Notes to the Financial Statements

for the year ended 31 December 2004

1. BACKGROUND AND PRINCIPAL ACTIVITIES

Sinopec Zhenhai Refining & Chemical Company Limited ("the Company") was established in the People's Republic of China ("the PRC") on 28 June 1994 as a joint stock limited company as part of a restructuring exercise to convert Zhenhai General Petrochemical Works ("ZGP"), a state-owned enterprise, into a joint stock limited company. ZGP was under the direct supervision and control of China Petrochemical Corporation ("Sinopec Group Company"), a ministry-level enterprise under the direct supervision of the State Council of the PRC, which is responsible for the administration and development of the petrochemical industry in the PRC. On 28 June 1994, the Company took over the business undertakings and subsidiaries of ZGP together with the relevant assets and liabilities, and issued to Sinopec Group Company 1,800,000,000 state-owned shares with a par value of RMB1.00 each.

As part of the reorganisation of Sinopec Group Company in 2000, Sinopec Group Company transferred all of its shareholdings in the Company to China Petroleum & Chemical Corporation ("Sinopec Corp"), a joint stock limited company established in the PRC on 25 February 2000. Since then, Sinopec Corp is the immediate parent company and Sinopec Group Company is the ultimate parent company.

The Company and its subsidiaries (collectively "the Group") is principally engaged in the production and sale of petroleum products (including gasoline, diesel, kerosene, naphtha, liquefied petroleum gas ("LPG"), solvent oil and fuel oil), intermediate petrochemical products, asphalt, urea and petrochemical products (including paraxylene and polypropylene). Gasoline, diesel and kerosene are three major products of the Group. The principal activities of its principal subsidiaries are shown in note 16.

2. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of the financial statements are set out below:

(a) Statement of compliance

The financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS") adopted by the International Accounting Standards Board ("IASB"). IFRS include International Accounting Standards ("IAS") and related interpretations. These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(a) Statement of compliance *(continued)*

The IASB has issued a number of new and revised IFRS and IAS ("new IFRS") which are effective for accounting periods beginning on or after 1 January 2005. The Group has not early adopted these new IFRS in the financial statements for the year ended 31 December 2004. The Group has commenced an assessment of the impact of these new IFRS but is not yet in a position to state whether these new IFRS would have a significant impact on its results of operations and financial position.

(b) Basis of preparation

The financial statements are presented in Renminbi, rounded to the nearest thousand. The measurement basis used in the preparation of the financial statements is historical cost modified by the revaluation of certain property, plant and equipment where stated in note 2(e). The accounting policies have been consistently applied by the Group and are consistent with those adopted in the previous year.

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from those estimates.

(c) Basis of consolidation

(i) Subsidiaries

The consolidated financial statements of the Group include the financial statements of the Company and all of its principal subsidiaries. Subsidiaries are those entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) Associates and jointly controlled entity

Associates are those entities in which the Company or the Group has significant influence, but not control, over the financial and operating policies.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(c) Basis of consolidation *(continued)*

(ii) Associates and jointly controlled entity (continued)

A jointly controlled entity is an entity which operates under a contractual arrangement between the Company or the Group and other parties, where the contractual arrangement establishes that the Company or the Group and one or more of the other parties share joint control over the economic activity of the entity.

The Company's financial statements and the Group's consolidated financial statements include the Company's and the Group's share of the total recognised gains and losses of the principal associates and jointly controlled entity on an equity accounted basis, from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. When the Company's or the Group's share of losses exceeds the carrying amount of the associate and the jointly controlled entity, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Company or the Group has incurred obligations in respect of the associate and the jointly controlled entity.

(iii) Transactions eliminated on consolidation

Intra-group transactions and balances, and any material unrealised profit arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(d) Translation of foreign currencies

Transactions in foreign currencies are translated into Renminbi at the applicable exchange rates quoted by the People's Bank of China ("PBOC rates") ruling at the transaction dates.

Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into Renminbi at the applicable PBOC rates ruling at that date.

Foreign currency translation differences relating to funds borrowed to finance the construction of property, plant and equipment to the extent that they are regarded as an adjustment to interest charges are capitalised during the construction period. All other exchange differences are dealt with in the income statement.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(e) Property, plant and equipment

Property, plant and equipment are stated in the balance sheets at cost or valuation (see note 14(b)) less accumulated depreciation and impairment losses (see note 2(t)). Revaluation is performed periodically to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

(i) Subsequent expenditure

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, is capitalised with the carrying amount of the component being written off. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is charged to the income statement as an expense in the period in which it is incurred.

(ii) Depreciation

Depreciation is provided to write off the costs or revalued amount of property, plant and equipment over their estimated useful lives on a straight-line basis, after taking into account their estimated residual values, as follows:

Buildings	20 to 40 years
Plant, machinery, equipment and others	8 to 18 years
Motor vehicles	8 to 10 years

(iii) Retirement or disposal

Gains or losses arising from the retirement or disposal of property, plant and equipment are determined as the difference between the net sales proceeds and the carrying amount of the assets and are recognised in the income statement on the date of retirement or disposal.

(f) Construction in progress

Construction in progress represents buildings, various plant and equipment under construction and pending installation, and is stated at cost less impairment losses (see note 2(t)). Cost comprises direct costs of construction as well as interest charges, and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest charges, during the construction period.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(f) Construction in progress *(continued)*

Construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

(g) Lease prepayments

Lease prepayments represent the amount of land use rights paid to the PRC land bureau. Land use rights are carried at historical cost less accumulated amortisation and impairment losses (see note 2(t)). Amortisation is calculated on a straight-line basis over the respective periods of the rights.

(h) Investments in subsidiaries

In the Company's balance sheet, investments in subsidiaries are accounted for using the equity method.

(i) Other investments

Other investments in unlisted equity securities are stated at cost less impairment losses (see note 2(t)). A provision is made where, in the opinion of management, the carrying amount of the other investments exceeds its recoverable amount.

(j) Inventories

Inventories, other than spare parts and consumables, are carried at the lower of cost and net realisable value. Cost includes the cost of materials computed using the weighted average method and expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of work in progress and finished goods, cost includes direct labour and an appropriate proportion of production overheads. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sales.

When inventories are sold, the carrying amount of the inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

Spare parts and consumables are stated at cost less any provision for obsolescence.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(k) Trade receivables

Trade receivables are stated at cost less allowance for doubtful accounts. An allowance for doubtful accounts is provided based upon the evaluation of the recoverability of these accounts at the balance sheet date.

