

Section III Summary of the Company's Business

I. Main business, business model and industry situation of the Company during the reporting period

1. Main business, business model of the Company during the reporting period

The Company is a modernized globally leading integrated iron and steel company and the core enterprise of China Baowu Steel Group Corporation Limited, which ranks among Fortune Global 500. Dedicated to its mission to change people's life through creativity, Baosteel is devoted to providing high-quality products and service for customers and creating best value for shareholder and the society for the joint development with stakeholders.

In November 2016, Zhanjiang project was fully put into operation. In February 2017, the Company absorbed and merged shares of Wuhan Iron and Steel Co., Ltd.. By now, the Company owns major production bases including Shanghai Baoshan, Nanjing Meishan, Zhanjiang Dongshan, Wuhan Qingshan etc. and owns world-renowned brands, world first-class technical levels and service capabilities, becoming one of the world's iron and steel enterprises with the most complete carbon steel varieties.

The Company continued the premium product development strategy characterized by technological leadership and paid close attention to the rapid growth of China's high-end manufacturing industry. The main products have been widely used in industries including automobile, home appliances, petrochemicals, machinery manufacturing, energy transportation etc. The Company has been in the leading position in the domestic market in six strategic product areas as automotive steel, silicon steel, tin plate, energy and pipeline steel, high-grade heavy plate, other high-grade sheet products. Based on the advanced technologies such as modern iron and steel smelting, hot and cold processing, hydraulic sensing, electronic control, computer and information communication etc., the Company's overall technology and equipment is characterized by its large-scale, continuity and automation. Thus, the Company has been in a leading position in the world steel industry.

The Company always adheres to take the road of development of "innovation, coordination, green, opening, sharing", pays attention to the cultivation of innovative capability, fully grasps the core technology of steel manufacturing, actively develops and applies the advanced energy saving and environmental protection technology, establishes nationwide and worldwide marketing networks and processing centers, and actively seeks green development and low-carbon solutions of the whole industry chain. The high-end products independently developed by the Company such as new generation of automotive high-strength steel, oriented silicon steel, high-grade home appliance steel, oil and gas pipes, bridge steel, hot rolling heavy rail is in international advanced level. Since 2002, Baoshan Iron & Steel Co., Ltd. has been awarded the "National Science and Technology Progress Award" for 14 consecutive years, which is the only enterprise to receive this award in China.

Taking the platform service for intelligent manufacturing and ouyeel's iron and steel ecology as two wings, the Company builds a new impetus to its development, strengthens five capabilities as "cost innovation, leading technology, service first, intelligent manufacturing and urban steel mills", and strives to achieve the strategic objectives to become "the world's most competitive steel enterprises" and "listed companies with the most investment value".

In 2016, the Company, under the unified arrangements of the group, set up a resolving excess capacity leading group and a resolving excess capacity work contact team to declare the situation of the proposed capacity to resolve. In August, the Company and the group signed the "Target Responsibility Book on Resolving the Excess Capacity of Steel of Baosteel". In November, the State Council SASAC sent national reducing excess steel capacity acceptance group to Baosteel for acceptance. The acceptance group thought that Luojing project and Baotong Iron and Steel of Baosteel successfully completed the task of reducing excess capacity after overcoming many difficulties such as equipment disposal, personnel placement, debt disposal etc.. In December, after the State Council SASAC's acceptance and the National Development and Reform Commission's review Baosteel was confirmed to have completed ahead of schedule the target task of reducing excess capacity of 4.65 million tons assigned to Baosteel in "Target Responsibility Book on Resolving the Excess Capacity" signed by the group and SASAC in 2016, including reducing excess capacity of 3.45 million tons of Luojing project, reducing excess capacity of 1.2 million tons of Baotong Iron and Steel.

2. Company's Industry Development Stage, Cyclical Characteristics and the Company's Industry Status during the Reporting Period

Year 2016 is the start year of "the 13th Five-year". Thanks to the growth of infrastructure, real estate and auto industry, throughout the year, crude steel production is 810 million tons with a year-on-year increase of 1.2%; crude steel apparent consumption is 710 million tons with a year-on-year increase of 2.0%.

