

DIRECTORS' REPORT

The Board of Directors of the Company (the “**Board of Directors**”) is pleased to present its directors’ report together with the audited financial statements of the Group for the year ended December 31, 2006.

I Key Activities of the Group and Geographical Analysis

The Group is engaged in a broad range of petroleum-related activities, including:

- the exploration, development, production and sales of crude oil and natural gas;
- the refining, transportation, storage and marketing of crude oil and petroleum products;
- the production and sales of basic petrochemical products, derivative petrochemical products and other chemical products; and
- the transmission of natural gas, crude oil and refined products, and sales of natural gas.

The operating segment information on the above areas is set out in note 40 to the financial statements prepared in accordance with International Financial Reporting Standards (“**IFRS**”).

The businesses of the principal subsidiaries in which the Company had material interest and which could significantly affect the results or assets of the Group are set out in note 18 to the financial statements prepared in accordance with IFRS.

I Share Capital Structure

The Company issued 15,824,176,200 H shares (including H shares underlying ADSs) in April 2000. At the same time, CNPC offered 1,758,241,800 shares held by it in the Company to the public. After the issue and offer, the public held 17,582,418,000 shares in the Company, representing 10% of the total share capital of the Company immediately after the issue. The net proceeds from the share issue amounting to RMB20,337 million were intended to fund the Company’s capital expenditures and investments, to provide additional funds for general corporate purposes, and to repay short-term loans borrowed from third party financial institutions. The Company’s ADSs and H shares were listed on The New York Stock Exchange, Inc. and the HKSE on April 6, 2000 and April 7, 2000 respectively.

The Company issued 3,196,801,818 new H shares at a price of HK\$6.00 per share in September 2005. The net proceeds from the issue of new H shares were approximately RMB19,692 million. CNPC also sold 319,680,182 state-owned shares it held concurrently with the Company’s issue of new H shares in September 2005.

The share capital of the Company in issue as fully paid or credited as fully paid as at December 31, 2006 was 179,020,977,818 shares, with a par value of RMB1.00 each. As at December 31, 2006, the share capital structure of the Company was as follows:

Shares	Number of shares as at December 31, 2006	Percentage of the total number of shares in issue as at December 31, 2006 (%)
State-owned shares	157,922,077,818	88.21
Foreign-invested shares (H shares and ADSs)	21,098,900,000	11.79
Total	179,020,977,818	100

Changes in the share capital of the Company are set out in note 29 to the financial statements in this annual report prepared in accordance with IFRS.

Results and Distribution

The results for the year are set out in the Consolidated Profit and Loss Account on page 94.

The financial condition of the Group as at December 31, 2006 are set out in the Consolidated Balance Sheet on page 95.

The consolidated cashflow of the Group for the year is set out in the statement on page 97.

Dividends

The Board of Directors recommends to pay final dividends of RMB0.154699 per share (inclusive of applicable tax) from the balance of 45% of the net profit for the twelve months ended December 31, 2006 less the interim dividends for 2006 paid on September 30, 2006. The proposed final dividends are subject to shareholders' approval at the annual general meeting to be held on May 16, 2007. The final dividends will be paid to shareholders whose names appear on the register of members of the Company at the close of business on May 16, 2007. The register of members will be closed from April 16, 2007 to May 16, 2007 (both days inclusive) during which period no transfer of shares will be registered. In order to qualify for the final dividend, all transfer documents must be lodged, together with the relevant share certificates, at Hong Kong Registrars Limited no later than 4 p.m. on April 13, 2007.

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In accordance with Article 149 of its Articles of Association, dividends payable to the Company's shareholders shall be declared in Renminbi. Dividends payable to the holders of state-owned shares shall be paid in Renminbi while dividends payable to the holders of H shares shall be paid in Hong Kong Dollars. The amount of Hong Kong Dollars payable shall be calculated on the basis of the average of the closing exchange rates for Renminbi to Hong Kong Dollar as published by the People's Bank of China for the week prior to the declaration of the dividend at the shareholders' meeting to be held on May 16, 2007.

Final dividend will be paid on or around June 1, 2007.

Five—Years Financial Summary

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 10 and page 11.

Bank Loans and Other Borrowings

Details of bank loans and other borrowings of the Company and the Group as at December 31, 2006 are set out in note 28 to the financial statements prepared in accordance with IFRS in this annual report.

Interest Capitalisation

Interest capitalisation for the Group for the year ended December 31, 2006 was RMB1,315 million.

Fixed Assets

Changes to the fixed assets of the Company and the Group during the year are summarised in note 15 to the financial statements prepared in accordance with IFRS in this annual report.

Land Value Appreciation Tax

No land value appreciation tax was payable by the Group during the year.

Reserves

Details of changes to the reserves of the Company and the Group for the year ended December 31, 2006 are set out in note 30 to the financial statements prepared in accordance with IFRS in this annual report.

Distributable Reserves

As at December 31, 2006, the reserves of the Company that can be distributed as dividend were RMB205,379 million.

Statutory Common Welfare Fund

Details of the statutory welfare fund, such as the nature, application and movements and the basis of calculation (including the percentage and profit figure used for calculating the amounts) are set out in note 30 to the financial statements prepared in accordance with IFRS in this annual report.

Management Contract

During the year, the Company did not enter into any management contracts concerning the management or administration of its overall business or any of its material business, nor did any such management contract exist.

Employees' Retirement Scheme

Details of the Company's employees' retirement scheme are set out in note 34 to the financial statements prepared in accordance with IFRS in this annual report.

Major Suppliers and Customers

CNPC is the Group's largest supplier of goods and services and the aggregate purchase attributable to CNPC was 38% of the total purchase of the Group for 2006. The aggregate purchase attributable to the five largest suppliers of the Group was 46% of the Group's total purchase.

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The aggregate revenue derived from the major customers is set out in note 38 to the financial statements prepared in accordance with IFRS in this annual report. The aggregate revenue derived from the five largest customers was less than 30% of the Group's total sales.

None of the Directors, Supervisors and their associates or any shareholder (who to the knowledge of the Directors were holding 5% or more of the Company's share capital) had any interest in any of the above-mentioned suppliers and customers.

Repurchase, Sale or Redemption of Securities

The Company or any of its subsidiaries did not sell any securities of the Company, nor did it repurchase or redeem any of the securities of the Company during the twelve months ended December 31, 2006.

Trust Deposits and Irrecoverable Overdue Time Deposits

As at December 31, 2006, the Company did not have any trust deposits or irrecoverable overdue time deposits.

Pre-emptive Rights

There is no provision regarding pre-emptive rights under the Articles of Association of the Company or the PRC laws.

Material Litigation

The Group was not involved in any material litigation or dispute in 2006.

Sufficiency of Public Float

Based on the information that is publicly available to the Company and within the knowledge of the Directors, the Directors confirm that the Company has maintained the amount of public float as required under the Listing Rules during the financial period.

Annual General Meeting

At the 2005 annual general meeting held on May 26, 2006, the following resolutions were passed:

- (a) the Report of the Board of Directors for the year 2005 was approved;
- (b) the Report of the Supervisory Committee for the year 2005 was approved;
- (c) the Audited Financial Statements of the Company for the year 2005 was approved;
- (d) the proposal for the declaration and payment of a final dividend for the year ended December 31, 2005 was approved;
- (e) the proposal for the authorisation of the Board of Directors to determine the distribution of the interim dividend for the year 2006 was approved;
- (f) the proposal for the appointment of domestic and international accounting firms as accountants of the Company and to authorise the Board of Directors to determine their remuneration for the year 2006 was approved;
- (g) the re-election of Mr Zheng Hu as Director;
- (h) the re-election of Mr Franco Bernabè as independent non-executive Director; and
- (i) the proposal for the authorisation of the Board of Directors to issue shares of the Company was approved.

