

MANAGEMENT'S DISCUSSION AND ANALYSIS

THE FOLLOWING DISCUSSION AND ANALYSIS SHOULD BE READ IN CONJUNCTION WITH THE COMPANY'S AUDITED FINANCIAL STATEMENTS AND THE ACCOMPANYING NOTES. PART OF THE FINANCIAL INFORMATION PRESENTED IN THIS SECTION IS DERIVED FROM THE COMPANY'S AUDITED FINANCIAL STATEMENTS THAT HAVE BEEN PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRS").

1 CONSOLIDATED RESULTS OF OPERATIONS

In 2005, the Company's turnover, other operating revenues and other income were RMB 832.5 billion, and the operating profit was RMB 66.8 billion, representing an increase of 34.3% and 5.9%, respectively, over those in the previous year. These results were largely attributable to the following factors: International crude oil prices continued to be volatile and remained at a

high level; chemical products prices remained at a high level; the Company strived to mitigate the effect of the tight price control over refined oil products, proactively developed the market, increased oil and gas production, optimised crude oil processing and output structure, increased chemicals production and sales of refined oil products. In addition, the Company received a one-time compensation of RMB

9.4 billion from the central government to compensate the Company's inability to fully pass the increased crude oil costs to the refined oil products due to the tight government control over prices of domestic refined oil products, which to some extent relieved the pressures imposed by the increased crude oil costs and contributed to the comparatively good operating results.

The following table sets forth the major items in the consolidated income statement of the Company for the indicated periods.

	Years Ended 31 December		Rate of Change (%)
	2005	2004	
	(RMB in millions)		
Turnover, other operating revenues and other income	832,532	619,783	34.3
Of which: Turnover	799,115	597,197	33.8
Other operating revenues	24,002	22,586	6.3
Other income	9,415	—	N/A
Operating expenses	(765,718)	(556,714)	37.5
Of which:			
Purchased crude oil, products, and operating supplies and expenses	(653,056)	(443,590)	47.2
Selling, general and administrative expenses	(33,709)	(31,843)	5.9
Depreciation, depletion and amortisation	(31,413)	(32,342)	(2.9)
Exploration expenses (including dry holes)	(6,411)	(6,396)	0.2
Personnel expenses	(18,483)	(18,634)	(0.8)
Employee reduction expenses	(369)	(919)	(59.8)
Taxes other than income tax	(17,152)	(16,324)	5.1
Other operating expenses, net	(5,125)	(6,666)	(23.1)
Operating profit	66,814	63,069	5.9
Net finance costs	(4,621)	(4,371)	5.7
Investment income and share of profit less losses from associates	1,035	908	14.0
Profit before tax	63,228	59,606	6.1
Taxation	(19,388)	(17,815)	8.8
Profit for the year	43,840	41,791	4.9
Attributable to:			
Equity shareholders of the Company	40,920	36,019	13.6
Minority interests	2,920	5,772	(49.4)

(1) Turnover, Other Operating Revenues and Other Income

In 2005, the Company's turnover, other operating revenues and other income were RMB 832.5 billion, of which, the turnover was RMB 799.1 billion, representing an increase of 33.8% over 2004. These results were largely attributable to the increase in international prices of crude oil and chemical products, and the Company's

efforts in expanding the sales volume of our petroleum and chemical products and optimising our sales and marketing structure. In 2005, the Company's other operating revenues went up to RMB 24 billion, representing an increase of 6.3% compared with 2004.

In 2005, the Company received from the central government a one-time compensation of RMB 9.4 billion to

compensate the Company's inability to fully pass the increased crude oil costs to refined oil products due to the tight government control over prices of domestic refined petroleum products.

The following table sets forth the Company's external sales volume, average realised prices and the respective rate of changes from 2004 to 2005 for the Company's major products.

	Sales Volume (thousand tonnes)			Average realised prices (RMB per tonne, RMB per thousand cubic meters)		
	2005	2004	Rate of Change (%)	2005	2004	Rate of change (%)
Crude oil	5,289	6,012	(12.0)	2,680	1,872	43.2
Natural gas (million cubic meters)	4,356	3,775	15.4	673	609	10.5
Gasoline	30,191	27,353	10.4	4,432	3,765	17.7
Diesel	67,247	60,419	11.3	3,772	3,221	17.1
Kerosene	6,003	5,680	5.7	3,710	2,923	26.9
Basic chemical feedstock	8,658	6,664	29.9	4,846	4,429	9.4
Monomers and polymers for synthetic fiber	2,993	2,704	10.7	8,879	8,022	10.7
Synthetic resin	6,343	5,401	17.4	9,005	7,986	12.8
Synthetic fiber	1,585	1,741	(9.0)	11,123	10,818	2.8
Synthetic rubber	678	556	21.9	13,040	10,238	27.4
Chemical fertiliser	1,822	2,622	(30.5)	1,539	1,355	13.6

Most of the crude oil and a small portion of the natural gas produced by the Company were internally used for refining and chemicals production, the remaining was sold to the refineries of Sinopec Group Company and other customers. In 2005, the turnover from crude oil and natural gas that were sold externally amounted to RMB 19.9 billion, representing an increase of 24.4% over 2004, accounting for 2.4% of the Company's total turnover, other operating revenues and other income. The increase was mainly due to the increase in crude oil prices and expansion of natural gas business.

