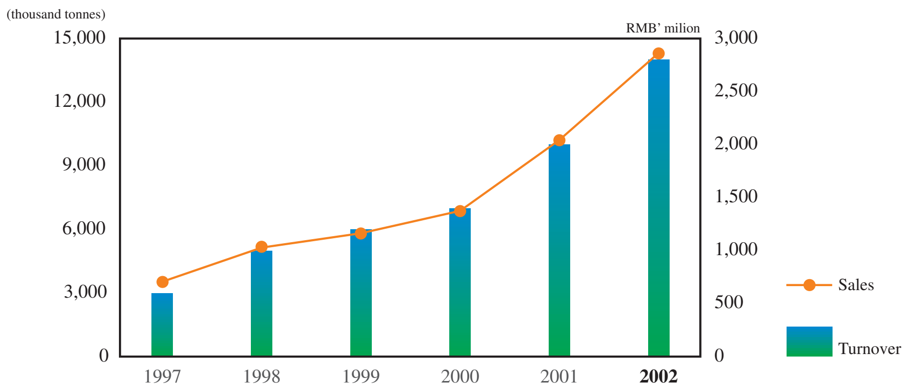
BUSINESS ENVIRONMENT

In 2002, China marked the debut on its accession to the World Trade Organisation. The Chinese economy sustained a continual and healthy development with rapid growth in its fixed asset investment as well as the foreign trade. The accelerated pace of structural realignments within the cement industry has brought favourable market opportunities to the Company's development.

OPERATING CONDITIONS OF PRINCIPAL OPERATIONS

The Group continued to focus on the development of its principal operations in cement and commodity clinker in 2002. Leveraging on the functions of marketing network and the market expansion capability of its grinding mills, the Company secured substantial growth in its market coverage and market share and further capitalised on the advantages of its economies of scale, which attributed to significant increase in its revenue. In addition, the Company was able to lower the production costs of its products by capitalising on its technology expertise and improving its product structure, that helped to strengthen the overall competitiveness of its products with a steady growth in its operating results.

Trend of changes in sales and turnover between 1997–2002



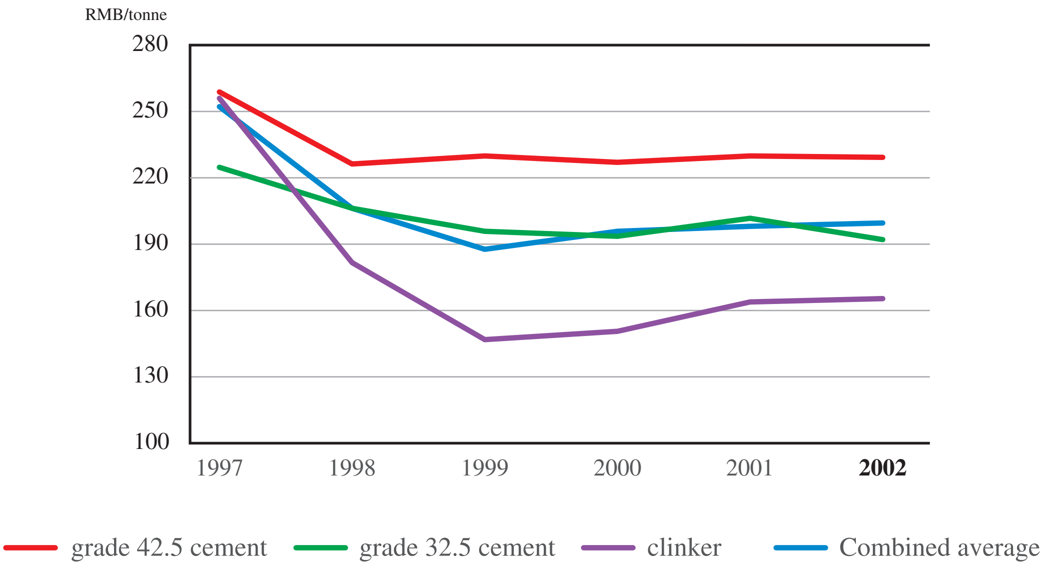
During the reporting period, the Group maintained a reasonable product structure after streamlining and expanding its market in view of different requirements from various sectors. Sales made by all products were relatively stable as compared to the previous year.

