

## BUSINESS

*This section discusses information regarding our mines, reserves and production volumes, including the mines, reserves and production volumes of the Huajin Joint Venture and Shanghai Datun Energy, which are not wholly-owned by us.*

*Unless otherwise stated, all technical data in this section is based on the SRK Report, which is included as Appendix VI to this Prospectus.*

### OVERVIEW

We are the second largest coal enterprise in China based on our 2005 revenue. According to *BP Statistical Review 2006*, China is the world's largest producer and consumer of coal, one of the most important energy resources in the world and the most important source of primary energy in China. We sold 92.2 million tonnes and 43.5 million tonnes of coal in 2005 and the six months ended 30 June 2006, respectively. Our total revenue from coal operations in the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2005 and 2006 was RMB11,656.7 million, RMB17,733.0 million, RMB25,147.7 million, RMB12,600.1 million and RMB11,761.0 million, respectively.

According to the SRK Report, we had total marketable coal reserves of 3,003 million tonnes as of 30 June 2006. We sell high-quality thermal coal and coking coal produced from nine operating coal mines and thirteen coal processing plants that we wholly or partially own and/or operate. Located in eastern, northern and northwestern China, our five mining areas consist of nine underground mines and three open pit mines, two of which, the Antaibao Open Pit Mine and the Anjialing Open Pit Mine, are among the largest open pit mines in China. Each of our mines and coal processing plants is situated in close proximity to our customers or with convenient access to transportation networks and facilities. Our raw coal output grew from 33.2 million tonnes in 2003 to 50.1 million tonnes in 2005, representing a CAGR of 22.8%.

We are also one of China's largest coal suppliers, with extensive market experience, well-established brand names and solid customer relationships. Our parent company, ChinaCoal Group, is the largest coal exporter in China. Our extensive sales and marketing network and established supply and distribution channels have contributed to our success in conducting our proprietary coal trading operations and providing coal import agency and export-related services.

As an integrated coal enterprise with coal production, sales and trading as our core business, we further supplement our coal operations with a diversified portfolio of other related operations. We operate one of China's largest coking operations not affiliated with a steelmaker. Our coking operations include the production and sale of coke and coal-based chemicals. We also own China's largest coal mining equipment manufacturing operations in terms of revenue. In addition, we operate ancillary businesses, including coal mine design and transportation services. We believe these operations represent a natural extension of our coal production, sales and trading capabilities while effectively expanding the scope of our product and service offerings and enhancing our core competitiveness.

In the year ended 31 December 2005 and the six months ended 30 June 2006, we had total revenue of RMB30,061.3 million and RMB14,679.7 million, respectively, and net profit of RMB3,343.5 million and RMB1,334.4 million, respectively.

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### OUR COMPETITIVE STRENGTHS

*We are the second largest coal enterprise in the PRC and have the potential to attain sustainable growth.*

We are the second largest coal enterprise in China in terms of revenue for 2005. We possess abundant coal reserves and advanced mining and coal processing technologies and facilities. We continue to expand our coal production business. Our total revenue from sales of coal and coal-related products as well as the provision of coal-related services in the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2005 and 2006 was RMB14,480.8 million, RMB22,163.8 million, RMB30,061.3 million, RMB15,011.9 million and RMB14,679.7 million, respectively.

We are also one of China's largest coal suppliers and our parent company, ChinaCoal Group, is the largest coal exporter in China. We rely on our extensive and strong sales network, established port service facilities, strong team of professionals, access to first-hand coal market information, ability to quickly adapt to changing coal market dynamics and relationships throughout the industry demand-supply chain. Our total coal sales revenue from external customers was RMB11,656.7 million, RMB17,733.0 million, RMB25,147.7 million, RMB12,600.1 million and RMB11,761.0 million in the years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2005 and 2006, respectively, representing a CAGR of 46.9% from 2003 to 2005. Our total raw coal production volume was 33.2 million tonnes, 39.7 million tonnes and 50.1 million tonnes in the years ended 31 December 2003, 2004 and 2005, respectively, representing a CAGR of 22.8%. From 2003 to 2005, the total production of raw coal in China grew at a CAGR of 12.8%.

We are an integrated coal enterprise with coal production, sales and trading as our core business. While maintaining our leading position in our core business, we also explore and develop coal production-related businesses, such as coal mine design, coal mining equipment manufacturing and the production of coal-based chemicals and coke. Through the comprehensive and balanced development of our coal production, sales and related business portfolio, we have achieved organic growth and effectively diversified our operational risks.

The PRC Government has promulgated a number of policies and regulations since 1999 to shut down or limit the operations of local coal producers and to encourage the integration and transformation of such operations by large coal producers. These policies and regulations were implemented to resolve certain problems arising from local small mining operations, such as low resource utilization and the lack of adequate environmental protection and safety measures. As one of the largest integrated coal producers in China, our mines are the key coal producers in China's Jinbei Base and Jinzhong Base, two of the 13 large coal bases in China designated by the PRC Government. Our controlling shareholder, ChinaCoal Group, as one of the largest coal enterprises in China, is supported by the PRC Government. We believe we are well positioned to take advantage of the favorable regulatory and market conditions. Our efforts to integrate and upgrade local small coal mines will enable us to rapidly expand our production capacity and drive our continuing organic growth and further contribute to our development.

*We offer high-quality coal products to our customers by leveraging our abundant, high-quality and diversified coal reserves as well as our advanced coal processing and blending capabilities.*

Based on SRK's estimate of our coal reserves as of 31 December 2005 and compared with publicly available sources for other coal companies as of 31 December 2005, we had the fifth largest proved and probable coal reserves among all listed coal companies in the world. Our recoverable coal reserves were 3,420 million tonnes as of 30 June 2006. Based on such recoverable reserves and our 2005 annual production level, we expect to be able to achieve stable production for the next 68 years. These coal reserves are deposited

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in five mining areas that include 12 coal mines, two of which, the Antaibao Open Pit Mine and the Anjialing Open Pit Mine, are among the largest open pit mines in China.

Our raw coal is of high quality. Most of our coal reserves are deposited in areas with favorable geological and mining conditions. The Pingshuo Mining Area, one of the largest export bases for thermal coal products in China, produces prime thermal coal featuring a high heat value and high ash fusion temperature. Many domestic power plants are designed to use coal possessing the qualities found in the coal produced in our Pingshuo Mining Area and at other coal mines in the Jinbei Base. The quality of thermal coal is generally determined by its high heat value, ash content and ash fusion temperature, and the quality of thermal coal produced in our Pingshuo Mining Area consistently meets the needs of our major customers. In addition, coking coal produced at our Shaqu Mine in the Liliu Mining Area has been designated by the PRC Government as a scarce and valuable mineral resource vital to national economic development, and significant emphasis has been placed on its exploitation and production.

We also offer a wide variety of coal products. Our nine mines in operation produce thermal coal, hard coking coal and semi-hard coking coal. With our high quality raw coal, advanced technologies and extensive experience, our thirteen coal processing plants are capable of processing and blending various types of raw coal produced and coal purchased from third parties according to the specifications of various industries, such as the electrical, metallurgical, construction and chemicals industries. As a result of our blending capability, we have significantly expanded our product offerings and improved their commercial value. Moreover, a diversified portfolio of our coal products has enabled us to avoid reliance on a single product and hence minimize our exposure to market risks.

We believe our high-quality coal products, abundant and diversified coal reserves and expertise in coal processing and blending provide us with a competitive advantage in both the domestic and international markets and serves as the basis for future growth.

***With our extensive market experience, well-recognized brand names, stable coal supply, comprehensive transportation facilities and solid customer relationships, we have one of the strongest coal sales and marketing networks in China.***

ChinaCoal Group, our Parent Company, is the largest coal exporter in China and has continued to maintain an important position in the Asia-Pacific regional coal export market. As a result of the Restructuring, except for certain Coal Export Rights which could not be freely transferred under applicable laws and regulations, we obtained all of ChinaCoal Group's sales and marketing resources, including its extensive sales and marketing network, stable coal supply from third parties, comprehensive transportation facilities and valuable market experience.

We believe our market knowledge and reputation are key factors contributing to our brand name recognition and customer satisfaction, which enable us to consistently provide our customers with a wide variety of products tailored to their needs. We believe that the coal products we market bearing the Pingshuo brand names are well recognized by both our domestic and international customers. ChinaCoal Group has over 20 years of sales experience. By leveraging this extensive experience, our understanding of customers' individual needs, our close relationship with long-term customers and our advanced technologies for coal processing and blending, we are able to offer a wide range of customized coal products, enabling us to secure long-term commitment and trust from our customers.

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We also cooperate closely with other major coal producers in China. We purchase coal from these producers and process and blend it with our own coal. This enables us to significantly expand our product variety.

With our headquarters in Beijing and a comprehensive distribution network covering major coal transportation ports along the coast of China, including Qinhuangdao, Tianjin, Qingdao, Rizhao and Lianyungang, we are able to respond quickly to customer demands and optimize our distribution capabilities. In addition, our strategically located Shanghai ChinaCoal East China Co., Ltd. in Shanghai will allow us to: (i) better serve our customers in the eastern China region; (ii) strengthen our market information collection capabilities; and (iii) allow us to take advantage of preferential governmental policies of the Shanghai Pudong New District. We believe that we are a leader in the PRC coal industry in terms of the scope of our distribution network and the total number and transportation capacity of ports available to us. Through centralized management from our headquarters, we have integrated our extensive sales network with strong marketing capabilities and strategically coordinated our sales operations and customer service initiatives, including pricing, quality control, transportation and inspection. We believe these efforts have not only improved our sales and marketing efficiency but also offer our customers a cost advantage.

We have established long-term relationships with many of our customers. We have entered into long-term supply agreements of over three years with a number of domestic and international customers. The average aggregate sales volume per annum under these agreements is approximately 62.5 million tonnes in 2006, 2007 and 2008. With the recent rapid economic growth in China resulting in increasing demand for coal, the visibility of our future sales volumes from existing and new clients is enhanced. In addition to our established presence in the long-term coal sales market, we believe we have also established a good reputation in the spot coal market as a result of the variety of coal products we offer and our reliable supply, thereby allowing us to further expand our customer base.

We believe the above factors distinguish our network as the strongest coal sales and marketing network in China and, combined with our position as the exclusive coal export services provider for ChinaCoal Group, will continue to support our domestic coal sales and export agency service offerings so as to allow us to continue to serve our domestic and international customers.

***Our coal mines and coal production facilities are situated with convenient access to transportation networks, thereby ensuring the timely, cost-effective and efficient delivery of our coal products.***

The distance from coal mines and coal production facilities to customers and transportation networks, such as railways and ports, plays a vital role in the development and operation of a coal producer. Our key mines are located in close proximity, and have convenient access, to coal transportation networks, particularly in the case of our Pingshuo and Datun Mining Areas.

Our largest mining area, the Pingshuo Mining Area, is located in the Jinbei Base, one of the 13 large coal bases in China designated by the PRC Government. Having recognized the importance of the Jinbei Base, the PRC Government constructed China's largest railway line in terms of transportation capacity dedicated to coal transportation, the Daqin Rail Line, mainly for the transportation of coal from the Jinbei Base. The Daqin Rail Line connects the coal production bases of northern and northwestern China with major coal loading ports and certain of our key customers in the coastal regions. The PRC Government plans to further increase the Daqin Rail Line's annual transportation capacity by 2010, which will further enhance and ensure the transportation capacity available to our Pingshuo Mining Area.

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Among the major coal mines in the coal-producing provinces of northern and northwestern China, the Pingshuo Mining Area is one of the closest areas to major coal loading ports. In addition to the Daqin Rail Line, the Pingshuo Mining Area is connected by other major regional and national railways and has direct transportation links to major coal loading ports, including the Qinhuangdao Port and the Tianjin Port, as well as to certain of our major customers. Currently, we own and operate the five coal loadout depots in the Jinbei Base for 10,000-tonne trains, ensuring our access to sufficient railway transportation, increasing our efficiency and substantially reducing our transportation costs.

The Datun Mining Area, located in the eastern coastal region of China, is one of the few coal mines in close proximity to the fast-growing industrial centers and coal-consuming regions in eastern China, including Shanghai. Through a 180 km dedicated coal-transport rail line legally and validly owned and operated by Shanghai Datun Energy, the Datun Mining Area is linked to the Longhai Rail Line and its coal products can be transported directly to major coal loading ports in eastern China, such as the Lianyungang Port. As a result, the Datun Mining Area is well-positioned to deliver coal products to our customers in a cost-effective and timely manner.

*We own two of the largest open pit mines in China and rely on advanced mining and recycling technologies to achieve optimal resource utilization and improve environmental protection.*

The resource utilization rate is an effective criteria for measuring the efficiency of coal mining enterprises and is an important indicator of their environmental protection standards. Open pit mines generally have high recovery rates. We own two of the largest open pit mines in China, the Antaibao Open Pit Mine and the Anjialing Open Pit Mine, which produced 32.8% and 29.9%, respectively, of our total production of raw coal in 2005. As China adopts a more rigorous policy on the exploitation of coal resources through the implementation of a compensation scheme in the future, we believe open pit mines will present even higher economic value. We have achieved a significantly higher recovery rate than the industry average in China.

We engage in both open pit and underground mining at our Anjialing Mines in the Pingshuo Mining Area. The recovery rate in the Pingshuo Mining Area exceeds 95% through surface mining and 75% through underground mining. By employing both surface and underground mining methods at these mines, we have been able to increase our resource utilization rate and expand our products offerings.

The coal seams at the Pingshuo Mining Area are shallow, stable, thick and have a low dipping angle. We maximize resource utilization and mining efficiency at these underground mines by using mechanized coal mining equipment, such as the fully mechanized longwall mining system.

We are also committed to resource recycling and re-utilization, and we are committed to environmental protection by utilizing various advanced equipment and technologies. For example, we reuse the waste coal, coal rejects and coal slurry produced during the coal production process to generate electricity at power plants that we use to support our own coal production or sell to the local power grid.

We believe that we have achieved a leading position in resource utilization and our management will continue to focus on improving our efficiency measures. We are also confident in our ability to further enhance our environmental protection capabilities, meet the increasingly stricter environmental standards imposed by the PRC Government and reduce any exposure to potential incremental costs or contingent liabilities relating to environmental protection.

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*Our extensive expertise in coal mine design and our position as the largest coal mining equipment manufacturer in China has made us the most integrated enterprise in the domestic coal industry, enabled us to increase our revenue and contributed to the continuing development of our core business.*

In addition to coal sales revenue, we generate other operating revenue by providing coal production related services, such as coal mine design, coal mine construction consulting services and coal mining equipment manufacturing. By leveraging our expertise in these areas and our self-owned and -operated mining productions and technologies, we are able to ensure the development and maintenance of our own coal mines.

