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Tiangong International Company Limited

天工國際有限公司*

(incorporated in the Cayman Islands with limited liability)

(Stock Code: 826)

ANNOUNCEMENT OF THE INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2021

FINANCIAL HIGHLIGHTS

RMB'million (unless otherwise specified)

	Six months ended 30 June 2021 (unaudited)	Six months ended 30 June 2020 (unaudited)	Change
Revenue	2,616.9	2,509.4	4.3%
Gross profit	666.2	541.6	23.0%
Profit attributable to equity shareholders of the Company	290.5	211.0	37.7%
Basic earnings per share (<i>RMB</i>)	0.110	0.082	34.1%
Diluted earnings per share (<i>RMB</i>)	0.110	0.082	34.1%
Gross profit margin	25.5%	21.6%	3.9 ppt
Net profit margin	11.3%	8.5%	2.8 ppt
	At 30 June 2021 (unaudited)	At 31 December 2020 (audited)	Change
Net Assets	6,526.9	5,640.3	15.7%
Net Debt ⁽¹⁾	–	1,803.9	(100.0%)
Net Gearing ⁽²⁾	0.0%	32.0%	(32.0 ppt)

Notes:

- (1) Net debt equals to total interest-bearing borrowings less pledged deposits, time deposits and cash and cash equivalents. Net debt of the Group as at 30 June 2021 was nil as total interest-bearing borrowings were less than pledged deposits, time deposits and cash and cash equivalents.
- (2) Net gearing is measured as net debt to equity.

The board (the “Board”) of directors (the “Directors”) of Tiangong International Company Limited (the “Company”) is pleased to announce the unaudited consolidated statement of profit or loss and other comprehensive income of the Company and its subsidiaries (collectively, the “Group”) for the six months ended 30 June 2021 and the consolidated statement of financial position of the Group as at 30 June 2021 which have been reviewed by the Company’s auditor, KPMG, and the audit committee of the Company (the “Audit Committee”), together with the comparative figures for the same period of 2020 as follows:

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

For the six months ended 30 June 2021 (unaudited)

		Six months ended 30 June	
		2021	2020
		(unaudited)	(unaudited)
	Note	RMB’000	RMB’000
Revenue	4	2,616,873	2,509,390
Cost of sales		(1,950,667)	(1,967,832)
Gross profit		666,206	541,558
Other income	5	48,491	13,961
Distribution expenses		(80,813)	(44,378)
Administrative expenses		(64,168)	(44,591)
Research and development expenses		(155,551)	(105,133)
Other expenses	6	(29,475)	(49,114)
Profit from operations		384,690	312,303
Finance income		10,104	13,732
Finance expenses		(78,139)	(85,189)
Net finance costs	7(a)	(68,035)	(71,457)
Share of profits of associates		5,674	2,234
Share of profits/(losses) of joint ventures		8,698	(2,817)
Profit before income tax	7	331,027	240,263
Income tax	8	(36,489)	(27,143)
Profit for the period		294,538	213,120
Attributable to:			
Equity shareholders of the Company		290,537	211,017
Non-controlling interests		4,001	2,103
Profit for the period		294,538	213,120
Earnings per share (RMB)	9		
Basic		0.110	0.082
Diluted		0.110	0.082

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the six months ended 30 June 2021 (unaudited)

	Six months ended 30 June	
	2021	2020
	(unaudited)	(unaudited)
	RMB'000	RMB'000
Profit for the period	294,538	213,120
Other comprehensive income for the period (after tax and reclassification adjustments):		
Items that will not be reclassified to profit or loss:		
Equity investments at fair value through other comprehensive income – net movement in fair value reserve (net of tax of RMB1,271,000 (2020: net of tax of RMB2,355,000)) (non-recycling)	21,888	(13,345)
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of:		
– financial statements of entities with functional currencies other than RMB	(386)	(4,807)
Other comprehensive income for the period	21,502	(18,152)
Total comprehensive income for the period	316,040	194,968
Attributable to:		
Equity shareholders of the Company	311,897	192,865
Non-controlling interests	4,143	2,103
Total comprehensive income for the period	316,040	194,968

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June 2021 (unaudited)

		At 30 June 2021 (unaudited) RMB'000	At 31 December 2020 (audited) RMB'000
	<i>Note</i>		
Non-current assets			
Property, plant and equipment		4,192,629	4,136,546
Lease prepayments		145,735	147,576
Intangible assets		17,892	18,842
Goodwill		21,959	21,959
Interest in associates		68,440	55,573
Interest in joint ventures		35,908	28,350
Other financial assets		155,691	135,810
Deferred tax assets		48,421	44,170
		<u>4,686,675</u>	<u>4,588,826</u>
Current assets			
Financial assets at fair value through profit or loss		455,881	877,117
Inventories		1,997,929	1,688,371
Trade and other receivables	10	2,155,173	2,481,866
Pledged deposits		153,754	384,700
Time deposits		1,117,712	350,000
Cash and cash equivalents		2,059,363	827,246
		<u>7,939,812</u>	<u>6,609,300</u>
Current liabilities			
Interest-bearing borrowings		1,957,094	2,773,982
Trade and other payables	11	1,695,367	1,618,745
Current taxation		37,113	64,138
Other financial liability	12	1,439,750	350,000
		<u>5,129,324</u>	<u>4,806,865</u>
Net current assets		<u>2,810,488</u>	<u>1,802,435</u>
Total assets less current liabilities		<u>7,497,163</u>	<u>6,391,261</u>
Non-current liabilities			
Interest-bearing borrowings		814,000	591,837
Deferred income		54,194	58,082
Deferred tax liabilities		102,046	101,033
		<u>970,240</u>	<u>750,952</u>
Net assets		<u>6,526,923</u>	<u>5,640,309</u>

CONSOLIDATED STATEMENT OF FINANCIAL POSITION*As at 30 June 2021 (unaudited) (Continued)*

		At 30 June 2021 (unaudited) <i>RMB'000</i>	At 31 December 2020 (audited) <i>RMB'000</i>
	<i>Note</i>		
Capital and reserves			
Share capital	13	49,399	46,186
Reserves		6,218,296	5,424,038
Total equity attributable to equity shareholders of the Company		6,267,695	5,470,224
Non-controlling interests		259,228	170,085
Total equity		6,526,923	5,640,309

1. REPORTING ENTITY

The Company was incorporated in the Cayman Islands on 14 August 2006 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961 as consolidated and revised) of the Cayman Islands.

The interim financial report of the Company as at and for the six months ended 30 June 2021 comprises the Company and its subsidiaries (collectively referred to as the “Group”) and the Group’s interest in associates and jointly controlled entities.

2. BASIS OF PREPARATION

This interim financial report of the Company and the Group has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard (“IAS”) 34, *Interim financial reporting*, issued by the International Accounting Standards Board (“IASB”). The interim financial report was authorised for issue on 19 August 2021.

The interim financial report has been prepared in accordance with the same accounting policies adopted in the 2020 annual financial statements, except for the accounting policy changes that are expected to be reflected in the 2021 annual financial statements. Details of any changes in accounting policies are set out in Note 3.

The preparation of an interim financial report in conformity with IAS 34 requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a period to date basis. Actual results may differ from these estimates.

This interim financial report contains condensed consolidated financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the 2020 annual financial statements. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for a full set of financial statements prepared in accordance with International Financial Reporting Standards (“IFRSs”).

The interim financial report is unaudited, but has been reviewed by KPMG in accordance with Hong Kong Standard on Review Engagements 2410, *Review of interim financial information performed by the independent auditor of the entity*, issued by the Hong Kong Institute of Certified Public Accountants. KPMG’s independent review report to the Board of Directors will be included in the interim financial report.

