

BUSINESS OPERATING REVIEW

The Company was established as a joint stock limited company with limited liability under the Company Law of the PRC on November 5, 1999 as part of the restructuring of CNPC. In the restructuring, CNPC injected into the Company most of the assets and liabilities of CNPC relating to its exploration and production, refining and marketing, chemicals and natural gas businesses. The ADSs and H shares of the Company were listed on The New York Stock Exchange and The Hong Kong Stock Exchange Limited on April 6, 2000 and April 7, 2000, respectively.

The Company is engaged in a broad range of petroleum-related activities, including:

- the exploration, development and production of crude oil and natural gas;
- the refining, transportation, storage and marketing, including import and export, of crude oil and petroleum products;
- the production and sale of chemical products; and
- the transmission, marketing and sale of natural gas.

The Company is China's largest producer of crude oil and natural gas and one of the largest companies in China in terms of sale. Currently, all of the Company's petroleum and natural gas reserves and production-related assets are located in China.

Exploration and Production

As at December 31, 2000, the Company had estimated proved reserves of approximately 11.03 billion barrels of crude oil and approximately 32.5 trillion cubic feet of natural gas. The Company believes that it holds exploration and production licences for the substantial majority of China's proved crude oil and natural gas reserves. In the 12 months ended December 31, 2000, the Company produced 765.4 million barrels of crude oil and 505.3 billion cubic feet of sales natural gas, representing an average production of approximately 2.10 million barrels of crude oil and approximately 1.38 billion cubic feet of sales natural gas per day and sold 719.2 million barrels of crude oil and approximately 480.5 billion cubic feet of natural gas. Approximately 71% of the crude oil the Company sold in 2000 was supplied to its refineries.

Refining and Marketing

In the 12 months ended December 31, 2000, the Company's refineries processed approximately 547 million barrels of crude oil or an average of approximately 1.50 million barrels per day. In 2000, the Company produced approximately 42.70 million tons of gasoline, diesel and jet fuel and sold approximately 44.16 million tons of these products. Approximately 93% of the crude oil processed in the Company's refineries was supplied by the exploration

and production segment of the Company. The Company is actively expanding its sales and distribution networks, in particular, the retail distribution network, by capitalising fully on the complementary value-added effect of integration of refining and marketing. As of December 31, 2000, the retail distribution network of the Company included 4,683 service stations owned and operated by the Company, 3,600 service stations wholly-owned by CNPC itself or jointly owned by CNPC with third parties and to which the Company provides supervisory support and approximately 3,067 franchise service stations owned and operated third parties with which the Company has long-term gasoline supply agreements. As of December 31, 2000, the Company owned and operated a crude oil pipeline network consisting of approximately 8,748 kilometres of pipelines with an average daily throughput of approximately 2.19 million barrels of crude oil. As of December 31, 2000, the Company also had a refined product pipeline network consisting of approximately 984 kilometres of pipelines with an average daily throughput of approximately 17,807 tons of refined products.

Chemicals

The Company is one of the two largest chemical producers in the PRC and the remaining domestic market shares are distributed unevenly among other chemical producers. In the 12 months ended December 31, 2000, the Company produced approximately 1.5 million tons of ethylene, approximately 1.85 million tons of synthetic resin, approximately 0.30 million tons of synthetic fibres, approximately 0.22 million tons of synthetic rubber, and approximately 3.11 million tons of urea. The Company is a major ethylene producer. Since ethylene is a major raw material in the production of various chemicals, the Company is upgrading its production efficiency in ethylene in order to reduce the production costs of chemicals. Through the improved technology and the adjustment of product-mix, there has been significant improvement in the operation results of the chemicals segment, achieving profitability gain in 2000.

Natural Gas

The natural gas segment is the core business segment for development. In the 12 months ended December 31, 2000, of the Company's production of sales natural gas of 480.5 billion cubic feet, 391.0 billion cubic feet was sold through the Company's natural gas segment. The Company currently owns and operates regional natural gas pipeline networks consisting of approximately 11,617 kilometres of pipelines, of which approximately 10,525 kilometres are operated by the natural gas segment. With the construction of the Seninglan Pipeline and the Zhongwu Pipeline, the natural gas segment will be provided with a solid foundation for future growth. The Company will engage in the construction of pipelines from Xinjiang to Shanghai as scheduled and is currently undertaking the preliminary work.