

The following discussion and analysis should be read in conjunction with the audited financial statements of the Company for 2001 and 2002 and the notes thereto included elsewhere in this report. Such financial statements have been prepared in accordance with IFRS and include the effects of the Railway Assets, which were acquired at the beginning of 2002. For a discussion of certain differences between IFRS and US Generally Accepted Accounting Principles ("US GAAP"), please refer to note 44 to the financial statements contained herein or the Company's annual report on Form 20-F filed with the Securities and Exchange Commission of United States of America, which will be provided to any shareholder upon written request.

## YEAR ENDED 31ST DECEMBER, 2002 COMPARED WITH YEAR ENDED 31ST DECEMBER, 2001

Net sales increased by RMB1,480.4 million, or 30.4%, to RMB6,356.4 million in 2002 from RMB4,876 million in 2001. The net sales of coal was increased by RMB1,337.9 million, or 27.4% to RMB6,213.9 million in 2002 from RMB4,876 million in 2001. Net income of the railway transportation service was RMB142.5 million.

After excluding the impact of the acquisition of the Railway Assets, the Company realized net sales of coal of RMB5,966.2 million, representing an increase of RMB1,090.2 million, or 22.4%, from RMB4,876 million in 2001. Such increase was principally due to: sales volume of coal was increased by 12.9%, resulting in an increase in net sales of coal by RMB630.4 million; average coal price was increased by 8.4%, resulting in an increase in net sales of coal by RMB459.8 million.

Cost of goods sold and service increased by RMB550.3 million, or 19.6%, to RMB3,362.9 million in 2002 from RMB2,812.6 million of 2001, of which the cost of coal sales was 3,309.9 million, the cost of services provided by the Railway Assets was RMB52.99 million.

After eliminating the effects of the acquisition of the Railway Assets, cost of coal sold increased by RMB497.3 million, or 17.7% to RMB3,309.9 million in 2002 from RMB2,812.6 million in 2001. This was mainly due to the increase in raw coal output, the increased proportion of washed clean coal and the increase in wages. The unit cost of coal sold was RMB94.5, representing an increase of RMB3.9, or 4.3%, compared with RMB90.6 of last year. The main reasons for the variation in the unit cost of coal sold are as follows: i) the adjustment in product structure by increasing the proportion of washed clean coal in sales volume which led to an increase of unit cost of coal sold by around RMB3.3; ii) wages and employee benefits increased following the increase of productivity which resulted in an increase of unit cost by RMB2.9; iii) as the government increased the management and supervision of coal mine production safety, the Company invested approximately RMB40 million to improve production safety, which resulted in an increase in unit cost by around RMB1.1/tonne; iv) raw coal output volume of Jining III coal mine increased by 2.92 million tonnes, which resulted in a decrease of unit cost of coal sold by around RMB0.96/tonne; v) the Company has successfully controlled the cost of production by applying advanced technology and equipment and transforming roof support system and auxiliary transport system to improve productivity. The coal out had increased at same time. As a result, the unit cost reduced by RMB2.4/tonne, partially offsetting effect to the Company by the increase in production cost as mentioned above.

Sales, general and administration expenses was RMB1,231.1 million in 2002, increased by RMB471.5 million, or 62.1%, from RMB759.6 million compared with the same period of last year, among which sales, general and administration expenses of the Railway Assets were RMB65.686 million.

After deducting the acquisition of the Railway Assets, sales, general and administrative expenses of the Company were RMB1,165.4 million, representing an increase of RMB405.8 million or 53.4% as compared with the same period in the previous year. The main reasons were as follows: 1. an increase in pension fund by RMB68.295 million; 2. an increase in wages of the management and employee benefits by RMB88.832 million; 3. an increase in wages surcharge by RMB40.672 million due to the introduction of supplementary medical insurance fund and

an increase in wages; 4. increase in provision for bad debt by RMB63.696 million; 5. increase in mineral resources compensation by RMB42.522 million; In addition, the increase in output and sales volume of the Company also led to an increase in sales, general and administrative expenses.

Other operating income reduced by RMB14.167 million, or 12.0%, to RMB103.7 million in 2002 from RMB117.9 million in 2001.

Operating income increased by RMB444.4 million, or 31.3%, to RMB1,866.1 million in 2002 from RMB1,421.7 million in 2001. This was principally due to the increase of net sales.

Interest expenses increased by RMB56.410 million, or 91.7%, to RMB117.9 million in 2002 from RMB61.519 million in 2001. This was principally due to the increase in interest expenses of long-term loan for the acquisition of the Railway Assets.

Before deduction of income taxes, income increased by RMB388 million, or 28.5%, to RMB1,748.2 million in 2002 from RMB1,360.2 million in 2001.

Net income increased by RMB251.1 million, or 25.9%, to RMB1,222 million in 2002 from RMB970.9 million in 2001.