The financial information relating to the financial year ended 31 December 2020 that is included in the interim financial report as comparative information does not constitute the Company’s statutory annual consolidated financial statements for that financial year but is derived from those financial statements for the financial year ended 31 December 2020. The Company’s auditor has reported on those financial statements for the financial year ended 31 December 2020. The auditor’s report was unqualified and did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying its report.

3. CHANGES IN ACCOUNTING POLICIES

Changes in accounting policies

The Group has applied the following amendments to IFRSs issued by the IASB to these financial statements for the current accounting period:

- Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16, Interest Rate Benchmark Reform Phase 2
- Amendment to IFRS 16, Covid-19-Related Rent Concessions beyond 30 June 2021

None of these developments have had a material effect on how the Group's results and financial position for the current accounting period or prior years have been prepared or presented in this financial report. The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

4. REVENUE AND SEGMENT REPORTING

(a) Revenue

Revenue represents mainly the sales value of high alloy steel, (including die steel ("DS") and high speed steel ("HSS")), cutting tools, titanium alloy and trading of goods after eliminating intercompany transactions. Further details regarding the Group's revenue are disclosed in Note 4(b).

Disaggregation of revenue from contracts with customers by products divisions is as follows:

	Six months ended 30 June	
	2021	2020
	<i>RMB'000</i>	<i>RMB'000</i>
DS	1,132,896	1,137,548
HSS	427,815	358,280
Cutting tools	459,219	396,517
Titanium alloy	105,022	90,817
Trading of goods	491,921	526,228
	2,616,873	2,509,390

The Group's revenue from contracts with customers was recognised at a point in time. Disaggregation of revenue from contracts with customers by geographic markets is disclosed in Note 4(b)(iii).

For the six months ended 30 June 2021, the Group's customer base is diversified and includes one customer (six months ended 30 June 2020: one customer) with whom transactions exceeded 10% of the Group's revenue. For the six months ended 30 June 2021, revenues from trading of goods to this customer amounted to approximately RMB263,927,000 (six months ended 30 June 2020: RMB526,228,000) and arose in the PRC.

(b) Segment reporting

The Group has five reportable segments, as described below, which are the Group's product divisions. For each of the product divisions, the Chairman (the chief operating decision maker) reviews internal management reports on at least a monthly basis. No operating segments have been aggregated to form the following reportable segments. The following describes the operations in each of the Group's reportable segments:

- DS The DS segment manufactures and sells materials that are used in the die set manufacturing industry.
- HSS The HSS segment manufactures and sells materials that are used in the tools manufacturing industry.
- Cutting tools The cutting tools segment manufactures and sells HSS and carbide cutting tools to the tooling industry.
- Titanium alloy The titanium alloy segment manufactures and sells titanium alloys to the titanium industry.
- Trading of goods The trading of goods segment sells general carbon steel products that are not within the Group's production scope.

(i) Segment results, assets and liabilities

For the purposes of assessing segment performance and allocating resources between segments, the Chairman (the chief operating decision maker) monitors the results, assets and liabilities attributable to each reportable segment on the following basis:

Segment assets include all tangible assets, intangible assets and current assets with the exception of interest in associates, interest in joint ventures, other financial assets, financial assets at fair value through profit or loss, pledged deposits, time deposits, cash and cash equivalents, deferred tax assets and other head office and corporate assets. Segment liabilities include bills payable, trade and non-trade payables, deferred income and accrued expenses attributable to the manufacturing and sales activities of the individual segments with the exception of interest-bearing borrowings, current taxation, other financial liability, deferred tax liabilities and other head office and corporate liabilities.

Revenue and expenses are allocated to the reportable segments with reference to sales generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

The measure used for reporting segment profit is "adjusted EBIT", i.e. "adjusted earnings before interest and taxes", where "interest" is regarded as net finance costs. To arrive at adjusted EBIT, the Group's earnings are further adjusted for items not specifically attributed to individual segments, such as share of profits less losses of associates and joint ventures and other head office or corporate administration costs.

In addition to receiving segment information concerning adjusted EBIT, management is provided with segment information concerning revenue (including inter-segment revenue) generated by the segments in their operations. Inter-segment revenue is priced with reference to prices charged to external parties for similar orders.

Information regarding the Group's reportable segments as provided to the Chairman (the chief operating decision maker) for the purposes of resource allocation and assessment of segment performance for the period ended 30 June 2021 and 2020 is set out below.

	Six months ended 30 June 2021					
	DS RMB'000	HSS RMB'000	Cutting tools RMB'000	Titanium alloy RMB'000	Trading of goods RMB'000	Total RMB'000
Revenue from external customers	1,132,896	427,815	459,219	105,022	491,921	2,616,873
Inter-segment revenue	–	143,285	–	–	–	143,285
Reportable segment revenue	1,132,896	571,100	459,219	105,022	491,921	2,760,158
Reportable segment profit (adjusted EBIT)	189,714	134,044	93,819	12,235	254	430,066
	As at 30 June 2021					
	DS RMB'000	HSS RMB'000	Cutting tools RMB'000	Titanium alloy RMB'000	Trading of goods RMB'000	Total RMB'000
Reportable segment assets	4,470,074	2,045,323	1,462,117	520,081	8	8,497,603
Reportable segment liabilities	1,034,453	448,206	180,803	57,648	81	1,721,191
	Six months ended 30 June 2020					
	DS RMB'000	HSS RMB'000	Cutting tools RMB'000	Titanium alloy RMB'000	Trading of goods RMB'000	Total RMB'000
Revenue from external customers	1,137,548	358,280	396,517	90,817	526,228	2,509,390
Inter-segment revenue	–	130,491	–	–	–	130,491
Reportable segment revenue	1,137,548	488,771	396,517	90,817	526,228	2,639,881
Reportable segment profit (adjusted EBIT)	201,867	106,581	71,849	9,553	154	390,004
	As at 31 December 2020					
	DS RMB'000	HSS RMB'000	Cutting tools RMB'000	Titanium alloy RMB'000	Trading of goods RMB'000	Total RMB'000
Reportable segment assets	4,639,627	1,998,369	1,285,545	521,917	7	8,445,465
Reportable segment liabilities	1,018,505	339,601	206,729	71,653	–	1,636,488

(ii) *Reconciliations of reportable segment revenue, profit or loss, assets and liabilities*

	Six months ended 30 June	
	2021	2020
	RMB'000	RMB'000
Revenue		
Reportable segment revenue	2,760,158	2,639,881
Elimination of inter-segment revenue	(143,285)	(130,491)
Consolidated revenue	<u>2,616,873</u>	<u>2,509,390</u>
	Six months ended 30 June	
	2021	2020
	RMB'000	RMB'000
Profit		
Reportable segment profit	430,066	390,004
Net finance costs	(68,035)	(71,457)
Share of profits of associates	5,674	2,234
Share of profits/(losses) of joint ventures	8,698	(2,817)
Other unallocated head office and corporate expenses	(45,376)	(77,701)
Consolidated profit before income tax	<u>331,027</u>	<u>240,263</u>
	At 30 June	At 31 December
	2021	2020
	RMB'000	RMB'000
Assets		
Reportable segment assets	8,497,603	8,445,465
Interest in associates	68,440	55,573
Interest in joint ventures	35,908	28,350
Other financial assets	155,691	135,810
Deferred tax assets	48,421	44,170
Financial assets at fair value through profit or loss	455,881	877,117
Pledged deposits	153,754	384,700
Time deposits	1,117,712	350,000
Cash and cash equivalents	2,059,363	827,246
Other unallocated head office and corporate assets	33,714	49,695
Consolidated total assets	<u>12,626,487</u>	<u>11,198,126</u>

	At 30 June 2021 RMB'000	At 31 December 2020 RMB'000
Liabilities		
Reportable segment liabilities	1,721,191	1,636,488
Interest-bearing borrowings	2,771,094	3,365,819
Current taxation	37,113	64,138
Deferred tax liabilities	102,046	101,033
Other financial liability	1,439,750	350,000
Other unallocated head office and corporate liabilities	28,370	40,339
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Consolidated total liabilities	6,099,564	5,557,817
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(iii) **Geographical information**

The Group's business is managed on a worldwide basis and divided into four principal economic regions, the People's Republic of China (the "PRC"), North America, Europe and Asia (other than the PRC).