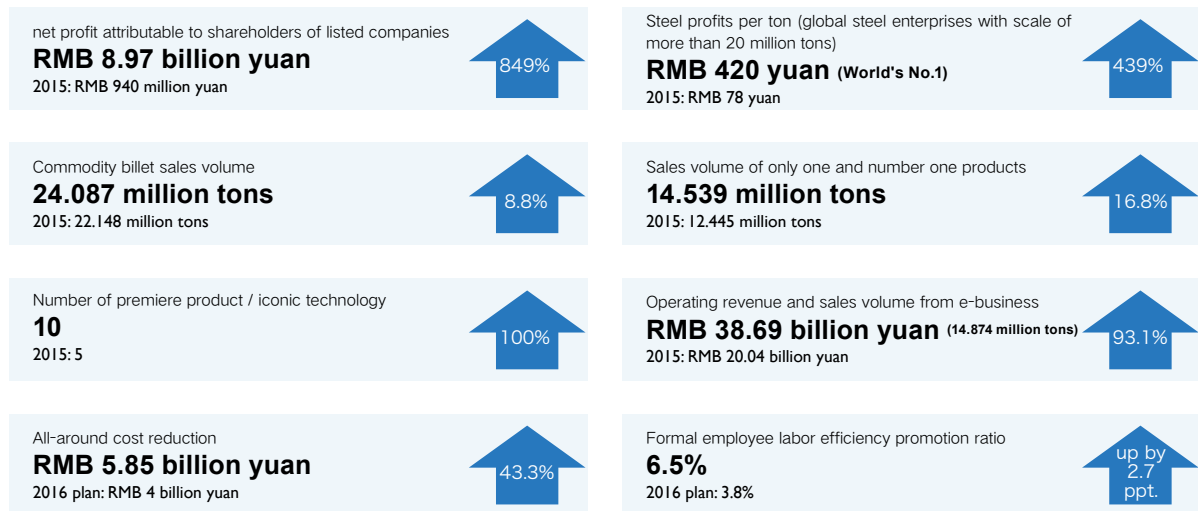
Under the background of implementation of policy on promotion of structural reform of the supply side of steel industry, strict implementation of environmental protection limited production and investigation and prosecution of "ground bar steel", domestic steel prices has successfully reversed the unilateral downward trend since 2011 and has increased significantly, leading to the decrease of China's steel exports. In 2016, China exported 110 million tons of steel with a year-on-year decrease of 3.5%. Based on the market recovery, steel price rise, quality and efficiency improvement of iron and steel enterprises through structural adjustment, transformation and upgrading, in 2016, domestic steel industry reversed the unfavorable situation of industry-wide loss in 2015 at one stroke, 99 large and medium-sized steel enterprises achieved profits of 30.38 billion yuan with a year-on-year increase of 94.91 billion yuan, turning from deficits to profit.

However, China's steel industry is still facing a number of challenges, such as excess capacity, low capacity utilization rate, low industry concentration, uneven development level, unreasonable industrial layout, insufficient innovation and is still in a critical period of transformation

and upgrading, poverty shaken-off and development.

In 2016, the Company adhered to the premium product development strategy, actively maintained differentiation competitive advantage of the domestic high-end product market and accelerated the manufacturing capacity increase of Dongshan base, product certification and market development, having an annual sales volume of unique leading products with a year-on-year increase of 16.8% and of strategic product with a year-on-year increase of 8.6% respectively and continuing to maintain more than 50% of the market share of cold rolled auto sheets. The Company actively expands marketing capabilities on overseas high-end markets, having an annual export volume with a year-on-year increase of 35.6%. The Company also continued to enhance the competitiveness of products by means of full range of cost reduction, further consolidating its competitive position on domestic and foreign markets.

