China Steel Corporation

Financial Statements for the
Six Months Ended June 30, 2006 and 2005 and
Independent Auditors' Report

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders
China Steel Corporation

We have audited the accompanying balance sheets of China Steel Corporation (the "Corporation") as of June 30, 2006 and 2005, and the related statements of income, changes in stockholders' equity and cash flows for the six months then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the Rules Governing the Audit of Financial Statements by Certified Public Accountants and auditing standards generally accepted in the Republic of China (ROC). Those rules and standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Corporation as of June 30, 2006 and 2005, and the results of its operations and its cash flows for the six months then ended, in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers and accounting principles generally accepted in the ROC.

Effective 2006, as stated in Note 3 to the accompanying financial statements, the Corporation adopted the newly issued Statement of Financial Accounting Standards (SFAS) No. 34 "Accounting for Financial Instruments," SFAS No. 36 "Disclosure and Presentation of Financial Instruments" and the related revisions to other SFASs.

July 21, 2006

<u>*Notice to Readers*</u>

The accompanying financial statements are intended only to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in the Republic of China and not those of any other jurisdictions. The standards, procedures and practices to audit such financial statements are those generally accepted and applied in the Republic of China.

For the convenience of readers, the auditors' report and the accompanying financial statements have been translated into English from the original Chinese version prepared and used in the Republic of China. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language auditors' report and financial statements shall prevail. Also, as stated in Note 2 to the financial statements, the additional footnote disclosures that are not required under generally accepted accounting principles were not translated into English.

2006 Amount	%	2005 Amount	%
21,516,956	8	$ 50,810,286	19
17,231,571	6	11,931,521	4
4,303,772	2	1,218,156	-
1,147,743	-	2,012,127	1
2,477,104	1	2,790,459	1
5,667,220	2	2,040,593	1
30,958,294	12	28,755,867	10
119,599	-	287,422	-
4,600,000	2	4,600,000	2
609,801	-	781,447	-
88,632,060	33	105,227,878	38
1,630,086	1	1,001,210	1
6,049,010	2	6,302,202	2
5,881,375	2	5,834,325	2
55,082,169	20	51,633,915	19
68,642,640	25	64,771,652	24
8,049,199	3	7,712,475	3
4,212,123	2	4,231,666	2
36,417,175	13	36,028,949	13
214,004,352	79	212,832,259	77
1,468,257	1	1,526,533	1
3,131,885	1	3,046,602	1
267,282,991	99	265,378,484	97
17,541,220	7	17,687,139	6
284,824,211	106	283,065,623	103
201,276,830	75	195,054,028	71
83,547,381	31	88,011,595	32
23,009,039	9	13,139,455	5
106,556,420	40	101,151,050	37
3,052,200	1	3,081,401	1
223,865	-	220,919	-
31,694	-	31,694	-
2,526,793	1	86,316	-
5,834,552	2	3,420,330	1
269,665,672	100	$ 274,570,910	100

	2006		2005	
LIABILITIES AND STOCKHOLDERS' EQUITY	**Amount**	**%**	**Amount**	**%**
CURRENT LIABILITIES				
Short-term loans and overdraft (Notes 4 and 24)	$ 16,693,318	6	$ 9,687,490	4
Notes and accounts payable (Note 23)	3,320,686	1	2,748,750	1
Income tax payable (Note 20)	2,762,891	1	9,668,220	3
Accrued expenses	4,677,513	2	6,416,155	2
Dividends payable (Note 19)	39,903,047	15	38,907,367	14
Bonds payable - current portion (Note 15)	5,000,000	2	10,000,000	4
Long-term bank loans - current portion (Note 16)	733,850	-	-	-
Other	3,656,149	2	4,314,595	2
Total current liabilities	76,747,454	29	81,742,577	30
LONG-TERM LIABILITIES				
Bonds payable, net of current portion (Note 15)	8,100,000	3	5,000,000	2
Bank loans, net of current portion (Notes 16 and 24)	2,794,275	1	3,582,500	1
Total long-term liabilities	10,894,275	4	8,582,500	3
RESERVE FOR LAND VALUE INCREMENT TAX (Note 12)	2,171,124	1	2,171,124	1
OTHER LIABILITIES				
Deferred income tax liabilities (Note 20)	2,774,763	1	3,018,718	1
Deferred credits - gain on intercompany transactions (Note 18)	1,145,282	-	1,148,442	-
Total other liabilities	3,920,045	1	4,167,160	1
Total liabilities	93,732,898	35	96,663,361	35
CAPITAL STOCK - authorized 10,600,000 thousand shares at NT$10 par value (Notes 2 and 19)				
Common shares - issued 10,545,975 thousand and 9,890,400 thousand shares as of June 30, 2006 and 2005, respectively	105,459,746	39	98,903,998	36
Preferred shares - issued 40,697 thousand and 40,714 thousand as of June 30, 2006 and 2005, respectively	406,970	-	407,140	-
Total capital stock	105,866,716	39	99,311,138	36
CAPITAL SURPLUS (Notes 2 and 19)	1,210,848	-	863,212	-
RETAINED EARNINGS (Notes 2 and 19)	63,219,176	23	78,836,214	29
OTHER EQUITY ITEMS				
Cumulative translation adjustments	(125,705)	-	(525,262)	-
Investees' unrecognized net loss on pension cost	(36,872)	-	(31,578)	-
Unrealized gain (loss) on financial instruments (Notes 3, 6 and 11)	5,610,604	2	(446,463)	-
Revaluation increment on assets (Notes 12 and 19)	1,535,363	1	1,535,363	-
Total other equity items	6,983,390	3	532,060	-
TREASURY STOCK - 81,818 thousand and 105,288 thousand shares as of June 30, 2006 and 2005, respectively (Notes 2 and 19)	(1,347,356)	-	(1,635,075)	-
Total stockholders' equity	175,932,774	65	177,907,549	65
TOTAL	$ 269,665,672	100	$ 274,570,910	100

CHINA STEEL CORPORATION

STATEMENTS OF INCOME
SIX MONTHS ENDED JUNE 30, 2006 AND 2005
(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2006		2005	
	Amount	**%**	**Amount**	**%**
REVENUES (Notes 2 and 23)	$ 80,035,536	100	$ 99,003,245	100
COST OF REVENUES (Notes 21 and 23)	65,656,958	82	56,033,541	56
GROSS PROFIT	14,378,578	18	42,969,704	44
REALIZED (UNREALIZED) GAIN ON INTERCOMPANY TRANSACTIONS	126,609	-	(702,785)	(1)
REALIZED GROSS PROFIT	14,505,187	18	42,266,919	43
OPERATING EXPENSES (Notes 21 and 23)				
Selling	1,068,746	1	1,157,588	1
General and administrative	920,112	1	1,350,702	1
Research and development	498,802	1	549,076	1
Total operating expenses	2,487,660	3	3,057,366	3
OPERATING INCOME	12,017,527	15	39,209,553	40
NONOPERATING INCOME AND GAINS				
Interest	170,077	-	260,077	-
Investment income under the equity method (Note 11)	4,604,393	6	3,637,387	4
Gain on appraisal of financial assets (Note 2)	81,490	-	373,786	-
Other	598,719	1	622,569	1
Total nonoperating income and gains	5,454,679	7	4,893,819	5
NONOPERATING EXPENSES AND LOSSES				
Interest	301,273	-	354,210	-
Impairment loss on long-term investment (Note 11)	-	-	906,000	1
Other	516,110	1	590,276	1
Total nonoperating expenses and losses	817,383	1	1,850,486	2
INCOME BEFORE INCOME TAX	16,654,823	21	42,252,886	43
INCOME TAX (Notes 2 and 20)	2,757,345	4	9,467,585	10

(Continued)

CHINA STEEL CORPORATION

STATEMENTS OF INCOME
SIX MONTHS ENDED JUNE 30, 2006 AND 2005
(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2006		2005	
	Amount	**%**	**Amount**	**%**
INCOME BEFORE CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES	$ 13,897,478	17	$ 32,785,301	33
CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES (Note 3) (Net of $64,547 thousand income tax benefit)	(37,822)	-	-	-
NET INCOME	$ 13,859,656	17	$ 32,785,301	33

	2006		2005	
	Before Tax	**After Tax**	**Before Tax**	**After Tax**
EARNINGS PER SHARE (Note 19)				
Basic	$ 1.58	$ 1.32	$ 4.05	$ 3.14
Diluted	$ 1.58	$ 1.32	$ 4.03	$ 3.13

PRO FORMA INFORMATION - if the Corporation's shares held by subsidiaries had been accounted for as investments rather than treasury stock

	2006	**2005**
Income before cumulative effect of changes in accounting principles	$ 13,898,946	$ 32,815,979
Net income	13,861,124	32,815,979
Basic earnings per share based on weighted-average number of outstanding common shares aggregating 10,544,375 thousand and 10,545,958 thousand for the six months ended June 30, 2006 and 2005, respectively	$ 1.31	$ 3.11
Diluted earnings per share based on weighted-average number of outstanding common shares aggregating 10,585,072 thousand and 10,586,672 thousand for the six months ended June 30, 2006 and 2005, respectively	$ 1.31	$ 3.10

(Concluded)

The accompanying notes are an integral part of the financial statements.

(With Deloitte & Touche audit report dated July 21, 2006)

Note 19) Preferred Stock	Capital Surplus (Notes 12 and 19)	Retained Earnings (Note 19) Legal Reserve	Special Reserve	Unappropriated	Total	Unrealized Gain (Loss) on Financial Instruments (Notes 3, 6 and 11)	Cumulative Translation Adjustments (Notes 2 and 3)	Investees' Unrecognized Net Loss on Pension Cost	Revaluation Increment on Assets (Notes 12 and 19)	Treasury Stock (Notes 2 and 19)	Total Stockholders' Equity
$ 406,980	$ 1,209,378	$ 30,614,261	$ 8,467,340	$ 51,026,001	$ 90,107,602	$ (446,483)	$ (335,992)	$ (36,872)	$ 1,535,363	$ (1,273,221)	$ 196,626,491
(10)	-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	3,936,398	261,188	-	-	-	4,197,586
-	-	5,060,439	-	(5,060,439)	-	-	-	-	-	-	-
-	-	-	(22,347)	22,347	-	-	-	-	-	-	-
-	-	-	-	(137,302)	(137,302)	-	-	-	-	-	(137,302)
-	-	-	-	(915,350)	(915,350)	-	-	-	-	-	(915,350)
-	-	-	-	(152,618)	(152,618)	-	-	-	-	-	(152,618)
-	-	-	-	(39,541,401)	(39,541,401)	-	-	-	-	-	(39,541,401)
-	-	-	-	13,859,656	13,859,656	-	-	-	-	-	13,859,656
-	-	-	-	-	-	(228,442)	-	-	-	-	(228,442)
-	1,468	-	-	-	-	-	-	-	-	(42,039)	(40,571)
-	-	-	-	-	-	-	-	-	-	(32,096)	(32,096)
-	2	-	-	(1,411)	(1,411)	2,349,131	(50,901)	-	-	-	2,296,821
$ 406,970	$ 1,210,848	$ 35,674,700	$ 8,444,993	$ 19,099,483	$ 63,219,176	$ 5,610,604	$ (125,705)	$ (36,872)	$ 1,535,363	$ (1,347,356)	$ 175,932,774
$ 421,770	$ 833,146	$ 25,452,594	$ 8,030,816	$ 52,159,008	$ 85,642,418	$ (454,039)	$ (365,599)	$ (32,003)	$ 339,174	$ (1,113,121)	$ 184,161,114
(14,630)	-	-	-	-	-	-	-	-	-	-	-
-	-	5,161,667	-	(5,161,667)	-	-	-	-	-	-	-
-	-	-	436,524	(436,524)	-	-	-	-	-	-	-
-	-	-	-	(138,243)	(138,243)	-	-	-	-	-	(138,243)
-	-	-	-	(714,035)	(714,035)	-	-	-	-	-	(714,035)
-	-	-	-	(158,785)	(158,785)	-	-	-	-	-	(158,785)
-	-	-	-	(38,572,559)	(38,572,559)	-	-	-	-	-	(38,572,559)
-	-	-	-	32,785,301	32,785,301	-	-	-	-	-	32,785,301
-	-	-	-	-	-	-	-	-	1,196,189	-	1,196,189
-	-	-	-	-	-	-	-	425	-	-	425
-	(988)	-	-	(7,883)	(7,883)	-	(159,663)	-	-	(546,153)	(714,687)
-	31,054	-	-	-	-	7,576	-	-	-	24,199	62,829
$ 407,140	$ 863,212	$ 30,614,261	$ 8,467,340	$ 39,754,613	$ 78,836,214	$ (446,463)	$ (525,262)	$ (31,578)	$ 1,535,363	$ (1,635,075)	$ 177,907,549

