

Notes to the Unaudited Interim Financial Report

1. Principal activities and basis of preparation

Sinopec Shanghai Petrochemical Company Limited (“the Company”) and its subsidiaries (collectively “the Group”) is a highly integrated entity which processes crude oil into synthetic fibres, resins and plastics, intermediate petrochemicals and petroleum products. The Company is a subsidiary of China Petroleum & Chemical Corporation (“Sinopec Corp”).

This interim financial report is unaudited, but has been reviewed by KPMG in accordance with Statement of Auditing Standards 700 “Engagements to review interim financial reports”, issued by the Hong Kong Institute of Certified Public Accountants. KPMG’s independent review report to the Board of Directors is included on page 29.

The interim financial report has been prepared in accordance with the requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standards 34 “Interim Financial Reporting” adopted by the International Accounting Standards Board (“IASB”).

The preparation of interim financial report in conformity with International Financial Reporting Standards requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates.

The financial information relating to the financial year ended 31 December 2005 included in the interim financial report do not constitute the Company’s statutory financial statements for that financial year but is derived from those financial statements. Statutory financial statements for the year ended 31 December 2005 are available from the Company’s registered office. The Company’s independent auditors have expressed an unqualified opinion on those financial statements in their audit report dated 24 March 2006.

The accounting policies have been consistently applied by the Group and are consistent with those adopted in the 2005 annual financial statements. The 2005 annual financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRSs”) promulgated by the IASB. IFRSs include International Accounting Standards (“IAS”) and related interpretations.

2. Segment reporting

Reportable information on the Group's operating segments is as follows:

	Six-month period ended 30 June	
	2006	2005
Turnover	RMB'000	RMB'000
Manufactured products		
<i>Synthetic fibres</i>		
-External sales	2,312,743	2,449,372
-Intersegment sales	38	43
Total	2,312,781	2,449,415
<i>Resins and plastics</i>		
-External sales	7,606,847	6,930,737
-Intersegment sales	29,577	27,797
Total	7,636,424	6,958,534
<i>Intermediate petrochemicals</i>		
-External sales	3,048,549	3,483,154
-Intersegment sales	6,340,998	6,408,146
Total	9,389,547	9,891,300
<i>Petroleum products</i>		
-External sales	9,074,588	8,351,262
-Intersegment sales	663,223	532,169
Total	9,737,811	8,883,431
All others		
-External sales	1,397,548	671,947
-Intersegment sales	1,890,620	1,808,478
Total	3,288,168	2,480,425
Elimination of intersegment sales	(8,924,456)	(8,776,633)
Consolidated turnover	23,440,275	21,886,472

External sales include sales to other Sinopec Corp group companies.

2. Segment reporting *(continued)*

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Profit before taxation		
(Loss) / profit from operations		
Synthetic fibres	84,956	282,430
Resins and plastics	500,963	1,319,350
Intermediate petrochemicals	272,977	863,539
Petroleum products	(941,320)	(175,287)
All others	62,302	74,886
Consolidated (loss) / profit from operations	(20,122)	2,364,918
Share of profits / (losses) of associates	180,156	(93,723)
Net financing costs	(107,335)	(113,407)
Consolidated profit before taxation	52,699	2,157,788

3. Profit before taxation

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

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Interest on bank loans and advances	183,908	146,728
Less: Amount capitalised as construction in progress	(26,859)	(15,933)
Interest expense, net	157,049	130,795
Cost of inventories sold	22,931,817	18,949,942
Depreciation	909,990	856,665
Amortisation of lease prepayment	6,244	10,326
Net loss on disposal of property, plant and equipment	73	1,811
Amortisation of deferred income	(5,759)	(5,759)

4. Taxation

Taxation in the consolidated income statement represents:

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Provision for PRC income tax for the period	15,679	357,730
Deferred taxation	(4,289)	2,230
	<u>11,390</u>	<u>359,960</u>

The charge for PRC income tax is calculated at the rate of 15% (2005: 15%) on the estimated assessable income of the period determined in accordance with relevant income tax rules and regulations. The Company did not carry out business overseas and therefore does not incur overseas income taxes. Up to the date of approval of these financial statements, the Company has not received notice from the Ministry of Finance that the 15% tax rate will be revoked in 2006 or in the future. It is possible that the Company's tax rate will increase in the future, however, management feels that 15% is the applicable rate for 2006 and future periods when temporary tax differences are expected to reverse.

5. Basic earnings per share

The calculation of basic earnings per share is based on the profit attributable to equity shareholders of the Company for the period of RMB 5,693,000 (period ended 30 June 2005: RMB 1,763,442,000) and 7,200,000,000 (period ended 30 June 2005: 7,200,000,000) shares in issue during the period.

The amount of diluted earnings per share is not presented as there were no dilutive potential ordinary shares in existence for both periods.

