

REPORT OF THE BOARD OF DIRECTORS

The following discussion and analysis should be read in conjunction with the Group's unaudited financial statements and the accompanying notes. The financial information presented in this section is derived from the Group's unaudited financial statements that have been prepared in accordance with International Financial Reporting Standards ("IFRS").

To All Shareholders

We hereby report the operating results of the Group for the six-month period ended 30 June 2003 ("reporting period"). For the six-month period ended 30 June 2003, the Group's turnover from principal operations amounted to RMB14,139.1 million (HK\$13,319.9 million), an increase of RMB4,616.1 million (HK\$4,348.7 million) or 48.47% as compared to the same period last year. Profit before tax amounted to RMB598.1 million (HK\$563.4 million), representing an increase of 118.52% as compared to the same period last year. Profit after tax and minority interests amounted to RMB484.1 million (HK\$456.1 million), an increase of 132.07% as compared to the same period last year.

Management Discussion and Analysis

The first half of 2003 witnessed significant fluctuations and sluggish recovery of the world economy amidst the advent of the Iraq War, appreciation of the Euro, depreciation of the US Dollar and the outbreak of the Severe Acute Respiratory Syndrome ("SARS"). During the first quarter of the year, the PRC economy recorded rapid growth, which slowed down in the second quarter with the outbreak of SARS but sustained an overall robust growth trend. The People's Republic of China ("PRC") economy demonstrated a notable rebound in June as SARS was brought under control. All these factors resulted in fluctuations of the prices of petrochemical products, featuring an overall rise, fall and subsequent rebound which pushed price levels higher than that of the first half of last year. The petrochemical industry performed better than the same period last year.

Operating Results

During the first half of 2003, the market prices of the four major products of the Group rose, fell and then rebounded. Compared to the same period last year, the selling prices of the major products of the Group, namely synthetic fibres, resins and plastics, intermediate petrochemical products and petroleum products, have all increased, but by different degrees. On the other hand, the price of crude oil, the major raw material of the Group, experienced severe fluctuations under the influence of the Iraq War and generally stood at a high level on average since the beginning of the year. The weighted average cost of crude oil was RMB 1,881.47 per ton, representing an increase of RMB 496.32 per ton or 35.83% as compared to the same period last year.

Confronted with a complex external environment, the Group implemented effective marketing strategies, further enhanced the operation of production plants and equipment and the raw material levels, rationalized the maintenance programs of production equipments and planned production to match market demand closely while exercising stringent cost controls. As a result, the Group's overall performance has been enhanced.

During first half of 2003, the Company's processed crude oil and product output recorded substantial increases. This was attributed to the completion of the "Phase IV" project and other newly constructed and renovated facilities. The Group processed 4.1233 million tons of crude oil, an increase of 726,900 tons or 21.4% as compared to the same period last year, including 715,300 tons Shengli oil, 3,045,300 tons imported oil and 362,700 tons offshore oil. During the first half of 2003, the output of ethylene was 461,500 tons, an increase of 35.74%; output of propylene was 251,700 tons, an increase of 39.37%; output of plastics and resins was 519,800 tons, an increase of 49.05%; output of polymers was 248,400 tons, an increase of 6.15%; output of synthetic fibres was 181,800 tons, an increase of 6.69% as compared to the same period of last year. While increasing output, the Group implemented timely adjustments to its marketing strategies in a bid to expand the sales of its products. The sales to output ratio during the six-month period ended 30 June 2003 reached 99.56%.

The following table indicates the Group's sales volume and net sales (net of business taxes and surcharges) during the six-month period ended 30 June 2003:

	Six-month periods ended 30 June					
	2003			2002		
	Sales volume '000 tons	RMB million	%	Sales volume '000 tons	RMB million	%
Synthetic fibres	192	1,897	13.68	187	1,638	17.71
Resins and plastics	671	4,140	29.86	487	2,681	28.99
Intermediate petrochemical products	505	1,940	13.99	413	1,156	12.50
Petroleum products	2,184	5,016	36.18	1,871	3,247	35.11
All others	-	872	6.29	-	526	5.69
Total	3,552	13,865	100.00	2,958	9,248	100.00