We own two coal mine design institutes, namely the China Coal Xi'an Design Engineering Co. Ltd. (中煤西安設計工程有限責任公司) and the China Coal Handan Design Engineering Co. Ltd. (中煤邯鄲設計工程有限責任公司). These design institutes are well recognized in the areas of coal mine and large public project design services in China. We are also the largest coal mining equipment manufacturer in China based on our 2005 sales revenue. Our coal mining equipment design and manufacturing subsidiaries have a long operating history and extensive experience in the industry and possess advanced technologies. China Coal Zhangjiakou Coal Mining Machinery Co., Ltd. (中煤張家口煤礦機械有限責任公司) and China Coal Beijing Coal Mining Machinery Co., Ltd. (中煤北京煤礦機械有限責任公司) are two of our most prestigious coal mining equipment manufacturing enterprises and are among the leading Chinese coal mining equipment manufacturers. In addition to the manufacturing of mining equipment, including those used in the longwall mining method, our coal mining equipment design and manufacturing subsidiaries are also capable of providing comprehensive services to domestic and international underground mining enterprises, including design, installation, testing and system integration services, all of which are essential to mechanized underground mines. With our knowledge of and experience in the Chinese coal industry and its practices, as well as our ability to effectively control costs, the coal mining equipment we manufacture and the mining related services we offer are highly suitable for coal mines in China and are well recognized in the market.

We believe that the PRC Government's encouragement of large procurement and the increasing use of domestically produced coal mining equipment will enable us to enjoy significant advantages with respect to the construction of future mines as we leverage our capabilities in coal mine design, construction consulting and coal mining equipment manufacturing.

*Our management team has extensive industry and management experience to effectively manage our operations and maximize shareholder value.*

Our senior management comprises a group of highly experienced professionals in the fields of coal production, coal trading and other coal-related businesses such as coking, coal mining equipment manufacturing and coal mine design, with average industrial experience exceeding 20 years. We believe that our management team possesses the knowledge critical to the industry in which we operate and is capable of taking advantage of market opportunities, formulating sound business strategies, assessing and managing risks, implementing management and production schemes and increasing our overall profit to maximize our shareholder value. We also have loyal and skilled employees who possess extensive industry experience. In order to align our corporate performance and the interests of our management and employees with those of our shareholders and to further incentivize our management, we plan to implement a long-term incentive program. We believe that our management team possesses the leadership capabilities required to ensure sustained development and our continued success.

## **OUR BUSINESS STRATEGIES**

We operate in a mature industry environment that is stable, fragmented and with strong regional characteristics. With the increasing commercialization of the coal industry in China, the PRC Government has been monitoring the development of local, small and sub-standard mining operations, increasing the consolidation of coal production and effectively raising the entry barrier to restrict the development of small-scale mining operations. Through our accumulated experiences over the years, we have gradually developed competitive strengths in resource control and in marketing and distribution. We have developed an integrated business structure, the ability to integrate other domestic mining operations and form cross-border joint ventures and alliances, and the capability to maximize profit by increasing efficiency and developing new profitable growth areas. We believe that the following strategies will help us to leverage our strengths to capture future growth opportunities in China's coal industry, increase the globalization of our operations and enhance our competitiveness.

*Seek rapid and sustainable growth through our organic growth supplemented by external development strategies.*

We plan to increase production capacity through organic growth and external expansion, increase our coal reserves, increase our operating scale and reduce production costs.

As of 30 June 2006, we had marketable coal reserves of 3,003 million tonnes. We plan to further expand and upgrade our existing mining operations. We intend to deploy advanced technologies developed from multiple sources, including those from our own research and development initiatives, in the coal production process. Our objective is to ensure full utilization of our existing and newly constructed coal mines and to achieve organic growth.

We are dedicated to further exploring and developing new coal resources, constructing new projects and upgrading and improving our existing facilities to maximize and optimize our coal production. We have commenced construction at our Pingshuo East Open Pit Mine, Antaibao Underground Mine and Wangjialing Mine in the Pingshuo and Xiangning Mining areas. These mines have designed annual production capacities of 20.0 million tonnes, 8.0 million tonnes and 6.0 million tonnes, respectively. Upon commencement of production at these three mines, and together with other expansion projects, we expect our total production capacity of raw coal to exceed 100.0 million tonnes by 2010. Supported by the relevant governmental policies, we plan to further increase our coal reserves and strengthen our competitiveness through applications to the PRC Government for new resources, mergers and acquisitions, joint ventures and other forms of cooperation as follows:

- *Applications for New Coal Reserves.* Taking advantage of the PRC Government's encouragement of the construction of large coal bases, we are currently applying to the PRC Government for the right to exploit new coal reserves.
- *Mergers and Acquisitions.* By taking advantage of governmental support and the favorable regulatory environment, we will continue to explore opportunities to acquire and integrate small-scale coal mines in China. By leveraging our strength in production, management, technology, coal mine design, coal mining equipment manufacturing and research and development capabilities, we believe we can optimize the utilization of coal resources at these small mines through technology improvement and equipment upgrades.

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- *Joint Ventures and Cooperation.* We are actively seeking cooperative relationships and joint venture opportunities with provincial governments and large domestic coal producers and operators possessing abundant coal reserves. We also plan to enhance our global presence and to mine coal resources located overseas by cooperating with large coal producers in countries with abundant coal reserves.

We believe that, through these organic and external growth strategies, we will be able to achieve rapid and sustainable growth in our coal production operations, satisfy the growing coal demand in China and overseas and achieve economies of scale.

***Maximize our profitability and maintain our competitiveness by improving operating efficiency and controlling costs.***

We view improving efficiency and cost control as the critical elements for maximizing our profitability and maintaining our competitiveness. We intend to reduce our per unit production costs and improve our operating efficiency by increasing our production scale, employing advanced automated production systems to increase resource utilization rates and strengthening our management control.

We will continue to expand our production scale by using both organic and external growth strategies in order to further reduce coal production costs and strengthen our competitiveness.

We employ automated production systems and focus on developing coal mines with high yields and high productivity. To improve productivity, we will continue to deploy advanced mining facilities and technologies, such as fully automated top coal caving equipment and related sophisticated mining methods. We will also allocate more management resources to mines which we believe have higher growth potential.

Our coal mining equipment manufacturing and coal mine design capabilities will further enhance our production efficiency and reduce our reliance on imported equipment and services, allowing us to better control and lower the costs of mine construction and coal production.

***Expand our sources of income by focusing on the development of high value-added coal-based chemicals products.***

To take advantage of government policies emphasizing the use of coal as the primary energy source in China, we intend to cooperate with large domestic and international coal and chemicals producers to develop high value coal-based chemicals products, such as coal-based methanol, dimethylether and alkene. These initiatives will allow us to further develop our core coal production business while contributing to the satisfaction of China's energy demand. We will increase our investment in research and development and cooperate with well-established research institutions in China and abroad. By developing techniques suitable for large-scale production of coal-based chemicals, we intend to build-up our proprietary patented technologies and seek new sources of income.

We further intend to promote the concept of the recycling and reuse of by-products and comprehensive resource utilization. By leveraging our current coking operations, we plan to expand our product lines to include coal-based chemical products such as methanol, tar and refined crude benzene.

***Strengthen our sales and marketing networks, optimize operations, enhance marketing capabilities and increase our market share.***

With a broad customer base and extensive marketing experience gained from years of operation, coupled with our existing marketing channels, we intend to increase our customer base through the expansion



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of our sales network, market research and consolidation of our sales and marketing facilities. We intend to increase our export volumes and achieve increased brand name recognition, with the goal of gaining international market share.

We intend to enhance our capital investment, expand our logistics network and strengthen our control of this network by actively investing in major coal suppliers, railways and ports. We are also dedicated to controlling logistics costs and promoting value-added services. By leveraging our diversified coal products and specialized coal processing and blending capabilities, we will provide a wide variety of customer-specific products and services to our customers. We believe our ability to provide tailored products is one of our competitive advantages.

We are the principal channel for coal export in China. In 2005, we exported approximately 45.7% of China's total coal export volume. We export coal via all the major coal loading ports from northern to southern China, including Qinhuangdao Port, Tianjin Port, Qingdao Port, Rizhao Port and Lianyungang Port.

Guided by this customer-centric principle, we plan to expand our regional sales and customer service centers to further improve and extend pre-sales and after-sales services such as transportation logistics support to our domestic and international customers.

***Increase our research and development efforts to lower production costs and increase the value of our products.***

We view our continuing development and operations as being dependent upon the research and development efforts in each of our operational segments. Therefore, we have established two design centers in China, the Datun Coal Mine Design Centre and Zhangjiakou Coal Mining Equipment Design Centre Company, for research in coal mining techniques and coal mining equipment. The Datun Coal Mine Design Centre is actively engaged in the research and development of more cost-efficient and effective coal mining techniques in underground coal mines. The Zhangjiakou Coal Mining Equipment Design Centre has recently undertaken projects for the development of domestically produced mining equipment, including heavy-duty armored-face conveyors and a complete set of 6.0 million-tonne face equipment. Through these research and development efforts, we believe we can effectively lower production costs and introduce high value, high quality coal mining equipment to satisfy market needs.

We believe that strengthening our research and development efforts will also allow us to increase our own technological skills. We also believe that by securing intellectual property rights, we will be able to better protect the results of our research and development activities. We will continue to invest in research and development in each of our operational segments, including through the establishment of a new national design center to foster the development of talented researchers and through increased contributions to research funds.

***Improve production safety and environmental protection to ensure our continuing development.***

We regard production safety as one of our most important corporate objectives. We are committed to maintaining and protecting the health and safety of our employees by formulating and implementing strict safety standards in the workplace. In 2003, 2004 and 2005, the production fatality rate at our mines was 0.12, 0.15 and 0.08 persons per million tonnes of raw coal, respectively. This was substantially lower than the average fatality rate of coal mines in China, which was 4.17, 3.10 and 2.81 persons per million tonnes of raw coal, respectively, during the same period. We will continue to invest in production safety.

We are in the process of improving the technologies and systems currently in use to enhance the efficiency of our coal production and increase our resource utilization. We are committed to the research and

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development of clean coal production technology and the development of coal processing and blending technologies. We focus on the environmentally friendly treatment and utilization of coal slack, slime, coal bed gas, surface and subsurface water discharge and other accompanying by-products, and also, in particular, on the development of electric power plants. In our key mining areas, we have installed environmental protection equipment to enhance the utilization of resources. For example, the circulating fluidized bed boilers used in our Datun power plant can effectively burn different types of solid coal waste, and had the capacity to process 720,070 tonnes of low quality coal in 2005. We expect to expand the use of the circulating fluidized bed boilers at our power plants to increase our resource utilization rate. We are equally committed to environmental protection and will ensure compliance with the relevant environmental protection laws and regulations in all aspects of our operations. We conduct environmental feasibility studies for all of our new production and expansion projects and have adopted a strict policy of using appropriate facilities for the discharge and treatment of pollutants and waste.

We believe that our focus on production safety, economic recycling and integrated resource utilization will further lower our accident rate, enhance our productivity and lower our current and future environmental protection costs.

### *Optimize internal control by strengthening our financial management and investment decision-making.*

We are committed to strictly implementing our policies on financial budgeting, financial reporting and internal control. We will further strengthen our financial management through an advanced financial information system.

We plan to enhance the careful and conservative monitoring of our cash flow, accounts receivable and capital expenditures by centralizing the authority to make major investment decisions at the corporate level. We will strictly follow our development strategy and investment return requirements when evaluating investment opportunities. We also plan to improve project management of our investments and improve our investment skills, reduce risks and seek higher returns.

## PRINCIPAL PRODUCTS AND SERVICES

Our principal operations include:

- Coal operations, which is our core business and includes coal production and sales and coal trading;
- Coking operations, including the production and sale of coke and coal-based chemical products;
- Coal mining equipment manufacturing operations, including coal mining equipment design, research and development, manufacturing and sales operations and after-sale services; and
- Other operations, including provision of coal mine design services.

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The following table sets forth the contributions by each of our operating segments in terms of revenue from outside customers and as a percentage of our total revenue for the periods indicated:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
	RMB (million)	%	RMB (million)	%	RMB (million)	%	RMB (million)	%	RMB (million)	%
<i>Segments</i>										
Coal operations . . . . .	11,656.7	80.5	17,733.0	80.0	25,147.7	83.7	12,600.1	83.9	11,761.0	80.1
Coking operations . . . . .	1,064.9	7.4	2,039.2	9.2	1,591.3	5.3	938.6	6.3	1,012.4	6.9
Coal mining equipment manufacturing operations . . . . .	1,057.9	7.3	1,479.4	6.7	1,891.2	6.3	889.1	5.9	971.9	6.6
Coal mine design and other businesses . . . . .	701.2	4.8	912.2	4.1	1,431.1	4.8	584.1	3.9	934.4	6.4
Total . . . . .	<u>14,480.8</u>	<u>100.0</u>	<u>22,163.8</u>	<u>100.0</u>	<u>30,061.3</u>	<u>100.0</u>	<u>15,011.9</u>	<u>100.0</u>	<u>14,679.7</u>	<u>100.0</u>

### COAL OPERATIONS

We generate our coal operations revenue primarily from (i) sales of coal extracted from our mines and coal processed by our facilities, and (ii) proprietary coal trading and the provision of coal import agency and export-related services. Our sales are made both within China through our own sales forces and overseas through ChinaCoal Group. See “Connected Transactions”.

We produce thermal coal, coking coal and semi-hard coking coal products from our nine operational coal mines located in four mining areas and thirteen coal processing plants located in northern, northwestern and eastern China. The following table sets forth the revenue from each business activity of our coal operations in the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2005 and 2006:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
	RMB (million)	%	RMB (million)	%	RMB (million)	%	RMB (million)	%	RMB (million)	%
Coal production and sales . . . . .	7,508.7	64.4	13,375.1	75.4	17,596.8	70.0	8,254.5	65.5	8,801.9	74.8
Coal trading and services <sup>(1)</sup> . . . . .	4,148.0	35.6	4,357.9	24.6	7,550.9	30.0	4,345.6	34.5	2,959.1	25.2
Total . . . . .	<u>11,656.7</u>	<u>100.0</u>	<u>17,733.0</u>	<u>100.0</u>	<u>25,147.7</u>	<u>100.0</u>	<u>12,600.1</u>	<u>100.0</u>	<u>11,761.0</u>	<u>100.0</u>

(1) Includes resale and proprietary trading of coal purchased from third party coal producers, coal import agency services and coal export-related services.