(l) Cash equivalents

Cash equivalents consist of time deposits with banks with an initial term of less than three months when acquired. Cash equivalents are stated at cost, which approximate fair value.

(m) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Group or the Company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(n) Revenue recognition

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue excludes value-added tax and is after deduction of any trade discounts and returns. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the possible return of goods, or when the amount of revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

Revenue from the rendering of services is recognised in the income statement upon performance of the services.

Dividend income is recognised when the shareholder's right to receive payment is established.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(o) Government grants

Capital-based government grants consist of grants for the purchase of equipment used for technology improvements. Such grants are initially recorded as long-term liabilities and are offset against the cost of asset to which the grants related when construction commences. Upon transfer to property, plant and equipment, the grants are recognised as income over the useful life of the property, plant and equipment by way of reduced depreciation charge.

(p) Net financing costs

Net financing costs comprise interest expense on borrowings, interest income from bank deposits, foreign exchange gains and losses and bank charges.

Interest income from bank deposits is accrued on a time-apportioned basis by reference to the principal outstanding and the rate applicable.

All interest and other costs incurred in connection with borrowings are expensed as incurred as part of net financing costs, except to the extent that they are capitalised as being directly attributable to the acquisition or construction of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

(q) Repairs and maintenance expenses

Repairs and maintenance expenses, including cost of major overhaul, are charged to the income statement as and when they are incurred.

(r) Research and development costs

Research and development costs comprise all costs that are directly attributable to research and development activities or that can be allocated on a reasonable basis to such activities. Because of the nature of the Group's research and development activities, no development costs satisfy the criteria for the recognition of such costs as an asset. The research and development costs are therefore recognised as expenses in the period in which they are incurred.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(s) Retirement benefits

Contributions to defined contribution scheme are recognised as an expense in the income statement as incurred. Further information is set out in note 9.

(t) Impairment losses

The carrying amounts of the Group's assets, other than trade receivables (refer to accounting policy k), inventories (refer to accounting policy j), and deferred tax assets (refer to accounting policy v), are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The recoverable amount is the greater of the net selling price and the value in use. In determining the value in use, expected future cash flows generated by the assets are discounted to their present value. The amount of the reduction is recognised as an expense in the income statement.

The Group assesses at each balance sheet date whether there is any indication that an impairment loss recognised for an asset in prior years may no longer exist. An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. A subsequent increase in the recoverable amount of an asset, when the circumstances and events that led to the write-down or write-off cease to exist, is recognised as income. The reversal is reduced by the amount that would have been recognised as depreciation had the write-down or write-off not occurred.

(u) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(v) Income tax

Income tax on the income statement for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

2. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(v) Income tax *(continued)*

Deferred tax is provided under the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. The effect on deferred tax of any changes in tax rates is charged to income statement.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(w) Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

(x) Operating leases

Operating lease payments are charged to the income statement on a straight-line basis over the period of the respective leases.

(y) Segment reporting

A segment is a distinguishable component of the Group that is engaged in providing products or services and is subject to risks and rewards that are different from those of other segments.

3. TURNOVER

Turnover represents the sales value of goods sold to customers, net of value-added tax and is after deduction of any sales discounts and returns.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

4. BUSINESS TAXES AND SURCHARGES

	2004 RMB'000	2003 RMB'000
Consumption tax	**1,355,469**	967,569
City construction tax	**178,855**	114,361
Education surcharge	**102,977**	65,831
Others	**16,198**	13,604
Total	**1,653,499**	1,161,365

Consumption tax is levied on producers of gasoline and diesel based on an applicable tax rate applied to the volume of sales. City construction tax and education surcharge are levied on an entity based on applicable tax rates applied to the total amount of value-added tax, consumption tax and business tax.

5. OTHER OPERATING EXPENSES

	2004 RMB'000	2003 RMB'000
Donations	**30,025**	4,520
Water utility fund	**28,700**	22,200
Provision for impairment of other investments	**17,442**	1,676
Others	**23,841**	11,782
Total	**100,008**	40,178

6. EMPLOYEE REDUCTION EXPENSES

In accordance with the Group's voluntary employee reduction plan, the Group recorded employee reduction expenses of RMB69,184,000 during the year ended 31 December 2003 in respect of the voluntary resignation of approximately 870 employees. There were no employee reduction expenses incurred during the year ended 31 December 2004.

7. PROFIT FROM ORDINARY ACTIVITIES BEFORE TAXATION

Profit from ordinary activities before taxation is arrived at after charging/(crediting):

	2004 RMB'000	2003 RMB'000
(a) Net financing costs		
Interest expense	67,434	97,291
Less: Amount capitalised as projects in progress*	(4,773)	(24,189)
Interest expense, net	62,661	73,102
Interest income	(12,324)	(8,122)
Net foreign exchange loss	22,480	16,475
Bank charges	836	452
Total	73,653	81,907

* The borrowing costs have been capitalised at a rate of 5.05%–5.49% (2003: 5.05%–5.49%) per annum for projects in progress.

	2004 RMB'000	2003 RMB'000
(b) Other items		
Cost of inventories #	34,862,907	25,092,790
Depreciation of property, plant and equipment #	1,032,879	844,305
Amortisation of lease prepayments	1,096	1,143
Repairs and maintenance expenses #	287,493	338,948
Research and development costs	14,076	41,864
Staff costs #		
— Salaries, wages, bonus and other staff welfare	639,461	653,278
— Contributions to retirement scheme	109,332	101,035
Provision for impairment of other investments	17,442	1,676
Auditors' remuneration	2,608	2,608
Operating lease charges	12,634	4,243
Dividend income from other investments	(6,141)	(6,079)

Cost of inventories includes RMB1,710,585,000 (2003: RMB1,588,967,000) relating to depreciation of property, plant and equipment, repairs and maintenance expenses and staff costs, which amount is also included in the respective total amounts disclosed separately above for each of these types of expenses.

The number of employees of the Group as at 31 December 2004 was 8,766 (2003: 9,178).

