BUSINESS ENVIRONMENT

In 2006, the PRC government began to implement the "Eleventh Five-Year Plan" along with the principle of "Developing in a scientific way" for the overall economic and social development; austerity measures will continue to be implemented, and the focus will be on structural changes in the economy and the momentum of economic growth; GDP for the year grew by 10.7%, an increase of 0.3 percentage points over the previous year; the year-on-year nationwide increase in fixed assets investment was 24.5%, which was 2 percentage points over the previous year. ***(Note: The above figures are quoted from the Statistics Publication of the National Economy and Social Development of the People's Republic of China for 2006)***

In 2006, a series of guiding documents such as the "Development Policy for the Cement Industry", "Special Planning for the Development of the Cement Industry" and "Opinions Relating to Speeding Up of the Structural Adjustments of the Cement Industry" were published by the government aiming at facilitating the development and structural adjustments of the cement industry, which have also confirmed that the 12 large cement companies across the country, headed by Anhui Conch, are to receive the key support of the government in respect of the structural adjustments, whereby these companies will receive preferential treatment regarding project approvals, land approvals and granting of credit facilities, thereby encouraging the acquisitions, reorganization and merger of these companies with a view to raise the concentration of production capacities and optimizing the deployment of resources. Over the past year, investment in fixed assets in the cement industry fell from the previous year, and proportion of production using the new dry process was increasing. In 2006, the production capacity using the new dry process amounted to approximately 80 million tonnes; as at the end of 2006, the production capacity using the new dry process was approximately 700 million tonnes, the proportion to the total production rose from approximately 45% to approximately 50%.

In 2006, the output of cement of the PRC amounted to 1,204 million tonnes, an increase of 19.07% over 2005; the volume of cement exported amounted to 19.41 million tonnes, an increase of 70.65% over 2005; the volume of clinker exported amounted to 16.72 million tonnes, an increase of 55.06% over 2005. The supply and demand relationship of the cement industry in the PRC saw further improvement and the industry was recovering fast with increase in output, and the price of cement was rising throughout the year from a low level and hit a record high. ***(Note: These figures are quoted from the second issue of "China Cement" for 2007)***

ANALYSIS OF OPERATION

Highlights of operation

In 2006, the Group seized the opportunity afforded by the continued growth of the cement industry and the steady increase in demand of cement to maximize our aggregate effectiveness, whereby we aimed at turning into an "energy saving and environmentally friendly" enterprise in order to push forward the sustainable development of the Company. In 2006, all of our economic technology indicators were above those of other players in the industry, and the costs of our production, operation and management were declining; production lines for cement and clinker and the residual heat electricity power generation project had been completed as scheduled; our output and sales volume, operating income and profit were picking up steadily.

Railway transport of bulk cement

During the Reporting Period, sales from principal activities of our Group under PRC Accounting Standards amounted to RMB15.246 billion, net profit after minority interests amounted to RMB1.428 billion and earnings per share amounted to RMB1.14. Revenue under IFRS amounted to RMB15.246 billion, net profit after tax and minority interests amounted to RMB1.483 billion and earnings per share amounted to RMB1.18.

Highlights of production

During the Reporting Period, the Group produced a total of 60.36 million tonnes of clinker, representing a year-on-year increase of 32%; 56.93 million tonnes of cement, representing a year-on-year increase of 40%.

Mining

The Group's output has been rising steadily over the years, which is mainly due to the following: the Group has established a scientific and sound production and management system and a team of professional, technical and management capabilities who, by strengthening our production and management, give full play to our existing production capacity. Also, our construction-in-progress had been making good progress and put into operation phase by phase as scheduled, which attained their respective targets quickly. During the year, the five production lines of daily production capacity of 5,000 tonnes of clinker including Prosperity Conch Cement Company Limited ("Prosperity Conch"), Wuhu Conch, and construction of the 12 cement mills of Anhui Changfeng Conch Cement Company Limited ("Changfeng Conch") and Jiangsu Baling Conch Cement Company Limited ("Baling Conch"), etc have been completed and put into operation, which also attained their targets quickly, in particular the growth in production volume of the South China regions, which output had increased by about 200% over the previous year.