### *Coal Production and Sales*

#### **Our coal mines**

As of the Latest Practicable Date, we had nine operational mines, including two open pit mines and seven underground mines. These mines are located in Shanxi, Shaanxi and Jiangsu Provinces. As of 30 June 2006, we had 9,489 million tonnes of coal resources, including total marketable reserves of 3,003 million tonnes, under our management. The estimated indicative life of our coal reserves may increase significantly when the available Inferred Coal Resources are converted to reserves following further mining and testing. Our mines currently have in excess of approximately 4,000 million tonnes of Inferred Coal Resources. In addition, we plan to increase our exploratory efforts as we continue to develop our reserve areas.

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The following table presents the coal reserves for each of our mining areas:

	<u>Proved reserves</u>	<u>Probable reserves</u>	<u>Proved and probable reserves</u>	<u>Recoverable reserves<sup>(3)</sup></u>	<u>Marketable reserves<sup>(4)</sup></u>
	(million tonnes)				
<b>Mining area<sup>(1)</sup></b>					
Pingshuo Mining Area <sup>(2)</sup> .....	1,181	1,331	2,512	2,351	2,047
Liliu Mining Area and Xiangning Mining Area <sup>(2)</sup> .....	338	390	728	752	684
Datun Mining Area <sup>(2)</sup> .....	173	84	257	266	221
Nanliang Mining Area <sup>(2)</sup> .....	28	23	51	51	51
<b>Total</b> .....	<b>1,720</b>	<b>1,828</b>	<b>3,548</b>	<b>3,420</b>	<b>3,003</b>

- (1) Reserves data includes reserves of our operational mines and mines under development. According to the SRK Report, we own the rights to 9,489 million tonnes of coal resources. The estimated indicative life of our coal reserves may increase significantly when the available Inferred Coal Resources are converted to reserves following further mining.
- (2) Resources and reserves are presented in the SRK Report. For our equity interests in these mining areas, see “Restructuring”.
- (3) Recoverable reserves of the mining areas are calculated by multiplying proved and probable reserves with mining dilution taking into account mining loss. The mining recovery rate is assumed to be 95% for open pit mines and 75% for underground mines.
- (4) Marketable reserves of the mining areas are calculated by multiplying recoverable reserves with the processing plant yield percentages.

The following table sets forth detailed information for each of our twelve mines as of 30 June 2006:

	Pingshuo Mining Area <sup>(2)</sup>				Liliu Mining Area and Xiangning Mining Area <sup>(2)</sup>			Datun Mining Area <sup>(2)</sup>			Nanliang Mining Area <sup>(2)</sup>	
	Operational mines		Mines under development		Shaqu	Wangjialing	Yaotiao	Operational mines		Kongzhuang	Operational mine	
	Antaihao	Anjialing	Antaihao	Pingshuo <sup>(4)</sup> East				Xuzhuang	Longdong			Nanliang
<b>Background data:</b>												
Start of commercial production .....	1987	2001	2004	2008	2009	2004	2009	1976	1979	1987	1977	1998
Mining area ( <i>square kilometers</i> ) .....	24.0	54.7	10.7	19.2	48.7	138.4	176.7	63.8	38.4	25.0	44.1	19.3
Nature of mine .....	OP	OP	UG	UG	OP	UG	UG	UG	UG	UG	UG	UG
<b>Reserve data:</b>												
Total in-place proved and probable reserves <sup>(1)(2)</sup> ( <i>million tonnes as of 30 June 2006</i> )	158	686	191	496	981	409	319	155	48	23	32	51
<b>Production data:</b>												
Raw coal production capacity ( <i>million tonnes per annum</i> ) .....	16.0	14.5	20.0	8.0	20.0	3.0	6.0	3.7	1.5	1.2	1.3	0.75
Raw coal production ( <i>million tonnes</i> )												
2003 .....	13.6	11.0	—	n/a	n/a	1.0	n/a	3.5	1.5	1.1	1.2	0.4
2004 .....	14.8	14.5	0.9	n/a	n/a	1.6	n/a	3.4	1.4	1.2	1.2	0.8
2005 .....	16.4	15.0	8.7	n/a	n/a	1.9	n/a	3.4	1.4	1.2	1.2	1.0
Six months ended 30 June 2006 .....	9.4	9.2	6.6	n/a	n/a	1.3	n/a	1.9	0.8	0.7	0.6	0.5

(1) Reserves and resources data includes reserves and resources of our operational mines and mines under development for which we have obtained mining rights certificates.

(2) Resources and reserves are reported on a 100% ownership basis for our wholly and majority owned mines. We own a 100% interest in the Pingshuo Mining Area. We own a 55% interest in the Nanliang Mine and a 62.43% equity interest in Shanghai Datun Energy, which owns the Datun Mining Area. We own a 50% equity interest in the Huajin Joint Venture, which owns and operates the Liliu Mining Area and the Xiangning Mining Area.

(3) Mining method includes open pit (“OP”) mines and underground (“UG”) mines.

(4) As of the Latest Practicable Date, we obtained the exploration right permit to formulate our production plan for the purpose of applying for the mining right permit in respect of Pingshuo East Open Pit Mine. We are currently applying for the mining rights. Subject to governmental approval, the mining rights are expected to be obtained in March 2007.

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The following map illustrates the locations of our mining areas:



### *Pingshuo Mining Area*

The Pingshuo Mining Area is the key mining area within the Jinbei Base, one of only 13 large coal bases in China designated by the PRC Government. The Pingshuo Mining Area currently consists of the Antaibao Open Pit Mine and the Anjialing Open Pit Mine, which are among the largest open pit mines in China in terms of production capacity, as well as the Anjialing Underground Mine. Substantially all coal produced at the Pingshuo Mining Area is high-quality thermal coal.

The Pingshuo Mining Area is located in northern Shanxi Province. Coal products are loaded onto 10,000-tonne trains at five coal loadout depots, and are transported via the Beitongpu and the Daqin Rail Lines directly to major coal loading ports and certain of our key customers in the coastal regions. The commencement of trial operations of three coal loadouts in 2006 will further enhance the transportation capacity of our coal. In addition, the PRC Government plans to increase the Daqin Rail Line's annual transportation capacity from its current capacity of 200 million tonnes to a target capacity of 400 million tonnes by the end of 2010.

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We are currently undergoing various capacity expansion projects at our Antaibao Open Pit Mine, Anjialing Open Pit Mine and Anjialing Underground Mine, all of which are located in the Pingshuo Mining Area. In addition, we are constructing the new Antaibao Underground Mine and the Pingshuo East Open Pit Mine within the Pingshuo Mining Area. See “— Expansions of our coal mines — Coal mines under development.”

*Antaibao Open Pit Mine.* We are currently extracting raw coal from three primary coal seams with thicknesses of 10, 14 and 4.5 meters at our Antaibao Open Pit Mine. As of 30 June 2006, the total marketable reserves at Antaibao Open Pit Mine amounted to 131 million tonnes. The Antaibao Open Pit Mine primarily produces thermal coal from an open pit employing the truck-and-shovel mining method. In 2005, the Antaibao Open Pit Mine’s annual production output was 16.44 million tonnes. As of 30 June 2006, the recovery rate of Antaibao Open Pit Mine was 96.0%.

*Anjialing Mines.* The Anjialing Mines consist of an open pit mine and an underground mine. We utilize a surface-and-tunnel extraction mining method in the Anjialing Mines to maximize the recovery rate. We are currently extracting raw coal from four primary coal seams with thicknesses of 9.5, 0.6, 14.4 and 4.2 meters at the Anjialing Open Pit Mine, and 7.3, 3.1, 13.8 and 3.7 meters at the Anjialing Underground Mine.

The total marketable reserves of the Anjialing Open Pit Mine were 572 million tonnes as of 30 June 2006. The Anjialing Open Pit Mine produces thermal coal employing the truck-and-shovel mining method. In 2005, the Anjialing Open Pit Mine’s annual production output was 15.01 million tonnes. As of 30 June 2006, the recovery rate of the Anjialing Open Pit Mine was 97.0%.

The Anjialing Underground Mine is an extension of the Anjialing Open Pit Mine, exploiting the same coal seams. The Anjialing Underground Mine is the newest addition to our operational mines, with an annual production capacity of 20.00 million tonnes. It commenced full production in September 2005. The total marketable reserves at the Anjialing Underground Mine were 146 million tonnes as of 30 June 2006. As of 30 June 2006, the recovery rate of the Anjialing Underground Mine was 84.0%.

### *Liliu Mining Area*

Our Liliu Mining Area, the main mining area at the Jinzhong Base, one of only 13 large coal bases in China designated by the PRC Government, is well recognized for its superior quality coking coal, which is ideal for metallurgical usage. Coking coal produced from the Liliu Mining Area has been designated by the PRC Government as a scarce and valuable mineral resource vital to national economic development. To protect this valuable mineral resource from over-exploitation and unauthorized exploitation, the PRC Government has designated the Liliu Mining Area as one of the three most valuable and best-quality coking coal reserves in China subject to national resources protection and supervision. The Liliu Mining Area is located in western Shanxi Province. Our Liliu Mining Area currently includes one operational mine, the Shaqu Mine, operated by the Huajin Joint Venture, in which we hold a 50% equity interest.

We own a 4,356-meter mine railway connecting our coal processing plant in the Liliu Mining Area to the Xiaoliu Rail Line, which in turn runs from Xiaoyi to Liulin and is the main rail line used for transporting our coal products to customers and ports.

*Shaqu Mine.* We are currently extracting raw coal from five primary coal seams with thicknesses of 3, 2.7, 7, 7 and 7 meters at the Shaqu Mine.

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The total marketable reserves at the Shaqu Mine were 379 million tonnes as of 30 June 2006. The Huajin Joint Venture utilizes the longwall mining method in the Shaqu Mine. In 2005, the Shaqu Mine's annual production output was 1.87 million tonnes of coking coal. As of 30 June 2006, the recovery rate of the Shaqu Mine was 69.0%.

### *Datun Mining Area*

The Datun Mining Area is one of the few coal mines that are in close proximity to the fast-growing and strategically important coal-consuming markets of Shanghai and other industrial centers in Eastern China, where we expect future demand for thermal and coking coal to increase significantly. Our Datun Mining Area integrates coal production, power generation and railway transportation facilities. Major coal products produced at the Datun Mining Area include semi-hard coking coal that can be further processed to metallurgical coal or thermal coal. The Datun Mining Area currently consists of four underground mines. We utilize the longwall mining method to extract raw coal from each of these mines.

The Datun Mining Area has convenient access to major transportation arteries and hubs, including the Longhai Rail Line, Rizhao Port and Lianyungang Port, and is in close proximity to major customers such as Baosteel Group. Transportation flexibility is further increased by easy access to a system of inland waterways in the greater Shanghai area. We believe that the location and access to transportation alternatives of the Datun Mines provide significant transportation cost advantages and reduce the risk of disruptions or delays due to transportation capacity constraints.

*Yaoqiao Mine.* We are currently extracting raw coal from three primary coal seams with thicknesses of 5.5, 3.3 and 1.1 meters at the Yaoqiao Mine. As of 30 June 2006, the total marketable reserves at the Yaoqiao Mine amounted to 130 million tonnes. In 2005, the Yaoqiao Mine's annual production output was 3.40 million tonnes. As of 30 June 2006, the recovery rate of the Yaoqiao Mine was 82.6%.

*Xuzhuang Mine.* We are currently extracting raw coal from three primary coal seams with thicknesses of 5, 2.9 and 1.1 meters at the Xuzhuang Mine. The total marketable reserves at the Xuzhuang Mine amounted to 40 million tonnes as of 30 June 2006, and its annual production output was 1.41 million tonnes in 2005. As of 30 June 2006, the recovery rate of the Xuzhuang Mine was 76.8%.

*Longdong Mine.* We are currently extracting raw coal from two primary coal seams with thicknesses of 5.5 and 0.7 meters at the Longdong Mine. The total marketable reserves at the Longdong Mine amounted to 21 million tonnes as of 30 June 2006. According to the SRK report, the Longdong Mine's production output was 1.16 million tonnes in 2005. As of 30 June 2006, the recovery rate of the Longdong Mine was 77.6%.

*Kongzhuang Mine.* We are currently extracting raw coal from three primary coal seams with thicknesses of 4.9, 3.1 and 0.8 meters at the Kongzhuang Mine. The total marketable reserves at the Kongzhuang Mine amounted to 30 million tonnes as of 30 June 2006 and its annual production output was 1.15 million tonnes in 2005. As of 30 June 2006, the recovery rate of the Kongzhuang Mine was 74.7%.

### *Nanliang Mining Area*

Our Nanliang Mining Area consists of one underground mine, the Nanliang Mine, located in northern Shaanxi Province. We are currently extracting raw coal from five primary coal seams with thicknesses ranging from 1.1 meters to 4.1 meters at the Nanliang Mine. The total marketable reserves of the Nanliang Mine amounted to 51 million tonnes as of 30 June 2006. The Nanliang Mine primarily produces thermal coal by utilizing the longwall mining method. In 2005, the annual production output of this mine was 0.98 million tonnes. As of 30 June 2006, the recovery rate of the Nanliang Mine was 75.0%.



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### Our Coal Processing Plants

We own and operate a total of thirteen coal processing plants, ten of which are located in close proximity to our mines, and three of which are strategically positioned at major coal collection and transportation centers in Shanxi Province. At these facilities, we process and blend raw coal extracted from our mines, along with coal we purchase from other coal producers. By purchasing raw coal from local and regional producers, we are able to increase our total coal output, and sell such coal through our extensive sales and distribution networks to our customers. We have constructed a new processing plant at the Shaqu Mine, which is currently under trial production. We have also recently commenced trial operations at three new coal processing plants in the Pingshuo Mining Area.

