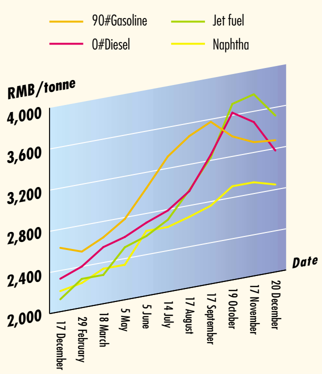
1. OPERATING ENVIRONMENT

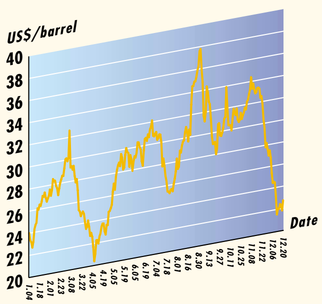
In 2000, the economy of the PRC had recovered from the adverse impacts of the Asian Financial Crisis, and began to turn around. The country's gross domestic product ("GDP") increased by 8 per cent over that of 1999. During the year, a series of macro regulatory polices and measures such as suspending the import of gasoline and diesel, stringent anti-smuggling activities and rectifying small refineries continued to be implemented by the State government and achieved significant result. The total domestic crude oil processing volume in 2000 amounted to 195 million tonnes, a growth of 14 per cent over that of 1999, and the consumption of petroleum products was 109 million tonnes, 5 per cent more than that of 1999.

In 2000, the price of crude oil in the international market fluctuated significantly at a high price level. The price of BRENT crude oil had reached its record high in a decade, and the yearly average crude oil price for the year stood at US$28.63 per barrel ("$/b"), 58.26 per cent higher than that of 1999.

The movement of ex-factory prices of the Company's major petrolum products in 2000 (inclusive of VAT and consumption tax)



Prices of BRENT crude oil in the Singapore market *in 2000*



Source of information: the Platts

A new pricing mechanism has been applied to match the domestic petroleum product prices with that of international market since June 2000. As a result, the petroleum product prices in the PRC are being adjusted on a monthly basis, to correspond to relevant petroleum product prices in the international market.

In 2000, the Company's refining margin was 3.57 $/b, which was lower than that of 1999. This was mainly due to rapid upsurge in crude oil price in the international market and the adjustment in domestic petroleum product prices was not in tandem with the crude price movement in the international market. As a result, the Company's average refining margin was only 1.35 $/b from January to April 2000. The average refining margin of the Company in the second half of 2000 increased to 4.70 $/b after the implementation of the new pricing mechanism. The profit margin was significantly higher than that in the first half of 2000, with improvement in the operating environment.

2. ANALYSIS OF OPERATING RESULTS[2]

2.1. Turnover

Table 1: Sales volume, average selling price and turnover

	1999	2000	% change
Sales volume ('000 tonnes)	7,209.6	**9,990.50**	+38.57
Average selling price (RMB/tonne)	1,497.98	**2,148.31**	+43.41
Turnover (RMB million)	11,015.10	**21,690.00**	+96.91
Including turnover of subsidiaries (RMB million)	215.30	**227.30**	+5.57

In 2000, the Company fully capitalized on its 12 million tpa comprehensive processing capacity to process a total of 10.74 million tonnes of feedstock oil, which was 38.25 per cent more than that of 1999. This made the Company the first refining enterprise with an annual feedstock throughput volume exceeding 10 million tonnes in the PRC. The increase in throughput volume had been in tandem with the upsurge in processing capacity. The Company's sales volume increased by 38.57 per cent to 9,990,500 tonnes in 2000.

The Company's average product selling prices increased by 43.41 per cent during the year as a result of 10 adjustments in the ex-factory prices of the Company's petroleum products in 2000. The turnover of the Company was RMB 21.69 billion, 96.91 per cent more than that of 1999.

2 The following discussion should be read together with the audited combined financial statements and their notes.

Table 2: Sales volume and turnover by products

	1999		2000	
	Turnover *(RMB million)*	Sales volume *('000 tonnes)*	Turnover *(RMB million)*	Sales volume *('000 tonnes)*
Gasoline	**1,918.7**	**1,287.5**	**3,973.2**	**1,721.7**
Diesel	**4,052.4**	**2,573.9**	**8,547.5**	**3,705.5**
Kerosene	**1,343.0**	**819.1**	**2,391.4**	**1,035.9**
Others:				
Urea	703.0	627.6	562.3	551.4
Chemical feed oil	1,071.1	714.0	2,244.9	1,013.6
Fuel oil	74.3	98.1	947.6	706.4
LPG	540.9	287.4	993.6	363.6
Solvent oil	81.8	44.4	149.4	56.0
Intermediate chemicals	676.4	300.4	1,042.9	350.1
Asphalt	251.4	270.2	475.2	369.4
Miscellaneous	153.7	187.0	134.7	116.9
Subsidiary companies	**215.3**	**–**	**227.3**	**–**
Total	**11,015.1**	**7,209.6**	**21,690.0**	**9,990.5**