As at 31 December 2006, our production capacity for clinker amounted to 59 million tonnes, and our production capacity for cement amounted to 65 million tonnes; moreover, the 3 residual heat power generation units at Ningguo Cement Plant, Jiande Conch Cement Company Limited ("Jiande Conch") and Chizhou Conch had been completed and put into operation, which afford a total installed capacity with residual heat of 43,000 kw.

An overview of sales

During the Reporting Period, the sales volume of the Group's cement and clinker amounted to 75.51 million tonnes, a year-on-year increase of 33%; of which the export volume of cement and clinker amounted to 13.96 million, representing an increase of 66% over the previous year.

US-standard clinker loaded on vessel for export

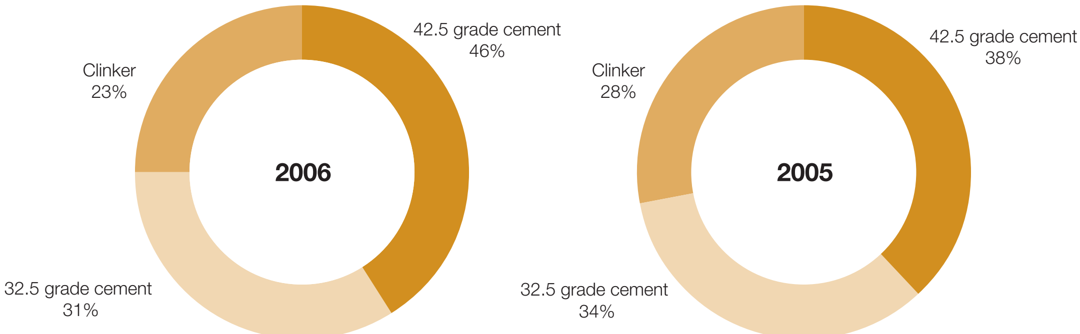
During the Reporting Period, the Group's strategy to develop the South China market yielded excellent results which, together with our "T" shape strategy for East China, has formed a large market network and a network of logistics and ensured supply. The Group seized the opportunities on the growth in fixed assets investment and the marketing opportunity of urbanization of the rural areas to continue to put more effort in major projects and development of markets in the rural areas, thereby raising our market share steadily as well as our control of the market; also, riding on the momentum in export from the previous year, we took the initiative to explore the international market, so that our export volume markedly increased, which became a vital force in heightening our sales volume and effectiveness.


Trucks carrying cement

During the Reporting Period, the selling prices of products of the Group were rising steadily; the full-year overall average price was RMB201.9/tonne, representing an increase of 6.2% over the previous year.

During the Reporting Period, the proportion of sales volume of 32.5 grade cement was basically stable, and the year-on-year increase of the proportion of the sales amount of 42.5 grade cement was 8 percentage points, which was mainly due to the implementation of the "Eleventh Five-Year Plan" in 2006, being the first year such that demand for higher grade cement for infrastructure projects was strong, and both the price and the proportion of sales amount of 42.5 grade cement had increased over the previous year; the proportion of sales amount of clinker had a year-on-year decrease of 5 percentage points, which was mainly due to the increase in the demand for clinker to meet the additional production capacity of cement of the Group during the Reporting Period.