In presenting geographical information, segment revenue is based on the geographical location of customers. Substantially all of the Group's assets and liabilities are located in the PRC and accordingly, no geographical analysis of segment assets, liabilities and capital expenditure is provided.

	Six months ended 30 June 2021 RMB'000	2020 RMB'000
Revenue		
The PRC	1,680,697	1,697,854
North America	367,417	363,039
Europe	387,223	293,257
Asia (other than the PRC)	166,720	138,061
Others	14,816	17,179
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Total	2,616,873	2,509,390
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5. OTHER INCOME

	Six months ended 30 June	
	2021	2020
	<i>RMB'000</i>	<i>RMB'000</i>
Government grants	24,288	7,419
Sales of scrap materials	3,462	1,114
Net gains on disposal of property, plant and equipment	–	331
Dividends income from listed securities	4,865	3,580
Realised and unrealised gains on structured deposits	11,881	–
Net realised and unrealised gains on trading securities	3,577	299
Others	418	1,218
	<hr/>	<hr/>
Total	48,491	13,961
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The subsidiaries of the Group, including Jiangsu Tiangong Tools Company Limited (“TG Tools”), Tiangong Aihe Company Limited (“TG Aihe”), Jiangsu Tiangong Technology Company Limited (“TG Tech”) and Jiangsu Tiangong Precision Tools Company Limited (“Precision Tools”), located in the PRC, collectively received unconditional grants amounting to RMB20,400,000 (six months ended 30 June 2020: RMB4,165,000) from the local government as a reward for their contribution to the local economy and to encourage technology innovation. TG Tools and TG Tech and TG Aihe also recognised amortisation of government grants related to assets of RMB3,888,000 (six months ended 30 June 2020: RMB3,254,000) during the six months ended 30 June 2021.

6. OTHER EXPENSES

	Six months ended 30 June	
	2021	2020
	<i>RMB'000</i>	<i>RMB'000</i>
Provision for loss allowance on trade receivables and other receivables	3,123	29,900
Net losses on disposal of property, plant and equipment	9,242	–
Charitable donations	700	1,625
Net foreign exchange losses	16,245	17,018
Others	75	571
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	29,475	49,114
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7. PROFIT BEFORE INCOME TAX

Profit before income tax is arrived at after charging/(crediting):

(a) Net finance costs

	Six months ended 30 June	
	2021 RMB'000	2020 RMB'000
Interest income	<u>(10,104)</u>	<u>(13,732)</u>
Finance income	<u>(10,104)</u>	<u>(13,732)</u>
Interest on bank loans	61,689	96,138
Interest arising on other financial liability	24,750	–
Less: interest expenses capitalised into property, plant and equipment under construction	<u>(8,300)</u>	<u>(10,949)</u>
Finance expenses	<u>78,139</u>	<u>85,189</u>
Net finance costs	<u>68,035</u>	<u>71,457</u>

(b) Other items

	Six months ended 30 June	
	2021 RMB'000	2020 RMB'000
Cost of inventories*	1,950,667	1,967,832
Depreciation	145,028	126,870
Amortisation of lease prepayments	1,841	1,448
Amortisation of intangible assets	950	–
Provision for write-down of inventories	9,379	5,607
Provision for loss allowance on trade receivables and other receivables	3,213	29,900

* *Cost of inventories includes RMB127,791,000 (six months ended 30 June 2020: RMB105,143,000) relating to depreciation expenses and provision for write-down of inventories, amounts of which are also included in the respective total amounts disclosed separately above for each of these types of expenses.*

8. INCOME TAX

	Six months ended 30 June	
	2021	2020
	RMB'000	RMB'000
Current tax		
Provision for PRC Income Tax	37,112	33,176
Provision/(reversal) for Hong Kong Profits Tax	738	(1,294)
Provision for Thailand Profits Tax	606	438
	38,456	32,320
Deferred tax		
Origination and reversal of temporary differences	(1,967)	(5,177)
	36,489	27,143

- (a) Pursuant to the rules and regulations of the Cayman Islands and British Virgin Islands, the Group is not subject to any income tax in the Cayman Islands or British Virgin Islands.
- (b) The provision for PRC Income Tax is based on the respective corporate income tax rates applicable to the subsidiaries located in the PRC as determined in accordance with the relevant income tax rules and regulations of the PRC.

TG Tools, TG Aihe, Precision Tools, TG Tech and Weijian Tools Technology Company Limited (“Weijian Tools”) are subject to a preferential income tax rate of 15% in 2021 available to enterprises which qualify as High and New Technology Enterprise (2020: 15%).

The statutory corporate income tax rate applicable to the Group’s other operating subsidiaries in the PRC is 25% (2020: 25%).

- (c) Hong Kong Profits Tax has been provided for Tiangong Development Hong Kong Company Limited (“TG Development”) at the rate of 16.5% (2020: 16.5%) on the estimated assessable profits arising in Hong Kong for the six months ended 30 June 2021.
- (d) Thailand Profits Tax has been provided for Tiangong Special Steel Company Limited and Tiangong Precision Tools (Thailand) Company Limited at the rate of 20% (2020: 20%) on the estimated assessable profits arising in Thailand for the six months ended 30 June 2021.

9. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB290,537,000 (six months ended 30 June 2020: RMB211,017,000) and the weighted average of 2,649,444,444 ordinary shares in issue during the interim period (six months ended 30 June 2020: 2,568,842,000).

(b) Diluted earnings per share

The diluted earnings per share for the six months ended 30 June 2021 and 2020 are the same as the basic earnings per share as there are no dilutive potential ordinary shares during the periods.

10. TRADE AND OTHER RECEIVABLES

	At 30 June 2021 RMB'000	At 31 December 2020 RMB'000
Trade receivables	1,141,360	1,253,802
Bills receivable	896,546	850,660
Less: loss allowance	(91,034)	(87,295)
Net trade and bills receivable	1,946,872	2,017,167
Prepayments	133,381	338,813
Non-trade receivables	78,908	130,400
Less: loss allowance	(3,988)	(4,514)
Net prepayments and non-trade receivables	208,301	464,699
	2,155,173	2,481,866

No trade receivables as at 30 June 2021 (2020: RMB160,835,000) have been pledged to a bank as security for the Group's bank loans.

At the end of the reporting period, the ageing analysis of trade and bills receivable (which are included in trade and other receivables), based on the invoice date and net of loss allowance, is as follows:

	At 30 June 2021 RMB'000	At 31 December 2020 RMB'000
Within 3 months	1,513,155	1,551,164
4 to 6 months	125,629	150,412
7 to 12 months	136,079	152,501
1 to 2 years	169,812	160,480
Over 2 years	2,197	2,610
	1,946,872	2,017,167

Trade and bills receivables are due from 90 to 180 days from the date of billing. Normally, the Group does not obtain collateral from customers.