6. Dividends

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Final dividend in respect of the previous financial year, approved during the period, of RMB 0.10 per share(2005: RMB 0.20 per share)	<u>720,000</u>	<u>1,440,000</u>

Pursuant to a resolution passed at the Annual General Meeting held on 15 June 2006, a final dividend of RMB 720,000,000 (2005: RMB 1,440,000,000) was declared and approved for the year ended 31 December 2005. The Directors do not recommend the payment of an interim dividend for the period (2005: RMB Nil).

7. Property, plant and equipment

	30 June 2006 RMB'000	31 December 2005 RMB'000
Cost or valuation:		
At 1 January	32,204,419	31,188,112
Additions	92,359	164,816
Transferred from construction in progress	437,790	1,023,427
Disposals	(93,551)	(171,936)
At 30 June / 31 December	32,641,017	32,204,419
Accumulated depreciation and impairment losses:		
At 1 January	17,553,252	15,981,787
Charge for the period / year	903,651	1,692,213
Written back on disposals	(20,043)	(120,748)
At 30 June / 31 December	18,436,860	17,553,252
Net book value:		
Balance at 30 June / 31 December	14,204,157	14,651,167

8. Investment Property

	30 June 2006 RMB'000	31 December 2005 RMB'000
Cost:		
At 1 January	528,465	512,343
Additions	-	16,122
At 30 June / 31 December	528,465	528,465
Accumulated depreciation:		
At 1 January	13,883	1,036
Charge for the period / year	6,339	12,847
At 30 June / 31 December	20,222	13,883
Net book value:		
At 30 June / 31 December	508,243	514,582

8. Investment Property (continued)

Investment property represents certain floors of an office building rented out under the terms of operating leases.

The fair value of the investment property of the Group as at 30 June 2006 is estimated by the directors to be approximately RMB 594,271,000, by reference to market conditions (31 December 2005: RMB 596,598,000). The investment property has not been valued by an external independent valuer.

Rental income of RMB 26,228,000 was received during the period ended 30 June 2006 (period ended 30 June 2005: RMB 6,021,000).

9. Trade accounts receivable

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Trade debtors	383,188	278,011
Less: Impairment losses for bad and doubtful debts	(27,739)	(25,845)
	355,449	252,166
Bills receivable	845,512	731,204
Amounts due from parent companies, fellow subsidiaries and associates	663,400	561,552
	<u>1,864,361</u>	<u>1,544,922</u>

The ageing analysis of trade accounts receivable (net of impairment losses for bad and doubtful debts) is as follows:

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Invoice date:		
Within one year	1,839,004	1,517,158
Between one and two years	25,357	27,764
	<u>1,864,361</u>	<u>1,544,922</u>

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

10. Short-term debt

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Short-term bank loans	2,301,562	2,523,537
Corporate bonds (Note a)	990,150	-
Current portion of long-term bank loans	410,986	1,373,205
	3,702,698	3,896,742

Note a:

The Company issued 270-day corporate bonds of face value at RMB 1 billion to corporate investors in the PRC interbank debenture market on 24 February 2006. The bonds were sold at a discounted value of RMB97.78 per RMB 100 par value, with an effective yield 3.069% per annum, and will mature in November 2006.

11. Trade accounts payable

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Trade creditors	1,389,300	963,230
Bills payable	412,628	68,302
Amounts due to parent company, fellow subsidiaries and associates	529,857	467,909
	2,331,785	1,499,441

The maturity analysis of trade accounts payable is as follows:

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Due within 1 month or on demand	1,705,614	1,269,809
Due after 1 month and within 3 months	626,171	229,632
	2,331,785	1,499,441

12. Reserve movement

No transfers have been made to the statutory surplus reserve, the statutory public welfare fund nor the discretionary surplus reserve from the income statement for the period (period ended 30 June 2005: RMB Nil).

13. Related party transactions

(a) Most of the transactions undertaken by the Group during the period ended 30 June 2006 have been effected with such counterparties and on such terms as determined by Sinopec Corp, the immediate parent company, 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. During the six-month period ended 30 June 2006, the value of crude oil purchased in accordance with Sinopec Corp's allocation was as follows:

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Purchases of crude oil	<u>15,173,359</u>	<u>12,424,946</u>

(b) Other transactions between the Group and other related parties during the six-month period ended 30 June 2006 were as follows:

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Sales of products and service fee income	9,153,900	9,075,959
Purchases other than crude oil	1,151,915	677,597
Insurance premiums paid	47,544	45,347
Net withdrawal of deposits placed with related parties	28,321	56,510
Interest received and receivable	182	277
New loans obtained from related parties	448,000	50,000
Loans repaid to related parties	448,000	50,000
Interest paid and payable	4,085	3,315
Transportation fees	177,120	186,133
Construction and installation fees	117,349	93,983
Gains from disposal of investment	24,308	-
Sales commissions	93,234	-
Net decrease of guarantees	<u>3,553</u>	<u>23,300</u>

13. Related party transactions *(continued)*

(c) Deposits with related parties

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Deposits, with maturity within 3 months	<u>152,945</u>	<u>181,266</u>

(d) Loans with related parties

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Short-term loans	30,000	30,000
Long-term loans	100,000	100,000
	<u>130,000</u>	<u>130,000</u>

(e) Key management personnel compensation and post-employment benefit plans

	<u>Six-month period ended 30 June</u>	
	2006 RMB'000	2005 RMB'000
Short-term employee benefits	3,616	1,384
Post-employment benefits	18	16
	<u>3,634</u>	<u>1,400</u>

Post-employment benefits are included in "contributions to defined contribution retirement plans" as disclosed in Note 13(f).