CHINA STEEL CORPORATION

STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2006 AND 2005
(In Thousands of New Taiwan Dollars)

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 13,859,656	$ 32,785,301
Cumulative effect of changes in accounting principles	37,822	-
Adjustments		
Depreciation	4,545,841	4,813,926
Amortization	230,316	83,723
Deferred income tax	(80,411)	(86,374)
Gain on appraisal of financial assets	(81,490)	(373,786)
Investment income under the equity method	(4,604,393)	(3,637,387)
Cash dividends from long-term investments under the equity method	348,499	3,831,602
Unrealized (realized) gain on intercompany transactions	(126,609)	702,785
Effect of exchange rate changes on foreign-currency long-term debts	(282)	(224,480)
Impairment loss on financial assets carried at cost	-	906,000
Others	20,822	93,069
Net cash provided by adjusted net income	14,149,771	38,894,379
Net changes in operating assets and liabilities		
Notes receivable	493,289	(300,792)
Accounts receivable	(442,475)	(728,296)
Other receivables	(512,965)	(364,298)
Inventories	4,659,723	(2,875,746)
Other current assets	550,936	(632,961)
Notes and accounts payable	984,279	(337,590)
Income tax payable	(4,815,586)	263,155
Accrued expenses	(2,203,619)	(599,144)
Other current liabilities	(1,763,270)	58,168
Net cash provided by operating activities	11,100,083	33,376,875
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of financial assets at fair value through profit or loss	(7,020,000)	(16,470,062)
Disposal of financial assets at fair value through profit of loss	1,001,447	27,549,681
Increase in long-term stock investments under equity method	(217,553)	(17,488,923)
Proceeds from reduced capital on financial assets carried at cost	18,000	-
Acquisition of properties	(5,264,962)	(6,789,268)
Proceeds from disposal of properties	1,836	89,051
Increase in other assets	(2,740,253)	(169,083)
Decrease in refundable deposits	122,965	-
Proceeds from disposal of long-term stock investments	-	23,457
Decrease in pledged time deposits	-	100,000
Net cash used in investing activities	(14,098,520)	(13,155,147)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in short-term bank loans and overdraft	5,219,935	5,221,531
Increase in bonds payable	8,100,000	-

(Continued)

CHINA STEEL CORPORATION

STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2006 AND 2005
(In Thousands of New Taiwan Dollars)

	2006	2005
Repayments of bonds payable	$ (5,000,000)	$ -
Decrease in commercial paper payable	(1,499,376)	(1,799,052)
Cash dividends	(12,551)	(182,466)
Purchase of treasury stocks	(32,096)	-
Increase in long-term loans	-	945,780
Net cash provided by financing activities	6,775,912	4,185,793
NET INCREASE IN CASH AND CASH EQUIVALENTS	3,777,475	24,407,521
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	17,739,481	26,402,765
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 21,516,956	$ 50,810,286
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest paid	$ 339,715	$ 255,448
Income tax paid	7,653,342	9,290,804
PURCHASE OF PROPERTIES		
Acquisition of properties	$ 5,529,615	$ 6,952,452
Increase in payable on properties purchased	(264,653)	(163,184)
Cash paid	$ 5,264,962	$ 6,789,268
NONCASH FINANCING ACTIVITIES		
Cash dividends payable	$ 39,694,019	$ 38,731,344
Payable for remuneration to directors and supervisors and bonus to employees	1,052,652	852,278

(Concluded)

The accompanying notes are an integral part of the financial statements.

(With Deloitte & Touche audit report dated July 21, 2006)

1. ORGANIZATION AND OPERATIONS

China Steel Corporation (the "Corporation") was incorporated on December 3, 1971. It manufactures and sells steel products and engages in machinery and communications engineering and construction.

The Corporation's stock is listed on the Taiwan Stock Exchange. As of June 30, 2006, the Ministry of Finance (succeeding the Ministry of Economic Affairs), Republic of China owned 23% of the Corporation's outstanding common stock.

As of June 30, 2006 and 2005, the Corporation had about 8,700 employees.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements have been prepared in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers and accounting principles generally accepted in the Republic of China (ROC). Under these guidelines and principles, the Corporation is required to make certain estimates and assumptions on recorded assets, liabilities, revenues and expenses, including those related to doubtful accounts, inventory loss, depreciation of properties, impairment loss on assets, pension and loss on lawsuits. Actual results could differ from these estimates.

For the convenience of readers, the accompanying financial statements have been translated into English from the original Chinese version prepared and used in the Republic of China. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language financial statements shall prevail. However, the accompanying financial statements do not include the English translation of additional disclosures that are not required under generally accepted accounting principles but are required by the Securities and Futures Bureau (SFB, formerly the Securities and Futures Commission before July 1, 2004) for their oversight purposes.

The Corporation's significant accounting policies are summarized as follows:

Current and Noncurrent Assets and Liabilities

Current assets include unrestricted cash and cash equivalents and other assets to be realized in cash or to be consumed within 12 months from the balance sheet date. Properties and other assets which do not belong to current assets are classified as non-current. Liabilities to be settled within 12 months from the balance sheet date are classified as current. Liabilities which do not belong to current liabilities are classified as noncurrent.

Cash Equivalents

Cash equivalents are short-term notes and bills with maturities of three months or less. The carrying value of cash equivalents approximates fair value.

Financial Assets at Fair Value Through Profit or Loss

Financial instruments (mainly open-end funds) are recognized as financial assets at fair value through profit or loss to remove significantly accounting inconsistency. These financial instruments are initially recognized at fair value plus transaction costs. When subsequently measured at fair value, the changes in fair value are recognized in current income. A regular way to purchase or sell financial assets is recorded using trade date accounting.

Fair value is based on the closing price on balance sheet date for listed stocks, based on net asset value on balance sheet date for open-end funds, and based on the quotation price by financial institution for bank debentures.

Available-for-sale Financial Assets

Available-for-sale financial assets are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition. When subsequently measured at fair value, the changes in fair value are excluded from earnings and reported as a separate component of stockholders' equity. The accumulated gains or losses are recognized in earnings when the financial asset is derecognized from the balance sheet. A regular way to purchase or sell financial assets is recorded using trade date accounting.

Cash dividends received from and after the year of investment acquisition are recognized as income in the period received. Stock dividends are recognized only as an increase in the number of shares of stock held on the ex-dividend date. Costs of investments sold are determined by the weighted-average method.

If there is objective evidence that a financial asset is impaired, an impairment loss is recognized. If, in a subsequent period, the amount of the impairment loss decreases, for equity securities, the previously recognized impairment loss is reversed to the extent of the decrease and recorded as an adjustment to stockholders' equity; for debt securities, the amount of the decrease is recognized in earnings, provided that the decrease is clearly attributable to an event which occurred after the impairment loss was recognized.

Factoring of Accounts Receivable

The following three conditions must be met to recognize factoring of accounts receivable:

a. The accounts receivable have been legally isolated from the Corporation.

b. The transferees have obtained the right to pledge or exchange accounts receivable, which are either the transferred accounts receivable or beneficial interest in the transferred assets.

c. The transferor does not maintain effective control, through an agreement to repurchase or redeem the transferred accounts receivable before their maturity, over the transferred accounts receivable.

If the three conditions are met, the difference between the proceeds and the face value of the accounts receivable is recognized as a loss and recorded as nonoperating expenses.

Inventories

Inventories are raw materials, supplies, fuel, finished products, work in process and by-products. Inventories are stated at the lower of total moving-average cost or market value. Market value is the net realizable value for finished products, work in process and by-products, and replacement costs for raw materials, supplies and fuel.

Financial Assets Carried at Cost

Investment that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are carried at original cost, such as non-publicly traded stocks and mutual funds. The costs of funds and non-publicly traded stocks are determined using the weighted-average method. If there is objective evidence that a financial asset is impaired, an impairment loss is recognized. No recording of a subsequent recovery in fair value is allowed.

The accounting treatment for cash dividends and stock dividends on financial assets carried at cost is the same as that for cash and stock dividends on available-for-sale financial assets.

Investment in Bonds Without Quoted Price

Investment that does not have a quoted market price in an active market and the receipt upon maturity is fixed or definite is carried at the amortized cost. Those financial assets are initially recognized at fair value plus transaction cost that are directly attributable to the acquisition. Earning or losses are recognized at the time of derecognition, impairment or amortization.

If there is objective evidence that a financial asset is impaired, an impairment loss is recognized. If, in a subsequent period, the amount of the impairment loss decreases and the decrease is clearly attributable to an event which occurred after the impairment loss was recognized, the previously recognized impairment loss is reversed to the extent of the decrease. The reversal should not result in a carrying amount of the financial asset that exceeds the amortized cost that would have been determined if no impairment loss had been recognized.

Long-term Stock Investment - Equity Method

Long-term stock investments in which the Corporation owns 20% or more of the outstanding voting shares or where the Corporation has significant influence on the investees are accounted for by the equity method. When the equity method is first applied or when a stock is acquired, the difference between the carrying value of an investment and the proportionate equity in the investee is amortized over five years.

Effective January 1, 2006, pursuant to the revised Statement of Financial Accounting Standard No.5 “Long-term Investment in Equity Securities” (SFAS No. 5), investment premiums, representing goodwill, are no longer being amortized, but annual impairment test is required. The investment discounts, representing the fair value of identifiable net assets acquired over investment costs, are allocated proportionately based on the fair values of noncurrent asset amounts and any remaining unallocated balance is recorded as extraordinary income. The investment discounts existed prior to January 1, 2006 will continue to be amortized over five years.

