General

Mr. Zhao Qichao
Executive Director
and General Manager

This discussion should be read in conjunction with the information in the Auditors' Report contained in this annual report. The information presented below interprets the Company's accounts as prepared in accordance with IFRS. For the Company's annual report on Form 20-F filed with the Securities and Exchange Commission of the United States of America, a copy will be provided to any shareholder upon written request.

The information set out below does not form part of the accounts audited by Arthur Andersen & Co, the auditors of the Company, and is included for information purposes only.

IFRS requires the management to make estimates, assumptions and judgments that may affect the reported amount of assets, liabilities and expenses, and related disclosures. On an on-going basis, the Company evaluates these estimates, including those related to valuation of inventory and assets and revenue recognition. The Company's estimates are based on past experience, information it receives from third parties and on various assumptions that the Company believes to be reasonable under the circumstances, the results of which form the basis for making judgments about assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. In response to Release 33-8040 by the U.S. Securities and Exchange Commission, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," the Company has identified its "critical" accounting policies as those that involve the most complex or subjective decisions or assessments. These policies are those relating to revenue recognition and the carrying value of inventory and assets. These policies are discussed in this section and the notes to our financial statements.

These critical accounting policies include:

Revenue and income are recognised when it is probable that the economic benefits associated with the transaction will flow to the Company and the amount of the revenue be measured reliably. Turnover represent the gross invoiced value of goods, net of value-added tax ("VAT"), sales taxes, discounts and returns, and are recognised upon delivery of goods and transfer of risks and rewards of ownership has been completed. Interest income from deposits placed with banks and other financial institutions is recognised on a time proportion basis that reflects the effective yield on the assets.

Property, plant and equipment are stated at revalued amount less accumulated depreciation and accumulated impairment loss. The initial cost of property, plant and equipment comprises its purchase price including import duties and non-refundable purchase taxes and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Property, plant and equipment acquired during the Reorganisation were revalued by independent valuers and were stated at revalued amount less accumulated depreciation and accumulated impairment loss. Revaluation is performed periodically to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. Property, plant and equipment acquired subsequent to Reorganistion are stated at historical cost basis. Depreciation is computed on a straight-line basis to write off the cost or revalued amount, after taking into account the estimated residual value of each property, plant and equipment over its expected useful life. The depreciation method and the expected useful lives of the assets are reviewed periodically.

Inventories are valued at the lower of cost and net realisable value, after provision for obsolete items. Net realisable value is the selling price in the ordinary course of business less the costs of completion, marketing and distribution. Cost is determined primarily on the basis of weighted average cost. For processed inventories, cost includes the applicable allocation of fixed and variable overhead costs based on a normal operating capacity.

The Company is one of the largest producers of ethylene, resins and plastics in the PRC. The vast majority of the Company's products fall within three principal product groups: (i) resins and plastics, (ii) synthetic rubber, and (iii) basic organic chemical products. In 2001, the Company accounted for approximately 8.1% of the total ethylene production in the PRC. The Company is a leading producer in the PRC of LDPE, cis-polybutadiene rubber, butyl rubber, phenol, acetone, SBS and polypropylene.

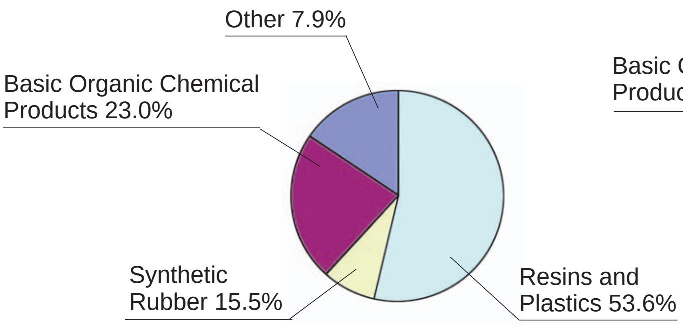
The Company's principal raw material is cracking feedstock, substantially all of which is purchased from the Parent Company. The Company mainly uses light industrial oil as its cracking feedstock. The Company also uses naphtha, VGO, cracking wax oil, and hydrogenated raffinate oil as substitute of light industrial oil achieved by the efforts of the Company's research and development. Since the establishment of Sinopec Group in 1998, prices of light industrial oil and naphtha have been determined by the State Development and Planning Commission ("SDPC") of the PRC and the Sinopec Group together. In 2001, the average State price of light industrial oil fluctuated in line with the crude oil price and decreased by approximately 9.7%, as compared with the price in 2000.

