Financial Review

Introduction

CITIC Pacific's 2006 Interim Report includes a letter from the Chairman to shareholders, the interim accounts and other information required by accounting standards, legislation, and the Hong Kong Stock Exchange. This Financial Review is designed to assist the reader in understanding the statutory information by discussing the contribution of each business segment, and the financial position of the company as a whole.

Pages 22 to 26 of the Interim Report contain the Consolidated Profit and Loss Account, Balance Sheet, Cash Flow Statement and Statement of Changes in Equity. Following these financial statements, on pages 27 to 31 of the Interim Report, are Notes that further explain certain figures presented in the statements.

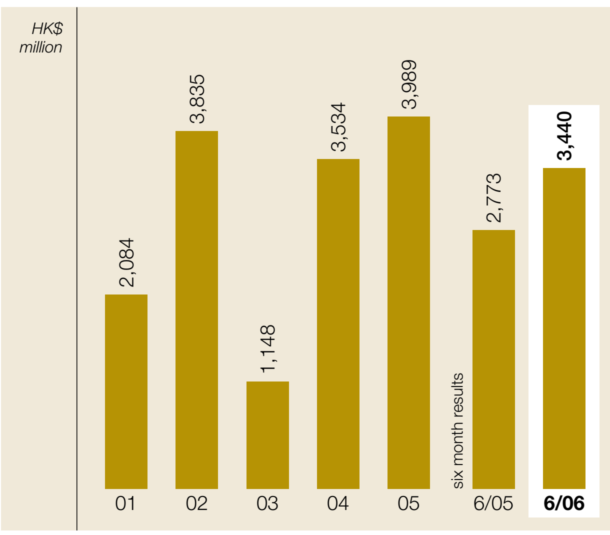
On page 32 is the report of CITIC Pacific's auditor – PricewaterhouseCoopers – of their independent review of CITIC Pacific's interim accounts.

Basis of Accounting

CITIC Pacific prepares its financial statements in accordance with generally accepted accounting standards issued by the Hong Kong Institute of Certified Public Accountants which have been converged with International Financial Reporting Standards.

Profit Attributable to Shareholders

The net profit attributable to shareholders for the six months ended 30 June 2006 was HK$3,440 million, an increase of 24% compared with HK$2,773 million for the same period in 2005. The reasons for the increase in profit are described below.



Business Segments Contribution

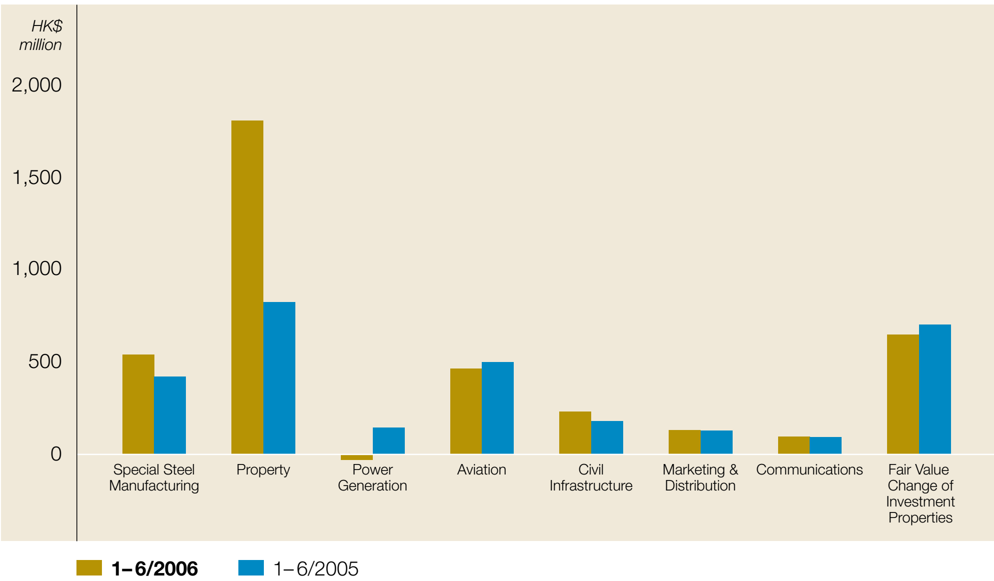
The Contribution (Note) made by major business segments in the first six months of 2006, compared with the same period of 2005, were:

	actual		change
HK$ million	**1–6/2006**	1–6/2005	2006–2005
Special Steel Manufacturing	**539**	420	119
Property	**1,803**	821	982
Power Generation	**(29)**	145	(174)
Aviation	**464**	499	(35)
Civil Infrastructure	**232**	180	52
Marketing & Distribution	**132**	128	4
Communications	**95**	92	3
Fair Value change of Investment Properties	***647***	*700*	*(53)*

Note: Please refer to Definition of Terms on page 42

Compared with the contribution for the six months ended 30 June 2005:

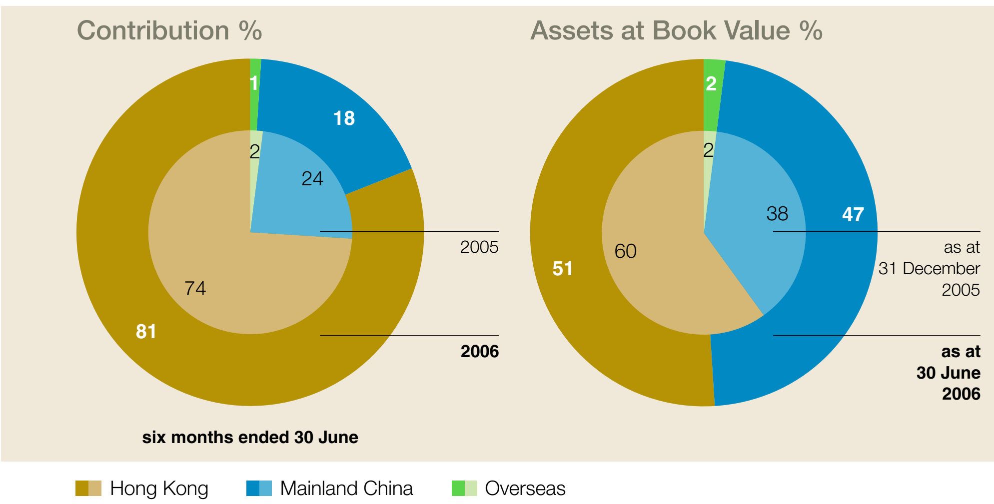
- Special steel manufacturing: Contribution increased due to continuing improved performance of Jiangyin Steel Plant and Xin Yegang Steel Plant including the contribution from Daye Special Steel which was acquired in November 2005.
- Property: Excluding the revaluation surplus of investment properties in both periods, contribution increased by 120% mainly due to the profit from the sale of 50% interest in Festival Walk and profit recognised on completion of Shanghai Westgate Garden in 2006. In the first half of 2005, there were also profits from the sales of properties including a piece of land at Hung Shui Kui in the New Territories. Rental income remained strong and stable.
- Power Generation: Excluding the impairment loss on Jilin Power Station and a loss arising from the share reform of an A share subsidiary company of North United Power Group, contribution increased by 23%.
- Aviation: Due to the continued high fuel cost, despite 13% growth in revenue, the profit of Cathay Pacific was almost the same as the first half of 2005 but Dragonair recorded a loss.
- Civil Infrastructure: Contribution from both vehicular tunnels increased. Toll charges of Eastern Harbour Tunnel was increased since May 2005.
- Marketing & Distribution: The contribution from motor business improved where the PRC market remained the major contributor to the growth. The performance of non-motor businesses during the period was affected by the challenging market and project development costs.
- Communications: Profit of CITIC Telecom 1616 increased but the rise was offset by the costs of other developing businesses. Results of CTM and Guoan were stable.
- Fair value change of investment properties: Increase in fair value of investment properties as a result of a revaluation reflecting the current market condition.



Pages 27 and 28 of the Interim Report contains business segment information for turnover and profit before net finance charges and taxation for consolidated activities, jointly controlled entities and associated companies.

Geographical Distribution

The contribution and assets between Hong Kong, mainland China and overseas is shown below based on the location of the base of each business's operations.



Interest Expense

The Group's interest expense net of amount capitalised increased from HK$240 million to HK$347 million mainly due to the increase in the amount of borrowings and the increase in the weighted average cost of debt from 3.9% to 5.0%.

Taxation

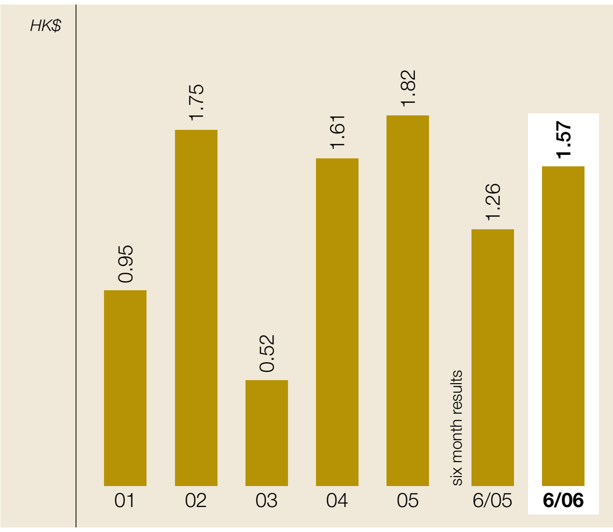
Taxation increased from HK$248 million in 2005 to HK$328 million in 2006 mainly due to increased profit.

Shareholders' Returns

CITIC Pacific's primary objective is to increase shareholder value for which it has used earnings per share as a proxy. The Company expects its businesses to provide returns on investment over their lives that will provide shareholders with an adequate return on equity.

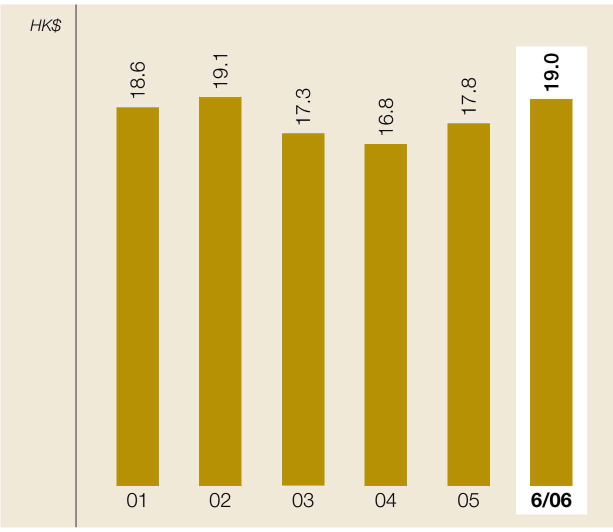
Earnings per Share

Earnings per Share was HK$1.57 for the first half of 2006, an increase of 24% compared with HK$1.26 for the same period in 2005. All the increases in Earnings per Share was attributable to the increase in profit as the number of shares outstanding in the two periods was substantially the same.



