English Translation of a Report Originally Issued in Chinese

Independent Auditors‘ Report

January 24, 2003

The Board of Directors and Stockholders
China Steel Corporation

We have audited the accompanying balance sheets of China Steel Corporation (the Corporation) as of December 31, 2002 and 2001, and the related statements of income, changes in stockholders‘ equity and cash flows for the years 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 Regulations for Audit of Financial Statements by Certified Public Accountants and generally accepted auditing standards in the Republic of China (ROC). Those 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 December 31, 2002 and 2001, and the results of its operations and its cash flows for the years then ended, in conformity with Guidelines for Securities Issuers’ Financial Reporting and generally accepted accounting principles in ROC.

Under the Statement of Financial Accounting Standards No. 30- “Treasury Stock” of ROC and a related ruling issued by the ROC’s Securities & Futures Commission, the Corporation’s shares acquired and held by its subsidiaries should be accounted for as treasury stock effective 2002. As a result, the Corporation reclassified the stock shares acquired by its subsidiaries from long-term investments to treasury stock. The reclassification is based on the book value of the shares as of the start of 2002. The effects of this accounting change on the Corporation’s financial statements as of December 31, 2002 were as follows: (a) decreases in long-term investments by NT$1,883,432 thousand, retained earnings by NT$144,328 thousand and net income by NT$144,328 thousand; and (b) increases in treasury stock by NT$1,340,018 thousand, unrealized loss on long-term investments by NT$481,700 thousand and capital surplus by NT$82,614 thousand.

T N Soong & Co
An Associate Member Firm of Deloitte Touche Tohmatsu
Effective April 22, 2002
(Formerly a Member Firm of Andersen Worldwide, SC)
Taipei, Taiwan
The Republic of China

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.

English Translation of Financial Statements Originally Issued in Chinese

CHINA STEEL CORPORATION

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

	December 31			
	2002		2001	
ASSETS	Amount	%	Amount	%
CURRENT ASSETS				
Cash and cash equivalents (Note 2)	$ 3,068,966	1	$ 4,302,175	2
Short-term investments (Notes 2 and 4)	19,751,336	10	12,206,524	6
Notes receivable (Note 18)	378,442	-	144,794	-
Accounts receivable (Note 18)	1,642,077	1	1,815,944	1
Inventories (Notes 2 and 5)	15,468,476	8	18,371,621	9
Pledged time deposits (Notes 9 and 19)	6,900,000	4	8,200,000	4
Other	372,108	-	1,238,409	1
Total Current Assets	47,581,405	24	46,279,467	23
LONG-TERM INVESTMENTS (Notes 2, 6 and 19)	35,532,286	18	35,026,411	18
PROPERTIES (Notes 2, 7, 18 and 19)				
Land	7,146,632	4	6,764,647	4
Land improvements	4,316,764	2	4,316,764	2
Buildings and improvements	35,814,229	18	35,664,534	18
Machinery and equipment	207,628,941	106	207,043,084	104
Transportation equipment	1,596,970	1	1,594,481	1
Miscellaneous equipment	2,826,054	2	2,651,344	1
Total cost	259,329,590	133	258,034,854	130
Appreciation	18,403,007	9	18,405,855	9
Total cost and appreciation	277,732,597	142	276,440,709	139
Less: Accumulated depreciation	177,076,769	90	167,376,583	84
	100,655,828	52	109,064,126	55
Constructions in progress	6,815,268	3	3,183,839	1
Net Properties	107,471,096	55	112,247,965	56
OTHER ASSETS (Notes 2, 8 and 19)	4,857,546	3	5,383,157	3
TOTAL ASSETS	$195,442,333	100	$198,937,000	100

	December 31			
	2002		2001	
LIABILITIES AND STOCKHOLDERS' EQUITY	Amount	%	Amount	%
CURRENT LIABILITIES				
Short-term bank loans and overdraft (Notes 9 and 19)	$ 809,688	-	$ 5,947,913	3
Commercial paper payable (Note 10)	998,347	1	2,843,252	2
Accounts payable (Note 18)	2,454,461	1	2,441,818	1
Income tax payable	3,730,522	2	-	-
Other payable	5,106,533	3	4,310,176	2
Bonds payable – current portion (Note 11)	9,200,000	5	5,850,000	3
Long-term debts – current portion (Notes 12 and 19)	2,985,045	1	2,290,269	1
Other	1,741,700	1	1,917,819	1
Total Current Liabilities	27,026,296	14	25,601,247	13
LONG-TERM LIABILITIES				
Bonds (Note 11)	25,000,000	13	34,200,000	17
Debts (Notes 12 and 19)	50,000	-	3,455,293	2
Total Long-Term Liabilities	25,050,000	13	37,655,293	19
RESERVE FOR LAND VALUE INCREMENT TAX (Note 7)	3,370,813	2	3,370,813	1
OTHER LIABILITIES (Note 14)	4,989,828	2	5,661,212	3
Total Liabilities	60,436,937	31	72,288,565	36
STOCKHOLDERS' EQUITY (Notes 3 and 15)				
Capital stock – authorized 10,600,000 thousand shares of $10 par value				
Common – issued 9,267,994 and 9,061,168 thousand shares as of December 31, 2002 and 2001, respectively	92,679,939	48	90,611,684	46
Preferred – 14% cumulative and participative - issued 47,767 and 47,768 thousand shares as of December 31, 2002 and 2001, respectively	477,670	-	477,680	-
Total capital stock	93,157,609	48	91,089,364	46
Capital surplus	481,597	-	416,570	-
Retained earnings	44,960,063	23	37,434,024	19
Unrealized loss on investees' long-term investments	(555,491)	-	(569,837)	-
Cumulative translation adjustments	222,391	-	198,881	-
Investees' unrecognized net loss on pension cost	(15,696)	-	(15,508)	-
Treasury stock	(3,245,077)	(2)	(1,905,059)	(1)
Total Stockholders' Equity	135,005,396	69	126,648,435	64
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$195,442,333	100	$198,937,000	100

The accompanying notes are an integral part of the financial statements.
(With T N Soong & Co report dated January 24, 2003)

English Translation of Financial Statements Originally Issued in Chinese

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CHINA STEEL CORPORATION

STATEMENTS OF INCOME

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

	Years Ended December 31			
	2002		2001	
	Amount	%	Amount	%
REVENUES (Notes 2 and 18)	$ 99,939,846	100	$ 85,101,266	100
COST OF REVENUES (Note 18)	75,111,810	75	73,223,833	86
GROSS PROFIT	24,828,036	25	11,877,433	14
OPERATING EXPENSES				
Selling	1,815,948	2	1,602,713	2
General and administrative	1,818,975	2	2,030,550	2
Research and development	819,497	-	850,640	1
Total Operating Expenses	4,454,420	4	4,483,903	5
OPERATING INCOME	20,373,616	21	7,393,530	9
NONOPERATING INCOME				
Interest	238,543	-	660,107	1
Investment income (Note 6)	1,997,703	2	-	-
Gain on disposal of short-term investments	239,669	-	4,081,649	5
Other	683,378	1	969,223	1
Total Nonoperating Income	3,159,293	3	5,710,979	

				7
NONOPERATING EXPENSES				
Interest (Notes 7 and 18)	2,212,246	2	2,732,813	3
Investment loss (Note 6)	-	-	1,611,175	2
Other	624,849	1	353,722	1
Total Nonoperating Expenses	2,837,095	3	4,697,710	6
INCOME BEFORE INCOME TAX	20,695,814	21	8,406,799	10
INCOME TAX (Notes 2 and 16)	3,856,734	4	947,049	1
NET INCOME	$ 16,839,080	17	$ 7,459,750	9

(Forward)