Operating Results

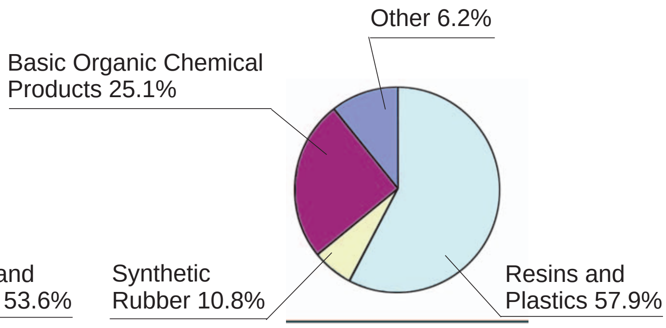
For the year ended 31st December, 2001, the Company's total sales decreased to RMB5,954.5 million from RMB7,824.5 million in 2000, representing a decrease of 23.9%. This decrease in sales was attributable to the decrease in the prices of petrochemical products resulting from an increase in the import of petrochemical products into China from nearby Asian countries. During the reporting period, the weighted average prices of the Company's eight principal petrochemical products decreased by 8.7%. There was also a large decrease in the production of the Company's principal petrochemical products due to the special production shutdown period of approximately 100 days required to complete the Ethylene Project. The Company recorded a loss before taxation of RMB426.5 million in 2001, as compared with a profit before taxation of RMB508.8 million in 2000, representing a decrease of 183.8%. The Company recorded a net loss of RMB283.4 million in 2001, as compared with a net profit of RMB 347.8 million in 2000, representing a decrease of 181.5%.

The following table sets forth a summary of the profit and loss accounts for the years ended 31st December, 2001 and 2000:

	2001	2000
	RMB'000	RMB'000
Turnover	**5,954,526**	7,824,547
Cost of goods sold	**(5,660,191)**	(6,664,093)
Gross profit	**294,335**	1,160,454
Selling, general and administrative expenses	**(560,940)**	(530,743)
Operating (loss) profit	**(266,605)**	629,711
Financial expenses, net	**(59,579)**	(97,893)
Other expenses, net	**(100,295)**	(23,030)
(Loss) Profit before taxation	**(426,479)**	508,788
Taxation	**143,120**	(161,029)
Net (loss) profit	**(283,359)**	347,759
(Losses) Earnings per share (RMB)	**(0.084)**	0.103
(Losses) Earnings per ADS (RMB)	**(4.200)**	5.154



2001 Turnover



2000 Turnover

The following table sets forth a summary of the financial data of the Company for the last five years:

	2001	2000	1999	1998	1997
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Total assets	**10,943,663**	9,159,923	8,852,805	8,430,316	7,600,671
Total liabilities	**5,631,610**	3,429,551	3,267,752	3,127,832	2,229,320
Net assets	**5,312,053**	5,730,372	5,585,053	5,302,484	5,371,351
Turnover	**5,954,526**	7,824,547	6,454,683	5,384,467	6,293,463
Operating (loss) profit	**(266,605)**	629,711	605,547	232,154	1,107,552
Net (loss) profit	**(283,359)**	347,759	346,421	115,799	728,372
Dividend declared	**-**	134,960	202,440	67,480	205,814

The following table sets forth the Company's turnover, net of product discounts, returns and VAT, by principal product groups for the years ended 31st December, 2001 and 2000:

	2001		2000	
	Turnover RMB '000	**Percentage of turnover**	Turnover RMB '000	Percentage of turnover
Resins and plastics	**3,192,077**	**53.6**	4,531,438	57.9
Synthetic rubber	**922,301**	**15.5**	848,028	10.8
Basic organic chemical products	**1,368,437**	**23.0**	1,964,733	25.1
Other	**471,711**	**7.9**	480,348	6.2
Total	**5,954,526**	**100.0**	7,824,547	100.0

The following table sets forth the Company's turnover, net of product discounts, returns and VAT, by geographical analysis for the years ended 31st December, 2001 and 2000:

	2001		2000	
	Turnover RMB Million	**Percentage of turnover**	Turnover RMB Million	Percentage of turnover
Northeastern China	**166.7**	**2.8**	219.1	2.8
Northern China	**2,876.1**	**48.3**	3,294.1	42.1
Eastern China	**1,857.8**	**31.2**	2,777.7	35.5
Central-southern China	**655.0**	**11.0**	1,025.0	13.1
Northwestern China	**41.7**	**0.7**	86.1	1.1
Southwestern China	**190.5**	**3.2**	281.7	3.6
Exports	**166.7**	**2.8**	140.8	1.8
Total	**5,954.5**	**100.0**	7,824.5	100.0

The following table sets forth the percentages of turnover to the principal operating expenses associated with the Company's business:

	2001	2000
	%	%
Turnover	**100.0**	100.0
Less: expenditures		
Raw materials consumed	**67.6**	62.2
Utilities	**13.2**	10.2
Depreciation	**8.5**	6.2
Repairs and maintenance	**1.9**	2.8
Salaries & staff welfare	**3.0**	2.8
Other overheads	**0.9**	1.0
Selling, general and administrative expenses	**9.4**	6.8
Operating margin	**(4.5)**	8.0

Raw material expenses were the largest component of the operating expenses. In 2001 and 2000, approximately 52.3% and 53.5%, respectively, of the cost of goods sold were expenses relating to purchases of cracking feedstock. In 2001, the total cracking feedstock expense was RMB2,959.6 million, as compared with RMB3,566.9 million in 2000, representing a decrease of RMB607.3 million, or 17.0%. This reduction was largely due to a decrease in the consumption of cracking feedstock resulting from the special production shutdown of the Company's major production facilities in 2001 which lasted for approximately 100 days for completing the Ethylene Project. The average price of the cracking feedstock used by the Company decreased by 1.81%, as compared with 2000. Although the price of light industrial oil decreased significantly in the fourth quarter of 2001 due to fluctuation of the crude oil price, the average price of light industrial oil in 2001 decreased by approximately 9.7%, as compared with the price in 2000.

The following table sets forth the changes in the State price of light industrial oil, the principal raw material of the Company, in 2001 and 2000 (including VAT):

unit: RMB/ton

Month / Year	1	2	3	4	5	6	7	8	9	10	11	12
2000	2,200	2,240	2,340	2,340	2,740	2,630	2,630	2,690	2,760	2,760	2,910	2,850
2001	2,430	2,260	2,540	2,465	2,520	2,615	2,575	2,260	2,190	2,250	1,800	1,800

Since a significant portion of the Company's expenses has been either fixed (as in the case of depreciation expense for a given piece of equipment) or consisted of stable unit costs (as in the case of cracking feedstock), fluctuations in sales, particularly those principally caused by changes in sales volume or raw material prices, caused disproportionately large fluctuations in profitability. In 2001, the special shutdown of the Company's major production facilities lasting approximately 100 days contributed to an unusually large decrease in the total sales volume for the year. Consequently, the operating margin of the Company decreased from 8.0% in 2000 to -4.5 % in 2001.

Year ended 31st December, 2001 compared with year ended 31st December, 2000

Turnover decreased to RMB 5,954.5 million in 2001 from RMB 7,824.5 million in 2000, representing a decrease of RMB1,870.0 million or 23.9%. Due to the large amount of imported products and the decrease in the price of crude oil in the international market, the weighted average price of the Company's eight principal products, which accounted for 71.6% and 75.4%, respectively, of total sales in 2001 and 2000, decreased by 8.7% in 2001. The decrease in turnover can be attributed primarily to a 20.9% decrease in the sales volume of these eight principal products as compared with 2000 and the special shutdown of the Company's production facilities for approximately 100 days in 2001.

Sales of resins and plastics, which accounted for 53.6% of the Company's turnover, decreased by approximately 29.6% from RMB 4,531.4 million in 2000 to RMB 3,192.1 million in 2001. This decrease was principally attributable to a decrease in the weighted average prices and the sales volume of resins and plastics. In 2001, the average prices for LDPE, HDPE, polypropylene, polystyrene and polyester chips decreased by 8.9%, 7.4%, 2.9%, 25.5% and 0.9%, respectively. The sales volume of resins and plastics decreased by 169,882 tons as compared with 2000.

Sales of synthetic rubber, which accounted for 15.5% of turnover, increased by approximately 8.8% from RMB 848.0 million in 2000 to RMB 922.3 million in 2001. The increase was primarily due to an increase in the sales volume of 13,659 tons, or 50.3%, of SBS, as compared with 2000.

Sales of basic organic chemical products, which accounted for 23.0% of turnover, decreased by approximately 30.4% from RMB 1,964.7 million in 2000 to RMB 1,368.4 million in 2001 as a result of decreases in product prices and sales volume.

Sales of other products, which accounted for 7.9% of turnover, decreased by approximately 1.8% to RMB 471.7 million in 2001 from RMB 480.3 million in 2000.

Cost of goods sold decreased to RMB 5,660.2 million in 2001 from RMB 6,664.1 million in 2000. The decrease was mainly due to the decreased sales volume in 2001. The Company's gross margin decreased from RMB 1,160.5 million in 2000 to 294.3 million in 2001, as gross profit fell from 14.8% in 2000 to 4.9% in 2001.

Selling, general and administrative expenses increased by RMB 30.2 million, or approximately 5.7%, to RMB 560.9 million in 2001 from RMB 530.7 million in 2000. This increase was primarily due to an increase of approximately RMB 50 million in reserves for bad and doubtful debt as compared with 2000.