The Company's refining segment and marketing and distribution segment sell refined oil products (mainly consisting of gasoline, diesel, jet fuel, kerosene and other refined oil products) to third parties. In 2005, the external sales

revenue of refined oil products by these two segments were RMB 542.1 billion, representing an increase of 33.5% over 2004, accounting for 65.1% of the Company's turnover, other operating revenues and other income. The increase was mainly due to the rise of refined oil products price, and our proactive efforts in increasing sales volume, optimising sales and marketing structure and expanding the market of other refined oil products. The sales revenues of gasoline, diesel and kerosene were RMB 409.7 billion, representing an increase of 30.4% over 2004, and accounting for 75.6% of the total sales revenues of refined oil products. The sales revenues of other refined oil products were RMB 132.4 billion, representing an increase of 43.9% over 2004, accounting for 24.4% of the total sales revenues of refined oil products.

The Company's external sales revenues of chemical products were RMB 160.8 billion, representing an increase of 27.6% over 2004, accounting for 19.3% of the Company's total turnover, other operating revenues and other income. The increase was mainly due to the fact that the Company captured the opportunity of the high level price of chemical products and increased its sales volume accordingly.

(2) Operating expenses

In 2005, the Company's operating expenses amounted to RMB 765.7 billion, representing an increase of 37.5% compared with 2004. The operating expenses mainly consisted of the following:

Purchased Crude Oil, Products, and Operating Supplies and Expenses

In 2005, the Company's purchased crude oil, products and operating supplies and

expenses were RMB 653.1 billion, representing an increase of 47.2% over 2004, accounting for 85.3% of the total operating expenses, of which:

- Purchased crude oil expenses were RMB 338.2 billion, representing an increase of 45.4% compared with 2004, accounting for 44.2% of the total operating expenses, up by 2.4 percentage points over 2004. To meet the increasing market demands in the fast growing Chinese economy, the Company increased its throughput of crude oil purchased from third parties. In 2005, the throughput of the Company's crude oil purchased externally was RMB 107.95 million tonnes (excluding amounts processed for third parties), representing an increase of 7.3% compared with 2004. Average cost for crude oil purchased externally in 2005 was RMB 3,133 per tonne (approximately US\$ 52.11 per barrel), representing an increase of 35.5% compared with 2004.
- In 2005, the Company's other purchase expenses were RMB 314.9 billion, representing an increase of 49.2% compared with 2004, accounting for 41.1% of the total operating expenses. The increase was mainly due to the increased costs of refined petroleum products and chemical feedstock purchased externally.

Selling, general and administrative expenses

In 2005, the Company's selling, general and administrative expenses totaled RMB 33.7 billion, representing an increase of 5.9% compared with 2004. The increase was largely due to:

- An increase of RMB 1.5 billion in the selling expenses, such as transportation costs, compared with 2004, resulted from the increase in the total sales volume of refined petroleum products and chemical products, and

increased sales volume through retail and direct distribution;

- An increase of RMB 1.2 billion in operating lease expenses compared with 2004 mainly due to the increased lease of operating facilities to increase sales volume;
- A decrease in repairing and maintenance expenses by RMB 800 million, mainly as a result of the increased maintenance carried out in 2004 for petrol stations.

Depreciation, depletion and amortisation

In 2005, the Company's depreciation, depletion and amortisation were RMB 31.4 billion, down by 2.9% compared with 2004. The decrease was mainly due to disposal of, and impairment loss on, less efficient assets in the previous years.

Exploration expenses

In 2005, the Company's exploration expenses were RMB 6.4 billion, maintaining at the same level as in 2004.

Personnel expenses

In 2005, the Company's personnel expenses were RMB 18.5 billion, down by 0.8% compared with 2004. The decrease was mainly due to the reduction of operating personnel resulting from the disposal of downhole operation assets in 2004.

Employee reduction expenses

In 2005, in accordance with the Company's voluntary employee reduction plan, the Company recorded employee reduction expenses of approximately RMB 370 million.

Taxes other than income tax

In 2005, the Company's taxes other than income tax were RMB 17.2 billion, representing an increase of 5.1% compared with 2004. The increase was

largely due to the increased consumption tax and associated surcharges as a result of the increase in the sales volume of gasoline and diesel.