3. Key Data



4. Highlights of the Company during the Reporting Period

- Annual total profit of 11.52 billion yuan, an increase of 553% over the same period last year, ranked second in profits and first in steel profits per ton in the global steel enterprises with scale of more than 20 million tons.
- Curing of cost reduction results. Cost reduction totaled 5.85 billion yuan for the year, exceeding the expected annual targets.
- Significant achievements in technological innovation. Project "Thin Strip Continuous Casting and Rolling Process, Equipment and Control Engineering Technology Integration and Product Development" won special award of metallurgical science and technology award; Result "Secondary Cold Rolling Products and Core Technology Research" won first prize of Shanghai Municipal Science and Technology Progress; Products such as oriented silicon steel B30R090, ultra-high strength continuous tubing steel CT110 etc. has accomplished the world's premiere.
- Zhanjiang Iron & Steel project is going smoothly. No.2 blast furnace was ignited smoothly on July 15, 2016, marking the completion of phase of the project two months ahead of schedule and the beginning to enter the operating stage. Technical and economic indicators and environmental protection indicators continued to improve and operating performance was better than the annual target.
- In February 2017, Baoshan Iron & Steel Co., Ltd. absorbed and merged Wuhan Iron and Steel Co., Ltd.. After the merger, its crude steel output, auto sheets output and oriented silicon steel output ranked third, third and first respectively in the listed global steel enterprises.
- Synchronous promotion of two wings construction. Ouyeel had an annual e-business volume of 14.874 million tons, achieved sales income of 38.69 billion yuan and its logistics platform has outperformed the "thousands of warehouse layout". Wisdom manufacturing path layout and 1580 slab library unmanned transformation has been put into operation.
- Energy saving and emission reduction during the whole process. The amount of energy saving by new technology is 15,000 tons of standard coal, 318,000 square meters of ecological green of the plant has been completed and photovoltaic power generation phase II project has been officially completed and conducted a trial run.
- In 2016, three major credit rating agencies, Standard & Poor's, Moody and Fitch honored the Company with a long-term enterprise credit rating and outlook of BBB+ (stable), Baa1 (negative) and A- (stable) respectively, the Company continued to enjoy the highest credit rating in global iron and steel industry.

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II. Explanation of Significant Changes in the Company's Major Assets during the Reporting Period

√ Applicable □ Not applicable

1. Changes in Equity Assets

(1) Formation of Shanghai Baosteel Asset Management Co., Ltd., specialized in the asset disposal work resulting from supply side reform

In order to respond positively to the requirements of the national supply side reform to resolve steel capacity and to withdraw inefficient and ineffective assets, to seek disposal channels at home and abroad of the assets within the joint stock company to be disposed and to increase the intensity of disposal of the Company's Luojing area and Baotong Iron & Steel downtime assets, to improve asset recovery value, the Company invested 1 billion yuan in December 2016 to set up wholly-owned Shanghai Baoshan Iron & Steel Asset Management Co., Ltd.

(2) Increase of capital to Shanghai Ouyeel Financial Information Services Co., Ltd.

In April 2016, Shanghai Ouyeel Financial Information Services Co., Ltd. issued additional 1.1 billion shares, the Company and its subsidiary Ouyeel Co., Ltd. subscribed for 500 million shares by 290 million yuan and 210 million yuan (totally 500 million yuan) respectively. Upon completion of the issuance, the share capital of Shanghai Ouyeel Financial Information Service Co., Ltd. was 1.4 billion yuan. The Company held 20.9% of its equity, and Ouyeel Co., Ltd. held 34% of its equity, totally 54.91% of its equity.

(3) In March 2016, Baosteel International completed the liquidation and closing of its wholly-owned subsidiary Baosteel Group Guangzhou Free Trade Zone International Trade Co., Ltd., taking back investment of 30 million yuan.

2. Changes in Fixed Assets and Construction in Progress

Fixed assets increased by 27.5 billion yuan compared with the beginning of the year, of which 39.2 billion yuan was transferred from construction in progress (of which 31.5 billion yuan was transferred from Zhanjiang Iron and Steel project), 11.83 billion yuan from depreciation.

The construction in progress decreased by 24.32 billion yuan compared with the beginning of the year, mainly due to the effect of transfer to the fixed assets of Zhanjiang Iron and Steel Construction in progress.

3. Situation of Foreign Assets

As of the end of 2016, the Company had foreign assets of 156.3 (unit: 100 million yuan Currency: RMB), accounting for 5.8% of the total assets.

(1) Development of Foreign State-owned Assets

In 2005, the Company acquired, through additional offering, the equity of overseas marketing companies such as Baosteel Europe, Baosteel America etc. and shipping company such as Bao-Trans and Bao-Island, and the preferred equity of BaoVale Mine Company held by Baosteel Group. Since the beginning of 2011, in order to expand the capacity of overseas manufacturing and processing services, the Company has set up one after another 7 wholly-owned companies or joint ventures such as Bao Li Steel Pipe, Baosteel India etc. in foreign countries. As of the end of 2016, the Company has owned 15 overseas subsidiaries at all levels and 6 overseas shareholding companies at all levels set up in countries and regions such as the United States, Japan, Germany, Singapore, Thailand, Hong Kong etc. As of 2016, the Company's direct investment in subordinate first-class overseas companies is 81.005 million US dollars and the investment area is steel trade and deep processing business. All funds are from the Company's own funds.