	Years Ended December 31			
	2002		2001	
	Amount	%	Amount	%
BASIC EARNINGS PER SHARE (Note 17)				
Before tax	$ 2.29		$ 0.90	
After tax	$ 1.86		$ 0.80	
DILUTED EARNINGS PER SHARE (Note 17)				
Before tax	$ 2.28			
After tax	$ 1.86			
PRO FORMA INFORMATION - AS IF THE CORPORATION'S STOCK SHARES HELD BY SUBSIDIARIES WERE ACCOUNTED FOR AS INVESTMENTS RATHER THAN TREASURY STOCKS (Notes 3 and 15)				
Net income	$ 16,983,408			
Basic earnings per share based on weighted-average number of outstanding common shares of 9,117,994 thousand				
Before tax	$ 2.28			
After tax	$ 1.86			
Diluted earnings per share based on weighted-average number of outstanding common stock shares of 9,165,761 thousand				
Before tax	$ 2.27			
After tax	$ 1.85			

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

(With T N Soong & Co report dated January 24, 2003)

English Translation of Financial Statements Originally Issued in Chinese

CHINA STEEL CORPORATION

STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
For the Years Ended December 31, 2002 and 2001
(In Thousands of New Taiwan Dollars)

	CAPITAL STOCK		CAPITAL SURPLUS	RETAINED EARNINGS (Note 15)				UNREALIZED LOSS ON INVESTEES' LONG-TERM INVESTMENTS	CUMULATIVE TRANSLATION ADJUSTMENTS	INVESTEES' UNRECOGNIZED NET LOSS ON PENSION COST	TREASURY STOCK	TOTAL STOCKHOLDERS' EQUITY
	Preferred Stock	Common Stock	(Notes 7 and 15)	Legal Reserve	Special Reserve	Unappro-priated	Total	(Note 2)	(Note 2)			
BALANCES, JANUARY 1, 2001	$477,770	$ 87,483,626	$409,005	$ 17,477,198	$ 9,815,701	$ 19,087,182	$ 46,380,081	($149,728)	$ 53,726	$ -	$ -	$ 134,654,480
Conversion of preferred stock to common stock	(90)	90	-	-	-	-	-	-	-	-	-	-
Appropriation of prior year's earnings												
Legal reserve	-	-	-	1,858,154	-	(1,858,154)	-	-	-	-	-	-
Special reserve	-	-	-	-	96,001	(96,001)	-	-	-	-	-	-
Bonus to employees – stocks	-	489,126	-	-	-	(489,126)	(489,126)	-	-	-	-	-
Compensation to directors and supervisors	-	-	-	-	-	(48,913)	(48,913)	-	-	-	-	(48,913)
Cash dividends to preferred stockholders - 15%	-	-	-	-	-	(71,652)	(71,652)	-	-	-	-	(71,652)
Cash dividends to common stockholders - 15%	-	-	-	-	-	(13,122,557)	(13,122,557)	-	-	-	-	(13,122,557)
Stock dividends to preferred stockholders - 3%	-	14,330	-	-	-	(14,330)	(14,330)	-	-	-	-	-
Stock dividends to common stockholders - 3%	-	2,624,512	-	-	-	(2,624,512)	(2,624,512)	-	-	-	-	-
Purchases of treasury stock	-	-	-	-	-	-	-	-	-	-	(1,905,059)	(1,905,059)
Net income in 2001	-	-	-	-	-	7,459,750	7,459,750	-	-	-	-	7,459,750
Compensation payable to directors and supervisors transferred to capital surplus	-	-	6,317	-	-	-	-	-	-	-	-	6,317
Adjustment of equity in investees due to change in percentage of ownership	-	-	1,248	-	-	(34,717)	(34,717)	-	-	-	-	(33,469)
Unrealized loss on investees' long-term investments	-	-	-	-	-	-	-	(420,109)	-	-	-	(420,109)
Translation adjustments of long-term investments	-	-	-	-	-	-	-	-	145,155	-	-	145,155
Investees' unrecognized net loss on pension cost	-	-	-	-	-	-	-	-	-	(15,508)	-	(15,508)
BALANCES, DECEMBER 31, 2001	477,680	90,611,684	416,570	19,335,352	9,911,702	8,186,970	37,434,024	(569,837)	198,881	(15,508)	(1,905,059)	126,648,435
Conversion of preferred stock to common stock	(10)	10	-	-	-	-	-	-	-	-	-	-
Shares held by subsidiaries accounted for as treasury stock	-	-	-	-	-	-	-	-	-	-	(1,356,485)	(1,356,485)
Transfer of special reserve to unappropriated retained earnings	-	-	-	-	(2,200,000)	2,200,000	-	-	-	-	-	-
Appropriation of prior year's earnings												
Legal reserve	-	-	-	745,975	-	(745,975)	-	-	-	-	-	-
Special reserve	-	-	-	-	290,463	(290,463)	-	-	-	-	-	-
Bonus to employees – stocks	-	276,458	-	-	-	(276,458)	(276,458)	-	-	-	-	-
Compensation to directors and supervisors	-	-	-	-	-	(27,646)	(27,646)	-	-	-	-	(27,646)
Cash dividends to preferred stockholders - 12%	-	-	-	-	-	(57,322)	(57,322)	-	-	-	-	(57,322)
Cash dividends to common stockholders - 8%	-	-	-	-	-	(7,128,935)	(7,128,935)	-	-	-	-	(7,128,935)
Stock dividends to preferred stockholders - 2%	-	9,553	-	-	-	(9,553)	(9,553)	-	-	-	-	-
Stock dividends to common stockholders - 2%	-	1,782,234	-	-	-	(1,782,234)	(1,782,234)	-	-	-	-	-
Transfer of capital surplus from gain on disposal of properties to unappropriated earnings	-	-	(20,514)	2,051	-	18,463	20,514	-	-	-	-	-
Net income for 2002	-	-	-	-	-	16,839,080	16,839,080	-	-	-	-	16,839,080
Adjustment of equity in investees due to change in percentage of ownership	-	-	2,927	-	-	(51,407)	(51,407)	-	-	-	1,773	(46,707)
Reversal of unrealized loss on investees' long-term investments	-	-	-	-	-	-	-	14,346	-	-	-	14,346
Translation adjustments of long-term investments	-	-		-	-	-	-	-	23,510	-	-	23,510
Investees' unrecognized net loss on pension cost	-	-	-	-	-	-	-	-	-	(188)	-	(188)
Disposal of shares held by subsidiaries	-	-	6,004	-	-	-	-	-	-	-	14,694	20,698
Cash dividends declared by the Corporation and received by subsidiaries	-	-	76,610	-	-	-	-	-	-	-	-	76,610
BALANCES, DECEMBER 31, 2002	$477,670	$ 92,679,939	$481,597	$ 20,083,378	$ 8,002,165	$ 16,874,520	$ 44,960,063	($555,491)	$222,391	($15,696)	($3,245,077)	$ 135,005,396

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

(With T N Soong & Co report dated January 24, 2003)

English Translation of Financial Statements Originally Issued in Chinese

CHINA STEEL CORPORATION

STATEMENTS OF CASH FLOWS

(In Thousands of New Taiwan Dollars)