11. TRADE AND OTHER PAYABLES

At the end of the reporting period, the ageing analysis of trade and bills payable (which are included in trade and other payables), based on the invoice date, is as follows:

	At 30 June 2021 RMB'000	At 31 December 2020 RMB'000
Within 3 months	955,110	695,190
4 to 6 months	214,261	200,952
7 to 12 months	87,631	477,115
1 to 2 years	11,875	15,044
Over 2 years	48,852	35,297
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Total trade and bills payable	1,317,729	1,423,598
Contract liabilities	37,289	37,351
Dividends payable	204,594	–
Non-trade payables and accrued expenses	135,755	157,796
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	1,695,367	1,618,745
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12. OTHER FINANCIAL LIABILITY

The analysis of the carrying amount of other financial liability is as follows:

	At 30 June 2021 RMB'000	At 31 December 2020 RMB'000
Contingent redeemable capital contributions in a subsidiary	1,439,750	350,000
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On 28 December 2020, the Company, TG Tools, Jurong Tiangong New Materials Technology Company Limited, China Tiangong (Hong Kong) Company Limited, Precision Tools, TG Aihe, Weijian Tools, Jiangsu Tiangong New Materials Company Limited and TG Development and certain third party investors (the “Investors”) entered into an investment agreement, pursuant to which the Investors would invest RMB1,415,000,000 to acquire 16.65% of the equity interest in TG Tools (collectively referred as “the Investment in TG Tools”). The Investors are entitled to the same voting rights and dividend rights as other equity holders of TG Tools, whereas certain special rights in TG Tools including redemption, anti-dilution and preferential liquidation rights are granted to the Investors. As at 30 June 2021, the Group received capital contributions of RMB1,415,000,000 from the Investors.

At the date of issuance of other financial liability, the Investment in TG Tools is initially recognised at fair value and is carried at amortised cost for subsequent periods. Interest on the Investment in TG Tools is calculated using the effective interest method and recognised in the consolidated statement of profit or loss.

13. CAPITAL, RESERVES AND DIVIDENDS

(a) Dividends

Dividends payable to equity shareholders attributable to the previous financial year, approved but not paid/approved and paid during the interim period:

	2021 <i>RMB'000</i>	2020 <i>RMB'000</i>
Dividends in respect of the previous financial year, approved but not paid during the interim period, of RMB0.0732 per share (2020: RMB0.0545 per share)	204,594	140,013

The directors did not recommend payment of an interim dividend for the interim period (no interim dividend for the six months period ended 30 June 2020).

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

	For the six months ended 30 June					
	2021		2020		Change	
	<i>RMB'000</i>	%	<i>RMB'000</i>	%	<i>RMB'000</i>	%
Die steel (“DS”)	1,132,896	43.3	1,137,548	45.3	(4,652)	(0.4)
High speed steel (“HSS”)	427,815	16.3	358,280	14.3	69,535	19.4
Cutting tools	459,219	17.6	396,517	15.8	62,702	15.8
Titanium alloy	105,022	4.0	90,817	3.6	14,205	15.6
Trading of goods	491,921	18.8	526,228	21.0	(34,307)	(6.5)
	<u>2,616,873</u>	<u>100.0</u>	<u>2,509,390</u>	<u>100.0</u>	<u>107,483</u>	<u>4.3</u>

DS – accounted for approximately 43% of the Group’s revenue in 1H2021

	For the six months ended 30 June					
	2021		2020		Change	
	<i>RMB'000</i>	%	<i>RMB'000</i>	%	<i>RMB'000</i>	%
Domestic	660,652	58.3	738,021	64.9	(77,369)	(10.5)
Export	472,244	41.7	399,527	35.1	72,717	18.2
	<u>1,132,896</u>	<u>100.0</u>	<u>1,137,548</u>	<u>100.0</u>	<u>(4,652)</u>	<u>(0.4)</u>

DS is manufactured using rare metals including molybdenum, chromium and vanadium, a type of high alloy special steel. DS is mainly used in die and mould casting as well as machining. Many different manufacturing industries require moulds, including the automotive, high-speed railway construction, aviation and plastic product manufacturing industries.

Looking back at the first half of 2021, the global economy has rebounded since the launch of vaccination programs in many countries and is gradually emerging from the haze of the Novel Coronavirus (COVID-19) pandemic. This became an important driving force for China’s export growth. In particular, many manufacturing industries in Europe resumed production, which is a strong support factor to the export of DS.

With the rapid recovery of the manufacturing industry in Europe and North America, the Group has successfully absorbed the rapid recovery of overseas demand. In the first half of 2021, revenue from export sales of DS recorded a significant increase of 18.2%, reaching RMB472,244,000 (1H2020: RMB399,527,000).

In order to catch up with the increase in export orders before the cancellation of export VAT return policy, the Group adjusted its production capacity and concentrated its production capacity to cope with the increase in export orders, resulting in a decrease of 10.5% in domestic revenue to RMB660,652,000 (1H2020: RMB738,021,000).

Overall, sales of the DS segment remained relatively stable at RMB1,132,896,000 (1H2020: RMB1,137,548,000).

HSS – accounted for approximately 16% of the Group’s revenue in 1H2021

	For the six months ended 30 June					
	2021		2020		Change	
	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>
Domestic	280,172	65.5	233,194	65.1	46,978	20.1
Export	147,643	34.5	125,086	34.9	22,557	18.0
	427,815	100.0	358,280	100.0	69,535	19.4

HSS, manufactured using rare metals including tungsten, molybdenum, chromium and vanadium, is characterised by greater hardness, heat resistance and durability. These attributes make HSS suited to such applications as cutting tools and in the manufacturing of high-temperature bearings, high-temperature springs, dies, internal-combustion engines and roll, with wide usage in specific industrial applications including automotive, machinery manufacturing, aviation and electronics industries.

With the extensive vaccination rollout in Europe and North America, the manufacturing industries recovered rapidly. Most factories resumed operations gradually. The Group benefited from the recovery of overseas demand.

Despite the orderly recovery of economic activities in Europe and North America under the extensive vaccination rollout, many non-industrial sectors were still adopting the work-from-home policy under the new normal, which helped make the stay-at-home economy a main driving force for sales growth in many parts of the world. Demand for DIY metal cutting tools, which directly drove the demand for HSS, was one that benefited from the stay-at-home economy.

HSS export revenue therefore benefited and increased by 18.0% to RMB147,643,000 in the first half of 2021 (1H2020: RMB125,086,000).

Revenue from the domestic market increased by 20.1% to RMB280,172,000 (1H2020: RMB233,194,000), which was driven by increased domestic demand for high-end HSS material.

In the first half of 2021, as the alloy price continued to rise, the Group raised the price of its products a number of times in response. The average selling price and sales volume of HSS increased by 5.3% and 13.4% respectively, which led to an increase of 19.4% in overall HSS revenue to RMB427,815,000 (1H2020: RMB358,280,000).

Cutting tools – accounted for approximately 18% of the Group’s revenue in 1H2021

	For the six months ended 30 June					
	2021		2020		Change	
	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>
Domestic	144,124	31.4	110,666	27.9	33,458	30.2
Export	315,095	68.6	285,851	72.1	29,244	10.2
	459,219	100.0	396,517	100.0	62,702	15.8

Cutting tools segment included HSS and carbide cutting tools. HSS cutting tools products can be categorised into four major types – twist drill bits, screw taps, end mills and turning tools. All of these are used in industrial manufacturing. The two main types of HSS cutting tools manufactured by the Group are twist drill bits and screw taps. The Group’s vertical integration extending from upstream HSS production to downstream HSS cutting tools production brought us a significant cost advantage over the Group’s peers. High-end carbide tools manufactured by the Group mainly comprised of customised tools.

Driven by domestic and overseas economic growth, the global manufacturing industry was gradually recovering, which continued to spur the growth in demand for machine tools since 2020. Demand for machine tools and cutting tools from Europe and the United States remained strong, resulting in a significant increase in exports in the first half of 2021. Thanks to the Group’s leading position in the domestic market and its overseas expansion strategy, the Group once again demonstrated its advantages as a leading enterprise in the first half of 2021. The overall sales volume of cutting tools recorded an increase of 7.4%, and the average selling price also increased by 7.8% driven by the price increase of raw materials. Overall revenue increased by 15.8% to RMB459,219,000 (1H2020: RMB396,517,000).

