

# REPORT OF THE BOARD OF DIRECTORS

The Board of Directors is pleased to present the Company's audited financial statements for the year ended 31 December 2003.

## Principle Activities and Results

The principal activities of the Company are the production and sale of (i) resins and plastics, (ii) synthetic rubber, and (iii) basic organic chemical products.

The operating results of the Company for the year ended 31 December 2003 and its financial position as at 31 December 2003 are set out in the audited income statement and balance sheet, respectively, which have been prepared in accordance with IFRS.

## Dividends and Proposed Profit Appropriations

The Company did not declare any interim dividends for the six months ended 30 June 2003.

On 2 April 2004, the Board of Directors resolved to recommend the distribution of a final dividend to all shareholders at RMB 0.05 per share for the year ended 31 December 2003, during the annual general meeting of the Company ("Annual General Meeting").

The shareholders on the register of members as of 18 May 2004 will be entitled to a final dividend. The Company will temporarily close the register of members from 19 May 2004 to 18 June 2004 (both days inclusive), during which time no share transfer will be effected.

In order to qualify for the distribution of the final dividend, all transfer forms accompanied by relevant share certificates must be lodged with the share transfer registry of the Company (Hong Kong Securities Clearing Company Limited ("HKSCC"), at 19/F., Hopewell Centre, 183 Queen's Road, Hong Kong) no later than 4:00 p.m. of the last transaction day immediately preceding the date of suspending the register of members for share transfer, i.e., 18 May 2004.

Upon the approval of shareholders at the Annual General Meeting to be held 18 June 2004, the proposed final dividend for the year ended 31 December 2003 will be a total RMB 168.7 million, which will be distributed to qualified shareholders on or before 2 July 2004.

According to the Articles of Association of the Company, the dividends for domestic state-owned shares held by the Parent Company will be distributed in RMB, and the dividends for H shares will be distributed in Hong Kong Dollars. The exchange rate will be calculated at the average (RMB 1.00 = HK\$ 0.94038) of the rate quoted by the People's Bank of China the week immediately preceding the date of announcement of dividend distribution.

# REPORT OF THE BOARD OF DIRECTORS

## Shares and Shareholders

### 1. Trading of Shares

Highest traded price during the year	(H Shares)	31 December 2003	HK\$3.075
	(ADS)	31 December 2003	US\$21.34
Lowest traded price during the year	(H Shares)	24 April 2003	HK\$0.82
	(ADS)	23 April 2003	US\$5.20
Total transaction volume for the year	(H Shares)		6,032,067,652 Shares
	(ADS)		5,854,537 Shares

### 2. Share Capital

As of 31 December 2003, the issued and fully paid share capital of the Company was as follows:

	Number of shares (‘000)	Percentage of total issued share capital
Domestic shares held by Parent Company of RMB 1.00 each	2,362,000	70
Foreign shares (in form of H shares) of RMB 1.00 each	<u>1,012,000</u>	<u>30</u>
Total	<u><u>3,374,000</u></u>	<u><u>100</u></u>

### 3. Purchase, Sale or Redemption of the Company's Listed Securities

For the year ended 31 December 2003, there was no purchase, sale, redemption or cancellation of any of the Company's listed securities.

### 4. Securities and Transactions in Securities

For the year ended 31 December 2003, there were no convertible securities, options, warrants or similar rights issued or granted by the Company, nor was there any issuance for cash of equity securities by the Company.

# REPORT OF THE BOARD OF DIRECTORS

## 5. Pre-emptive Rights

Under the Articles of Association of the Company and the laws of the PRC, there are no pre-emptive rights that require the Company to offer new shares to existing shareholders in proportion to their shareholding.

