

# **China Steel Corporation**

**Financial Statements for the  
Six Months Ended June 30, 2012 and 2011 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, 2012 and 2011, 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. 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, 2012 and 2011, 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, requirements of the Business Accounting Law and Guidelines Governing Business Accounting relevant to financial accounting standards, and accounting principles generally accepted in the Republic of China.

We have also reviewed the consolidated financial statements of the Corporation and its subsidiaries as of and for the six months ended June 30, 2012 and 2011 on which we issued an unqualified review report.

August 27, 2012

### Notice to Readers

*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.*

# CHINA STEEL CORPORATION

## BALANCE SHEETS

JUNE 30, 2012 AND 2011

(In Thousands of New Taiwan Dollars, Except Par Value)

ASSETS	2012		2011		LIABILITIES AND STOCKHOLDERS' EQUITY	2012		2011	
	Amount	%	Amount	%		Amount	%	Amount	%
CURRENT ASSETS					CURRENT LIABILITIES				
Cash	\$ 1,412,807	-	\$ 2,169,635	1	Short-term loans and overdraft	\$ 9,518,105	2	\$ 13,145,257	3
Available-for-sale financial assets - current	2,583,888	1	2,103,011	-	Commercial paper payable	8,697,694	2	6,397,371	2
Hedging derivative assets - current	68,360	-	-	-	Hedging derivative liabilities - current	8,073	-	2,429	-
Notes receivable	782,047	-	810,980	-	Accounts payable	6,950,843	2	5,643,379	1
Notes receivable - related parties	580,796	-	613,337	-	Accounts payable - related parties	979,328	-	1,688,377	-
Accounts receivable	3,094,132	1	2,903,749	1	Income tax payable	998,893	-	2,820,573	1
Accounts receivable - related parties	552,660	-	720,027	-	Accrued expenses	8,087,249	2	11,116,365	3
Other receivables	3,144,125	1	3,578,560	1	Dividends payable	15,530,656	3	27,275,047	7
Other financial assets - current	3,122,196	1	2,156,583	1	Other payables	9,117,008	2	6,309,163	1
Inventories	58,507,295	13	62,156,567	15	Bonds payable - current portion	11,297,543	3	5,599,499	1
Deferred income tax assets - current	2,490,843	1	662,237	-	Long-term debt - current portion	8,058,787	2	-	-
Restricted assets - current	5,664,926	1	4,650,004	1	Others	2,890,311	1	3,259,790	1
Others	2,473,012	-	2,312,520	1					
Total current assets	84,477,087	19	84,837,210	21	Total current liabilities	82,134,490	19	83,257,250	20
INVESTMENTS					LONG-TERM LIABILITIES				
Available-for-sale financial assets - noncurrent	3,242,725	1	3,323,540	1	Hedging derivative liabilities - noncurrent	3,088	-	11,126	-
Hedging derivative assets - noncurrent	27,347	-	-	-	Bonds payable	37,973,270	9	29,583,115	7
Financial assets carried at cost - noncurrent	7,637,696	2	3,818,813	1	Long-term debt	18,402,740	4	24,352,993	6
Bond investments with no active market - noncurrent	3,754,000	1	3,573,000	1	Long-term notes payable	11,995,316	3	3,748,475	1
Investments accounted for by the equity method	145,000,045	33	124,223,515	30					
Other financial assets - noncurrent	173,709	-	2,464,664	1	Total long-term liabilities	68,374,414	16	57,695,709	14
Total investments	159,835,522	37	137,403,532	34	RESERVE FOR LAND VALUE INCREMENT TAX	10,011,916	2	8,673,466	2
PROPERTY, PLANT AND EQUIPMENT					OTHER LIABILITIES				
Land	9,225,591	2	10,976,123	3	Accrued pension cost	51,491	-	-	-
Land improvements	4,222,123	1	4,223,646	1	Deferred income tax liabilities - noncurrent	298,002	-	542,313	-
Buildings	52,915,354	12	44,844,743	11	Deferred credits - gain from affiliates	2,027,696	-	2,053,384	1
Machinery and equipment	308,040,224	70	277,042,416	68					
Transportation equipment	1,844,859	1	1,746,493	-	Total other liabilities	2,377,189	-	2,595,697	1
Other equipment	5,194,233	1	5,053,803	1					
Spare parts	7,268,173	2	7,031,329	2	Total liabilities	162,898,009	37	152,222,122	37
Total cost	388,710,557	89	350,918,553	86	CAPITAL STOCK - NT\$10 par value, authorized 17,000,000 thousand shares				
Revaluation increment	48,786,916	11	42,962,522	11	Common shares - issued 15,046,209 thousand shares and 13,527,901 thousand shares as of June 30, 2012 and 2011, respectively	150,462,093	35	135,279,009	34
Cost and revaluation increment	437,497,473	100	393,881,075	97	Preferred shares - issued 38,268 thousand shares	382,680	-	382,680	-
Less: Accumulated depreciation	266,537,237	61	254,764,641	63					
	170,960,236	39	139,116,434	34	Total capital stock	150,844,773	35	135,661,689	34
Constructions in progress and prepayments for equipment	17,439,489	4	41,659,029	10	CAPITAL SURPLUS	36,287,500	8	20,125,417	5
Net property, plant and equipment	188,399,725	43	180,775,463	44	RETAINED EARNINGS	66,752,465	15	82,685,699	20
INTANGIBLE ASSETS	162,984	-	205,216	-	OTHER EQUITY				
OTHER ASSETS					Unrealized revaluation increment	26,755,768	6	21,865,924	5
Assets leased to others, net	4,889,149	1	3,112,839	1	Unrealized gain on financial instruments	3,239,199	1	2,481,703	1
Refundable deposits	212,075	-	215,090	-	Cumulative translation adjustments	(190,772)	-	(390,033)	-
Restricted assets - noncurrent	19,834	-	21,806	-	Net loss not recognized as pension cost	(230,770)	-	(79,210)	-
Total other assets	5,121,058	1	3,349,735	1	Treasury stock - 303,278 thousand shares and 278,842 thousand shares as of June 30, 2012 and 2011, respectively	(8,359,796)	(2)	(8,002,155)	(2)
TOTAL	\$ 437,996,376	100	\$ 406,571,156	100	Total other equity	21,213,629	5	15,876,229	4
					Total stockholders' equity	275,098,367	63	254,349,034	63
					TOTAL	\$ 437,996,376	100	\$ 406,571,156	100