Directors

As at the date of this annual report, the Directors of the Company are as follows:

◆ Chairman	Mr Chen Geng	
◆ Vice Chairman	Mr Jiang Jiemin	
◆ Executive Director	Mr Duan Wende	
◆ Non-executive Directors	Mr Zheng Hu	Mr Zhou Jiping
	Mr Wang Yilin	Mr Zeng Yukang
	Mr Gong Huazhang	Mr Jiang Fan
	Mr Chee-Chen Tung	Mr Liu Hongru
◆ Independent Non-executive Directors	Mr Franco Bernabè	

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I Changes in Board of Directors and Supervisory Committee during the reporting period

Changes in the Board of Directors and the Supervisory Committee during the reporting period can be found in the section headed "Board of Directors and Supervisory Committee" in the Chairman's Report.

I Brief Biography Of Directors, Secretary to the Board of Directors, Supervisors and Senior Management

◆ Directors

• Chairman

Chen Geng: aged 60, is Chairman of the Board of the Company. Mr Chen is a senior economist and holds a college degree. He has nearly 40 years of working experience in China's oil and gas industry. Mr Chen was appointed Deputy Director of Changqing Petroleum Exploration Bureau in October 1983, Deputy Director of the Labour Department under the Ministry of Petroleum Industry in April 1985, Director of the Labour Bureau of China National Petroleum Corporation from August 1988, Assistant to the General Manager of China National Petroleum Corporation in December 1993, Deputy General Manager of China National Petroleum Corporation in September 1997, Deputy Director of the State Petroleum and Chemical Industry Bureau in March 1998, Deputy General Manager of CNPC in February 2001, and the General Manager of CNPC from April 2004 to November 2006. Mr Chen was appointed as a Director of the Company in June 2001. He was the President of the Company from December 2002 to May 2004. He became the Chairman of the Company in May 2004.

• Vice Chairman

Jiang Jiemin: aged 51, is the Vice Chairman, President of the Company and the General Manager of CNPC. Mr Jiang is a senior economist and has been awarded with post-graduate qualification. Mr Jiang has over 30 years of working experience in China's oil and gas industry. He was made Deputy Director of the Shengli Petroleum Administration Bureau in March 1993, Senior Executive of the Qinghai Petroleum Administration Bureau in June 1994 and Director of Qinghai Petroleum Administration Bureau in November 1994, Assistant to the General Manager and Team Leader for the Restructuring and Listing Preparatory

Team of CNPC in February 1999, and a Director and Vice President of the Company from November 1999 to June 2000. Mr Jiang was appointed Deputy Provincial Governor of Qinghai Province since June 2000, was made a member of the provincial party committee of the Qinghai Province and Deputy Provincial Governor of Qinghai since November 2000, and the deputy secretary of the provincial party committee of Qinghai Province and Deputy Provincial Governor of Qinghai since June 2003. Mr Jiang became the Vice Chairman and President of the Company in May 2004 and the General Manager of CNPC since November 2006.

- Executive Director

Duan Wende: aged 55, is a Director and Senior Vice President of the Company. He is a senior engineer and has been awarded with post-graduate qualification. He has over 35 years of working experience in China's petrochemical industry. From April 1975 to May 1997, Mr Duan was the Deputy Factory Manager of Fushun Chemical Fibres Factory, the Commander of the Fushun Ethylene Project Command Division, Deputy Factory Manager of the ethylene factory, the Factory Manager of the acrylic fibres factory and the detergent factory. He has been the Deputy Manager of Fushun Petrochemical Corporation since May 1997. He has been the Manager of Fushun Petrochemical Corporation since May 1999; he has been appointed as the General Manager of Fushun Petrochemical Branch Company since October 1999. He has been Assistant to the General Manager of CNPC since August 2001. He has been a Vice President of the Company since March 2002. He was appointed as a Director of the Company since May 2004. He has been appointed as a Senior Vice President of the Company since November 2005.

- Non-executive Directors

Zheng Hu: aged 60, is a Director of the Company and a Deputy General Manager of CNPC. Mr Zheng is a senior engineer and holds a college degree. He has nearly 40 years of working experience in China's oil and gas industry. From May 1990 to July 1992, Mr Zheng was the Vice Chancellor of Beijing Petroleum Managers Training Institute. From July 1992 to September 1999, Mr Zheng worked as Deputy General Manager and General Manager of China Petroleum Technology Development Corporation, China Petroleum Materials and Equipment (Group) Corporation, and from September 1999, as director of Personnel and Labour Department of CNPC. He has been a Director of the Company since June 2000. He has been appointed a Deputy General Manager of CNPC since August 2000.

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Zhou Jiping: aged 54, is a Director of the Company and a Deputy General Manager of CNPC. Mr Zhou is a senior engineer and holds a master's degree. He has over 35 years of working experience in China's oil and gas industry. In November 1996, he was Deputy Director of the International Exploration and Development Co-operation Bureau of China National Petroleum Corporation and Deputy General Manager of China National Oil & Gas Exploration and Development Corporation. In December 1997, he was appointed General Manager of China National Oil & Gas Exploration and Development Corporation and Deputy Director of the International Exploration and Development Co-operation Bureau of China National Petroleum Corporation. Since August 2001, he was Assistant to the General Manager of CNPC and General Manager of China National Oil & Gas Exploration and Development Corporation. Since December 2003, Mr Zhou has been a Deputy General Manager of CNPC. Mr Zhou was appointed a Director of the Company in May 2004.

Wang Yilin: aged 50, is a Director of the Company and a Deputy General Manager and Safety Director of CNPC. Mr Wang is a senior engineer and holds a doctorate's degree. He has nearly 25 years of working experience in China's oil and gas industry. Mr Wang had been the Deputy Director and Chief Exploration Geologist of Xinjiang Petroleum Administration Bureau since June 1996. He was appointed as the President of the Xinjiang Oilfield Branch of the Company since September 1999. He had been the Senior Executive of Xinjiang Petroleum Administration Bureau and the President of the Xinjiang Oilfield Branch of the Company since June 2001. From July 2003 onwards, he was appointed as the Assistant to General Manager of CNPC, Senior Executive of Xinjiang Petroleum Administration Bureau and the President of the Xinjiang Oilfield Branch of the Company concurrently. In December 2003, he was appointed as the Deputy General Manager of CNPC and Senior Executive of Xinjiang Petroleum Administration Bureau and the President of the Xinjiang Oilfield Branch of the Company concurrently. From May 2004, he ceased to work as the Senior Executive of Xinjiang Petroleum Administration Bureau and the President of the Xinjiang Oilfield Branch of the Company. From July 2004 onwards, he also worked as the Safety Director of CNPC. He was appointed as Director of the Company since November 2005.

Zeng Yukang: aged 56, is a Director of the Company and a Deputy General Manager of CNPC. Mr Zeng is a senior economist and holds a college degree. He has nearly 40 years of working experience in China's oil and gas industry. Mr Zeng had been the Senior Executive of the Exploration and Development Institute of Daqing Petroleum Administration Bureau since December 1996. From February 2000 onwards, he was appointed as the Standing Deputy Director of Daqing Petroleum Administration Bureau. Since March 2001, he was appointed as the Director of Daqing Petroleum Administration Bureau. Since November 2002, he was the Assistant to the General Manager of CNPC. From September 2005 onwards,

he has been the Deputy General Manager of CNPC. He was appointed as a Director of the Company since November 2005.

Gong Huazhang: aged 60, is a Director of the Company and the General Accountant of CNPC. Mr Gong is a senior accountant and has over 40 years of working experience in China's oil and gas industry. Mr Gong worked as the Chief Accountant, deputy director and director of the Finance Bureau of China National Petroleum Corporation from 1991. He was the director of Finance and Assets Department of CNPC since October 1998 and has been the General Accountant of CNPC since February 1999. Mr Gong has been a Director of the Company since November 1999.

Jiang Fan: aged 43, is a Director of the Company and the President of Dalian Petrochemical Company. Mr Jiang is a senior engineer and holder of a master's degree. He has over 20 years of working experience in China's petrochemical industry. Mr Jiang was appointed as the Deputy Manager of Dalian Petrochemical Company since December 1996. In September 1999, he was appointed as the Deputy General Manager of Dalian Petrochemical Company. In February 2002, he became the General Manager of Dalian Petrochemical Company. Mr Jiang has been a Director of the Company since November 2005.