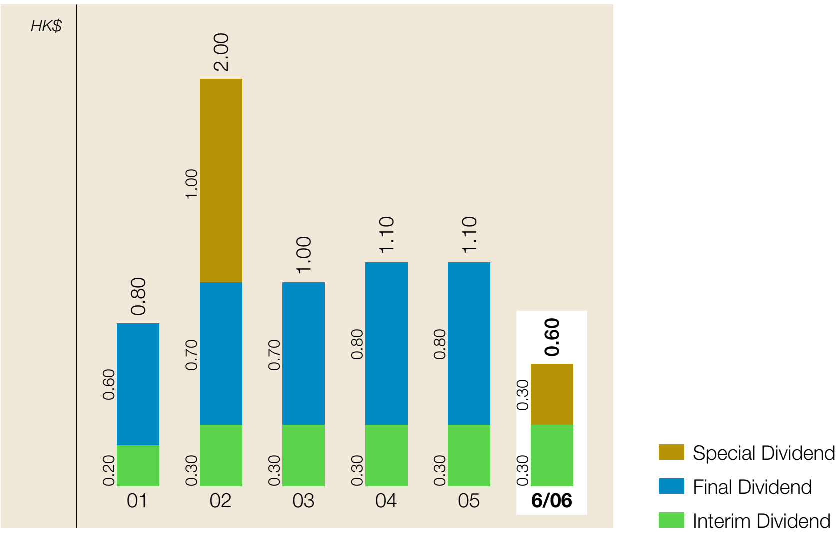
Shareholders' Funds per Share

Shareholders' Funds per share at 30 June 2006 was HK$19.0. The increase was mainly due to profit during the period.



Dividend per Share

An interim dividend of HK$0.3 per share and a special dividend of HK$0.3 is proposed for the first half of 2006.

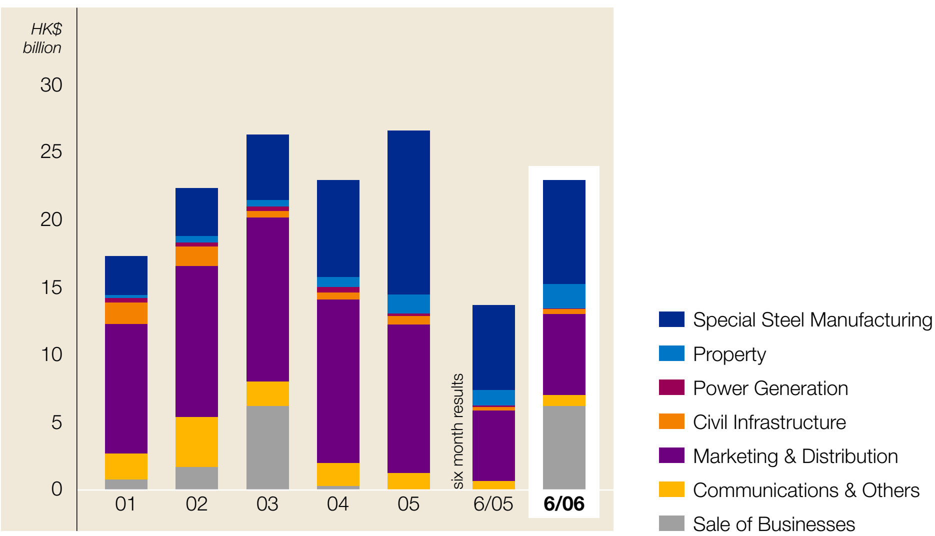


Turnover

Special Steel Manufacturing turnover increased by 22% mainly due to turnover of Daye Special Steel which was acquired in November 2005.

The proceeds on disposal of 50% interest in Festival Walk amounted to approximately HK$6 billion.

Marketing & Distribution turnover increased by 16% mainly due to increased sales in mainland China particularly for the motor business.



Capital Expenditure

The property development projects in the Mainland are continuing and the first phase of New Westgate Garden was completed during the first half of 2006.

Further capital contribution was made to Zhengzhou during the period. The construction of new power generators by Ligang Power and Zhengzhou Power are on schedule.

An investment of 12% effective interest in Kunming CGE Water Suppy Co., Ltd. was made while capital expenditures were also incurred by various existing businesses.

Others includes the deposit paid for the acquisition of the right to mine a magnetite iron ore in Australia.

As at 30 June 2006, the Group's contracted capital commitment was approximately HK$10 billion, related mainly to PRC projects of Property, Special Steel Manufacturing including the acquisition of Shijiazhuang Steel Mill, and the acquisition of magnetite iron ore mining right in Australia.

HK$ million	**1–6/2006**	1–6/2005	1–12/2005
Special Steel Manufacturing	**163**	795	2,063
Property	**976**	807	2,526
Power Generation	**174**	615	1,518
Civil Infrastructure	**127**	8	225
Marketing & Distribution	**110**	89	200
Communications	**145**	42	134
Others	**156**	514	554

Group Liquidity and Capital Resources

General Policies

The Group's policy is to maintain a high degree of financial control and transparency. Financing and cash management activities are centralised at head office level to enhance risk management, control and the best utilisation of financial resources of the Group.

