

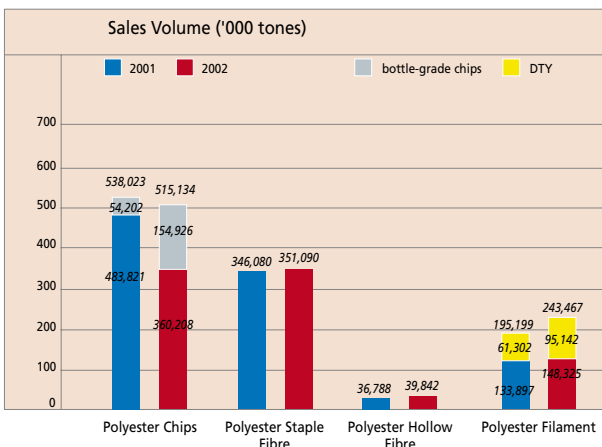
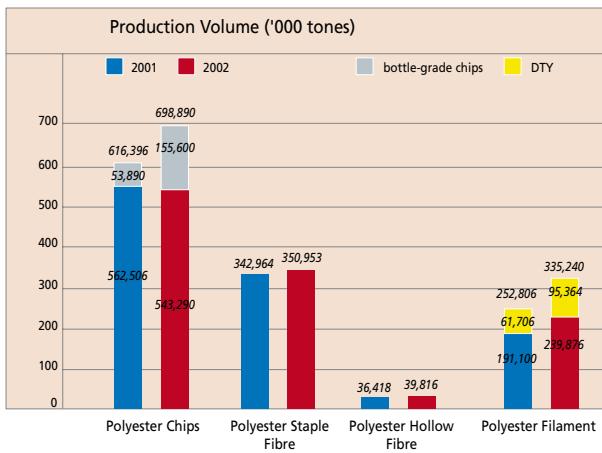


Xu Zheng-ning, Managing Director

The information set out below does not constitute part of the financial statements audited by KPMG or KPMG Huazhen, as set out on pages 56 to 89 and pages 90 to 126, respectively, of this annual report, and is included for information purpose. This discussion and analysis should be read in conjunction with the information contained in the Consolidated Financial Statements and Notes thereto (the "Financial Statements") presented in this annual report. Financial figures, where applicable, except for specifically noted, contained herein have been extracted from the financial statements prepared in accordance with IFRS.

1. Results of Operations

In 2002, under fierce market competition, the Group took great efforts to increase production volume and sales volume, enhance its product structure, further reduce costs and expenses, and try the best to increase operating result.



(1) Turnover

In 2002, the Group's total production volume of polyester products increased to 1,424,899 tonnes, representing an increase of 14.1 per cent as compared with 1,248,584 tonnes for last year. Of which, the total production volumes of bottle-grade polyester chips, polyester filament and DTY increased by 188.7 per cent, 32.6 per cent and 54.5 per cent respectively. Increase was mainly due to the commencement of operation of its structural improvement and expansion projects since September 2001, such as the direct-melt-spinning polyester filament project with an annual capacity of 75,000 tonnes, the SSP project with an annual capacity of 100,000 tonnes, the DTY project with an annual capacity of 50,000 tonnes, and extension of the processing chain. The average capacity utilisation rate reached 101.5 per cent whereas that of last year was 101.1 per cent. The total production volume of PTA amounted to 342,474 tonnes, an increase of 5.0 per cent as compared with 326,072 tonnes of last year.


Production volume

	For the year ended 31 December			
	2002	Percentage of total production volume (%)	2001	Percentage of total production volume (%)
	Production volume (tonnes)		Production volume (tonnes)	
Polyester products				
Polyester chips	698,890	49.0	616,396	49.4
Of which: bottle-grade polyester chips	155,600	10.9	53,890	4.3
Polyester staple fibre	350,953	24.6	342,964	27.5
Polyester hollow fibre	39,816	2.8	36,418	2.9
Polyester filament	335,239	23.6	252,806	20.2
Of which: DTY	95,364	6.7	61,706	4.9
Total	<u>1,424,898</u>	<u>100.0</u>	<u>1,248,584</u>	<u>100.0</u>