We use modern dense media processing methods for the majority of our coal processing. The following table sets forth key information regarding our coal processing plants:

	Output in 2005 (million tonnes)	Output in 2006E (million tonnes)	Processing method	Coal yield <sup>(1)</sup> (%)	Designed annual capacity (million tonnes)	Utilization rate in 2006E (%)
<b><i>Pingshuo Mining Area</i></b>						
Antaibao . . . . .	15.8	19.16	DMC	82	15.0	127.7 <sup>(2)</sup>
New Antaibao <sup>(3)</sup> . . . . .	—	3.79	DMC	80	10.0	37.9
Anjialing . . . . .	15.5	17.17	DMC	80	15.0	114.5
New Anjialing <sup>(4)</sup> . . . . .	—	3.30	DMC	80	10.0	33.0
Muguajie <sup>(5)</sup> . . . . .	—	0.57	DMC	80	6.0	9.5
<b><i>Liliu Mining Area</i></b>						
Shaqu . . . . .	1.0 <sup>(6)</sup>	1.57 <sup>(6)</sup>	Jig	85	1.5	52.3 <sup>(6)</sup>
New Shaqu . . . . .			DMC	85	3.0	
<b><i>Datun Mining Area</i></b>						
Datun . . . . .	1.3	1.25	Jig	68	1.8	69.4
Longdong . . . . .	1.3	0.21	Jig	85	1.2	17.5
Kongzhuang . . . . .	0.9	0.92	DMC	68	1.1	83.6
<b><i>Other Coal Processing Plants</i></b>						
Shuozhong . . . . .	2.5	1.85	DMC	75	5.0	37.0
Zhongxin . . . . .	2.7	1.01	DMC	85	3.6	28.1
Dazhong . . . . .	<u>3.3</u>	<u>1.60</u>	DMC	92	3.6	44.4
<b>Total</b> . . . . .	<u><u>44.2</u></u>	<u><u>52.40</u></u>				

(1) Coal yield is for wash plant yield only.

(2) Utilization rates of our coal processing plants are estimated as of 30 June 2006 based on the assumption that each coal processing plant will be operated on a 300-day basis annually. As a result, where any one of the coal processing plants is operated for more than 300 days in any given year at its full capacity, its utilization rate may exceed 100%.

(3) New Antaibao commenced trial operations in July 2006.

(4) New Anjialing commenced trial operations in June 2006.

(5) Muguajie commenced trial operations in February 2006.

(6) On 3 August 2005, the new coal processing plant at the Shaqu Mine replaced the Shaqu coal processing plant.

### Expansion of Our Coal Mines

#### *Coal mines under development*

***Antaibao Underground Mine.*** We commenced construction of an underground mine, the Antaibao Underground Mine, in the Pingshuo Mining Area in 2005. As of 30 June 2006, the total proved and probable

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reserves of this mine were 496 million tonnes and the marketable reserves amounted to 380 million tonnes, according to the SRK Report. After its completion, coal from the Antaibao Underground Mine will be used to produce thermal coal products. The Antaibao Underground Mine is scheduled for full production in 2009, and it is expected to have an annual production volume of 8.0 million tonnes of coal. We plan to spend approximately RMB298.0 million, RMB390.0 million and RMB29.0 million, respectively, in 2006, 2007 and 2008 on the construction of the Antaibao Underground Mine.

***Pingshuo East Open Pit Mine.*** We commenced construction of our third open pit mine, the Pingshuo East Open Pit Mine, in the Pingshuo Mining Area in 2006. As of 30 June 2006, the total proved and probable reserves of this mine were 981 million tonnes and the marketable reserves amounted to 818 million tonnes, according to the SRK Report. Coal from the Pingshuo East Open Pit Mine will be used to produce thermal coal products. Full production is scheduled for 2009 with a planned annual output of 20.0 million tonnes of coal. We plan to spend approximately RMB200.0 million, RMB2,447.0 million and RMB2,224.0 million on the construction of the Pingshuo East Open Pit Mine in 2006, 2007 and 2008, respectively. As of the Latest Practicable Date, we obtained the exploration right permit to formulate our production plan to apply for the mining right permit in respect of the Pingshuo East Open Pit Mine. We are currently applying for the mining rights. Subject to the government approval, the mining rights are expected to be obtained in March 2007.

***Wangjialing Underground Mine.*** The Huajin Joint Venture is currently constructing a large underground mine, the Wangjialing Mine. Wangjialing Underground Mine is situated at the southwestern part of the Xiangning Mining Area in the Shanxi Province. All the coal mined at the Wangjialing Underground Mine will be used to produce coking coal products. As of 30 June 2006, the total proved and probable reserves of this mine were 319 million tonnes and the marketable reserves amounted to 305 million tonnes. We expect the Wangjialing Underground Mine to reach a total production capacity of 6.0 million tonnes once it reaches full production in 2010. In addition, the Huajin Joint Venture plans to construct a coal processing plant with a designed production capacity of 6.0 million tonnes per annum and an electric power plant with an installed capacity of 2 x 50 MW using coal tailing from the Wangjialing Underground Mine as fuel to power the mine and the coal processing plant. The total investment in the construction of the Wangjialing Underground Mine and ancillary facilities is estimated to be RMB2,311.2 million. The Huajin Joint Venture plans to spend RMB182.0 million, RMB1,070.0 million and RMB1,023.0 million on the expansion project in 2006, 2007 and 2008, respectively.

We believe that by 2010, after commencement of full production at these three new mines, our total annual coal production capacity will exceed 100.0 million tonnes.

### **Risk Assessment**

Our independent technical consultant, SRK, has performed a risk assessment on each of our coal mines and coal processing plants and has confirmed in its report that none of them is at high risk. SRK has further confirmed that no management problems or foreseeable dangers and risks of decreased production exist at our coal mines and coal processing plants. Our management team is aware of the operational risks and fully understands that the management of safety and production are important elements to reduce the operational risks involved. However, we do not have any provisions for any unforeseeable decreases in production. As all of our production facilities operate on the basis of designed production capacity, in the event that any unforeseeable events result in decreased production, SRK is of the opinion that we do not have additional production capacity to compensate for any loss in production volumes. See “Appendix VI — Independent Technical Report”.

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### Coal products

Our coal products include raw coal extracted from our own mines. We blend coal at our processing plants from various sources, including our own mines, to achieve specific thermal contents, as well as particular chemical and physical properties, in accordance with customer requirements. The required properties may vary depending on the intended use of the coal, such as for power generation, metallurgical production, or other purposes. We produce a variety of coal products based on our customers' needs and subject to the quality and properties of the coal produced from each of our coal mines. The following table sets forth certain coal characteristics of our current principal coal products:

	<u>Calorific value</u> (Kcal/kg)	<u>Sulphur content</u> (%)	<u>Ash content</u> (%)	<u>Moisture content</u> (%)	<u>Ash fusion temperature</u> (°C)	<u>Volatile matter content</u> (%)
<i>Thermal coal</i>						
Pingshuo No. 1 .....	5,800	1.0	17.0	9.0	1,400	30.5
Pingshuo No. 2 .....	5,500	1.3	20.0	9.0	1,400	30.0
Pingshuo No. 3 .....	5,000	1.2	26.0	9.0	1,400	28.0
Pingshuo No. 4 .....	4,000	1.3	36.0	9.0	1,400	24.0
Pingshuo No. 5 .....	4,900	—	27.0	9.0	1,400	28.0
Pingshuo No. 6 .....	5,200	1.1	21.0	11.5	1,400	30.0
Datun Thermal .....	5,500	1.0	21.5	8.0	1,400	38.0
Nanliang Thermal .....	6,000	0.4	10.0	12.5	1,150	33.0
<i>Coking coal</i>						
Huajin Metallurgical .....	—	<0.5	<10.0	10.0	—	18.0-21.0
<i>Semi-hard coking coal</i>						
Datun Metallurgical .....	—	0.75	7.5	13.0	—	37.0

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### Mining rights

The mining rights associated with each of the Pingshuo Mining Area, Liliu Mining Area, Xiangning Mining Area, Datun Mining Area and Nanliang Mining Area are owned by the respective operator of the mine. We hold at least a majority interest in all of these mine operators, except for the Huajin Joint Venture, in which we hold a 50% interest. Registered holders of mining right permits are required to pay mining right permit fees and taxes to the government. See “Appendix VI — Independent Technical Report” for detailed information on our mining right permits. The following table sets forth details of our mining rights.

<u>Mining area/mines</u>	<u>Registered mining right permit holder/certificate number</u>	<u>Mining method*</u>	<u>Area</u> (km <sup>2</sup> )	<u>Mining right permit date</u> (year/month)	<u>Mining right validity</u> (years)	<u>Mining right permit renewal date</u> (year/month)
<b>Operational mines</b>						
<b>Pingshuo Mining Area</b>						
Antaibao . . . . .	Shanxi China Coal Ping Shuo Antaibao Coal Company Limited/ 1000000620107	OP	24.0	2006/09	25	2031/01
Anjialing . . . . .	Pingshuo Anjialing Surface Mine Co., Ltd./ 1000009940011	OP	54.7	1999/05	30	2029/05
Anjialing . . . . .	Pingshuo Anjialing Surface Mine Co., Ltd./ 1000000410027	UG	10.7	2004/07	30	2034/07
<b>Liliu Mining Area</b>						
Shaqu . . . . .	Huajin Coking Coal Co., Ltd./ 1000000420071	UG	138.4	2004/12	27	2031/09
<b>Datun Mining Area</b>						
Yaoqiao . . . . .	Shanghai Datun Energy Resources Co., Ltd./ 1000000020071	UG	63.8	2000/04	29	2029/04
Kongzhuang . . . . .	Shanghai Datun Energy Resources Co., Ltd./ 1000000020072	UG	44.1	2000/04	29	2029/04
Xuzhuang . . . . .	Shanghai Datun Energy Resources Co., Ltd./ 1000000320025	UG	38.4	2003/08	26	2029/04
Longdong . . . . .	Shanghai Datun Energy Resources Co., Ltd./ 1000000020073	UG	25.0	2000/04	29	2029/04
<b>Nanliang Mining Area</b>						
Nanliang . . . . .	Shaanxi Nanliang Coal Co., Ltd./ 1000009920052	UG	19.3	1999/08	20	2019/08
<b>Mines under development</b>						
Antaibao . . . . .	Our Company/ 1000000620127	UG	19.2	2006/11	29	2036/08
Wangjialing . . . . .	Huajin Coking Coal Co., Ltd./ 1000000420072	UG	176.7	2004/12	27	2031/09

\* Mining method includes open pit (“OP”) mines and underground (“UG”) mines.

In addition, as of the Latest Practicable Date, we obtained the exploration right to formulate our production plan for the purpose of applying for the mining right permit in respect of the Pingshuo East Open Pit Mine, which is currently still under development. We are currently applying for the mining right permit. Subject to the government approval, the mining right permit is expected to be obtained in March 2007. According to an opinion issued by our PRC legal adviser, Jia Yuan Law Firm, under PRC laws, there are no legal obstacles to obtaining such mining right permit; however, in the event that we are unable to obtain such mining right permit at the expected date, our business development and financial condition may be adversely affected. We own the mining right permit for the Antaibao Underground Mine.

Where residual reserves remain after the term of the mining rights expires, the holders of such mining rights have a preemptive right to apply for extensions for additional terms, according to the mineral resources regulations of the PRC and corresponding regulations. There is no minimum residual reserve requirement for the renewal of mining rights, provided that any residual reserves remain. Apart from the remaining proved and

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probable reserves within a mining area, there are no other conditions affecting the application for extension for additional terms provided that the holder of such mining rights has fulfilled all of its obligations. If any of our mines has any residual proved and probable reserves when its mining right permit expires, we intend to submit an application to renew the mining right permit. The Directors of our Company believe that under the current legal requirements there would be no foreseeable major obstacle in renewing our mining rights when any of them expire. The following table sets forth details of the recoverable reserves, the year the mining rights should be renewed, volumes mined under the current mining right tenure and volumes mined under the renewed mining right tenure of our mines. See also “Appendix VI — Independent Technical Report” to this Prospectus for mining quantities under current mining rights and renewed mining rights.

<u>Mine</u>	<u>Recoverable reserves<sup>(1)</sup></u> (Mt)	<u>Year the mining rights should be renewed</u>	<u>Tonnes mined under current mining right tenure</u> (Mt)	<u>Tonnes mined under renewed mining right tenure</u> (Mt)
<b><i>Pingshua Mining Area</i></b>				
Antaibao Open Pit .....	151	2031	151	—
Anjialing Open Pit .....	656	2029	575	81
Anjialing Underground .....	168	2034	168	—
Pingshuo East Open Pit <sup>(2)</sup> .....	939			
Antaibao Underground .....	<u>436</u>	<u>2036</u>	<u>240</u>	<u>196</u>
<b><i>Liliu Mining Area</i></b>				
Shaqu .....	423	2031	125	298
Wangjialing .....	<u>330</u>	<u>2031</u>	<u>150</u>	<u>180</u>
<b><i>Datun Mining Area</i></b>				
Yaoqiao .....	161	2029	78	83
Xuzhuang .....	50	2029	32	19
Longdong .....	23	2029	23	—
Kongzhuang .....	<u>33</u>	<u>2029</u>	<u>26</u>	<u>7</u>
<b><i>Nanliang Mining Area</i></b>				
Nanliang .....	<u>51</u>	<u>2019</u>	<u>16</u>	<u>35</u>
<b>Total</b> .....	<u><u>3,420</u></u>		<u><u>1,584</u></u>	<u><u>898</u></u>

(1) Recoverable reserves are based on 30 June 2006 figures.

(2) As of the Latest Practicable Date, we obtained the exploration right permit to formulate our production plan to apply for the mining right permit in respect of the Pingshuo East Open Pit Mine. We are currently applying for the mining rights. Subject to government approval, the mining rights are expected to be obtained in March 2007.

### **Coal production process**

Our mining operations involve five main processes: tunneling and underground mine layout, which is applicable to underground mines only, mining, conveying, coal processing and reclamation.

#### *Tunneling and Underground Mine Layout*

When constructing an underground mine, the tunneling process is necessary for the installation of conveyors and for the preparation of the mining work face. We also use tunneling to construct new longwall mining work faces after we finish constructing the underground mine to ensure continuous mining operations. We use high-powered tunneling machines to make tunnels where conditions are suitable. When the geological conditions are not suitable for the use of tunneling machines, we use explosives for tunneling. We send all the

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coal extracted from these tunnels to our coal bunkers and store it together with the coal extracted from the longwall coalfaces.

### *Extracting*

We use two principal mining methods for underground mines:

- If the depth and geological conditions of the coal seam are suitable, we utilize an advanced and comprehensive top coal caving mining technology to extract the coal. After utilizing longwall mining technology to mine the coal at the height of the supporting facilities of the mining face and lowering the tail canopy of the hydraulic roof support, the pressure from the roof of the coal seam will cause the coal at the top to naturally drop to the conveyor behind the hydraulic roof support, which will convey the coal outside of the coal mining face. This technology has the benefit of high mining efficiency, safety and high recovery rate.
- The longwall mining technique is a fully mechanized mining method for underground mines. The mining face is supported by hydraulic roof supports, and the coal is extracted by coal shearers, after which the coal is conveyed by a conveyor system to the ground surface. Once the area utilizing the longwall mining has been mined, the longwall mining system will be moved to a new mining area. The benefits of the longwall mining system are high production volumes, high recovery rates, safety and reliability.