- Independent Non-executive Directors

Chee-Chen Tung: aged 64, is an independent non-executive Director of the Company. Mr Tung is the Chairman and Chief Executive Officer of Orient Overseas (International) Limited and was educated at the University of Liverpool, England, where he received his Bachelor of Science degree. He later acquired a Master's degree in Mechanical Engineering at the Massachusetts Institute of Technology in the United States. He served as Chairman of the Hong Kong Shipowners' Association between 1993 and 1995. From 1999 to 2001, he was the Chairman of the Hong Kong General Chamber of Commerce. He is an independent non-executive director of Zhejiang Expressway Co. Ltd., BOC Hong Kong (Holdings) Limited, Sing Tao News Corporation Limited, Wing Hang Bank, Limited and Cathay Pacific Airways Limited, and a member of the Hong Kong Port Development Board. Mr Tung is also the Chairman of the Institute for Shipboard Education Foundation, the Chairman of the Advisory Council of the Hong Kong Polytechnic University, and is a member of the Board of Trustees of the International Academic Centre of the University of Pittsburgh and the School of Foreign Service of Georgetown University. Mr Tung has been appointed as an independent non-executive Director of the Company since November 5, 1999.

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Liu Hongru: aged 76, is an independent non-executive Director of the Company. Mr Liu graduated from the Faculty of Economics of the University of Moscow in 1959 with an associate Doctorate's degree. Mr Liu worked as Vice-Governor of the Agricultural Bank of China, Vice-Governor of the People's Bank of China, Deputy Director of the State Economic Restructuring Committee, and the Chairman of the China Securities Regulatory Commission. Mr Liu is currently the President of the China Foundation for Development of Financial Education and the Chairman of the Capital Market Research Institute. Mr Liu is also a professor at the Peking University, the Postgraduate School of the People's Bank of China and the City University of Hong Kong. Mr Liu serves as an independent non-executive director or non-executive director in three other listed companies in Hong Kong, and possesses the accounting or financial management qualification required under the Listing Rules. Mr Liu was appointed as an independent Supervisor of the Company in December 1999. Upon his resignation from this post, he has been appointed as an independent non-executive Director of the Company since November 19, 2002.

Franco Bernabè: aged 58, is an independent non-executive Director of the Company. Mr Bernabè is the Chairman of the Franco Bernabè Group and Vice Chairman of H3G. He is also a vice chairman of Rothschild Europe. He was a former Chief Executive Officer of ENI and Telecom Italia. He has also served as a special representative of the Italian government for the reconstruction of the Balkan region. Mr Bernabè joined ENI in 1983 to become an assistant to the chairman; in 1986 he became director for development, planning and control; and between 1992 and 1998 was the Chief Executive Officer of ENI. Mr Bernabè led the restructuring program of the ENI Group, making it one of the world's most profitable oil companies. Between 1998 and 1999, Mr Bernabè was the Chief Executive Officer of Telecom Italia. Prior to his joining ENI, Mr Bernabè was the head of economic studies at FIAT. Mr Bernabè was a senior economist at the OECD Department of Economics and Statistics in Paris. Prior to that, he was a professor of economic politics at the School of Industrial Administration, Turin University. Mr Bernabè has been appointed as an independent non-executive Director of the Company since June 30, 2000.

- Secretary to the Board of Directors

Li Huaiqi: aged 57, is the Secretary to the Board of Directors of the Company. Mr Li is a senior economist. He has over 35 years of working experience in China's oil and gas industry. Mr Li once worked in the Daqing Oil Field, the Liaohe Oil Field and the Huabei Oil Field and in the Nanhai Petroleum Company. From June 1992 to October 1998, Mr Li worked as Deputy Director and Director of the Foreign Affairs Bureau and Chairman of the Foreign Service Company of China National Petroleum Corporation.

From October 1998, Mr Li was appointed as Director of the International Co-operation Department (Foreign Affairs Bureau) of CNPC. Mr Li has been the Secretary to the Board of Directors of the Company since August 2001.

◆ Supervisors

• Chairman

Wang Fucheng: aged 56, is the Chairman of the Supervisory Committee. Mr Wang is a senior economist and holds a bachelor's degree. Mr Wang has over 40 years of working experience in China's oil and gas industry. From August 1986 to December 1992, Mr Wang worked as Senior Executive of the Shengli Petroleum Administration Bureau. Since December 1992, Mr Wang worked as Senior Executive of the Liaohe Oil Exploration Bureau. Since November 1997, Mr Wang worked as Director of the Liaohe Oil Exploration Bureau. Since October 1999, Mr Wang was the President of the Liaohe Oil Field Branch of the Company. Mr Wang was appointed as a Director of the Company since June 2000 and was appointed as the Vice President of the Company in July 2000. Prior to the appointment as Supervisor of the Company, Mr. Wang has resigned from his office as Director of the Company. Mr Wang has been appointed as the Chairman of the Supervisory Committee of the Company since November 2005.

• Supervisors

Wen Qingshan: aged 48, is a Supervisor of the Company and the Director of the Finance and Assets Department of CNPC. Mr Wen is a senior accountant and holder of a master's degree. He was the Deputy Chief Accountant of the Finance and Assets Department of CNPC from November 1998, Deputy Director of the Finance and Assets Department of CNPC from May 1999 and Director of the Finance and Assets Department of CNPC from May 2002. He has been a Supervisor of the Company since November 2002.

Sun Xianfeng: aged 54, is a Supervisor of the Company and the Director of the Audit Department and the Audit Services Centre of CNPC. Mr Sun holds a college degree. Mr Sun worked as Deputy Director of the Supervisory Bureau of China National Petroleum Corporation from November 1996, before being transferred to the Eighth Office of the State Council Compliance Inspectors' General Office (Supervisory Committee of Central Enterprises Working Commission) as its temporary person-in-charge in June 1998.

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He has been the Deputy Director of the Audit Department of CNPC from October 2000, and as the Director of the Audit Services Centre since December 2000. He has been the Director of the Audit Department of CNPC and the Director of the Audit Services Centre since April 2004. He has been a Supervisor of the Company since May 2004.

Xu Fengli: aged 59, is a Supervisor and General Manager of the Audit Department of the Company. Mr Xu is a senior accountant and has nearly 35 years of work experience in China's petrochemical industry. Mr Xu has been the Chief Accountant of Fushun Petrochemical Corporation in November 1995, Deputy Director of the Finance and Assets Department of CNPC in November 1998, Deputy General Manager of the Finance Department of the Company since December 1999, and Director of the Administrative Office of the Supervisory Committee of the Company since October 2003. He has been a Supervisor of the Company since May 2004 and the General Manager of the Audit Department of the Company since November 2005.

Qin Gang: aged 53, is an employee representative of the Company's Supervisory Committee and a Senior Executive of the Tarim Oilfield Branch of the Company. Mr Qin is a senior engineer and has over 35 years of experience in China's oil and gas industry. Mr. Qin has acted as a Deputy Commander of Tarim Petroleum Exploration and Development Headquarters since November 1997 and a Deputy General Manager of Tarim Oilfield Company since September 1999. From June 2000, Mr Qin worked as the Senior Executive of Tarim Southwest Company concurrently. Since July 2002, Mr Qin has worked as an executive and the Chairman of Labour Union of CNPC Tarim Oilfield Company. Mr Qin was appointed as a Supervisor of the Company in November 2005.

- Independent Supervisors

Li Yongwu: aged 62, is an independent Supervisor of the Company. Mr Li is a senior engineer and holder of a bachelor's degree. Since June 1991, Mr Li was appointed as the Director of Tianjin Chemicals Bureau. Since July 1993, he was appointed as the Director of Tianjin Economic Committee. He became the Deputy Director of the Chemical Industry Department since April 1995. He became Director of the State's Petroleum and Chemical Industry Bureau since March 1998. Since April 2001, he was appointed as a Deputy Director of the Liaison Office of the Central Government at the Special Administrative Region of Macau. Since December 2004, he was appointed as the Vice President of China Petroleum and Petrochemical Industry Association. Since May 2005, he became the President of China Petroleum

and Petrochemical Industry Association. Mr Li has been an Independent Supervisor of the Company since November 2005. In 2003, he was elected as a standing member of the Tenth Chinese People's Consultative Conference.