# CHINA STEEL CORPORATION

## STATEMENTS OF INCOME

SIX MONTHS ENDED JUNE 30, 2012 AND 2011

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2012		2011	
	Amount	%	Amount	%
OPERATING REVENUES	\$ 110,675,420	100	\$ 120,134,316	100
OPERATING COSTS	<u>107,777,870</u>	<u>97</u>	<u>103,970,109</u>	<u>87</u>
GROSS PROFIT	2,897,550	3	16,164,207	13
UNREALIZED GAIN FROM AFFILIATES, NET	<u>(8,146)</u>	<u>-</u>	<u>(91,327)</u>	<u>-</u>
REALIZED GROSS PROFIT	<u>2,889,404</u>	<u>3</u>	<u>16,072,880</u>	<u>13</u>
OPERATING EXPENSES				
Research and development	661,448	1	715,635	1
Selling	1,161,794	1	1,261,218	1
General and administrative	<u>1,213,633</u>	<u>1</u>	<u>1,577,981</u>	<u>1</u>
Total operating expenses	<u>3,036,875</u>	<u>3</u>	<u>3,554,834</u>	<u>3</u>
OPERATING INCOME (LOSS)	<u>(147,471)</u>	<u>-</u>	<u>12,518,046</u>	<u>10</u>
NONOPERATING INCOME AND GAINS				
Interest income	58,337	-	40,559	-
Investment income recognized under equity method, net	2,171,434	2	4,498,411	4
Exchange gain	184,627	-	307,913	-
Others	<u>541,697</u>	<u>1</u>	<u>488,615</u>	<u>1</u>
Total nonoperating income and gains	<u>2,956,095</u>	<u>3</u>	<u>5,335,498</u>	<u>5</u>
NONOPERATING EXPENSES AND LOSSES				
Interest expense	609,470	1	352,764	-
Others	<u>270,382</u>	<u>-</u>	<u>197,186</u>	<u>-</u>
Total nonoperating expenses and losses	<u>879,852</u>	<u>1</u>	<u>549,950</u>	<u>-</u>
INCOME BEFORE INCOME TAX	1,928,772	2	17,303,594	15
INCOME TAX EXPENSE (BENEFIT)	<u>(16,318)</u>	<u>-</u>	<u>1,959,181</u>	<u>2</u>
NET INCOME	<u>\$ 1,945,090</u>	<u>2</u>	<u>\$ 15,344,413</u>	<u>13</u>