## 6. Substantial Shareholders

According to the records entered into the register kept by the Company pursuant to Section 336 of the Securities and Futures Ordinance, as of 31 December 2003, the interests held by the persons other than the directors, supervisors or senior management of the Company were as follows:

Long position in the domestic shares of the Company:

	Number of domestic shares	Percentage of the total issued domestic share capital	Percentage of total issued share capital
New Sinopec	2,362,000,000 (Note 1)	100.00	70.00

Long position in H shares of the Company:

	Number of H shares	Percentage of the total issued H share capital	Percentage of total issued share capital
J.P. Morgan Chase & Co.	111,292,000 (Note 2)	11.00	3.30
HSBC Asset Management (Hong Kong) Limited	87,332,000 (Note 3)	8.63	2.59
Templeton Asset Management Limited	70,407,482 (Note 4)	6.96	2.09

### Note:

- 1) These 2,362,000,000 domestic shares are directly held by New Sinopec.
- 2) Among which, 252,000 H shares are directly held by J.P. Morgan Chase & Co., 82,248,000 H shares are held in the capacity of investment manager, and 28,792,000 H shares are held in the capacity of custodian corporation/approved lending agent.
- 3) These 87,332,000 H shares are held by HSBC Asset Management (Hong Kong) Limited in its capacity as investment manager.
- 4) These 70,407,482 H shares are held by Templeton Asset Management Limited in its capacity as investment manager.

## 7. Controlling Shareholder

The controlling shareholder of the Company is China Petroleum & Chemical Corporation, whose controlling shareholder is China Petrochemical Corporation. Both China Petroleum & Chemical Corporation and China Petrochemical Corporation are registered in Beijing, the PRC.

## Connected Transactions

For the year ended 31 December 2003, the amounts involved in connected transactions are set out in note 22 of the financial statements.

As stated in the prospectus of the Company (the "Prospectus") issued in June 1997 in connection with its global public offering, SEHK has granted conditional waivers to the Company from strict compliance with the Rules Governing the Listing of Securities on the SEHK ("Listing Rules") in respect of certain connected transactions mentioned in the Prospectus.

The independent non-executive directors confirm that during the year ended 31 December 2003, (i) relevant connected transactions were entered into by the Company in the ordinary and usual course of its business, either on normal commercial terms or on terms that are otherwise fair and reasonable so far as the shareholders of the Company are concerned; and either in accordance with the terms of the agreement governing each such transaction or on terms no less favorable than terms available to/from independent third parties, and (ii) the amount of each category of the connected transaction has not exceeded its relevant cap as stated in the Prospectus.

The auditors of the Company have reviewed the transactions described above and have confirmed with the Board of Directors that:

- (a) the transactions described above have been approved by the Board of Directors; and
- (b) the transactions described above have been entered into in accordance with the terms of the agreements governing such transactions, or where there is no such agreement, nothing came to their attention that caused them to believe the transactions described above were not conducted on normal commercial terms (which expression was applied by reference to transactions of a similar nature made by similar entities within the PRC).

## Major Litigation or Arbitration

For the year ended 31 December 2003, the Company was not involved in any material litigation or arbitration.

# REPORT OF THE BOARD OF DIRECTORS

## Disclosure of Major Events

1. At the 2002 Annual General Meeting held on 27 June 2003, the Company decided to continue appointing KPMG and KPMG Huazhen as its international and domestic auditors, respectively.
2. At the 2002 Annual General Meeting held on 27 June 2003, the following 12 persons were elected to comprise the third session of the Board of Directors: Du Guosheng, Wang Yuying, Wang Yongjian, Yang Qingyu, Wang Ruihua, Xu Hongxing, Cui Guoqi, Xiang Hanyin, Zhang Haoruo, Zhang Yanning, Liu Haiyan and Yang Xuefeng, among whom, Mr. Zhang Haoruo, Mr. Zhang Yanning, Mr. Liu Haiyan and Mr. Yang Xuefeng were elected as non-executive independent directors of the Company; the following 9 persons were elected to comprise the third session of the board of supervisors of the Company ("Board of Supervisors"): Shang Bo, Ren Jinxiang, Wang Guifen, Wang Shulan, Liu Changwei, Rong Guozhong, Zhang Jianjun, Geng Dianming and Zhao Shaohua, among whom, Mr. Geng Dianming and Mr. Zhao Shaohua were elected as independent supervisors of the Company.
3. At the first meeting for the third session of the Board of Directors held on 27 June 2003, Mr. Du Guosheng was elected as the Chairman of the Board of Directors, and Mr. Yang Qingyu was elected as the Vice-chairman of the Board of Directors. It was resolved that Mr. Xu Hongxing be appointed as the General Manager of the Company, Mr. Zhao Qichao be appointed as the Deputy General Manager of the Company, Mr. Guo Hong be appointed as the Chief Financial Officer of the Company, and Mr. Zhou Quansheng be appointed as the Board Secretary of the Company. It was resolved that an audit committee be comprised of Zhang Haoruo, Zhang Yanning, Liu Haiyan and Yang Xuefeng; Mr. Yang Xuefeng was elected as the Chairman of the audit committee.
4. At the first meeting for the third session of the Board of Supervisors held on 27 June 2003, Mr. Shang Bo was elected as the Chairman of the Board of Supervisors.