The Company's loss from operations in 2001 was RMB 266.6 million, as compared with a profit of RMB 629.7 million in 2000. The Company's operating margin decreased to -4.5% in 2001, as compared with 8.0% in 2000, mainly due to higher unit sales cost and lower sales volume for principal products.

Aggregate financial expenses decreased to RMB 59.6 million in 2001 from RMB 97.9 million in 2000, primarily due to an increase in the capital to finance the Ethylene Project which led to the enhanced capitalization of the current loan interest used for the Ethylene Project.

In 2001, the Company recorded a loss before taxation of RMB 426.5 million, as compared with a profit before taxation of RMB 508.8 million in 2000. The Company has approximately RMB 143.1 million in deferred tax credits in 2001 due to an adjustment of deferred tax according to IFRS. The Company's net loss for 2001 was RMB 283.4 million, yielding a net loss margin of 4.8%, as compared with the Company's net profit of RMB 347.8 million and net profit margin of 4.4% in 2000.

Liquidity and capital resources

The Company has principally relied on funds from operations, bank loans and equity capital to finance its capital expenditures and working capital.

The Company's net cash flow derived from operations is generally higher than its net profit, mainly due to substantial depreciation and amortization expenses. In 2001, the Company's net cash flow from operating activities was RMB 668.2 million, primarily consisting of (i) loss before taxation of RMB 426.5 million, (ii) total depreciation and amortization expenses of RMB 541.7 million and (iii) a net decrease of RMB 596.6 million in operating assets. The net decrease in net operating assets was due to a RMB216.0 million decrease in operating assets and a RMB380.6 million increase in operating liabilities. The decrease in operating assets was primarily due to a RMB53.0 million decrease in account receivables, a RMB284.5 million decrease in inventories, and a RMB139.2 million increase in receivables from related companies. As of 31st December 2001, the Company's accounts receivable and notes receivable were RMB 414.2 million, equivalent to 25 days of 2001 sales. The increase in operating liabilities was primarily due to an increase of RMB379.8 million in payables to related companies and the Parent Company. Cash flow from operating activities was also reduced due to the loss.

Net cash used in investing activities was RMB2,046 million in 2001. The Ethylene Project, including LDPE support facilities, became operational at the end of 2001.

The Company's short term and long term loans are primarily obtained from PRC domestic banks. In 2001, the Company repaid RMB 1,470.0 million of its short term loans and RMB 249.0 million of its long term loans, and borrowed RMB 2,490.0 million in short term loans and RMB 1,019.0 million in long term loans. As of 31st December, 2001, the Company's total loans from banks, the Parent Company and a related company increased by approximately 68.1% to RMB 4,418.2 million (including RMB 2,030.0 million of short term loans) from RMB 2,628.5 million (including RMB 1,010.0 million of short term loans) as of 31st December, 2000. The extent to which borrowings are at fixed interest rates was amounted to RMB3,500.0 million (2000: RMB980.0 million) as at 31st December, 2001.

The Company expects to incur capital expenditures of RMB 600.0 million, RMB 300.0 million and RMB 200.0 million in 2002, 2003 and 2004, respectively. Such capital expenditures will be for the expansion of the supporting facilities of the Ethylene Project and other technical improvement projects. The Company believes the cash flow from its operating activities and new bank loans will be sufficient to cover the Company's expected capital expenditures for the above period.

Gearing Ratio

In 2001 the Company's gearing ratio was 83.2%, as compared with 45.9% in 2000. The increase in the gearing ratio was mainly due to a large increase in both the long term and short term debts. The gearing ratio is calculated by dividing the total of long term and short term debts by the total of shareholders' equity.

Dividend policy

Following the establishment of the Company as a joint stock limited company in April 1997, the distribution of the Company's dividends is considered annually by the Board of Directors and decided by the shareholders in general meeting. Payment of future dividends will depend on the Company's revenue, financial condition, future earnings and other factors.

Contingent Liabilities

As of 31st December 2001, the Company had no significant contingent liabilities.

Purchase, Sale and Investment

Save as disclosed in this report, during the year 2001, there was no material purchase, sale or investment in connection with the Company's subsidiaries and associates.

Pledges of Assets

During the year 2001, there was no material pledge of assets by the Company.

Exposure to Fluctuations in Exchange Rates and Any Related Hedges

The Company is exposed to foreign currency risk as a result of its foreign currency denominated long term debt and, to a limited extent, cash and cash equivalents denominated in foreign currencies. The Company had no foreign currency hedging activity in 2001.

US GAAP Reconciliation

The Company prepares a set of accounts in compliance with IFRS, which differs in certain respects from US GAAP. Please refer to note 27 to the financial statement for the differences in accounting policies.