If an investee issues additional shares and the Corporation acquires shares at a percentage different from its current equity in the investee, capital surplus is adjusted for the difference between the carrying values of the investments and the Corporation’s equity in the investee’s net assets. If the carrying value is less than equity in net assets, the difference is added to capital surplus. If the carrying value is more than equity in net assets, the difference is deducted from capital surplus, or from unappropriated earnings when capital surplus is not enough for debiting purposes.

If the market prices of investees significantly decline below carrying value and the decline is permanent, the investment loss should be recognized as realized loss in the same year of the decline. This investment will be revalued if an investee’s market value becomes higher than book value per share. The difference between the new cost of the investment and the proportionate equity in the investee is amortized over five years.

Properties

Properties are stated at cost or at cost plus appreciation, less accumulated depreciation except the land. Interest expense for the purchase or construction of properties is capitalized as property cost. Major additions, renewals and betterments are capitalized, while maintenance and repairs are expensed currently.

Depreciation is calculated by the straight-line method over service lives estimated as follows: land improvements, 10 to 40 years; buildings and improvements, 5 to 60 years; machinery and equipment, 3 to 25 years; transportation equipment, 3 to 25 years; and miscellaneous equipment, 3 to 10 years. Depreciation on appreciation is calculated by the straight-line method over the remaining service lives of the revalued assets. When a property reaches its residual value but is still in use, its residual value is depreciated over its reestimated service life.

Upon sale or other disposal of properties, the related cost, appreciation and accumulated depreciation are removed from the accounts. Gains or losses are credited or charged to current income.

Rental Assets

Rental assets (included in other assets) are stated at the lower of carrying value or recoverable value.

Asset Impairment

Assets (primarily properties, rental assets and long-term investments under the equity method) are evaluated on the basis of their recoverable value. If the recoverable value is less than the carrying value of the assets, the decline is charged to impairment loss and accumulated impairment loss is established. If the value of the impaired assets recovers, the accumulated impairment loss will be reversed. However, the loss reversal is only to the extent that the increased carrying amount of an asset does not exceed the asset carrying amount (net of depreciation) that would have been determined had no impairment loss been recognized in prior years.

Unamortized Repair Costs

Unamortized repair costs refer to the major repairs of blast furnaces and are amortized over five years.

Treasury Stock

The Corporation reacquired its issued shares in accordance with government regulations and recorded this reacquisition as treasury stock at cost, which is presented as a deduction to stockholders’ equity.

Effective 2002, the Corporation’s shares acquired and held by subsidiaries are reclassified to treasury stock from long-term investments and accounted for at the carrying value recorded by subsidiaries for short-term or long-term investments as of January 1, 2002.

Effective 2005, the revised Statement of Financial Accounting Standards No. 7, “Consolidated Financial Statements”, requires that equity-method investees that are not majority-owned but over which the Corporation has controlling capability in substance are deemed as subsidiaries. Thus, the Corporation’s shares held by these investees are treated as treasury stock.

Revenue Recognition and Allowance for Doubtful Accounts

Revenues are recognized when titles to products and risks of ownership are transferred to customers as follows: domestic sales - when products are delivered out of the Corporation’s premises to customers; exports - when products are loaded onto vessels.

Sales are measured at fair value, which is the price (net of any trade discounts and sales discounts) agreed to by the Corporation and customers. But if the related receivable is due within one year, the difference between its present value and receivable amount is immaterial, and sales transactions are frequent, the fair value of receivables is equivalent to the nominal amount of cash to be received.

An allowance for doubtful receivable is provided based on a review of the collectibility of accounts receivable. The Corporation determines the amount of allowance for doubtful receivable by examining the aging analysis of outstanding accounts receivable and current trends in the credit quality of its customers.

Capitalization and Expense

Expenditure which amount is significant and has future economic benefits is classified as asset; otherwise is classified as expense or loss.

Pension

Pension costs under defined benefits pension plan are recognized on the basis of actuarial calculations. The difference between the actuarial pension cost and the amount appropriated to a special fund (Note 17) is recognized as accrued pension liability (included in accrued expenses) or prepaid pension. Unamortized net transition assets and actuarial gains or loss are amortized over 11 years and the average remaining service life of employees, respectively.

Pension costs under defined contribution plan are recognized based on contributions made by the Corporation to the employees' individual accounts.

Income Tax

Income tax is provided based on inter-period and intra-period allocation basis. Tax effects of deductible temporary differences are recognized as deferred income tax assets. Valuation allowance is provided for deferred tax assets with uncertain realizability. Tax effects of taxable temporary differences are recognized as deferred tax liabilities. A deferred tax asset or liability is classified as current or noncurrent depending on the classification of the related asset or liability for financial reporting. But if the deferred income tax asset or liability cannot be related to an asset or liability for financial reporting, the classification is based on the expected reversal or realization date of the temporary difference.

Tax credits arising from expenditures for purchases of equipment, research and development, employees' training, and investment in newly emerging, important and strategic industries are recognized when those credits are granted.

Adjustments of prior years' tax liabilities are added to or deducted from the current year's tax expense.

Annual earnings are appropriated under a resolution adopted in the stockholders' meeting in the year following the year of earnings generation. Under tax regulations, unappropriated earnings generated after 1998 are subject to 10% income tax. This tax is recorded as expenses in the year when the stockholders resolve to retain the earnings.

Foreign-currency Transactions

Foreign-currency transactions, except derivative transactions, are recorded in New Taiwan dollars at the rates of exchange in effect when the transactions occur. Gains or losses resulting from the application of prevailing exchange rates when foreign-currency assets and liabilities are settled or converted, are credited or charged to income in the year of settlement or conversion. On the balance sheet date, foreign-currency monetary assets and liabilities are restated at the spot exchange rates, and resulting differences are accounted for as follows:

a. Equity-method stock investments - as cumulative translation adjustments under stockholders' equity;

b. Other assets and liabilities - as credits or charges to current income.

The spot exchange rates use the middle price of the main correspondent bank.

Hedge Accounting

The Corporation uses financial instruments to hedge the currency change of a net investment in a foreign operation. The hedge is attributable to fair value hedge and using the non-derivative financial instruments to be the hedge tools.

For the fair value hedge, both the fair value change of the investments and financial instruments are recorded as gain or loss in the current period.

The Corporation uses the hedge activities to control the net investment currency exchange and fair value risk.

Reclassification

As stated in Note 3, certain accounts for the period ended June 30, 2005 had been reclassified to conform to the classifications in 2006.

As of June 30, 2006, according to the regulation change, the revaluation increment on assets of $1,535,363 thousand included in capital surplus had been reclassified to other item under the stockholders' equity.

3. ACCOUNTING CHANGES

Effective 2006, the Corporation adopted the newly issued Statement of Financial Accounting Standards No.34 "Accounting of Financial Instruments", No.36 "Disclosure and Presentation of Financial Instruments" and the related revisions of previously released SFASs.

a. Effect of adopting the newly released SFASs and related revisions of previously released SFASs

   The Corporation had properly categorized its financial assets and liabilities upon initial adoption of the newly released SFASs and related revisions of previously released SFASs. The adjustments made to the carrying amounts of the financial instruments categorized as financial assets or financial liabilities at fair value through profit or loss were included in the cumulative effect of changes in accounting principles; on the other hand, the adjustments made to the carrying amounts of those categorized as financial assets carried at cost and available-for-sale financial assets were recognized as adjustments to shareholders' equity.

   In addition, the foreign-currency investment under cost method is reclassified as financial assets carried at cost were revalued based on the historical exchange rate at initial investment date and adjustment was made to cumulative translation adjustment recorded in shareholders' equity and related financial assets.

   The Corporation also reassessed the hedge effectiveness for the equity investment in East Asia United Steel Corporation and adjusted the exchange loss of $193,641 thousand previously recorded to cumulative effect of changes in accounting principles.

The effect of adopting the newly released SFASs is summarized as follows:

	Recognized as Cumulative Effect of Changes in Accounting Principles (Net of Tax)	Recognized as a Separate Component of Stockholders' Equity (Net of Tax)
Financial assets at fair value through profit or loss	$ 155,819	$ -
Available-for-sale financial assets	-	3,936,398
Financial assets carried at cost	(193,641)	261,188
	$ (37,822)	$ 4,197,586

The net effect of the change in accounting principles is not significant to the Corporation's net income and basic earnings per share for the six months ended June 30, 2006.

b. Reclassifications

Upon the adoption of SFAS No.34, certain accounts in the financial statements as of and for the six months ended June 30, 2005 were reclassified to conform with the financial statements as of and for the six months ended June 30, 2006. The previously issued financial statements as of and for the six months ended June 30, 2005 is not required to be restated.

Certain accounting policies prior to the adoption of the newly released SFASs are summarized as follows:

1) Short-term investments

Short-term investments that were publicly-traded, easily converted to cash, and not acquired for the purpose of controlling the investees or establishing close business relationship with the investees were carried at the lower of cost or market value at the balance sheet date, with any temporary decline in value charged to current income. The market value of publicly-traded stocks was determined using the average-closing prices for the last month of the period.

2) Long-term stock investment

Long-term stock investments in which the Corporation owns less than 20% of the outstanding voting shares or where the Corporation has no significant influence on the investees are accounted for by the cost method. The investments listed on the Taiwan Stock Exchange are stated at the lower of total cost or market value and unrealized loss on long-term investment is classified as a deduction item of the stockholders' equity.

On the balance sheet date, foreign-currency assets and liabilities are restated at the prevailing exchange rates, and resulting differences are accounted for as cumulative translation adjustments under stockholders' equity if restated balances are lower than their costs; otherwise, no adjustment is made.

Certain accounts in the financial statements as of and for the six months ended June 30, 2005 have been reclassified to conform to the classifications prescribed by the newly released and revised SFASs. The reclassifications of certain accounts are summarized as follows:

	Before Reclassification	After Reclassification
Balance sheet		
Short-term investments	$ 13,149,677	$ -
Long-term investments	13,137,737	-
Unrealized loss on long-term investments	(446,463)	-
Financial assets at fair value through profit or loss	-	11,931,521
Available-for-sale financial assets - current	-	1,218,156
Available-for-sale financial assets - noncurrent	-	1,001,210
Investment in bonds without quoted price- noncurrent	-	5,834,325
Financial assets carried at cost - noncurrent	-	6,302,202
Unrealized gain (loss) on financial instrument	-	(446,463)

Effective January 1, 2006, the Corporation adopts amended SFAS No.1 “Conceptual Framework for Financial Accounting and Preparation of Financial Statements”, No.5 ”Long-Term Investment under Equity Method” and No.25 “Business Combinations.” The amendment of the previous SFASs mainly included the difference between the carrying value of investment and the proportionate equity shall be analyzed, and goodwill should be tested for impairment annually and is no longer being amortized. Such change did not have significant effect on the Corporation’s financial statements as of and for the six months ended June 30, 2006.

c. Revision of the Commercial Accounting Law

Certain accounts in the financial statements as of and for the six months ended June 30, 2005 have been reclassified to conform to the revision of Commercial Accounting Law. The reclassification of the account balances was as follows:

	Before Reclassification	After Reclassification
Capital surplus	$ 1,535,363	$ -
Revaluation increment on assets – stockholders’ equity	-	1,535,363

4. CASH AND CASH EQUIVALENTS

	June 30, 2006	June 30, 2005
Cash on hand	$ 18,567	$ 18,605
Checking accounts and demand deposits	2,468,140	2,384,422
Time deposits	2,150,000	14,202,132
Negotiable certificates of time deposits	8,200,000	500,000
Cash equivalents - short-term notes and bills	8,680,249	33,705,127
	$ 21,516,956	$ 50,810,286

As of June 30, 2006, the Corporation’s foreign bank deposits is $1,069 thousand (￥3,784 thousand) in Japan-Osaka.

5. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

This mainly represents open-end funds. As of June 30, 2006 and 2005, the balances of financial assets at fair value through profit or loss were $17,231,571 thousand and $11,931,521 thousand, respectively. The purpose of reclassifying open-end funds in this account is to remove the accounting inconsistency between investment income and interest expense.

Net gain arising from the financial assets at fair value through profit or loss for the six months ended June 30, 2006 was $81,490 thousand (including gain on appraisal and disposal of financial assets).

6. AVAILABLE-FOR-SALE FINANCIAL ASSETS

	June 30, 2006		June 30, 2005	
	Current	Noncurrent	Current	Noncurrent
Listed stock				
Maruichi Steel Tube Ltd.	$ -	$ 757,920	$ -	$ 757,920
Advanced Material Technology Corporation (AMTC)	-	243,290	-	243,290
Taiwan Semiconductor Manufacturing Company (TSMC)	967,456	-	967,456	-
Bank debentures - Taiwan Cooperative Bank	250,580	-	250,700	-
Allowance for appraisal	3,085,736	628,876	-	-
	$ 4,303,772	$ 1,630,086	$ 1,218,156	$ 1,001,210

The unrealized loss on abovementioned financial assets which was determined at fair value as at June 30, 2006 was $228,442 thousand.

The Corporation has borrowed foreign - currency bank loans to hedge exchange rate fluctuations on the investments in Maruichi Steel Tube Ltd. (Notes 16 and 26)

7. NOTES AND ACCOUNTS RECEIVABLE

The Corporation entered into two factoring accounts receivable contracts (without recourse) with The International Commercial Bank of China (ICBC) and Bank of Taiwan for the facilities of $5.84 billion and $2.5 billion, respectively. Under the contracts, the Corporation is empowered to sell accounts receivable to the banks upon the delivery of products to customers and is required to complete related formalities at the following bank working day.

The Corporation entered into a purchasing commercial papers contract, which was due on October 31, 2005, with Chung Hsing Bills Finance Corporation for the facility of $2.5 billion. Customers issued commercial papers to the Corporation upon the Corporation’s delivery of its products. The commercial papers were sold to Chung Hsing Bills Finance Corporation (without recourse) upon the Corporation’s endorsements.

As of June 30, 2006, there was no outstanding endorsed commercial paper.

The related information for the Corporation’s sale of its notes and accounts receivable for the six months ended June 30, 2006 and 2005 is as follows:

Transaction Counter-Party	Total Factoring Amounts	Related Expenses	Proceeds Received	Interest Rate (%)
2006				
Accounts receivable				
International Commercial Bank of China	$ 6,059,232	$ 35,879	$ 6,023,353	1.57-1.95
Bank of Taiwan	517,549	3,038	514,511	1.57-1.95
	$ 6,576,781	$ 38,917	$ 6,537,864	
2005				
Notes receivable				
Chung Hsing Bills Finance Corporation	$ 1,581,059	$ 9,376	$ 1,571,683	1.70-1.95
Accounts receivable				
International Commercial Bank of China	2,992,352	19,510	2,972,842	1.64-1.95
Bank of Taiwan	1,516,742	10,303	1,506,439	1.64-3.83
	4,509,094	29,813	4,479,281	
	$ 6,090,153	$ 39,189	$ 6,050,964	

8. INVENTORIES

	June 30, 2006	June 30, 2005
Finished products	$ 4,221,976	$ 4,904,862
Work in process	12,428,085	8,678,379
Raw materials	6,987,139	7,764,918
Supplies	5,437,534	4,691,276
Fuel	121,616	82,910
Materials in transit and others	1,085,038	2,667,136
Others	676,906	125,942
	30,958,294	28,915,423
Less: Allowance for losses	-	159,556
	$ 30,958,294	$ 28,755,867

9. FINANCIAL ASSETS CARRIED AT COST

	June 30, 2006	June 30, 2005
Common stocks without quoted market prices		
Industrial Bank of Taiwan	$ 1,000,000	$ 1,000,000
CDIB & Partners Investment Holding Corporation	500,000	500,000
Asia Pacific Broadband Telecom Co., Ltd. (APBT)	240,000	240,000
Phalanx Biotech Group Corporation (PBG)	105,370	105,370
CDIB BioScience Ventures I, Inc. (CBVI)	102,000	120,000
Overseas Investment & Development Corporation	50,000	50,000
CTB I Venture Capital Co., Ltd.	50,000	50,000

(Continued)

	June 30, 2006	June 30, 2005
GenMont Biotech Inc. (GMB)	$ -	$ 31,337
Kaohsiung Arena Development Corp. (KADC)	-	135,000
Tang Eng Iron Works Corporation (TEIWC)	-	-
Preferred stocks without quoted market prices		
East Asia United Steel Corporation (EAUS)	2,822,500	2,864,000
Dragon Steel Corporation	999,877	999,877
Fund - Sino-Canada Biotechnology Development Fund, LP (SCBDF)	179,263	206,618
	$ 6,049,010	$ 6,302,202

The stocks which have quoted prices and their fair value cannot be measured reliably were classified as financial assets carried at cost.

In June 2006, CBVI reduced its capital and returned $18,000 thousand to the Corporation.

In May 2003, the Corporation signed a slab production joint-venture contract with Sumitomo Metal Industries, Ltd. and Sumitomo Corporation. In July 2003, the joint venture company of East Asia United Steel Corporation (EAUS) was established. As of June 30, 2006, the Corporation had invested in EAUS the amount of ￥10 billion (Notes 16 and 26). The Corporation thus enjoys a stable supply of good quality slab from this joint venture. The Corporation also signed a contract with Chung Hung Steel Corporation (CHSC) to transfer the purchasing right of slabs from EAUS, and the Corporation receives premiums on this contract based on the volume purchased by CHSC.

The Corporation promised to invest 100 units ($10,000 thousand Canadian dollars) in the SCBDF fund. As of June 30, 2006, the Corporation had invested $219,025 thousand (CAD$9,435 thousand) in SCBDF fund, representing 94.35% of total investments committed to invest. The difference between the above cumulative investment and the carrying value was cash dividends received by the Corporation.

In 2005, the Corporation recognized an impairment loss of $906,000 thousand (recorded as nonoperating expense) on its investment in APBT.

10. INVESTMENT IN BONDS WITHOUT QUOTED PRICE

	June 30, 2006	June 30, 2005
Taiwan High Speed Rail Corporation		
Preferred C (THSRC)	$ 4,646,991	$ 4,699,941
Preferred B (THSRC)	934,384	984,384
Taigen Biotechnology Co., Ltd. (TBC)	300,000	150,000
	$ 5,881,375	$ 5,834,325

In September 2003, the Corporation acquired 100,000 thousand Preferred B shares of THSRC for $1,000,000 thousand. Dividend on these shares is at 5%, payable on a nonparticipating and cumulative basis, these shares could be prolonged for 13 months before the due date within six years from the acquisition date. In April 2005 and August 2004, the Corporation acquired additional 505,370 thousand Preferred C shares of THSRC for $3,199,944 thousand and $1,499,997 thousand, respectively. These shares, which may be converted to common shares within four years from the acquisition date, have a 9.5% dividend in the first two years and 0% in the next two years. At the end of four years, i.e., in 2009 and 2008, if the Corporation has not converted the preferred shares into common shares and THSRC cannot redeem the shares, the unredeemed shares will have 4.71% dividends. THSRC builds and operates public transportation systems.

In November 2005 and March 2004, the Corporation totally acquired 20,000 thousand preferred shares of TBC for $300,000 thousand. Preferred shareholders are entitled to 8% participating and noncumulative dividends as well as voting and election rights. TBC mainly researches and develops drugs. The Corporation can request TBC to redeem all or part of preferred shares by issuing new stock or its own retained earning after July of 2007.

11. LONG-TERM STOCKS INVESTMENT - EQUITY METHOD

	June 30, 2006		June 30, 2005	
	Amount	% of Owner-ship	Amount	% of Owner-ship
Stocks listed on the Taiwan Stock Exchange				
Chung Hung Steel Corporation (CHSC)	$ 1,854,393	24	$ 2,308,110	24
China Steel Chemical Corporation (CSCC)	1,070,666	30	934,346	30
China Hi-ment Corporation (CHC)	597,111	20	551,896	20
China Steel Structure Corporation (CSSC)	506,523	18	461,499	18
China Ecotek Corporation (CEC)	377,729	36	387,543	36
	4,406,422		4,643,394	
Less: Shares held by subsidiaries accounted for as treasury stock	327,280		326,068	
	4,079,142		4,317,326	
Stocks with no quoted market prices				
Dragon Steel Corporation (DSC)	15,453,207	47	1,612,101	37
Gains Investment Corporation (GIC)	8,067,835	100	5,630,048	100
C. S. Aluminum Corporation (CAC)	6,997,897	100	6,665,590	98
China Steel Express Corporation (CSE)	6,883,171	100	6,442,966	100
China Prosperity Development Corporation (CPDC)	4,653,350	100	4,763,682	100
Kaohsiung Rapid Transit Corporation (KRTC)	3,087,703	31	3,195,392	31
China Steel Asia Pacific Holdings Pte. Ltd. (CSAPH)	2,469,880	100	2,926,722	100
Goang Yaw Investment Corporation and other two companies	1,285,222	99	1,574,126	99
China Steel Global Trading Corporation (CSGT)	943,005	100	932,084	100
China Steel Machinery Corporation (CSMC)	824,279	100	768,931	100
Info-Champ Systems Corporation (ICSC)	538,588	100	498,434	99
Taiwan Rolling Stock Co., Ltd. (TRSC)	250,974	22	154,615	27
China Steel Security Corporation (CSS)	232,077	100	221,602	100
Kaohsiung Arena Development Corporation (KADC)	189,799	18	-	-
Baolai Greeting Development Co., Ltd. (BGDC)	52,235	45	-	-
Hi-mag Magnetic Corporation (HMC)	43,635	50	-	50
China Steel Management Consulting Corporation (CSMCC)	6,989	38	6,196	38
TaiAn Technologies Corporation (TTC)	3,726	17	2,681	17
	51,983,572		35,395,170	
Less: Shares held by subsidiaries accounted for as treasury stock	980,545		1,309,007	
	51,003,027		34,086,163	

(Continued)

	June 30, 2006		June 30, 2005	
	Amount	% of Owner-ship	Amount	% of Owner-ship
Prepaid long-term stock investments				
Dragon Steel Corporation	$ -		$ 13,230,426	
	$ 55,082,169		$ 51,633,915	

As of June 30, 2006 and 2005, the Corporation's total equity in CHSC was 39%, including directly owned - 24% and indirectly owned - 15%. The Corporation's total equity in TTC was 22%, including directly owned - 17% and indirectly owned through CSCC - 5%. In March 2005 and November 2004, the Corporation had invested in KADC $135,000 thousand totally and invested additionally $63,000 thousand in June 2006. The subsidiary - CPDC also invested in KADC in April 2006, thus, the Corporation's total equity in KADC was 34%, including directly owned - 18% and indirectly owned by CPDC - 16%. Accordingly, the long-term investment in KADC accounted for by cost method was changed to equity method.