	Years Ended December 31	
	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$16,839,080	$7,459,750
Depreciation	11,335,753	11,954,277
Amortization	401,733	648,429
Deferred tax	354,706	(107,786)
Provision (reversal) of allowance for doubtful accounts	1,260	(615)
Provision (reversal) of allowance for loss on inventories	33,836	(241,685)
Investment loss (income) under the equity method	(2,566,906)	1,623,266
Long-term investment loss under the cost method	597,214	-
Loss on disposal of properties	64,678	43,865
Cash dividends on long-term investments under the equity method	1,343,998	148,894
Gain on disposal of short-term investments	(239,669)	(4,081,649)
Amortization of discount (premium) and exchange loss (gain) on forward exchange	5,073	(33,141)
Decrease (increase) in notes receivable	(233,648)	182,633
Decrease (increase) in accounts receivable	172,607	(87,424)
Decrease in inventories	2,869,309	934,393
Increase in other current assets	(167,940)	(827,578)
Increase in accounts payable	650,182	19,680
Increase (decrease) in income tax payable	3,730,522	(3,339,555)
Increase (decrease) in other payable	777,243	(1,250,553)
Increase (decrease) in other current liabilities	(176,119)	234,912
Net Cash Provided by Operating Activities	35,792,912	13,280,113
CASH FLOWS FROM INVESTING ACTIVITIES		
Increase in short-term investments	(7,305,143)	(917,378)
Increase in long-term investments	(1,148,397)	(2,617,955)

Acquisition of properties	(6,534,741)	(5,738,543)
Decrease (increase) in other assets	35,057	(1,622,360)
Decrease (increase) in pledged time deposits	1,300,000	(600,000)
Net Cash Used in Investing Activities	(13,653,224)	(11,496,236)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payment of cash dividends	(7,166,275)	(13,180,003)
Increase (decrease) in commercial paper payable	(1,844,905)	1,750,333
Increase (decrease) in short-term bank loans and overdraft	(5,138,225)	3,014,880
Decrease in long-term debts	(2,710,517)	(2,546,834)
Purchase of treasury stock	-	(1,905,059)
Decrease in payable on properties purchased	(637,539)	(4,202)

(Forward)

	Years Ended December 31	
	2002	2001
Increase (decrease) in bonds payable	($5,850,000)	$ 238,000
Compensation to directors and supervisors	(27,646)	(48,913)
Net increase in cash resulting from forward exchange contracts	2,210	38,478
Net Cash Used in Financing Activities	(23,372,897)	(12,643,320)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,233,209)	(10,859,443)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	4,302,175	15,161,618
CASH AND CASH EQUIVALENTS, END OF YEAR	$3,068,966	$4,302,175
SUPPLEMENTAL INFORMATION		
Interest paid, excluding capitalized amounts	$2,478,479	$2,952,306
Income tax paid		
Payment for prior years' income taxes	$ -	$3,088,787
Prepayment and withholding	23,450	1,263,214
Separate income tax on interest income	3,728	42,389
	$ 27,178	$4,394,390
NONCASH FINANCING ACTIVITIES		
Long-term liabilities due within one year	$12,185,045	$8,140,269
The Corporation's shares acquired and held by subsidiaries accounted for as treasury stock	$1,340,018	$ -

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

(With T N Soong & Co report dated January 24, 2003)

CHINA STEEL CORPORATION

NOTES TO FINANCIAL STATEMENTS
December 31, 2002 and 2001
(Amounts in Thousand New Taiwan Dollars, Unless Otherwise Stated)

1. GENERAL

The Corporation was incorporated in December 1971. It manufactures and sells steel products.

The Corporation 's stock is listed on the Taiwan Stock Exchange. As of December 31, 2002, the Ministry of Economic Affairs, Republic of China (MOEA - ROC) owned 40.8% of the Corporation' s outstanding common stock.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies of the Corporation, which conform to Guidelines for Securities Issuers' Financial Reporting and generally accepted accounting principles in ROC, are summarized below.

Cash equivalents

Cash equivalents represent commercial papers within three-month maturities.

Short-term investments

Short-term investments consist of bond funds and stocks listed on the Taiwan Stock Exchange and are stated at the lower of weighted-average cost or market value.

Market value represents net asset value of bond funds on the balance sheet date or average price of listed stocks in the last month of the period.

Allowance for doubtful accounts

Allowance for doubtful accounts is provided on the basis of the evaluation of the collectibility of individual receivables.

Inventories

Inventories consist of raw materials, supplies, fuel, finished products, work in process, by-products and construction in progress. Construction revenues are recognized by the percentage-of-completion method, and construction in progress is valued by the costs incurred plus (less) the estimated gain (loss). Other inventories are stated at the lower of weighted moving average cost or market value. Market value represents net realizable value for finished products, work in process, by-products and construction in progress; and replacement costs for raw materials, supplies and fuel.

Long-term investments

Long-term stock investments in which the Corporation owns 20% or more of the investees' voting stock or has significant influence on the investees are accounted for by equity method. If the financial statements of investee of which the Corporation owns not more than 50% of voting shares cannot be obtained on time, the Corporation will recognize investment gains or loss on related investments in June of the next year.

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. Unrealized gains or losses from transactions with investees and from transactions between investees are eliminated. Cash dividends received from investees are recorded as a deduction in the investment carrying value. Translation adjustments, unrealized loss on investees' long-term investments and investees' unrecognized net loss on pension cost are recognized proportionately to the Corporation's shareholdings. When the investee issues additional shares but the Corporation does not acquire shares at a ratio equal to its initial equity, the Corporation's ownership percentage is changed. As a result, capital surplus is adjusted for the difference between the carrying values of the investments and the Corporation's equity in the investees' net assets. If the carrying value is less than equity in net assets, the difference is credited to capital surplus. If the carrying value is more than equity in net assets, the difference is debited to capital surplus; if capital surplus is not enough, the difference will be debited to unappropriated earnings. If the market prices of investees decline significantly and the decline is other than temporary, the investment loss decline should be recognized as realized loss in the same year of the decline. Such investment will be reevaluated by equity method if an investee's market value becomes higher than book value per share. The difference between the new cost of the investment and proportionate equity in the investee is amortized over five years.

Other investments are accounted for by cost method. If certain evidences indicate that the market value of investments has significantly declined and the decline is other than temporary, the decline should be recognized as realized investment loss. The previous carrying value less the amount of write-down becomes the new cost basis for such investments.

Properties and other assets

Properties and other assets (leased assets) are stated at cost or cost plus appreciation less accumulated depreciation. Interest expense arising from the purchase or construction of properties is capitalized as cost. Major additions, renewals and betterments are capitalized while maintenance and repairs are expensed currently.

Depreciation of properties is calculated by straight-line method over service lives estimated as follows: land improvements, 10 to 40 years; buildings and improvements, 4 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 provided by the straight-line method over the remaining service lives of the revalued assets. When a property reaches its original service life but is still in use, its residual value is written off over its reestimated service life.

Depreciation of machinery and equipment leased to the Corporation's investee (under other assets-leased assets) is calculated by the working hours method.

Upon sale or disposal of property, the related cost, appreciation and accumulated depreciation are removed from the accounts. Gains or losses are credited or charged to current income. Before 2000, any such gains, net of applicable income tax, are transferred to capital surplus at year-end.

Unamortized repair expense

Unamortized repair expense refers to the major repair of blast furnaces and is amortized by the straight-line method over fives years.

Treasury stock

Treasury stock is stated at cost, and its book value is presented as a reduction to arrive at stockholders' equity. Effective 2002, the Corporation's shares acquired and held by subsidiaries are accounted for as treasury stocks.

Revenue recognition

Revenues are recognized when titles to products and risks of ownership are transferred to customers (domestic sales - when products are taken out of the Corporation's premises for delivery to customers; exports - when products are loaded onto vessels.)

Pension

Pension costs are recognized on the basis of actuarial calculations. The difference between the pension costs recognized and the amount appropriated to a special fund (Note 13) is recognized as accrued pension liabilities. Pension benefits paid in excess of the fund and accrued pension liabilities are charged to expense.

Income tax

Income tax is provided on the interperiod allocation basis. Tax effects on deductible temporary differences and unused tax credits 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. 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 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.