With the increase in overseas market share, the export sales volume and average selling price increased by 4.8% and 5.2% respectively in the first half of 2021. Export revenue increased by 10.2% to RMB315,095,000 (1H2020: RMB285,851,000). Benefiting from the expansion of domestic manufacturing industries, demand for computer numerical control (“CNC”) machine tools and high-end tools increased. Domestic revenue was therefore increased by 30.2% to RMB144,124,000 (1H2020: RMB110,666,000).

Titanium alloy – accounted for approximately 4% of the Group’s revenue in 1H2021

	For the six months ended 30 June					
	2021		2020		Change	
	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>	<i>RMB'000</i>	<i>%</i>
Domestic	103,827	98.9	89,744	98.8	14,083	15.7
Export	1,195	1.1	1,073	1.2	122	11.4
	105,022	100.0	90,817	100.0	14,205	15.6

The corrosion resistance nature of titanium alloy promoted the extensive applications of titanium alloy in various industries, including aerospace, chemical pipeline equipment, nuclear and ocean industries.

In the first half of 2021, the demand for titanium alloy products returned to growth. With the sustained recovery of the domestic economy, the demand for products from downstream enterprises has gradually improved after the impact of the pandemic. As a result, the revenue contributed by the titanium alloy segment increased by 15.6% to RMB105,022,000 (1H2020: RMB90,817,000).

The domestic titanium industry underwent structural adjustment in 2020. The development towards high-end consumption has achieved strong results, with the proportion from aerospace, marine engineering, high-end chemical industry and sports and leisure gradually increasing. The Group’s titanium alloy products have obtained the Quality Management System for Aerospace Certification issued by Bureau Veritas, an international authoritative quality certification body. Titanium alloys have also been listed as key strategic materials whose application is expected to be vigorously promoted. The Group is confident that the application level and acceptance of the Group’s products will be further enhanced through the in-depth transformation and upgrading of products from billets to finished products.

Trading of goods

This segment involved the trading of general carbon steel products outside of the Group’s production scope. As the Group continued to focus on its principal and core businesses in the first half of 2021, the business volume of commodity trading continued to decrease.

FINANCIAL REVIEW

Net profit attributable to equity shareholders of the Company increased by 37.7% from RMB211,017,000 in the first half of 2020 to RMB290,537,000 in the first half of 2021. The increase was mainly attributable to the increased gross profit margin of the Group’s products which was partially offset by increased research and development effort incurred before the mass production of new powder metallurgy products.

Revenue

Revenue of the Group for the first half of 2021 totalled RMB2,616,873,000, representing an increase of 4.3% when compared with RMB2,509,390,000 in the first half of 2020. The increase in revenue was mainly caused by the increase in revenue from HSS, cutting tools and titanium alloy segments. While revenue from DS segment remained relatively stable, the other three segments recorded an increase of 15.6% to 19.4% in revenue, partly due to increase in raw material prices. The total revenue from the four major production segments increased by 7.1% to RMB2,124,952,000 (1H2020: RMB1,983,162,000). For an analysis of individual segments, please refer to the “Business Review” section.

Cost of sales

The Group’s cost of sales decreased from RMB1,967,832,000 for the first half of 2020 to RMB1,950,667,000 for the first half of 2021, representing a decrease of 0.9%. The decrease was mainly due to a decrease in sales under the trading of goods business during the period.

Gross margin

For the first half of 2021, gross margin was 25.5% (1H2020: 21.6%). Set out below is the gross margin for the five segments of the Group for the first half of 2020 and 2021:

	For the six months ended 30 June	
	2021	2020
DS	30.4%	27.1%
HSS	30.6%	27.9%
Cutting tools	28.1%	20.2%
Titanium alloy	16.8%	18.1%
Trading of goods	0.05%	0.03%

DS

The gross margin of DS increased from 27.1% in the first half of 2020 to 30.4% in the first half of 2021. During the period, average purchase prices of raw materials increased continuously. The Group passed on the increased costs effectively to the customers through responsive price adjustments. In addition, during the upward pricing cycle, existing finished goods were sold at an increased price, which further enhanced the Group’s gross profit margin.

HSS

The situation of HSS was largely similar to that of DS’s in the first half of 2021. Gross margin of HSS increased from 27.9% in the first half of 2020 to 30.6% in the first half of 2021.

Cutting tools

Gross margin of cutting tools increased from 20.2% in the first half of 2020 to 28.1% in the first half of 2021. During the period, the proportion of complex and high value-added cutting tools products increased by 7.7% in terms of value. These products contributed a higher profit margin to the whole segment. Also, the increased cost of HSS, which was the main raw materials for production of cutting tools, was also passed on to the end customer through price adjustments. This further enhanced the overall gross profit margin.

Titanium alloy

Gross margin of titanium alloy decreased from 18.1% in the first half of 2020 to 16.8% in the first half of 2021. Demand for titanium alloy products began to resume during the period. However, the average selling prices were still under pressure, leading to a shrinking profit margin.

Other income

The Group's other income increased from RMB13,961,000 in the first half of 2020 to RMB48,491,000 in the first half of 2021. The increase was mainly attributable to an increase in government grants received from the local government and interest income from structured deposits.

Distribution expenses

The Group's distribution expenses were RMB80,813,000 (1H2020: RMB44,378,000), representing an increase of 82.1%. Notwithstanding gradual resumption of export sales with the stabilisation of COVID-19 in Europe and North America, freight and related logistic expenses increased compared to the first half of 2020 and the average freight expense also increased due to the tight supply of overseas freight services during this period.

Administrative expenses

For the first half of 2021, the Group's administrative expenses increased to RMB64,168,000 (1H2020: RMB44,591,000). The increase was mainly attributable to (i) local government exempted social insurance contribution during the outbreak of COVID-19 in 2020 which was not available in 2021; and (ii) professional fees incurred for preparation and consultation for spin-off project of TG Tools. For the first half of 2021, administrative expenses as a percentage of revenue was 2.5% (1H2020: 1.8%).

Net finance costs

The Group's net finance costs decreased from RMB71,457,000 in the first half of 2020 to RMB68,035,000 in the first half of 2021, which was the result of repayment of significant amount of bank loans with the other financial liability, which is a contingent redeemable capital contributions in a subsidiary, at a lower cost of fund.

Income tax expense

The Group's income tax expense increased from RMB27,143,000 in the first half of 2020 to RMB36,489,000 in the first half of 2021. The increase was mainly due to an increase in operating income for the period.

Profit for the period

As a result of the factors set out above, the Group's profit increased by 38.2% to RMB294,538,000 for the first half of 2021 from RMB213,120,000 for the first half of 2020. The Group's net profit margin increased from 8.5% in the first half of 2020 to 11.3% in the same period of 2021.

Profit attributable to equity shareholders of the Company

For the first half of 2020, profit attributable to equity shareholders of the Company was RMB290,537,000 (1H2020: RMB211,017,000), representing an increase of 37.7%.

Trade and bills receivable

Net trade and bills receivable decreased from RMB2,017,167,000 as at 31 December 2020 to RMB1,946,872,000 as at 30 June 2021. The provision for doubtful debts of RMB91,034,000 (2020: RMB87,295,000) accounted for 4.5% (2020: 4.1%) of the trade and bills receivable.

INDUSTRY REVIEW

Entering into 2021, the domestic economy made a good start, with GDP growth reaching 12.7%. With the achievements of pandemic prevention and control, the popularisation of COVID-19 vaccines, the gradual normalisation of policies and the recovery of household income, the trend toward sustained and stable recovery has been well maintained. Among them, thanks to the support of national policies, industrial productivity took the lead in recovery, and the overall export performance was better than expected. According to statistics, China's industrial production continued to support economic growth in the first half of 2021, with an increase of 15.9% year-on-year. Under the trend of accelerating industrial transformation and upgrading, the high-tech and equipment manufacturing industries achieved faster growth.