In 2005, DSC issued additional shares and declared stock dividends for its preferred stock. The Corporation further increased its investment in DSC by 980,032 thousand shares for $13,230,426 thousand ($13.50 per share) and common stock dividends appropriated from DSC received by the Corporation. The Corporation's equity in DSC increased from 37% to 47%.

In August 2005, CSAPH reduced its capital and returned US$18,000 thousand (29,455 thousand shares) to the Corporation.

In May 2006, the Corporation invested $54,000 thousand to acquire 5,400 thousand shares of BGDC, representing 45% equity. The Corporation plans to totally invest in BGDC $216,000 thousand. BGDC will engage in hotel business and is currently in development stage.

The market value of listed stocks was $9,339,260 thousand and $8,999,641 thousand based on the closing prices on June 30, 2006 and average closing prices in June 2005, respectively.

The Corporation's Board of Directors approved plans for additional investments in Wuxi Teco Electric & Machinery Co., Ltd., DSC, TRSC, etc. The related subscription schedule depends on the investees' capital increase requirements. As of June 30, 2006, the Corporation's future infused capital in these investees aggregated $5,367,764 thousand.

Investment income (loss) under the equity method was as follows:

	For the six months Ended June 30	
	2006	2005
CSE	$ 1,767,523	$ 1,435,918
CHSC (including Goang Yaw Investment Corporation and two other Subsidiaries)	1,183,574	790,209
CAC	366,967	163,064
GIC	363,363	191,325
DSC	330,765	96,786
CSCC	176,282	150,670
CSGT	152,245	179,053
CSAPH	94,040	219,279
CHC	73,403	66,383

(Continued)

	For the six months Ended June 30	
	2006	2005
HMC	$ 44,676	$ -
CSSC	36,810	181,880
ICSC	34,829	37,096
CEC	(703)	23,778
CSMC	(9,520)	73,395
KRTC	(22,704)	18,846
Others	12,843	9,705
	$ 4,604,393	$ 3,637,387

Above investment income (loss) was recognized based on the investees' audited financial statements.

The Corporation prepared the consolidated financial statements including majority-owned and controlled-in-substance subsidiaries in accordance with the related regulations.

12. PROPERTIES

	Cost	Appreciation	Total
June 30, 2006			
Cost and appreciation			
Land	$ 8,049,199	$ 5,840,732	$ 13,889,931
Land improvements	4,212,123	492,990	4,705,113
Buildings and improvements	36,417,175	2,424,237	38,841,412
Machinery and equipment	214,004,352	8,717,718	222,722,070
Transportation equipment	1,468,257	33,748	1,502,005
Miscellaneous equipment	3,131,885	31,795	3,163,680
	267,282,991	17,541,220	284,824,211
Accumulated depreciation			
Land improvements	3,157,499	427,269	3,584,768
Buildings and improvements	15,824,222	1,651,353	17,475,575
Machinery and equipment	167,815,773	8,715,296	176,531,069
Transportation equipment	1,193,190	33,732	1,226,922
Miscellaneous equipment	2,426,716	31,780	2,458,496
	190,417,400	10,859,430	201,276,830
Constructions in progress	23,009,039	-	23,009,039
	$ 99,874,630	$ 6,681,790	$ 106,556,420
June 30, 2005			
Cost and appreciation			
Land	$ 7,712,475	$ 5,840,732	$ 13,553,207
Land improvements	4,231,666	492,990	4,724,656
Buildings and improvements	36,028,949	2,425,010	38,453,959
Machinery and equipment	212,832,259	8,862,195	221,694,454
Transportation equipment	1,526,533	33,748	1,560,281
Miscellaneous equipment	3,046,602	32,464	3,079,066
	265,378,484	17,687,139	283,065,623

(Continued)

	Cost	Appreciation	Total
Accumulated depreciation			
Land improvements	$ 3,046,606	$ 416,141	$ 3,462,747
Buildings and improvements	14,933,639	1,595,124	16,528,763
Machinery and equipment	162,573,040	8,857,622	171,430,662
Transportation equipment	1,236,202	33,722	1,269,924
Miscellaneous equipment	2,329,483	32,449	2,361,932
	184,118,970	10,935,058	195,054,028
Constructions in progress	13,139,455	-	13,139,455
	$ 94,398,969	$ 6,752,081	$ 101,151,050

In 1981 and 1994, the Corporation revalued its properties and patents in accordance with government regulations, resulting in an increment of $17,662,343 thousand. After the deduction of the reserve for land value increment tax of $3,370,813 thousand, an increment of $14,291,530 thousand was credited to revaluation increment on assets. As of June 30, 2006, revaluation increment on assets totaling $13,952,356 thousand have been transferred to capital stock, reducing the balance of revaluation increment on assets to $339,174 thousand. In January 2005, the government revised the land increment tax law to reduce the tax rate. Thus, the reserve for land value increment tax decreased and the revaluation increment on assets increased each by $1,196,189 thousand.

In 2005, the Corporation decreased reserve for land value increment tax by $3,500 thousand resulting from sale of its land. As of June 30, 2006, the balance of reserve for land value increment tax amounted to $2,171,124 thousand. In January 2005, the Corporation repurchased land from CPDC for $834,673 thousand, and after offsetting unrealized gain on intercompany transaction of $268,876 thousand which occurred in 1999, the actual purchase cost was $565,797 thousand.

13. RENTAL ASSETS - NET

	June 30, 2006	June 30, 2005
Land - at cost	$ 2,966,398	$ 2,966,398
Machinery and equipment - at cost	2,000,000	2,000,000
Less: Accumulated depreciation	1,320,198	1,290,997
Accumulated impairment loss	594,000	594,000
	85,802	115,003
	$ 3,052,200	$ 3,081,401

The Corporation has leased some of its plant property and machinery to its subsidiaries (Note 23).

14. SHORT-TERM BANK LOANS AND OVERDRAFT

	June 30, 2006	June 30, 2005
Letters of credit - due within 180 days; interest at 0.34%-6.036% p.a. and 0.24%-6.038% p.a. as of June 30, 2006 and 2005, respectively	$ 1,291,806	$ 1,571,664
Overdraft - interest at 1.2685%-1.427% p.a. and 0.9%-2.52% p.a. as of June 30, 2006 and 2005, respectively	3,201,512	1,546,720
Short-term loans from related parties (Note 23)	-	569,106
Credit loans - interest at 1.518%-1.6% p.a. and 1.264%-1.265% p.a. as of June 30, 2006 and 2005, respectively	12,200,000	6,000,000
	$ 16,693,318	$ 9,687,490

Time deposits aggregating $4,600,000 thousand as of June 30, 2006 and 2005, respectively, have been pledged as collateral for bank overdraft.

15. LONG-TERM BONDS PAYABLE

	June 30, 2006	June 30, 2005
5-year unsecured bonds - issued at par in:		
June 2006; repayable in June 2011; 2.32% interest p.a., payable annually	$ 8,100,000	$ -
November 2001; repayable in November 2006; 3.1% interest p.a., payable annually	3,500,000	3,500,000
November 2001; repayable in November 2006; 3.0763% interest p.a., compounded semiannually and payable annually	1,500,000	1,500,000
June 2001; repayable in June 2006; 4.27% interest p.a., payable annually	-	5,000,000
November 2000; repayable in December 2005; 5.18% interest p.a., payable annually	-	5,000,000
	13,100,000	15,000,000
Current portion	5,000,000	10,000,000
	$ 8,100,000	$ 5,000,000

16. LONG-TERM DEBTS

	June 30, 2006	June 30, 2005
Repayable in July 2010 (￥4.4 billion); floating rates at 0.3525% and 0.2168% p.a. as of June 30, 2006 and 2005, respectively	$ 1,241,900	$ 1,261,040
Repayable in December 2006 (￥2.6 billion); floating rates at 0.594% and 0.2160% p.a. as of June 30, 2006 and 2005, respectively	733,850	745,160
Repayable in July 2010 (￥2.2 billion); floating rates at 0.6240% and 0.2590% p.a. as of June 30, 2006 and 2005, respectively	620,950	630,520

(Continued)

	June 30, 2006	June 30, 2005
Repayable in July 2010 (￥3.3 billion); floating rates at 0.4506% and 0.3550%; p.a. as of June 30, 2006 and 2005, respectively	$ 931,425	$ 945,780
	3,528,125	3,582,500
Current portion	733,850	-
	$ 2,794,275	$ 3,582,500

As of June 30, 2006, the Corporation had long-term bank loans in yen to hedge the exchange rate fluctuations on the investments in yen in East Asia United Steel Corporation and Maruichi Steel Tube Ltd. (Note 26).

17. PENSION PLAN

The Labor Pension Act (the "Act") became effective on July 1, 2005. The Corporation's regular employees hired before June 30, 2005 have chosen to continue their pension plan under the Labor Standards Law (those employees may change their choice to the "Act" before July 1, 2010) or have chosen the pension plan under the Act, but retained their employment seniority earned until June 30, 2005. Employees hired after July 1, 2005 can only adopt the pension plan under the Act.

Under the Act, a defined contribution plan, the Corporation makes monthly contribution to employees' personal retirement account at amounts equal to 6% of the salaries and wages of employees.

The pension costs are as follows:

	For the six months Ended June 30	
	2006	2005
Under Labor Standards Law	$ 711,422	$ 676,762
Under Labor Pension Act	3,835	-
	$ 715,257	$ 676,762

The Corporation has a retirement plan in accordance with the Labor Standards Law. Retirement benefits are based on employee's length of service and his/her average salaries and wages of the last six months before retirement.

The Corporation makes contributions, equal to a certain percentage of salaries, to a pension fund, which is deposited in the Central Trust of China in the name of, and administered by the employees' pension fund administration committee. The changes in the fund are summarized as follows:

	For the six months Ended June 30	
	2006	2005
Balance, beginning of period	$ 11,759,018	$ 10,503,035
Contributions	895,008	673,559
Gains	248,241	117,438
Payment of benefits	(162,116)	(70,702)
Balance, end of period	$ 12,740,151	$ 11,223,330

Since August 1999, the Corporation has also made contributions, equal to a certain percentage of salaries of management personnel (vice presidents and above), to another pension fund, which is deposited in the International Commercial Bank of China in the name of, and administered by an officers' pension fund management committee. The changes in the fund are summarized as follows:

	For the six months Ended June 30	
	2006	**2005**
Balance, beginning of period	$ 14,478	$ 9,982
Contributions	2,142	2,602
Interest income	132	69
Payment of benefits	(1,290)	-
Balance, end of period	$ 15,462	$ 12,653

Pension costs recognized based on actuarial calculations for the six months ended June 30, 2006 and 2005 were $711,422 thousand and $665,668 thousand, respectively.