Coal extraction at our open pit mines is conducted using the following process:

- At present, coal production at our open pit mines utilizes a truck-and-power shovel mining system. We determine the mining area arrangement and overburden stripping position in accordance with the alignment of the coal deposit. Subsequent to professional blasting of the mines, the rock is removed by power shovel and truck from above the coal seam. Coal is extracted using a power shovel and transported to our processing plant using a truck and conveyor system.
- We believe that with the technological advancements allowing greater access to the mining face in the open pit mines, we will in the future use continuous or semi-continuous mining methods that combine the use of power shovels and removable crushers and conveyors so as to control and reduce costs.

### *Conveying*

We convey the coal we extract from our coal mines either to ground storage or to the respective coal processing plants via an overland conveyor system, such as by conveyor belts or trucks. In addition, we have constructed comprehensive underground roadway systems in each of our underground mines to transport workers and equipment.

### *Coal processing*

We transport raw coal to our coal processing plants after excavation for classification and for further purification to remove slush, rock, inorganic sulfur and other contaminants. We also blend different types of coal to adjust its coal characteristics and quality to meet customer specifications. Each of our four mining areas has one or more coal processing plants. In addition, we have constructed three independent coal processing plants at major coal collection and transportation centers in Shanxi Province, for a total of thirteen coal processing plants owned and operated by us. All of our coal processing plants are highly automated and

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equipped with advanced coal processing facilities. We purchase most of our equipment from international manufacturers. After the coal has been processed, it is loaded onto cars through automated, high-speed loadout depots connected to our mine railways.

### *Reclamation*

We believe that the operations at all of our mines are in substantial compliance with environmental and reclamation requirements. We are required by the PRC laws to reclaim and restore mining sites to their prior condition after completion of mining operations. Reclamation activity typically involves the removal of buildings, equipment, machinery and other physical remnants of mining, restoration of land features in mined-out areas, dumping sites and other mining areas, and contouring, covering and revegetation of waste rock piles and other disturbed areas. We had accrued RMB698.5 million for the provision of close down, restoration and environmental costs as of 30 June 2006.

### **Raw materials, energy and water**

We purchase certain raw materials for our coal production and sales, consisting principally of coal purchased from third parties that we blend with our coal. Other materials include facility accessories, diesel fuel, explosives for mining activities and roof supporting materials.

We believe that we have established stable cooperative relationships with our key suppliers of raw materials, which enable us to obtain a reliable supply of most of the materials required by our coal production process. We further believe that many alternative suppliers exist for most of the materials we purchase and, therefore, we do not foresee any difficulty in obtaining an adequate supply of these materials. We generally receive credit terms from our suppliers for our coal operations ranging from ten days to one month.

Electricity and diesel fuel are our main sources of energy.

Our main source of water is underground water. We have not experienced any major disruption in electricity, diesel fuel or water supply in recent years.

### **Coal sales**

The following table sets forth information regarding the domestic and overseas sales of raw coal from our mines and clean coal processed at our coal processing plants:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
	(Million tonnes)	(% of total)	(Million tonnes)	(% of total)	(Million tonnes)	(% of total)	(Million tonnes)	(% of total)	(Million tonnes)	(% of total)
Domestic sales . . . .	23.2	62.3	31.7	67.7	39.5	77.5	16.9	72.4	21.7	83.0
Overseas sales . . . .	14.0	37.7	15.2	32.3	11.5	22.5	6.4	27.6	4.4	17.0
Total . . . . .	<u>37.3</u>	<u>100.0</u>	<u>46.9</u>	<u>100.0</u>	<u>51.0</u>	<u>100.0</u>	<u>23.4</u>	<u>100.0</u>	<u>26.2</u>	<u>100.0</u>

### *Domestic sales*

We conduct coal sales in the domestic market by means of long-term sales contracts and spot market sales. The long-term sales contracts generally have a minimum term of not less than one year, with annual price determination provisions. The spot market sales generally specify the quantities and timing of purchases planned over a period of no more than one year.

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Since 2002, the price of domestic coal sales has been largely determined by market forces. For further details on the price of domestic coal, see “Industry Overview — The PRC coal industry”. Currently, our pricing decisions take into account: (i) prices in the relevant local coal markets (inclusive of transportation costs); (ii) the grade and quality of the coal; and (iii) the sales volume and the length and stability of relationships with customers. Our long-term contracts contain provisions relating to price adjustment mechanisms, coal quality requirements, coal quantity, permitted sources of supply, future regulatory changes, extension options, force majeure, termination and assignment of contract. Depending on the sales region and the type of customer, our coal prices may be quoted as ex-mine prices, FOB, DES or CFR (all inclusive of VAT). Since 2000, domestic coal prices have been on an upward trend, driven primarily by increased demand from the power and steel industries. The following table sets forth selected price information, for the periods indicated, for our domestic sales to external customers from long-term contract sales and spot market sales:

	Year ended 31 December									Six months ended 30 June					
	2003			2004			2005			2005			2006		
	Price	Sales volume	Percentage of sales volume	Price	Sales volume	Percentage of sales volume	Price	Sales volume	Percentage of sales volume	Price	Sales volume	Percentage of sales volume	Price	Sales volume	Percentage of sales volume
(RMB/tonne)	(million tonnes)	(% of total)	(RMB/tonne)	(million tonnes)	(% of total)	(RMB/tonne)	(million tonnes)	(% of total)	(RMB/tonne)	(million tonnes)	(% of total)	(RMB/tonne)	(million tonnes)	(% of total)	
Long-term contract sales . .	202	9.9	42.4	269	26.9	84.7	315	34.4	87.1	318	15.2	89.6	320	21.0	96.7
Spot market sales	<u>154</u>	<u>13.4</u>	<u>57.6</u>	<u>189</u>	<u>4.8</u>	<u>15.3</u>	<u>262</u>	<u>5.1</u>	<u>12.9</u>	<u>267</u>	<u>1.8</u>	<u>10.4</u>	<u>305</u>	<u>0.7</u>	<u>3.3</u>
Total . . . . .	175	<u>23.2</u>	<u>100.0</u>	257	<u>31.7</u>	<u>100.0</u>	308	<u>39.5</u>	<u>100.0</u>	312	<u>16.9</u>	<u>100.0</u>	320	<u>21.7</u>	<u>100.0</u>

As of the Latest Practicable Date, we had long-term domestic sales contracts for thermal coal with four of the five largest Chinese companies in the power generation sector. In addition, we had 15 long-term coal supply contracts with China’s major power companies. Pursuant to the terms and conditions of these long-term domestic sales contracts, we have agreed to supply approximately 46.4 million tonnes, 53.8 million tonnes, and 59.8 million tonnes of thermal coal in 2006, 2007, and 2008, respectively, to our domestic customers.

### *Overseas sales*

Through our licensing arrangement with ChinaCoal Group, our centralized sales force manages all the sales of our coal products to overseas customers, mainly located in countries and territories in the Asia-Pacific region, including Japan, Korea and China Taiwan. ChinaCoal Group generally charges us an agency fee. See “Connected Transactions” for details regarding this agency fee.

Our export contracts generally have terms ranging from one to five years. Contracts of a longer term typically do not include price terms, which are negotiated on an annual basis. These contracts typically stipulate procedures for quality control, sampling and weighing. In some instances, buyers have the option to adjust annual or monthly volumes within a pre-set range as agreed by the parties. We believe we have a good record of meeting our contractual delivery, supply and coal quality requirements.

We generally sell our coal on an FOB basis at the loading port, with purchasers paying the costs of ocean freight. Payments for our overseas sales are made by letter of credit or telegraphic transfer in U.S. dollars.



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### *Coal Trading and Services*

The following table sets forth information regarding the revenue generated by our proprietary coal trading and import/export-related services in the years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2005 and 2006:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
	(RMB million)	%	(RMB million)	%	(RMB million)	%	(RMB million)	%	(RMB million)	%
Proprietary coal trading . . . . .	4,025.5	97.0	4,159.2	95.4	7,263.4	96.2	4,231.5	97.4	2,856.5	96.5
Import and export related services . . . . .	122.4	3.0	198.7	4.6	287.5	3.8	114.2	2.6	102.6	3.5
<b>Total . . . . .</b>	<u>4,148.0</u>	<u>100.0</u>	<u>4,357.9</u>	<u>100.0</u>	<u>7,550.9</u>	<u>100.0</u>	<u>4,345.6</u>	<u>100.0</u>	<u>2,959.1</u>	<u>100.0</u>

### **Proprietary coal trading**

We source raw coal and clean coal from both domestic and international coal producers and resell it without further processing to customers, including power plants, steelmakers, coking plants, chemicals plants and other coal traders. In 2005, we resold 18.6 million tonnes of coal directly to domestic customers and 2.5 million tonnes to overseas consumers. Our trading sales are concentrated in the power production sectors.

The weighted average sales prices per tonne for our domestic proprietary trading sales over the past three years were RMB239 in 2003, RMB287 in 2004 and RMB307 in 2005, and the weighted average export sales price per tonne were RMB260, RMB612, and RMB627 in the same periods, respectively.

### **Import and export-related services**

Our parent company, ChinaCoal Group, is the largest coal exporter in China, with coal exports of 14.3 million tonnes in the six months ended 30 June 2006 and over 20 years of trading experience. ChinaCoal Group is one of only four companies in China possessing the Coal Export Right. Coal exports in China must comply with the national export quotas determined annually by the NDRC and MOFCOM. For the years ended 2003, 2004, 2005 and 2006, the total national export quotas for coal were 100.0 million tonnes, 80.0 million tonnes, 80.0 million tonnes and 80.0 million tonnes, respectively. For the same periods, ChinaCoal Group received 49.6 million tonnes, 36.2 million tonnes, 38.2 million tonnes and 38.2 million tonnes, respectively, of the total national export quotas, accounting for nearly 50% of the total national export quotas for each of the relevant periods and among which 14.0 million tonnes, 15.2 million tonnes, 11.5 million tonnes and 4.4 million tonnes, respectively, were allocated to us for the export of our coal products.

Through the Restructuring, we succeeded to the export and domestic trading businesses of ChinaCoal Group, including its sales force, distribution network, customer relationships and port facilities. Pursuant to the Services Agreement, which expires in 2008, we export our coal products through ChinaCoal Group. We intend to renew this agreement upon its expiration to continue exporting our coal products through ChinaCoal Group, and we believe that, given our close relationship with ChinaCoal Group and its interest in our Company, there will be no obstacles to our obtaining such renewal. Furthermore, because the PRC Government allocates export quotas to three other coal exporters in addition to ChinaCoal Group, we are also able to export our coal products through these other coal exporters. Under PRC regulations, only State-owned enterprises are authorized to apply for annual export quotas and the relevant coal export permits, and currently only four coal enterprises have received such authorization. See “Regulations — The coal industry — Coal trading”. The coal export agency services industry is generally market-driven, and each of the four Coal Export Right holders generally provides services to any coal producers who engage it for coal export, subject to

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the quota allocated to them by the NDRC and MOFCOM. We therefore do not believe that we will face any obstacles in exporting our coal products through these other three coal exporters. Together with ChinaCoal Group (which, as the holder of the Coal Export Right, performs such services as entering into export agreements, customs clearance, and receipt of payment and settlements), we provide a full range of export-related documentary and logistical services. See “Connected Transactions”.

The overseas sales for which ChinaCoal Group acts as an export agent, including overseas sales of our coal products, are made principally to coal consumers in the Asia-Pacific region.

We receive service fees for the provision of export-related services to ChinaCoal Group for its export agency services to domestic coal exporters. According to the Services Agreement, we are entitled to deduct 0.8% to 1.3% of the total export transaction amount from the export coal producers as our service fees.

We act as an agent to procure coal in the international markets and from overseas coal producers on behalf of domestic coal consumers. As no operating license is required for the coal import business, we are not restricted by any import quotas and are able to operate our coal import business according to market demand and customers’ needs. Our services include one or the combination of: (i) sourcing coal products from international markets or overseas coal producers based on the customers’ specifications; (ii) negotiating the price for domestic consumers; (iii) co-signing of sales and purchase contracts with domestic consumers; and (iv) arranging logistics and customs clearance. We believe that our customers are able to receive quality coal products at reasonable prices by benefiting from our market knowledge and relationships with overseas coal producers.

### *Sales and Marketing*

Our coal sales and proprietary trading business are primarily carried out by our centralized sales forces located in Beijing, northern China and the major ports for coal sales. A limited amount of our coal products produced in the Liliu Mining Area and the Datun Mining Area are sold by the sales teams of the Huajin Joint Venture and Shanghai Datun Energy, respectively.

Our domestic sales are conducted primarily through our own sales force. Our centralized sales force sells: (i) raw coal from our mines; (ii) clean coal processed from our coal processing plants; and (iii) raw and clean coal that we purchase from other producers. We are in the process of further centralizing and coordinating our sales and marketing efforts to take full advantage of our extensive sales and distribution channels, wide network of customer relationships and industry knowledge and experience. In China, we have established sales branch offices to sell our own coal products, conduct domestic coal trading and support coal transshipment and export services at such major coal ports as Qinhuangdao, Tianjin, Qingdao, Rizhao and Lianyungang. Our sales personnel periodically visit our customers to provide after-sales services.

We determine a customer’s payment method based on factors such as our prior dealings with the customer, volume of sales, the customer’s current financial position and the prevailing market conditions. For new or short-term customers, we require full payment prior to delivery. All payments by our domestic customers are made in Renminbi. In recent years, we have not experienced any significant payment collection issues.

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### Customers

Our customers for coal are located in various regions throughout China and around the world.

We sell thermal coal to large coal-fired power plants, chemical engineering companies, and cement and construction material companies in eastern, southern and northern China. ChinaCoal Group sells our thermal coal under an export agency agreement to power plants and other customers in various industries in other countries and territories, mainly Japan, Korea and China Taiwan.

Our major external coking coal customers include large steelmakers, including Baosteel, Taisteel, and Baogang, and independent coking plants in China. ChinaCoal Group, acting as our export agent, sells our coking coal under an export agency agreement to major overseas customers including Nippon Steel and Posco Iron and Steel. Since August 2003, we have also sold limited amounts of coking coal to our coking plants. Such sales are accounted for as inter-segment sales in our combined financial statements, and are eliminated upon consolidation.

We generally grant our external customers for our coal operations credit terms ranging from three to six months.

