Scope of the principal business of the Group and its operating conditions

The principal activities of the Group include cargo shipping. Cargo shipping mainly consists of the shipment of oil and dry bulk cargoes (primarily coal) along the coast of the PRC.

In 2004, the growth rate of the global economy was 5 per cent due to the further economic recovery, which has correspondingly led to the increase in demand for energy and shipping capacity. The international shipping market remained robust and the freight rate index kept increasing. On the other hand, the PRC domestic economy sustained a steady improvement in 2004. The GDP growth rate for 2004 was 9.5 per cent as compared with 2003. The demand for oil and coal shipping in the domestic shipping market was strong, and the shipping capacity was short in supply. The Group took advantage of the favourable opportunity of the steady improvement in both international and domestic shipping market. By making readjustment to its operation strategies and shipping capacity, and by spending substantial efforts in controlling its operating costs, the Group made further improvement in its operating profit. The growth of the operating results of the Group continued to be strong. During the Reporting Period, the volume of cargo undertaken by the Group was 113,340,000 tons, and the shipping volume was 115.9 billion tonne-nautical miles, increasing by 7% and 13% respectively as compared with the same period of last year. The total revenue derived from shipment was RMB6.14 billion (after operation tax and supplementary duty, the same in the following), and the net profit was RMB1.84 billion, increasing by 26% and 80% respectively as compared with the same period of last year.

Analysis of the principal operations

An analysis of the principal operations in terms of products transported (Unit: RMB'000):

Segments	Turnover Rmb'000	Operating costs Rmb'000	Gross profit margin %	Increase/ (decrease) in turnover %	Increase/ (decrease) in operating costs %	Increase/ (decrease) in gross profit margin %
Oil Shipment	3,673,786	2,323,039	37	13	7	13
Coal Shipment	1,720,253	1,107,664	36	61	34	59
Others	741,945	333,688	55	28	(21)	100
Total	6,135,984	3,764,391	39	26	10	30

Segments	Turnover Rmb'000	Proportion of turnover from principal operations	Profit Rmb'000	Proportion of turnover from principal operations
Domestic transportation	3,733,349	61%	1,389,895	59%
International transportation	2,402,635	39%	981,698	41%

(1) Oil Transportation

Oil transportation has been one of the Group's core businesses and will be the focus for further development. In 2004, the global demand for oil kept on increasing significantly, and the overall oil shipping market was favorable to the operation of the Group. During the Reporting Period, the volume of oil shipped by the Group was 53.01 billion tonne-nautical miles, and the revenue derived from oil shipment was RMB 3.67 billion, increased by 6.4 per cent and 13.4 per cent respectively as compared with 2003.

In 2004, the volume of crude oil imported by China increased significantly due to the fast growth in the economy of China. For shipping oil products in the PRC, the significant increase in the imported crude oil drove upward the transshipment of imported crude oil along the domestic coast in the PRC. The Group made use of increasing opportunities arising from transshipment of imported oil. By fully leveraging on the advantages of cross-shipment within and outside the PRC, the Group improved the shipping efficiency, and minimised the adverse impact led by the commencement of Ningbo-Shanghai-Nanjing oil pipeline. In 2004, the shipping volume of transshipped crude oil carried by the Group was 4.37 billion tonne-nautical miles, and the revenue arising from transshipment business of imported crude oil was RMB 770 million, increasing by 4.7 per cent and 4.4 per cent respectively as compared with 2003. The shipping volume of offshore crude oil in the PRC kept on increasing due to the opening of the new oil fields in Bo Hai Bay. The Group enhanced communication with China National Offshore Oil Corp ("CNOOC") and made full use of its superiority on shipping capacity, so as to stabilize its share in the offshore crude oil shipping market. In 2004, the Group achieved a shipping volume of 9.67 billion tonne nautical miles of offshore oil, and also achieved a revenue of RMB910 million derived from such shipping business, increasing by 19.2 per cent and 27.9 per cent, respectively, as compared with 2003.

The Group's revenue from the shipment of foreign trade oil increased due to improved market analysis and corresponding measures taken by the Group. In 2004, the oil supply was sufficient and the freight rates remained at high level. The Group took advantage of such favourable opportunity, and actively explored the foreign trade oil shipping market. In 2004, with several new oil tankers coming into operation, the Group focused on preparation of the shipping routes for the new oil tankers. By making active exploration of the market of import and export oil shipment and third country shipment, the Group improved its operating efficiency. In 2004, the Group achieved a shipping volume of 35.67 billion tonne-nautical miles, and also achieved a revenue of RMB1.72 billion increasing by 9.8 per cent and 25.6 per cent respectively as compared with 2003.