During the first half of 2003, net sales of the Group amounted to RMB13.865 billion, representing an increase of 49.92% as compared to the same period last year. Net sales of synthetic fibres, resins and plastics, intermediate petrochemical products and petroleum products during the six-month period ended 30 June 2003 recorded an increase of 15.81%, 54.42%, 67.82% and 54.48%, respectively, as compared to the same period last year. The increase was mainly attributable to the fact that, in line with the general increase in the average selling prices of the products as compared to the same period last year, there has been a considerable growth in the sales volume of the products with the on-going completion and commencement of operations of the "Phase IV" project in June 2002. During the reporting period, the average selling price (excluding tax) for synthetic fibres, resins and plastics, intermediate petrochemical products and petroleum products of the Group increased by 12.80%, 12.08%, 37.25% and 32.34%, respectively as compared to the first half of 2002, while sales volume increased by 2.67%, 37.78%, 22.28% and 16.73%, respectively.

Most of the products manufactured by the Group were sold in Eastern China.

The Group's cost of sales increased by 48.88% to RMB12,850.4 million representing 92.68% of net sales during the first half of 2003. With increases in the average cost of crude oil purchased and volume of processing crude oil of the Group, total crude oil costs increased by 64.02% to RMB7,716.0 million during the six-month period ended 30 June 2003 as compared to the same period last year.

Crude oil costs of the Group accounted for 60.01% of the cost of sales in the first half of 2003 (first half of 2002: 54.50%).

Expenses for other ancillary materials significantly increased to RMB1,918.8 million during the first half of 2003, as compared to the same period last year, which was primarily attributed to the upsurge in the sales volume of the products. With the completion and commissioning of the “Phase IV” project, depreciation expenses of the Group amounted to RMB904.7 million for the reporting period, representing an increase of RMB 179.4 million as compared to the same period last year. Maintenance costs were RMB351.9 million for the reporting period. In addition, given the increased demand for electricity and steam to service new equipment installed, fuel and power expenses of the Group went up from RMB 295 million for the first half of 2002 to RMB357.1 million for the first half of 2003.

Selling and administrative expenses increased to RMB228.6 million during the first half of 2003 from RMB200.4 million in the same period last year, mainly attributable to the substantial growth in products sales volume.

Net financing costs during the first half of 2003 rose 16.25% to RMB201.6 million as compared to the same period last year, which was mainly attributed to the completion of the “Phase IV” project, which marked the cessation of the capitalisation of borrowing costs for the projects and increased the financing costs expensed for the current reporting period.

Profit after tax of the Group for the first half of 2003 amounted to RMB484.1 million, representing an increase of 132.04% as compared to RMB208.6 million in the same period last year.

Liquidity and Capital Resources

During the first half of 2003, net cash inflow from the Group's operating activities amounted to RMB1,286.1 million, an increase of RMB486.8 million as compared to the same period last year. Profit before tax and depreciation contributed an operating cash inflow of RMB1,502.8 million to the Group (an increase of RMB503.8million of cash inflow as compared to the same period last year). An increase in inventory as at the end of the reporting period contributed to an increase in cash outflow of RMB45.9 million (as compared to an increase in cash outflow of RMB 358.7 million in the same period last year due to an increase in inventory as at the end of that period). Change in the balance of trade creditors, other creditors and bills payable accounted for RMB101.1 million in the increase of cash outflow (as compared to a decrease in cash inflow of RMB235.5 million in the same period last year). Increase in the balance of debtors, bill receivables and deposits accounted for RMB22.0 million in the decrease of cash inflow (compared to a decrease in the cash inflow by RMB142.2 million as a result of the increase of such balance at the end of the same period last year).

Borrowings

The Group's long-term loans were mainly used for capital expenditure projects. The Group usually arranged its long-term loans according to its capital expenditure plan, and in general, there were no seasonal loans. Short-term loans were used to meet working capital requirements arising from normal production operations of the Group. The total amount of the Group's borrowings dropped by RMB132.2 million from the beginning of this year to RMB8,461.1 million as at 30 June 2003, including a RMB321.6 million increase in short-term loans and a RMB453.8 million decrease in long-term loans.

As at 30 June 2003, the Group had contingent liabilities of RMB299.7 million in respect of guarantees issued to banks in favour of its associated companies and other non-listed investment companies.

