$29.05 million (approximately RMB29.73 million), representing HK\$ 0.01 per share, for the year ended 31 December 2006.
- (b) At a meeting held on 30 March 2006, the directors proposed a final dividend in respect of the year ended 31 December 2005 of HK\$130.73 million (approximately RMB136.04 million), representing HK\$0.045 per ordinary share. The Annual General Meeting held on 17 May 2006 approved the directors' dividends proposal.
- (c) At a meeting held on 3 April 2007, the directors proposed a final dividend in respect of the year ended 31 December 2006 of HK\$133.63 million (approximately RMB132.15 million), representing HK\$0.046 per ordinary share. This proposed dividend is not reflected as a dividends payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2007.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(i) Reconciliation of profit before taxation to cash generated from operations is as follows

	2006	2005
Profit before income tax	1,233,236	1,004,196
Reversal of impairment provision for receivables (Note 25)	(600)	—
Depreciation of property, plant and equipment (Note 7,25)	326,691	207,734
Depreciation of investment properties (Note 8,25)	1,112	445
Amortisation of leasehold land and land use rights (Note 6,25)	1,477	1,314
Amortisation of intangible assets (Note 9,25)	3,582	682
(Reversal of)/write-down inventories to their net realisable value (Note 25)	(10,754)	12,632
Impairment provision for property, plant and equipment (Note 7,25)	41,859	—
Share of losses of an associate company (Note 11)	984	2,319
Loss on disposal of property, plant and equipment, net (Note 23)	7,329	36,490
Gain on disposal of intangible assets, net (Note 23)	(85)	—
Exchange loss (Note 23)	2,979	44,858
Interest income (Note 27)	(18,930)	(62,596)
Dividend income on financial assets at fair value through profit or loss (Note 24)	(1,061)	(3,728)
Interest expenses (Note 27)	50,387	74,189
Employee share option scheme (Note 18)	16,745	—
Operating profit before working capital changes	1,654,951	1,318,535
Decrease/(Increase) in financial assets at fair value through profit or loss	64,498	(64,633)
Increase in inventories	(293,770)	(215,799)
Decrease in restricted bank balances	32,432	221,254
Increase in trade receivables, prepayments, deposits and other receivables and other current assets	(940,355)	(574,438)
Decrease in long-term advances to suppliers	—	50,000
(Decrease)/Increase in trade payables, current income tax liabilities, accruals, advances from customers and other current liabilities	(11,965)	90,466
Decrease in long-term advances from customers	(25,000)	—
Decrease in amount due to related parties	(221)	(200,905)
Cash generated from operations	480,570	624,480

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

32. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT *(Continued)*

(ii) Major non-cash transactions:

During the year ended 31 December 2006, the Group endorsed bank acceptance notes to the supplier for purchase of property, plant and equipment amounting to approximately RMB324 million (2005: approximately RMB801 million).

(iii) In the cash flow statement, proceeds from sales of property, plant and equipment comprise:

	2006	2005
Net book amount <i>(Note 7)</i>	15,398	40,503
Loss on disposals of property, plant and equipment <i>(Note 23)</i>	(7,329)	(36,490)
Proceeds from disposal of property, plant and equipment	<u>8,069</u>	<u>4,013</u>

33. CONTINGENT EVENTS

The Group

Guarantee for third parties

	2006	2005
Guarantee for bank borrowings of third parties <i>(i)</i>	18,900	28,986
Guarantee for letter of credit issued by a third party <i>(ii)</i>	50,520	248,429
	<u>69,420</u>	<u>277,415</u>

(i) As at 31 December 2006, Jinxi Limited provided guarantee for bank borrowings in favour of third parties amounting to approximately RMB18.9 million (2005: approximately RMB28.99 million).

(ii) During the year ended 31 December 2006, a third party acted as an agent and issued letter of credit to import property, plant and equipment for Jinxi Limited. Accordingly, Jinxi Limited pledged notes receivable amounting to RMB51 million *(Note 13)* as collaterals (2005: approximately RMB248 million).

The Directors of the Company believe that to settle the obligation will not probably cause an outflow of resources embodying economic benefits.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

33. CONTINGENT EVENTS *(Continued)*

The Company

	2006	2005
Guarantee for bank borrowings of subsidiaries	<u>90,000</u>	<u>872,900</u>

In January 2006, the Company and Foshan Jin Lan collectively granted a guarantee in favour of Foshan Jinxi for current bank facilities amounting to RMB150 million. In accordance with the guarantee contract, the Company and Foshan Jin Lan shall bear 60% and 40% of the guarantee obligation respectively.