### *Certificates and Compliance with Regulations for Coal Operations*

Enterprises that engage in coal production are required to obtain a mining right permit, work safety permit, coal production permit, mine manager qualification certificate and mine principal safety qualification certificate. Jia Yuan Law Firm, our PRC legal adviser, has confirmed that each of our nine mines in operation has obtained all the foregoing certificates and/or permits. Jia Yuan Law Firm has also confirmed that the scope and operations of our coal production business are in compliance with relevant laws, regulations and administrative rules and that we have obtained for our coal production business the requisite licenses, permits, certificates, authorizations and approvals. For details of the laws, regulations and regulatory documents relating to coal production, see “Regulations — The coal industry — Coal production”.

Enterprises that engage in the wholesaling and retailing of raw coal, processed coal production and the distribution of coal for residential use shall obtain a Coal Operation Qualification Certificate. Jia Yuan Law Firm has also confirmed that ten of our companies, which are our subsidiaries and joint ventures, have obtained the said certificates, and thus are qualified to conduct the relevant coal operations.

Jia Yuan Law Firm has also confirmed that the controlling shareholder of our Company, ChinaCoal Group, is one of only four coal companies in China possessing a Coal Export Right.

In addition, Jia Yuan Law Firm has confirmed that the scope and operations of our coal trading and export service-related services are in compliance with the relevant laws, regulations and regulatory documents and that we have obtained for our coal trading business the requisite licenses, permits, certificates, authorizations and approvals. For details of the laws, regulations and regulatory documents relating to coal trading and export, see “Regulations — The coal industry — Coal trading”.

Our Company is subject to regular inspections and examinations by the relevant PRC authorities, such as the annual review of coal mines by the NDRC. The latest results of regular inspections and examinations by the State Administration of Coal Mine Safety and Administration of Coal Mine Safety in Shaanxi and Shanxi Province for our Yaoqiao Mine, Longdong Mine and Xuzhuang Mine in April 2006, for our Nanliang Mine in August 2006 and for our other mines in September 2006 indicate that such mines meet the relevant requirements. In addition, all the mines of our Company have passed the 2005 Annual Review by the NDRC with respect to their Coal Production Permit.

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### *Competition*

A number of factors affect the markets in which we sell our coal products. Coal prices depend primarily on the coal consumption patterns of the electric power and metallurgical industries in China, the availability, location and cost of transportation and price of competing coal and other energy resources. Coal consumption patterns are affected primarily by the demand for electricity, by environmental and other governmental regulations and by technological developments.

We principally compete in China's domestic market and the Asia-Pacific regional market.

#### **Domestic market**

China's domestic coal market is characterized by competition among a very large number of coal suppliers, with no individually dominant nationwide supplier. The five and ten largest coal producers in China, including ChinaCoal Group, accounted for only 17.7% and 25.2%, respectively, of the country's total 2005 raw coal production. The domestic coal market is segmented principally by location, given the significant costs associated with coal transport, and also by coal characteristics, such as heat value, sulphur content, ash content and moisture content and volatility. We compete on the basis of reliable and timely delivery, customer service, coal quality and price.

Our principal domestic competitors are a number of large coal producers located in the major coal-producing provinces and regions, including Shanxi and Shaanxi Provinces and the Inner Mongolia Autonomous Region, including Shenhua Group Corporation, Datong Coal Mining Company, Shanxi Coking Coal Company and Yankuang Group Company. Certain of our competitors from these regions have substantial reserves and enjoy better mining conditions, the latter of which allows them to mine coal at a relatively lower production cost. However, competitors from these regions also face significantly higher transportation costs when transporting their coal products to sea ports and to their customers in eastern China due to the greater distances. Our Pingshuo Mining Area is one of the closest to end customers among all major coal mines situated in the major coal-producing provinces in northern and northwestern China, and our Datun Mining Area is located in the heart of one of China's largest coal demand centers. In addition to the large-scale coal producers which are our principal competitors, we also compete to a certain degree with smaller mines located in proximity to our customers. See "Risk Factors — Risks relating to China's coal industry and our businesses — We may be unable to compete effectively against other coal producers and sellers".

We and other domestic coal producers encounter limited competition from imports for our domestic customers. In 2005, only 1.2% of the coal consumed in China was imported.

#### **Export market**

We mainly export coal through ChinaCoal Group to several countries and territories in the Asia-Pacific market, including Japan, Korea and China Taiwan. These markets are generally characterized by high energy consumption levels and small coal reserves, creating a significant demand for coal imports. With respect to overseas sales, we compete with certain major overseas coal mining companies, mainly located in Australia and Indonesia, and major Chinese coal exporters. Certain of these competitors have greater financial, marketing, distribution and other resources than we do. However, we believe that we benefit from a more established customer base and sales channel compared to our domestic competitors and shorter transportation distances and lower costs compared to our overseas competitors.

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## COKING OPERATIONS

### *Overview*

We operate one of China's largest coking businesses not affiliated with a steelmaker. Our main products include coke and coal-based chemicals. In addition, we provide export agency services to China's coke exporters who engage ChinaCoal Group as an export agent. In China, conducting the direct export of coke products is subject to the export quota and export permit system. We plan to apply for export quotas in 2008 to export our coke products directly in 2009. Prior to May 2003 when we started operating our first coking plant, our coking operations focused on the sale of coke in China's domestic market on a trading basis and the provision of export-related services. We have gradually increased our production since the fourth quarter of 2003 by constructing new coking plants and upgrading existing plants. We sold 1.0 million tonnes, 1.0 million tonnes, 1.3 million tonnes and 1.0 million tonnes of coke in 2003, 2004, 2005 and the six months ended 30 June 2006, respectively. The following table illustrates our domestic and overseas sales by revenue and percentage of their contribution to our coking operations segment for the periods indicated:

	Year ended 31 December						Six months ended 30 June			
	2003		2004		2005		2005		2006	
	(RMB million)	(%)	(RMB million)	(%)	(RMB million)	(%)	(RMB million)	(%)	(RMB million)	(%)
Domestic sales . . . . .	83.3	7.8	233.6	11.5	587.3	36.9	215.1	22.9	610.3	60.3
Overseas sales	981.7	92.2	1,805.6	88.5	1,004.0	63.1	723.5	77.1	402.1	39.7
Total . . . . .	<u>1,064.9</u>	<u>100.0</u>	<u>2,039.2</u>	<u>100.0</u>	<u>1,591.3</u>	<u>100.0</u>	<u>938.6</u>	<u>100.0</u>	<u>1,012.4</u>	<u>100.0</u>

(1) Revenue includes coal-based chemicals and coke export-related services.

### *Products and Services*

Our coke products include mainly metallurgical coke and foundry coke. We process coking coal into coke in our five coking plants pursuant to specifications given by our customers. We also purchase and resell coke in the domestic and international markets. We produce coal-based chemicals in our coking plants and ancillary facilities. Our main chemicals products include coke oven gas, refined tar, benzene, technical and refined naphthalene, methanol, sulfur and phenol. All the coke oven gas we produce is used in power generation so as to increase the efficient use of resources and increase cost-efficient recycling.

ChinaCoal Group, having been granted export quotas by the PRC Government, is one of the largest coke exporters in China. Through the Restructuring, we succeeded to the long-established export and domestic trading business of ChinaCoal Group, including the sales force, distribution network, customer relationships and port facilities.

In 2005, ChinaCoal Group allocated all of its export quotas to us.

### *Coking Facilities*

We, through wholly owned and majority-owned subsidiaries and an associated company, operate coking facilities in five separate locations across northern and northeastern China. Depending on the raw material and production process, as of 30 June 2006, our coking plants and ancillary facilities had an annual production capacity of up to 4.5 million tonnes of coke, 1,532 million cubic meters of coke oven gas, 167,580 tonnes of coal tar, 47,880 tonnes of crude benzol and 36,180 tonnes of ammonium nitrate.

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The following table sets forth the designed annual production capacity of our five coking plants:

<u>Coking plant</u>	<u>Designed annual production capacity<sup>(1)</sup></u>	<u>Utilization rate</u>
	(million tonnes)	Six month period ended 30 June 2006 (%)
Jiuxin Plant . . . . .	2.0	33.9
Jingda Plant <sup>(2)</sup> . . . . .	0.5	23.8
Longquan Plant <sup>(2)</sup> . . . . .	0.4	42.3
Mudanjiang Plant <sup>(2)</sup> . . . . .	0.4	85.9
Xuyang Plant . . . . .	1.2	53.7

(1) Designed maximum annual production capacity calculated as of 30 June 2006 on a 300-operational day basis.

(2) The companies that own and operate these coking plants are currently in the process of applying to be included in the qualified producers catalog. We confirm that there are no substantial obstacles in the application process.

As of 30 June 2006, the Jiuxin Plant, Jingda Plant, Longquan Plant and Xuyang Plant were in the start-up stage and not in full operation. As a result, the estimated utilization rates of these four plants were lower than that of Mudanjiang Plant, our first coking plant.

### *Raw Materials*

We have centralized the procurement of raw materials, including coking coal, for all of our coking operations, to obtain the best available pricing and supply terms. Our major sources of coking coal include: (i) mines in the vicinity of our various coking plants; and (ii) the Huajin Joint Venture, which agreed in 2005 to supply us with up to 180,000 tonnes of high-quality coking coal. We generally receive credit terms ranging from five to forty-five days from our suppliers for our coking operations. As of the Latest Practicable Date, we had not experienced any major interruption of raw material supplies for our coking operations.

To date, none of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest suppliers for our coking operations.

### *Sales and Marketing*

We sell coke and coal-based chemicals in the domestic and international markets through a specialized sales and marketing force operated by China Coal & Coke Holding Limited, our wholly owned subsidiary, which sets prices for our coking products and enters into sales contracts with our customers. Through the implementation of our centralized management system, including centralizing our sales and marketing forces, we have been able to significantly reduce duplication of marketing efforts and potential competition among our plants.

ChinaCoal Group serves as our agent to export coke produced in our coking plants. See “Connected Transactions”.

### *Customers*

Customers of our coking business mainly include steelmakers. We generally grant credit terms ranging from one to two months to our external customers for our coking operations. None of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest customers of our coke business.

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### *Certificates and Compliance with Regulations for Coking Operations*

From 1 January 2006, the new construction, alteration and expansion of any coking plant must meet the Entry Requirement and be included in the qualified producers catalog. Among the five subsidiaries and joint ventures of our Company, China Coal & Coke Xuyang Limited has already been included in the *Announcement of Qualified Enterprises for Entry Coke Industry* (first group), issued by the NDRC, while the remaining four are in the process of applying to be included in the announcement (second group).

Jia Yuan Law Firm, our PRC legal adviser, has confirmed that the scope and operations of our coke production business, conducted by our subsidiaries and joint ventures, are in compliance with the relevant laws, regulations and administrative rules and, except for those which are in the application process, we have obtained for our coke production business the requisite license, permits, certificate, authorization and approval. We confirm that there are no substantial obstacles preventing our four subsidiaries from being adopted into the announcement. For details of the laws, regulations and regulatory documents relating to coke production, see “Regulations — The coal industry — Coke production”.

Our Company is subject to regular inspections and examinations by the relevant PRC authorities, such as the annual review by the NDRC in respect of our coking facilities. However, as of the Latest Practicable Date, no inspection on our coking facilities was scheduled or enforced.

### *Competition*

We compete primarily with domestic coke producers, including: (i) large steelmakers who have their own coking plants; (ii) independent coking plants; and (iii) numerous coal producers in China which are equipped with coke production capabilities. We principally compete on the basis of quality, chemical characteristics of our coke, transportation costs from the coking plants to the customer, the reliability of supply and price. Due to our well established sales and marketing network, as well as our broad range of high quality products, we believe that we are well-positioned to compete with other coke producers. In addition, we believe that by having secure and stable raw material sources, we have a competitive advantage over other coal mining companies with coking capacities.

## COAL MINING EQUIPMENT MANUFACTURING OPERATIONS

We are the largest coal mining equipment manufacturer in China based on our 2005 sales revenue. We focus mainly on the production of mining and conveying equipment for longwall mining systems, such as curved armored face conveyors, hydraulic roof supports, coal shearers and coal ploughs. Other than manufacturing mining and conveying equipment, we are also one of the few mining equipment suppliers that are capable of providing comprehensive mining services, including design, production, installation and testing services to underground mines within and outside China. We are also in the process of developing shortwall mining equipment and longwall mining equipment.

### *Products*

Our products include a complete set of equipment for underground mining systems, such as hydraulic roof supports, curved armored face conveyors, shearers, coal ploughs, stage loaders, breakers and mining electric appliances. Our external revenue from coal mining equipment manufacturing increased from RMB1,057.9 million in 2003 to RMB1,891.2 million in 2005.

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### *Manufacturing Facilities*

The following table presents the location and principal products manufactured at our equipment manufacturing facilities as of the Latest Practicable Date:

Plant	Location	Principal product
China Coal Zhangjiakou Mining Machinery Co., Ltd. (中煤張家口煤礦機械有限責任公司)	Zhangjiakou, Hebei Province, PRC	Armored face conveyors, coal ploughs, stage loaders and breakers
China Coal Beijing Coal Mining Machinery Co., Ltd. (中煤北京煤礦機械有限責任公司)	Beijing, PRC	Hydraulic roof supports
China Coal Handan Coal Mining Machinery Company Limited (中煤邯鄲煤礦機械有限責任公司)	Handan, Hebei Province, PRC	Hydraulic props
Zhangjiakou China Coal Chuangli Mining Machinery Co., Ltd. (張家口中煤創力採掘設備有限責任公司)	Zhangjiakou, Hebei Province, PRC	Coal shearers

### *Raw Materials*

We use steel as the raw material for our coal mining equipment manufacturing operations. We generally receive credit terms ranging from ten days to one month from our suppliers for our coal mining equipment manufacturing operations after certain delivery conditions have been fulfilled.

To date, none of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest suppliers for our coal mining equipment manufacturing operations.

### *Research and Development*

We dedicate significant resources to research and development. At present, we have over 900 professionals engaged in the research and development of underground coal mining equipment. As a result of our research and development activities, we were awarded five top prizes in China's coal industry, were granted three patents for curved armored face conveyors, and developed the first domestically manufactured 6.5 meter, heavy-duty hydraulic roof support and a complete equipment set of the super heavy-duty 3 X 700 KW armored-face conveyor. Our research and development unit was also selected to develop the equipment for a six million tonne integrated mining face as part of a national research and development program. In addition, we successfully developed a fully automated coal plough system.