In 2000, the Company continued to adjust its product mix in accordance with the market demand. The Company's diesel to gasoline output ratio increased from 2.01 in 1999 to 2.2 in 2000, with all of its gasoline manufactured in compliance with the new domestic standards from July 2000. The Company also increased the output of the high-grade paving asphalt and fuel oil to substitute for imported products.

The urea plant was closed for a major overhaul in October 2000 for market reasons. As a result, the sales volume of urea decreased by 12 per cent from that of the previous year.

Table 3: Domestic and export sales volume

	1999 (*'000 tonnes*)	**2000** (***'000 tonnes***)	**% change**
Domestic	6,224.9	**9,139.9**	+46.83
Export	984.7	**850.6**	−13.62
Total	7,209.6	**9,990.5**	+38.57

In 2000, the Company continued to emphases on meeting the growing demand of the domestic market. As a result, the percentage growth in domestic sales volume was higher than that of the Company's total sales volume. The exported products were mainly gasoline and jet fuel with the latter mainly being supplied to the Hong Kong airport.

2.2. Cost of sales

Table 4: Cost of sales

	1999 (*RMB'000*)	**2000** (***RMB'000***)	**% change**
Raw material	8,060,638	**18,233,555**	+126.20
Direct labor	50,720	**58,555**	+15.45
Manufacturing overhead	1,453,160	**1,811,905**	+24.69
Total	9,564,518	**20,104,015**	+110.19

In the year of 2000, the Company's raw material cost increased by 126.2 per cent over that of 1999 due to substantial increase in the Company's throughput volume of feedstock oil and the upsurge in international crude oil prices. Through increasing the processing volume of sour and heavy crude oil, capturing the opportunities to purchase crude oil at lower price in the international market and transporting crude oil by large tankers, the Company managed to control the average unit processing cost of feedstock oil at RMB 1,774 per tonne, or 28.6 $/b in 2000, despite a significant upsurge in transportation fee due to strong demand for oil tankers in the world market. The average unit processing cost was 63 per cent higher than that of 1999 and was basically in line with the average FOB price of Brent crude oil in the international market during the period.

The Company's full year overhaul expenses decreased by RMB 26.63 million. Manufacturing overheads increased by RMB 358.75 million due to the increase in the throughput volume of crude oil and additional depreciation charges arising from the commissioning of new facilities during the year. Cost of direct labor increased by RMB 7.83 million in the year 2000. As a result, the Company's cost of sales increased by RMB 10,539 million or 110.19 per cent when compared with that of 1999.

In 2000, the Company's refining unit-processing cost decreased by 22.10 per cent from that of 1999, and saved RMB 288 million in cost by strengthening management, optimizing facilities integration and benefited from the significant increase in processing volume. For instance, commissioning of the CFB boiler enabled the Company to achieve integration in refining and thermoelectricity generation. The project served to save RMB 65 million in energy expense for the Company.

In 2000, the Company's refining unit-operating cash cost was 1.17 $/b, which was 27.78 per cent less from that of the previous year.

2.3. Selling, administration and financial expenses

Table 5: Selling, administration and financial expenses ("S,G&A expenses")

	1999 *(RMB '000)*	**2000** ***(RMB '000)***	**% change**
Selling expenses	118,788	**268,488**	+126.02
Administration expenses	459,372	**483,234**	+5.19
Financial expenses	61,939	**115,929**	+87.17
Total	640,100	**867,652**	+35.55

In 2000, the increase in selling expenses was mainly attributed to the change in the accounting treatment in some of the Company's subsidiaries. Some expenses, which had been treated as cost of goods sold in previous year, were booked as selling expenses in 2000. Administration expenses increased by RMB 23.86 million due mainly to the increase in the wages of the employees and labour insurance premium. Following the commissioning of the 8 million tpa refining capacity expansion project ("RCEP" project) during the year under review, interest expenses for the related facilities, ceased to be capitalized, and were charged as financial expenses, resulting in an upsurge in financial expenses. Total S,G&A expenses increased by RMB 227.55 million in 2000.