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

8. DIRECTORS' AND SUPERVISORS' EMOLUMENTS

(a) Directors' and supervisors' emoluments are as follows:

Name	Fees		Basic salaries, allowances and benefits in kind		Bonus		Retirement scheme contributions		Total	
	2004	2003	**2004**	2003	**2004**	2003	**2004**	2003	**2004**	2003
	(Amounts in RMB'000)									
Directors:										
Sun Weijun	**—**	—	**67**	67	**203**	165	**36**	32	**306**	264
Zhan Juping	**—**	—	**67**	67	**203**	165	**36**	32	**306**	264
Xu Liqiao	**—**	—	**54**	54	**163**	132	**36**	32	**253**	218
Sun Jianli	**—**	—	**54**	54	**163**	132	**36**	32	**253**	218
Zhao Jinxuan	**—**	—	**54**	54	**163**	132	**36**	32	**253**	218
Yu Renming	**—**	—	**54**	54	**163**	132	**36**	32	**253**	218
External directors:										
Wang Lisheng	**3**	3	**—**	—	**—**	—	**—**	—	**3**	3
Hu Weiqing	**3**	7	**—**	—	**—**	—	**—**	—	**3**	7
Independent non-executive directors:										
Sun Yongsen	**12**	17	**—**	—	**—**	—	**—**	—	**12**	17
Cen Kefa	**16**	19	**—**	—	**—**	—	**—**	—	**16**	19
Li Linghong	**16**	17	**—**	—	**—**	—	**—**	—	**16**	17
Qiu Yun	**14**	19	**—**	—	**—**	—	**—**	—	**14**	19
Supervisors:										
Gu Yueguang	**—**	—	**54**	52	**163**	128	**35**	32	**252**	212
Lu Xiangyang	**6**	4	**—**	—	**—**	—	**—**	—	**6**	4
Zhang Jianjun	**6**	4	**—**	—	**—**	—	**—**	—	**6**	4
Bao Chuntian	**14**	17	**—**	—	**—**	—	**—**	—	**14**	17
Luo Jie	**18**	19	**—**	—	**—**	—	**—**	—	**18**	19
Liu Youyin	**—**	—	**46**	27	**93**	84	**35**	31	**174**	142
Chen Yaohuan	**—**	—	**49**	35	**107**	106	**35**	31	**191**	172
	108	126	**499**	464	**1,421**	1,176	**321**	286	**2,349**	2,052

For the years ended 31 December 2004 and 2003, no emolument was paid to the directors or supervisors as an inducement to join or upon joining the Company or as compensation for loss of office.

(b) Five individuals with highest emoluments:

The five individuals with highest emoluments of the Company in 2004 and 2003 were all executive directors, whose total emoluments have been shown above.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

9. RETIREMENT SCHEME

As stipulated by the regulations of the PRC, the Group participates in a defined contribution retirement scheme organised by the Ningbo Labour Insurance Administration Department. The Group is required to make contributions to the retirement scheme at a rate of 20% of total salaries and benefits in kind of its employees. A member of the scheme is entitled to retirement benefits equal to a fixed proportion of the salary prevailing at his retirement date.

Other than the above, pursuant to a document "Lao Bu Fa [1995] No. 464" dated 29 December 1995 issued by the Ministry of Labour of the PRC, the Group has set up a supplementary defined contribution retirement scheme for its employees. The assets of the scheme are held separately from those of the Group in an independent fund administered by representatives from the Group. The scheme is funded by contributions from the Group which are calculated at a rate based on the salaries and benefits in kind of its employees. The contribution rate for 2004 was 5% (2003: 5%).

The Group has no other material obligation for the payment of retirement benefits associated with this scheme beyond the annual contributions described above.

10. INCOME TAX EXPENSE

Individual companies within the Group are mainly subject to Enterprise Income Tax ("EIT") at 33% on taxable income determined according to the PRC tax laws.

Pursuant to the document "Cai Shui Zi [1994] No. 1" issued by the Ministry of Finance ("MOF") and the State Administration of Taxation of China ("SAT") on 29 March 1994, the Group is eligible for certain EIT preferential treatments because of its recycling of certain waste materials. During 2004, the amount of EIT refund was RMB71,747,000 (2003: RMB9,833,000).

Pursuant to the document "Cai Shui Zi [1999] No. 290" issued by the MOF and SAT on 8 December 1999, the Group is eligible for certain EIT preferential treatments because of its purchase of certain domestic equipment for technical improvements. During 2004, the amount of EIT refund was RMB29,812,000 (2003: RMB29,441,000).

The Group did not carry on business overseas and in Hong Kong and therefore does not incur overseas and Hong Kong Profits Tax.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

10. INCOME TAX EXPENSE *(continued)*

(a) Income tax expense in the consolidated income statement represents:

	2004 RMB'000	2003 RMB'000
Current tax expense		
— Current year	**1,137,917**	509,421
— Under provision in respect of prior years	**477**	5,120
	1,138,394	514,541
Deferred taxation	**(3,836)**	(165)
Share of associates' and jointly controlled entity's income tax	**17,517**	7,189
Total income tax expense in consolidated income statement	**1,152,075**	521,565

(b) Reconciliation of effective tax rate:

	2004 RMB'000	2003 RMB'000
Profit from ordinary activities before taxation	**3,765,434**	1,609,594
Expected income tax at statutory tax rate of 33%	**1,242,593**	531,166
Non-deductible expenses	**7,771**	15,386
Tax exempt revenue	**(2,027)**	(2,006)
EIT preferential treatments	**(101,559)**	(39,274)
Effect of tax losses not recognised	**1,334**	11,060
Differential tax rate of associates	**129**	778
Under provision of income tax expenses in respect of prior years	**477**	5,120
Others	**3,357**	(665)
Income tax expense	**1,152,075**	521,565

11. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The profit attributable to shareholders of RMB2,613,288,000 (2003: RMB1,087,987,000) has been dealt with in the financial statements of the Company.

12. DIVIDENDS

(a) Dividends attributable to the year

	2004 RMB'000	2003 RMB'000
Interim dividend declared and paid of RMB0.09 per share (2003: RMB0.05 per share)	227,138	126,188
Final dividend proposed after the balance sheet date of RMB0.21 per share (2003: RMB0.09 per share)	529,988	227,138
	757,126	353,326

Pursuant to a resolution passed at the Board of Directors' meeting on 8 April 2005, a final dividend of RMB0.21 (2003: RMB0.09) per share totalling RMB529,988,438 (2003: RMB227,137,902) was proposed for shareholders' approval at the Annual General Meeting.