As at 31 December 2006, pursuant to the aforementioned agreement, current secured borrowings of Foshan Jinxi amounting to RMB150 million were guaranteed by the Company and Foshan Jin Lan collectively.

As at 31 December 2005, the Company pledged bank deposits amounting to US\$110 million (equivalent to approximately RMB888 million) as collaterals to secure current borrowings of Jinxi Limited and Foshan Jinxi.

The Directors of the Company believe that to settle the obligation will not probably cause an outflow of resources embodying economic benefits.

34. COMMITMENTS — GROUP

(a) Capital commitments

Capital expenditure at the balance sheet date but not yet incurred is as follows:

	2006	2005
To acquire the minority interest in Jinxing Charging	<u>8,900</u>	—
To acquire interests in certain mining enterprises	<u>83,421</u>	—
	<u>92,321</u>	—
Purchase of property, plant and equipment		
— Contracted but not provided for	<u>6,599</u>	256,266
— Authorised but not contracted for	<u>1,971,348</u>	—
	<u>1,977,947</u>	<u>256,266</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

34. COMMITMENTS — GROUP *(Continued)*

(b) Operating lease commitments

The future aggregate minimum lease rental expenses in respect of land use rights and building under non-cancellable operating leases are payable as follows:

	2006	2005
Not later than one year	5,723	4,629
Later than one year and not later than five years	17,086	13,404
Later than five years	93,571	65,969
	116,380	84,002

35. RELATED PARTY TRANSACTIONS

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

- (a) During the year 2006 and 2005, the directors are of the view that the following companies and persons are related parties of the Group:

Name	Relationship with the Group
Wellbeing	Substantial shareholder of the Company
Smart Triumph	Substantial shareholder of the Company
Qianxi County Heli Industry and Trade Co., Ltd. ("Qianxi Heli") (i)	The controlling shareholder was Mr. Han Jingyuan, a director of the Company
Tangshan Qianxi County Fuqin Industrial and Trade Co., Ltd. ("Qianxi Fuqin")	The controlling shareholder is Mr. Han Jingyuan, a director of the Company
Pioneer Metals Co., Ltd. ("PMC")	The controlling shareholder is Ms. Chen Ningning, a director of the Company
Tangshan City Jinxi Iron and Steel Group Co., Ltd. ("Tangshan Jinxi Group")	Shareholder of Jinxi Limited and its legal representative is Mr. Han Jingyuan, a director of the Company

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

35. RELATED PARTY TRANSACTIONS *(Continued)*

- (a) During the year 2006 and 2005, the directors are of the view that the following companies and persons are related parties of the Group *(Continued)*:

Name	Relationship with the Group
Beijing PMC New Century Technology Co., Ltd. ("Beijing PMC")	Subsidiary of PMC
Foshan Jin Lan	Substantial shareholder of Foshan Jinxi
Zhongxing Iron Mine	Jinxi Limited's associated company
Beijing Wanlihe Trading Co., Ltd. ("Beijing Wanlihe")	Its controlling shareholder is Mr. Han Jingyuan, a director of the Company
Mr. Han Jingyuan	Chairman and Chief Executive Officer of the Company
Mr. Zhou Weijie	Director of Foshan Jinxi
Ms. Fu Ruiyun	The shareholder of Jinxing Charging

- (i) Qianxi Heli was deregistered in March 2005 and ceased to be the Group's related party from then on.

- (b) Save as disclosed elsewhere in these consolidated financial statements, during the year 2006 and 2005, the directors were of the view that the following significant related party transactions were carried out in the normal course of business of the Group:

(i) Purchases

	2006	2005
Purchase of property, plant and equipment — Foshan Jin Lan	—	25,785
Purchases of inventories: — Zhongxing Iron Mine	—	28,383

(ii) Loan received

Tangshan Jinxi Group provided a loan to Foshan Jinxi, amounting to RMB30 million. The loan are unsecured, bore interest at a rate of 5.58% per annum and repayable within one year. For the year ended 31 December 2006, interest expense of approximately RMB1.2 million was incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

35. RELATED PARTY TRANSACTIONS *(Continued)*

(b) Save as disclosed elsewhere in these consolidated financial statements, during the year 2006 and 2005, the directors were of the view that the following significant related party transactions were carried out in the normal course of business of the Group *(Continued)*:

(ii) Loan received *(Continued)*

Foshan Jin Lan entered into an agreement with Foshan Jinxi and Accordpower in January 2006. Pursuant to the agreement:

- (1) Foshan Jin Lan provided a loan amounting to RMB11.86 million, approximated to US\$1.5 million, to Foshan Jinxi in the form of (a) lending of RMB1 million in cash, (b) repayment the borrowings to a third party on behalf of Foshan Jinxi of RMB10 million, (c) postponement of interest collection by RMB0.86 million approximately, on condition that Accordpower provided a loan to Foshan Jinxi of US\$2.25 million.
- (2) Foshan Jin Lan designated the existing receivable from Foshan Jinxi amounting to RMB44.67 million as interest-free, on the condition that Accordpower additionally provided another loan to Foshan Jinxi of US\$9.03 million. Interest expense of approximately RMB0.44 million was incurred before Accordpower provided the loan to Foshan Jinxi *(Note 21)*.

During the year 2006, Foshan Jinxi has paid certain expenses on behalf of Foshan Jin Lan amounting to approximately RMB0.99 million, which was deducted from the loans provided by Foshan Jin Lan.

All the above loans granted by Foshan Jin Lan in accordance with the agreement are unsecured, interest-free and repayable only after five years.

Tangshan Jinxi Group provided a loan, amounting to RMB70 million to Jinxi Limited, which was fully repaid to Tangshan Jinxi Group during the year ended 31 December 2005. The loan was unsecured, interest free and had no fixed term of repayment.

(iii) Contribution

Pursuant to the "New Joint Venture Agreement" as announced in the Company's circulars dated 18 January 2005, Foshan Jin Lan contributed a building to Foshan Jinxi in February 2005, with a fair value of approximately RMB2.8 million.

(iv) Repayment of the amount due to PMC and Qianxi Heli

Subject to certain agreements entered into December 2003, the payables amounting to PMC and Qianxi Heli, amounting to RMB100 million and RMB116 million respectively, were due after 30 June 2005. In the year 2005, Jinxi Limited repaid RMB100 million to Beijing PMC according to the written instruction of PMC, and repaid RMB114 million to Beijing Wanlihe and RMB2 million to Qianxi Fuqin according to the written instruction of Qianxi Heli.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

35. RELATED PARTY TRANSACTIONS *(Continued)*

- (c) As at 31 December 2006 and 2005, the directors were of the view that the following related party balances were attributed to the aforementioned related party transactions, amounts paid on behalf of the Group, dividends appropriation during the years.

	2006	2005
Borrowings from related parties:		
Non-current		
— Foshan Jin Lan <i>(Note 35 (b)(ii))</i>	55,529	—
Current		
— Tangshan Jinxi Group <i>(Note 35 (b)(ii))</i>	31,194	—
— Foshan Jin Lan <i>(Note 35 (b)(ii))</i>	—	45,082
— Ms. Fu Ruiyun	16,783	16,783
	103,506	61,865
Dividends payable due to		
— Tangshan Jinxi Group	5,391	—
— Zhongxing Iron Mine	2,535	2,535
	7,926	2,535
Others:		
— Mr. Han Jinyuan	771	—
	112,203	64,400

Except for the loan provided by Foshan Jin Lan and Tangshan Jinxi Group as disclosed in Note 35 (b)(ii), the related party balances were all unsecured, interest free and had no fixed term of repayment.

36. SUBSEQUENT EVENTS

Saved as disclosed elsewhere in this announcement, the significant subsequent events of the Group were as follows:

- (i) Jinxi Limited entered into an agreement with Ms. Fu Ruiyun on 23 December 2006 to acquire 38% equity interests of Jinxing Charging held by Ms. Fu Ruiyun. The total consideration was RMB8.9 million in the form of cash. All of the cash consideration was paid in January 2007. Consequently, in accordance with the aforementioned agreement, Jinxing Charging become a wholly owned subsidiary of Jinxi Limited.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2006
(All amounts in RMB thousands unless otherwise stated)

36. SUBSEQUENT EVENTS *(Continued)*

- (ii) On 30 March 2007, the directors of Jinxi Limited proposed a final dividend of RMB181 million in respect of the year ended 31 December 2006.
- (iii) Change of mainland China enterprise income tax law

On 16 March 2007, the Enterprise Income Tax Law (the “new EIT law”) was passed at the Fifth Session of the Tenth National People’s Congress of the People’s Republic of China. The new EIT law will be effective as at 1 January 2008, and the “Income Tax Law of the People’s Republic of China for Enterprises with Foreign Investment and Foreign Enterprises” and “Provisional Regulations of the People’s Republic of China on Enterprise Income Tax” both of which the Group was originally subjected to will be abrogated simultaneously. The Group has already commenced an assessment of the impact of the new EIT but is not yet in a position to state the accurate impact on the Group’s results of operations and financial position in the future.