In 2002, due to the increase in production volume and the sales promotion efforts, the Group's total sales volume of the polyester products amounted to 1,149,533 tonnes, representing an increase of 3.0 per cent as compared with 1,116,090 tonnes of 2001. Of which, the total sales volumes of bottle-grade polyester chips, polyester filament and DTY increased by 185.8 per cent, 24.7 per cent and 55.2 per cent respectively. Export sales achieved a new edge with total export products amounting to 35,625 tonnes. The difference between the sales growth rate and the production growth rate reflected the Group's extension of product processing chain and increase in the production of high value-added products. The ratio of sales to production reached 100.2 per cent (2001: 100.9 per cent). Due to the recognition of high quality and excellent sales services, the selling prices of the Group's products remained high in the domestic market during the year. During the most sluggish period for the polyester industry in January and February 2002, the product prices fell to historical low. From March 2002 onwards, although the prices rebounded owing to the substantial increases in the prices of upstream polyester raw materials, the weighted average prices (excluding VAT) of the Group's polyester products decreased from Rmb6,919/tonne to Rmb6,882/tonne, representing 0.5 per cent decrease.

Sales volume

	For the year ended 31 December			
	2002	Percentage of total sales volume (%)	2001	Percentage of total sales volume (%)
	Sales volume (tonnes)		Sales volume (tonnes)	
Polyester products				
Polyester chips	515,134	44.8	538,023	48.2
Of which: bottle-grade polyester chips	154,926	13.5	54,202	4.9
Polyester staple fibre	351,090	30.5	346,080	31.0
Polyester hollow fibre	39,842	3.5	36,788	3.3
Polyester filament	243,467	21.2	195,199	17.5
Of which: DTY	95,142	8.3	61,302	5.5
Total	<u>1,149,533</u>	<u>100.0</u>	<u>1,116,090</u>	<u>100</u>

**Average prices for products (excluding VAT) (Rmb/tonne)**

	For the year ended 31 December		
	2002	2001	Change increase/ (decrease) (%)
Polyester products			
Polyester chips	6,036	5,994	0.7
Polyester staple fibre	6,938	7,356	(5.7)
Polyester hollow fibre	7,556	8,745	(13.6)
Polyester filament	8,479	8,350	1.5
Weighted average price	6,882	6,919	(0.5)

Turnover

	For the year ended 31 December			
	2002		2001	
	Turnover	Percentage	Turnover	Percentage
	Rmb'million	of turnover	Rmb'million	of turnover
		(%)		(%)
Polyester products				
Polyester chips	3,109	38.8	3,225	41.3
Polyester staple fibre	2,436	30.4	2,545	32.6
Polyester hollow fibre	301	3.8	322	4.1
Polyester filament	2,065	25.8	1,630	20.9
Others	99	1.2	87	1.1
Total	8,010	100.0	7,809	100.0

In 2002, the Group's turnover amounted to Rmb8,010 million, representing an increase of 2.6 per cent as compared with Rmb7,809 million for last year. The increase was mainly due to the combined efforts of the increase in sales volume, the change in sales mix and the decrease in the product prices.

The Group continued to hold a leading market share in the PRC.

(2) Cost of sales

In 2002, the Group's cost of sales amounted to Rmb7,305 million, representing 91.2 per cent of the turnover, which increased by 0.4 percentage as compared with last year. The increase was mainly due to the increased production volume which led to the increase in raw materials procurement, and the increase in the price of principal polyester raw materials, PTA. Total costs of raw materials increased by Rmb205 million from Rmb5,431 million in 2001 to Rmb5,636 million in 2002, which accounted for 77.2 per cent of cost of sales in 2002. The increase was mainly due to the increase in raw materials procurement. The Group's weighted average purchase price of polyester raw materials remained unchanged as compared with last year. The average purchase cost of PTA increased by 7 per cent as compared with last year, while the average purchase costs of MEG and PX decreased by 6 per cent and 10 per cent respectively as compared with last year. The Group produced PTA for its own use, which partly offset the impact on the Group as a result of the increase in PTA prices. In addition, the Group purchased large quantities of raw materials at the market low, which helped the Group in achieving substantial savings in purchasing costs.