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

(b) Dividends attributable to the previous financial year, approved and paid during the year

	2004 RMB'000	2003 RMB'000
Final dividend in respect of the previous financial year, approved and paid during the year, of RMB0.09 per share (2003: RMB0.08 per share)	227,138	201,900

13. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to ordinary shareholders of RMB2,613,288,000 (2003: RMB1,087,987,000) and the weighted average number of ordinary shares of 2,523,754,468 (2003: 2,523,754,468) in issue during the year.

(b) Diluted earnings per share

There were no dilutive potential ordinary shares in existence during the years ended 31 December 2003 and 2004.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

14. PROPERTY, PLANT AND EQUIPMENT

The Group

	Buildings RMB'000	**Plant, machinery, equipment and others** RMB'000	**Motor vehicles** RMB'000	**Total** RMB'000
Cost or valuation:				
At 1 January 2004	920,712	12,645,870	138,104	13,704,686
Reclassification	(8,740)	8,740	—	—
Transfer from construction in progress *(note 15)*	95,458	929,616	40,598	1,065,672
Additions	—	86,601	2,844	89,445
Disposals	(15,220)	(70,130)	(26,859)	(112,209)
At 31 December 2004	**992,210**	**13,600,697**	**154,687**	**14,747,594**
Accumulated depreciation:				
At 1 January 2004	208,094	4,876,000	92,673	5,176,767
Depreciation charge for the year	41,146	979,677	12,056	1,032,879
Written back on disposal	(3,242)	(53,815)	(24,014)	(81,071)
At 31 December 2004	**245,998**	**5,801,862**	**80,715**	**6,128,575**
Net book value:				
At 31 December 2004	**746,212**	**7,798,835**	**73,972**	**8,619,019**
At 31 December 2003	712,618	7,769,870	45,431	8,527,919

14. PROPERTY, PLANT AND EQUIPMENT *(continued)*

The Company

	Buildings	Plant, machinery, equipment and others	Motor vehicles	Total
	RMB'000	RMB'000	RMB'000	RMB'000
Cost or valuation:				
At 1 January 2004	460,885	11,757,612	103,396	12,321,893
Reclassification	(8,700)	8,700	—	—
Transfer from construction in progress *(note 15)*	59,335	918,425	18,511	996,271
Additions	—	86,153	2,844	88,997
Disposals	(14,007)	(55,975)	(22,887)	(92,869)
At 31 December 2004	**497,513**	**12,714,915**	**101,864**	**13,314,292**
Accumulated depreciation:				
At 1 January 2004	97,352	4,505,004	75,330	4,677,686
Depreciation charge for the year	17,200	931,995	9,028	958,223
Written back on disposal	(2,722)	(39,995)	(21,899)	(64,616)
At 31 December 2004	**111,830**	**5,397,004**	**62,459**	**5,571,293**
Net book value:				
At 31 December 2004	**385,683**	**7,317,911**	**39,405**	**7,742,999**
At 31 December 2003	363,533	7,252,608	28,066	7,644,207

(a) All of the Group's buildings are located in the PRC.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

14. PROPERTY, PLANT AND EQUIPMENT *(continued)*

(b) The Company was established in the PRC on 28 June 1994 as a joint stock limited company as part of the restructuring of ZGP. On the same date, the principal business undertakings of ZGP together with the relevant assets and liabilities were taken over by the Company. As required by the relevant PRC rules and regulations, a valuation of the assets and liabilities to be injected into the Company was carried out as at 31 March 1994 by an independent valuer, Zhong Fa International Properties Valuation Corporation, and approved by the State-owned Assets Administration Bureau. The injected assets and liabilities were reflected in the financial statements on this basis.

In accordance with *IAS 16 Property, plant and equipment,* subsequent to this revaluation, which was based on depreciated replacement costs, property, plant and equipment are carried at revalued amount, being the fair value at the date of the revaluation less any subsequent accumulated depreciation and impairment losses. Revaluation is performed with sufficient regularity to ensure that the carrying amount of these assets does not differ materially from that which would be determined using fair value at the balance sheet date. Based on a revaluation performed by an independent valuer registered in the PRC, China United Assets Appraisal Corporation as of 31 December 2004, which was based on depreciated replacement costs, the carrying value of property, plant and equipment did not differ materially from their fair value.

15. CONSTRUCTION IN PROGRESS

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Projects in progress				
At 1 January	**489,618**	1,101,062	**473,110**	1,089,606
Additions	**1,357,177**	2,095,427	**1,296,359**	1,984,455
Transfer to property, plant and equipment *(note 14)*	**(1,065,672)**	(2,706,871)	**(996,271)**	(2,600,951)
At 31 December	**781,123**	489,618	**773,198**	473,110
Construction materials	**59,036**	94,782	**17,838**	94,782
	840,159	584,400	**791,036**	567,892

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

16. INTERESTS IN SUBSIDIARIES

	The Company 2004 RMB'000	2003 RMB'000
Share of net assets, unlisted	**1,177,158**	1,115,362
Amounts due from subsidiaries	**248,516**	441,026
Amounts due to subsidiaries	**(567,857)**	(566,589)
	857,817	989,799

The following list contains only the particulars of subsidiaries, all of which are companies established and operating in the PRC, which principally affected the results, assets or liabilities of the Group:

Name of subsidiary	Registered capital RMB'000	Percentage of equity held by the Company	Percentage of equity held by subsidiary	Type of legal entity	Principal activity
Zhenhai Refining & Chemical Maintenance and Installation Company	30,000	100%	—	Joint stock company	Repairing and installation of industrial equipment
Ningbo Economic & Technical Development Zone Zhenhai Refining & Chemical Warehousing Company	300,000	100%	—	Joint stock company	Warehousing services
Zhenhai Refining & Chemical Engineering Company	50,000	100%	—	Joint stock company	Contractor for construction projects

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

16. INTERESTS IN SUBSIDIARIES *(continued)*

Name of subsidiary	Registered capital RMB'000	Percentage of equity held by the Company	Percentage of equity held by subsidiary	Type of legal entity	Principal activity
Zhenhai Refining & Chemical Materials and Equipment Company	245,000	100%	—	Joint stock company	Trading in construction materials and supplies
Ningbo Bonded Area Zhenhai Refining & Chemical International Trading Company	10,000	90%	10%	Limited company	Import and export of petrochemical products
Zhenhai Refining & Chemical Haida Development Company	40,290	100%	—	Joint stock company	Contract labour services, trading in daily necessities for employees and trading in petrochemical products
Ningbo Bonded Area Zhenhai Refining & Chemical Gas Stations Investment Company Limited	50,000	95%	5%	Limited company	Wholesale and retail of petrochemical products and warehousing services
Zhenhai Refining & Chemical Pressure Containers Examination and Maintenance Station	200	100%	—	Collective enterprise	Provision of repairs and maintenance services for containers and pipelines