We aim to diversify our funding sources through utilisation of both banking and capital markets. To the extent it is possible, financing is arranged to match business characteristics and cash flows. Limited or non-recourse project finance is employed when it is available and appropriate.

Foreign Currency Exposure

CITIC Pacific conducts business mainly in Hong Kong and mainland China, therefore it is subject to the market risk of foreign exchange rates of the HK Dollar, US Dollar and Renminbi. To minimise currency exposure, non Hong Kong dollar assets are usually financed in the same currency as the asset or cash flow from it, either by borrowing or using foreign exchange contracts. Achieving this objective is not always possible due to limitation in financial markets and regulatory constraints, particularly on investment into mainland China as the Renminbi is currently not a free convertible currency. In addition, 'Registered Capital', which usually accounts for no less than 25% of the total investment amount for projects in mainland China, is required to be paid in US or HK Dollars. As a result, CITIC Pacific has an increasing exposure to the Renminbi. As of 30 June 2006, around 47% (around HK$29 billion) of the Group's total assets were based in mainland China.

The underlying cash flow of the Group's businesses is mainly in HK dollars or in Renminbi. CITIC Pacific entered into forward contracts to minimise potential exposure to US dollar denominated debt principal and interest payments. As of 30 June 2006, such contracts outstanding amounted to US$532 million. CITIC Pacific also entered into a cross currency swap contract to hedge the JPY8.1 billion floating rate note issued in 2005 so as to limit foreign currency exposure. In addition, foreign exchange forward contracts were employed by our trading business to hedge currency fluctuations. As of 30 June 2006, such contracts outstanding amounted to HK$839 million.

Interest Rate Exposure

The Group aims to maintain a suitable mixture of fixed and floating rate borrowings in order to stabilise interest costs despite rate movements. Interest rate hedging ratio is determined after taking into consideration of the general market trend, the Group's cash flow pattern, interest coverage ratio and etc.

The Group uses interest rate swaps, forward rate agreements, interest rate option contracts and other instruments to hedge exposures or to modify the interest rate characteristics of its borrowings. As of 30 June 2006, CITIC Pacific had outstanding interest rate swap / option contracts with a notional amount of HK$10.3 billion. After the swaps, HK$6.1 billion or 33% of the Group's total borrowings were effectively paying fixed rate and the remaining were effectively paying floating rate of interest. The US Federal Reserve increased interest rate from 1% in June 2004 for 17 times consecutively to 5.25% as at end of June 2006. However, due to the Group's active interest hedging program, the overall weighted average all-in cost of debt (including fees and hedging costs) for the six months ended 30 June 2006 was maintained at around 5%, compared with 3.9% for the same period last year.

Employment of Derivative Products

The Group employs a combination of financial instruments, including derivative products, to manage its exposure to fluctuations in interest and currency rates. Derivative transactions are only used for interest rate and currency hedging purposes, speculative trading is prohibited. Counterparties' credit risks are carefully reviewed and in general, the Group only deals with financial institutions with investment grade credit rating. The amount of counterparties' lending exposure to the Group is also an important consideration as a means to control credit risk.

Following the adoption of HKAS32 and HKAS39 as described under 'Significant accounting policies', all derivatives are stated at fair market value. Certain derivative transactions, while the objective is for hedging purposes under the Group's risk management strategies, may not qualify for hedge accounting treatment under the specific rules of the new accounting standards. The changes in the fair value of such kind of derivative transactions are recognised in the profit and loss account. The fair market value of outstanding derivative transactions is calculated at least semi-annually based on the price quotations obtained from major financial institutions or the Group's own calculation where applicable.

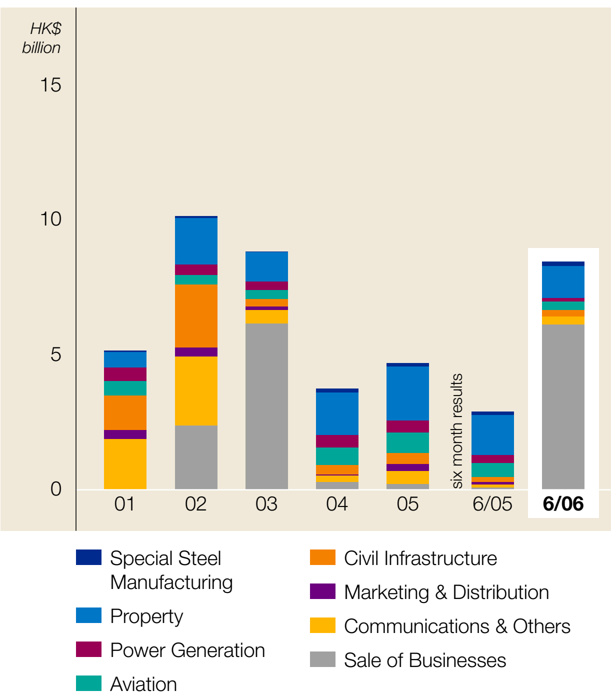
Cash Flow

By design, majority of the Group's debt is raised at the holding company level (except for project based financing or arrangements limited by regulation). As such, the actual net amount of cash flow from each business to the Group is an important indicator as to the Group's ability to service its debts. During the period, the Group's cash flow remained strong. Following is a summary of the cash contributions by each business segment:

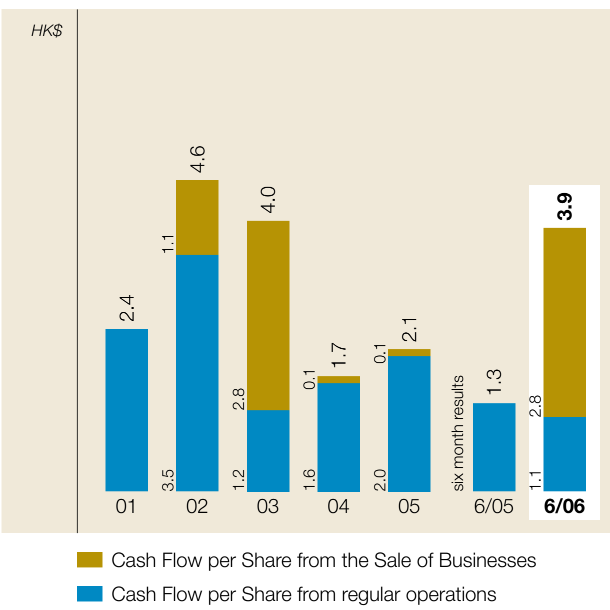
	for the six months ended 30 June	
HK$ million	**2006**	2005
Special Steel Manufacturing	**168**	143
Property	**7,317**	1,475
Power Generation	**116**	298
Aviation	**324**	534
Civil Infrastructure	**236**	169
Marketing & Distribution	**0**	93
Communications	**172**	140
Others	**60**	4
Total	**8,393**	2,856

The significant increase from property sector was mainly attributable to the disposal of Festival Walk (disposal proceeds approximately HK$6 billion) in March 2006. Civil Infrastructure sector also contributed higher cashflow thanks to the strong performance of tunnel operations. Cashflow from aviation sector dropped as higher cost of fuel affected the industry substantially. Cashflow from Power generation sector dropped as the 2005 final dividend declared by Ligang Power Station was retained for reinvestment. There was no cash contribution to the Group from Marketing & Distribution during the period as cash flow generated from operations was reinvested for new projects in the mainland.

Cash Flow from Operations



Cash Flow per Share



Summary of Consolidated Cash Flow Statement

HK$ million	for the six months ended 30 June **2006**	2005
Net Cash generated from consolidated activities	**1,186**	851
jointly controlled entities	**133**	200
associated companies	**613**	1,017
other financial assets	**9**	102
Sale of business interests and marketable securities	**7,016**	487
Capital expenditure and investment in new businesses	**(1,790)**	(2,668)
Tax	**(97)**	(87)
Net interest paid	**(387)**	(263)
	6,683	(361)
Dividends paid	**(1,755)**	(1,754)
(Decrease) / Increase in borrowings	**(3,233)**	2,310
Repurchase of shares	**(35)**	–
Share options exercised	**23**	12
	(5,000)	568
Increase in cash and cash equivalents	**1,683**	207

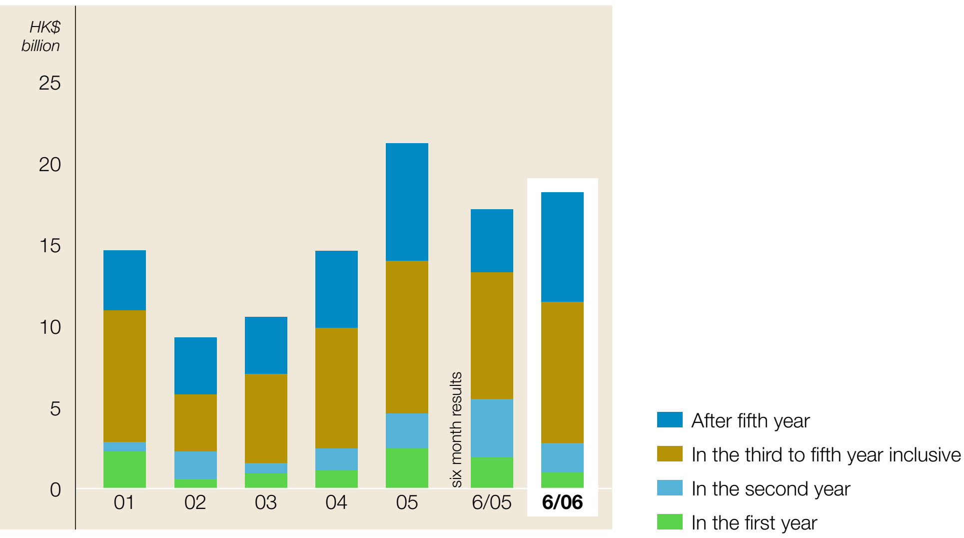
Group Debt and Liquidity

The financial position of the Group as at 30 June 2006, as compared to 31 December 2005 and 30 June 2005, is summarised as follows:

HK$ million equivalent	**30 June 2006**	31 December 2005	30 June 2005
Total debt	**18,178**	21,218	17,129
Cash and bank deposits	**4,289**	2,579	2,622
Net debt	**13,889**	18,639	14,507
Leverage (Net debt to Total capital)	**25%**	32%	28%

Total Debt

Total debt decreased mainly due to the proceeds from disposal of Festival Walk of approximately HK$6 billion. As at 30 June 2006, total debt including outstanding short term loans that will mature to the end of 2006 amounted to HK$1 billion or 5% of the total debt. On the other hand, the Group had deposits with banks of HK$4.3 billion on that date, exceeding the loans due for repayment in second half of 2006.