Wu Zhipan: aged 50, is an independent Supervisor of the Company. Mr Wu is a holder of doctorate degree. Mr Wu is currently the Vice-chancellor of the Peking University. He is also an expert consultant of the Supreme People's Court of the PRC, an arbitrator of the Arbitration Panel of China International Economic and Trade Arbitration Commission and President of the China Economic Law Research Societies. Mr Wu has been an independent Supervisor of the Company since December 1999.

◆ Other Senior Management

Wang Guoliang: aged 54, is Chief Financial Officer of the Company. Mr Wang is a senior accountant and holds a master's degree. Mr Wang has 25 years of working experience in China's oil and gas industry. Mr Wang worked as the Vice President of China Petroleum Finance Company Limited from October 1995 to November 1997. From November 1997 to November 1999, he was the Deputy General Manager and General Accountant of China National Oil & Gas Exploration and Exploitation Corporation. Mr Wang was appointed as the Chief Financial Officer of the Company since November 1999. From November 1999 to March 2002, he was also the General Manager of the Company's Finance Department.

Liao Yongyuan: aged 44, is the Vice President of the Company. Mr Liao is a senior engineer and a master's degree holder. He has nearly 25 years of working experience in China's oil and gas industry. He was Deputy Director of the New Zone Exploration and Development Department of China National Petroleum and Gas Corporation from June to November 1996, the Standing Deputy Commander and then Commander of Tarim Petroleum Exploration and Development Headquarters from November 1996 to September 1999. He was General Manager of Tarim Oilfield Branch Company from September 1999 to October 2001, and also Deputy Director of Gansu Provincial Economic and Trade Committee from October 2001 to January 2004. He has worked as the Assistant to the General Manager of CNPC since January 2004 and has been concurrently the Head of Coordination Team for Oil Enterprises in Sichuan and Chongqing and Director of Sichuan Petroleum Administration Bureau since April 2004. He has been a Vice President of the Company since November 2005.

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Jia Chengzao : aged 58, is a Vice President of the Company. Mr Jia is a senior engineer, a Doctorate degree holder and a fellow of the Chinese Academy of Sciences. He has over 25 years of working experience in the oil and geological industry of the PRC. From August 1994, Mr. Jia has worked as the Deputy Chief Geologist of the Tarim Oil Exploration and Exploitation Headquarters and the Chief Geologist and Deputy Commander of the Tarim Oil Exploration and Exploitation Headquarters. From February 1998, he has also been a Vice President of the China Oil Exploration and Exploitation Scientific Research Institute of CNPC. From September 1999, Mr. Jia worked as the Deputy General Manager of the Tarim Oil Field Branch of the Company. He has been the Chief Geologist of the Company from July 2000. Mr Jia also served as the President of the China Oil Exploration and Exploitation Research Institute from December 2002 to October 2006. Mr Jia has been a Vice President of the Company since November 2005.

Hu Wenrui: aged 57, is a Vice President of the Company. Mr Hu is a senior engineer and has over 35 years of working experience in China's oil and gas industry. From April 1984, Mr Hu was Manager of Changqing Oilfield No. 2 Oil Extraction Plant. He was Deputy Director of Changqing Petroleum Exploration Bureau since April 1989, Standing Deputy Director since November 1996, and eventually Director of Changqing Petroleum Exploration Bureau since April 1999. From September 1999 to December 2002, he was the General Manager of Changqing Oilfield Branch Company. He has been President of the Company's Exploration and Production Branch since December 2002. Mr Hu has been a Vice President of the Company since November 2005.

◆ Qualified Accountant

In an announcement dated October 18, 2004, the Company announced that it had not been able to find a suitable accountant with professional accounting qualifications recognised to assume the position of qualified accountant as required under Rule 3.24 of the Listing Rules by September 30, 2004. The Company is still in the process of identifying suitable candidates with professional accounting qualifications to assist the Chief Financial Officer to oversee the compliance by the Company of the financial reporting and other related accounting matters. However, despite numerous attempts to find such a candidate, given the importance of the role and the function of the qualified accountant, the Company has still not been able to find a suitable candidate that meets all the requirements in Rule 3.24 of the Listing Rules. The Company is trying its best to identify a candidate with the appropriate qualifications, experience and understanding of the oil and gas industry to act as the joint qualified accountant to assist the Chief Financial Officer of the Company to carry out his duties. The Company will make an application for a 3-year waiver to the HKSE when it has identified the joint qualified accountant.

Shareholdings of Major Shareholders

As at December 31, 2006, the register of interests in shares and short positions kept by the Company under section 336 of the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) (the “SFO”) showed that the persons in the following table and notes held interests or short positions in the Company’s shares:

Name of Shareholder	Type of Shares	No. of Shares	Percentage (%) of the total number of that class in issue	Percentage (%) of the total share capital
CNPC	State-owned shares	157,922,077,818	100.00	88.21
Warren E. Buffett ⁽¹⁾	H shares	2,347,761,000	11.13	1.311
J.P. Morgan Chase & Co. ⁽²⁾	H shares	1,062,215,120(L) 711,247,550(S) ⁽³⁾ 821,572,360(P) ⁽⁴⁾	5.03(L) 3.37(S) 3.89(P)	0.593 0.397 0.459
Templeton Asset Management Limited	H shares	1,054,208,903(L)	5.00(L)	0.589

Notes:

(1) By virtue of Warren E. Buffett’s 35.4% interest in Berkshire Hathaway Inc., Berkshire Hathaway’s 100% interest in OBH Inc., OBH Inc.’s 100% interest in National Indemnity Co. and 100% interest in GEICO Corporation, and GEICO Corporation’s 100% interest in Government Employees Inc. Company, each of Warren E. Buffett, Berkshire Hathaway Inc. and OBH Inc. is deemed to be interested in 2,279,151,000 H shares held by National Indemnity Co. and 68,610,000 H shares held by Government Employees Inc. Company, totalling 2,347,761,000 H shares.

(2) J.P. Morgan Chase & Co. through its various controlled corporations is deemed to be interested in an aggregate of 1,062,215,120 H shares of the Company

Of these 1,062,215,120 H shares, 831,400,360 H Shares are directly held by JP Morgan Chase Bank, N.A., J.P. Morgan Chase & Co. is deemed to be interested in these 831,400,360 H shares by virtue of its 100% interest in JP Morgan Chase Bank, N.A.; 9,894,000 H shares are directly held by J.P. Morgan Securities Ltd., by virtue of J.P. Morgan Chase International Holdings Limited’s 98.95% interest in J.P. Morgan Securities Ltd., J.P. Morgan Chase (UK) Holdings Limited’s 100% interest in J.P. Morgan Chase International Holdings Limited, J.P. Morgan Capital Holdings Limited’s 100% interest in J.P. Morgan Chase (UK) Holdings Limited and J.P. Morgan International Finance Limited’s 100% interest in J.P. Morgan Capital Holdings Limited, J.P. Morgan Chase International Holdings Limited, J.P. Morgan Chase (UK) Holdings Limited, J.P. Morgan Capital Holdings

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Limited and J.P. Morgan International Finance Limited are deemed to be interested in these 9,894,000 H shares; 87,525,058 H shares are directly held by J.P. Morgan Whitefriars Inc., J.P. Morgan Overseas Capital Corporation is deemed to be interested in these 87,525,058 H shares by virtue of its 100% interest in J.P. Morgan Whitefriars Inc.; 26,935,702 H shares are directly held by J.P. Morgan Investment Management Inc., JP Morgan Asset Management Holdings Inc. is deemed to be interested in these 26,935,702 H shares by virtue of its 100% interest in J.P. Morgan Investment Management Inc.; 2,234,000 H shares are directly held by JF International Management Inc., JP Morgan Asset Management (Asia) Inc. is deemed to be interested in these 2,234,000 H shares by virtue of its 100% interest in JF International Management Inc.; 101,756,000 H shares are directly held by JF Asset Management Limited, JP Morgan Asset Management (Asia) Inc. is deemed to be interested in these 101,756,000 H shares by virtue of its 100% interest in JF Asset Management Limited; 2,470,000 H shares are directly held by J.P. Morgan International Bank Limited, J.P. Morgan Overseas Capital Corporation is deemed to be interested in these 2,470,000 H shares by virtue of its 100% interest in J.P. Morgan International Bank Limited.