The tax credits from expenditures for certain purchase of equipment, research and development, and employees' training costs are recognized as income tax credits when those credits are granted.

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

Annual earnings should be appropriated under a resolution passed in the stockholders' meeting in the next year. Under tax regulations, unappropriated earnings are subject to 10% income taxes. These taxes are recorded as expenses when the stockholders resolve to retain the earnings.

Foreign-currency transactions

Foreign-currency transactions, except derivative financial instruments, 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 different exchange rates when foreign-currency receivables and payables are settled, are credited or charged to income in the year of settlement. On the balance sheet date, foreign-currency assets and liabilities are restated at prevailing exchange rates, and resulting adjustments are credited or charged to income. The changes in the Corporation's investments in foreign subsidiaries from exchange rate are shown as cumulative translation adjustments under stockholders' equity.

Derivative financial instruments

Forward exchange transactions entered into as hedge for foreign-currency net assets or net liabilities are recorded in New Taiwan dollars at spot rates on the date of each forward contract. The differences between spot rates and forward rates are amortized over the period of each forward contract and recognized as gains or losses. Year-end balances of forward exchange contracts are restated at the prevailing exchange rates, and the resulting adjustments are credited or charged to income. Exchange gains or losses on forward exchange transactions entered into as hedge for foreign-currency commitments are deferred as adjustments to transaction prices.

The related receivable and payable balances for forward contracts are netted against each other, and the resulting balance is accounted for as either current asset or liability.

Earnings per share

Basic earnings per share (EPS) equals:

$$\frac{\text{Net income} - \text{preferred dividends}}{\text{Weighted average of common shares outstanding}}$$

For diluted EPS, the formula is the same as the above but the numerator and denominator include the effect of outstanding preferred shares using the if-converted method.

3. ACCOUNTING CHANGE

Under the Statement of Financial Accounting Standards No. 30- "Treasury Stock" of ROC and a related ruling issued by the ROC's Securities & Futures Commission, the Corporation's shares acquired and held by its subsidiaries should be accounted for as treasury stock effective 2002. As a result, the Corporation reclassified the stock shares acquired by its subsidiaries from long-term investments to treasury stock. The reclassification is based on the book value of the shares as of the start of 2002. The effects of this accounting change on the Corporation's financial statements as of December 31, 2002 were as follows: (a) decreases in long-term investments by NT$1,883,432 thousand, retained earnings by NT$144,328 thousand and net income by NT$144,328 thousand; and (b) increases in treasury stock by NT$1,340,018 thousand, unrealized loss on long-term investments by NT$481,700 thousand and capital surplus by NT$82,614 thousand.

4. SHORT-TERM INVESTMENTS

	2002	2001
Bond funds	$18,783,880	$11,239,068
Stocks listed on the Taiwan Stock Exchange	967,456	967,456
	$19,751,336	$12,206,524

5. INVENTORIES

	2002	2001
Finished products	$3,742,381	$4,725,721
Work in process	4,480,124	6,764,375
Raw materials	2,813,293	3,002,420
Supplies	3,343,868	3,265,255
Fuel	84,580	78,605
Constructions in progress	2,545	-
Materials in transit and unallocated freight expenses	1,135,651	624,558
Others	35,723	46,540
	15,638,165	18,507,474
Allowance for losses	169,689	135,853
	$15,468,476	$18,371,621

6. LONG-TERM INVESTMENTS

	2002		2001	
	Amount	% of Ownership	Amount	% of Ownership
Stocks - under equity method				
C. S. Aluminum Corporation (CAC)	$5,857,035	98	$5,508,891	98
China Steel Express Corporation (CSE)	5,492,165	100	5,519,921	100
Gains Investment Corporation (GIC)	4,936,000	100	4,189,482	100
China Prosperity Development Corporation (CPDC)	4,070,362	100	4,090,900	100
Kaohsiung Rapid Transit Corporation (KRTC)	3,139,515	31	3,012,620	37
China Steel Asia Pacific Holdings Pte Ltd (CSAPH)	2,164,996	100	1,646,053	100
China Steel Global Trading Corporation (CSGT)	1,055,353	100	861,286	100
Taisil Electronic Materials Corporation (TEM)	1,031,691	35	1,009,937	35
China Steel Chemical Corporation (CSCC)	810,063	31	778,433	31
China Steel Machinery Corporation (CSMC)	755,105	100	803,300	100
Kuei Yi Industrial Co. (KYIC)	557,098	30	592,916	30
Info-Champ Systems Corporation (ICSC)	506,463	99	462,204	100
China Hi-ment Corporation (CHC)	489,784	20	480,268	20
China Steel Structure Corporation (CSSC)	467,871	18	465,463	18

Yieh Loong Enterprises Corporation (YLEC)	370,175	24	249,768	24

(Forward)

	2002		2001	
	Amount	% of Owner-ship	Amount	% of Owner-ship
China Ecotek Corporation (CEC)	$ 364,215	36	$ 365,502	36
Goang Yaw Investment Corporation and other two companies	279,294	100	168,097	100
China Steel Security Corporation (CSS)	205,383	100	193,051	100
Taiwan Rolling Stock Co., Ltd. (TRSC)	160,647	27	-	-
Phalanx Biotech Group (PBG)	100,000	21	-	-
Hi-mag Magnetic Corporation (HMC)	-	50	103,571	50
GenMont Biotech Inc. (GMB)	-	-	60,990	17
	32,813,215		30,562,653	
Less: Shares held by subsidiaries accounted for as treasury stock	1,340,018		-	
	31,473,197		30,562,653	
Stocks - under cost method				
Eastern Broadband Telecommunications Co., Ltd.	1,200,000	2	1,200,000	2
Industrial Bank of Taiwan	1,000,000	4	1,000,000	4
Tang Eng Iron Works Corporation (TEIWC)	-	9	597,214	9
CDIB & Partners Investment Holding Corporation (Southeast Asia Investment Holding Corporation)	500,000	5	500,000	5
Overseas Investment & Development Corporation	50,000	6	50,000	6
Maruichi Steel Tube Ltd.	757,919	2	715,550	2
Advanced Material Technology Corporation	249,349	3	182,200	3
GenMont Biotech Inc. (GMB)	60,990	17	-	-
CDIB BioScience Ventures I, Inc.	120,000	5	-	-
	3,938,258		4,244,964	
Prepayments for investments				
CDIB BioScience Ventures I, Inc.	-		120,000	
Others	120,831		98,794	
	$35,532,286		$35,026,411	

As of December 31, 2002, the Corporation's total shareholdings in YLEC was 39.3%: 23.7% directly owned and 15.6% indirectly owned.

In September 2001, the Corporation invested $799,930 in CSMC, a wholly owned subsidiary. The subsidiary mainly manufactures, sells and maintains machinery and equipment.

In September 2001, the Corporation invested $60,000 in GMB, representing 22% shareholdings. GMB does biotechnology research and related production and sales. In December 2001, GMB had a capital increase, but the Corporation did not acquire shares in proportion to its original equity. Thus, the Corporation’s ownership decreased to 17%, and the Corporation’s investment in GMB started to be accounted for by cost method in 2002.

In September 2002, the Corporation invested $120,000 in CDIB BioScience Ventures I, Inc., representing 4.8% shareholdings.

In August 2002, the Corporation increased the investment in CSAPH by $169,022 (US$5,000,658). CSAPH used this amount to increase its investment in Ornasteel Enterprise Corporation (M) Sdn. Bhd. Thus, the Corporation' s stockholdings in Ornasteel Enterprise was increased from 70% to 72.27%.

In October 2002, the Corporation invested $160,000 in TRSC, representing 27% shareholdings. TRSC mainly manufactures, sells, and rents motor-trolleys and parts.