Currently, the United States is benefiting from the large-scale quantitative easing policy and the continuous introduction of active fiscal policies, and its economy has shown a significant recovery. Major developed economies in Europe, such as Britain, Germany, France and Italy, continued to suffer from the economic impacts of the pandemic in the first quarter, but the recovery of production and consumption activities accelerated in the second quarter under the extensive vaccination programs. For the six month ended 30 June 2021, the United States goods and services trade deficit increased US\$135.8 billion, or 46.4% from the same period in 2020, among which exports increased US\$150.9 billion or 14.3% while imports increased

US\$286.7 billion or 21.3%. The widening of trade deficit indicated that the resurgent United States economy drove strong demand for foreign-made goods ahead of the COVID variant surge. It was further proof of how United States consumers and businesses have stepped up spending and investment as the economy has recovered to its pre-COVID-19 size, fuelling demand for imports.

MARKET REVIEW

Looking back at the DS market, in the first half of 2021 the price of special alloy raw materials continued to rise, thus causing an increase in the market price of DS. As the widespread vaccination rollout eased the pandemic in Europe and the United States, the demand for automobiles, household appliances and electronic consumer goods gradually recovered and is expected to resume expansion in 2021. This will lead to an increase in the demand for DS in overseas developed economies. In addition, the market share of Chinese DS enterprises in the domestic high-end DS market continues to increase. As the DS industry has high competition barriers and strong customer stickiness, enterprises will benefit in the long run after entering the supply chain, as the domestic alternative market is pushing the industry into a new stage of high-quality growth.

Cutting tools are the main application market for HSS. In recent years, the transformation and upgrading of the manufacturing industry and the improvement of mechanical properties of processing materials have led to the increasing use and proportion of advanced cutting materials, such as high-performance HSS and carbide. At the same time, the penetration rate of CNC machine tools in China has further increased, and the corresponding increase in consumer demand for high-end cutting tools has driven the demand for high-end HSS. This has led to a continuous increase in the scale of the domestic cutting tool market. With the development of high efficiency cutting, high reliability requirements of CNC tools and metallurgical technology, low-alloy HSS and ordinary HSS in the low-end market will be gradually eliminated, and high-performance HSS will usher in a broader space for development. According to the “Analysis of the Economic Operation of the Machine Tool Industry in the First Quarter of 2021” issued by the China Machine Tool Industry Association, China’s export of cutting tools increased by 49.6% to US\$830 million compared with the same period in 2020, while new orders for metal-cutting machine tools increased by 111.5% in the same period. This shows that the growth in both export and domestic demand are equally significant.

From the policy point of view, the Chinese government has issued a series of policies to support the development of the special steel industry since 2015, including the inclusion of special steel products in the catalogue of new materials in the 13th Five-Year Plan for the Development of New Materials Industry, and the inclusion of HSS and DS in *Made-in-China 2025 Plan*, which focuses on the development of advanced basic materials, as well as various policies to boost the manufacturing industry. All of these have added impetus to the high-quality development of the special steel industry. In addition, China has set the important strategic goal of achieving carbon emission peak by 2030 and carbon neutrality by 2060. To this end, the China Iron and Steel Association has launched a collection of special

standards for carbon emission peak and carbon neutrality in the iron and steel industry. This will effectively enhance the relevant standards for low-carbon technologies and processes in the iron and steel industry, and help the industry achieve greener and more sustainable development.

ACCOMPLISHMENTS

According to the world ranking of HSS and DS (collectively known as tools steel) released by the world's authoritative SMR Steel and Metal Market Research, the Group ranked first in the world in terms of tools steel products output in 2020. The Group's annual production capacity of tools steel is 250,000 tons, of which the annual output of HSS products was ranked first in the world for 17 consecutive years. Furthermore, according to China Special Steel Enterprises Association, the Group's HSS production capacity ranked first in China for 25 consecutive years.

As a well-known manufacturer of advanced basic materials such as HSS and DS, key strategic materials such as titanium alloy and precision cutting tools, the Group will further accelerate its transformation and upgrading strategy in 2021, ushering in the key strategic development period with the largest investment in high-tech projects since its establishment. The 50,000-ton tools steel production capacity upgrading project, the second phase of powder metallurgy project, the second phase of Thailand project, intelligent powder metallurgy tap project and carbide cutting tool project are all under intensive planning and implementation.

In order to meet the needs of the Group's business development and maintain capital flexibility, the Group conducted a share placement of 200 million shares in May 2021 (with the assistance of a substantial shareholder by way of placing existing shares and subscribing equal number of new shares at the same price). Approximately 7% and 43% of the net proceeds raised, about RMB834 million, will be used to expand the Group's industrial park in Thailand and develop new precision tools products, while the remaining proceeds are intended as general working capital.

The Group's plant in the Rojana Rayong Pluak Daeng Industrial Park, Rayong, Thailand, was completed in September 2020 and commenced mass production in the first quarter of 2021. It is the Group's first overseas factory for highly automated cutting tools, with an annual production capacity of 48 million pieces. Shortly after the commencement of formal operation of the Thailand production line, the Group's products received the acceptance of a customer in May 2021 which served as strong affirmation of the Group's product quality.

As for new precision tools, the Group is committed to the research and development of carbide and powder metallurgy taps. Currently, according to 華經產業研究院 (Huajing Industrial Research*), China's carbide products are of middle and low-grade and not capable of meeting the needs of the domestic high-end manufacturing industry. Therefore, high-end carbide CNC blades and other high-tech, high value-added carbide products have to be imported from abroad. The Group's research and development of carbide and powder taps will bring great benefits to the Group and the special new materials industry in China.

In April 2021, TG Tools, a subsidiary of the Group, formally kicked-off the spin-off listing plan on the A-share market, marking a meaningful milestone for the Group in the capital market.

FUTURE OUTLOOK

Operation Strategy

The Group has led the industry with its professional equipment, technology and management advantages, focusing on research and development and cost control for many years, in order to meet the domestic market demand and gain international market share.

Precise strategic layout, efficient execution ability and world-leading technology are the three core pillars of the Group. Looking back at the first half of 2021, the Group continued to implement the strategy of high-quality transformation and development, continuously overcame the difficulties of smelting technology through industry-leading research and development capabilities, and strived to optimise the production process and product structure. With excellent products, the Group promoted the direct sales strategy to deeply bind high-quality customers. At the same time, by virtue of its leading industry position and pioneering advantages in China, the Group will actively extend the industrial supply chain and increase the added value of products to reflect their true value.

Domestic industry development

Currently, China is still in a stable period of economic recovery after the pandemic. Enterprises are pursuing cost reduction and efficiency enhancement and are actively improving production efficiency to match the national pace. Among them, the steel and special new materials industry continued to record a simultaneous increase in production capacity and output, triggering a rise in commodity prices. Since the beginning of the year, prices for the Group's DS and HSS products have also risen eight consecutive times, including two increases in June 2021, due to the rising prices of raw materials such as scrap steel, ferrovanadium and other auxiliary materials.

The joint meeting of the National Development and Reform Commission and other departments in May 2021 emphasised “guaranteeing supply and stabilising prices”, minimising the impact of market sentiment and speculation on commodity prices, and adjusting the pressure brought about by the imbalance between supply and demand in the industry with positive policy signals. At the same time, it is expected that, with the overall supply easing in the second half of the year after the Central Bank lowered the reserve requirement ratio, the demand for infrastructure, construction machinery, automobiles and household appliances will further stabilise, and the demand for special steel will maintain an upward trend driven by the continuous increment of high-end manufacturing equipment and the shipbuilding industry.

In order to keep pace with the market demand, the “50,000 Tons Tools Steel Capacity Expansion Project” planned by the Group at the beginning of this year is now being carried out in an orderly manner. The project will mainly focus on high-end tools steel products, including HSS and DS. After the project reaches its planned production capacity, the Group will have an annual production capacity of 300,000 tons of tools steel. The Group will continue to strengthen the research and development of high-end tools steel, so as to enhance the competitiveness of the Group’s products.