## Changes in Directors, Supervisors and Other Executive Officers

### 1. Directors

- (a) According to Article 95 of the Company's Articles of Association, a director shall serve a term of three years. According to the service contract entered into between each director and the Company, the term of employment of each of the existing directors commences from the date of appointment, i.e., 27 June 2003 and ends on 26 June 2006.
- (b) At the 2002 Annual General Meeting held on 27 June 2003, the following 12 persons were elected to comprise the third session of the Board of Directors: Du Guosheng, Wang Yuying, Wang Yongjian, Yang Qingyu, Wang Ruihua, Xu Hongxing, Cui Guoqi, Xiang Hanyin, Zhang Haoruo, Zhang Yanning, Liu Haiyan and Yang Xuefeng, among whom, Mr. Zhang Haoruo, Mr. Zhang Yanning, Mr. Liu Haiyan and Mr. Yang Xuefeng were elected as non-executive independent directors of the Company.

## 2. Resignation of an Independent Non-executive Director

The Board of Directors wishes to announce that Mr. Zhang Haoruo, an independent non-executive director of the Company, passed away on 27 March 2004.

The Board of Directors would like to take this opportunity to extend their deepest sympathy and condolences to the family of the late Mr. Zhang and express their gratitude for his devotion and dedication to the Company during his tenure of office.

It is not expected that there will be any disruption to the operations of the Company due to Mr. Zhang's resignation. The Company currently has no intention of making any arrangement to fill the resulting vacancy. As the Company will still continue to have three independent non-executive directors, it is in full compliance with Rule 3.19(2) of the Listing Rules.

## 3. Supervisors

(a) In accordance with Article 116 of the Company's Articles of Association, a supervisor shall serve a term of three years. According to the service contract entered into between each supervisor and the Company, the term of employment of each of the existing supervisors of the Company ("Supervisors") commences from the date of appointment, i.e., 27 June 2003 and ends on 26 June 2006.

(b) At the 2002 Annual General Meeting held on 27 June 2003, the following 9 persons were elected to comprise the third session of the Board of Supervisors: Shang Bo, Ren Jinxiang, Wang Guifen, Wang Shulan, Liu Changwei, Rong Guozhong, Zhang Jianjun, Geng Dianming and Zhao Shaohua, among whom, Mr. Geng Dianming and Mr. Zhao Shaohua were elected as independent supervisors of the Company.

(c) At the first meeting for the third session of the Board of Supervisors held on 27 June 2003, Mr. Shang Bo was elected as the Chairman of the Board of Supervisors of the Company.

## 4. Other Executive Officers

At the first meeting for the third session of the Board of Directors held on 27 June 2003, Mr. Du Guosheng was elected as the Chairman of the Board of Directors, and Mr. Yang Qingyu was elected as the Vice-chairman of the Board of Directors. It was resolved that Mr. Xu Hongxing be appointed as the General Manager of the Company, Mr. Zhao Qichao be appointed as the Deputy General Manager of the Company, Mr. Guo Hong be appointed as the Chief Financial Officer of the Company, and Mr. Zhou Quansheng be appointed as the Board Secretary of the Company.