Of these 1,062,215,120 H shares, 99,889,058 H shares are indirectly held by J.P. Morgan International Finance Limited, by virtue of Bank One International Holdings Corporation's 100% interest in J.P. Morgan International Finance Limited, J. P. Morgan International Inc.'s 100% interest in Bank One International Holdings Corporation, JP Morgan Chase Bank, N.A.'s 100% interest in J. P. Morgan International Inc, J.P. Morgan Chase & Co.'s 100% interest in JP Morgan Chase Bank, N.A., Bank One International Holdings Corporation, J. P. Morgan International Inc., JP Morgan Chase Bank, N.A. and J.P. Morgan Chase & Co. are also deemed to be interested in these 99,889,058 H shares; 89,995,058 H shares are also indirectly held by J. P. Morgan Overseas Capital Corporation, J. P. Morgan International Finance Limited is also deemed to be interested in these shares by virtue of its 100% interest in J. P. Morgan Overseas Capital Corporation; 130,925,702 H shares are also indirectly held by JP Morgan Asset Management Holdings Inc., J.P. Morgan Chase & Co. is also deemed to be interested in these shares by virtue of its 100% interest in JP Morgan Asset Management Holdings Inc.; and 130,990,000 H shares are also indirectly held by JP Morgan Asset Management (Asia) Inc., JP Morgan Asset Management Holdings Inc. is also deemed to be interested in these shares by virtue of its 100% interest in JP Morgan Asset Management (Asia) Inc.

(3) Comprising the short positions as defined in the SFO.

(4) Comprising 821,790,360 H shares in the lending pool as defined in the SFO. The term "lending pool" is defined as (i) shares that the approved lending agent holds as agent for a third party which he is authorised to lend and other shares that can be lent according to the requirements of the Securities Borrowing and Lending Rules; and (ii) shares that have been lent by the approved lending agent, and only if the right of the approved lending agent to require the return of the shares has not yet been extinguished.

As at December 31, 2006, save as disclosed above, no person (other than the Directors, senior management or the Supervisors of the Company) had recorded an interest in the register of interests in shares and short positions kept pursuant to section 336 of the SFO.

Interests of Directors and Supervisors in the Share Capital of the Company

As at December 31, 2006, none of the Directors or Supervisors had any interest and short positions in any shares, underlying shares or debentures of the Company or any associated corporation within the meaning of Part XV of the SFO required to be recorded in the register mentioned under Section 352 of the SFO or as otherwise notifiable to the Company and the HKSE by the Directors and Supervisors pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the “**Model Code**”).

As at December 31, 2006, the Company has not granted its Directors, Supervisors or their respective spouses or children below 18 any rights to subscribe for its equity securities or debt securities.

Service Contracts of Directors and Supervisors

No service contract existed or has been proposed between the Company or any of its subsidiaries with any of the above Directors or Supervisors. No Director or Supervisor has entered into any service contract with the Company which is not terminable by the Company within one year without payment of compensation other than statutory compensation.

Interests of Directors and Supervisors in Contracts

None of the Directors or Supervisors had any material personal interest, either directly or indirectly, in any contract of significance to which the Company or any of its subsidiaries was a party to during the year.

Remuneration of Directors and Supervisors

Details of remuneration of Directors and Supervisors and the remuneration policy are set out in note 10 to the financial statements prepared in accordance with IFRS in this annual report.

Connected Transactions

As at December 31, 2006, CNPC directly owns an aggregate of approximately 88.21% of the shares of the Company and therefore transactions between the Group and CNPC constitute connected

DIRECTORS' REPORT

transactions between the Group and CNPC under Chapter 14A of the Listing Rules. As at December 31, 2006, CNPC (Hong Kong) Limited (stock code: 135) ("**CNPC (HK)**") is a 51.99% owned subsidiary of CNPC which is also the Company's controlling shareholder holding approximately 88.21% of the issued share capital of the Company. Therefore, transactions between the Group and CNPC (HK) constitute connected transactions between the Group and CNPC (HK) under Chapter 14A of the Listing Rules. As Beijing Gas Group Co., Ltd. ("**Beijing Gas**") and China Railway Materials and Suppliers Corporation ("**CRMSC**") are respectively a substantial shareholder (as defined under the Listing Rules) of Beijing Huayou Gas Corporation Limited and PetroChina and CRMSC Oil Marketing Company Limited, the Group's subsidiaries, pursuant to Chapter 14A of the Listing Rules, the transactions between the Group and Beijing Gas and CRMSC respectively constitute connected transactions of the Group. Each of CNPC and the Company is interested in 50% interest in CNPC Exploration and Development Company Limited ("**CNPC E&D**") respectively, and therefore, CNPC E&D is a connected person of the Company. On December 28, 2006, the Company became interested in 67% equity interest in PetroKazakhstan Inc. ("**PKZ**") through CNPC E&D. Pursuant to the Listing Rules, any subsidiaries of CNPC E&D being a connected person will also be treated as connected person(s) of the Company. Therefore, transactions between the Group and (i) CNPC E&D and (ii) PKZ constitute connected transactions of the Group under the Listing Rules.

◆ One-off Connected Transaction

Acquisition of 67% interest in PKZ

Pursuant to an acquisition agreement dated August 23, 2006 entered into between Pervinage Holding B.V. (a wholly-owned subsidiary of CNPC E&D) and 819 Luxembourg S. a r. l. (an indirect wholly-owned subsidiary of CNPC), CNPC E&D has acquired from CNPC the 67% equity interest indirectly held by CNPC in PKZ for a cash consideration of RMB21,376 million. The acquisition was completed on December 28, 2006. As CNPC is the controlling shareholder of the Company and as each of CNPC and the Company is interested in 50% interest in CNPC E&D respectively, therefore, CNPC and CNPC E&D are connected persons of the Company. The acquisition constitutes a connected transaction for the Company under the Listing Rules. Details of the transaction were announced by the Company on August 23, 2006.

◆ Continuing Connected Transactions

I. Continuing Connected Transactions with CNPC

The Group and CNPC continue to carry out certain existing continuing connected transactions and have entered into new continuing connected transactions throughout the reporting period. The Company sought independent shareholders' approval at the general meeting held on November 8, 2005 for a renewal of the existing continuing connected transactions and the new continuing connected transactions and proposed the new caps for existing continuing connected transactions and the new continuing connected transactions for January 1, 2006 to December 31, 2008. The Company further sought independent shareholders' approval at the general meeting held on November 1, 2006 for a renewal of the caps for the existing continuing connected transactions for January 1, 2006 to December 31, 2008 which were previously approved by shareholders at the general meeting held on November 8, 2005.

The Group and CNPC will continue to carry out the existing continuing connected transactions referred to in the following agreements:

1. Comprehensive Products and Services Agreement, First Supplemental Comprehensive Agreement and Second Supplemental Comprehensive Agreement

(1) The Group and CNPC continue to implement the Comprehensive Products and Services Agreement ("**Comprehensive Agreement**") entered into on March 10, 2000 for the provision (i) by the Group to CNPC and (ii) by CNPC to the Group, of a range of products and services which may be required and requested from time to time by either party and/or its subsidiary companies and affiliates. The Comprehensive Agreement has been amended by the First Supplemental Comprehensive Agreement and the Second Supplemental Comprehensive Agreement.