Other operating expenses, net

In 2005, the Company's other operating expenses, net were RMB 5.1 billion, representing a decrease of 23.1% compared with 2004. The decrease was largely due to the decrease of RMB 2.1 billion in impairment loss on long-lived assets and an increase of RMB 400 million in net losses of disposal of assets compared with 2004.

(3) Operating profit

In 2005, the Company's operating profit was RMB 66.8 billion, representing an increase of 5.9% compared with 2004.

(4) Net finance costs

In 2005, the Company's net finance costs were RMB 4.6 billion, representing an increase of 5.7% over 2004. The increase was mainly due to the following factors:

- An increase of RMB 1.3 billion in net interest expenses as a result of the increase in long term loans borrowed in accordance with the investment plans, and the increase in short term debts attributable to the increased working capital requirement, as a result of the increased crude oil price and the expansion of production and operation;
- An increase of RMB 1.1 billion in net foreign exchange gains due to fluctuation of the foreign exchange rate.

(5) Profit before income tax

In 2005, the Company's profit from ordinary activities before income tax was RMB 63.2 billion, representing an increase of 6.1% compared with 2004.

(6) Taxation

In 2005, the Company's taxation was RMB 19.4 billion, representing an increase of 8.8% compared with 2004.

(7) Profit attributable to minority interests

In 2005, the Company's profit attributable to minority interests was RMB 2.9 billion, representing a decrease of 49.4% compared with 2004. The decrease was largely due to the decreased profit in certain subsidiaries and our privatisation of Beijing Yanhua.

(8) Profit attributable to equity shareholders to the Company

In 2005, the Company's profit attributable to equity shareholders of the Company was RMB 40.9 billion, up by 13.6% over 2004.

2 DISCUSSIONS ON RESULTS OF SEGMENT OPERATIONS

The Company divides its operations into four business segments (exploration and production segment, refining segment, marketing and distribution segment and chemicals segment) and corporate and others. Unless otherwise specified, the inter-segment transactions have not been eliminated in the financial data discussed in this section. In addition, the operating revenue data of each segment have included the "other operating revenues" and "other income" of the segment.

The following table sets forth the operating revenues by each segment, the contribution of external sales and inter-segment sales as a percentage of operating revenues before elimination of inter-segment sales, and the contribution of external sales as a percentage of consolidated operating revenues (i.e. after elimination of inter-segment sales) for the periods indicated.

	Operating Revenues		As a Percentage of the Consolidated Operating Revenues Before Elimination of Inter-segment Sales		As a Percentage of the Consolidated Operating Revenues, After Elimination of Inter-segment Sales	
	Years Ended 2005	31 December 2004	2005	2004	2005	2004
	RMB in millions		(%)		(%)	
Exploration and Production Segment						
External sales ⁽¹⁾	30,607	25,253	2.2	2.5	3.7	4.1
Inter-segment sales	84,423	60,053	6.2	5.9		
Operating revenues	115,030	85,306	8.4	8.4		
Refining Segment						
External sales ⁽¹⁾	97,646	68,574	7.2	6.7	11.7	11.1
Inter-segment sales	386,456	289,699	28.3	28.5		
Operating revenues	484,102	358,273	35.5	35.2		
Marketing and Distribution Segment						
External sales ⁽¹⁾	460,650	343,595	33.8	33.8	55.3	55.4
Inter-segment sales	3,172	2,831	0.2	0.3		
Operating revenues	463,822	346,426	34.0	34.1		
Chemicals Segment						
External sales ⁽¹⁾	166,624	132,183	12.2	13.0	20.0	21.3
Inter-segment sales	12,199	12,510	0.9	1.2		
Operating revenues	178,823	144,693	13.1	14.2		
Corporate and others						
External sales ⁽¹⁾	77,005	50,178	5.7	4.9	9.3	8.1
Inter-segment sales	44,897	32,046	3.3	3.2		
Operating revenues	121,902	82,224	9.0	8.1		
Operating revenues before elimination of inter-segment sales	1,363,679	1,016,922	100.0	100.0		
Elimination of inter-segment sales	(531,147)	(397,139)				
Consolidated operating revenues	832,532	619,783			100.0	100.0

Note: (1) include other operating revenues and other income.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The following table sets forth the operating revenues, operating expenses and operating profit by each segment before elimination of the inter-segment transactions for the periods indicated, and the rate of changes from 2004 to 2005.