18. DEFERRED CREDITS - GAIN ON INTERCOMPANY TRANSACTIONS

	June 30, 2006	**June 30, 2005**
Gain on disposal of land	$ 1,136,164	$ 1,136,164
Gain on contracted projects	9,118	12,278
	$ 1,145,282	$ 1,148,442

A deferred income of $1,405,040 thousand was the unrealized gain from the sale of land to CPDC in February 1999. The Corporation repurchased some of the land in the first half of 2005 for the construction of office building and thus the deferred credits decreased by $268,876 thousand. The remaining deferred credit will be recognized as income when CPDC sells the rest of the land to third parties.

The Corporation obtained building construction projects from KRTC, resulting in deferred revenue. The accumulated credits will be recognized as income over the service lives of the buildings after completion of the construction, expected in 2007.

19. STOCKHOLDERS' EQUITY

a. Capital stock

In August 2005, the Corporation through capitalization of retained earnings issued new common stock totaling 655,558 thousand shares.

b. Treasury stock

Purpose	Thousand Shares Beginning of Period	Increase	Decrease	June 30 Thousand Shares	Book Value
2006					
1) Shares acquired and held by subsidiaries	78,899	1,625	306	80,218	$ 1,307,825
2) Shares acquired by the Corporation for transfer to employees	300	1,300	-	1,600	39,531
	79,199	2,925	306	81,818	$ 1,347,356
2005					
Shares acquired and held by subsidiaries	106,652	-	1,364	105,288	$ 1,635,075

1) Shares acquired and held by subsidiaries

The Corporation's shares acquired and held by subsidiaries (with 50% or more shareholdings) were accounted for as treasury stock (recorded as long-term or short-term investment by investees). As mentioned in Note 2, effective 2005, the Corporation's shares acquired and held by other equity-method investees substantially controlled by the Corporation were also reclassified as treasury stock. This accounting change resulted in an increase of 22,189 thousand treasury shares in treasury stock, with a carrying value of $539,707 thousand as of January 1, 2005. For the six months ended June 30, 2006, treasury stock increased by 1,625 thousand shares, respectively, because of subsidiaries purchase of additional treasury shares. Treasury stock decreased by 306 thousand shares and 1,364 thousand shares, respectively, because of subsidiaries' disposal of their holdings of the Corporation's shares and adjustment of equity in investees due to change in percentage of ownership.

The difference between the sale prices ($8,849 thousand and $54,140 thousand for the six months ended June 30, 2006 and 2005, respectively) and carrying values ($7,381 thousand and $23,541 thousand for the six months ended June 30, 2006 and 2005, respectively) of $1,468 thousand and $30,599 thousand were credited to capital surplus.

As of June 30, 2006 and 2005, the market values of those treasury shares are $2,626,351 thousand and $3,785,462 thousand, respectively.

Although these shares are treated as treasury stock in the financial statements, the stockholders are entitled to exercise their rights on these stocks, except participation in the Corporation's capital increase by cash. However, effective June 2005, the revised Company Law restricts the treasury stockholders from exercise of voting rights.

2) Shares acquired for transfer to employees

The Corporation under relevant regulations reacquired its issued common shares from the public market at a total of 1,600 thousand shares during December 2005 to February 2006.

Under the Securities Transaction Law, the Corporation’s share repurchase is restricted to up to 10% of total issued shares, and the total purchase amount should not exceed the sum of retained earnings, paid-in capital in excess of par value and realized capital surplus. In addition, the Corporation should transfer those shares to employees within three years. Otherwise these shares are deemed unissued and the Corporation should then register with the government for capital decrease. As of June 30, 2006, total reacquired shares have not yet been transferred to employees. Further, the Corporation should not pledge these stocks as collateral and should not collect dividends or exercise voting rights on these stocks.

c. Overseas depositary receipts

In May 1992, February 1997 and October 2003, the ROC’s Ministry of Economic Affairs (MOEA) (the shares were transferred to the Ministry of Finance in 2005) sold its shares in the Corporation through issuances of 88,329,150 units of Global Depositary Receipts (international GDR), with each unit representing 20 shares of the Corporation’s common stock, or equivalent to the Corporation’s common shares totaling 1,873,506,074 shares. The depositary shares then increased by 5,346,146 units resulting from the capitalization of retained earnings. Under relevant regulations, the International GDR holders may also request the conversion to the shares represented by the International GDR. The foreign investors may also request the reissuance of such depositary receipts within the originally approved units. As of June 30, 2006, the outstanding depositary receipts were 8,816,578 units, equivalent to 176,331,694 common shares, which represented 1.67% of the outstanding common shares.

d. Preferred stock

Preferred stockholders have the following entitlements or rights:

1) 14% annual dividends, with dividend payments ahead of those to common stockholders;

2) Preference over common stock in future payment of dividends in arrears;

3) Redemption of stock, at the Corporation’s option out of its retained earnings or the proceeds from issuance of new shares;

4) The same rights as common stockholders, except the right to vote for directors and supervisors; and

5) Conversion of shares into common stock.

e. Capital surplus

Following are the capital surplus sources:

	June 30, 2006	June 30, 2005
Treasury stock transaction	$ 962,339	$ 660,571
Long-term investments under the equity method	240,410	194,542
Others	8,099	8,099
	$ 1,210,848	$ 863,212

Under relevant regulations, capital surplus from treasury stock transaction may be used to offset a deficit or transferred to capital. Capital surplus from long-term investments accounted for under the equity method is prohibited from any use.

f. Other items

Revaluation increment on assets may only be used to offset a deficit. In the future, the Corporation, except the appropriations in accordance with the Company Law, shall return the revaluation increment on assets from retained earnings before any appropriations are made.

As of June 30, 2006, the Corporation's revaluation increment on assets was not used to offset a deficit.

g. Appropriation of retained earnings

The Corporation's Articles of Incorporation provide that the annual net income, less any deficit, should be appropriated in the following order of presentation:

1) 10% as legal reserve, until its balance equals the issued capital stock;

2) Preferred stock dividends at 14% of paid-in capital;

3) Of the remainder, 0.3% as compensation to directors and supervisors and 3% to 5% as bonus to employees;

4) Common-stock dividends at 14% of paid-in capital; and

5) The remainder, if any, as additional dividends divided equally between the holders of preferred and common stocks.

The Board of Directors should propose the appropriation of annual income. If necessary, it may, after appropriating preferred stock dividends at 14% of paid-in capital, propose to retain certain earnings as a special reserve. These proposals should be submitted to the stockholders' meeting for approval.

The Corporation is required to appropriate a special reserve from annual earnings for any net debit balance resulting from adjustments to the stockholders' equity, excluding treasury stock. Effective 2002, if the market price is lower than the carrying value of the Corporation's shares held by subsidiaries, the Corporation should appropriate a special reserve equal to the difference between market price and carrying value. The Corporation may release a portion of this special reserve when debit balances are partially or fully reversed.

The Corporation's steel business is in a phase of stable growth; thus, more than 75% of the appropriation of dividends and bonus should be in cash and less than 25% in stock.

Under the Company Law, legal reserve should be appropriated from retained earnings until its balance equals the issued capital stock. Legal reserve may be used to offset a deficit, or be distributed as dividends and bonuses for the portion in excess of 50% of the paid-in capital if the Corporation has no unappropriated earnings and the reserve balance has exceeded 50% of the Corporation's capital stock. The Company Law also prescribes that, when the reserve has reached 50% of the Corporation's capital stock, up to 50% of the reserve may be transferred to capital.

The Corporation's stockholders in their June 2006 and 2005 meetings, approved the following appropriations of the 2005 and 2004 earnings, which were proposed by the Board of Directors in March 2006 and 2005, respectively.

	Amount 2005	Amount 2004	Dividends Per Share 2005	Dividends Per Share 2004
Legal reserve	$ 5,060,439	$ 5,161,667		
Special reserve	(22,347)	436,524		
Preferred stocks				
Cash dividends	152,618	158,785	$ 3.75	$ 3.90
Stock dividends	14,244	20,357	0.35	0.50
			$ 4.10	$ 4.40
Common stocks				
Cash dividends	39,541,401	38,572,559	$ 3.75	$ 3.90
Stock dividends	3,690,531	4,945,200	0.35	0.50
			$ 4.10	$ 4.40
Remuneration to directors and supervisors	$ 137,302	$ 138,243		
Bonus to employees				
Cash dividends	915,350	714,035		
Stock dividends	1,373,025	1,590,021		
	$ 50,862,563	$ 51,737,391		

As of June 30, 2006 and 2005, cash dividends declared had not been distributed to stockholders and were recorded as dividends payable. Capitalization of retained earnings (including bonus to employees) of $5,077,800 thousand was approved by the government and it will be effected on August 1, 2006.

Information on the Board of Directors' proposed appropriation of earnings and related stockholders' meeting may be accessed through the Web site of the Taiwan Stock Exchange Corporation.

20. INCOME TAX

a. Reconciliation between the income tax expense and the income tax calculated on pre-tax financial statement income based on the statutory tax rate:

	For the six months ended June 30 2006	For the six months ended June 30 2005
Tax on pretax income at statutory rate (25%)	$ 4,163,706	$ 10,563,222
Add (deduct) tax effects of differences:		
Permanent		
Investment income under equity method	(1,127,588)	(854,527)
Unrealized gain on appraisal of financial assets and disposal of investment	(20,373)	(93,446)
Tax-exempt income	(5,278)	(29,575)
Investment loss resulting from investees' capital decrease	-	(74,652)
Others	(44,629)	16,069
	(1,197,868)	(1,036,131)
Temporary		
Depreciation	105,923	102,044
Unrealized foreign exchange loss	34,544	68,869
Unrealized loss (gain) on intercompany transactions	(31,652)	175,696

(Continued)

	For the six months ended June 30	
	2006	**2005**
Foreign investment income under equity method	$ (23,510)	$ (54,820)
Impairment loss on long-term investments	-	226,500
Others	7,105	(17,237)
	92,410	501,052
Income tax payable based on taxable income	3,058,248	10,028,143
Tax credits	(306,289)	(452,994)
Separate income tax on interest income	17,699	26,542
Prior periods' adjustments	68,098	(47,732)
Tax payable	2,837,756	9,553,959
Deferred tax adjustments	(80,411)	(86,374)
	$ 2,757,345	$ 9,467,585

b. Changes in income tax payable

	For the six months ended June 30	
	2006	**2005**
Balance, beginning of period	$ 7,578,477	$ 9,405,065
Current income tax	2,837,756	9,553,959
Payment in current period	(7,653,342)	(9,290,804)
Balance, end of period	$ 2,762,891	$ 9,668,220

c. Deferred income tax assets and liabilities

Current		
Deferred income tax assets		
Unrealized gain on intercompany transactions	$ 62,302	$ 174,306
Severance pay	48,119	48,966
Provision for inventory loss	-	39,889
Others	32,203	44,732
	142,624	307,893
Deferred income tax liabilities		
Temporary difference - inventory	(23,025)	(20,471)
	119,599	287,422
Noncurrent		
Deferred income tax assets		
Impairment loss on long-term investment	240,000	240,000
Impairment loss on rental assets	95,061	121,620
Cumulative effect of changes in accounting principles	64,547	-
Others	2,635	3,933
	402,243	365,553
Deferred income tax liabilities		
Temporary difference - depreciation methods	(2,775,768)	(2,983,735)
Foreign investment income	(346,745)	(331,667)
Unrealized foreign exchange gain	(54,493)	(68,869)
	(3,177,006)	(3,384,271)
	(2,774,763)	(3,018,718)
Total deferred income tax liabilities - net	$ (2,655,164)	$ (2,731,296)

Temporary difference for depreciation between tax reporting and financial reporting resulted from the adoption of accelerated depreciation method in the filing of income tax returns.