37. APPROVAL OF ACCOUNTS

These consolidated financial statements were approved by the board of directors on 3 April 2007.

SUMMARY OF FINANCIAL INFORMATION

A summary of the consolidated income statement and of the consolidated assets, liabilities and minority interest of the Group for the last five financial years prepared on the basis as hereunder stated is as set out below:

Consolidated Income Statement

	2006 RMB'000	Year ended 31 December			Proforma 2002 RMB'000
		Audited		2003 RMB'000	
		2005 RMB'000	Restated 2004 RMB'000		
Revenue	9,782,116	9,182,693	9,118,875	5,277,874	2,571,304
Profit before income tax	1,233,236	1,004,196	1,175,832	1,142,666	586,361
Income tax expense	(210,886)	(157,081)	33,686	(40,018)	(188,850)
Profit for the year	1,022,350	847,115	1,209,518	1,102,648	397,511
Attributable to:					
Equity holders of the Company	1,032,754	846,585	1,181,006	1,076,290	388,020
Minority interest	(10,404)	530	28,512	26,358	9,491
	1,022,350	847,115	1,209,518	1,102,648	397,511

Consolidated Assets, Liabilities and Minority Interest

	2006 RMB'000	Audited			Proforma 2002 RMB'000
		Audited		2003 RMB'000	
		2005 RMB'000	Restated 2004 RMB'000		
TOTAL ASSETS	8,221,367	8,152,862	7,481,892	3,876,614	2,214,756
TOTAL LIABILITIES	(2,619,918)	(3,420,767)	(3,481,028)	(2,907,580)	(1,868,265)
MINORITY INTEREST	(122,322)	(138,643)	(115,524)	(23,168)	(8,273)
	5,479,127	4,593,452	3,885,340	945,866	338,218

SUMMARY OF FINANCIAL INFORMATION

Notes:

1. The summary of the proforma consolidated result of the Group for the year ended 31 December 2002 was extracted from the Company's prospectus dated 18 February 2004 (the "Prospectus"). Such summary was prepared as if the group structure as at 20 January 2004 had been in existence throughout this financial year. The audited consolidated income statement of the Group for the two years ended 31 December 2004 was extracted from the Company's annual report of 2004 and 2005. The audited consolidated income statement of the Group for the two years ended 31 December 2006 are those set out on page 36 of this annual report.
2. The summary of the proforma consolidated assets, liabilities and minority interest as at 31 December 2002 was extracted from the Prospectus. Such summary was prepared on the same basis as detailed in note 1 above. The audited consolidated assets, liabilities and minority interest as at 31 December 2003 and 2004 were extracted from the Company's annual report of 2004 and 2005. The audited consolidated assets, liabilities and minority interest as at 31 December 2005 and 2006 are those set out on page 33 and 34 of this annual report.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the Annual General Meeting of China Oriental Group Company Limited will be held at Lotus Room, 6th Floor, The Marco Polo Hongkong Hotel, 3 Canton Road, Tsim Sha Tsui, Kowloon on Tuesday, 22 May 2007 at 9:30 a.m. for the following purposes:

1. To receive and consider the audited financial statements of the Group, the audited balance sheet of the Company, the reports of the Directors and the Independent Auditor for the year ended 31 December 2006.
2. To declare a final dividend of HK4.6 cents per share for the year ended 31 December 2006.
3. To re-elect the Directors (Mr. Zhu Jun, Mr. Wong Man Chung, Francis and Mr. Yu Jianshui) and to authorize the Directors to fix their remuneration.
4. To re-appoint PricewaterhouseCoopers as Auditors and to authorise the Directors to fix their remuneration.
5. To approve and ratify the ordinary remuneration of the Directors for the Board of the Company be fixed at the sum of HK\$2,850,000 for each financial year commencing from 1 January 2006 onwards until the Company in general meeting otherwise determines.

To consider as **Special Business** and, if thought fit, pass with or without amendments, the following resolutions as **ordinary resolutions**:

6A. **“THAT:**

- (a) subject to paragraph (b) of this Resolution, the exercise by the Directors during the Relevant Period of all the powers of the Company to repurchase shares in the capital of the Company on The Stock Exchange of Hong Kong Limited or on any other stock exchange recognized for this purpose by the Securities and Futures Commission of Hong Kong and The Stock Exchange of Hong Kong Limited in accordance with any applicable law or Bermuda law and the requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited as amended from time to time, be and is hereby generally and unconditionally approved;
- (b) the aggregate nominal amount of the share capital to be repurchased by the Directors pursuant to the approval in paragraph (a) shall not exceed 10% of the aggregate nominal amount of the shares of the Company in issue on the date of the passing of this Resolution; and

NOTICE OF ANNUAL GENERAL MEETING

- (c) for the purpose of this Resolution:

“Relevant Period” means the period from the passing of this Resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Company; or
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by any applicable law or Bermuda Companies Act or the existing bye-laws of the Company to be held; or
- (iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this Resolution.”