In 2002, since the ratio of cost of sales to turnover increased, the Group's gross profit decreased by Rmb14 million as compared with last year. The Group's gross margin was 8.8 per cent (2001: 9.2 per cent).

**(3) Selling, administrative and financial expenses**

	For the year ended 31 December		
	2002	2001	Change increase/ (decrease)
	Rmb'000	Rmb'000	(%)
Selling expenses	167,646	138,933	20.7
Administrative expenses	345,309	265,510	30.1
Financial expenses	34,360	28,824	19.2
Total	<u>547,315</u>	<u>433,267</u>	<u>26.3</u>

In 2002, selling expenses increased by Rmb29 million, mainly due to the increase in transportation costs as a result of increased sales and the reform of remuneration system of sales staff. Administrative expenses increased by Rmb80 million, mainly due to the increase in R&D expenses. Financial expenses increased by Rmb6 million, mainly due to the change in borrowings structure as a result of the increase in capital expenditure and the commencement of the operation of new construction projects. The total of these three types of expenses increased by 26.3 per cent as compared with last year.

(4) Profit from operations, profit from ordinary activities before taxation, profit attributable to shareholders

	For the year ended 31 December		
	2002	2001	Change increase/ (decrease)
	Rmb'000	Rmb'000	(%)
Profit from operations	191,105	242,199	(21.1)
Profit from ordinary activities before taxation	156,745	213,375	(26.5)
Income tax expense	7,156	40,087	(82.1)
Profit attributable to shareholders	144,321	170,789	(15.5)
Earnings per share (in Rmb)	<u>0.036</u>	<u>0.043</u>	<u>(15.5)</u>

In 2002, the Group's profit from operations and profit from ordinary activities before taxation amounted to Rmb191 million and Rmb157 million, decreased by 21.1 per cent and 26.5 per cent respectively as compared with Rmb242 million and Rmb213 million in 2001. It was mainly due to the decrease in selling prices of the polyester products as compared with last year. Profit attributable to shareholders was Rmb144 million, a decrease of 15.5 per cent as compared with Rmb171 million in 2001, mainly due to the increase in selling expenses, financial expenses and administrative expenses. The Group's operating profit margin and net profit margin reached 2.4 per cent and 1.8 per cent respectively.

**(5) Statement of the principal operations by products**

Polyester products contributed more than 10 per cent of the Group's income from principal operations and profit from principal operations. The following is the statement of principal operations by products for the year ended 31 December 2002 in accordance with the PRC Accounting Rules and Regulations:

Products	Income from principal operations <i>Rmb'000</i>	Cost of principal operations <i>Rmb'000</i>	Gross profit margin (%)	Increase/ (decrease) in income from principal operations as compared to last year (%)	Increase/ (decrease) in cost of principal operations as compared to last year (%)	Gross margin ratio as compared to last year
Polyester products	7,910,769	7,169,685	9.4	2.4	2.5	Decrease by 0.1 point
Of which: connected transactions	727,607	665,033	8.6	(17.5)	(17.2)	Decrease by 0.3 point

(6) Operations of principal subsidiaries in 2002

1. Foshan Group. The Company directly holds 100 per cent of the equity interest of Foshan Chemical. Foshan Chemical's registered capital is Rmb32,933,000. Its principal activity is the provision of management and administration services. The Company directly holds 59 per cent and indirectly holds 41 per cent of the equity interest of Foshan Polyester. Foshan Polyester's registered capital is US\$85,427,000. Its principal activities are the production and sales of chemical, chemical fibre, textile and its ancillary raw materials, and after sales services for its products. As at 31 December 2002, the total assets of Foshan Group was Rmb907,017,000. For the year ended 31 December 2002, Foshan Group made a net profit of Rmb12,587,000 million.
2. Kangqi Group. The Company directly holds 95 per cent and indirectly holds 5 per cent of the equity interest of Kangqi Company. Kangqi Company's registered capital is Rmb60,000,000. Its principal activities are production and operation of polyester fibre business. Kangqi Company, through its 13 subsidiaries in major domestic markets, has established a sales network in the PRC. As at 31 December 2002, the total assets of Kangqi Group was Rmb353,093,000. For the year ended 31 December 2002, Kangqi Group made a net profit of Rmb11,383,000.