	Years Ended 31 December		Rate of Change (%)
	2005	2004	
	(RMB in millions)		
Exploration and Production Segment			
Operating revenues	115,030	85,306	34.8
Operating expenses	68,159	59,692	14.2
Operating profit	46,871	25,614	83.0
Refining Segment			
Operating revenues	484,102	358,273	35.1
Operating expenses	487,607	352,330	38.4
Operating (loss) profit	(3,505)	5,943	(159.0)
Marketing and Distribution Segment			
Operating revenues	463,822	346,426	33.9
Operating expenses	453,472	331,710	36.7
Operating profit	10,350	14,716	(29.7)
Chemicals Segment			
Operating revenues	178,823	144,693	23.6
Operating expenses	164,527	125,972	30.6
Operating profit	14,296	18,721	(23.6)
Corporate and others			
Operating revenues	121,902	82,224	48.3
Operating expenses	123,100	84,149	46.3
Operating loss	(1,198)	(1,925)	(37.8)

(1) Exploration and production segment

Most of the crude oil and a small portion of the natural gas produced by the exploration and production segment were used for the Company's refining and chemicals production. Most of the natural gas and a small portion of crude oil produced were sold to refineries owned by Sinopec Group Company and other customers.

In 2005, the operating revenues of this segment were RMB 115 billion, representing an increase of 34.8% over 2004, largely due to the increase in the sales price and volume of crude oil compared with those in 2004.

In 2005, this segment sold 36.86 million tonnes of crude oil and 4.44 billion cubic meters of natural gas, representing an increase of 1.7% and 14.7% respectively

compared with those in 2004. The average realised price of crude oil was RMB 2,665 per tonne (approximately US\$ 45.9 per barrel), representing an increase of 36.2% over 2004. The average realised price of natural gas was RMB 673 per thousand cubic meters, representing an increase of 9.3% compared with 2004.

In 2005, the operating expenses of this segment were RMB 68.2 billion, representing an increase of 14.2% compared with 2004. The increase was mainly due to:

- The rise of raw materials and utilities costs attributed to approximately RMB 2.2 billion in the increase of operating expenses compared with 2004;

- The increase of approximately RMB 1.6 billion in other operating expenses including expenses related to the sales of materials compared with 2004;
- The increase of RMB 1.5 billion resulted from the increased production activities in this segment to take advantage of the high crude oil price environment.
- The increase of approximately RMB 700 million in resources tax due to the change of tax rate, and the increased construction tax, education surcharges as well as mineral resources compensation fees associated with the increased sales revenues of crude oil.

In 2005, in light of the high crude oil price, the Company increased its oil production in higher cost areas, which, together with the increased water and electricity rates for oil and gas production, contributed to the increase of the lifting cost of crude oil and natural gas by 20.8% from US\$ 6.72 per barrel in 2004 to US\$ 8.12 per barrel in 2005.

In 2005, this segment's operating profit was RMB 46.9 billion, representing an increase of 83.0% compared with 2004.

(2) Refining segment

The business activities of the refining segment consist of purchasing crude oil from the exploration and production segment and third parties, processing crude oil into refined oil products, selling gasoline, diesel and kerosene to marketing and distribution segment, selling a portion of

chemical feedstock to chemicals segment and selling other refined oil products to domestic and foreign customers.

In 2005, this segment's operating revenues were approximately RMB 484.1 billion, representing an increase of 35.1% compared with 2004. The increase was

mainly due to the increased sales prices and sales volume of various refined petroleum products.

The following table sets forth the sales volumes, average realised prices and the respective rate of changes of the Company's major refined oil products of the segment from 2004 to 2005.

	Sales Volume (thousand tonnes)			Average Realised Prices (RMB per tonne)		
	2005	2004	Rate of Change (%)	2005	2004	Rate of Change (%)
Gasoline	21,520	21,420	0.5	3,763	2,977	26.4
Diesel	54,128	50,271	7.7	3,462	2,890	19.8
Chemical feedstock	26,446	23,165	14.2	3,734	2,682	39.2
Other refined petroleum products	32,724	31,710	3.2	3,121	2,583	20.8

In 2005, the sales revenues of gasoline by the segment were RMB 81 billion, representing an increase of 27.0% compared with 2004, accounting for 16.7% of this segment's operating revenues.

In 2005, the sales revenues of diesel by the segment were RMB 187.4 billion, representing an increase of 29.0% compared with 2004, accounting for 38.7% of this segment's operating revenues.

In 2005, the sales revenues of chemical feedstock by the segment were RMB 98.8 billion, representing an increase of 58.9% compared with 2004, accounting for 20.4% of this segment's operating revenues. The increase in the sales revenues of chemical feedstock was more than that in the sales revenues of gasoline and diesel, which was primarily due to the smaller increase in gasoline and diesel prices as compared with chemical feedstock prices as a result of tight government control over domestic gasoline and diesel prices. In addition, the segment also increased the sales volume of chemical feedstock.

In 2005, the sales revenues of refined petroleum products other than gasoline, diesel and chemical feedstock were RMB 102.1 billion, representing an increase of

24.7% compared with 2004, accounting for 21.1% of this segment's operating revenues.