6B. **“THAT:**

- (a) subject to paragraph (c) of this Resolution, the exercise by the Directors during the Relevant Period of all the powers of the Company to allot, issue and deal with any unissued shares in the capital of the Company and to make or grant offers, agreement and options which would or might require such shares to be allotted and issued be and is hereby generally and unconditionally approved;
- (b) the Directors be authorized to make or grant offers, agreement and options during the Relevant Period which would or might require shares in the capital of the Company to be allotted and issued either during or after the end of the Relevant Period pursuant to (a) above;
- (c) the aggregate nominal value of the share capital of the Company allotted, issued and dealt with or agreed conditionally or unconditionally to be allotted, issued and dealt with (whether pursuant to an option or otherwise) by the Directors pursuant to the respective approval and authorization referred to in sub-paragraphs (a) and (b) above, otherwise than pursuant to (i) a Rights Issue, (ii) any scrip dividend or similar arrangement providing for the allotment of shares of the Company in lieu of the whole or part of a dividend on shares in accordance with the bye-laws of the Company or (iii) any adjustment of rights to subscribe for shares under options and warrants or a specific authority granted by the shareholders, shall not exceed the aggregate of (i) 20% of the aggregate nominal amount of the share capital of the Company in issue at the date of the passing of this resolution and (ii) the aggregate nominal amount of the share capital of the Company that may have been repurchased pursuant to the repurchase mandate referred to in resolution 6A; and

NOTICE OF ANNUAL GENERAL MEETING

(d) for the purpose of this Resolution:

“Relevant Period” means the period from the passing of this Resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Company; or
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by any applicable law or Bermuda Companies Act or the existing bye-laws of the Company to be held; or
- (iii) the passing of an ordinary resolution by the shareholders of the Company in general meeting revoking or varying the authority given to the Directors by this Resolution.

“Rights Issue” means an offer of shares open for a period fixed by the Directors to holders of shares of the Company on the register of members on a fixed record date in proportion to their then holdings of such shares of the Company (subject to such exclusion or other arrangements as the Directors may deem necessary or expedient in relation to fractional entitlements or having regard to any legal or practical restrictions or obligations under the laws of, or the requirements of, any recognized regulatory body or any stock exchange in any territory applicable to the Company) and an offer, allotment or issue of shares of the Company by way of rights shall be construed accordingly.”

6C. **“THAT** subject to the passing of Resolutions 6A and 6B above, the authority of the Directors pursuant to Resolution 6B be and is hereby approved to extend to cover such amount representing the aggregate nominal amount of the shares in the capital of the Company repurchased pursuant to the authority granted pursuant to Resolution 6A.”

By Order of the Board
China Oriental Group Company Limited
Han Jingyuan
Chairman and Chief Executive Officer

Hong Kong, 27 April 2007

NOTICE OF ANNUAL GENERAL MEETING

Notes:

1. A member of the Company entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and vote in his/her stead. A proxy need not be a member of the Company. In order to be valid, the completed proxy form, together with the power of attorney or other authority (if any) under which it is signed or a certified copy of that power of attorney or authority, must be deposited at the Company's Branch Share Registrar, Tricor Investor Services Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong not less than 48 hours before the time fixed for holding the meeting or adjourned meeting (as the case may be).
2. With regard to Resolutions 6A, 6B and 6C above, the Directors do not have immediate plans to issue any new shares or repurchase any existing shares. Approval is being sought from members of the Company for general mandates pursuant to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.
3. A circular containing further information concerning Resolutions 3, 6A, 6B and 6C will be sent to shareholders together with the Company's Annual Report for 2006.
4. The register of members of the Company will be closed from Friday, 18 May 2007 to Tuesday, 22 May 2007, all days inclusive, during which period no transfer of Shares will be effected. In order to qualify for the proposed final dividend and be eligible to attend and vote at the Annual General Meeting, all transfer documents accompanied by the relevant share certificates must be lodged with the Company's Branch Share Registrar in Hong Kong, Tricor Investor Services Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong not later than 4:30 p.m. on Thursday, 17 May 2007.



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