As a pioneer in the domestic industry, the Group will continue to become a dominant player in the field of tool steel. As the cornerstone of the domestic manufacturing industry, the Group will take solving the “bottleneck” technology at the material end as its core task, actively cooperate with downstream and terminal customisation needs through leading research and development and promote the integration of the industrial supply chain with the overall supply scheme of “material + services”.

Export operation

In the first half of 2021, monetary policies in the United States and the Eurozone remained loose, and external demand maintained a relatively rapid growth. Other major overseas steel producing countries, including India and Japan, are still suffering from the pandemic, which has affected the supply side to a certain extent, thus stimulating the increase in China’s steel exports. Currently, the growth in China’s net steel export volume is relatively stable. In the first five months of 2021, China’s cumulative net steel export volume was 24.83 million tonnes, representing a year-on-year increase of 27% and an increase of 2.5% as compared with the same period in 2019. Net exports are expected to be more stable in the second half of the year as the overseas economy gradually recovers.

Overseas expansion

The Group continued to press ahead its overseas expansion plan despite that waves of pandemic continue to plague the world. The Group is focused on promoting the globalisation strategy to hedge the uncertainties relating to the Sino-US trade conflicts by opening up a wider overseas market. In the second quarter of this year, the factory in Thailand Rojana Rayong Pluak Daeng Industrial Park officially commenced its trial production, and the second phase of the project will soon be launched. This is an important starting point for overseas expansion. For the first half of 2021, the Thailand factory produced a total of 1.95 million pieces of cutting tools, and is expected to gradually achieve an annual output of 48 million pieces.

Product Development Strategy

Powder Metallurgy Industry

In recent years, thanks to the rapid development of the automobile, machinery manufacturing, metal industry, aerospace, instrumentation, hardware tools, engineering machinery, electronic household appliances and high-tech industries, the capacity of powder metallurgy has been expanding, and development opportunities are enormous. The growth of China's powder metallurgy industry is also related to the development and application of new products, new materials, new processes and new equipment, as well as the continuous improvement and innovation of existing products and production processes.

In March 2018, the Group began to plan and prepare its first industrialised powder metallurgy production line in China. The production line with an annual capacity of 2,000 tons was officially completed and put into operation in November 2019, making the successful first step into the powder metallurgy industry. The Group began to gradually expand powder metallurgy production in the first half of 2021. Contract orders have increased significantly since then, and powder metallurgy has become a growth driver for the Group. The Group's distribution of powder metallurgy with a leading supplier of special steel products in Europe, which is also a business partner, has also achieved fruitful results.

The Group will continue to deepen the transformation of high-end products and make unremitting efforts to invest in the research and development of powder metallurgy. It is expected that the second phase of the powder metallurgy production line will be completed in 2022 as planned, with an additional annual production capacity of 3,000 tons. The total production capacity is expected to further increase. At the same time, with the increasing market demand for efficient cutting and CNC tools, it is expected that the proportion of powder metallurgy applications in HSS will further increase significantly. The Group is intensively promoting the application of powder metallurgy HSS cutting tools, including powder metallurgy taps and complex cutting tools. It is expected that the annual production of 10 million powder taps will be completed in 2022, realising import substitution and greatly improving the machine tool processing capacity of China's manufacturing industry.

Carbide Cutting Tools Industry

Cutting tools are the foundation of the machinery manufacturing industry and major technical fields. The quality of cutting tools directly determines the production level of the machinery manufacturing industry and is one of the most important factors for the manufacturing industry to improve production efficiency and product quality. In recent years, the Group has actively sought to upgrade its products and focused on the high-end carbide cutting tools market, providing cutting tools with higher alloy content and higher added value to seize the opportunities brought by the continuous growth of demand for high-end carbide cutting tools in China.

Marketing Strategy

The Group has been investing resources to expand its online sales channels. The Group's products are sold on a number of major e-commerce platforms around the world, including Alibaba, Amazon, eBay, JD.com and Tmall, which further drives the sales of cutting tools. During the pandemic, the e-commerce platforms sales has proved its significance. Compared to the same period last year, overall online sales increased by 51.0%.

Information Technology

In order to cope with the Group's expansion of production capacity, international development, expansion of product lines, more precise and professional production processes and more diversified sales channels, the Group has invested heavily in building a digital information system, "Digital Tiangong", which covers all business areas of the Group. The system completes the digital development of five areas: from sales to payment collection, purchases to payment, planning to resources, manufacturing to costs, and order to delivery. This system effectively improves the performance of network procurement, comprehensively enhance the synergy of the industrial supply chain, greatly enhance the competitiveness of the Group, and make the best preparation for the transformation of the Group to an amoeba management model. The responsive shift of production capacity for DS's export sales was one of the achievements of the system during the first half of 2021.

After 14 months of successful completion of the first phase of the "Digital Tiangong" project, the second phase of the smart manufacturing project was officially launched in June 2021, which involved a wider range of departments and functions. The Group will accelerate its digitalisation and smart development to stay aligned with national smart upgrade strategy, in order to achieve comprehensive management, research and development, as well as overall production technology transformation and upgrade, and to lead the change and development of the industry.

OUR MISSION

The Group has always strived for innovation and advancements in competitiveness to consolidate its leading market position.

We re-affirm our mission to maximise shareholder value, uphold corporate governance standards that create maximum value for shareholders and maintain the highest standards of corporate governance.

FORWARD LOOKING STATEMENTS

This management discussion and analysis contains certain forward-looking statements with respect to the financial condition, results of operations and business of the Group. These forward-looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance, or events to differ materially from those expressed or implied in such statements.

Forward looking statements involve inherent risks and uncertainties. Readers, including shareholders and potential investors, should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward-looking statement.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2021, the Group's current assets mainly included cash and cash equivalents of RMB2,059,363,000, inventories of RMB1,997,929,000, trade and other receivables of RMB2,155,173,000, time deposits of RMB1,117,712,000 and pledged deposits of RMB153,754,000. The Group's current assets were RMB7,939,812,000 compared to RMB6,609,300,000 as at 31 December 2020, an increase of 20%.

As at 30 June 2021, interest-bearing borrowings of the Group were RMB2,771,094,000 (31 December 2020: RMB3,365,819,000), RMB1,957,094,000 (31 December 2020: RMB2,773,982,000) of which were repayable within one year and RMB814,000,000 (31 December 2020: RMB591,837,000) of which were repayable over one year. The Group's net gearing ratio (calculated based on the total outstanding interest-bearing debt less pledged deposits, time deposits and cash and cash equivalents and divided by the total equity) was nil, compared to 32.0% as at 31 December 2020.

As at 30 June 2021, interest-bearing borrowings of RMB1,797,700,000 (31 December 2020: RMB2,046,800,000) were denominated in RMB, USD71,043,419 (31 December 2020: USD90,409,032) were denominated in USD, EUR61,216,273 (31 December 2020: EUR75,226,245) were denominated in EUR and HKD52,716,798 (31 December 2020: HKD149,017,583) were denominated in HKD. The majority of the borrowings of the Group were subject to interest payable at rates ranging from 0.75% to 4.75% (31 December 2020: 0.75% to 5.66%). Net cash generated from operating activities during the period was RMB342,161,000 (1H2020: RMB450,520,000).

CAPITAL EXPENDITURES AND CAPITAL COMMITMENTS

For the first half of 2021, the Group's net increase in property, plant and equipment amounted to RMB56,083,000 (1H2020: RMB70,158,000). The increase was mainly related to the infrastructure of the "50,000 Tons Tools Steel Capacity Expansion Project". As at 30 June 2021, capital commitments were RMB520,960,000 (31 December 2020: RMB544,430,000), of which RMB112,100,000 (31 December 2020: RMB69,910,000) was contracted for and RMB408,860,000 (31 December 2020: RMB474,520,000) was authorised but not contracted for. The majority of capital commitments related to smelting, forging and grinding facilities for the "50,000 Tons Tools Steel Capacity Expansion Project".