In 2005, the operating expenses of the segment were RMB 487.6 billion, representing an increase of 38.4% compared with 2004. The increase was primarily due to the increase in crude oil price and throughput.

In 2005, the average crude oil cost was RMB 3,064 per tonne (approximately US\$ 50.96 per barrel), representing an increase of 35.5% compared with 2004. Refining throughput was 136.08 million tonnes (excluding amounts processed for third parties) in 2005, representing an increase of 5.6% compared with 2004. The total crude oil costs in 2005 were RMB 416.9 billion, representing an increase of 43.1% compared with 2004, accounting for 85.5% of the total operating expenses of the segment, up by 2.8 percentage points over 2004.

In 2005, although crude oil prices remaining at a high level; the Chinese government implemented tight control over domestic prices of refined oil products, as a result, the Company's refining segment incurred significant loss. To ensure our refining segment's normal operation, the Company

strived to lower its production cost and controlled the internal transfer prices between the different segments. In addition, through timely communication with the government, the Company received a one-time financial grant in the amount of RMB 9.4 billion. In 2005, the operating losses of the segment were RMB 3.5 billion, representing a decrease in operating profit of RMB 9.4 billion compared with 2004. The refining margin was US\$ 1.32 per barrel (defined as the sales revenues less the crude oil costs and refining feedstock costs and taxes other than income tax, divided by the throughput of crude oil and refining feedstock) in 2005, representing a decrease of US\$ 2.54 per barrel, or 65.8%, from US\$ 3.86 per barrel in 2004.

In 2005, the refining cash operating cost (defined as operating expenses less the purchase costs of crude oil and refining feedstock, depreciation and amortisation, taxes other than income tax, other business expenses and adjustments; and divided by the throughput of crude oil and refining feedstock) was US\$ 1.91 per barrel, representing a decrease of US\$ 0.07 per barrel, or 3.5%, compared with 2004. This change was mainly due to the continued reduction of costs and increased throughput in this segment.

(3) Marketing and distribution segment

The business activities of marketing and distribution segment include purchasing refined oil products from the refining segment and third parties, and wholesale selling of refined oil products to domestic customers, directly selling and retail distributing the refined oil products through the retail network owned by this segment and provision of related services.

In 2005, the operating revenues of this segment were RMB 463.8 billion, representing an increase of 33.9% compared with 2004. The increase was primarily due to the increases in sales

volume and prices of gasoline, diesel and kerosene including jet fuel, the continuous optimisation of marketing structure to further increase the percentage of retail sales in the total sales volume of gasoline and diesel.

In 2005, the operating revenues from sales of gasoline and diesel were RMB 390.2 billion, accounting for 84.1% of the operating revenues of this segment. The percentage of retail sales in the total sales volume of gasoline and diesel increased from 54.6% in 2004 to 59.5% in 2005, up by 5.0 percentage points. The percentage of sales of gasoline and diesel by direct sales

in the total sales volume decreased from 20.3% in 2004 to 19.1% in 2005, down by 1.2 percentage points. The percentage of wholesale sales in the total sales volume of gasoline and diesel decreased from 25.1% in 2004 to 21.3% in 2005, down by 3.8 percentage points.

The following table sets forth the sales volumes, average realised prices and the respective rate of changes of the four major product categories in 2004 and 2005 in different forms of sales channels for gasoline and diesel.

	Sales Volume (thousand tonnes)			Average Realised Prices (RMB per tonne)		
	2005	2004	Rate of Change (%)	2005	2004	Rate of Change (%)
Gasoline	30,319	27,508	10.2	4,430	3,762	17.8
Of which: Retail	21,629	18,416	17.4	4,562	3,911	16.6
Direct Sales	2,839	2,890	(1.8)	4,206	3,536	18.9
Wholesale	5,851	6,202	(5.7)	4,050	3,426	18.2
Diesel	67,925	61,097	11.2	3,767	3,215	17.2
Of which: Retail	36,896	29,997	23.0	3,885	3,351	15.9
Direct Sales	15,909	15,123	5.2	3,786	3,211	17.9
Wholesale	15,120	15,978	(5.4)	3,458	2,963	16.7
Kerosene	5,955	5,623	5.9	3,710	2,923	26.9
Fuel oil	13,334	9,685	37.7	2,374	1,793	32.4

In 2005, the segment's operating expenses were RMB 453.5 billion, representing an increase of 36.7% compared with 2004. The increase was mainly due to the increase in purchase expenses, of which, purchase expenses for gasoline and diesel were RMB 355.5 billion, up by 36.3% over 2004, accounting for 78.4% of the segment's operating expenses. In 2005, average purchase prices of gasoline and diesel increased by 27.3% and 20.9%, respectively, to RMB 3,844 per tonne and RMB 3,518 per tonne compared with 2004. The purchase volume of gasoline and diesel increased by 10.2% and 11.2%, respectively, compared with 2004 to 30.32 million tonnes and 67.93 million tonnes.