16. INTERESTS IN SUBSIDIARIES *(continued)*

Name of subsidiary	Registered capital RMB'000	Percentage of equity held by the Company	Percentage of equity held by subsidiary	Type of legal entity	Principal activity
Zhenhai Refining & Chemical Dong Hai Hotel	30,000	100%	—	Joint stock company	Provision of hotel and catering services
Ningbo Jinchen Trading Company Limited	18,000	90%	10%	Limited company	Sales of petrochemical products and warehousing services
Ningbo Donghai Petrochemical Company Limited	4,000	90%	10%	Limited company	Wholesale and retail of petrochemical products

None of the subsidiaries has issued any debt securities.

17. INTERESTS IN ASSOCIATES

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Share of net assets	**189,650**	215,167	**129,420**	107,184

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

17. INTERESTS IN ASSOCIATES *(continued)*

The following list contains only the particulars of principal associates, which are companies established and operating in the PRC, which principally affected the results, assets or liabilities of the Group:

Name of associate	**Registered capital** RMB'000	**Percentage of equity held by the Company**	**Type of legal entity**	**Principal activity**
Xiamen Luyong Petrochemical Company Limited	40,000	50%	Limited company	Trading in petroleum products
Zhuhai Gulf Petrochemical Company Limited	10,000	45%	Limited company	Trading in petroleum and petrochemical products
Nantong Donghai Petrochemical Company Limited	73,000	50%	Collective enterprise	Trading in petrochemical products
Hangzhou Xiaoshan Donghai Petrochemical Company Limited	15,000	50%	Limited company	Trading in petroleum products
Wenzhou Donghai Petrochemical Company Limited	11,644	50%	Limited company	Trading in petrochemical products
Zhejiang Petroleum Products Pipage and Storage Company Limited	90,000	50%	Limited company	Pipage and storage of petroleum products

18. INTEREST IN JOINTLY CONTROLLED ENTITY

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Share of net assets	**44,962**	8,178	**44,962**	8,178

Details of the Group's interest in the jointly controlled entity are as follows:

Name of jointly controlled entity	Place of incorporation and operation	Registered capital	Percentage of ownership interest held by the Company	Type of legal entity	Principal activity
		USD'000			
Zhenhai Refining & Chemical BP (Ningbo) LPG Company Limited	PRC	10,000	50%	Limited company	Trading of LPG

19. OTHER INVESTMENTS

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Other investments in unlisted shares, at cost	**191,746**	169,108	**169,108**	169,108
Less: Provision for impairment losses	**(42,750)**	(25,308)	**(42,483)**	(25,308)
	148,996	143,800	**126,625**	143,800

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

20. DEFERRED TAX ASSETS

The movements and components of deferred tax assets are as follows:

		The Group					
	Note	Balance at 1 January 2003 RMB'000	Recognised in income statement RMB'000	Recognised in reserve RMB'000	**Balance at 31 December 2003 RMB'000**	Recognised in income statement RMB'000	**Balance at 31 December 2004 RMB'000**
Current							
Provisions, primarily for receivables and inventories		29,675	(5,950)	—	**23,725**	2,596	**26,321**
Non-current							
Government grants	*(a)*	—	—	16,302	**16,302**	(1,318)	**14,984**
Provision for other investments		7,799	553	—	**8,352**	5,668	**14,020**
Land use rights		55,000	(1,320)	—	**53,680**	(1,320)	**52,360**
Property, plant and equipment		14,494	6,882	—	**21,376**	(1,790)	**19,586**
		106,968	165	16,302	**123,435**	3,836	**127,271**

		The Company					
	Note	Balance at 1 January 2003 RMB'000	Recognised in income statement RMB'000	Recognised in reserve RMB'000	**Balance at 31 December 2003 RMB'000**	Recognised in income statement RMB'000	**Balance at 31 December 2004 RMB'000**
Current							
Provisions, primarily for receivables and inventories		19,490	(5,950)	—	**13,540**	1,680	**15,220**
Non-current							
Government grants	*(a)*	—	—	16,302	**16,302**	(1,318)	**14,984**
Provision for other investments		7,799	553	—	**8,352**	5,668	**14,020**
Land use rights		55,000	(1,320)	—	**53,680**	(1,320)	**52,360**
Property, plant and equipment		14,494	6,882	—	**21,376**	(1,790)	**19,586**
		96,783	165	16,302	**113,250**	2,920	**116,170**

20. DEFERRED TAX ASSETS *(continued)*

(a) According to the Company's IFRS accounting policy (note 2(o) refers) regarding government grants, capital-based government grants are offset against cost of the asset to which the grants related. However, for tax purposes, such government grants could not be offset against the cost of the asset but should be treated as a non-taxable item and credited to capital reserve. The difference between the carrying amount of the asset, reduced by the amount of the government grants received, and its tax base is a temporary difference and gives rise to a deferred tax asset. The deferred tax is credited directly to capital reserve.

(b) The Group has not recognised deferred tax assets in respect of the unutilised tax losses of certain subsidiaries amounting to RMB7,801,000 (2003: RMB6,467,000). Except for this, there is no other significant deferred tax asset or liability that has not been provided for in the financial statements.

21. INVENTORIES

	The Group		**The Company**	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Raw materials	**674,824**	634,212	**674,824**	634,212
Work in progress	**725,606**	526,188	**725,606**	526,188
Finished goods	**479,366**	304,808	**479,366**	304,808
Spare parts and consumables	**136,445**	144,050	**34,410**	56,475
	2,016,241	1,609,258	**1,914,206**	1,521,683

As at 31 December 2004, the carrying amount of the Group's and the Company's inventories carried at net realisable value amounted to RMB107,799,000 (2003: RMB80,884,637).