(2) Dry Bulk Cargo Transportation

The dry bulk cargoes shipped by the Group mainly consist of coal, as well as ores, fertilisers, grain and other large volume bulk cargoes. In 2004, due to the short supply of electricity in the PRC, the demand for both thermal coal and shipping capacity kept on increasing significantly, which in turn drove upward the increase of freight rate. The Group made active adjustment on the allocation of its shipping capacity according to the cargo supply, and raised the freight rate of coal along the domestic coast. In addition, the Group enhanced the communication with the cargo owners and port authorities, so as to improve its shipping efficiency. In 2004, the Group achieved a total shipping volume of coal of 43.25 billion tonne-nautical miles, and achieved a revenue of RMB1.72 billion derived from such shipment business, increasing by 34.9 per cent and 61.2 per cent respectively as compared with 2003.

During the Reporting Period, both domestic and international bulk shipping market kept on improving. Both the Baltic Dry Bulk Freight Index (the "BDI") and the PRC coastal bulk freight index remained at high level. By fully leveraging on the advantages of cross-shipment within and outside the PRC, the Company arranged various domestic bulk carriers to undertake the international shipping business for the higher freight rate. As a result, the Group achieved satisfactory operating results in dry bulk shipment. In 2004, the Group achieved a total shipping volume of dry bulk cargo of 19.68 billion tonne nautical miles, representing a decrease of 5.1 per cent as compared with 2003 and achieved a total revenue of RMB0.74 billion from such dry bulk shipment, representing an increase of 28.2 per cent as compared with 2003.

Operation of the jointly-controlled and invested entities

The jointly-controlled entities established by the Company and its major customers have played an active role in stabilizing and enhancing the Company's market share. By taking advantage of its close affiliation with the Company's major customers, the Company's shipping capacity has improved. Through co-operation with large cargo owners, the Company further established and improved its market share in the shipping market.

Name	Date and place of incorporation registration and operation	Legal status	Percentage of equity attributable to the Company (%)	Registered capital	Principal activities
China Shipping Development (Hong Kong) Marine Co., Limited	2001.11.14 Hong Kong, the PRC	Limted liability company	100	USD500,000	International ocean cargo transportation, ship leasing, ship repair, shipping agency, cargo forwarding, supply of ship spare parts, supply of bunker, materials and food, trade.
Hainan Haixiang Investment Co., Ltd.	1993.11.8 Hainan, the PRC	Limted liability company	95	Rmb101,000,000	Coastal and middle and lower reaches of Yangtze River cargo transportation, refined oil transportation, ship repair and leasing.
Zhuhai New Century Marine Co., Ltd.	2001.9.25 zhuhai, the PRC	Limted liability company	50	Rmb90,000,000	Coastal and middle and lower reaches of Yangtze River cargo transportation, domestic trade (excluding the goods controlled by the state).
Shanghai Friendship Marine Co., Ltd.	2001.11.12 Shanghai, the PRC	Limted liability company	50	Rmb20,000,000	Coastal and middle and lower reaches of Yangtze River cargo transportation, foreign trade, entrepot trade.

Financial analysis

In 2004, the Group made some effective measures to increase its major operating revenue; on the other hand, the Group continued to implement its overall control on the operating costs. In 2004, the total operating costs of the Group was RMB3.76 billion, representing an increase of 10 per cent as compared with 2003, far lower than the growth rate of operating revenue of 26 per cent.

Since the beginning of 2004, with the recovery of the world economy, the demand for oil further increased. Meanwhile, the unstable situation in the Middle East, and the decision made by Organization of the Petroleum Exporting Countries for decreasing oil output, led to the high level in international crude oil price.

As part of the countermeasures against the significant increase in fuel prices, the Group strengthened its evaluation of the vessels in respect of their full-saving performance. On the other hand, more efforts were put into the renovation and application of energy-saving technologies to its vessels. The Group also carefully increased the proportion of fuel oil used, and would choose ports with lower fuel prices for filling (as appropriate) based on the routes of the vessels. In 2004, the fuel cost of the Group was RMB 1.26 billion, representing an increase of 17.5 per cent as compared with 2003, and accounting for 33.4 per cent of the total operating costs of the Group. In addition, the Group also made effective measures to successfully control the increased rate of port charges, maintenance costs and other major operating costs.

a. Liquidity

During the Reporting Period, the net cash inflow from operating activities of the Group increased from RMB1,880,940,000 for the corresponding period in 2003 year to RMB2,792,883,000, representing an increase of 48.5%. The increase of net cash inflows was mainly due to the increase in principal operations and favourable condition in respect of recovery of funds. The cash and cash equivalents of the Group were RMB 1,275,622,000 as at 31 December 2004, increasing by 13.2% from RMB1,127,184,000 of cash and cash equivalents as at 31 December 2003.