In 2005, the segment's cash selling cost (defined as the operating expenses less the purchasing costs, taxes other than income tax, depreciation and amortisation, and divided by the sales volume) was RMB 162.55 per tonne, representing a decrease by 2.7% compared with 2004. This decrease was primarily due to the segment's continuous effort in cost saving and the scale effect of increase in sales volume.

In 2005, the segment's operating profit was RMB 10.4 billion, representing a decrease of 29.7% compared with 2004.

(4) Chemicals Segment

The business activities of the chemicals segment include purchasing chemical feedstock from the refining segment and third parties, and producing, marketing and distribution of petrochemical products and inorganic chemical products.

In 2005, the segment's operating revenues were RMB 178.8 billion, representing an increase of 23.6% compared with 2004,

which was primarily due to the increases in prices and sales volume of major chemical products.

In 2005, the sales revenues of the Company's six major categories of chemical products (i.e. basic organic chemicals, monomers and polymers for synthetic fiber, synthetic resin, synthetic fiber, synthetic rubber and chemical fertiliser) totaled approximately RMB 159.5 billion,

representing an increase of 27.9% compared with 2004, accounting for 89.2% of the total operating revenues of this segment.

The following table sets forth the sales volume, average realised price and the respective rate of changes for each of these six categories of chemical products of this segment from 2004 to 2005.

	Sales Volume (thousand tonnes)			Average Realised Prices (RMB/Tonne)		
	2005	2004	Rate of Change (%)	2005	2004	Rate of Change (%)
Basic organic chemicals	9,509	7,384	28.8	4,828	4,292	12.5
Monomers and polymers for synthetic fiber	3,003	2,704	11.1	8,872	8,022	10.6
Synthetic resin	6,366	5,402	17.8	9,007	7,986	12.8
Synthetic fiber	1,585	1,741	(9.0)	11,123	10,818	2.8
Synthetic rubber	703	563	24.9	13,000	10,247	26.9
Chemical fertiliser	1,824	2,659	(31.4)	1,539	1,355	13.6

In 2005, the operating expenses of the segment were RMB 164.5 billion, representing an increase of 30.6% compared with 2004. The increase was primarily due to the price increases of various raw materials, the increased consumption of various raw materials and auxiliary materials, the increased utilities expenses and other variable expenses and fixed costs, all associated with the increased production of the chemical products. More specifically:

- Affected by the increase in the consumption of raw materials and their unit prices, the costs for raw materials increased by RMB 37.6 billion compared with 2004. Consumption of naphata and other cracking materials increased by 2.43 million tonnes over 2004, and unit price of raw materials was RMB 3,704 per tonne, up by RMB 1,160 per tonne over 2004.

- Due to increased sales volume of chemical products, selling expenses, such as transportation costs, increased by RMB 700 million compared with 2004.

In 2005, the segment's operating profit was RMB 14.3 billion, representing a decrease of RMB 4.4 billion compared with 2004.

(5) Corporate and others

The business activities of corporate and others mainly consist of the import and export businesses of the subsidiaries, research and development activities of the Company and managerial activities of its headquarters.

In 2005, the operating revenues of corporate and others were RMB 121.9 billion, representing an increase of 48.3% compared with 2004. The increase was due

to the fact that China Petrochemical International Co., Ltd. and its subsidiaries increased their trading volume in importing and exporting crude oil and petrochemical products and other business transactions.

In 2005, the segment's operating expenses were RMB 123.1 billion, representing an increase of 46.3% compared with 2004. The increase was primarily due to the increased purchase expenses of China Petrochemical International Co., Ltd. and its subsidiaries associated with the increase in their revenues.

The segment's operating losses were RMB 1.2 billion, representing a decrease of RMB 700 million compared with 2004.

3 ASSETS, LIABILITIES, EQUITY AND CASH FLOWS

The Company's primary sources of funding were from operating activities, short-term and long-term borrowings, and primary uses of funds were for operating expenses, capital expenditures and repayments for short-term and long-term borrowings.