As at 30 June 2003, all short-term loans and more than 95% of long-term loans borrowings were borrowed at floating rates. Borrowings amounted to RMB2,679.4 million and RMB42.5 million were denominated in USD and Japanese yen respectively. The remaining loans were in Renminbi.

Fluctuation of exchange rates

The Company purchases the majority of its materials, including crude oil, from abroad and exports a portion of its products through Sinopec. Therefore, any fluctuation in exchange rates will have a direct impact on the prices at which the Company purchases materials and exports products, which may impact the profitability of the Company. In addition, some of the debts of the Company were denominated in foreign currencies. Changes in the exchange rates will also affect the interest payments and the Company's profitability.

Capital expenditure

During the first half of 2003, the Group's capital expenditure amounted to RMB907.9 million, which primarily comprised the 130,000-ton acrylonitrile plant renovation project, the polyester 1# resin technical renovation project and the flare gas recovery system renovation project. In addition, the Group has also planned a 12,000-ton industrial polyester filament plant expansion project and other technical renovation and investment projects in the second half of the year. The Group's planned capital expenditures can be financed by cash inflow from operating activities and bank loans available.

During the reporting period, the Group continued to carry out the Sino-foreign joint investment project with China Petroleum & Chemical Corporation ("Sinopec Corp") and BP Chemicals East China Investments Limited. As at 30 June 2003, the Group had contributed RMB356.3 million to the equity joint venture.

Debt-equity ratio

The debt-equity ratio of the Group was 22.68% for the first half of 2003 (first half of 2002: 24.46%). The ratio is computed by long-term borrowings divided by the sum of long-term borrowings and shareholders' equity.

Employees

As at 30 June 2003, the number of employees of the Company was 30,022. The staff cost for the reporting period was RMB541 million.

In compliance with paragraph 40 of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), the Company confirms that, save as disclosed herein, there has been no material change in the current information regarding the Company in relation to those matters set out in paragraph 32 of Appendix 16 to the Listing Rules from the information in relation to those matters disclosed in the Annual Report 2002 of the Company.

Segmental reporting prepared in accordance with the People's Republic of China ("PRC") Accounting Rules and Regulations

	Income from principal operations (RMB'000)	Cost of sales (RMB'000)	Gross profit margin (%)	Increase/ decrease of income from principal operations compared to last year (%)	Increase/ decrease of cost of sales compared to last year (%)	Increase/ decrease of gross profit margin compared to last year (%)
Segments						
Synthetic fibres	1,904,874	1,873,545	1.64	15.58	21.32	-4.66
Resins and plastics	4,158,411	3,734,904	10.18	54.21	60.68	-3.62
Intermediate petrochemicals	1,950,095	1,443,280	25.99	67.51	60.85	3.09
Petroleum products	5,240,592	4,587,525	12.46	50.72	53.91	-1.82
All others	885,098	754,698	14.73	64.82	138.48	-26.34
Including: connected transactions	4,872,132	4,506,941	7.50	50.69	60.87	-5.85

Price-setting principles of connected transactions The Board of Directors of the Company believes that the above transactions were entered into in the normal course of business and were conducted on normal commercial terms or in accordance with the terms of the relevant agreements. The above transactions were confirmed by the Company's non-executive Directors.

Analysis of the geographical segments for the principal operations

Region	Income from principal operations (RMB'000)
Eastern China	12,402,723
Other regions	872,067
Export	864,280

During the reporting period, there was no significant change to the geographical segments for the principal operations of the Group as compared to the same period in 2002.

Share Capital and Major Shareholders

1. Change of Share Capital

During the reporting period, there was no change to the Company's share capital structure.

2. Number of shareholders at the end of the reporting period

At 30 June 2003, the share capital of the Company totalled 7.2 billion shares, which were held by 292,035 shareholders, with 288,780 of them being holders of A shares and 3,225 of them being holders of H shares.

3. Shareholding of major shareholders

The top ten shareholders of the Company at 30 June 2003.