In October 2002, the Corporation invested $100,000 in PBG, representing 21% shareholdings. PBG mainly does biochip research and production.

In October 2002, GYIC and other eight investment companies were merged into three companies through capital decrease.

In 2002, the Corporation' s shareholdings in KRTC and ICSC decreased because the Corporation did not acquire shares in proportion to the original equity when KRTC issued additional shares and because CSS issued stock bonus to its employees.

The Corporation' s Board of Directors approved plans for additional investments of up to $3,641,802 in GIC, KRTC, KYIC and CPDC in 2002 and 2001. The related implementation schedule depends on the investees' schedules. As of December 31, 2002, the Corporation' s investment in GIC and KRTC had increased to $1,137,340.

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

	2002	2001
CSE	$ 942,184	$1,078,403
CAC	506,560	172,057
CSAPH	350,737	(70,166)
CSGT	200,083	102,891
CSCC	170,643	152,440
GIC	168,695	238,318
YLEC	120,407	(2,150,506)
Goang Yaw Investment Corporation and other two companies	111,202	(994,887)
ICSC	83,858	84,691
CHC	42,180	38,127
TEM	21,754	(37,573)
CSSC	18,959	71,051
CSS	11,674	9,672
CEC	8,390	22,656
TRSC	647	-
CPDC	(7,682)	5,724
KRTC	(1,108)	(2,510)
KYIC	(30,518)	(330,739)
CSMC	(48,195)	3,370

HMC	(103,564)	(15,763)
GMB	-	(522)
	$2,566,906	($1,623,266)

In 2001, the stock price of YLEC dropped significantly. The Corporation recognized an investment loss of $1,584,382 based on the year-end market price. However, in 2002, the stock price of YLEC recovered to a level higher than its book value per share, and YLEC had profitable operations in 2002. The investment in YLEC started to be accounted for by equity method in November 2002, according to the interpretation issued by the Accounting Research and Development Foundation of the Republic of China.

Investment income (loss) as presented in the statements of income are as follows:

	2002	2001
Long-term investment income (loss) under the equity method	$2,566,906	($1,623,266)
Long-term investment loss under the cost method - TEIWC	(597,214)	-
Cash dividends	28,011	12,091
	$1,997,703	($1,611,175)

The Corporation fully recognized the balances of its investments in HMC and TEIWC as losses to reflect the these investees' operation losses.

The Corporation has prepared consolidated financial statements to include CAC, the only subsidiary with individual total assets or total operating revenue more than 10% of those of the Corporation in 2002 and 2001. For other subsidiaries, the total assets and total revenues of individual subsidiaries, of which the Corporation owned more than 50% shares, are each less than 10% of those of the Corporation, respectively, and the total assets and total revenues of all subsidiaries are each less than 30% of the Corporation's total assets and revenues, respectively. Therefore, those subsidiaries are not considered as entities for preparing consolidated financial statements.

7. PROPERTIES

	Cost	Appreciation	Total
December 31, 2002			
Cost and appreciation			
Land	$ 7,146,632	$ 5,850,597	$12,997,229
Land improvements	4,316,764	492,990	4,809,754
Buildings and improvements	35,814,229	2,445,529	38,259,758
Machinery and equipment	207,628,941	9,539,413	217,168,354
Transportation equipment	1,596,970	39,186	1,636,156
Miscellaneous equipment	2,826,054	35,292	2,861,346
	259,329,590	18,403,007	277,732,597
Accumulated depreciation			
Land improvements	2,667,778	356,083	3,023,861
Buildings and improvements	12,800,874	1,456,137	14,257,011

Machinery and equipment	146,769,102	9,523,943	156,293,045
Transportation equipment	1,268,771	39,058	1,307,829

(Forward)

	Cost	Appreciation	Total
Miscellaneous equipment	$ 2,159,762	$ 35,261	$ 2,195,023
	165,666,287	11,410,482	177,076,769
Constructions in progress	6,815,268	-	6,815,268
	$100,478,571	$ 6,992,525	$107,471,096
December 31, 2001			
Cost and appreciation			
Land	$ 6,764,647	$ 5,850,597	$12,615,244
Land improvements	4,316,764	492,990	4,809,754
Buildings and improvements	35,664,534	2,445,529	38,110,063
Machinery and equipment	207,043,084	9,542,254	216,585,338
Transportation equipment	1,594,481	39,186	1,633,667
Miscellaneous equipment	2,651,344	35,299	2,686,643
	258,034,854	18,405,855	276,440,709
Accumulated depreciation			
Land improvements	2,489,300	336,638	2,825,938
Buildings and improvements	11,899,016	1,398,209	13,297,225
Machinery and equipment	138,412,627	9,520,466	147,933,093
Transportation equipment	1,189,708	38,936	1,228,644
Miscellaneous equipment	2,056,427	35,256	2,091,683
	156,047,078	11,329,505	167,376,583
Constructions in progress	3,183,839	-	3,183,839
	$105,171,615	$ 7,076,350	$112,247,965

The Corporation constructed and acquired certain properties (e.g., factories or equipment) through bank loans. Information on interest capitalization is as follows:

	2002	2001
Total interest expense	$2,346,195	$2,886,755
Interest expense capitalized (under constructions in progress)	133,949	153,942
Interest rate for capitalization	5.23%	5.66%

In 1981 and 1994, the Corporation revalued its properties and patents in accordance with government regulations, resulting in an increment of $17,662,343. After the deduction of the reserve for land value increment tax of $3,370,813, an increment of $14,291,530 was credited to capital surplus. As of December 31, 2002, a capital surplus of $13,952,356 had been transferred to a capital account.

8. OTHER ASSETS

	2002	2001
Rental properties (Notes 2, 12 and 18)		
Land - at cost	$2,966,398	$2,951,652
Machinery and equipment - at cost, less accumulated depreciation of $1,077,937 and $974,369 as of December 31, 2002 and 2001, respectively	922,063	1,025,631
	3,888,461	3,977,283
Unamortized repair expenditures - major repair for blast furnaces (Note 2)	717,408	1,114,329
Other	251,677	291,545
	$4,857,546	$5,383,157

The Corporation has leased to its subsidiaries some of its plant property and machinery acquired through a loan from the National Defense Industrial Development Fund.

9. SHORT-TERM BANK LOANS AND OVERDRAFT

	2002	2001
Credit loans - due within 180 days, interest at 1.875% p.a. and 2.45%-2.56% p.a., as of December 31, 2002 and 2001, respectively	$ 400,000	$4,700,000
Letters of credit - due within 180 days, interest at 0.26%-4.5% p.a. and 0.33%-4.56% p.a., as of December 31, 2002 and 2001, respectively	367,321	172,961
Overdraft - interest at 6.375% p.a. and 2.65%-6.79% p.a., as of December 31, 2002 and 2001, respectively	42,367	1,074,952
	$ 809,688	$5,947,913

As of December 31, 2002, the Corporation provided time deposits of $6,900,000 as collaterals for short-term borrowings. The unused credit lines for short-term borrowings aggregated about $49,223,031.