Percentage of sales by products
(Year ended 31 December)

Items	2002 Amount (RMB'million)	2002 Percentage (%)	2001 Amount (RMB'million)	2001 Percentage (%)
Cement				
Grade 42.5	**1,262**	**42.08**	861	41.85
Grade 32.5	**1,384**	**46.15**	947	45.98
Sub-total	**2,646**	**88.23**	1,808	87.83
Clinker	**354**	**11.77**	250	12.17
Total	**3,000**	**100.00**	2,058	100.00

The Group has set up a price control committee to improve its pricing management. With the establishment of such open and fair price control system, the Group can make timely adjustments to prices, resulting in more stable selling prices of products.

Changes in cement and clinker prices between 1997–2002



Percentage of sales of products by region
(Year ended 31 December)

	2002		2001	
	Amount (RMB'million)	**Percentage (%)**	Amount (RMB'million)	Percentage (%)
Region				
Shanghai City	**488**	**16.3**	325	15.8
Jiangsu Province	**851**	**28.4**	400	19.4
Zhejiang Province	**735**	**24.5**	668	32.4
Fujian Province	**122**	**4.1**	187	9.1
Jiangxi Province	**170**	**5.7**	61	3.0
Anhui Province	**633**	**21.0**	417	20.3
Total	**3,000**	**100.0**	2,058	100.0

The Company continued to develop its market by way of enlarging its operation scale through acquisitions and mergers in 2002. The expansion projects of grinding mills in Zhangjiagang, Nantong, Nanjing, Jiande, Changfeng and Bangbu were completed successfully as scheduled. The inclusion of Zhongguo Cement Plant and Lushan Cement Plant in the Group helped to enlarge the operation scale that led to substantial increases of the Company's market share in each region. As such, the market position of the Company was further consolidated.

OPERATING RESULTS

The Group exerted strenuous efforts on enhancing the Company's profitability and corporate values in line with the accelerated paces of business development. Nevertheless, the Group kept a steady growth in profits despite of the fact that the preferential treatment for income tax refund was cancelled due to the realignment of the State's taxation policies for the year. The Group's net profit after tax and minority interests amounted to RMB263.76 million as calculated in accordance with the PRC Accounting Standards, representing an increase of 30.11% as compared with that of last year, while the Group's net profit after tax and minority interests as calculated in accordance with the IFRS amounted to RMB267.6 million, representing an increase of 29.48% as

compared to the previous year. The net profit calculated in accordance with the IFRS exceeded the net profit calculated in accordance with the PRC Accounting Standards by RMB3.84 million primarily because of the differences between these two accounting standards in respect of the presentation of the surplus arising on revaluation of land upon the conversion of the Company upon establishment. An analysis of the major changes to the Group's income statement as prepared in accordance with the PRC Accounting Standards is set out as follows:

Changes to major items in the Group's income statement as prepared in accordance with the PRC Accounting Standards:

Item	**Amount ('000)** **2002** **RMB'000**	 2001 RMB'000	**Increase(+)** **Decrease(-)** **in %**
Income from principal operations	**2,999,776**	2,058,349	45.74
Profit from principal operations	**1,019,260**	737,075	38.28
Total profit	**543,729**	314,874	72.68
Net profit	**263,758**	202,726	30.11

2002 Gross profit by products and comparison

Product items	Income from principal operations (RMB' million)	Costs of principal operations (RMB' million)	Gross profit margin (%)	Changes in income from principal operations over previous year (%)	Changes in costs of principal operations over previous year (%)	Increase /decrease of gross profit margin over previous year (%)
Grade 42.5 cement	1,262.24	798.18	36.76	46.55	52.39	-6.19
Grade 32.5 cement	1,384.33	941.21	32.01	46.26	49.81	-4.79
Clinker	353.21	221.78	37.21	40.99	48.22	-7.61