# REPORT OF THE BOARD OF DIRECTORS

## Details of the Current Session of the Directors and Supervisors of the Company

Name	Position	Sex	Age	Term of Office	Annual	
					Emolument and Allowances (in RMB)	
Du Guosheng	Chairman	M	47	Until June 2006	235,609	
Yang Qingyu	Executive Director and Vice-chairman	M	57	Until June 2006	209,348	
Xu Hongxing	Executive Director and General Manager	M	45	Until June 2006	207,625	
* Wang Yuying	Non-executive Director	F	57	Until June 2006	-	
* Wang Yongjian	Non-executive Director	M	44	Until June 2006	-	
* Wang Ruihua	Non-executive Director	M	56	Until June 2006	-	
* Cui Guoqi	Non-executive Director	M	50	Until June 2006	-	
* Xiang Hanyin	Non-executive Director	M	49	Until June 2006	-	
**Zhang Haoruo	Independent Non-executive Director	M	72	Until June 2006	-	
* Zhang Yanning	Independent Non-executive Director	M	77	Until June 2006	-	
* Liu Haiyan	Independent Non-executive Director	M	62	Until June 2006	-	
* Yang Xuefeng	Independent Non-executive Director	M	65	Until June 2006	-	
* Shang Bo	Chairman of the Board of Supervisors	M	56	Until June 2006	-	
* Ren Jinxiang	Supervisor	M	56	Until June 2006	-	
* Wang Guifen	Supervisor	F	51	Until June 2006	-	
* Wang Shulan	Supervisor	F	49	Until June 2006	-	
Liu Changwei	Supervisor	M	46	Until June 2006	130,362	
Rong Guozhong	Supervisor	M	46	Until June 2006	116,694	
* Zhang Jianjun	Supervisor	F	52	Until June 2006	-	
* Geng Dianming	Independent Supervisor	M	57	Until June 2006	-	
* Zhao Shaohua	Independent Supervisor	M	64	Until June 2006	-	

\* Such person did not receive any emolument or allowance from the Company.

\*\* Mr. Zhang Haoruo did not receive any emolument or allowance from the Company. In addition, Mr. Zhang passed away on 27 March 2004. For details, please refer to the section "Changes in Directors, Supervisors and Other Executive Officers - Resignation of an Independent Non-executive Director".

## **Directors', Supervisors' and Other Executive Officers' Interests in Shares**

As of 31 December 2003, none of the directors, supervisors or senior management of the Company had (a) any interests or short-term positions that were required to be registered in the registry preserved pursuant to Section 352 of the Securities and Futures Ordinance or (b) interests or short-term positions that were required to be reported to the Company or the SEHK pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, in any shares, relevant shares or debentures of the Company or any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance).

## **Directors' and Supervisors' Service Contracts**

Each of the directors and supervisors has entered into a service contract with the Company.

For the year ended 31 December 2003, the aggregate amount of cash remuneration paid to the directors of the Company ("Directors") was RMB 606,184, as compared with RMB 519,285 in 2002. The aggregate amount of non-cash remuneration (consisting solely of contributions to pensions and retirement benefit plans) paid to the Directors in 2003 was RMB 46,398, as compared with RMB 28,358 in 2002.

For the year ended 31 December 2003, the aggregate amount of cash remuneration paid to the Supervisors was RMB 224,271, as compared with RMB 116,285 in 2002. The aggregate amount of non-cash remuneration (consisting solely of contributions to pensions and retirement benefit plans) paid to the Supervisors in 2003 was RMB 22,785, as compared with RMB 11,209 in 2002.

No other service contract exists between the Company and any of the Directors or Supervisors. Except as disclosed above, no Director or Supervisor has entered into any service contract with the Company that is not terminable by the Company without payment other than statutory compensation.

## **Directors' and Supervisors' Interests in Contracts**

Except as disclosed above, there was no contract of significance, to which the Company was a party, in existence during or at the end of the year under review in which a Director or Supervisor of the Company had a material interest.

## **Loans to Directors, Supervisors and Senior Management**

For the year ended 31 December 2003, the Company had not provided any loans to any of its Directors, Supervisors or senior management.



## **Employees' Benefit, Retirement Scheme and Employee Housing Subsidy**

As of 31 December 2003, the Company had 10,207 employees as compared with 10,366 employees in 2002, representing a decrease of 159 employees. In addition, the Company offered its employees the opportunities for education and training based upon its development and actual performance of the employees.

The Company's employees participated in retirement benefit plans provided by the Company, details of which are set out in note 21 of the financial statements.

Under the relevant laws and regulations of the PRC, the policy for the allocation of housing as welfare benefits has ceased to apply. The Company is considering detailed measures for payment of housing subsidies through increasing wages or making lump sum payments to qualified employees. Once determined, these measures will be reflected in the financial statements of the Company of the relevant year. As disclosed in the Company's Prospectus dated 17 June 1997, Yanshan Company is willing to pay such a lump sum payment. For this purpose, the Company is not expecting any cash outflows.