(2) Operation Status of Foreign State-owned Assets

Foreign trade subsidiaries mainly include: Howa, Baosteel America, Baosteel Singapore and their subsidiaries; overseas shipping service subsidiaries include Bao-Trans; foreign steel manufacturing and processing service subsidiaries mainly include Bao Li Steel Pipe, BGM, India Cutting Center and Indonesia Steel Processing Center.

(3) Overall Situation of Foreign State-owned Assets

As of the end of 2016, the assets of the Company's subordinate first-class overseas totaled 15.63 billion yuan, operating income totaled 46.19 billion yuan and owner's interests totaled 4.45 billion yuan. In 2016, first-class overseas subsidiaries totally have achieved a total profit of 630 million yuan with a net profit of 510 million yuan and a net assets income ratio of 11.6%.

III. Analysis of Core Competitiveness during the Reporting Period

√ Applicable □ Not applicable

The core competitiveness of the Company is mainly reflected in technological innovation, manufacturing capacity, cost control, customer service, brand building, sustainable development capacity and so on.

1. Technological Innovations

The Company continued the premium product development strategy characterized by technological leadership. In 2016, Baoshan Iron & Steel Co., Ltd. increased investment in technological innovation and made continuous progress in the aspects of product development, technological progress and so on with R&D investment rate of 2.0%, proportion of invention patent applications of over 70% and new test unique ratio of over 71%; Three products as high magnetic sense oriented silicon steel B27R080, B30R090, continuous tubing CT110 have accomplished the world's premiere.

2. Manufacturing Capacity

In 2016, Zhanjiang Iron and Steel has put into operation projects such as cold rolling, heavy plate, No. 2 blast furnace etc.. Phase I project has been fully into capacity climbing period. Thanks to its existing manufacturing base and the use of various forms of mutual feed, the Company not only effectively alleviates the contradiction between supply and demand of some varieties and enhances user support capabilities, but also maximizes its overall efficiency.

In 2016, the company provided a strong guarantee for user certification and industrial production of new varieties of strategic products by means of its stronger manufacturing capacity.

Automotive steel: cold rolling ultra-high strength steel sales volume increased by more than 40% on a year-on-year basis. High elongation cold rolling steel QP980, QP1180 have successfully passed Nissan materials certification, becoming world's fourth, China's first Nissan supplier of such products.

Silicon steel: non-oriented silicon steel has passed BYD new energy vehicle certification and has begun to be ordered in bulk replacing imported materials for the manufacturing of new energy vehicle drive motor. Low noise transformer steel products have been used in bulk for the manufacturing of power transformers, distribution transformers, reactors and so on.

Heavy plate: Marine 2205 duplex stainless steel + DH36 rolling composite plate have passed BV Classification Society certification, becoming world's first manufacturer of 2205 duplex stainless steel composite plate passing the Classification Society certification. The Company has completed smoothly SA738Gr. for CAPI400 nuclear power plant 2 # containment and B steel sheet first contract. LPG marine ultra-low temperature steel has passed main Classification Societies' certification and acquired a certificate from authoritative Classification Society ABS, marking all-round supply capacity in the field of Baosteel.

Hot rolling: Bridge shell steel BQT800 has passed German Daimler plate spring type bridge shell certification. The actual use effect of product BW300TP has been fully recognized in the concrete mixer industry and at downstream users, its comprehensive finished product rate was more than 90%, increasing significantly compared with the amount of contract in 2015.

Cold rolling: The Company has achieved technology, equipment, on-line detection technology industrialization of coated iron new products. The Company has completed the first industrial trial production of zinc, aluminum and magnesium and has completed the first industrial trial production of the low-aluminum zinc-aluminum-magnesium and high-aluminum zinc-aluminum-magnesium coating respectively. The Company has also completed zinc-aluminum-magnesium coating color coated plate trial production and initially mastered zinc-magnesium coating hot-dip plating and color coating technology.