The term of the Comprehensive Agreement was initially 10 years starting from the date when the Company's business license was issued. This term has been amended by the Second Supplemental Comprehensive Agreement to 3 years commencing from January 1, 2006.

During the term of the Comprehensive Agreement, termination of the product and service implementation agreements described below may be effected from time to time by the parties to the product and service implementation agreements providing at least 6 months' written notice of termination in relation to any one or more categories of products or services. Further, in respect of any products or services already contracted to be provided, termination may not take place until after such products and services have been provided.

DIRECTORS' REPORT

(A) Products and Services to be provided by the Group to CNPC

Under the Comprehensive Products and Services Agreement, products and services to be provided by the Group to CNPC include such products as refined products, chemical products, natural gas, crude oil and such services as relating to the supply of water, electricity, gas and heating, quantifying and measuring and quality inspection and other products and services as may be requested by the CNPC Group for its own consumption, use or sale from time to time.

(B) Products and Services to be provided by CNPC to the Group

More products and services are to be provided by CNPC to the Group, both in terms of quantity and variety, than those to be provided by the Group to CNPC. Products and services to be provided by CNPC to the Group have been grouped together and categorised according to the following types of products and services:

- Construction and technical services, including but not limited to exploration technology service, downhole operation service, oilfield construction service, oil refinery construction service and engineering and design service;
- Production services, including but not limited to water supply, electricity generation and supply, gas supply and communications;
- Supply of materials services, including but not limited to purchase of materials, quality control, storage of materials and delivery of materials;
- Social services, including but not limited to security services, education and hospitals;
- Ancillary services, including but not limited to property management, training centers and guesthouses; and
- Financial services, including but not limited to loans and deposits services.

The Comprehensive Agreement details specific pricing principles for the products and services to be provided pursuant to the Comprehensive Agreement. If, for any reason, the specific pricing principle for a particular product or service ceases to be applicable, whether due to a change in circumstances or otherwise, such product or service must then be provided in accordance with the following general pricing principles as defined in the Comprehensive Agreement:

- (a) state-prescribed prices; or
- (b) where there is no state-prescribed price, then according to the relevant market prices; or
- (c) where neither (a) nor (b) is applicable, then according to:
 - (i) the actual cost incurred; or
 - (ii) the agreed contractual price.

In particular, the Comprehensive Agreement stipulates, among other things, that:

- (i) the loans and deposits shall be provided at prices determined in accordance with the relevant interest rate and standard for fees as promulgated by the People's Bank of China. Such prices must also be more favourable than those provided by independent third parties; and
- (ii) the guarantees shall be provided at prices not higher than the fees charged by the state policy banks in relation to the provision of guarantees. References must also be made to the relevant state-prescribed price and market price.

(2) First Supplemental Comprehensive Agreement

The First Supplemental Comprehensive Agreement dated June 9, 2006 was entered principally to amend the definitions of "state-prescribed price" and "market price" in the Comprehensive Agreement in view of the characteristics of overseas business and to amend the term of the Comprehensive Agreement to three years. The First Supplemental Comprehensive Agreement took effect on December 19, 2006.

(3) Second Supplemental Comprehensive Agreement

The Second Supplemental Comprehensive Agreement entered into by CNPC and the Company on September 1, 2006 provides for certain new continuing connected transactions between the Company and certain companies in which both the Company and CNPC are shareholders, and where CNPC and/or its subsidiaries and/or affiliates (individually or together) is/are entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of such company ("**Jointly-owned Companies**"). In the Second Supplemental Comprehensive Agreement, CNPC and the Company agreed to amend certain terms of the Comprehensive Agreement, including, among other things, that:

- both CNPC and the Company shall provide and shall procure their respective entities including their subsidiaries, branches and other relevant units to provide products and services in accordance with

the terms and principles of the Comprehensive Agreement;

- the CNPC Group will provide certain risk operation services as part of the construction and technical services to the Group, and these include the provision of exploration, production and other relevant services within certain and specific reserves of the Company with exploration and exploitation difficulties;
- the Group will provide certain financial assistance to the Jointly-owned Companies including entrustment loans and guarantees;
- the Jointly-owned Companies will provide certain financial assistance to the Group including entrustment loans and guarantees; and

Under the Second Supplemental Comprehensive Agreement, the products and services shall be provided at prices determined according to the pricing principles for the corresponding products or services under the Comprehensive Agreement (as amended).

The Second Supplemental Comprehensive Agreement has taken effect on January 1, 2006.

2. Product and Service Implementation Agreements

According to the current arrangements, from time to time and as required, individual product and service implementation agreements may be entered into between the relevant service companies and affiliates of CNPC Group or the Group providing the relevant products or services, as appropriate, and the relevant members of the Group or CNPC Group, requiring such products or services, as appropriate.

Each product and service implementation agreement will set out the specific products and services requested by the relevant party and any detailed technical and other specifications which may be relevant to those products or services. The product and service implementation agreements may only contain provisions which are in all material respects consistent with the binding principles and guidelines and terms and conditions in accordance with which such products and services are required to be provided as contained in the Comprehensive Agreement.

As the product and service implementation agreements are simply further elaborations on the provision of products and services as contemplated by the Comprehensive Agreement, they do not as such constitute new categories of connected transactions.

3. Land Use Rights Leasing Contract

The Company and CNPC continue to implement the Land Use Rights Leasing Contract entered into on March 10, 2000 under which CNPC has leased a total of 42,476 parcels of land in connection with all aspects of the operations and business of the Company covering an aggregate area of approximately 1,145 million square metres, located throughout the PRC, to the Company for a term of 50 years at an annual fee of RMB2 billion. The total fee payable for the lease of all such property may, after the expiration of 10 years from the effective date of the Land Use Rights Leasing Contract, be adjusted (to reflect market conditions prevalent at such time of adjustment, including the then prevailing marketing prices, inflation or deflation and such other factors considered as important by both parties in negotiating and agreeing to any such adjustment) by agreement between the Company and CNPC. In addition, any governmental, legal or other administrative taxes and fees required to be paid in connection with the leased properties will be borne by CNPC. However, any additional amount of such taxes payable as a result of changes in the PRC government policies after the effective date of the contract shall be shared proportionately on a reasonable basis between CNPC and the Company.

4. Buildings Leasing Contract and Buildings Supplementary Leasing Agreement

The Company and CNPC continue to implement the Buildings Leasing Contract entered into on March 10, 2000 pursuant to which CNPC has leased to the Company a total of 191 buildings covering an aggregate of area of 269,770 square metres, located throughout the PRC for the use by the Company for its business operation including the exploration, development and production of crude oil, the refining of crude oil and petroleum products, the production and sale of chemicals, etc. The 191 buildings were leased at a price of RMB145 per square metre per year, that is, an aggregate annual fee of RMB39,116,650 for a term of 20 years. The Company is responsible for the payment of any governmental, legal or other administrative taxes and maintenance charges required to be paid in connection with these 191 buildings.

Further to the Buildings Leasing Contract mentioned above, the Company entered into a Supplemental Buildings Leasing Agreement (the “**Supplemental Buildings Agreement**”) with CNPC on September 26, 2002 under which CNPC agreed to lease to the Company another 404 buildings in connection with the operation and business of the Company, covering an aggregate of 442,730 square meters. Compared to the Buildings Leasing Contract, the increase in the units being leased in the Supplemental Buildings Agreement is mainly attributable to the expansion of the Company’s operations

mainly in the areas such as oil and natural gas exploration, the West-East Gas Pipeline Project and the construction of the northeast refineries and chemical operation base. The total rent payable under the Supplemental Buildings Agreement amounts to RMB157,439,540 per annum. The Company and CNPC will, based on any changes in their production and operations, and changes in the market price, adjust the sizes and quantities of buildings leased under the Buildings Leasing Contract as well as the Supplemental Buildings Agreement every three years. The Supplemental Buildings Agreement became effective on January 1, 2003 and will expire at the same time as the Buildings Leasing Contract. The terms and conditions of the Buildings Leasing Contract will, to the extent not contradictory to the Supplemental Buildings Agreement, continue to apply.