2.4. Profit before taxation and profit after taxation

Tabel 6: Profit before taxation and profit after taxation

	1999 (RMB '000)	**2000 (RMB '000)**	**% change**
EBITDA	1,530,902	**1,502,327**	–1.87
EBIT	871,292	**685,161**	–21.36
Profit before taxation	811,780	**575,604**	–29.09
Provision for income tax	248,894	**154,827**	–37.79
Profit after taxation	562,886	**420,777**	–25.25

The Company's profit after taxation for the year 2000 was RMB 421 million, 25.25 per cent lower than that of 1999, as a result of the substantial increase in feedstock oil cost and the adjustment in the petroleum price lagged behind the movement of international oil prices during January to April of 2000.

3. ANALYSIS OF FINANCIAL POSITION

Table 7: Major items of the balance sheet

	1999 (RMB'000)	**2000 (RMB'000)**
Total liabilities	3,830,265	**4,146,057**
Including:		
Long-term loans(note)	2,238,255	**2,280,341**
Short-term loans(note)	230,210	**52,743**
Shareholders' equity	7,149,181	**7,450,762**
Total liabilities and shareholders' equity	10,979,446	**11,596,817**
Current assets	3,508,578	**4,465,951**
Current liabilities	1,479,223	**1,692,433**
Inventories	832,789	**1,525,515**
Trade receivables, net	123,417	**212,814**
EBIT / Interest expense	16.64(X)	**6.25(X)**
EBITDA / Interest expense	25.72(X)	**13.71(X)**

Note: Long-term loans, net of current portion, but included the Company's convertible bonds. Short-term loans included the current portion of long-term loans.

The asset-liability ratio increased slightly from 34.89 per cent as at the end of 1999 to 35.75 per cent as at the end of 2000. The Company assets structure was still at a reasonable level. The Company's current ratio increased from 237.19 per cent in 1999 to 263.88 per cent in 2000.

During the year 2000, due to the Company's stringent control, the turnover of the Company's account receivables improved from 28.03 times to 46.68 times and the turnover of inventories improved from 13.23 times to 17.05 times, despite an almost 100 percent increase in turnover.

4. CAPITAL EXPENDITURE

Capital expenditure for the year 2000 was RMB 589 million, RMB 298 million of which was invested in the first phase of the RCEP project for further facility integration. The first phase of the RCEP project has been completed in 2000 and is expected to be commissioned in the first half of 2001. It is expected that there would be a substantial saving in project investment.

Capital expenditure for the year 2001 is expected to be RMB 1,400 million.

5. FUTURE PROSPECTS

5.1. Refining capacity expansion project

China's imported crude oil volume increased significantly in the past five years. China is expected to further increase its imported crude oil volume to support the development of the domestic economy. Sinopec has worked out a plan to expand the imported crude oil processing capacity in the coastal areas. The Company is one of the refining enterprises to be given priority for further development given its strategic market location, advanced processing facilities and healthy financial position.

The Company's refining capacity expansion projects in the next five years mainly include the following: in expanding its refining capacity, the Company plans to enhance refining capacity, in particular to improve its sour crude oil processing capacity, mainly through upgrading its existing facilities. After expanding its comprehensive processing capacity to 16 million tpa by 2003. The Company will further increase its processing capacity in accordance with the market demand. In enhancing product quality, the Company aims to have its domestically sold gasoline and diesel meeting the new domestic standards, and strives to produce gasoline for large PRC cities and export meeting the standards of AUTO II level. To meet these ends, the Company plans to strengthen its capacity in hydrocracking, reforming and hydrogenetation.

With the completion of the aforementioned expansion projects, the Company will become a leading refining enterprise in the PRC in terms of operation scale, advanced technology, facility integration and product quality, and will provide a solid foundation for the Company's downstream expansion into the manufacture of chemical products.

5.2. Paroxylene project ("PX" project)

A 450,000 tonnes-PX project was originally planned under the RCEP project. But the construction of PX project was postponed in 1997 in response to unfavourable market condition. It is estimated that the production capacity of PTA, which is the downstream product of PX, will substantially increased in the next five years, and the growth in domestic demand for PX will exceed world average. For this reason, the Company has decided to resume the development of the PX project. Total investment in the project will be trimmed to RMB 1.7 billion through further optimization of resources. The PX project is expected to be completed in 2003.

Supported by the Company's large scale refining facilities, the PX project can have reliable supply of resources. Applying the state-of-the-art international technology, the project will have an annual capacity of 450,000 tpa, which meets the international standard for a single unit. As the only commercial supplier of PX in the PRC, the PX project is expected to have a strong market prospect.

The Company also plans to expand and upgrade the integrated supporting and logistic facilities, including product storage and transportation and the utility facilities, to meet the needs of refining capacity expansion and PX projects.