(f) Contributions to defined contribution retirement plans

The Group participates in defined contribution retirement plans organised by municipal governments for its staff. The contributions to defined contribution retirement plans are as follows:

	<u>Six-month period ended 30 June</u>	
	2006 RMB'000	2005 RMB'000
Municipal retirement scheme costs	99,703	79,423
Supplementary retirement scheme costs	30,744	29,459
	<u>130,447</u>	<u>108,882</u>

At 30 June 2006 and 31 December 2005, there was no material outstanding contribution to post-employment benefit plans.

13. Related party transactions *(continued)*

(g) Transactions with other state-owned entities in the PRC

The Group is a state-controlled enterprise and operates in an economic regime currently dominated by entities directly or indirectly controlled by the PRC government (collectively referred as “state-controlled entities”) through its government authorities, agencies, affiliations and other organisations.

Apart from transactions with parent companies, fellow subsidiaries and associates, the Group has transactions with other state-controlled entities include but are not limited to the following:

- sales and purchase of goods and ancillary materials;
- rendering and receiving services;
- lease of assets, purchase of property, plant and equipment;
- placing deposits and obtaining finance; and
- use of public utilities.

These transactions are conducted in the ordinary course of the Group’s business on terms comparable to those with other entities that are not state controlled. The Group has established its procurement policies, pricing strategy and approval process for purchases and sales of products and services which do not depend on whether the counterparties are state-controlled entities or not.

Having considered the potential for transactions to be impacted by related party relationships, the entity’s pricing strategy, procurement policies and approval processes, and the information that would be necessary for an understanding of the potential effect of the related party relationship on the financial statements, the directors are of the opinion that the following transactions require disclosure of numeric details:

(i) Transactions with other state-controlled energy and chemical companies

The Group’s major domestic suppliers of crude oil and refined petroleum products are China National Offshore Oil Corporation and its subsidiaries (“CNOOC Group”), which are state-controlled entities.

During the six-month period ended 30 June 2006, the aggregate amount of crude oil purchased by the Group’s refining segment from CNOOC Group was RMB 862,530,000 (period ended 30 June 2005: RMB 985,852,000).

The amounts due from / to CNOOC Group are nil as at 30 June 2006 (31 December 2005: Nil).

13. Related party transactions *(continued)*

(g) Transactions with other state-owned entities in the PRC *(continued)*

(ii) Transactions with state-controlled banks

The Group deposits its cash with several state-controlled banks in the PRC. The Group also obtains short-term and long-term loans from these banks in the ordinary course of business. The interest rates of the bank deposits and loans are regulated by the PBOC. The Group's interest income from and interest expenses to these state-controlled banks in the PRC are as follows:

	<u>Six-month period ended 30 June</u>	
	2006	2005
	RMB'000	RMB'000
Interest income	17,431	15,414
Interest expenses	141,085	117,129

The amounts of cash deposited at and loans from state-controlled banks in the PRC are summarised as follows:

	At 30 June	At 31 December
	2006	2005
	RMB'000	RMB'000
Cash and cash equivalents at state-controlled banks in the PRC	646,390	1,164,382
Short-term loans and current portion of long-term loans	2,702,548	3,396,494
Long-term loans excluding current portion of long-term loans	1,449,654	1,256,735
Total loans from state-controlled banks in the PRC	4,152,202	4,653,229

14. Capital commitments

The Group had capital commitments outstanding as at 30 June 2006 and 31 December 2005 not provided for in the financial statements as follows:

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Contracted but not provided for	1,022,149	222,711
Authorised by the Board but not contracted for	107,672	1,501,490
	<u>1,129,821</u>	<u>1,724,201</u>

These capital commitments relate to the acquisition of property, plant and equipment and capital contributions to the Group's investments.

15. Contingent liabilities

Contingent liabilities of the Group are as follows:

	At 30 June 2006 RMB'000	At 31 December 2005 RMB'000
Guarantees issued to banks in favour of:		
- associates	40,000	40,000
- joint ventures	24,747	28,300
	<u>64,747</u>	<u>68,300</u>

Guarantees issued to banks in favour of associates and other unlisted investment companies are given to the extent of the Company's respective interest in these entities. The Company monitors the conditions that are subject to the guarantees to identify whether it is probable that a loss has occurred, and recognise any such losses under guarantees when those losses are estimable. At 30 June 2006, it is not probable that the Company will be required to make payments under the guarantees. Thus no liability has been accrued for a loss related to the Company's obligation under the guarantees arrangement.