We are increasing our cooperation with companies outside of China, having acquired the assets and technologies of an internationally renowned industrial chain manufacturing company based in the United Kingdom. We also recently cooperated with British and German businesses to produce gearbox electro-hydraulic control valve systems. We also established a specialized research and development organization to centralize and coordinate our research and development activities.



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### *Sales and Marketing; Customers*

We sell our products to domestic and foreign customers, and also utilize them at our Pingshuo Mining Area, Liliu Mining Area, Xiangning Mining Area and Datun Mining Area. In 2005, domestic sales of equipment for use in mines accounted for over 90% of our total coal mining equipment revenue.

We are actively searching for overseas markets to expand our customer base and increase our sales. We recently exported a complete set of coal mining equipment and technology to Russia. At present, we supply to mines in over ten countries and regions.

We generally grant our external customers for our coal mining equipment manufacturing operations credit terms ranging from three to six months.

To date, none of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest external customers for our coal mining equipment manufacturing operations.

### *Competition*

We compete with major mining equipment manufacturers in China and abroad. For longwall mining system components such as hydraulic roof supports and curved armored face conveyors, our primary domestic competitors are Ningxia Northwest BN Industrial Group Co. Ltd. (西北奔牛實業有限公司) and Zhengzhou Coal Mining Machinery Group Co. Ltd. (鄭州煤礦機械集團有限責任公司), respectively. In addition, we compete with international mining equipment manufacturers such as DBT and Joy Mining Machinery Company in providing design, installation, testing and system integration services on a turn-key basis for the underground mining industry. We believe that we are well positioned to compete in both the domestic and international markets for coal mining equipment.

## COAL MINE DESIGN AND OTHER OPERATIONS

We are among the best coal mine design companies in China. As of 30 June 2006, we had completed more than 1,000 medium and large projects both inside and outside of China. We are the principal designer of China's first 100 million-tonne coal mine, Shendong Coal Mining Area. One-third of all underground coal mines in China with production capacity of 10 million tonnes or above were designed by us.

We have been awarded more than 100 national and provincial awards in recognition of our outstanding mine design capability, among which four awards represented the highest national accolade, more than any of our competitors.

We also engage in the following businesses: (i) primary aluminum production and sales; (ii) electric power generation; (iii) and coal transportation services. For the years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2005 and 2006, our coal mine design and other operations accounted for 4.8%, 4.1%, 4.8%, 3.9% and 6.4%, respectively, of our total revenue.

## PURCHASES FROM OUR LARGE SUPPLIERS

In the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, 2.6%, 2.1%, 5.7% and 4.1%, respectively, of our total cost of sales were attributable to purchases from our largest supplier. In the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, 9.9%, 6.9%, 11.0% and 12.1%, respectively, of our total cost of sales were attributable to purchases from our five largest suppliers. None of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest suppliers.

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### SALES MADE TO OUR LARGE CUSTOMERS

In the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, 12.9%, 11.9%, 9.9% and 12.7%, respectively, of our total sales were generated from sales made to our largest customer. In the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, 25.0%, 25.2%, 22.9% and 37.9%, respectively, of our total sales were generated from sales made to our five largest customers, including domestic power plants and steel makers. None of our Directors, their associates or ChinaCoal Group is related to or owns any interest in any of the five largest customers.

### ENVIRONMENTAL MATTERS

Our operations are subject to numerous national and provincial environmental laws and regulations relating to air and water emissions, hazardous substances and waste management, mining site reclamation and restoration, and groundwater quality and availability. We are committed to following environmentally responsible practices and abiding by relevant environmental laws and regulations in all aspects of our business. We conduct environmental feasibility studies and environmental impact assessments for all of our new building or reconstruction projects. Installation for the prevention and control of pollution at a construction project must be designed, built and commissioned together with the principal part of the project. Before the new facilities may be put to use, the pollution control and waste processing facilities must be inspected and considered to be up to standard by the environmental protection department and be commissioned simultaneously with the new facilities. Each of our coal mines are in compliance with environmental regulations, details of which are as follows:

#### *Pingshuo Mining Area*

The holder of the mining right permits for the Antaibao Open Pit Mine, Anjialing Underground Mine and Anjialing Open Pit Mine has obtained the operational licenses at the provincial level for boundary noise, gaseous emissions and water discharge, as well as licenses from the local government for groundwater extraction. Each of our mines in the Pingshuo Mining Area prepares an individual environmental report to SEPA, the Shanxi Environmental Protection Bureau and the local environmental protection bureau twice yearly. These reports incorporate information regarding volumes of solid waste generated, noise data, wastewater data, gaseous emissions data, environmental budgets and completed rehabilitation. They are passed down from state to provincial regulators for approval, then to local county environmental regulators who conduct random inspections. Consequently, we are subject to random inspections carried out by both provincial and local environmental agencies several times a year to ensure compliance. To date, none of our mines in the Pingshuo Mining Area has been fined for any breach of environmental non-compliance.

#### *Liliu Mining Area*

The holder of the mining right permit for the Shaqu Mine in the Liliu Mining Area has obtained the operational licenses at the provincial level for boundary noise, gaseous emissions and water discharge, as well as licenses from the local government for groundwater extraction. The Shaqu Mine in the Liliu Mining Area must prepare an individual environmental report to the Shanxi Environmental Protection Bureau. These reports incorporate information on waste volumes generated, noise data, wastewater data and gaseous emissions data. After approval, the report is passed down from the state to provincial regulators and then to the local environmental regulators, both of which conduct random inspections. We are subject to random inspections carried out by the provincial and local environmental agencies several times a year to ensure compliance. We maintain our own in-house environmental monitoring station which collects data on noise,

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water and emissions to monitor our continued compliance. To date, the Shaqu Mine has not been fined for any breach of environmental non-compliance.

### *Datun Mining Area*

The holder of the mining right permit for our four mines in the Datun Mining Area, namely the Yaoqiao Mine, the Kongzhuang Mine, the Xuzhuang Mine and the Longdong Mine, has obtained the operational licenses at the provincial level for boundary noise, gaseous emissions and water discharge, as well as licenses from the local government for fuel storage and groundwater extraction. Each of our mines in the Datun Mining Area prepares an individual annual environmental report to the SEPA, incorporating information on waste volumes generated, noise data, wastewater data and gaseous emissions data. This report is passed down from the state to provincial regulators for approval, then to the local county environmental regulators. Both the provincial and local regulators conduct random inspections. Consequently, we are subject to random inspections, which are carried out by the provincial and local agencies several times a year to ensure compliance. To date, none of our mines in the Datun Mining Area has been fined for any breach of environmental non-compliance.

In addition to the environmental inspections conducted by the local and provincial agencies, the China Quality Association audits Datun Coal and Electricity (Group) Limited-Liability Company annually to re-examine its corporate ISO14001:1996 accreditation for environment management systems. Datun Coal and Electricity (Group) Limited Liability Company has achieved sound results with regard to its environmental credentials, has had no fines to date and maintains its ISO14001:1996 accreditation.

### *Nanliang Mining Area*

The holder of the mining right permit for the Nanliang Mine in the Nanliang Mining Area has obtained the environmental licenses at the provincial level for boundary noise, gaseous emissions and water discharge, as well a license from the local government for groundwater extraction. The Nanliang Mine is required to prepare an Annual Environment Report to the Environmental Protection Bureau of Shaanxi Province, incorporating data on waste volumes generated, noise data, wastewater data and gaseous emissions data. Upon approval, the provincial regulators pass the report down to the local county environmental regulators who conduct random inspections. Consequently, we are subject to random inspections, which are carried out by the local agencies several times a year to ensure compliance. To date, Nanliang Mine has not received any fines for breach of any environmental regulations.

Jia Yuan Law Firm, our PRC legal adviser, have advised us that our operational activities are in compliance with the relevant PRC environmental laws and regulations, and that we have not been fined for any material breach of the relevant environmental laws in the past three years.

As the environmental regulatory regime in China develops, we continue to invest in our environmental protection and control systems. We have adopted many environmentally responsible practices in our operations and have installed sophisticated abatement equipment to minimize the impact of our operations on the environment. We have developed comprehensive water management and conservation practices that include the use of surface runoff and infiltrated water for dust suppression, and we have installed closed water recycling and water treatment facilities at all of our coal processing plants, greatly reducing the amount of water used in the coal processing process and the amount of wastewater released. We burn coal waste, tailings and slurry from all of our coal processing plants to generate electric power for use in our own plants and for sale to the local power grids, rather than disposing of such waste. These generating plants are equipped with high-efficiency low-emissions circulating fluidized bed boilers, which substantially reduce sulfur dioxide and

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nitrogen monoxide emissions. We recover substantially all of the coke oven gas produced in the coking process and use such gas, after treatment and recovery of coking chemicals co-products, as fuel for the coking ovens and for on-site power generating plants. All of our power generating plants are equipped with high-efficiency particle filtration and desulphurization equipment. We will continue to adhere to the strict environmental requirements by implementing waste handling and processing measures at each of our coal mining areas and coke production plants. We will also undertake measures to protect our coal resources from over-exploitation and unauthorized exploitation by us and by third parties. We will monitor the extraction of our coal reserves and devise coal production plans to maximize resource utilization and to minimize the environmental impact of our operations.

In addition to regular inspections by the relevant government authorities, we undertake routine and periodic inspections of all of our coal mines and coking plants. We have established departments or teams at each principal subsidiary that are responsible for ensuring that all of our coal mines and coking plants are in compliance with applicable environmental laws and regulations. All new mines and plants must conduct environmental impact assessments before beginning construction. Our environmental department coordinates environmental impact assessments, testing, and rehabilitation projects. For the years ended 31 December 2003, 2004 and 2005 and the six months ended 30 June 2006, we spent approximately RMB179.9 million, RMB261.1 million, RMB197.9 million and RMB23.9 million, respectively, to comply with local and national environmental protection ordinances. As of the Latest Practicable Date, we believe that we have been in full compliance with the applicable PRC environmental laws and regulations in all material respects, and were not subject to any major environmental claims, lawsuits, penalties or disciplinary actions.

The newly promulgated *Emission Standard for Pollutants from Coal Industry*, effective from 1 October 2006, imposes stricter standards and higher technical requirements for our coal mines, coal processing plants and coal waste, storage and loading depots. Our Directors believe that the operations of our coal mines, coal processing plants and depots are in compliance with the newly enforced standards as we had already adopted advanced pollution control technologies and measures prior to the promulgation of the new standards.

## OCCUPATIONAL HEALTH AND SAFETY

The PRC Government places significant regulatory requirements on coal mine and employee safety. We regard occupational health and safety as one of our important social responsibilities and have implemented a number of measures at our coal mines to ensure compliance with the stringent regulatory requirements. We have established a safety supervision department at each of our operating coal mines. The safety supervision departments conduct periodic inspections of our mining safety facilities to ensure that all parts of our coal mining operations are in compliance with existing laws and regulations. As we believe that safe practices are the best ways to ensure employee safety, our safety supervision departments also conduct regular training sessions for employees on accident prevention and management.

We have designed and adopted underground mining techniques to minimize the risk of injury at our underground coal mines. Underground mining activities are inherently dangerous as they may trigger explosions from sparks in underground coal mines with high levels of coal dust and methane. We have adopted strict policies, requiring gas to first be extracted from the mine until the concentration level of gas is within a permissible range in accordance with the national standard, before mining activities are permitted to commence. To regularly supervise gas levels, we have installed a mine gas monitoring system in all of our underground mines.

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However, our business operations, particularly our coal mining operations, involve significant risks and hazards that are inherent in such activities and may not be completely eliminated by safety measures. These risks and hazards could result in damage to, or destruction of, properties or production facilities, personal injury, environmental damage, business interruption and possible legal liability. See “Risk Factors — Risks relating to China’s coal industry and our businesses — We may not have sufficient insurance coverage against potential operational risks.”

In 2003, 2004 and 2005, the employee fatality rate for our mines, which includes both full-time and temporary employees, was 0.12, 0.15 and 0.08 persons per million tonnes of raw coal production, respectively. This was substantially lower than the average rate for coal mines in China, which was 4.17, 3.10 and 2.81 persons per million tonnes, respectively, during the same periods. In March 2001, a mining-related accident in which five people died occurred at the Kongzhuang coal mine in the Datun Mining Area. However, no other major accidents, as defined under applicable Chinese laws to mean accidents involving three to nine fatalities, have occurred at any of our coal mines in the past several years. No other accident has had, individually or in the aggregate, a material effect on us. While we are committed to further reducing our fatality rates and maintaining high safety standards at our production facilities, there is no assurance that accidents will not occur in the future.

We provide various healthcare benefits to our employees in accordance with applicable laws and regulations.

### INTELLECTUAL PROPERTY

In connection with the Restructuring, we have entered into a trademarks license framework agreement with ChinaCoal Group, pursuant to which ChinaCoal Group has agreed to grant to us the right to use certain trademarks for a nominal fee of RMB1.0 per year for a term of 10 years, and which is automatically renewable at our option. The trademarks license framework agreement contains a non-cancellable provision under which ChinaCoal Group shall not terminate the agreement without our consent.

As of the Latest Practicable Date, we held 21 patents for mining-related technologies, and had 16 additional patent applications pending before the State Intellectual Property Office of China, or SIPO. Our coal mining equipment manufacturing operations hold 5 patents in connection with mining equipment, of which 3 are for the production of armored face conveyor systems.

### PROPERTIES

Our head office is located at 1 Huangsidajie, Chaoyang District, Beijing, the PRC. As of 30 September 2006, we operated our businesses through 2,654 properties in the PRC, Hong Kong and Australia for our mines, production facilities, offices and other places of operation. These properties comprised: (i) the land use rights to 160 parcels of land with a total site area of approximately 45.82 million m<sup>2</sup>; (ii) 1,788 buildings with a total gross floor area of approximately 1.58 million m<sup>2</sup>; (iii) 68 buildings under construction; and (iv) 534 leased properties with a total gross floor area of approximately 0.24 million m<sup>2</sup> and 104 parcels of leased land with a total site area of approximately 3.00 million m<sup>2</sup>. According to the Restructuring Agreement, the above properties were transferred to us or our relevant subsidiaries by ChinaCoal Group as part of the Restructuring.

Savills, an independent property valuer, valued our owned property interests at approximately RMB2,561.62 million as of 30 September 2006. The text of the valuer’s letter, summary of values and valuation certificates prepared by Savills in connection with its valuation are set out in “Appendix V — Property Valuation” included in this Prospectus.

