

## **CHAIRMAN'S LETTER**

Dear Shareholders,

I am pleased to submit to you the annual report of the Company for the year ended December 31, 2003.

### **Review of Results and Operations**

The Company is the largest oil and gas producer and seller that assumes a leading position in the oil and gas industry in the PRC. The Company is engaged in a broad range of petroleum-related activities.

In 2003, the Company calmly responded to the outbreak of severe acute respiratory syndrome (SARS) and overcome the adverse effects of the situation through efficient organisation. By enhancing management efforts and taking other measures, the Company managed to achieve satisfactory operating results, with its overall development trend remarkably better than anticipated. In 2003, the Company's profit before taxation was RMB98.322 billion, representing an increase of 42.00% compared to the previous year. Net profit was RMB69.614 billion, representing an increase of 48.40% over the previous year. The exploration and production segment remained a principal source of profit for the Company.

The basic and diluted earnings per share of the Company was RMB0.40.

The Board of Directors of the Company recommends a final dividend of RMB0.079324 per share for 2003 (together with the interim dividend of RMB 0.098841 per share, the annual dividend for 2003 is RMB0.178165 per share), subject to the approval of the shareholders in the annual general meeting to be held on May 18, 2004.

### **Board of Directors and Supervisory Committee**

The 2002 annual general meeting of the Company was held in Beijing, the PRC on May 28, 2003. Article 89 of the Company's Articles of Association provides that "Directors shall be elected by the shareholders' meeting for a term of three years and may serve consecutive terms if re-elected upon expiry of their term of office". As the term of office of three of the Company's Directors had expired, a resolution for the election of three Directors of the Company was considered and approved at the meeting. It was resolved that Mr Wang Fucheng and Mr Zheng Hu be elected as Directors and Mr Franco Bernabè as an independent Director of the Company. Please refer to the section "Brief Biography of Directors, Secretary, Supervisors and Senior Management" in the "Report of Directors" for their respective brief biography.

The Board of Directors currently consists of twelve Directors, including three independent non-executive Directors. In 2003, the Board of Directors held three regular and three extraordinary meetings, at which sixteen resolutions were approved.

Mr Wu Yaowen, Vice Chairman of the Company, has applied for resignation from the posts of Director and Vice Chairman by reason of his age. Mr Wu has already resigned from the post of Vice President of CNPC.

In accordance with the Company's Articles of Association, the Board of Directors shall consist of thirteen Directors. Mr Wu's resignation will result in two vacancies. To ensure the normal operation of the Board of Directors, Mr Zhou Jipin and Mr Duan Wende have been nominated as candidates for Directors in accordance with the procedures stipulated in the Company's Articles of Association. Their official appointment is subject to approval by the shareholders.

Mr Zhou Jipin, aged 52, holds a Master's degree in marine geologic structure from the Nanhai Marine Research Institute of the China Academy of Sciences. Mr Zhou worked as Vice-Director of the International Exploration and Development Cooperation Bureau of China National Petroleum Company, Deputy General Manager of China National Oil & Gas Exploration and Exploitation Corporation and concurrently as President of the Greater Nile Petroleum Operating Company (Sudan) from November 1996. He has been General Manager of China National Oil & Gas Exploration and Exploitation Corporation and concurrently Deputy Director of the International Exploration and Development Cooperation Bureau of China National Petroleum Company since December 1997, Assistant to the General Manager of CNPC and concurrently General Manager of China National Oil & Gas Exploration and Exploitation Corporation since August 2001 and Deputy General Manager of CNPC since December 2003.

Please refer to the section "Brief Biography of Directors, Secretary, Supervisors and Senior Management" in the "Report of Directors" for the brief biography of Mr Duan Wende.

As Mr Chen Geng's term of office as Director is due to expire, he will serve consecutive terms if he is re-elected at shareholders' meeting.

The Supervisory Committee consists of seven Supervisors. Having both reached retirement age, Mr Chen Weizhong and Mr Bai Xinhe have requested to resign from their posts as Supervisors.

In order to fill the two vacancies and ensure the normal operation of the Supervisory Committee, Mr Sun Xianfeng and Mr Xu Fengli have been nominated as candidates for Supervisors. Their official appointment is subject to approval by the shareholders.

Mr Sun Xianfeng, aged 51, graduated from the Exploration Discipline of Huadong Petroleum Institute. Mr Sun worked as Deputy Director of the Supervisory Bureau of China National Petroleum Company from November 1996, transferred to the Eighth Office of the State Council Compliance Inspectors' General Office (Supervisory Committee of Central Enterprises Working Commission) as its temporary director in June 1998. He has been Deputy Director of the Audit Department of CNPC since October 2000, and has worked concurrently as Director of the Audit Services Centre of CNPC since December 2000.

Mr Xu Fengli, aged 56, graduated from the Financial Management Discipline of Xi'an Petroleum Institute for Cadres in Charge of Financial Affairs. Mr Xu has been Chief Accountant of Fushun Petrochemical Corporation since November 1995, Deputy Director of Finance and Assets Department of CNPC since November 1998, Deputy General Manager of the Finance Department of the Company since December 1999 and Director of

the Administrative Office of the Supervisory Committee of the Company since October 2003.