The original denomination of the Group's borrowings as well as cash and deposit balances by currencies as of 30 June 2006 is summarised as follows:

	denomination					
HK$ million equivalent	HK$	US$	Renminbi	Yen	other	total
Total debt	10,029	3,690	3,238	1,063	158	18,178
Cash and bank deposits	153	1,997	1,921	95	123	4,289
Net debt	9,876	1,693	1,317	968	35	13,889

Various derivative instruments are employed to minimise foreign exchange exposure. Details see descriptions under 'Foreign Currency Exposure'.

Maturity Profile of Outstanding Debt

The Group actively manages and extends its debt maturity profile to ensure that the Group's maturing debt each year will not exceed the anticipated cash flow and the Group's ability to refinance the debt in that year.

HK$ million	2006	2007	2008	2009	2010	2011 and beyond	total	percentage
Parent Company	15	27	208	3,203	3,644	6,714 [1]	13,811	76%
Subsidiaries	937	1,772	1,210	408	40	0	4,367	24%
Total Maturing Debt	952	1,799	1,418	3,611	3,684	6,714	18,178	100%
Percentage	5%	10%	8%	20%	20%	37%	100%	
Available Facilities [2]	0	78	1,292	921	550	13,584	16,425	

1. *Including a US$450 million global bond due in 2011 and a JPY8.1 billion floating rate note due in 2035 which were issued by wholly owned special purposes vehicles.*

2. *The maturity years of the relevant committed facilities are shown for reference.*

Available Sources of Financing

In addition to cash and deposits balance of HK$4.3 billion as of 30 June 2006, the Group had undrawn available facilities totaling HK$18.4 billion, of which HK$16.4 billion was in committed long term loans and HK$2.0 billion of money market lines. Besides, available trade facilities amounted to HK$2.3 billion. Borrowings by sources of financing as of 30 June 2006 is summarised as follows:

HK$ million	total facilities	outstandings	available facilities
Committed Facilities			
Bank Loans	29,621	13,196	16,425
Global Bonds	3,510	3,510	0
Private Placement	404	404	0
Total Committed	33,535	17,110	16,425
Uncommitted Facilities			
Money Market Lines and Short Term Facilities	3,051	1,049	2,002
Trade Facilities	2,765	448	2,317

In addition, the Company has signed cooperative agreements with major PRC banks. The purpose of these cooperative agreements is to facilitate our funding requirement for new investments in PRC. Because of specific legal regulations in PRC, the utilisation of these facilities is subject to certain conditions (e.g. proper approval of the underlying project and the loan arrangements must fulfill relevant PBOC regulations and guidelines). As at 30 June 2006, the aggregate credit limit granted for such facilities was RMB23 billion, of which approximately RMB8 billion remained available.

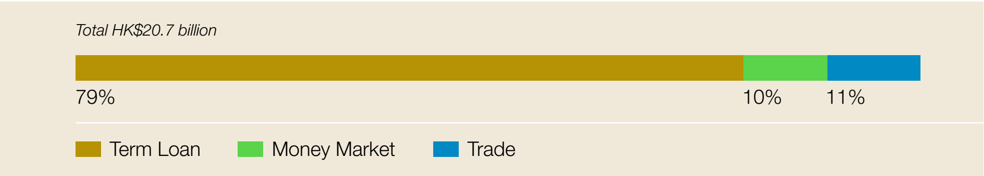
New Financing Activities

During the period, CITIC Pacific successfully completed a HK$7.2 billion syndicated loan facility. In addition, 1.8 billion committed bilateral loan facilities were newly established, renewed or extended. In August, the Company established 2 cooperative agreements with major PRC banks. Substantial amount of credit limit have been established to further support the Group's expansion strategy in the mainland.

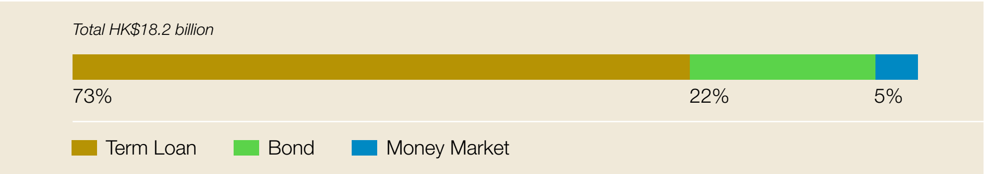
Financial Position at a Glance

The charts below show the type, interest rate, maturity and currency profiles of borrowings of the Group as at 30 June 2006:

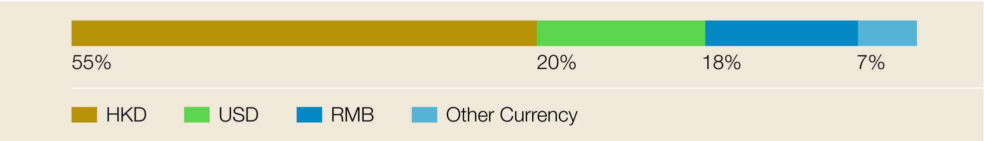
1. Available Facilities by Type



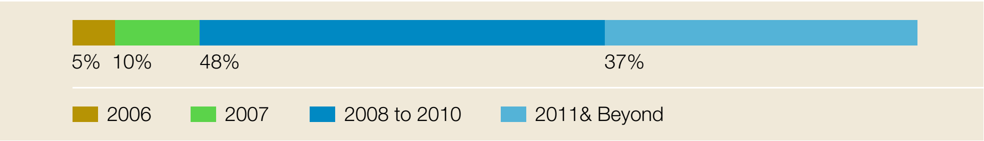
2. Outstanding Debt by Type



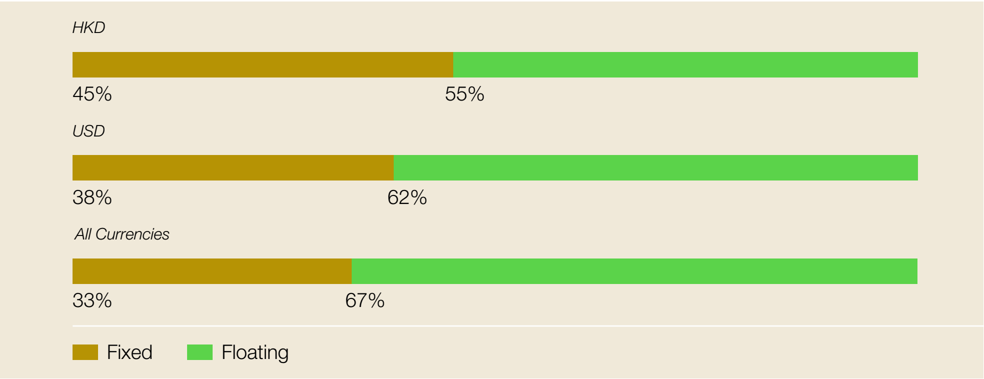
3. Outstanding Debt by Currency



4. Outstanding Debt by Maturity



5. Interest Rate Base



Debt / Cash in Jointly Controlled Entities and Associated Companies

For accounting purposes, some of the Group's businesses are classified as jointly controlled entities and associated companies. The following table shows the debt / cash position of jointly controlled entities and associated companies by business sector as of 30 June 2006 which, under Hong Kong generally accepted accounting standards, are not consolidated into the Group's accounts.

Business Sector *HK$ million*	total net debt/ (cash)	proportion of net debt/(cash) attributable to CITIC Pacific	amount of debt guaranteed by CITIC Pacific or its subsidiaries
Special Steel Manufacturing	(2)	(1)	
Property	(253)	(111)	
Power Generation	35,142	9,169	606
Aviation	14,537	3,235	
Civil Infrastructure	2,043	729	
Marketing & Distribution	1,138	500	
Communications	1,796	1,039	
Others	841	434	
Total	55,242	14,994	606

Except for the guarantee related to Jilin Power Station as described under Financial Guarantees below, the debt amount shown in the above table were arranged by jointly controlled entities and associated companies without recourse to their shareholders. Certain Group's investments, such as Discovery Bay, are 100% financed by their shareholders and do not have any external borrowings.

Financial Guarantees and Pledged Assets

In a limited number of cases, financial guarantees were given by CITIC Pacific or its subsidiaries for loan facilities which were not included in the consolidated borrowings. As of 30 June 2006, CITIC Pacific provided guarantees to support its share of loan facilities totaling RMB624 million at Jilin Power Station. In late July 2006, CITIC Pacific entered into an agreement to dispose its entire 60% shareholding in Jilin Power Station, and the guarantee will be released upon completion of the disposal.

CITIC Pacific has provided a guarantee to support loan facilities of RMB400 million to Shijiazhuang Iron & Steel Co. Ltd. ('Shijiazhuang Steel') prior to the completion of the acquisition. The release of this guarantee is being arranged.

As at 30 June 2006, subsidiaries' assets of HK$692 million (31 December 2005: HK$585 million) were pledged to secure banking facilities, these arrangements mainly related to Daye Special Steel Co., Ltd. and Dah Chong Hong's business overseas.

Contingent Liabilities

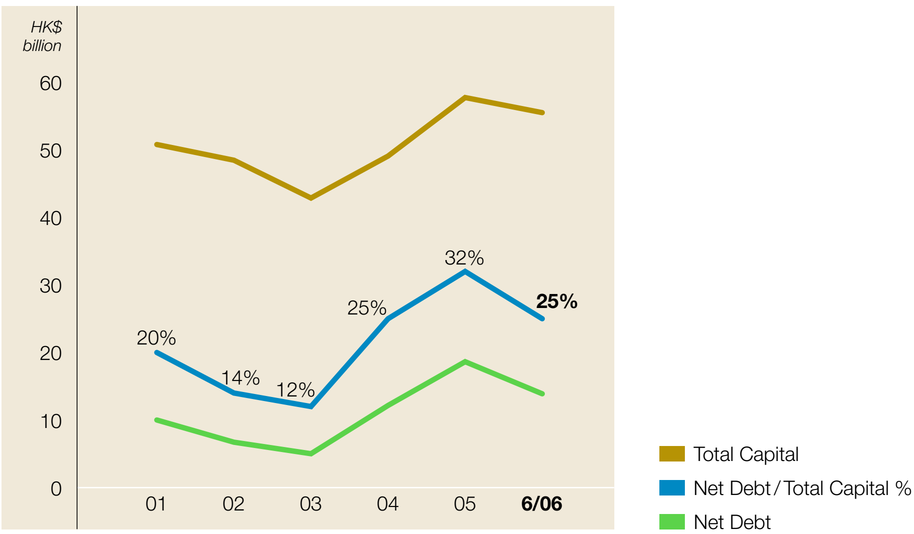
As at 30 June 2006, the Group's contingent liabilities had not changed significantly from the last year end.