22. TRADE RECEIVABLES — THIRD PARTIES

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Bills receivable	**137,202**	177,095	**110,680**	160,887
Accounts receivable	**93,918**	91,956	**69,666**	79,593
	231,120	269,051	**180,346**	240,480
Less: Allowance for doubtful accounts	**(1,103)**	(1,264)	**—**	(529)
	230,017	267,787	**180,346**	239,951

The ageing analysis of trade receivables — third parties (before allowance for doubtful accounts) is as follows:

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Invoice date:				
Within one year	**228,890**	267,557	**180,346**	239,951
Between one and two years	**1,607**	329	**—**	—
Between two and three years	**6**	—	**—**	—
Over three years	**617**	1,165	**—**	529
	231,120	269,051	**180,346**	240,480

Sales are generally on a cash term. Subject to negotiation, credit is generally only available for major customers with well-established trading records.

23. OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS

Other receivables, deposits and prepayments of the Group and the Company expected to be recovered after more than one year is RMB86,144,073 (2003: RMB108,794,000).

24. AMOUNTS DUE FROM ASSOCIATES AND JOINTLY CONTROLLED ENTITY

The amounts due from associates and jointly controlled entity are unsecured, interest free and have no fixed repayment terms.

25. AMOUNTS DUE FROM PARENT COMPANIES AND FELLOW SUBSIDIARIES

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade balances	**616,056**	402,586	**615,690**	402,586
Non-trade balances	**153,778**	116,639	**7,311**	9,130
	769,834	519,225	**623,001**	411,716

The amounts due from parent companies and fellow subsidiaries are unsecured, interest free and have no fixed repayment terms. All the trade and non-trade balances aged less than one year.

26. DEPOSITS WITH BANKS AND CASH AND CASH EQUIVALENTS

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash at bank and in hand	**1,994,534**	1,021,069	**1,943,974**	993,965
Time deposits with an initial term of less than three months	**100,000**	7,449	**100,000**	7,449
Cash and cash equivalents	**2,094,534**	1,028,518	**2,043,974**	1,001,414
Time deposits with an initial term over three months	**40,806**	31,121	**30,000**	30,000
	2,135,340	1,059,639	**2,073,974**	1,031,414

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

27. BANK LOANS

(a) Bank loans as at 31 December 2004 were unsecured and repayable as follows:

	The Group and the Company	
	2004	2003
	RMB'000	RMB'000
Within 1 year or on demand		
Current portion of long-term bank loans	430,000	884,200
After 1 year but within 2 years	320,000	430,000
After 2 years but within 5 years	—	380,000
	320,000	810,000
	750,000	1,694,200

All the bank loans as at 31 December 2004 were denominated in Renminbi.

(b) The interest rates and terms of repayment of long-term bank loans are as follows:

			The Group and the Company	
Long-term bank loans	**Interest rate**	**Interest type**	2004	2003
			RMB'000	RMB'000
Due in 2004	5.04% – 6.12%	Floating	—	884,200
Due in 2005	5.22% – 5.49%	Floating	430,000	430,000
Due in 2006	5.05% – 5.22%	Floating	320,000	380,000
Total long-term bank loans			750,000	1,694,200
Less: Current portion of long-term bank loans			(430,000)	(884,200)
Non-current portion of long-term bank loans			320,000	810,000

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

28. TRADE PAYABLES — THIRD PARTIES

The maturity analysis of trade payables — third parties is as follows:

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Due within 1 month or on demand	**481,548**	896,817	**281,560**	796,414
Due after 1 month and within 6 months	**190,024**	160,593	**76,176**	146,828
	671,572	1,057,410	**357,736**	943,242

29. AMOUNTS DUE TO PARENT COMPANIES AND FELLOW SUBSIDIARIES

		The Group		The Company	
		2004	2003	**2004**	2003
	Note	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Trade balances	*(a)*	**829,056**	81,228	**828,690**	35,891
Non-trade balances	*(b)*	**362,665**	177,937	**234,648**	121,111
		1,191,721	259,165	**1,063,338**	157,002

(a) The maturity analysis of the trade balances included in the amounts due to parent companies and fellow subsidiaries is as follows:

	The Group		The Company	
	2004	2003	**2004**	2003
	RMB'000	RMB'000	**RMB'000**	RMB'000
Due within 1 month or on demand	**828,040**	81,228	**827,674**	35,891
Due after 1 month and within 6 months	**1,016**	—	**1,016**	—
	829,056	81,228	**828,690**	35,891

(b) All the non-trade balances are unsecured, interest free and have no fixed repayment terms.

30. SHARE CAPITAL

	The Group and the Company	
	2004	2003
	RMB'000	RMB'000
Authorised:		
1,800,000,000 state-owned shares of RMB1.00 each	**1,800,000**	1,800,000
1,381,000,000 H shares of RMB1.00 each	**1,381,000**	1,381,000
	3,181,000	3,181,000
Issued and fully paid:		
1,800,000,000 state-owned shares of RMB1.00 each	**1,800,000**	1,800,000
723,754,468 H shares of RMB1.00 each	**723,755**	723,755
	2,523,755	2,523,755

State-owned shares and H shares rank pari passu in all material respects, except that the shareholders of the state-owned shares are restricted to the legal persons, while the shareholders of H shares are restricted to investors outside the PRC. In addition, dividends on the state-owned shares are payable in Renminbi, while dividends on H shares are payable in Hong Kong dollars.

31. RESERVES AND RETAINED EARNINGS

(a) According to the Articles of Association of the Company and its subsidiaries in the PRC, each of these entities is required to transfer 10% of its profit after taxation, as determined in accordance with the PRC Accounting Rules and Regulations, to the statutory surplus reserve ("SSR") until the reserve balance reaches 50% of its registered capital. The transfer to this reserve must be made before distribution of dividends to shareholders of these entities.

The SSR can be used to make good its previous years' losses, if any, or to expand its production and operation, and may be converted into share capital by the issue of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of its registered capital.

31. RESERVES AND RETAINED EARNINGS *(continued)*

(b) According to the Articles of Association of the Company and its subsidiaries in the PRC, each of these entities is required to transfer 5% to 10% of its profit after taxation, as determined in accordance with the PRC Accounting Rules and Regulations, to the statutory public welfare fund ("SPWF"). This fund can only be utilised on capital items for the collective benefits of its employees such as the construction of dormitories, canteen and other staff welfare facilities. This fund is non-distributable other than in liquidation. The transfer to this fund must be made before distribution of dividends to shareholders of these entities. The Board of Directors of the Company has resolved to transfer 10% (2003: 10%) of its current year's profit after taxation to the SPWF.