I would like to take this opportunity to express my gratitude to Mr Wu Yaowen, Vice Chairman and Director, and Mr Chen Weizhong and Mr Bai Xinhe, Supervisors, for their contributions to the Company during their respective terms of office, and to congratulate Mr Wang Fucheng, Mr Zheng Hu and Mr Franco Bernabè for being re-elected as Directors of the Company. I would also like to take this opportunity to express my sincere thanks for the support of our shareholders, the close cooperation of our Board of Directors and Supervisory Committee and the hard work of all our employees.

### **Standardised Operations and Business Prospects**

The Company strictly follows the regulatory laws and regulations of its places of listing and operates according to relevant laws and standards. In 2003, a number of positive and effective measures were taken according to regulatory requirements. The Company's H share price rose steadily in 2003 to a closing price of HK\$4.45 per share at the end of the year, representing an increase of almost 200% over the price at the end of 2002, or an increase of almost 250% over the issue price of the H shares.

In 2003, the Company continued to enhance exploration and exploitation of oil and gas reserves, advance geological survey and integrate exploration and exploitation, making a series of important achievements. The target of a steady increase in crude oil production was attained through strategic adjustments of crude oil production in the east on the one hand and speeding up of production in the west on the other hand. Natural gas business continued its rapid growth, recording substantial increases in both output and the sales volume. Overseas project in Indonesia was running well in terms of production and operations.

The Company continued to emphasise on the improvement of resources allocation and restructuring of the refining and chemicals business. While speeding up the construction of 10-million-ton-class refining and chemicals production bases, the Company improved the allocation of resources, carefully organised production and operations, accelerated the construction of key refining and chemicals projects and technology upgrading, stepped up the construction of sales networks for end products in the oil refining business, and unified the sales of chemical products, thus leading to a remarkable increase in scale-related strengths and profitability, an increase in the profits from oil refining business and the turning of the overall loss of the chemicals business into profits.

By accelerating the construction of key projects such as the West-East Pipeline project, the Company increased its efforts to achieve continued developments. The eastern section of the West-East Pipeline project was completed and began to supply gas to downstream users from October 16, 2003. Major work of the western section was completed. The controlling work for the Zhongxian-Wuhan pipeline was half-completed. The preliminary design of the second Shaanxi-Beijing gas pipeline was completed and the controlling work has already started.

The Company continued to promote e-commerce by making use of the website "Energyahead" ([www.energyahead.com](http://www.energyahead.com)), which was maintained as an e-commerce platform.

Procurement cost was lowered through the unification of procurement activities and the promotion of centralised procurement of goods in large quantities.

In the course of its production and operation, the Company persistently adhered to the principle of “safety first and focus on prevention”, carried out management work in a way that is orientated towards the people, and provided in-depth skills training for each post and work safety education centred around the post responsibility system, tightened the administration of safety production on contract basis and fully promoted the establishment of the Health, Safety and Environment (HSE) management system. The Company achieved clean production by treating pollution at its sources and controlling the discharge of pollutants.

Looking forward, the Company intends to continue to improve oil and gas exploration and exploitation, adjust and optimise its refining and chemicals business, speed up the construction of key projects, stress on marketing efforts and develop its overseas business, so as to achieve better operating results.

For the exploration and production business, the Company will continue to give top priority to exploration, greatly improve pre-exploration work and strive to increase reserves of good quality and high efficiency. Emphasis will be put on the tapping of resource potentials of existing oilfields and the continuous increase of recovery rate. The expansion of the production capacity of new blocks will be sped up, so as to ensure a steady increase in the output of crude oil, a significant growth in the output of natural gas and an overall improvement in exploration and exploitation standards and economic benefits, and maintain the Company’s leading position in China’s oil and gas industry.

For the refining and chemicals business, the Company will continue to optimise resources and restructure its business, use its best endeavours to organise operations and the construction of key projects, and strive to achieve a continuous and steady increase in profits.

For the marketing business, the Company will continue to improve its marketing structure, push ahead the construction of marketing networks and use its best endeavours to open up new markets, so as to achieve a continued increase in its market shares and marketing benefits.

For the natural gas and pipeline business, the Company intends to monitor pipeline construction work with the West-East Pipeline project as the focus, and achieve targets in terms of the control of construction timetable, quality and investments. The Company intends to continue to plan the development of the national pipeline network and facilities, so as to establish a solid foundation for the gradual formation of a trunk pipeline network connecting the source of natural gas and covering major markets in China.

For the overseas business, the Company will accelerate the implementation of its overseas business development strategy and expand its international operation. It will actively promote its overseas oil and gas exploration and development business, selectively develop overseas refining and chemicals processing business and marketing networks,

speed up the development of its international trade and continue to open up new areas for international business operations.

The Company's management will persist in enhancing the Company's value and strive to maximise benefits and value for its shareholders. The Company will make substantial efforts in technological innovation and management innovation, establish a sound internal control system and mechanism which comply with regulatory requirements and, by way of prudent operations, promote the continuous, effective and speedy development of the Company.

**Ma Fucai**  
*Chairman of the Board*  
Beijing, the PRC  
March 24, 2004