5. Intellectual Property Licensing Contracts

The Company and CNPC continue to implement the three intellectual property licensing contracts entered into on March 10, 2000, being the Trademark Licensing Contract, the Patent and Know-how Licensing Contract and the Computer Software Licensing Contract. Pursuant to these licensing contracts, CNPC has granted the Company the exclusive right to use certain trademarks, patents, know-how and computer software of CNPC at no cost. These intellectual property rights relate to the assets and businesses of CNPC which were transferred to the Company pursuant to the restructuring.

6. Contract for the Transfer of Rights under Production Sharing Contracts

The Company and CNPC continue to implement the Contract for the Transfer of Rights under Production Sharing Contracts dated March 10, 2000. As part of the restructuring, CNPC transferred to the Company relevant rights and obligations under 23 Production Sharing Contracts entered into with a number of international oil and natural gas companies, except for the rights and obligations relating to CNPC's supervisory functions.

7. Guarantee of Debts Contract

The Company and CNPC continue to implement the Guarantee of Debts Contract entered into on March 10, 2000, pursuant to which all of the debts of CNPC relating to the assets transferred to the Company in the restructuring were also transferred to, and assumed by, the Company.

In the Guarantee of Debts Contract, CNPC has agreed to guarantee certain of the debts of the Company at no cost. As at December 31, 2006, the total amount guaranteed was RMB597 million.

As each of the applicable percentage ratio(s) (other than the profits ratio) in respect of the Trademark Licensing Contract, the Patent and Know-how Licensing Contract, the Computer Software Licensing Contract, the Contract for the Transfer of Rights under Production Sharing Contracts and the Guarantee of Debts Contract is less than 0.1%, these transactions are exempted from the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules. The Directors believe that these transactions had been entered into in the normal and ordinary course of business for the benefits of the Company, and are in the interests of the shareholders as a whole.

II. New Continuing Connected Transactions with CNPC E&D

The following new continuing connected transactions arose as a result of the completion of the acquisition of the 67% equity interest in PKZ on December 28, 2006:

- the provision of production services by CNPC Group to the Group;
- the provision of construction and technical services such as exploration technology services by CNPC Group to the Group;
- the provision of material supply services by CNPC Group to the Group.

Upon completion of the acquisition of the 67% equity interest in PKZ on December 28, 2006, PKZ became a subsidiary (as defined under the Listing Rules) of CNPC E&D. As CNPC is the controlling shareholder of the Company and as each of CNPC and the Company is interested in 50% interest in CNPC E&D respectively, therefore, CNPC and CNPC E&D are connected persons of the Company under the Listing Rules. The caps for these continuing connected transactions have already been included in that for continuing connected transactions between the Group and CNPC.

III. Continuing Connected Transactions with CNPC (HK)

As part of the restructuring of CNPC and in preparation for the listing of the Company on HKSE, and as disclosed in the Company's prospectus dated March 27, 2000, CNPC and the Company entered into the Contract for the Transfer of Rights under Production Sharing Contracts whereby the relevant rights and obligations (other than the supervisory functions related to CNPC's role as representative of the PRC

DIRECTORS' REPORT

government) of CNPC under certain contracts, including the Blocks 9-1 to 9-5 of the Xinjiang Karamay Oilfield Petroleum Contract dated July 1, 1996, entered into between CNPC and Hafnium Limited ("**Xinjiang Contract**") and the Leng Jiapu Area Petroleum Contract dated December 30, 1997, entered into between CNPC and Beckbury International Limited ("**Liaohe Contract**"), were novated to the Company.

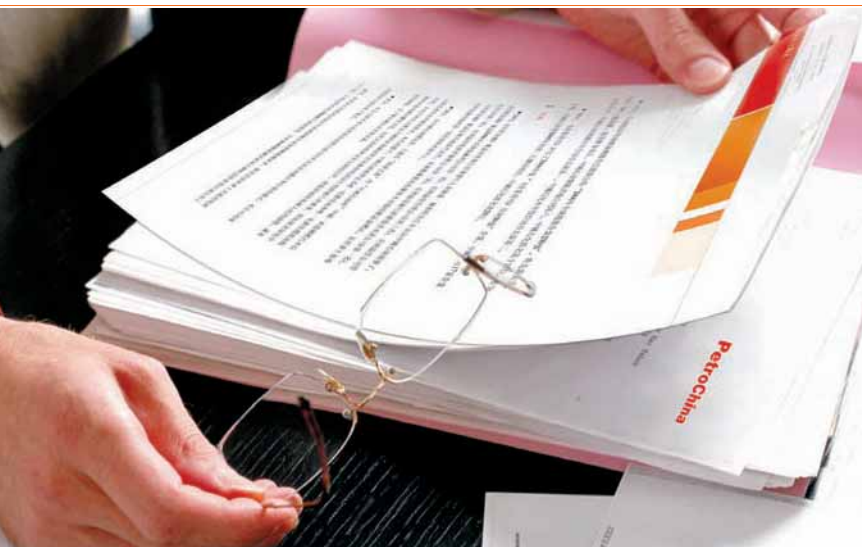
CNPC (HK) is a company listed on the HKSE and a 51.99% owned subsidiary of CNPC. CNPC is also the Company's controlling shareholder which holds approximately 88.21% of the issued share capital of the Company. Upon the effective novation by CNPC to the Company of the above interest in the PRC Oil Production Sharing Contracts (the Xinjiang Contract and the Liaohe Contract), certain transactions pursuant to the PRC Oil Production Sharing Contracts constitute continuing connected transactions between the Company and CNPC (HK).

Summary of the major terms and conditions of these continuing connected transactions under the Xinjiang Contract and the Liaohe Contract are as follows:

(1) Production and development cost sharing between the Company and CNPC (HK): The Company and CNPC (HK) shall share the oil and natural gas produced from blocks 9-1 to 9-5 of the Karamay Oilfield, as to 46% by the Company and 54% by CNPC (HK), and from the Leng Jiapu Oilfield, as to 30% by the Company and 70% by CNPC (HK). CNPC (HK) shall be responsible for 100% of the development costs in respect of blocks 9-1 to 9-5 of the Karamay Oilfield. The Company is responsible for 30% and CNPC (HK) is responsible for 70% of the development costs in respect of the Leng Jiapu Oilfield.

(2) Provision of assistance by the Company to CNPC (HK): The Company shall provide assistance to CNPC (HK), including: (i) leasing warehouses, terminal facilities, barges, pipeline and land, etc.; (ii) obtaining approvals necessary for the conduct of the petroleum operations; and (iii) obtaining office space, office supplies, transportation and communication facilities. For such assistance, CNPC (HK) will pay an annual assistance fee of US\$50,000 for each of blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield. The amount of such fee was determined after negotiations, and has taken into account the actual circumstances and conditions, including the scope of the projects and the level of demand for such assistance. This fee shall be accounted for as operating costs and shared by the Company and CNPC (HK) in accordance with the procedures described in the Xinjiang Contract and the Liaohe Contract.

(3) Payment of training fees: In the course of development and operations of each oilfield, CNPC (HK) shall pay the Company an amount of US\$50,000 annually for the training of personnel carried out by



the Company for each of blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield. The amount of such fee was determined after negotiations, and has taken into account the actual circumstances and conditions, including the scope of the projects and the level of demand for training.

(4) Sale of crude oil by CNPC (HK) to the Company: CNPC (HK) has the right to deliver its share of oil production from each of blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield to a destination of its choice, except for destinations which infringe on the political interests of the PRC. However, given the transportation costs and the prevailing oil prices, the only likely purchaser of the oil production attributable to CNPC (HK) from each of blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield is CNPC or its affiliates, including the Company, which will accept delivery of oil produced in blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield at the market price. Since the signing of the PRC Oil Production Sharing Contracts, CNPC (HK) has sold all of its share of the oil production to CNPC or its affiliates, including the Company. As far as the Board of Directors is aware, CNPC (HK) intends to continue with this arrangement. There is no contractual obligation upon the Company to purchase oil produced from blocks 9-1 to 9-5 of the Karamay Oilfield and the Leng Jiapu Oilfield, although, from a commercial perspective, the Company intends to continue to accept part of the deliveries. The price of various grades of crude oil sold shall be set either with reference to the price approved by the relevant PRC authorities, or as determined with reference to the prevailing fair market price for transactions of crude oil of a similar quality in the major oil markets. This will be adjusted to take into account the terms of transportation, payment and other terms.