Under related regulations, the above tax credits resulted from certain purchases of machinery and equipment, research and development, employees' training, and investment in newly emerging, important and strategic industries.

The Corporation's income tax returns through 2002 had been examined by the tax authorities.

d. Imputation tax system

Under the Imputation Tax System, domestic stockholders are allowed a tax credit for the income tax paid by the Corporation on earnings generated since 1998. Nonresident stockholders, including holders of overseas depository receipts, are allowed only a tax credit from the 10% income tax on undistributed earnings, which can be used to offset withholding income tax on dividends paid.

As of June 30, 2006, the balance of the imputation credit account (ICA) aggregated $14,924,579 thousand. The estimated creditable tax ratio for the 2005 earnings was 29.84%, and the actual ratio for the 2004 earnings was 28.89%.

As of June 30, 2006, undistributed earnings generated up to 1997 amounted to $35,440 thousand, which is not subject to the Imputation Tax System.

21. PERSONNEL EXPENDITURE, DEPRECIATION AND AMORTIZATION

	For the six months ended June 30							
	2006				2005			
	Cost of Revenues	Operating Expense	Others	Total	Cost of Revenues	Operating Expense	Others	Total
Personnel Expenditure								
Salary	$ 6,094,276	$ 985,864	$ 77,524	$ 7,157,664	$ 7,450,269	$ 1,321,567	$ 73,497	$ 8,845,333
Labor and health insurance	289,481	44,704	993	335,178	249,184	42,466	568	292,218
Pension and consolation money	615,459	117,617	62,174	795,250	566,014	110,748	61,366	738,128
Others	217,591	33,791	29,589	280,971	255,035	43,614	21,453	320,102
	$ 7,216,807	$ 1,181,976	$ 170,280	$ 8,569,063	$ 8,520,502	$ 1,518,395	$ 156,884	$ 10,195,781
Depreciation	$ 4,421,396	$ 110,124	$ 14,321	$ 4,545,841	$ 4,640,020	$ 160,071	$ 13,835	$ 4,813,926
Amortization	227,528	589	2,199	230,316	79,712	640	3,371	83,723

22. EARNINGS PER SHARE

	For the six months ended June 30			
	2006		2005	
	Before Tax	After Tax	Before Tax	After Tax
Basic EPS				
Net income before cumulative effect of changes in accounting principles	$ 1.59	$ 1.33	$ 4.05	$ 3.14
Cumulative effect of changes in accounting principles	(0.01)	(0.01)	-	-
Net income	$ 1.58	$ 1.32	$ 4.05	$ 3.14
Diluted EPS				
Net income before cumulative effect of changes in accounting principles	$ 1.59	$ 1.32	$ 4.03	$ 3.13
Cumulative effect of changes in accounting principles	(0.01)	-	-	-
Net income	$ 1.58	$ 1.32	$ 4.03	$ 3.13

	Amount (Numerator)		Shares (Denominator) (Thousand)	Earnings Per Share (Dollars)	
	Before Tax	After Tax		Before Tax	After Tax
For the six months ended June 30, 2006					
Net income	$ 16,552,454	$ 13,859,656			
Less: Preferred dividends	(34,140)	(28,488)			
Basic EPS					
Net income of common Stockholders	16,518,314	13,831,168	10,464,157	$ 1.58	$ 1.32
Effect of potentially dilutive shares:					
Add: Preferred dividends	34,140	28,488	40,697		
Diluted EPS					
Net income of common stockholders and effect of potentially dilutive shares	$ 16,552,454	$ 13,859,656	10,504,854	1.58	1.32
For the six months ended June 30, 2005					
Net income	$ 42,252,886	$ 32,785,301			
Less: Preferred dividends	(36,730)	(28,500)			
Basic EPS					
Net income of common Stockholders	42,216,156	32,756,801	10,435,406	4.05	3.14
Effect of potentially dilutive shares:					
Add: Preferred dividends	36,730	28,500	40,714		
Diluted EPS					
Net income of common stockholders and effect of potentially dilutive shares	$ 42,252,886	$ 32,785,301	10,476,120	4.03	3.13

In EPS calculation for the six months ended June 30, 2005, the number of outstanding shares was retroactively adjusted for the effect of capitalization of 2004 retained earnings. Thus EPS before tax and after tax decreased from NT$4.31 to NT$4.05 and from NT$3.35 to NT$3.14, respectively.

Capitalization of the 2005 retained earnings of $5,077,800 thousand (507,780 thousand shares) will be effected on August 1, 2006 (Note 19). The EPS will then be retroactively adjusted for the effect of such capitalization of retained earnings, summarized as follows:

(New Taiwan dollars)

	For the six months ended June 30			
	2006		2005	
	Before Tax	After Tax	Before Tax	After Tax
Basic EPS	$ 1.51	$ 1.26	$ 3.86	$ 2.99
Diluted EPS	1.50	1.26	3.85	2.99
If the Corporation's shares held by subsidiaries had been accounted for as investments rather than treasury stock				
Basic EPS	1.49	1.25	3.82	2.97
Diluted EPS	1.49	1.25	3.81	2.96

23. RELATED-PARTY TRANSACTIONS

a. Related parties

Related Parties	Relationship with the Corporation
C. S. Aluminum Corporation (CAC)	Subsidiary
China Steel Express Corporation (CSE)	Subsidiary
China Steel Chemical Corporation (CSCC)	Subsidiary
China Steel Global Trading Corporation (CSGT)	Subsidiary
China Hi-ment Corporation (CHC)	Subsidiary
China Ecotek Corporation (CEC)	Subsidiary
China Steel Structure Corporation (CSSC)	Subsidiary
Chung Hung Steel Corporation (CHSC)	Subsidiary
China Steel Machinery Corporation (CSMC)	Subsidiary
Gains Investment Corporation (GIC)	Subsidiary
China Steel Security Corporation (CSS)	Subsidiary
China Prosperity Development Corporation (CPDC)	Subsidiary
Info-Champ Systems Corporation (ICSC)	Subsidiary
China Steel Management Consulting Corporation (CSMCC)	Subsidiary
Hi-mag Magnetic Corporation (HMC)	Subsidiary
Long-Yuan-Fa Investment Corporation	Subsidiary
Horng-Yih Investment Corporation	Subsidiary
Goang-Yaw Investment Corporation	Subsidiary
Dragon Steel Corporation (DSC)	Subsidiary
China Steel Asia Pacific Holdings Pte Ltd. (CSAPH)	Subsidiary
Chung Mao Trading (BVI) Corp. (CSGT-BVI)	Indirect investee under Corporation's substantial control
Chung Mao Trading Corp. (SAMOA)	Indirect investee under Corporation's substantial control
CSGT (Singapore) Pte. Ltd.	Indirect investee under Corporation's substantial control
Mentor Consulting Corporation (MCC)	Indirect investee under Corporation's substantial control
Steel Castle Technology Corp.	Indirect investee under Corporation's substantial control
Union Steel Development Corp.	Indirect investee under Corporation's substantial control
Betacera Inc.	Indirect investee under Corporation's substantial control
Wabo Globe Trading Corporation (WGTC)	Indirect investee under Corporation's substantial control
Universal Exchange Inc. (UEI)	Indirect investee under Corporation's substantial control
United Steel Engineering and Construction Corporation (USECC)	Indirect investee under Corporation's substantial control
Thintech Materials Technology Co., Ltd.	Indirect investee under Corporation's substantial control
Pao Good Industrial Co., Ltd.	Indirect investee under Corporation's substantial control
Ornasteel Enterprise Corp. (M) Sdn. Bhd. (OEC)	Indirect investee under Corporation's substantial control

(Continued)

Related Parties	Relationship with the Corporation
Group Steel Enterprise Corp. (M) Sdn. Bhd (GEC)	Indirect investee under Corporation's substantial control
CSGT (JAPAN) Co., Ltd.	Indirect investee under Corporation's substantial control
CSGT Hong Kong Limited	Indirect investee under Corporation's substantial control
CSGT (SHANGHAI) Co., Ltd.	Indirect investee under Corporation's substantial control
Ningbo Huayang Aluminum - Tech Co., Ltd. (NHAT)	Indirect investee under Corporation's substantial control
Taiwan Rolling Stock Co., Ltd. (TRSC)	Investee
Kaohsiung Rapid Transit Corporation (KRTC)	Investee
TaiAn Technologies Corporation (TTC)	Investee
Kaohsiung Labor Assemble & Disassemble Co., Ltd.	Indirect investee under Corporation's substantial control
Others	Under Corporation's substantial control but with no significant transactions

b. Significant related-party transactions:

	For the six months ended June 30			
	2006		2005	
	Amount	%	Amount	%
Sales				
CSSC	$ 1,232,330	2	$ 1,777,206	2
CHSC	1,204,141	1	780,550	1
CSCC	846,946	1	892,621	1
OEC	677,634	1	1,770,656	2
Others	998,572	1	1,488,995	1
	$ 4,959,623	6	$ 6,710,028	7
Purchases				
CSE	$ 5,517,126	15	$ 7,755,557	21
CAC	1,330,332	3	898,085	2
Others	353,669	1	1,330,629	4
	$ 7,201,127	19	$ 9,984,271	27

Sales to and purchases from related parties are made under normal terms, except those with OEC, CSCC, CAC, CHC and CSE, for which there were no similar transactions in the market for comparison.

Asset lease

The Corporation leases its land and office to CAC, CSSC, CHC, CSCC and CSMC, etc. Rentals are calculated at 4% to 10% p.a. of land value as published by the government or under normal terms. Rentals are collected semiannually, except for rental from CAC and that from CSCC on the storage tank and pipelines, which are collected monthly. Lease information is as follows:

	Expiry of Contracts	Rental Income For the six months ended June 30 2006	2005
CAC	February 2016	$ 23,541	$ 23,537
CSMC	November 2011	12,223	11,473
CSCC	December 2010	9,425	10,030
CSSC	May 2018	7,831	7,985
CHC	April 2012	2,456	2,467
Others	April 2009	3,672	1,529
		$ 59,148	$ 57,021

Property transaction

In January 2005, the Corporation purchased land from CPDC for office construction at the price of $834,673 thousand, which was determined by reference to appraisal report.

Other expenditures

Other expenditures paid to related parties pertaining to furnace slag and clearance services, property maintenance or construction, export shipping charges, commissions for export and import services, etc..

	For the six months ended June 30 2006	2005
CEC	$ 1,249,839	$ 632,004
CSMC	875,264	380,807
CSSC	520,956	539,660
USECC	336,006	234,379
CHC	299,587	255,417
Others	653,899	639,319
	$ 3,935,551	$ 2,681,586

Other revenues

Other revenues pertained to labor services, processing of products, utilities and other services to related parties.