(7) Acquisition, divestment and investment

The Group did not make any material acquisition, divestment or investment in relation to any of its subsidiaries or associates in 2002.



2. Liquidity

As at 31 December 2002, the Group's cash and cash equivalents amounted to Rmb491 million, representing an increase of Rmb46 million as compared with Rmb445 million as at 31 December 2001. The increase was mainly due to the decrease in the Group's operating cashflow.

In 2002, the Group's net cash inflow from operating activities was Rmb1,386 million, as compared with that of Rmb668 million in 2001. The increase was attributable to the increase in both production and sales volume, leading to a faster loan repayment for the Group, as well as the favourable payment method obtained. As at 31 December 2002, inventories increased by Rmb189 million, and trade and other receivables increased by Rmb55 million. In 2001, there were a decrease of Rmb119 million and Rmb51 million respectively for inventories and trade and other receivables. Increase in inventories was mainly caused by the purchases of cheap raw materials at the end of the year, and increase in trade and other receivables was mainly due to the increase in bills receivable in transit.

In 2002, the Group's net cash outflow from investing activities was Rmb1,415 million, as compared with that of Rmb809 million for last year. The increase was mainly due to the increase in capital expenditure from Rmb1,424 million in 2001 to Rmb1,531 million during the year.

In 2002, the Group's net cash inflow from financing activities was Rmb74 million, as compared with net cash outflow of Rmb15 million in 2001. The change was mainly due to the appropriate increase in bank loans and the decrease in dividend payment.

As at 31 December 2002, the Group's bank loans amounted to Rmb1,386 million, as compared with Rmb1,230 million at the end of 2001. The increase was due to the appropriate increase in short-term loans. Among those bank loans, short-term loans due in 2003 amounted to Rmb686 million, and long-term loans amounted to Rmb700 million, of which Rmb150 million will be due in 2004, Rmb150 million will be due in 2005, and the remaining will be due in 2003.

As at 31 December 2002, the Group's shareholders' funds (excluding minority interests) increased by Rmb64,321,000. The change was mainly due to the profit attributable to shareholders of Rmb144,321,000 for the year and the payment of 2001's final dividend of RMB80,000,000. At 31 December 2002, the total liabilities increased by Rmb914,117,000 as a result of the increase in raw materials purchase for the production. As a result of the above combined effect, the Group's total assets increased by Rmb981,996,000, total liabilities to total assets ratio reached 26.5 per cent as compared with 20.6 per cent of last year.



3. Capital Expenditure

In 2002, the Company's capital expenditure amounted to Rmb1,531 million. The following table provided information on the Group's major construction projects and their profitabilities in 2002:

Main projects	Amount invested in 2002 <i>Rmb'000</i>	Project Status <i>Rmb'000</i>	Information on the profitability of the main projects (Actual sales amount) <i>Rmb'000</i>
SSP project with an annual capacity of 100,000 tonnes	27,900	Completed	541,500
DTY improvement project with an annual capacity of 50,000 tonnes	62,300	Completed	282,410
Multi-functional fibre project with an annual capacity of 7,500 tonnes	16,580	Completed	40,870
Sea island filament yarn project with an annual capacity of 750 tonnes	15,680	Completed	410
PTA project with an annual capacity of 450,000 tonnes	1,021,000	Under construction	–
Staple fibre project with an annual capacity of 90,000 tonnes	65,000	Under construction	–
Specialised polyester chip project with a daily capacity of 450 tonnes	9,700	Under construction	–
Improvement project of No. 5K production line	1,200	Under construction	–
Others	<u>311,805</u>	–	<u>–</u>
Total	<u><u>1,531,165</u></u>		<u><u>865,190</u></u>

The Company's capital expenditure for the year 2003 is expected to be approximately Rmb1,000 million, including: PTA project with an annual capacity of 450,000 tonnes, staple fibre project with an annual capacity of 90,000 tonnes, differential polyester chip with a daily capacity of 450 tonnes and improvement project of No. 5K production line amounting to Rmb200 million, Rmb220 million, Rmb147 million and Rmb12 million respectively. The planned capital expenditures will be funded from cash generated from operations and banking facilities.