Costs analysis

	2002 RMB/tonne	2001 RMB/tonne	**Changes**
Raw materials	**34.01**	47.78	-13.77
Energy and power	**64.11**	54.76	9.35
Labour costs	**2.88**	2.64	0.24
Manufacturing overheads	**32.60**	24.80	7.8
Combined costs	**133.60**	129.98	3.62

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Based on the cost structure, energy and power costs accounted for 48% of the total costs. Hence, price fluctuations of coal made a relatively high impact on the costs of the Company. To tackle this problem, the Group implemented a stringent cost control system and strengthened its management and checks on materials consumption, in particular, energy consumption to minimise the effects of price increase of coal on costs.

Expenses analysis

Changes in major expenses items (prepared in accordance with the PRC Accounting Standards)

Expenses for the period	Amount (RMB'000) 2002	2001	Percentage of operating income 2002	2001
Administrative expenses	**190,970**	137,293	**6.37%**	6.67%
Operating expenses	**216,923**	194,736	**7.23%**	9.46%
Finance expenses	**95,495**	110,912	**3.18%**	5.39%

During the reporting period, the Company tightened its budget management and put stringent control over expenses, thus resulting in a more favourable increase in gross profit over its profit from principal operations.

FINANCIAL POSITION

Assets-liabilities structure

For the reporting period, the total assets of the Group were RMB8.9 billion, while its total liabilities were RMB4.87 billion with net assets of RMB3.22 billion (as calculated in accordance with the PRC Accounting Standards).

Changes in assets and liabilities items (prepared in accordance with the PRC Accounting Standards)

	2002 RMB'000	2001 RMB'000	Changes RMB'000	Percentage (%)
Fixed assets	**6,939,550**	4,383,054	2,556,496	58.33
Current and other assets	**1,960,074**	1,684,967	275,107	16.33
Total assets	**8,899,624**	6,068,021	2,831,603	46.66
Current liabilities	**3,548,876**	1,929,781	1,619,095	83.90
Non-current liabilities	**1,323,979**	1,108,002	215,997	19.49
Minority interests	**806,103**	819,714	(13,611)	(1.66)
Shareholders' equity	**3,220,666**	2,210,524	1,010,142	45.70
Total liabilities and equity	**8,899,624**	6,068,021	2,831,603	46.66

The gearing ratio calculated in accordance with the PRC Accounting Standards increased by 4.7 percentage points from 2001 to 54.75%, while the gearing ratio increased by 3.78 percentage points from last year to 54.77% as calculated in accordance with the IFRS. The primary reason for the increase of liabilities is the rapid growth of the Group which led to further increases in the scale of credit facilities. However, no operating risks is expected since the short-term repayment ability of the Group has improved under its sound cash flows and the proceeds from the successful public listing of its 200 million A shares.

Liquidity and source of funds

As at 31 December 2002, in accordance with the PRC Accounting Standards, the Group's total current assets amounted to RMB1,423.25 million while its current liabilities totalled RMB3,548.88 million. The current ratio, based on current assets over current liabilities was 0.40:1.

As at 31 December 2002, in accordance with the IFRS, the Group's total current assets amounted to RMB1,423.35 million while its current liabilities totalled RMB3,446.83 million. The net current liabilities were RMB2,023.48 million.

Maturity analysis of bank loans of the Group as at 31 December 2002 is as follows:

	As at 31 December 2002 RMB'000	As at 31 December 2001 RMB'000
— not exceeding one year	**2,360,064**	1,318,746
— more than one year but not exceeding two years	**294,162**	590,074
— more than two years but not exceeding five years	**865,410**	474,232
— more than five years	**80,000**	33,706
Total	**3,599,636**	2,416,758

As at 31 December 2002, the Group's loans in foreign currency amounted to approximately US$27.6182 million (equivalent to approximately RMB228.67 million), of which loans with maturity not exceeding one year were US$13.6182 million. The Group will pay close attention to changes in the foreign currency market to monitor its foreign exchange risks in a prudent manner.