10. COMMERCIAL PAPER PAYABLE

	2002	2001
Commercial paper - interest at 1.49% p.a. and 2%-3.47% p.a. as of December 31, 2002 and 2001, respectively	$1,000,000	$2,850,000
Unamortized discounts	(1,653)	(6,748)
	$ 998,347	$2,843,252

11. LONG-TERM BONDS PAYABLE

	2002	2001
5-year unsecured bonds - issued at par in:		
November 2001, payable in November 2006; interest at 3.1% p.a., payable annually	$3,500,000	$3,500,000
November 2001, payable in November 2006; interest at 3.0763% p.a., compounded semiannually and payable annually	1,500,000	1,500,000
June 2001, payable in June 2006; interest at 4.27% p.a., payable annually	5,000,000	5,000,000
November 2000, payable in December 2005; interest at 5.18% p.a., payable annually	5,000,000	5,000,000
July 1999, payable in July 2004; interest at 5.99%p.a., compounded semiannually and payable annually	2,250,000	2,250,000
May 1999, payable in June 2004; interest at 5.69% p.a., compounded semiannually and payable annually	7,750,000	7,750,000
November 1998, payable in two equal installments in 2002 and 2003; interest at 6.785% p.a., compounded semiannually and payable annually	2,500,000	5,000,000
May 1998, payable in three annual installments from May 2001 through May 2003; interest at 7.4% p.a., compounded semiannually and payable annually	1,700,000	3,350,000
June 1997, interest at 6.5% p.a., repaid in June 2002	-	1,700,000
4-year unsecured bond - issued at par in March 1999, payable in March 2003; interest at 6.5% p.a., compounded semiannually and payable annually	5,000,000	5,000,000
	34,200,000	40,050,000
Current portion	(9,200,000)	(5,850,000)
	$25,000,000	$34,200,000

12. LONG-TERM DEBTS

	2002	2001
Equipment import loans:		
Sumitomo Bank - payable in 10 equal installments from August 1998 to February 2003, interest at 6.715% p.a.	$ 173,765	$ 525,000
Kreditanstalt fur Wiederaufbau - interest at 6.4% - 6.99% p.a., repaid in September 2002	-	1,023,992
West Merchant Bank - interest at 5.38% p.a., repaid in April 2002	-	286,287
Hitachi Zosen Corporation - interest at 6.99% p.a., repaid in February 2002	-	68,133

	2002	2001
Mortgage bank loan on machinery and equipment:		
Payable in June 2004, floating rates at 3.125% p.a. and 4.95% p.a., as of December 31, 2002 and 2001, respectively (Note 19)	50,000	50,000
Payable in March 2003, floating rates at 3.125% p.a. and 4.95% p.a., as of December 31, 2002 and 2001, respectively (Note 19)	2,050,000	2,050,000
Payable in December 2003, interest rate at 1.0466% p.a. (Note 19)	761,280	698,360
(Forward)		
Loan from National Defense Industrial Development Fund (NDIDF) - floating rate at 5.60% p.a. as of 2001, repaid in May 2002	$ -	$1,043,790
	3,035,045	5,745,562
Current portion	(2,985,045)	(2,290,269)
	$ 50,000	$3,455,293

The Corporation assumed the balance of NDIDF's loan (repayable from July 1989 to June 2003) and acquired the related machinery and equipment (M&E) from a third party. The repayment of this loan is based on the M&E depreciation charges based on the quantity of aluminum products sold by CAC and a percentage of CAC's profit based on the ratio of the M&E cost to CAC's aluminum-producing M&E. In May 2002, the Corporation fully settled the loans and got the titles to the M&E, which the Corporation later leased to CAC (Note 8).

13. PENSION PLAN

The Corporation has a pension plan for all regular employees, which provides pension benefits based on length of service and monthly average salary of the year before retirement.

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

	2002	2001
Balance, beginning of year	$6,735,145	$5,563,997
Contributions	1,093,563	841,095
Interest income	258,275	383,699
Payment of benefits	(43,473)	(53,646)
Balance, end of year	$8,043,510	$6,735,145

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

	2002	2001
Balance, beginning of period	$ 16,462	$ 17,350
Contributions	2,787	2,746
Interest income	546	840
Payment of benefits	(3,478)	(4,474)
Balance, end of period	$ 16,317	$ 16,462

Pension information based on actuarial calculation is as follows:

	2002	2001
a. Pension cost components		
Service cost	$1,024,132	$ 927,329
Interest cost	343,664	319,739
Expected return on plan assets	(367,027)	(382,682)
Amortization	(9,536)	(11,295)
Net Pension Cost	$ 991,233	$ 853,091
b. Reconciliation of the funded status of the plan and accrued pension liability		
Benefit obligation		
Vested	$ 122,887	$ 91,791
Non-vested	6,350,226	4,243,613
Accumulated	6,473,113	4,335,404
Additional benefits based on future salaries	2,517,629	2,554,475
Projected	8,990,742	6,889,879
Fair value of plan assets	(8,231,496)	(6,993,420)
Funded status	759,246	(103,541)
Unrecognized net asset at transition	109,663	119,199
Unamortized net actuarial gain (loss)	(814,964)	137,604
Accrued pension liabilities (under other current liabilities)	$ 53,945	$ 153,262

The difference between the pension fund and the fair value of plan assets as of December 31, 2002 and 2001 represented the accrued interest income of the fund.

	2002	2001
c. Vested benefits	$ 133,642	$ 94,379

d. Actuarial assumptions

Discount rate used in determining present values	3.5%	5.0%
Future salary increase rate	3.0%	4.0%
Expected rate of return on plan assets	3.5%	5.0%

14. OTHER LIABILITIES

	2002	2001
Deferred income tax liabilities (Note 16)	$3,584,788	$4,256,172
Deferred revenue	1,405,040	1,405,040
	$4,989,828	$5,661,212

Deferred revenue is the unrealized gain from the February 1999 sale of lands to a subsidiary, China Prosperity Development Corporation.

15. STOCKHOLDERS' EQUITY

a. Treasury stock

Purpose	Thousand Shares: Beginning of Year	Increase	Decrease	December 31, 2002: Thousand Shares	Amount
2002					
Shares acquired for transfer to employees	150,000	-	-	150,000	$1,905,059
Shares acquired and held by subsidiaries	96,026	1,778	994	96,810	1,340,018
	246,026	1,778	994	246,810	$3,245,077
2001					
Shares acquired for transfer to employees	-	150,000	-	150,000	$1,905,059

1) Shares acquired for transfer to employees

In 2001, the Corporation acquired its common stocks for transfer to employees. The shares transferred amounted to 149,964 thousand shares in January 2003, resulting in decreases of $82,614 in capital surplus and $14,863 in retained earnings.

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 retained earnings plus 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. These shares are deemed unissued if they are not transferred on time and the Corporation should then register with the government a capital decrease. Further, the Corporation should not pledge these stocks as collateral and is not entitled to dividends and or the exercise of voting rights on these stocks.

2) Shares acquired and held by subsidiaries

As stated in Note 3, the Corporation's shares acquired and held by subsidiaries were accounted for as treasury stocks at their book value as of January 1, 2002. As of December 31 2002, the treasury stock carrying value was $1,340,018 and market value was $1,896,516.

Although these shares are treated as treasury stocks in the financial statements, the stockholders are entitled to exercise their rights on these stocks, except participation in capital increase by cash.

b. Overseas depositary receipts

In May 1992 and February 1997, the ROC's Ministry of Economic Affairs sold 20,537,550 units of Global Depositary Receipts (GDR) and 7,631,800 units of Rule 144A American Depositary Receipts (ADR) to international investors, with each unit representing 20 shares of the Corporation's common stock. The depositary shares increased by 3,506,236 units when retained earnings were capitalized. Under relevant regulations, the GDR or ADR holders may request, after holding the depositary receipts for three months, the domestic sale of the shares represented by the GDR or ADR. As of December 31, 2002, the outstanding depositary shares were 9,950,197 units, equivalent to 199,004,056 common shares and 2% of the issued common shares.

c. 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 option of the Corporation 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.

d. Capital surplus

Following are the capital surplus sources:

	2002	2001
Revaluation increment on assets (Note 7)	$339,174	$339,174
Purchase of treasury stock	82,614	-
Long-term investment under equity method	51,710	48,783
Gain on disposal of properties	-	20,514
Others	8,099	8,099
	$481,597	$416,570

Under relevant regulations, the capital surplus from revaluation increment on assets can only be used to offset a deficit. Capital surplus from treasury stock can be used to offset a deficit or transferred to capital. Capital surplus from long-term investment under equity method is prohibited from any use. The capital surplus from gain on disposal of properties has been transferred to retained earnings based on resolution of the stockholders' meeting in 2002.

e. Appropriation of retained earnings

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

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

2) Preferred stock dividends at 14% of aggregate par value;

3) Of the remainder, 0.3% as compensation to directors and supervisors and 3% as bonus to employees;
4) Common-stock dividends at 14% of aggregate par value; and

5) The remainder, if any, as additional dividends divided equally among 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 aggregate par value, 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. If the market price is lower than the carrying value of the Corporation's shares held by subsidiaries, the Corporation should appropriate 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 life cycle of the Corporation's steel industry is in the phase of stable growth, and the appropriation of dividends and bonus should be at more than 75% in cash and less than 25% in stock. However, subject to the need for working capital to further develop the Corporation's business, the Corporation may decrease the cash dividend appropriation.