## **Basic Medical Insurance for Employees**

According to the Beijing Municipal Government Order (2001) No. 68, and in line with the arrangements of Beijing Municipal Labor Security Authority, the Company has implemented the Regulations of Beijing Municipality on Basic Medical Insurance (the "Regulations") on 1 September 2002. Prior to the implementation of such Regulations, the Company has been complying with relevant State regulations by drawing 14% of the employees' total current wages as welfare fees to be used as the medical expenditure of the Company's employees, whilst relevant welfare fees were set out in the labor costs of the Company for the specific current term. After the implementation of the Regulations, the medical insurance fees to be paid represented 9% of the total wages, and such amount has been included in the 14% employee welfare fees to be drawn by the Company. As a result, there will be no impact on the income statement and the balance sheet of the Company upon implementation of the Regulations.

## **Major Suppliers and Customers**

For the year ended 31 December 2003, 53.4% of purchases (not including the purchase of items which are of a capital nature) were attributable to the Company's largest supplier, the Parent Company, and 7.7% of purchases were attributable to the Company's five largest suppliers (excluding the Parent Company) in aggregate.

The aggregate amount of sales attributable to the Company's five largest customers, excluding Yanshan Company, represented no more than 10.2% of the Company's turnover. The amount of sales attributable to Yanshan Company and its subsidiaries, the Company's largest customer, represented 10.6% of the Company's turnover.

To the knowledge of the Directors, at no time during the year have the Directors and Supervisors, their associates, or any shareholder of the Company (who to the knowledge of the Directors own more than 5% of the Company's share capital) had any interests in these major suppliers and customers.

## **Reserves**

Changes in reserves of the Company for the year ended 31 December 2003 are set out in the statements of changes in equity.

## **Fixed Assets**

Changes in fixed assets of the Company for the year ended 31 December 2003 are set out in note 9 to the financial statements.

## **Bank Loans and Other Borrowings**

Details of bank loans and other borrowings of the Company as at 31 December 2003 are set out in notes 17 and 18 to the financial statements.

## **Interest Capitalised**

Interest capitalised on the Company's property, plant and equipment during the year ended 31 December 2003 amounted to RMB 9.6 million.

## **Taxation**

The Company has been subject to the PRC enterprise income tax of 33% for the year ended 31 December 2003. The Company is not aware of any changes in government policy that may affect the Company's tax rate.

Details of the Company's taxation are set out in note 5 to the financial statements.

## **Auditors**

At the 2002 Annual General Meeting held on 27 June 2003, a resolution was passed for the continued appointment of KPMG and KPMG Huazhen as the Company's international and domestic auditors, respectively.

## **Compliance with the Code of Best Practice**

The Board of Directors believes that, for the year ended 31 December 2003, the Company complied with the Code of Best Practice as set out in Appendix 14 of the Listing Rules.

## **Audit Committee**

The Board of Directors has established an audit committee in 2002. For the year ended 31 December 2003, the audit committee was composed of Mr. Zhang Haoruo, Mr. Zhang Yanning, Mr. Liu Haiyan and Mr. Yang Xuefeng, the independent directors of the Company. Mr. Yang Xuefeng was elected as the Chairman of the audit committee. The audit committee is responsible for the review and supervision of the Company's financial reporting process and internal control as set out in the Code of Best Practice. For the year ended 31 December 2003, the audit committee held two meetings. The audit committee, together with the management of the Company, has reviewed the accounting policies adopted by the Company, and has discussed the contents of the auditing, internal supervising and the financial statements.

## **Impact of the Recent Economic Development**

Unstable factors inevitably exist in the international economy, which might bring adverse impact on the production and operation of the Company in the near future. Nevertheless, the Company believes that the steady growth of China's economy will undoubtedly lead to a further increase in the demand for the products of the Company, whilst the commissioning of the ethylene facilities with 710,000 tons capacity will elaborate the scale merit of the Company. The Company believes that, through the implementation of various effective operating and development strategies, it will be able to provide satisfactory returns to the shareholders.

## **Trust Deposits**

As of 31 December 2003, the Company did not have any trust deposits with any financial institutions in the PRC. The Company has not encountered any difficulty with respect to withdrawing its deposits.

By Order of the Board of Directors

**Du Guosheng**

Chairman

2 April 2004, Beijing, the PRC