During the Reporting Period, the commitments on capital expenditures for the Group amounted to RMB4,381,222,000 (the finacial year ended 31 December 2003: RMB4,006,262,000), the source of funding was mainly financed by the Company's working capital and bank loans.

b. Capital structure

It is the intention of the Group to maintain an appropriate mix of equity and debt to ensure an efficient capital structure from time to time. As at 31 December 2004, the shareholders' equity, bank loans, other interest-bearing borrowings and finance leases payable amounted to RMB8,659,080,000, RMB2,122,322,000 and RMB120,049,000 respectively. As at 31 December 2004, the debt-to-equity ratio was 34% (31 December 2003: 33%).

Details of the bank borrowings outstanding as at 31 December 2004 were presented in Note 26 to the financial statements. As at 31 December 2004, 5.35% of the Group's bank borrowings was subject to fixed interest rates while 94.65% was subject to floating interest rates. There are no seasonal adjustments with respcet to the Group's borrowings.

As at 31 December 2004, the Group's borrowings were primarily denominated in RMB and EURO dollars, in which 5.35% of the Group's borrowings were denominated in EURO dollars. Its cash and cash equivalents were mainly held in RMB and US dollars in which 59% of the cash and cash equivalents were held in US dollars.

The Board considers that the Group's debt-to-equity ratio is maintained at a reasonable level. There is still room for debt financing with regard to the Group's further development in the future.

c. Borrowings

As at 31 December 2004, the Group's total borrowing (excluding finance leases payable) was RMB2,122,322,000, all of which was bank loans. Borrowings repayable within one year amounted to RMB294,455,000. Among the bank loans, RMB627,495,000 were guaranteed by China Shipping. Other bank loans amounting to RMB1,080,927,300 were pledged by 36 vessels owned by the Company. As at 31 December 2004, the total net book value of such vessels were RMB2,692,262,000. Interests of the above loans were calculated at the annual rate of 6.12%, 5.76%, 5.508% or 5.184%. The Group's gearing ratio was 25.4%, calculated by dividing total liabilities over total assets of the Group.

Datails of interest-bearing bank and other borrowings are presented in note 26 to the financial statements.

d. Risk on foreign currency

As at 31 December 2004, the Group's foreign exchange liabilities mainly comprised of finance lease rental payable in EURO dollars equivalent to approximately RMB120,049,000. In addition, the Company would pay dividend of H shares in Hong Kong dollars.

The Group's revenue from foreign shipment is denominated and translated into US dollars. Currently, the currency level of RMB remains stable. The Group expected that there is no significant exposure on foreign currency, but it cannot be assured operating results in future will not be affected.

e. Pledge of assets

Details of the Group's bank loans secured by assets of the Group are included in note 26 to the financial statements.

f. Contingent liabilities

Details are set out in Note 36 to the financial statements.

Prospects

In 2005, it was expected that the world economy would keep on growing, and the international shipping market would remain at high level. The Directors expect that China's domestic economy will continue to grow at a high speed, and the demand for oil, coal, ore, other energy goods and dry bulk cargoes will be strong. Thus, the domestic and foreign trade shipping volume will be increasing steadily. Especially, the coastal market demand for coal will exceed supply, with the shipping capacity falling short. This in turn will create favourable conditions for the Company in maintaining its advantages in terms of coastal transportation and a healthy development of the Company. However, following the increasing market competition of domestic coastal shipping, the Company will have to monitor closely the impact of uncertain factors such as the changes in the shipping market, the macro policies, the relevant PRC laws and regulations and the fluctuation of oil price.