Analysis on the Group's Financial Obligations

category	description	30 June 2006 *HK$ million*	31 December 2005 *HK$ million*
Borrowings of Holding Company	Include bond and notes issued by wholly owned special purposes vehicles.	13,811	16,813
Borrowings of Subsidiaries	Mainly related to the RMB borrowings of steel subsidiaries and Dah Chong Hong. According to PRC regulations, RMB borrowings must be raised at the operating subsidiary level.	4,367	4,405
Borrowings of Jointly Controlled Entities and Associated Companies	Share of net debt of jointly controlled entities and associated companies. Except for the debt of Jilin Power Station mentioned above, all the debts are non-recourse to the Company and its subsidiaries.	14,994	14,131

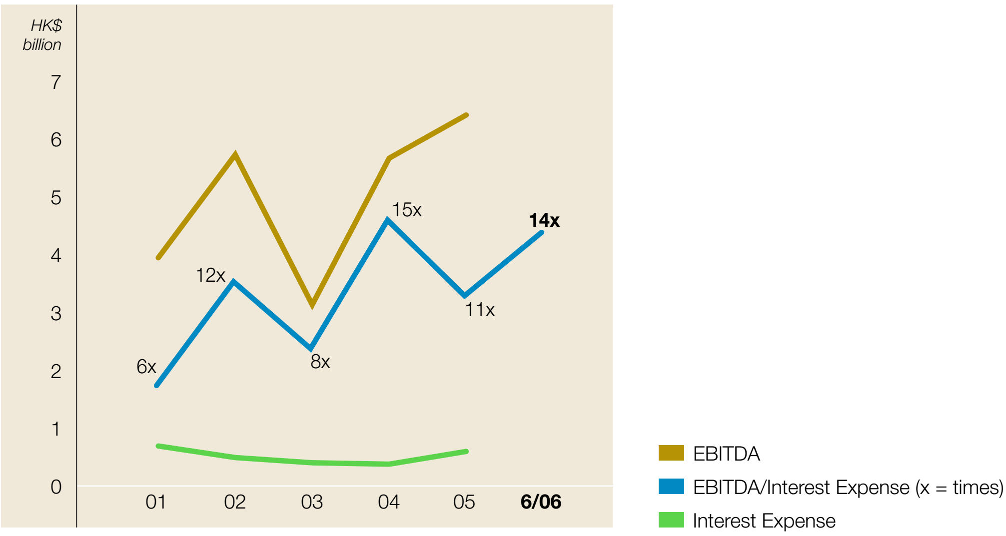
Leverage

Net debt divided by total capital was 25% at 30 June 2006 compared with 32% at the end of 2005.



Interest Cover

EBITDA divided by interest expense for the six months ended 30 June 2006 was 14 compared to 11 in 2005, due to the 23% increase in EBITDA and a 45% increase of interest expenses.



Loan Covenants

Over the years, CITIC Pacific has developed a set of standard loan covenants to facilitate the management of its loan portfolio and debt compliance. The financial covenants are generally limited to three major categories, namely, a minimum net worth undertaking, a maximum ratio of total borrowings to net worth and a limit on the amount of pledged assets as a percentage of the Group's total assets. CITIC Pacific has been in compliance with all of its loan covenants.

	covenant limits	for the six months ended 30 June 2006
Minimum Consolidated Net Worth:		
Consolidated Net Worth	≥ HK$25 billion	HK$44.1 billion
Gearing:		
Consolidated Borrowing / Consolidated Net Worth	≤ 1.5	0.43
Negative Pledge:		
Pledged Assets / Consolidated Total Assets	≤ 30%	1%

For the purpose of the above covenant limits, as defined in the relevant borrowing agreements:

'Consolidated Net Worth' means the aggregate of shareholders' funds and goodwill from acquisitions and developments having been written off against reserves or profit and loss account.

'Consolidated Borrowing' means the aggregate of all consolidated indebtedness for borrowed money and all contingent obligations in respect of indebtedness for borrowed money other than aforesaid consolidated indebtedness for borrowed money.

Credit Ratings

Moody's and Standard & Poor's downgraded CITIC Pacific's credit rating during the period. The current long term credit ratings of the Company are Ba1 by Moody's Investor Service and BB+ by Standard & Poor's. For both ratings, the credit outlook is stable. The main rationale for the change in ratings, as stated in their press release, was based on the agencies' perception that the business focus of CITIC Pacific has shifted towards the mainland market where they believe subject to higher risk, and also concerned about the Group's moving forward more volatile business areas such as specialty steel, property development and the new mining project. CITIC Pacific believes, however, that the change in business strategy, particularly the increased business focus in the fast growing mainland market, is necessary.

The Group's new investments, which focus mainly in the areas where CITIC Pacific has greatest expertise, are expected to contribute significantly in both profit and cash flow to the Group in the coming years. The Group's objective is to maintain its financial discipline when expanding its businesses.

Forward Looking Statements

This Interim Report contains certain forward looking statements with respect to the financial condition, results of operations and business of the Group. These forward looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements.

Forward looking statements involve inherent risks and uncertainties. Readers should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward looking statement.