Name of shareholders (In full)	Increase / decrease during the period	Number of shares held at end of the period	Percentage of total shareholdings (%)	Type of shares (circulating/ non-circulating)	Number of shares pledged or frozen	Type of Shares
China Petroleum & Chemical Corporation	-	4,000,000,000	55.56	Non-circulating	-	Promotor legal person share
HKSCC Nominees Ltd. *	8,001,000	1,866,016,401	25.92	Circulating	-	H share
Hongkong & Shanghai Banking Corporation (Nominees) Limited *	148,000	354,728,000	4.93	Circulating	-	H share
Puhui Fund	Not available	20,245,493	0.28	Circulating	-	A share
Shanghai Kangli Gong Mao Company	-	16,730,000	0.23	Noncirculating	16,430,000	Legal person share
Zhejiang Province Economic Construction and Investment Company	-	12,000,000	0.17	Non-circulating	-	Legal person share
Tianhua Fund	Not available	10,443,996	0.15	Circulating	-	A share
Hongkong & Shanghai Banking Corporation (Nominees) Limited *	-	10,336,000	0.14	Circulating	-	H share
Jinxin Fund	Not available	8,975,139	0.12	Circulating	-	A share
Jintai Fund	Not available	8,624,042	0.12	Circulating	-	A share
Relationship among the top ten shareholders						-

* Nominee shareholders

Shares held by legal person shareholders holding 5% or more of the Company's shares were not pledged or frozen.

Directors', Supervisors' and Senior Management's Interests in Shares and Substantial Shareholders

1. Directors, Supervisors and Senior Management and their interests in shares

As at 30 June 2003, the interests held by Directors, Supervisors and senior management in the Company were as follows (Unit: Share):

Name	Position	Number of shares held at the beginning of the period	Number of shares held at the end of the year	Reasons for change
Lu Yiping	Chairman and President	3,600	3,600	No change
Xu Kaicheng	Vice Chairman	3,600	3,600	No change
Rong Guangdao	Director and Vice President	3,600	3,600	No change
Feng Jianping	Director and Vice President	3,600	3,600	No change
Jiang Baoxing	Director	3,600	3,600	No change
Li Weichang	Director	1,000	1,000	No change
Liu Wenlong	External Director	Nil	Nil	No change
Zhang Baojian	External Director	Nil	Nil	No change
Gu Chuanxun	Independent Director	Nil	Nil	No change
Wang Yongshou	Independent Director	3,600	3,600	No change
Wang Xingyu	Independent Director	Nil	Nil	No change
Chen Xinyuan	Independent Director	Nil	Nil	No change
Du Chongjun	Chairman of Supervisory Committee	1,000	1,000	No change
Zhang Chenghua	Supervisor	Nil	Nil	No change
Zhu Weiyan	Supervisor	Nil	Nil	No change
Zhang Jianjun	External Supervisor	Nil	Nil	No change
Lu Xiangyang	External Supervisor	Nil	Nil	No change
Zhou Yunnong	Independent Supervisor	Nil	Nil	No change
Liu Xiangdong	Independent Supervisor	Nil	Nil	No change
Zhang Zhiliang	Vice President	3,600	3,600	No change
Liu Xunfeng	Vice President	1,500	1,500	No change
Wu Haijun	Vice President	1,500	1,500	No change
Yin Jihai	Vice President	Nil	Nil	No change
Han Zhihao	Chief Financial Officer	Nil	Nil	No change
Zhang Jingming	Company Secretary	Nil	Nil	No change

The shares held by the above people are A shares and represented their personal interests in their capacity as beneficial owners.

2. Interests and Short Positions of Directors and Supervisors in Shares, underlying Shares and Debentures

Other than as set out above, as at 30 June 2003, none of the Directors or Supervisors had any interests or short positions in any shares, underlying shares of equity derivatives or debentures of the Company or its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

As at 30 June 2003, none of the Directors or Supervisors and their respective spouses and children under 18 years of age had been granted by the Company or had exercised any rights to subscribe for shares or debentures of the Company or any of its associated corporations.