Under the Company Law, legal reserve may be used to offset a deficit. When the reserve has reached 50% of paid-in capital, up to 50% thereof may be transferred to capital.

f. Effect of bonus to employee and compensation to directors and supervisors

In their June 2002 meeting, the Corporation's stockholders approved the 2001 earnings appropriation, which was proposed by the Board of Directors in March 2002. The appropriation of employee bonus and compensation to directors and supervisors was as follows:

	Amount	Shares (Thousands)	Percentage to Common Shares Outstanding as of December 31, 2001 (%)
Bonus to employee - stock	$276,458	27,646	0.31
Compensation to directors and supervisors - cash	27,646	-	-
	$304,104		

Had the bonus to employee and compensation to directors and supervisors been charged to expense in 2001 (stock bonus calculation was based on par value), the basic earnings per share (after tax) for 2001 would have decreased from $0.80 to $0.77, giving effect of the retroactive adjustment of capitalization of retained earnings in 2002.

As of the auditors' report date, the appropriation of 2002 earnings had not been proposed by the Board of Directors. Information on the Board of Directors' proposed appropriation of the 2002 earnings and related stockholders' may be accessed through the Web site of the Taiwan Stock Exchange Corporation.

g. 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. Non-resident stockholders, including holders of overseas depository receipts, are allowed only a tax credit from the 10% income tax on undistributed earnings, which can be the withholding income tax on dividends paid.

As of December 31, 2002, the balance of the Imputation Credit Account (ICA) aggregated $94,023, equivalent to 22.78% of the 2002 undistributed earnings. This percentage may change depending on the ICA balance on the dividend distribution date. In June 2002, the Corporation distributed the 2001 earnings, and the ratio of tax credits allocated to stockholders was 29.38%.

As of December 31, 2002, undistributed earnings up to 1997 amounted to $86,848, which is not subject to the Imputation Tax System.

16. INCOME TAX

	2002	2001
Tax on pretax income at statutory rate (25%)	$5,173,954	$2,101,700
Add (deduct) tax effects of differences:		
Depreciation	698,814	492,597
Investment income - net	(555,597)	(617,619)
Provision (reversal) of allowance for loss on inventories	8,459	(60,422)
Realized foreign exchange loss - net	(24,695)	(93,373)
Investment loss due to a reduction in investees' capital	(355,490)	-

Others	34,153	(35,958)

(Forward)

	2002	2001
Income tax payable	$4,979,598	$1,786,925
Tax benefit from investment tax credit	(1,756,015)	(798,664)
Separate income tax on interest income	3,728	42,389
Tax on undistributed earnings	430,506	274,949
Deferred tax adjustments	354,706	(107,786)
Prior periods' adjustments	(155,789)	(250,764)
Income tax	$3,856,734	$ 947,049

Deferred income tax assets and liabilities were as follows:

	2002	2001
Current (included in other current assets)		
Deferred income tax assets		
Provision for Loss on inventories	$ 42,422	$ 33,963
Others	27,944	11,271
	$ 70,366	$ 45,234
Noncurrent (included in other liabilities)		
Deferred income tax assets		
Unrealized foreign exchange loss	$ 8,070	$ 32,766
Others	3,210	5,573
	11,280	38,339
Deferred income tax liabilities		
Depreciation difference	(3,596,068)	(4,294,511)
Deferred income tax liabilities, net	($3,584,788)	($4,256,172)

The temporary difference from depreciation resulted from differences in depreciation methods between tax reporting and financial reporting.

Income tax payable is net of prepaid taxes.

The Corporation's income tax returns through the year ended December 31, 1999 had been examined by tax authorities.

17. EARNINGS PER SHARE

Following is the reconciliation of the numerators and denominators used in calculating basic and diluted earnings per share (EPS) for the years ended December 31, 2002 and 2001:

2002	Numerator-Amount Before Tax	Numerator-Amount After Tax	2002	Denominator (Thousand Shares)
Net income	$ 20,695,814	$ 16,839,080	Weighted average of issued common shares	9,267,994
Less: Dividends to preferred stocks	82,190	66,874	Less: Weighted average of treasury stocks	
			- Purchased by the Corporation	150,000
			- Held by subsidiaries	96,810
Basic EPS				
Net income belonging to common stockholders	20,613,624	16,772,206		9,021,184
Effect of potential dilutive shares: 14% cumulative and convertible preferred stocks	82,190	66,874		47,767
Diluted EPS				
Net income belonging to common stockholders and effect of potential dilutive shares	$ 20,695,814	$ 16,839,080		9,068,951

2001	Numerator-Amount Before Tax	Numerator-Amount After Tax	2001	Denominator (Thousand Shares)
Net income	$ 8,406,799	$ 7,459,750	Weighted average of issued common shares	9,061,168
Less: Dividends to preferred stockholders	75,365	66,875	Add: Retroactive adjustments for capitalization of retained earnings	206,825
			Less: Weighted average of treasury stocks	29,925
Net income belonging to common stockholders	$ 8,331,434	$ 7,392,875		9,238,068

The number of shares is retroactively adjusted for the effect of retained earnings capitalization on EPS calculation. Thus, EPS before tax and after tax decreased from $0.92 to $0.90 and from $0.82 to $0.80, respectively, for the year ended December 31, 2001.

18. RELATED-PARTY TRANSACTIONS

a. Related party

Related party	Relationship
C. S. Aluminum Corporation (CAC)	Investee
China Steel Express Corporation (CSE)	Investee
China Steel Chemical Corporation (CSCC)	Investee
China Steel Global Trading Corporation (CSGT)	Investee
China Hi-ment Corporation (CHC)	Investee
China Ecotek Corporation (CEC)	Investee
China Steel Structure Corporation (CSSC)	Investee

(Forward)

	Relationship
Info-Champ Systems Corporation (ICSC)	Investee
China Steel Security Corporation (CSS)	Investee
Yieh Loong Enterprises Corporation (YLEC)	Investee
China Steel Machinery Corporation (CSMC)	Investee
Hi-mag Magnetic Corporation (HMC)	Investee
Kuei Yi - Industrial Co., (KYIC)	Investee
WABO Global Trading Corporation (WGTC)	Substantially indirect investee
Chung Mao Trading (BVI) Corp. (CSGT-BVI)	Substantially indirect investee
Jyh Yang management Corporation (JYCC)	Substantially indirect investee
Ornasteel Enterprise Corp. (M) Sdn. Bhd (OEC)	Substantially indirect investee
Universal Exchange Inc. (UEI)	Substantially indirect investee
United Steel Engineering and Construction Corporation (USECC)	Substantially indirect investee
Tang Eng Iron Works Corporation (TEIWC)	CSC is a director of TEIWC

b. Significant related-party transactions:

	2002		2001	
	Amount	%	Amount	%
Sales				
YLEC	$4,818,301	5	$3,881,438	4
OEC	1,972,908	2	2,288,702	3
CSSC	1,855,559	2	1,468,761	2
CSCC	774,343	1	629,120	1
Others	1,006,392	1	342,706	-
	$10,427,503	11	$8,610,727	10
Purchases				
CSE (Import freight)	$5,225,821	14	$5,399,623	16
CAC	1,523,332	5	1,604,718	5
Others	625,513	2	479,949	1
	$7,374,666	21	$7,484,290	22

Sales to and purchases from related parties are made under normal arms-length terms, except those with OEC, CSCC, CAC and CSE due to no comparison data.