(Continued)

# CHINA STEEL CORPORATION

## STATEMENTS OF INCOME

SIX MONTHS ENDED JUNE 30, 2012 AND 2011

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2012		2011	
	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
EARNINGS PER SHARE				
Basic	<u>\$ 0.13</u>	<u>\$ 0.13</u>	<u>\$ 1.22</u>	<u>\$ 1.08</u>
Diluted	<u>\$ 0.13</u>	<u>\$ 0.13</u>	<u>\$ 1.21</u>	<u>\$ 1.07</u>

Pro forma information (after income tax) assuming the Corporation's shares held by its subsidiaries were accounted for as investments instead of treasury stock is as follows:

	2012	2011
Net income	\$ 1,947,119	\$ 15,397,199
Basic earnings per share based on weighted-average number of outstanding common shares aggregating 15,272,476 thousand and 14,432,476 thousand shares for the six months ended June 30, 2012 and 2011, respectively	<u>\$0.13</u>	<u>\$1.06</u>
Diluted earnings per share based on weighted-average number of outstanding common shares aggregating 15,330,877 thousand and 14,590,648 thousand shares for the six months ended June 30, 2012 and 2011, respectively	<u>\$0.13</u>	<u>\$1.06</u>

(Concluded)

# CHINA STEEL CORPORATION

## STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY SIX MONTHS ENDED JUNE 30, 2012 AND 2011 (In Thousands of New Taiwan Dollars, Except Dividends Per Share)