	For the six months ended June 30 2006	2005
KRTC	$ 741,690	$ 346,511
CHSC	157,356	118,849
Others	400,215	373,037
	$ 1,299,261	$ 838,397

Short-term loans payable to related parties

In January 2005, the Corporation borrowed $1,238,738 thousand (USD$38,500 thousand) from CSAPH at no interest and repaid in September 2005.

c. Balances at period-end

	June 30, 2006		June 30, 2005	
	Amount	%	Amount	%
Receivables				
KRTC	$ 327,841	13	$ 43,707	2
CSCC	165,735	7	149,905	5
Others	288,494	12	224,140	8
	$ 782,070	32	$ 417,752	15
Payables				
CSE	$ 650,807	20	$ 1,047,285	38
Others	217,521	6	152,025	6
	$ 868,328	26	$ 1,199,310	44

24. PLEDGED ASSETS

a. Time deposits of $4,631,694 thousand as of June 30, 2006 and 2005 have been pledged mainly as collateral for bank overdrafts, etc.

b. The Corporation provided machinery and equipment with carrying values of $2,553,007 thousand and $2,845,227 thousand as of June 30, 2006 and 2005, respectively, as collaterals for long-term credit lines with banks.

25. COMMITMENTS AS OF JUNE 30, 2006

a. The Corporation engaged in several construction contracts, under guarantees of $1,278,546 thousand granted by the International Commercial Bank of China and Taipei Fubon Bank.

b. Unused letters of credit amounted to $7.9 billion.

c. The Corporation entered into raw material purchase contracts with suppliers in Australia, India, Brazil, Canada, Indonesia, North Korea, Japan, Philippines, Russia and domestic companies with contract terms of 1 to 10 years. Contracted annual purchases of 8,300,000 metric tons of coal, 16,000,000 metric tons of iron ore, and 2,800,000 metric tons of stones are at prices negotiable every year. Unpaid purchase amounts as of June 30, 2006 were US$9 billion (12,590,000 metric tons of coal; 138,000,000 metric tons of iron ore; and 1,680,000 metric tons of stones).

d. CHSC entered into a Syndicated Credit Facility Agreement with Chiao Tung Bank and 23 other Banks, and another Syndicated Agreement with The International Commercial Bank of China and 19 other financial institutions. Under these agreements, the Corporation and its related parties should collectively hold at least 30% of CHSC's issued shares and have over half of CHSC's board seats as well as significant influence on its operations. As of June 30, 2006, the Corporation had total direct and indirect shareholdings in CHSC of 39% and total seats in the Board of Directors and influence on its operations.

e. KRTC entered a Syndicated Credit Facility Agreement with the Taiwan Bank and 24 other Banks. Under this agreement, the Corporation and its subsidiaries should collectively hold at least 30% of KRTC's capital stock during the construction period. As of June 30, 2006, the Corporation's total equity in KRTC was 31%.

26. FINANCIAL INSTRUMENTS

The Corporation had no derivative transactions for the six months ended June 30, 2006 and 2005.

a. As of June 30, 2006 and 2005, the information of fair values was as follows:

	2006		2005	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Cash and cash equivalents	$ 21,516,956	$ 21,516,956	$ 50,810,286	$ 50,810,286
Financial assets at fair value through profit or loss	17,231,571	17,231,571	11,931,521	12,049,045
Available-for-sale financial assets	5,933,858	5,933,858	2,219,366	5,479,993
Financial assets carried at cost	6,049,010	-	6,302,202	-
Notes receivable	1,147,743	1,147,743	2,012,127	2,012,127
Accounts receivable	2,477,104	2,477,104	2,790,459	2,790,459
Pledged time deposits	4,631,694	4,631,694	4,631,694	4,631,694
Other receivable	5,667,220	5,667,220	2,040,593	2,040,593
Investment in bonds without quoted price	5,881,375	5,881,375	5,834,325	5,834,325
Refundable deposits	223,865	223,865	220,919	220,919
Liabilities				
Short-term loans and overdraft	16,693,318	16,693,318	9,687,490	9,687,490
Notes and accounts payable	3,320,686	3,320,686	2,748,750	2,748,750
Accrued expenses	4,677,513	4,677,513	6,416,155	6,416,155
Long-term bonds	13,100,000	13,231,715	15,000,000	15,877,820
Long-term bank debts	3,528,125	3,528,125	3,582,500	3,582,500

Effective 2006, the Corporation adopted the newly issued Statement of Financial Accounting Standards No. 34 "Accounting for Financial Instruments", thus, some change of fair value in financial asset were not recognized in 2005.

The cumulative effect of changes in accounting principles and the adjustment of stockholders' equity were stated in Note 3.

b. The assumptions and methods used to estimate the fair values of financial instruments are as follows:

1) The carrying values of cash and cash equivalents, notes and accounts receivable, short-term bank loans and overdraft and notes and accounts payable, approximate fair value because of the short maturities of these instruments.

2) The fair value of financial assets at fair value through profit of loss and available-for-sale financial assets are determined at their market value.

3) The fair values of long-term liabilities are determined by the present values of future cash flows, with the values discounted at the interest rates of similar long-term debts available for the Corporation.

4) The fair values of refundable deposits and pledged time deposits are determined at their carrying values.

5) The fair value of investment in bonds without quoted price is determined at their carrying values.

c. There is no gain or loss for the estimated change in fair value by using valuation technique for the six months ended June 30, 2006.

d. As of June 30, 2006, the financial assets and liabilities with the cash flow risk of the interest rate change were $250,750 thousand and $20,221,443 thousand respectively. The financial liabilities with fair value risk of the interest rate change were $13,100,000 thousand.

e. The Corporation's total interest revenues and expenses which were not recognized from financial assets and liabilities at fair value through profit or loss were $170,077 thousand and $301,273 thousand, respectively for the six months ended June 30, 2006.

f. Financial risk information

1) Market risk

This includes fair value risk of interest rate change, exchange rate risk, and market price risk. The Corporation had long-term loans in yen to hedge the exchange rate fluctuations on its investment in yen, thus, the exchange rate risk can be hedged naturally. The Corporation issues the bonds payable with the fixed interest rate, and the fair value will be influenced by the market interest rate change. For market interest rate change of 1% each time, the fair value of bonds payable will increase or decrease by $378,926 thousand.

The Corporation invested in the bond funds and stocks of Taiwan Semiconductor Manufacturing Ltd. Company, Advanced Material Technology Corporation and Maruichi Steel Tube Ltd. with having market risk. Except the minor fluctuation of the bond fund's market price, if the share price of the stocks increases or decreases by $1 each time, fair value will increase or decrease by $94,875 thousand.

2) Credit risk

Credit risk represents the potential loss that would be incurred by the Corporation if the counter-parties or third-parties breached the contracts. The Corporation's financial instruments are affected by its credit risk concentration, component, contract amounts and other receivables.

As of June 30, 2006, the Corporation's credit risks amounted to $9,515,932 thousand and the maximum credit risk and carrying value are the same. The credit risks of the cash and bank deposits of the Corporation were considered to be not significant.

3) Liquidity risk

The Corporation has sufficient operating capital to meet cash needs. Therefore, the cash flow risk is low.

Financial assets at fair value through profit or loss and available-for-sale financial assets could be sold rapidly at prices approximating fair value because those financial assets could be sold in secondary financial market at market value.

There are liquidity risk for the financial assets carried at cost and bond investments without quoted price because no market values are available.

4) Cash flow risk of interest rate change

Market interest rate change will influence the effective interest rate of the financial instruments which have cash flow risk of the interest rate change, and make future cash flow fluctuate. As the market interest rate increases 1%, the Corporation's cash outflow will increase $199,707 thousand.

g. Fair value hedge

The Corporation had long-term bank loans in yen to effectively hedge the exchange rate fluctuations on the investments in East Asia United Steel Corporation and Maruichi Steel Tube Ltd in yen.

Hedged item	Appointed hedging instrument: Financial instrument	Appointed hedging instrument: Changes of fair value
Stock investments in Maruichi Steel Tube Ltd.	Long-term bank loans in yen	$ 6,630
Stock investments in East Asia United Steel Corporation	Long-term bank loans in yen	25,245

CHINA STEEL CORPORATION

ADDITIONAL EXPLANATION FOR ACCOUNTS IN STOCKHOLDERS' EQUITY
SIX MONTHS ENDED JUNE 30, 2006 AND 2005

1. ADJUSTMENT OF EQUITY IN INVESTEES DUE TO CHANGE IN PERCENTAGE OF OWNERSHIP

a. Long-term investment adjustment

When an investee's capital surplus changed, the investor should adjust its long-term investment account and capital surplus account based on its stockholding percentage.

b. Adjustment of equity in investee due to change in percentage of ownership

If an investee issues new shares and original stockholders do not subscribe the new shares proportionately, then the investment percentage, e.g. the equity in the investee's net assets, will change. This change shall be reflected as an adjustment of the additional paid-in capital (capital surplus) and the long-term investments accounts. If this adjustment is to reduce the additional paid-in capital resulting from long-term stock investments and its balance is insufficient, the difference should be adjusted to the unappropriated retained earnings.

2. UNREALIZED GAIN (LOSS) ON FINANCIAL INSTRUMENTS

Available-for-sale financial asset is measured at fair value and its value change is recorded as a reconciliation item in the stockholders' equity.

3. INVESTEES' UNRECOGNIZED NET LOSS ON PENSION COST

a. Unrecognized net loss on pension cost is the minimum pension liability exceeding the sum of unrecognized prior service cost and unrecognized transitional net benefit obligation. It is classified as a reduction of stockholders' equity.

b. Minimum pension liability, which is calculated actuarially, is the minimum amount of pension liability that is required to be recognized on the balance sheet.

c. Prior service cost is the increase in projected benefit obligation due to an employee's accumulation of service years at the initial introduction of pension data or the subsequent pension data amendment.

d. Unrecognized transitional net assets or benefit obligation means the amount resulting from a change from a method specified in Statement of Financial Accounting Standards No. 18, "Accounting for Pensions." This amount is the difference between (a) the fair market value of plan assets plus accrued pension liability or less prepaid pension cost recognized previously in the books and (b) the projected benefit obligation. If the difference is positive, it is treated as unrecognized transition net assets; if the difference is negative, it is treated as unrecognized transition net benefit obligations.

4. TRANSFER OF TREASURY STOCK TO EMPLOYEES.

Treasury stock is transferred at the price which is determined at the purchase cost plus the Corporation financial cost up to the time that the transfer is made.

When treasury stocks are transferred, if the transfer price is higher than the book value, the difference should be credited to capital surplus. If the transfer price is lower than book value, the difference should first be offset against capital surplus from the same class of treasury stock transactions, and the remainder, if any, should be debited to unappropriated retained earnings.

5. DISPOSAL OF THE CORPORATION'S SHARES HELD BY SUBSIDIARIES

A parent company should account for its outstanding stocks held by its subsidiary as treasury stocks when it recognizes investment income and prepares financial statements, and the accounting treatment is the same as that stated in item 4 above.

6. CASH DIVIDENDS DECLARED BY THE CORPORATION AND RECEIVED BY SUBSIDIARIES

When an investor receives cash dividends from short-term investments or long-term cost-method investments from a year after investment acquisition, it records these dividends as investment income. But if the cash dividend is from the parent company, the accounting for these dividends is the same as that for treasury stock, i.e., the investment income should be credited to capital surplus when the parent company prepares financial statements.