(c) The transfer to the discretionary surplus reserve ("DSR") from profit after taxation is subject to the approval by shareholders at Annual General Meeting. Its usage is similar to that of SSR.

The Company has proposed to transfer RMB1,000,000,000 of its profit after taxation to this reserve in respect of the financial year 2004 (2003: RMB nil). The Company's subsidiaries have proposed not to transfer any of its profit after taxation to this reserve in respect of the financial year 2004 (2003: RMB11,682,000).

(d) According to the Company's Articles of Association, the amount of retained earnings available for distribution to shareholders of the Company is the lower of the amount determined in accordance with the PRC Accounting Rules and Regulations and the amount determined in accordance with IFRS. At 31 December 2004, the amount of retained earnings available for distribution, which was the amount determined in accordance with the PRC Accounting Rules and Regulations, was RMB2,300,542,000 (2003: RMB1,664,776,000). After the balance sheet date, the Board of Directors proposed a final dividend of RMB529,988,438 (2003: RMB227,137,902) in respect of the financial year 2004.

(e) Effective 1 January 2002, land use rights which are included in lease prepayments are carried at historical cost less accumulated amortisation and impairment losses. Accordingly, the surplus on the revaluation of land use rights net of deferred tax asset was reversed to shareholders' equity at 1 January 2002.

(f) Before 1 January 2004, appropriation of SSR, SPWF and DSR ("three reserves") was provided by the individual legal entities respectively and the balances of these three reserves presented in the Company's consolidated financial statements reflected the total of the balances in the individual financial statements of the Company and its subsidiaries. However, according to a notice issued by State-owned Assets Supervision and Administration Commission of the State of Council on 22 October 2004, the appropriation of these three reserves in an enterprise's consolidated financial statements should be based on its consolidated profit after tax.

The effect of this change did not have a material impact on the Group's financial condition and results of operations in the years prior to the change. As such, certain comparative figures have been reclassified to conform with the current year's presentation.

32. RELATED PARTY TRANSACTIONS

Most of the transactions undertaken by the Group during the year ended 31 December 2004 have been effected with such counterparties and on such terms as have been determined by the Company's immediate parent company, Sinopec Corp, and other relevant PRC authorities. Sinopec Corp negotiates and agrees the terms of crude oil supply with suppliers on a group basis, which is then allocated among its subsidiaries, including the Group, on a discretionary basis.

(a) Major transactions between the Group with Sinopec Corp or Sinopec Group Company are as follows:

	Note	**2004** **RMB'000**	2003 RMB'000
Research and development expenses	*(i)*	**—**	35,000
Research and development subventions received	*(i)*	**—**	7,820
Insurance premium expenses	*(ii)*	**54,150**	44,714
Safety insurance fund received	*(iii)*	**16,831**	18,271

(i) The Group paid Sinopec Corp for research and development expenditures in accordance with the provisions of an agreement between the Group and Sinopec Corp in 2003. Also, the Group undertook certain research and development projects for Sinopec Corp. During 2004, the Group undertook research and development projects itself in accordance with Sinopec Corp's instructions and no such expenses paid or payable to Sinopec Corp were incurred.

(ii) Pursuant to administrative measures issued by Sinopec Corp, the Group maintains insurance coverage with a subsidiary of Sinopec Group Company, which cover the Group's buildings, machinery, equipment and inventories. The insurance premium expenses are calculated based on certain percentage of the carrying value of the Group's assets covered.

(iii) Safety insurance fund received from Sinopec Group Company can only be utilised to enhance the Group's security and safety measures or to conduct specified researches.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

32. RELATED PARTY TRANSACTIONS *(continued)*

(b) Major transactions between the Group with the related companies under Sinopec Corp or Sinopec Group Company are as follows:

	2004 RMB'000	2003 RMB'000
(i) Sinopec Yizheng Chemical Fibre Company Limited		
Sales of products — paraxylene	**1,771,026**	293,474

	2004 RMB'000	2003 RMB'000
(ii) Others		
Sales of products and service fee income	**30,353,232**	21,071,622
Import of crude oil through related companies	**14,853,070**	6,162,495
Purchase of crude oil	**—**	2,102,218
Purchase of equipment and related service fee charges	**403,722**	830,863
Construction fee expense	**384,102**	346,829
Service fee charges in relation to import and export of crude oil	**74,551**	46,492
Operating lease expense in respect of land	**12,634**	—
Interest income, net	**1,464**	735

(c) Major transactions between the Group with its associates and jointly controlled entity are as follows:

	2004 RMB'000	2003 RMB'000
Sales of products	**3,530,382**	936,221

32. RELATED PARTY TRANSACTIONS *(continued)*

(d) Settlement account with a related company:

	2004 RMB'000	2003 RMB'000
Balance of settlement account	**1,626,615**	669,334

The balance of the settlement account with a related company mainly represents the proceeds from sales of certain petroleum products made to a sales subsidiary of Sinopec Corp.

Balances of amounts due from/to parent companies, fellow subsidiaries, associates and jointly controlled entity have been disclosed on the face of the Group's consolidated balance sheet and the Company's balance sheet.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the ordinary course of business and on normal commercial terms or in accordance with the terms of agreements governing such transactions.

33. SEGMENT REPORTING

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

33. SEGMENT REPORTING *(continued)*

(a) Business segments

The Group conducts the majority of its business activities in two areas, refining and chemicals. An analysis of business segments is as follows:

	2004			
	Refining RMB'000	Chemicals RMB'000	Elimination RMB'000	Total RMB'000
Net sales	39,846,725	1,078,243	(586,986)	40,337,982
Cost of sales	(35,744,133)	(811,440)	586,986	(35,968,587)
Gross profit	4,102,592	266,803	—	4,369,395
Other operating income				76,820
Selling and administrative expenses				(531,995)
Other operating expenses				(100,008)
Net loss on disposal of property, plant and equipment				(28,202)
Profit from operations				3,786,010
Net financing costs				(73,653)
Share of profits less (losses) from associates and jointly controlled entity				53,077
Profit from ordinary activities before taxation				3,765,434
Income tax expense				(1,152,075)
Profit from ordinary activities after taxation				2,613,359
Minority interests				(71)
Profit attributable to shareholders				2,613,288
Other segment information				
Segment assets	12,029,167	1,030,840	—	13,060,007
Unallocated assets				2,432,772
Total assets				15,492,779
Segment liabilities	3,584,125	120,000	—	3,704,125
Unallocated liabilities				372,543
Total liabilities				4,076,668
Capital expenditure	1,426,419	20,203	—	1,446,622
Depreciation	944,560	88,319	—	1,032,879