The waiver in respect of the above continuing connected transactions between the Company and CNPC (HK) granted by the HKSE expired on December 31, 2006. As each of the applicable percentage ratio(s) (other than the profits ratio) in respect of the above continuing connected transactions between the Company and CNPC (HK) is more than 0.1% but less than 2.5%, these transactions are exempted from the independent shareholders' approval requirements and are only subject to the reporting and announcement requirements under Rule 14A.34 of the Listing Rules. An announcement was made by the Company on August 23, 2006 in respect of the reporting and announcement obligations for these continuing connected transaction for the period from January 1, 2007 to December 31, 2008.

IV. Continuing Connected Transactions with CRMSC and Beijing Gas

The Group has entered into continuing connected transactions with Beijing Gas and CRMSC pursuant to the following agreements. For the transactions with Beijing Gas, the Group has complied with the procedures for reporting and announcements obligations to the HKSE. The transactions with CRMSC and the caps for these transactions have been approved by HKSE and the same were first approved by shareholders at the extraordinary general meeting held on November 8, 2005 and subsequently approved by shareholders at the extraordinary general meeting held on November 1, 2006 with the revised caps.

(a) Beijing Gas Products and Services Agreement

The Company entered into a Products and Services Agreement with Beijing Gas on September 1, 2005. Pursuant to the agreement, the Group shall continuously provide products and services to Beijing Gas, including the provision of natural gas and natural gas related transmission services. The agreement was effective from January 1, 2006.

(b) CRMSC Products and Services Agreement

On September 1, 2006, the Company entered into the CRMSC Products and Services Agreement with CRMSC. Under the CRMSC Products and Services Agreement, products and services to be continuously provided by the Company to CRMSC include, among other things, refined products (such as gasoline, diesel and other petroleum products). The term of the CRMSC Products and Services Agreement is 3 years commencing from January 1, 2006.

During the term of the CRMSC Products and Services Agreement, the product and service implementation agreements may be terminated from time to time by the contracting parties providing at least 6 months' written notice of termination in relation to any one or more categories of products or services. Further, in respect of any products or services already contracted to be provided, termination may not take place until after such products and services have been provided.

Caps for the Continuing Connected Transactions

The following caps in respect of the continuing connected transactions are set based on the annual volumes of the relevant transactions for the period from January 1, 2006 to December 31, 2008:

(A) In relation to the products and services contemplated under (a) the Comprehensive Agreement as amended by the First Supplemental Comprehensive Agreement and the Second Supplemental Comprehensive Agreement and also include the new continuing connected transactions arising as a result of the acquisition of interest in PKZ, (b) Buildings Leasing Contract and Supplemental Buildings Agreement, and (c) the CRMSC Products and Services Agreement, the total annual revenue or expenditure in respect of each category of products and services will not exceed the proposed maximum annual aggregate values set out in the following table:

Category of Products and Services	Proposed annual caps		
	2006	2007	2008
	RMB(in millions)		
(i) Products and services to be provided by the Group to the CNPC Group (Note 1)	36,670	44,970	50,129
(ii) Products and services to be provided by CNPC to the Group			
(a) Construction and technical services (Note 1)	114,681	115,039	105,661
(b) Production services (Note 1)	63,983	96,437	98,518
(c) Supply of materials services (Note 1)	5,356	5,459	5,574
(d) Social and ancillary services (Note 3)	5,000	5,000	5,000
(e) Financial Services			
-Aggregate of the average daily outstanding principal of loans; the total amount of interest paid in respect of these loans; and other relevant charges (Note 3)	43,312	50,132	56,547
-Aggregate of the average daily amount of deposits; and the total amount of interest received in respect of these deposits (Note 3)	9,081	9,102	9,126
(iii) Financial services to be provided by the Group to the Jointly-owned Companies (Note 3)	21,235	32,840	44,465
(iv) Fee for land leases paid by the Group to CNPC (Note 3)	2,260	2,260	2,260
(v) Rental for buildings paid by the Group to CNPC (Note 3)	140	140	140
(vi) Provision of goods by the Group to CNPC (HK) (Note 4)	1.6	1.6	1.6
(vii) Provision of goods by CNPC (HK) to the Group (Note 4)	23,092	4,370	4,241
(viii) Products and services provided by the Group to CRMSC (Note 2)	11,048	12,025	13,152
(ix) Products and services provided by the Group to Beijing Gas (Note 5)	4,939	5,983	7,097

Notes:

1. The Company sought independent shareholders' approval at the general meeting held on November 8, 2005 for the renewal of the existing continuing connected transactions and the proposed the new annual caps from January 1, 2006 to December 31, 2008. The Company further sought independent shareholders' approval at the general meeting held on November 1, 2006 for a revision of these annual caps which were previously approved by shareholders at the general meeting held on November 8, 2005.

DIRECTORS' REPORT

2. The Company sought shareholders' approval at the general meeting held on November 8, 2005 for the renewal of the existing continuing connected transactions and the proposed the new annual caps from January 1, 2006 to December 31, 2008. The Company further sought shareholders' approval at the general meeting held on November 1, 2006 for a revision of these annual caps which were previously approved by shareholders at the general meeting held on November 8, 2005.
3. The Company sought shareholders' approval at the general meeting held on November 8, 2005 for the renewal of the existing continuing connected transactions and the proposed the new annual caps from January 1, 2006 to December 31, 2008.
4. The Board of Directors approved the annual caps for these continuing connected transactions from January 1, 2007 to December 31, 2008 at the board meeting held on August 23, 2006. Details of such transactions were announced on the same day.
5. The annual caps of this continuing connected transaction are only subject to announcement requirement. Details of such transaction were announced on September 1, 2005.

(B) In relation to the Trademark Licensing Contract, the Patent and Know-how Licensing Contract and the Computer Software Licensing Contract, CNPC has granted the Company the right to use certain trademarks, patents, know-how and computer software of CNPC at no cost.

Independent non-executive Directors confirmation

In relation to the connected transactions undertaken by the Group in 2006, the independent non-executive Directors of the Company confirm that:

- (i) the connected transactions mentioned above have been entered into in the ordinary and usual course of business of the Company;
- (ii) the connected transactions mentioned above have been entered into on terms that are fair and reasonable to the shareholders of the Company;
- (iii) the connected transactions mentioned above have been entered into on normal commercial terms either (1) in accordance with the terms of the agreements governing such transactions, or (2) (where there is no such agreement) on terms no less favourable than terms available to independent third parties; and
- (iv) where applicable, the connected transactions have been entered into within the annual caps for the years mentioned above.

Auditor's confirmation

The auditors of the Company have reviewed the connected transactions mentioned above and have provided the Board of Directors with a letter stating that:

- (i) all the connected transactions have received the approval of the Board of Directors;
- (ii) all the connected transactions have been conducted in accordance with the terms of the agreements governing such transactions; and
- (iii) where applicable, the connected transactions have been entered into within the annual caps for the years mentioned above.

| Accounting Principle

For the year 2006, the Company adopted certain new accounting principles and they are contained in Note 2 to the Company's financial report prepared in accordance with the IFRS.

| Auditors

PricewaterhouseCoopers (Certified Public Accountants, Hong Kong) and PricewaterhouseCoopers Zhong Tian CPAs Limited Company (certified public accountants in the PRC) were the Company's international and domestic auditors respectively in 2006. The Company has retained the above two firms of accountants since the date of its listing. A resolution to continue the appointment of the international and domestic auditors for 2006 will be proposed at the annual general meeting of the Company which will be held on May 16, 2007.

By Order of the Board
Chen Geng
Chairman
Beijing, the PRC
March 19, 2007