(1) Assets, liabilities and equity

Unit: RMB in millions

	As of 31 December		Amount Changes
	2005 RMB millions	2004 RMB millions	
Total assets	537,321	474,594	62,727
Current assets	145,291	120,271	25,020
Non-current assets	392,030	354,323	37,707
Total liabilities	284,325	250,508	33,817
Current liabilities	170,649	146,277	24,372
Non-current liabilities	113,676	104,231	9,445
Equity attributable to equity shareholders of the Company	223,556	193,040	30,516
Share capital	86,702	86,702	—
Reserves	136,854	106,338	30,516
Minority interests	29,440	31,046	(1,606)
Total equity	252,996	224,086	28,910

The Company's total assets were RMB 537.321 billion, representing an increase of RMB 62.727 billion compared with those at the end of 2004, of which:

- The current assets increased by RMB 25.02 billion from those at the end of 2004 to RMB 145.291 billion. The increase was mainly due to the increases in inventories of crude oil and refined oil products as a result of the increase in prices and volume of crude oil and refined oil products.
- The non-current assets increased by RMB 37.707 billion from those at the end of 2004 to RMB 392.03 billion. The increase was mainly due to the increase of RMB 30.45 billion in property, plant and equipment and the increase of RMB 2.082 billion in construction in progress.

The total liabilities were RMB 284.325 billion, representing an increase of RMB 33.817 billion compared with those at the end of 2004, of which :

- The current liabilities increased by RMB 24.372 billion from those at the end of 2004 to RMB 170.649 billion. The increase was mainly due to the increase of RMB 29.175 billion in accounts payable associated with the expansion of production and operation, and the decrease of RMB 7.554 billion in bills payable resulted from adjustment of financing structures.
- The non-current liabilities increased by RMB 9.445 billion from those at the end of 2004 to RMB 113.676 billion. The decrease was mainly due to the fact that long-term loans of the Company increased by RMB 9.405 billion compared with those at the end of 2004.

The equity attributable to equity shareholders of the Company was RMB 223.556 billion, representing an increase of RMB 30.516 billion in reserves compared with those at the end of 2004.

(2) Cash flow

In 2005, the Company's cash and cash equivalent decreased by RMB 2.614 billion, which, together with the decrease of RMB 22 million due to the change in foreign exchange rates, contributed to the net decrease of RMB 2.636 billion, down from RMB 16.381 billion as of 31 December, 2004 to RMB 13.745 billion as of 31 December 2005.

The following table sets forth the major items on the consolidated cash flow statements in 2004 and 2005.

Major items of cash flows

Unit: RMB in millions

	Years Ended 31 December	
	2005	2004
Net cash flow from operating activities	76,497	69,081
Net cash flow from investing activities	(71,051)	(73,992)
Net cash flow from financing activities	(8,060)	5,028
Net (decrease)/increase in cash and cash equivalent	(2,614)	117

Net cash flow from operating activities was RMB 76.497 billion.

In 2005, profit before taxation was RMB 63.228 billion; after adjusting the non-cash expenses items, the adjusted cash flow from operating activities was RMB 105.23 billion. Major non-cash expense items included: depreciation, depletion and amortisation of RMB 31.413 billion, dry holes costs of RMB 2.992 billion, net losses from disposal of properties, plants and equipments of RMB 2.095 billion, and impairment losses on long-lived assets of RMB 1.851 billion.

The changes in operating-related accounts receivable and payable items reduced cash inflow of RMB 1.828 billion. In order to meet the market demand, the Company expanded production and operation, as a result, the working capital required by the ordinary business settlement increased, of which, the changes in inventory led to a decreased cash inflow of RMB 24.998 billion, the increase in accounts payable due to the increase in operation and purchase costs led to an increased cash inflow of RMB 28.97 billion, and the increase in accounts receivable and other assets led to a decreased cash inflow of RMB 5.8 billion.

After adjusting the non-cash expense items and accounts receivable and payable items with regard to the profit before taxation, and deducting the cash outflow for payment of income tax totaling RMB 20.998 billion, and the net cash outflow for net interests paid as well as the dividend received totaling RMB 5.907 billion, the net cash flow from operating activities was RMB 76.497 billion.

Net cash flow for investing activities was RMB 71.051 billion.

The net cash flow for investing activities mainly represented cash outflows of RMB 63.135 billion for capital expenditures and RMB 4.324 billion for acquisition of minority interests in subsidiaries such as Beijing Yanhua by the Company, and cash outflows of RMB 2.474 billion for capital expenditures by the Company's jointly controlled entities.

Net cash flow for financing activities was RMB 8.06 billion.

The net cash outflow for financing activities increased because the amount of newly added bank loans and other loans by the Company and its jointly controlled entities was less than

the amount of repayment of bank loans and other loans, resulting in a cash outflow of RMB 2.921 billion. The net cash outflow for financing activities was further increased by the distribution of final dividend for 2004 and interim dividend for 2005 totaling RMB 10.404 billion; and the distribution of cash in connection with petrochemical assets and catalyst assets totaling RMB 3.128 billion. On the other hand, the cash outflow was partially offset by the proceeds from the issuance of short term financial bonds totaling RMB 9.875 billion.

During 2005, the Company captured the opportunity of robust market demand to steadily increase cash flow from operating activities. At the same time, the Company tightened its control over integrated cash management and strictly controlled the scale of cash and cash equivalents to decrease the amount of idle cash, and accelerate capital turnover. As a result, the overall cash efficiency of the Company improved.