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

33. SEGMENT REPORTING *(continued)*

(a) Business segments *(continued)*

	2003			
	Refining RMB'000	Chemicals RMB'000	Elimination RMB'000	Total RMB'000
Net sales	27,716,100	648,643	(455,765)	27,908,978
Cost of sales	(25,569,853)	(514,571)	455,765	(25,628,659)
Gross profit	2,146,247	134,072	—	2,280,319
Other operating income				59,593
Selling and administrative expenses				(511,645)
Other operating expenses				(40,178)
Net loss on disposal of property, plant and equipment				(22,506)
Employee reduction expenses				(69,184)
Profit from operations				1,696,399
Net financing costs				(81,907)
Share of profits less (losses) from associates and jointly controlled entity				(4,898)
Profit from ordinary activities before taxation				1,609,594
Income tax expense				(521,565)
Profit from ordinary activities after taxation				1,088,029
Minority interests				(42)
Profit attributable to shareholders				1,087,987
Other segment information				
Segment assets	10,878,001	1,178,823	—	12,056,824
Unallocated assets				1,431,761
Total assets				13,488,585
Segment liabilities	3,478,171	613,954	—	4,092,125
Unallocated liabilities				164,965
Total liabilities				4,257,090
Capital expenditure	1,978,364	590,584	—	2,568,948
Depreciation	808,126	36,179	—	844,305

33. SEGMENT REPORTING *(continued)*

(a) Business segments *(continued)*

The above segment information is presented in respect of the Group's business segments. The format of which is based on the Group's management and internal reporting structure.

Inter-segment transfer pricing is based on cost plus an appropriate margin, as specified by Sinopec Corp's policy.

Segment assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise cash and cash equivalents, deposits with banks, corporate assets and liabilities.

Segment capital expenditure is the total costs incurred during the year to acquire property, plant and equipment and projects in progress that are expected to be used for more than one year.

The Group conducts the majority of its business activities in two areas, refining and chemicals. The specific products of each segment are as follows:

(i) The refining segment is principally engaged in the production and sale of petroleum, intermediate petrochemical and other petrochemical products. Gasoline, diesel and kerosene are three major products of the segment.

(ii) The chemical segment is principally engaged in the production and sale of urea.

(b) Geographical segments

In presenting information on the basis of geographical segments, segment net sales is based on the geographical location of customers. No segment assets and capital expenditure are disclosed as all the assets of the Group are located in the PRC.

	2004 RMB'000	2003 RMB'000
Net sales:		
— Domestic sales in Mainland China	40,337,982	25,197,291
— Export sales to other countries or regions	—	2,711,687
	40,337,982	27,908,978

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

34. COMMITMENTS

(a) Capital commitments

Capital commitments relate primarily to construction of buildings, plant, machinery, purchase of equipment and capital contributions to investments. The Group and the Company had capital commitments outstanding at 31 December 2004 not provided for in the financial statements as follows:

	The Group and the Company	
	2004	2003
	RMB'000	RMB'000
Contracted for	**195,307**	353,076
Authorised but not contracted for	**21,118**	283,197
	216,425	636,273

(b) Lease commitments

At 31 December 2004, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group and the Company	
	2004	2003
	RMB'000	RMB'000
Within 1 year	**8,354**	7,791
After 1 year but within 5 years	**33,415**	31,166
After 5 years	**350,384**	334,167
	392,153	373,124

The Group leases land in the PRC under operating leases. The leases run for an initial period of 25 to 50 years and lease payments are fixed. None of the leases includes contingent rentals.

35. FINANCIAL INSTRUMENTS

(a) Financial risk factors and financial risk management

Financial assets of the Group and the Company include cash and cash equivalents, deposits with banks, other investments, trade and other receivables, and amounts due from parent companies and fellow subsidiaries. Financial liabilities of the Group and the Company include bank loans, trade and other payables, and amounts due to parent companies and fellow subsidiaries. The Group does not hold or issue financial instruments for trading purposes. The Group had no positions in derivative contracts that are designated and qualified as hedging instruments at 31 December 2004 and 2003.

(i) Interest rate risk

The interest rates and terms of repayment of bank loans of the Group and the Company have been disclosed in note 27.

(ii) Credit risk

Deposits with banks

The Group's financial instruments do not represent a concentration of credit risk because the Group deals with a variety of major financial institutions with good credit ratings.

Trade and other receivables

Majority of the Group's sales were made to group companies of Sinopec Corp. Credit risks with other customers were controlled by establishing credit limits and credit terms based on periodic review of their creditability.

(iii) Foreign currency risk

The Group has foreign currency risk as dividend paid to H share shareholders was in Hong Kong dollars. Depreciation or appreciation of Renminbi against foreign currencies will affect the Group's financial position and results of operations.

Notes to the Financial Statements *(continued)*

for the year ended 31 December 2004

35. FINANCIAL INSTRUMENTS *(continued)*

(b) Fair value

The following table presents the carrying amount and fair value of the Group's long-term bank loans at 31 December 2004:

	2004		2003	
	Carrying amount RMB'000	Fair value RMB'000	Carrying amount RMB'000	Fair value RMB'000
Liabilities				
Long-term bank loans	750,000	746,780	1,694,200	1,692,754

The fair value of long-term bank loans are estimated based on applying a discounted cash flow using current market interest rates for similar financial instruments.

Other investments are unquoted interests. There is no quoted market price for such other investments in the PRC, and accordingly a reasonable estimate of fair value could not be made without incurring excessive costs.

The fair values of cash and cash equivalents, trade and other receivables, trade and other payables and the amounts due from/to parent companies and fellow subsidiaries are not materially different from their carrying amounts.

The carrying amount of deposits with banks is estimated to approximate its fair value based on the nature or short-term maturity of this instrument.

Fair value estimates are made at a specific point in time and based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

36. CONTINGENT LIABILITIES

At 31 December 2004, the Company provided bank loan guarantees amounting to RMB50,000,000 (2003: RMB110,000,000) to an associate of the Group.

37. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year's presentation. Further details are set out in note 31(f).

38. PARENT COMPANIES

The directors consider the immediate parent company and the ultimate parent company at 31 December 2004 to be Sinopec Corp and Sinopec Group Company respectively, which are established in the PRC.