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### *Land Use Rights*

The land use rights transferred by ChinaCoal Group to us comprise five categories of land use rights as follows:

- (i) 82 parcels of granted land with a total site area of approximately 3.09 million m<sup>2</sup> for which ChinaCoal Group or its relevant subsidiaries have obtained granted land use rights certificates;
- (ii) 28 parcels of authorized allocated land with a total site area of approximately 3.21 million m<sup>2</sup> for which MLR has authorized ChinaCoal Group to manage and operate, including contributing such land as capital in our Company;
- (iii) 32 parcels of retained allocated land with a total site area of approximately 38.74 million m<sup>2</sup> which the relevant subsidiaries of ChinaCoal Group have been authorized by the MLR to retain the land use rights;
- (iv) 6 parcels of allocated land with a total site area of approximately 0.01 million m<sup>2</sup> for which ChinaCoal Group has obtained allocated land use rights certificates, but such parcels of land are not included in the authorized allocated land and retained allocated land, respectively, referred to in sub-paragraphs (ii) and (iii) above; and
- (v) 12 parcels of land with a total site area of approximately 0.77 million m<sup>2</sup> for which ChinaCoal Group has not established proper legal title and for which we are in the process of applying for the relevant land use rights certificates.

The transfer of registration of the granted land, authorized allocated land and retained allocated land held by ChinaCoal Group to under our name has not yet been completed and as of the Latest Practicable Date, the transfer of registration of approximately 3 parcels of land remains outstanding. According to the legal opinion of our PRC legal adviser, we or our relevant subsidiaries shall not have any legal obstacles to obtaining the relevant land use rights certificates. The land use rights of the 32 parcels of retained allocated land were transferred to us upon ChinaCoal Group transferring to us the equity interests held by it in the relevant subsidiaries.

### *Buildings*

The buildings transferred to us by ChinaCoal Group as part of the Restructuring comprise:

- (i) 1,628 buildings with a total gross floor area of approximately 1.45 million m<sup>2</sup> for which ChinaCoal Group has proper building ownership certificates or building title proof. Among these buildings, 1,497 buildings with a total gross floor area of approximately 1.38 million m<sup>2</sup> were built on the land which ChinaCoal Group has proper land use rights certificates; 13 buildings with a total gross floor area of approximately 0.01 million m<sup>2</sup> were built on the land for which ChinaCoal Group has not established proper legal titles as those stated in the above sub-paragraphs (iv) and (v) under “Land Use Rights”; and the remaining 118 buildings with a total gross floor area of approximately 0.06 million m<sup>2</sup> were built on the land leased by ChinaCoal Group. According to the legal opinion of our PRC legal adviser, we or our relevant subsidiaries legally and effectively own such buildings; and
- (ii) 160 buildings with a total gross floor area of approximately 0.12 million m<sup>2</sup> for which ChinaCoal Group or its relevant subsidiaries does not have proper building ownership certificates. Among these buildings, 59 buildings with a total gross floor area of approximately 0.06 million m<sup>2</sup> were

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built on the land which ChinaCoal Group has proper land use rights certificates; 29 buildings with a total gross floor area of approximately 0.02 million m<sup>2</sup> were built on the land which ChinaCoal Group has not established proper legal titles as those stated in the above subparagraphs (iv) and (v) under “Land Use Rights”; and the remaining 72 buildings with a total gross floor area of approximately 0.04 million m<sup>2</sup> were built on the land leased by ChinaCoal Group. According to the legal opinion of our PRC legal adviser, we or our relevant subsidiaries shall not have any legal obstacle to obtaining proper building ownership certificates for those buildings erected on the land with proper land use rights certificates.

The transfer of registration of the buildings with building ownership certificates held by ChinaCoal Group to under our name has not been completed and as of the Latest Practicable Date, the transfer of registration of 3 buildings has not yet been completed. According to the legal opinion of our PRC legal adviser, we or our relevant subsidiaries shall not have any legal obstacle to obtaining the relevant building ownership certificates.

With respect to the land and buildings without proper legal title certificates as referred to in “Land Use Rights” and “Buildings” above, our Directors consider that the absence of proper title certificates in respect of part of the land and buildings will not result in any material adverse impact on the business of our Company because:

- (i) most of the land and buildings owned by us but without title certificates are used for office and ancillary production uses. Such land without land use right certificates represent approximately 1.6% of the total site area of land owned by us, while the buildings without property ownership certificates represent approximately 7.5% of the total gross floor area of the buildings owned by us. The absence of title certificates of such land and buildings will not result in any material impact on the operations of our Company; and
- (ii) our Directors consider that the relevant land and buildings can be substituted easily without creating additional burdens on our Company.

Regarding the land and buildings used for office administration purpose, our PRC legal adviser, Jia Yuan Law Firm, has confirmed that such use is consistent with the specified use of the relevant land and properties.

Further, Jia Yuan Law Firm has confirmed that in addition to the land and buildings used for office administration purposes, the uses of all other land and buildings owned by our Company but without legal title certificates are consistent with the specified use of the relevant land and properties.

In addition, ChinaCoal Group has undertaken to provide all necessary assistance to us in order to apply for the state-owned land use rights certificates/building ownership certificates within 12 months from the date of establishment of our Company in respect of the properties for which ChinaCoal Group has not obtained proper title certificates under the Restructuring Agreement. ChinaCoal Group has also undertaken to compensate against all losses due to any issue arising from failing to obtain the state-owned land use rights certificates/building ownership certificates, except for the settlement of land grant fees, which shall be paid by us.

### ***Buildings Under Construction***

We also obtained from ChinaCoal Group 68 new buildings under construction, which, upon completion, will have an estimated total gross floor area of approximately 0.13 million m<sup>2</sup>.

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The relevant building ownership certificates of the buildings under construction will be obtained by us or our relevant subsidiaries upon completion of the particular building and after property registration with the relevant authorities. We intend to use these buildings for production and offices and for other ancillary uses.

Our mining operations require land use rights for our mines. Our PRC legal adviser, Jia Yuan Law Firm, have confirmed that we have obtained all the requisite land use rights for our mining operations.

### *Leased Land and Properties*

In addition, our Company or our relevant subsidiaries occupy 104 parcels of leased land with a total site area of approximately 3.00 million m<sup>2</sup>. Of this leased land, 93 parcels of land are leased by ChinaCoal Group or its associates to our Company or our relevant subsidiaries and 11 parcels of land are leased by third parties to our Company or our relevant subsidiaries. Such leases were initially entered into by ChinaCoal Group with the relevant lessors but have been transferred to us or our relevant subsidiaries as part of the Restructuring. Of the land leased by us, proper land titles have not been established by ChinaCoal Group and the third parties in respect of 20 and 7 parcels of land, respectively.

As of 30 September 2006, we leased approximately 526 buildings in the PRC, 5 buildings in Hong Kong and 3 buildings in Australia. The total gross floor area of the leased buildings is approximately 0.24 million m<sup>2</sup>. Among these leased buildings, we or our relevant subsidiaries leased from ChinaCoal Group or its associates 476 buildings with a total gross floor area of approximately 0.21 million m<sup>2</sup> and we or our relevant subsidiaries also leased 58 buildings from various independent third parties with a total gross floor area of approximately 0.03 million m<sup>2</sup>. Of the buildings leased by us in the PRC, building ownership certificates have not been obtained by ChinaCoal Group and the third parties in respect of 3 and 10 buildings, respectively.

In respect of the above land and buildings leased by us from ChinaCoal Group or its associates and for which no proper land titles have been established and no building ownership certificates have been obtained, ChinaCoal Group has undertaken to legalize its relationships with us and obtain the relevant building ownership certificates within 12 months from the date of establishment of our Company.

### *Waiver From Certain Valuation Report Requirements*

As we either own or lease a substantial number of properties, we have applied to the Hong Kong Stock Exchange for a waiver from strict compliance with:

- (a) Rules 5.01, 5.06(1) and 5.06(3) of the Hong Kong Listing Rules, which require the particulars of each property to be disclosed in a valuation report on an individual basis;
- (b) Rule 19A.27(4) of the Hong Kong Listing Rules relating to preparation of a certified English translation of a valuation report; and
- (c) paragraph 3(a) of Practice Note 16 of the Hong Kong Listing Rules relating to the inclusion of a full valuation report in the Prospectus in respect of the properties legally and beneficially owned by us.

We have also applied for an exemption from the SFC from strict compliance with paragraph 34(2) of the Third Schedule to the Companies Ordinance relating to the disclosure of certain particulars of our properties in the valuation report on the grounds that it would not be practical and would be unduly burdensome for us to include a fully compliant valuation report in this Prospectus and the inclusion of such detailed information would be irrelevant to potential investors as we are not a property company and would not



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be material to a potential investor's investment decision. The SFC has granted us a waiver pursuant to section 342A(1) of the Companies Ordinance.

The Hong Kong Stock Exchange has also granted us a waiver in respect of the preparation of an English translation of the valuation report since it would be unduly burdensome to prepare an English translation of the report, as substantially all of the properties are located in the PRC and consequently the underlying valuation and title information is in Chinese.

The exemption has been granted by the SFC under section 342(1) of the Companies Ordinance and the waiver has been granted by the Hong Kong Stock Exchange from Rules 5.01, 5.06(1), 5.06(3) and 19A.27(4) and paragraph 3(a) of Practice Note 16 of the Hong Kong Listing Rules, subject to the following conditions:

- a full valuation report in the Chinese language complying with all the applicable requirements of the Hong Kong Listing Rules and paragraph 34(2) of the Third Schedule will be made available for inspection in accordance with "Appendix XI — Documents Delivered to the Registrar of Companies and Available for Inspection";
- the valuer's letter and the valuer's certificate containing a summary valuation of all of our property interests, including particulars of occupancy, market values and the title status thereof, based on the full valuation report, will be included in this Prospectus in the form set out in Appendix V to this Prospectus; and
- this Prospectus must set out particulars of this exemption.

## **INSURANCE**

In accordance with what we believe is customary practice for other companies that conduct the same business that we do, we do not currently maintain fire, liability or other property insurance covering our property, equipment or inventory relating to our principal operations. We carry occupational injury, medical pension and unemployment insurance for our employees, in compliance with applicable regulations. See "Risk Factors — Risks relating to China's coal industry and our businesses — We may not have sufficient insurance coverage against potential operational risks."

We will continue to review and assess our risk portfolio and make necessary and appropriate adjustments to our insurance practice in line with our needs and with industry practice in China.

## **EMPLOYEES**

As of 31 December 2003 and 2004, ChinaCoal Group had approximately 98,167 and 99,490 employees, respectively. During the same periods, ChinaCoal Group had 1,839 and 2,751 temporary

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employees, respectively. After the Restructuring, we had 51,792 employees, including 2,242 temporary employees, as of 30 June 2006. The table below sets forth the number of our employees by their functions:

	As of 31 December 2005		As of 30 June 2006	
	Number of Employees	% of Total	Number of Employees	% of Total
Operations and maintenance				
Coal operations.....	22,112	43.2	21,149	40.8
Coking operations.....	3,325	6.5	4,458	8.6
Coal mining equipment manufacturing operations...	9,034	17.6	8,906	17.2
Other businesses.....	<u>16,759</u>	<u>32.7</u>	<u>17,279</u>	<u>33.4</u>
Total .....	<u>51,230</u>	<u>100.0</u>	<u>51,792</u>	<u>100.0</u>
Management, finance and administrative .....	4,943	9.6	5,257	10.2
Research and development and technical support .....	8,585	16.8	8,623	16.6
Sales and marketing.....	419	0.8	892	1.7
Others .....	<u>37,283</u>	<u>72.8</u>	<u>37,020</u>	<u>71.5</u>
Total .....	<u>51,230</u>	<u>100.0</u>	<u>51,792</u>	<u>100.0</u>

We have implemented a number of initiatives in recent years to enhance the productivity of our employees. Our employees are selected through a competitive process. We conduct periodic performance reviews for our employees, and their salaries and bonuses are performance-based. In addition, we have implemented training programs for different job requirements. We believe that these initiatives have contributed to increased employee productivity.

The remuneration package for our employees generally includes salary and bonuses. Employees also receive welfare benefits including medical care, housing subsidies, retirement, occupational injury insurance and other miscellaneous items. As required by applicable regulations, we participate in various pension funds organized by municipal and provincial governments for our staff. We are required to make contributions to the pension funds of approximately 20% of the salaries, bonuses and certain allowances of our staff. A member of the plan is entitled to a pension equal to a fixed proportion of the salary prevailing at his retirement date. We have no other material obligations for the payment of pension benefits associated with these plans beyond the annual contributions described above. Our contributions in the years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2005 and 2006 were RMB78.6 million, RMB105.4 million, RMB186.2 million, RMB81.9 million and RMB105.6 million, respectively.

Total remuneration of our employees includes wages and bonuses. We paid our employees an aggregate of RMB1,191.6 million, RMB1,556.4 million, RMB1,847.5 million, RMB976.0 million and RMB1,121.7 million, in wages, bonuses and subsidies in the years ended 31 December 2003, 2004, 2005 and the six months ended 30 June 2005 and 2006, respectively.

In 2005, total contributions paid by us for our Directors to the pension fund amounted to approximately RMB53,342. In addition, each of our employees currently pays a percentage of his or her salary as contribution to the pension scheme. Upon retirement, our employees are entitled to a pension payment from the scheme.

Currently, all members of our work force are employed under employment contracts which specify the employee's position, responsibilities, remuneration and grounds for termination. We and our subsidiaries have labor unions that protect employees' rights, aim to assist in the fulfillment of our and our subsidiaries' economic objectives, encourage employee participation in management decisions and assist in mediating disputes between us and union members. Each of our and our subsidiaries' operating units has a separate labor union branch. We have not experienced any strikes or other labor disturbances which have interfered with our operations, and we believe that we have positive relations with our employees.

## **BUSINESS**

All employees who are unable to work due to illness or disability are entitled to receive certain benefits during their period of absence from the workplace. In addition, the PRC Government requires us to provide work-related injury insurance for each of our employees.

### **LEGAL PROCEEDINGS**

As of the Latest Practicable Date, we were involved in five legal proceedings of which the relief sought amounted to more than RMB5.0 million. Of these five proceedings, our Company is named as plaintiff to three, and defendant to two. The Directors of our Company believe we have recorded adequate provision for potential liabilities relating to any such claims and that there is no individual case or group of related cases pending that is likely to have a material adverse effect on our financial condition, results of operations or cash flows.

Neither we nor any of our subsidiaries is a party to any other litigation or arbitration of which the relief sought amounts to more than RMB5.0 million and no material litigation, arbitration or claim is known to us to be pending or threatened by or against us or our subsidiaries or with respect to any of our properties or operations.