As at 31 December 2002, the short-term borrowings were guaranteed by the machinery and equipment of the Group with a net book value of approximately RMB108.809 million (2001: RMB118.081 million).

Capital commitments for acquisition of machinery and equipment for the purpose of production, but not provided for in the accounts as at 31 December 2002 were as follows:

	31 December 2002 RMB'000	31 December 2001 RMB'000
Authorised and contracted for	**680,397**	591,838
Authorised but not contracted for	**1,178,815**	402,184
	1,859,212	994,022

The Group currently has sufficient liquidity resources on hand. As at 31 December 2002, cash on hand and bank deposits (as calculated in accordance with the PRC Accounting Standards) amounted to RMB809.73 million, which is sufficient for the Group to meet its normal business commitments and loan repayments. At the same time, the Group will continue to pursue its prudent policy in financial management and will maintain a cash-on-delivery sales policy in order to strive for a 100% collection of its sales proceeds.

The increase of net cash flows of the Group for 2002 of RMB191.01 million (as calculated in accordance with the PRC Accounting Standards) is summarised below:

	2002 RMB'000	2001 RMB'000
Net cash flows from operating activities	**908,137**	735,980
Net cash flows from investment activities	**(2,144,530)**	(899,465)
Net cash flows from financing activities	**1,427,403**	421,770
Net increase in cash and cash equivalents	**191,010**	258,285
Cash and cash equivalents at the beginning of the year	**608,437**	350,152
Cash and cash equivalents at the end of the year	**799,447**	608,437

In 2002, the Group continued to focus on minimising capital risks and improving operational efficiency. Coupled with the adoption of a stringent settlement policy for sales, the Group attained a steady source of cash inflows from its operating activities. For the reporting period, net cash flows from operating activities amounted to RMB908.137 million, representing an increase of RMB172.157 million over last year.

Capital expenditure

During the reporting period, the aggregate of investment activities and capital expenditure of the Group amounted to RMB2,154.46 million, of which approximately RMB27.66 million was attributable to investment activities in acquiring subsidiaries. Capital expenditure for the acquisition of buildings, plant and equipment amounted to approximately RMB2,126.8 million.

As at 31 December 2002, the Group's investment in associated companies amounted to RMB47.42 million.

It is estimated that the capital expenditure for 2003 will be approximately RMB2.7 billion, which is expected to be applied mostly for expanding the clinker and cement grinding production capacity of the Group.

PROSPECTS FOR 2003

2003 is the first year for the State to fully embark upon establishing an affluent community. The launch of large-scale industrial and urban construction projects will bring an upsurge in demand for infrastructure materials, which will expedite the structural realignment process of the cement industry and offer opportunities for the Group's business development.

In 2003, the Company will continue to proceed with the projects of construction of the clinker and grinding production lines, improve the flows of construction control of the projects with the aims at enhancing the pace and ensuring the quality of construction as well as lowering the construction costs of the projects. In addition to the construction of the large-scale clinker production lines with daily production capacity over 10,000 tonnes of Chizhou Hailuo, Zongyang Hailuo and Tongling Hailuo, the Company will also complete the construction of the clinker production lines with an annual production capacity of 1.5 million tonnes each of Digang Hailuo and Jiande Hailuo and the clinker production line with an annual production capacity of 750,000 tonnes of Fenyi Hailuo.

To cope with its continuous expansion in size, the Company will respond to the upcoming new situations ahead positively. By focusing on the standardisation of workflows and the synergy amongst businesses, the Company strives to strengthen its foundation management and various professional management in order to fully capitalise on its cost advantages in terms of economies of scale and improve its operating quality and efficiency.

Meanwhile, the Company intends to accelerate the pace of recruiting additional staff and offering more training programs so as to meet the demand for talents resulting from the rapid development. Through such measures, the Company will be able to enhance the quality of its employees to support its sustainable development.

In addition, the Company will in particular focus on the comprehensive and effective utilisation of resources as well as environmental protection along with its accelerated business development. The Company will be able to maintain the sustained, healthy and rapid growth of the enterprise by enhancing the corporate culture and fostering the cohesion of its unity.