3. Interests and short positions of substantial shareholders and other persons in shares and underlying shares

As at 30 June 2003, the interests and short positions of substantial shareholders (being persons who are entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of the Company) and other persons who are required to disclose their interests pursuant to Part XV of the SFO (other than Directors and Supervisors) in the shares and underlying shares of equity derivatives of the Company as recorded in the register required to be kept under Section 336 of the SFO were as set out below:

(1) (a) Interests in ordinary shares of the Company

Name of shareholder	Number and type of shares held	% of total issued share capital	% of shareholding in the Company's total issued H share	Capacity
China Petroleum & Chemical Corporation	4,000,000,000 promoter legal person shares	55.56%	-	Beneficial owner
J.P.Morgan Chase & Co.*	349,066,000 H shares	4.8%	14.98%	Beneficial owner; investment manager; other (lending pool)

* Such H-shares were held through a nominee.

(b) Interests in underlying shares of the Company

No interests of substantial shareholders or other persons who are required to disclose their interests pursuant to Part XV of the SFO in the underlying shares of equity derivatives of the Company were recorded in the register required to be kept under Section 336 of the SFO.

(2) Short positions in shares and underlying shares of the Company

No short positions of substantial shareholders or other persons who are required to disclose their interests pursuant to Part XV of the SFO in the shares or underlying shares of equity derivatives of the Company were recorded in the register required to be kept under Section 336 of the SFO.

Save as stated above, as at 30 June 2003, no interests or short positions of any person in the shares or underlying shares of equity derivatives of the Company were recorded in the register required to be kept under Section 336 of the SFO.

Audit Committee

The audit committee and the management of the Company has reviewed the accounting principles, accounting standards and discussed matters relating to auditing, internal supervising and financial reporting, including the unaudited interim report for the six-month period ended 30 June 2003.

Change of Directors, Supervisors and senior Management

The Company convened the 2002 Annual General Meeting on 18 June 2003 and consented the resignation of Mr. Zhang Zhiliang, Mr. Zhang Honglin and Mr. Wang Jian from the Directors of the fourth session of the Board of Directors, Mr. Chen Xinyuan from the Independent Supervisor of the fourth session of the Supervisory Committee; elected Mr. Chen Xinyuan as the Independent Director of the fourth session of the Board of Directors of the Company, Mr. Zhou Yunnong as the Independent Supervisor of the fourth session of the Supervisory Committee.

Compliance with Code of Best Practice

Non-executive directors are subject to retirement by rotation at Annual General Meetings in accordance with the articles of association, and are not appointed for a specific terms. Other than this, none of the Directors is aware of any information that would reasonably indicate that the Company is not, or was not during the period, in compliance with the Code of Best Practice as set out in Appendix 14 of the Listing Rules.

Purchase, Sale or Redemption of Securities

During the reporting period, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities.

OTHER INFORMATION

A. Corporate Governance

The Board of Directors (the "Board") of the Company is composed of twelve Directors, half of whom are external Directors in the Board. The Board has four Independent Directors, being one-third of the total number of Directors, with one of whom being a professional accountant. The Board has set up the Audit Committee and the Remuneration Committee, membership of which are mainly composed of Directors. The Supervisory Committee of the Company comprises seven Supervisors, over half of whom are external Supervisors and two of whom are staff representatives. The existing Articles of Association has been approved by the relevant ministerial commissions of the State subsequent to its approval by the Company and the 2002 Annual General Meeting. Rules of proceedings of the Company that are currently in effect include Rules of Proceedings for General Meetings, Rules of Proceedings for Board Meetings, Rules of Proceedings for Supervisory Committee Meetings and Rules of Proceedings for General Manager's Office Meetings.

B. Interim dividend for 2003

The Board of Directors of the Company does not recommend any interim dividend for the six-month period ended 30 June 2003.

C. 2002 Profit Appropriation Plan

The profit appropriation plan for 2002 was approved at the Company's 2002 Annual General Meeting. A dividend of RMB0.50 (tax included) per 10 shares will be distributed to shareholders, based on the total share capital of 7,200,000,000 shares at the end of 2002. Relevant announcement was published on Shanghai Securities News, China Securities Journal, South China Morning Post and Hong Kong Commercial Daily on 19 June 2003. On 30 June 2003, the Company has published the profit appropriation plan for A shares. In respect of the distribution of A-share dividend, the share right registration date was 3 July 2003, ex-dividend date was 4 July 2003. The dividend payment date for social public shares of A shares and H shares was 10 July 2003. Such profit appropriation plan has been implemented as scheduled.

D. Material Litigation and Arbitration

The Group was not involved in any material litigation or arbitration during the reporting period.