(3) Contingent liabilities

Refer to the descriptions under Major Guarantees and Performance in the section entitled Disclosure of Significant Events.

(4) Capital expenditure

Refer to the descriptions under Capital Expenditure in the section entitled Business Review and Prospects.

(5) Research and development expenses and environmental expenses

Research and development expenses refer to the expenses that have been recognised during the period in which they incurred. In 2005, the Company's research and development expenses were RMB 2.243 billion.

Environmental expenses refer to the normal routine pollutant discharge fees paid by the Company, excluding any capitalised costs of pollutant discharge facilities. In 2005, the Company's environmental expenses were RMB 493 million.

(6) Analysis of financial statements prepared under the PRC Accounting Rules and Regulations

The major differences between the Company's financial statements prepared

under the IFRS and those under the PRC Accounting Rules and Regulations are set out in Section C of the financial statements of the Company on pages 164 to page 165 of this report.

The following table sets forth each of its segments' income and profit from principal operations, costs of sales, taxes and surcharges, as prepared under the PRC Accounting Rules and Regulations.

Unit: RMB in millions

	Years Ended 31 December	
	2005	2004
	RMB in millions	RMB in millions
Income from principal operations		
Exploration and Production Segment	104,285	76,023
Refining Segment	469,266	352,548
Marketing and Distribution Segment	462,464	345,671
Chemicals Segment	172,982	122,118
Others	121,265	79,145
Elimination of inter-segment sales	(531,147)	(384,873)
Consolidated income from principal operations	799,115	590,632
Cost of sales, sales taxes and surcharges		
Exploration and Production Segment	40,118	36,073
Refining Segment	477,843	340,360
Marketing and Distribution Segment	427,308	306,309
Chemicals Segment	149,431	96,994
Others	118,152	78,410
Elimination of inter-segment cost of sales	(527,451)	(382,736)
Consolidated cost of sales, sales taxes and surcharges	685,401	475,410
Profit from principal operations		
Exploration and Production Segment	59,732	37,997
Refining Segment	(7,838)	12,005
Marketing and Distribution Segment	35,156	39,362
Chemicals Segment	23,551	25,123
Others	3,113	735
Consolidated profit from principal operations	113,714	115,222
Net profit	39,558	32,275

Profit from principal operation: in 2005, the Company's realised profit from principal operations was RMB 113.714 billion, representing a decrease of RMB 1.508 billion compared with 2004. The decrease was mainly due to the fact that crude oil price continued to be volatile and remained at a high level in international market, and the Chinese government implemented tight price control over domestic refined oil product, resulting in smaller increase in the price of refined oil products as compared with that in crude oil price. The Company strived to expand sales volume and

optimise marketing and distribution structures, but was still unable to completely offset the pressure from the increased crude oil costs. As a result, profit from principal operations declined compared with 2004.

Net profit: in 2005, the net profit realised by the Company was RMB 39.558 billion, representing an increase of RMB 7.283 billion, or 22.57%, over that in 2004.

Financial data prepared under the PRC Accounting Rules and Regulations:

Unit: RMB in millions

	At 31 December		Changes
	2005	2004	
Total assets	520,572	460,081	60,491
Long-term liabilities	107,774	98,407	9,367
Shareholders' funds	215,623	186,350	29,273

Analysis of changes:

Total assets: in 2005, the total assets increased by RMB 60.491 billion from those at the end of 2004 to RMB 520.572 billion. The increase was primarily due to a number of factors, of which, the fixed assets increased by RMB 32.706 billion as a result of the Company's implementation of a prudent investment policy to meet the market demands; the current assets increased by RMB 24.84 billion resulted from increases in inventories of crude oil and refined oil products in line with the rise of price and expansion of production and operation; other assets, including intangible assets, increased by RMB 2.945 billion.

Long-term liabilities: the Company's long-term liabilities were RMB 107.774 billion as of 31 December 2005, representing an increase of RMB 9.367 billion from those as of 31 December 2004, which was primarily due to the

increase in long term borrowings in line with investment plans.

Shareholders' funds: At the end of 2005, shareholders' funds of the Company was RMB 215.623 billion, representing an increase of RMB 29.273 billion compared with those at the end of 2004. This increase was primarily due to: first, the realised net profit in 2005 amounted to RMB 39.558 billion; second, in 2005, the distribution of the final dividend of 2004 amounted to RMB 6.936 billion and the interim dividend for 2005 totaled RMB 3.468 billion.

(7) Significant differences between the financial statements prepared under IFRS and U.S. GAAP

The major differences between the Company's financial statements prepared under IFRS and US GAAP are set out in Section D of the financial statements of the Company on page 166 to page 168 of this report.