Land and office lease

The Corporation leases its land and office to CAC, CSSC, CHC, CSCC, UEI, CSMC, etc. Annual rentals are calculated at 4% to 10% of land value as published by the government or under normal arms-length terms. Lease information is as follows:

	Expiry Date	Rental Income 2002	Rental Income 2001
CAC	February 2016	$ 47,318	$ 47,315
CSCC	December 2010	26,311	25,018
CSMC	November 2011	24,858	-
CSSC	May 2018	15,716	15,738
CHC	April 2012	5,012	5,134
UEI	September 2003	2,724	3,258
Others		1,733	618
		$123,672	$ 97,081

Property purchase

The Corporation signed a contract to buy from HMC land and factories for $202,704, based on independently appraised value. The total amount had been paid as of December 31, 2002.

Factoring of notes receivable

The Corporation sold some of its notes receivable to JYCC without recourse for $3,630,869 and $2,615,582 as of December 31, 2002 and 2001, respectively. The related interest expenses were $51,400 in 2002 and $57,916 in 2001.

Other expenditures

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

	2002	2001
CEC	$ 558,545	$ 788,156
USECC	432,028	477,734
CSSC	394,070	321,875
CHC	338,909	452,682
CSE	323,828	326,452
Others	878,602	900,476
	$2,925,982	$3,267,375

Other revenues

Other revenues pertained to labor services, processing of products, liquid waste processing and recycling, and other services to related parties.

	2002	2001
TEIWC	$ 588,434	$ 618,027
CAC	119,730	142,939
CEC	99,987	7,887
CSCC	49,832	52,207
KYIC	44,801	17,185
CSSC	38,818	34,363
Others	59,696	119,835
	$1,001,298	$ 992,443

b. Balances at year-end

	2002		2001	
	Amount	%	Amount	%
Receivables				
CSCC	$ 67,588	3	$ 44,844	2
OEC	52,462	3	127,044	7
CSSC	40,125	2	28,865	1
TEIWC	36,444	2	212,609	10
Others	37,572	2	101,483	6
	$234,191	12	$514,845	26
Payables				
CSE	$321,699	13	$184,110	7
CAC	104,218	4	42,217	2
Others	12,820	-	5,015	-
	$438,737	17	$231,342	9

19. PLEDGED ASSETS

a. Time deposits of $6,931,396 and $8,231,396 (included in pledged time deposits and other assets) as of December 31, 2002 and 2001, respectively, were pledged mainly as collateral for bank overdraft, etc.

b. The Corporation provided 20,000,000 shares of CAC’s stock as collateral for obtaining a credit line from China Development Industrial Bank (director of the Corporation).

c. The Corporation provided machinery and equipment with book values of $6,033,570 and $9,291,347 as of December 31, 2002 and 2001, respectively, as collaterals for a long-term credit line.

20. COMMITMENTS AS OF DECEMBER 31, 2002

a. The Corporation had several construction contracts, with a $531,037 guarantee granted by the International Commercial Bank of China.

b. Unused letters of credit amounted to $4,400,000.

c. The Corporation sold its note receivables of $421,603 to Chung Hsing Bills Finance Corporation and also fully guaranteed these receivables. To reduce its risk on this guarantee, the Corporation obtained credit risk insurance from an insurance company and entered into an agreement for Chung Hsing Bills Finance Corporation to share any loss from credit risk.

d. Contracted annual purchases of 8,000,000 metric tons of coal, 15,300,000 metric tons of iron ore, and 2,800,000 metric tons of stones are at prices negotiable every year.

21. FINANCIAL INSTRUMENTS

The Corporation uses both derivative and nonderivative financial instruments.

There were no outstanding forward exchange contracts as of December 31, 2002. As of December 31, 2001, the outstanding balances of forward exchange contracts were as follows:

a. Contract amount (or nominal principal) and credit risk

Financial Instruments	Contract Amount (Nominal Principal)	Credit Risk
Forward exchange contracts	$445,929	$ 8,962

b. The derivative financial instruments held by the Corporation are for nontrading purposes, mainly for hedging the exchange rate or price risks from foreign-currency rights or obligations. Thus, the Corporation chooses derivative financial instruments that reduce the risks associated with the hedged items and evaluates the effectiveness of hedging instruments periodically.

c. Forward exchange contracts resulted in accounts receivable of $8,149 as of December 31, 2001, a net exchange loss of $5,593 in 2002 and a net exchange gain of $28,535 in 2001.

d. As of December 31, 2002 and 2001, the estimated fair values of financial instruments were as follows:

	2002	2001

	Carrying Value	Fair Value	Carrying Value	Fair Value
Nonderivative financial instruments				
Assets				
Cash and cash equivalents	$3,068,966	$3,068,966	$ 4,302,175	$ 4,302,175
Short-term investments	19,751,336	21,484,931	12,206,524	15,294,466
Notes receivable	378,442	378,442	144,794	144,794
Accounts receivable	1,642,077	1,642,077	1,815,944	1,815,944
Pledged time deposits	6,900,000	6,900,000	8,200,000	8,200,000
Long-term investments	35,532,286	39,363,672	35,026,411	35,911,042
Liabilities				
Short-term bank loans and overdraft	809,688	809,688	5,947,913	5,947,913
Commercial paper payable	998,347	998,347	2,843,252	2,843,252
Accounts payable	2,454,461	2,454,461	2,441,818	2,441,818

(Forward)

	2002		2001	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Other payable	$ 5,106,533	$ 5,106,533	$ 4,310,176	$ 4,310,176
Long-term bonds	34,200,000	37,027,461	40,050,000	43,395,620
Long-term debts	3,035,045	3,035,045	5,745,562	5,745,562
Derivative financial instruments				
Forward exchange contracts - purchases	$ -	$ -	$ 3,409	$ 5,918
Forward exchange contracts - sales	-	-	4,740	3,044
	$ -	$ -	$ 8,149	$ 8,962

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 receivable, accounts receivable, pledged time deposits, short-term bank loans and overdraft, commercial paper payable and accounts payable approximate fair value because of the short maturity of these instruments.

2) The fair values of marketable securities and long-term investments are determined at market values or net equity values.

3) The fair values of long-term liabilities are determined on the estimated

present values of future cash flows; discount rates are the interest rates of similar long-term debts available for the Corporation.

4) The fair values of forward exchange contracts are calculated using the swap rates published by Moneyline (Hong Kong) Ltd., Taiwan branch, and forward rates of forward contracts.

22. SEGMENT INFORMATION

The Corporation operates entirely in one industry segment: steel. In compliance with Statement of Financial Accounting Standards No. 20 – "Disclosure For Dominant Segment Information," export information is disclosed as follows:

	2002	2001
Geographic area		
Southeastern Asia	$18,879,309	$14,868,404
Northeastern Asia	7,439,360	6,977,982
Other areas	435,993	1,552,438
	$26,754,662	$23,398,824
% to total revenues	27	28