	Issued		Capital Surplus	Retained Earnings				Other Equity					
	Common Shares	Preferred Shares		Legal Reserve	Special Reserve	Unappropriated Earnings	Total	Unrealized Revaluation Increment	Unrealized Gain on Financial Instruments	Cumulative Translation Adjustments	Net Loss Not Recognized As Pension Cost	Treasury Stock	Total Stockholders' Equity
BALANCE, JANUARY 1, 2012	\$ 150,462,093	\$ 382,680	\$ 36,247,705	\$ 52,829,209	\$ 7,615,701	\$ 19,606,971	\$ 80,051,881	\$ 26,757,590	\$ 3,020,919	\$ 17,192	\$ (230,590)	\$ (8,122,461)	\$ 288,587,009
Appropriation of 2011 earnings													
Legal reserve	-	-	-	1,949,368	-	(1,949,368)	-	-	-	-	-	-	-
Cash dividends to preferred stockholders - NT\$1.25 per share	-	-	-	-	-	(47,835)	(47,835)	-	-	-	-	-	(47,835)
Cash dividends to common stockholders - NT\$1.01 per share	-	-	-	-	-	(15,196,671)	(15,196,671)	-	-	-	-	-	(15,196,671)
Net income for the six months ended June 30, 2012	-	-	-	-	-	1,945,090	1,945,090	-	-	-	-	-	1,945,090
Change in unrealized gain on available-for-sale financial assets	-	-	-	-	-	-	-	-	280,391	-	-	-	280,391
Change in unrealized revaluation increment	-	-	-	-	-	-	-	(1,655)	-	-	-	-	(1,655)
Adjustment from changes in equity recognized under equity method	-	-	37,766	-	-	-	-	(167)	72,457	-	(180)	(7,749)	102,127
Foreign exchange loss on translation of foreign-currency financial statements	-	-	-	-	-	-	-	-	-	(271,003)	-	-	(271,003)
Foreign exchange gain on hedge of a net investment in a foreign operation	-	-	-	-	-	-	-	-	-	63,039	-	-	63,039
Change in unrealized gain on financial instruments for cash flow hedging	-	-	-	-	-	-	-	-	(134,568)	-	-	-	(134,568)
Purchase of the Corporation's shares by subsidiaries	-	-	-	-	-	-	-	-	-	-	-	(243,297)	(243,297)
Disposal of the Corporation's shares held by subsidiaries	-	-	2,029	-	-	-	-	-	-	-	-	13,711	15,740
BALANCE, JUNE 30, 2012	<u>\$ 150,462,093</u>	<u>\$ 382,680</u>	<u>\$ 36,287,500</u>	<u>\$ 54,778,577</u>	<u>\$ 7,615,701</u>	<u>\$ 4,358,187</u>	<u>\$ 66,752,465</u>	<u>\$ 26,755,768</u>	<u>\$ 3,239,199</u>	<u>\$ (190,772)</u>	<u>\$ (230,770)</u>	<u>\$ (8,359,796)</u>	<u>\$ 275,098,367</u>
BALANCE, JANUARY 1, 2011	\$ 135,279,009	\$ 382,680	\$ 20,072,476	\$ 49,070,526	\$ 7,615,701	\$ 37,651,735	\$ 94,337,962	\$ 21,873,940	\$ 2,374,377	\$ (101,443)	\$ (117,015)	\$ (8,151,621)	\$ 265,950,365
Appropriation of 2010 earnings													
Legal reserve	-	-	-	3,758,683	-	(3,758,683)	-	-	-	-	-	-	-
Cash dividends to preferred stockholders - NT\$1.99 per share	-	-	-	-	-	(76,153)	(76,153)	-	-	-	-	-	(76,153)
Cash dividends to common stockholders - NT\$1.99 per share	-	-	-	-	-	(26,920,523)	(26,920,523)	-	-	-	-	-	(26,920,523)
Net income for the six months ended June 30, 2011	-	-	-	-	-	15,344,413	15,344,413	-	-	-	-	-	15,344,413
Change in unrealized gain on available-for-sale financial assets	-	-	-	-	-	-	-	-	226,458	-	-	-	226,458
Change in unrealized revaluation increment	-	-	-	-	-	-	-	(7,851)	-	-	-	-	(7,851)
Adjustment from changes in equity recognized under equity method	-	-	155	-	-	-	-	(165)	(63,471)	-	37,805	83	(25,593)
Foreign exchange loss on translation of foreign-currency financial statements	-	-	-	-	-	-	-	-	-	(383,760)	-	-	(383,760)
Foreign exchange gain on hedge of a net investment in a foreign operation	-	-	-	-	-	-	-	-	-	95,170	-	-	95,170
Change in unrealized gain on financial instruments for cash flow hedging	-	-	-	-	-	-	-	-	(55,661)	-	-	-	(55,661)
Disposal of the Corporation's shares held by subsidiaries	-	-	52,786	-	-	-	-	-	-	-	-	149,383	202,169
BALANCE, JUNE 30, 2011	<u>\$ 135,279,009</u>	<u>\$ 382,680</u>	<u>\$ 20,125,417</u>	<u>\$ 52,829,209</u>	<u>\$ 7,615,701</u>	<u>\$ 22,240,789</u>	<u>\$ 82,685,699</u>	<u>\$ 21,865,924</u>	<u>\$ 2,481,703</u>	<u>\$ (390,033)</u>	<u>\$ (79,210)</u>	<u>\$ (8,002,155)</u>	<u>\$ 254,349,034</u>