USE OF PLACING PROCEEDS

The Group placed an aggregate of 200,000,000 shares (representing 7.16% of the enlarged issued share capital of the Company) at the placing price of HK\$4.22 per share to not less than six placees. The placing of the 200,000,000 shares was completed on 7 May 2021 with the net proceeds of approximately HK\$834 million representing a net issue price of approximately HK\$4.215 per share. The market price of the placing share was HK\$4.88 per share as quoted on the Stock Exchange of Hong Kong on 4 May 2021, the last full trading day immediately before the time at which the Placing and Subscription Agreement was signed. The proceeds from the placing have been used as follows:

Intended use of proceeds from the placing	Actual use of proceeds (as at 30 June 2021)	Proposed use of the remaining unutilised proceeds (as at 30 June 2021)
(i) Expansion of the industrial park of the Group in Thailand	Nil was used in the expansion of the industrial park of the Group in Thailand	The remaining unutilised proceeds was HK\$59.9 million
(ii) Development of the new precision tools products of the Group	HK\$12.0 million was used in development of the new precision tools products of the Group	The remaining unutilised proceeds was HK\$347.2 million
(iii) Replenishment of Group's working capital to procure raw materials and meet any cashflow requirements that may arise from daily operations	HK\$138.1 million was used as working capital and for daily operation, including payment of electricity, staff salaries and procurement of raw materials	The remaining unutilised proceeds was HK\$277.2 million

The unutilised proceeds are expected to be fully utilised by 31 December 2022.

RISK AND PREVENTION

Operating Exposure

The pandemic undoubtedly had a profound impact on the Chinese economy. Affected by the various prevention and control measures, the movement of people and business activities have been severely restricted, causing disruptions as well as raw materials and labor shortages in the logistics and manufacturing industries, especially those labor-intensive segments. In the midst of the pandemic, China issued multiple policies to promote the coordinated resumption of work and production of leading enterprises and key links to ensure China's important position in the global manufacturing industry. The pandemic also stimulated the rapid development of smart manufacturing. The promotion of automation and intelligent production, the adoption of more high-tech technologies to effectively respond to labor fluctuations, the high-end parts and components, the intelligent logistics, and the strengthening of the supply chain's anti-risk capabilities have also received high attention.

During this period, the Group made multiple deployments in operations to respond to the rapid changes in the market. In response to the rapid increase in global demand for anti-pandemic products, the Group provided machinery and materials for the manufacturing of such products which successfully offset the risks of a business downturn. In addition, the Group's efforts in overseas business expansion continued under the pandemic. The smooth completion and production commencement of the Thailand project, as well as the launch of the Europe powder metallurgy distribution agreement, have laid a solid foundation for the Group's overseas business, which will help diversify the various operational risks brought by the high concentration of operating regions. In addition, the continuous breakthrough of powder metallurgy "bottleneck" technology and the successful research and development of new carbide tools have also injected strong momentum for the Group's medium and long-term development.

Despite the new waves of pandemic and the uncertainties in economic development, the Group has successfully resisted the various challenges and difficulties by virtue of its decisive and precise strategic deployment, leading industry position, superior quality products and world-class research and development capabilities.

Foreign Exchange Exposure

The Group's revenue was denominated in RMB, USD and EUR, with RMB accounting for the largest portion (64.2% (1H2020: 67.7%)). 35.8% (1H2020: 32.3%) of the total sales and operating profit was subject to exchange rate fluctuations. The Group did not enter into any financial instruments to hedge against foreign exchange risk. The Group has put into place measures such as monthly reviews of product pricing in light of foreign exchange fluctuation and incentivising overseas customers to settle balances on a timely basis to minimise any significant financial impact from exchange rate exposure.

PLEDGE OF ASSETS

As at 30 June 2021, the Group pledged certain bank deposits amounting to approximately RMB153,754,000 (31 December 2020: RMB384,700,000) and no trade receivables (31 December 2020: RMB160,835,000). Details are set out in the notes to the interim financial statements.

EMPLOYEE'S REMUNERATION AND TRAINING

As at 30 June 2021, the Group employed 3,071 employees (31 December 2020: 3,008). The Group provided employees with remuneration packages comparable to the market rates and employees are further rewarded based on their performance according to the framework of the Group's salary, incentives and bonus scheme. In order to enhance the Group's productivity and further improve the quality of the Group's human resources, the Group provides compulsory continuous education and training for all of its staff on a regular basis.

CONTINGENT LIABILITIES

Both the Group and the Company had no material contingent liabilities as at 30 June 2021 (31 December 2020: No material contingent liabilities).

INTERIM DIVIDEND

The Directors do not recommend payment of an interim dividend for the period (no interim dividend for the six months period ended 30 June 2020).

SHARE OPTIONS SCHEME

The current share option scheme of the Company was approved by the Company in the Annual General Meeting held on 26 May 2017.

On 11 January 2018, options entitled holders to subscribe for a total of 60,000,000 shares of USD0.0025 each were granted to and accepted by certain Directors, employees and consultants of the Company in respect of their services to the Group. 50% of these share options would be vested on 31 March 2019 if the consolidated audited net profit of the Company for the year ended 31 December 2018 represented an increase of 50% or more as compared to that of the year ended 31 December 2017. The remaining 50% of these share options would be vested on 31 March 2020 if the consolidated audited net profit of the Company for the year ended 31 December 2019 represents an increase of 50% or more as compared to that of the year ended 31 December 2018. All these options have an initial exercise price of HKD1.50 per share of USD0.0025 each and an exercise period commencing from the relevant vesting date and ending on 31 December of the same year as the vesting date. The closing price of the Company's shares at the date of grant was HKD1.29 per share of USD0.0025 each.

Among these 60,000,000 share options, 30,000,000 share options were vested on 31 March 2019. All share options for these 30,000,000 shares were exercised between 29 August 2019 to 27 December 2019.

The remaining 30,000,000 shares were vested on 31 March 2020. All share options for these 30,000,000 shares were exercised between 23 November 2020 to 30 December 2020.

PURCHASE, SALES OR REDEMPTION OF SECURITIES

During the six months ended 30 June 2021, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed securities.

CORPORATE GOVERNANCE

During the six months ended 30 June 2021, the Company has, so far where applicable, complied with the code provisions set out in the Corporate Governance Code (“CG Code”) contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited except for the following deviation:

Code Provision A.6.7

Code provision A.6.7 of the CG Code stipulates that independent non-executive directors (“INEDs”) and other non-executive directors should also attend general meetings. Mr. Gao Xiang was unable to attend the annual general meeting of the Company held on 1 June 2021 due to the COVID-19 pandemic.

AUDIT COMMITTEE

The Audit Committee comprises three INEDs. The Audit Committee held a meeting on 18 August 2021 to consider and review the interim report and interim financial statements of the Group and to give their opinion and recommendation to the Board. The Audit Committee considers that the 2021 interim report and interim financial statements of the Group have complied with the applicable accounting standards and the Group has made appropriate disclosure thereof.

APPRECIATION

The Board would like to take this opportunity to express gratitude to our shareholders, customers, the management and employees for their unreserved support to the Group.

By Order of the Board
Tiangong International Company Limited
Zhu Xiaokun
Chairman

Hong Kong, 19 August 2021

As at the date of this announcement, the directors of the Company are:

Executive Directors: ZHU Xiaokun, YAN Ronghua, WU Suojun and JIANG Guangqing

Independent non-executive Directors: GAO Xiang, LEE Cheuk Yin, Dannis and WANG Xuesong

** For identification purposes only*