The domestic demand for oil has increased significantly due to the continuous improvement in the PRC economy. It is estimated that the annual volume of imported crude oil will keep on growing and the transshipment oil supply will be further increased. The ocean oil output will be stable with room for further improvement, thereby creating conditions for the Company to further expand its ocean oil market. The six new oil tankers which the Company contracted for the construction in 2003, will be delivered into operation in 2005. It is estimated that the Company will increase its tanker shipping capacity by 644,000 dead weight tons. In 2005, the Company will continue to take advantage of its economy of scale, further enhance its cooperation with major goods ship-owners, stabilize domestic trade supply and freight rate, explore foreign trade shipping, make use of the favorable conditions brought about by the commencement of operations of six new tankers during the year, and further stabilize and expand its market share in terms of Far-east imported crude oil, product oil, and third country shipping market.

The rapid growth of the PRC economy has driven up the market demand for dry bulk shipping. The international dry bulk market has been growing strongly since 2003. Currently, the BDI reaches approximately 4,500 point. In 2005, with the further growth in Chinese economy, the demand for thermal coal shipment is expected to remain strong, and the freight rate of thermal coal shipment along domestic coast of the PRC will increase steadily. The current market situation provides a favorable foundation for the Group to achieve better operating results in 2005. In the coal and other dry bulk shipping market, the Group will continue to focus on the shipping of domestically coastal coal, fully utilize the regulating effect of domestic and foreign trade shipping capacity, make scientific review of shipping lines, accelerate the circulation of ships, actively explore different forms of cooperation, and make much efforts to further stabilise and enhance its market share. The six new bulk carriers which the Company contracted for the construction in 2002 and 2003, will be delivered into operation in 2005. It is expected that the bulk shipping capacity will increase by 342,000 tons for 2005. As a result, the Group will further increase its operating revenue and its market share in the domestic coal and dry bulk cargo shipping market.

In 2005, the Group will insist on the operating strategy of "focusing on coastal shipment and expanding ocean transportation". The Group will, through the execution of contracts of affreightment with its major customers, make best efforts to further stabilize and enhance its market share. It will keep close attention to the variation of fuel price, and adopt various measures such as control over fuel prices and energy saving of vessels in order to control cost. In addition, the Group will take various active measures to decrease its operating costs, such as maintenance costs, management expenses and port charges, so as to fulfil the target for 2005 as set by the Board.

Other Significant Events

1. Sale of assets

Sale of assets (Unit: Rmb'000)

The other party to the transaction and assets sold	Time of disposal	Sales Price	Profit/(loss) arising from disposal of assets	Connected transaction (Yes/No)	Pricing policy
Shandong Xinhe Shipping Co., Ltd (M/V "Youyi 22")	January 2004	10,450	(18,360)	No	Market price
Jiangmen Yuzhou Ship Dismantling Company of GuangDong Province (M/V "Daqing 45")	September 2004	14,327	12,035	Yes	Market price
China Shipping Industry Co., Ltd (M/V "Daqing 246")	October 2004	24,840	6,528	Yes	Market price
Shanghai Friendship Shipping Co., Ltd (M/V "Zhenfeng 8")	October 2004	49,680	39,895	No	Market price

The sale of the above vessels were carried out in accordance with the overall strategic plan of the Company's operation and development. Through the implementation of the adjustments to the Company's existing fleet composition, the Company is expected to further adapt itself to the shipping market and enhance its operational benefits.

2. Material contracts and the implementation of the contracts

(1) Pursuant to the services agreement entered into between the Company and the China Shipping, the China Shipping (or its subsidiaries) will provide to the Company the necessary supporting shipping materials and services for the ongoing operations of the Company. The details of the related business transactions for 2004 are set out in the note 40 to the financial statements.

(2) Pursuant to the Services Agreement stated in the Note 40, to the financial statements, the management charges paid by the Company to the China Shipping for the provided services was Rmb 38,960,000 during the Reporting Period (2003: Rmb45,140,000).

3. Commitment

China Shipping made the following commitment to the Company on 23 May 2001:

(1) Not to engage in competitive business with the Company; and

(2) Not to support the jointly-controlled companies to conduct the competitive business againse the Company.

China Shipping has not breached any of the above commitment during Reporting Period.

4. Information of the domestic and international auditors of the Company

During the Reporting Period, neither the domestic auditors nor the international auditors which were appointed by the Company changed. Shanghai Zhonghua Huyin C.P.A. and Ernst & Young have been appointed as the domestic and international auditors of the Company for 11 years. During the Reporting Period, the service fees payable to the above auditors were as follows:

Shanghai Zhonghua Huyin C.P.A.: auditing fee Rmb 670,000 (2003: Rmb500,000), travelling charges Rmb48,500 (2003: Rmb29,700)

Ernst & Young: auditing fees Rmb2,110,000 (2003: Rmb2,011,300)