# CHINA STEEL CORPORATION

## STATEMENTS OF CASH FLOWS SIX MONTHS ENDED JUNE 30, 2012 AND 2011 (In Thousands of New Taiwan Dollars)

	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 1,945,090	\$ 15,344,413
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	8,606,266	8,150,687
Amortization	21,097	21,229
Deferred income tax	(1,231,860)	(37,731)
Provision for loss on inventories	1,513,226	133,835
Investment income under equity method, net	(2,171,434)	(4,498,411)
Unrealized gain from affiliates, net	8,146	91,327
Cash dividends received from equity method investees	3,114,694	3,227,318
Loss on purchase commitments	810,666	-
Others	11,877	(28,604)
Net changes in operating assets and liabilities		
Notes receivable	84,724	(104,905)
Notes receivable - related parties	(112,396)	(76,129)
Accounts receivable	(329,833)	(1,006,341)
Accounts receivable - related parties	556	(130,496)
Other receivables	(44,381)	(153,456)
Inventories	7,409,052	(15,293,280)
Other current assets	(760,469)	(814,989)
Notes payable - related parties	-	(23,163)
Accounts payable	2,285,241	1,012,579
Accounts payable - related parties	128,014	378,713
Income tax payable	(758,782)	(1,012,944)
Accrued expenses	(218,860)	383,735
Other payables	1,057,415	1,931,378
Other current liabilities	(281,309)	(642,669)
Net cash provided by operating activities	<u>21,086,740</u>	<u>6,852,096</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Acquisition of financial assets carried at cost	(352,373)	(468,585)
Acquisition of investments accounted for by equity method	(21,119,718)	(2,168,507)
Acquisition of property, plant and equipment	(9,918,463)	(8,223,621)
Proceeds from disposal of property, plant and equipment	-	1,267
Proceeds from disposal of assets leased to others	-	5,000
Decrease (increase) in refundable deposits	11,140	(98,572)
Decrease (increase) in other financial assets	1,080,369	(2,833,846)
Decrease in restricted assets	<u>27,807</u>	<u>9,657</u>
Net cash used in investing activities	<u>(30,271,238)</u>	<u>(13,777,207)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Increase in short-term loans and overdraft	3,058,895	11,803,493

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# CHINA STEEL CORPORATION

## STATEMENTS OF CASH FLOWS SIX MONTHS ENDED JUNE 30, 2012 AND 2011 (In Thousands of New Taiwan Dollars)

	2012	2011
Increase in commercial paper payable	\$ 5,101,817	\$ 2,697,732
Repayments of bonds payable	-	(8,100,000)
Decrease in long-term notes payable	-	(750,000)
Proceeds from long-term debt	1,757,611	1,279,567
Cash dividends	<u>(4,625)</u>	<u>(6,662)</u>
Net cash provided by financing activities	<u>9,913,698</u>	<u>6,924,130</u>
NET INCREASE (DECREASE) IN CASH	729,200	(981)
CASH, BEGINNING OF PERIOD	<u>683,607</u>	<u>2,170,616</u>
CASH, END OF PERIOD	<u>\$ 1,412,807</u>	<u>\$ 2,169,635</u>
SUPPLEMENTAL CASH FLOW INFORMATION		
Interest paid	\$ 320,601	\$ 378,070
Capitalized interest	<u>(78,451)</u>	<u>(179,989)</u>
Interest paid (excluding capitalized interest)	<u>\$ 242,150</u>	<u>\$ 198,081</u>
Income tax paid	<u>\$ 1,974,324</u>	<u>\$ 3,009,856</u>
INVESTING AND FINANCING ACTIVITIES AFFECTING BOTH CASH AND NON-CASH ITEMS		
Cash paid for acquisition of property, plant and equipment		
Acquisition of property, plant and equipment	\$ 11,787,397	\$ 7,881,234
Decrease (increase) in payable for equipment purchased	<u>(1,868,934)</u>	<u>342,387</u>
	<u>\$ 9,918,463</u>	<u>\$ 8,223,621</u>
Cash dividends paid to stockholders		
Total cash dividends payable to stockholders	\$ 15,244,506	\$ 26,996,676
Increase in dividends payable	<u>(15,239,881)</u>	<u>(26,990,014)</u>
	<u>\$ 4,625</u>	<u>\$ 6,662</u>
NON-CASH FINANCING ACTIVITIES		
Current portion of long-term liabilities	<u>\$ 19,356,330</u>	<u>\$ 5,599,499</u>

(Concluded)