Steel pipe: The Company supplied, for the first time and in bulk, the ultra-high strength coiled tubing CT110 to North America, Iran and other markets, achieving a milestone breakthrough in overseas markets. A scale application of the on-line cold control technology of the international premiere seamless steel pipe has been achieved.

3. Cost Control

Cost reduction is the core strategy for the Company to enhance its competitiveness. In 2016, the Company improved the agile operation, management and control system cored on cost reduction, organized and carried out cost fine management and cost benchmarking in Baoshan base, continuously optimized the financing strategy and reduced capital use cost.

Technological cost reduction: In 2016, the Company mainly carried out work in three aspects: First, reducing cost from the perspective of the whole process, cored on product consistent manufacturing technology. Second, for mature main category products, optimizing product composition, optimizing and simplifying the process, stabilizing manufacturing and improving the finished product rate, achieving low-cost

production from design to production, focused on three dimensions as "specification expansion, cost reduction, manufacturing stability", optimize product composition. Third, giving full play to the role of plant integration, enhancing technological cost reduction effectiveness from the dimensions such as "ability upgrading, structural optimization, process optimization, energy saving and consumption reduction," etc.

4. Custom Service

In 2016, the Company actively explored the research and application of wisdom manufacturing in the supply chain collaboration. Wisdom supply chain collaboration, taking auto sheet users as pilot, established full supply chain intelligent collaboration model, implemented "driving organization of production on demand", improved delivery accuracy, shortened the delivery cycle, reduced supply chain inventory, achieved supply assurance collaboration solutions characterized by low inventory costs, low capital occupation, high efficiency response, stability and reliability, consolidated and continued to enhance Baosteel's competitive advantage in the aspects of supply chain security and assurance. In 2016, the wisdom supply chain system selected 2 pilots, accurately calculating the order according to user needs and inventory, guaranteeing the manufacturing unit's weekly delivery and tracking the contract management and inventory break-point early warning management.

Based on the "customer-centered" business philosophy, focused on differentiated competitive strategies, and according to strategic requirements of transformation from manufacturing to service, the Company actively explored and expanded EVI project, institutionalized EVI project management process and built EVI team. In 2016, the Company's EVI plan covered nearly 60 EVI projects in six major industries, including automotive, home appliances and electronics, transmission and distribution, metal packaging and containers, engineering/machinery and construction, energy and transportation.

5. Brand Building

The Company continued to deepen and improve its brand by taking "creates a change in life" as the starting point for brand building. From November 2014, the Company has advertised for 2 consecutive years by selecting position of Pudong Airport T1 domestic gateway channel light box and Hongqiao Airport T2 security area channel light box; gradually built Baosteel product brand social media platform matrix based on WeChat platform "Hello Baosteel"; continued to carry out three-dimensional brand communication activities, promote the development of "automotive steel overall solution" and promote Baosteel electrical steel product brand themed on "create a life, green travel" and "create a life, bright city".

Focused on its core brand value, the Company further strengthened enterprise brand image spreading by taking "innovation leading", "value sharing", "urban steel mills", "social responsibility" as the basic connotation, shaping and enhancing its brand value.

6. Sustainable Development Capacity

The Company has been committed to work together to create a green industry chain, becoming a best environmentally friendly practitioner. In the aspect of main energy, environmental protection indicators, the Company continued to maintain the world's advanced level and to be an environmental protection leader in China's steel industry. In 2016, the main initiatives and effects of the Company in improving the environment and building green factories were as follows: ① increasing investment in environmental protection technology improvement, implementing the transformation of stockyard, the denitrification of sintered flue gas, the flue gas clean emission transformation of coal-fired units of the power plant, effectively controlling the standard pollutant discharge ② increasing the green area, completing green transformation area of 206,000 square meters such as forest belt construction around the factory, of which the new green area was 144,000 square meters; ③ strengthening the pollution source emission monitoring management, adding on-line monitoring facilities to key emission sources such as steel-making, electric stove, sintering machine tail respectively and so on; ④ expanding photovoltaic power generation. Golden Sun phase II photovoltaic power generation project was officially completed on March 29. The annual total power generation of Phase I and phase II projects was 60 million kWh, equivalent to saving 19,000 tons of standard coal and reducing 47,000 tons of carbon dioxide emissions.