Total assets increased by RMB1,741.4 million, or 15.6%, to RMB12,924 million as at 31st December, 2002 from RMB11,182.6 million as at 31st December, 2001. This was principally due to the acquisition of the Railway Assets and the increase in assets from the Company's production and operation activities.

Total liabilities increased by RMB804 million, or 37.9%, from RMB2,120.1 million as at 31st December, 2001 to RMB2,924.1 million as at 31st December, 2002. This was principally due to the increase in long-term loan for the payment for the acquisition of the Railway Assets.

Shareholders' equity increased by RMB935.0 million, or 10.3%, from RMB9,060.0 million as at 31st December, 2001 to RMB9,995.0 million as at 31st December, 2002. This was principally attributed to the increase in profits arising from the Company's production and operation activities.

## LIQUIDITY AND CAPITAL RESOURCES

In 2002, the Company's principal sources of capital were cash flow from operations and loan from the bank. The Company's principal uses of the capital include payment for operating expenses, the acquisition of Jining III coal mine and the Railway Assets and the purchase of property, plants, equipment and payment of shareholders' dividend.

As at 31st December, 2001, the balance of the Company's accounts receivable and notes receivable was RMB802.9 million, an increase of RMB108.6 million, or 15.6% from RMB694.3 million as at 31st December, 2001. That is principally due to the substantial increase of coal sales volume.

Inventories increased by RMB136.7 million, or 31.1%, to RMB576.6 million as at 31st December, 2002 from RMB439.9 million as at 31st December, 2001. This was principally due to: (i) increases in total production and varieties of coal products, resulting in higher volume of total coal stocks; (ii) the Company increased sales volume transported through the canals, resulting in higher volume of coal in transit.

Prepayment and other current assets reduced by RMB97.2 million or 11.4% to RMB756 million as at 31st December, 2002, from RMB853.2 million as at 31st December, 2001. This was principally due to the decrease in VAT export rebate receivable and provision for land subsidence costs.

Accounts payable and notes payable decreased by RMB33.7 million, or 5.3%, to RMB602.7 million as at 31st December, 2002 from RMB636.4 million as at 31st December, 2001.

Other accounts payable and provisions increased by RMB101.9 million, or 19.1%, to RMB634.8 million as at 31st December, 2002 from RMB532.9 million as at 31st December, 2001, principally due to the increase in provisions, other taxes payable, and employee benefits payable.

Long-term liabilities increased to RMB1,261.3 million as at 31st December 2002 from RMB72.456 million as at 31st December, 2001. This was principally due to the increase in long-term bank loan for the payment of the acquisition of the Railway Assets.

The Company's capital expenditure for the purchase of property, machinery and equipment was RMB728.6 million and 831.8 million in 2001 and 2002, respectively.

As at 31st December, 2002, the consideration for the acquisition of Jining III coal mine of RMB2,450.9 million has been settled by the Company with cash in hand of RMB996.1 million and the net proceeds raised from the new issue of A shares and H shares. The consideration for mining right of RMB132.479 million will be paid in ten equal installments without interest each year commencing from 2001. The Company has paid RMB26.496 million for the mining right at the end of this report period.

The Company completed the acquisition of the Railway Assets on 1st January, 2002. The purchase consideration of RMB1,243 million has been settled by the Company at the end of this report period. In accordance with the Railway Assets Acquisition Agreement, when the annual transportation volume of the Railway Assets reaches the volume milestones targets of 25 million tonnes, 28 million tonnes and 30 millions tonnes for the year 2002, 2003 and 2004, respectively, the Company will pay the Parent Company an amount of RMB40 million before 30th June of each year in the three years from 2003. The transportation volume of the Railway Assets in 2002 was 27.04 million and the Company has paid RMB40 million in accordance with the terms stated above.

As at 31st December, 2002, the Company's debt to equity ratio was 12.0%, which was calculated based on the total shareholder's equity and amount of long term bank loan amounting to RMB9,995 million and RMB1,200 million, respectively.

Since 2002, the Company resumed transfers to future development fund, the details of which are provided in the section headed "Consolidated Statement of Changes in shareholders' Equity" of the financial statements prepared under IFRS.

The Company's Board of Directors had recommended a final dividend of RMB298.48 million to be paid out of the Company's cash revenue from operations.

Taking into account the cash in hand and existing abundant capital sources, the Company believes that it will have sufficient capital for its operational requirements.

## TAXATION

The Company is still subject to an income tax rate of 33% on its taxable profits in 2002.

## US GAAP RECONCILIATION

The Company's audited financial statements are prepared in compliance with IFRS, which differs in certain respects from US GAAP. Please refer to note 44 to the financial statements contained herein for a description of the differences between IFRS and US GAAP, and the adjusted net income for the year ended 31st December, 2002 and the shareholders' equity as at 31st December, 2002 after reconciliation made in accordance with US GAAP.