Percentage of sales by type



During the Reporting Period, the proportion of sales amount of the Group in the South China regions had a year-on-year increase of 10 percentage points, which was mainly due to the fact that the 4 production lines of clinker and the 6 cement mills of Prosperity Conch in the South China region were put into operation in 2006; also, companies in the south such as Xingye Kuiyang Conch Cement Company Limited, Fusui Xinning Conch Cement Company Limited and Jiangmen Conch Cement Company Limited commenced operation in the second half of 2005, and the production capacity of which were fully utilized in 2006; the international demand was robust, and the proportion of export value continued to increase, which accounted for approximately 22% of our sales amount. Growth in export had effectively improved the domestic supply and demand and helped a long way to balance our low season productivity and stabilize the price for domestic trade. The proportion of sales amount of the Group in the East China regions had a year-on-year decrease of 15 percentage points, which was mainly due to the fact that the growth areas of our sales amount in 2006 were concentrated in the South China regions and in export, whereas the speed of growth in production capacity in the East China regions was less prominent.

Regional sales amount (RMB million)

	2006		2005		
Region	**Sales**	**percentage (%)**	Sales	percentage (%)	**Increase/decrease**
East China	**9,264**	**61**	8,223	76	Decreased by 15 percentage points
South China	**2,670**	**17**	757	7	Increased by 10 percentage points
Export	**3,312**	**22**	1,846	17	Increased by 5 percentage points
Total	**15,246**	**100**	10,826	100	Increased by 41 percentage points

Profit

In 2006, the Group's sales from principal activities under the PRC Accounting Standards amounted to RMB15,246.28 million, representing an increase of 41% over the previous year; net profit after tax and minority interests amounted to RMB1,427.93 million, representing an increase of 251% over the previous year. Revenue under IFRS amounted to RMB15,246.28 million, representing an increase of 41% over the previous year; our profit after tax and minority interests amounted to RMB1,482.79 million, representing an increase of 284% over the previous year. Our profit enjoyed a substantial increase over the previous year, was mainly due to the increase in sales volume and price and the decrease in production costs.

Major items in the income statement prepared in accordance with the PRC Accounting Standards

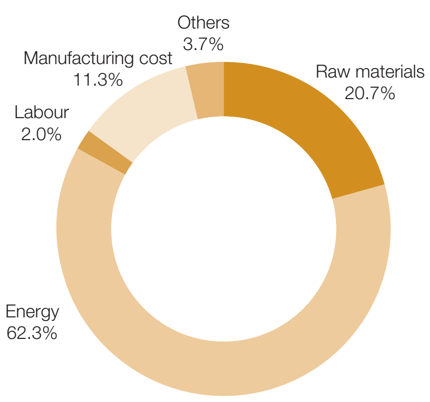
Item	2006 (RMB'000)	2005 (RMB'000)	Increase (+) Decrease (–) (%)
Sales from principal activities	**15,246,277**	10,826,214	40.83
Profit from principal activities	**4,406,920**	2,446,126	80.16
Profit before income tax	**2,498,309**	861,374	190.04
Net profit after tax and minority interests	**1,427,931**	406,892	250.94
Net cash flow from operating activities	**2,926,949**	1,523,523	92.12

Major items in the income statement prepared in accordance with IFRS

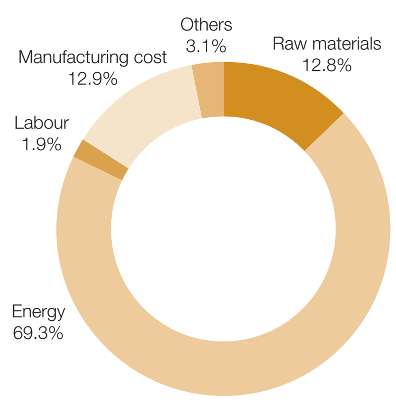
Item	2006 (RMB'000)	2005 (RMB'000)	Increase (+) (%)
Revenue	**15,246,277**	10,826,214	40.83
Gross profit	**4,415,158**	2,410,546	83.16
Profit before taxation	**2,521,383**	871,009	189.48
Profit after taxation and minority interests	**1,482,795**	385,832	284.31

During the Reporting Period, energy expenses accounted for 62.3% of the total costs, representing a decrease of 7 percentage points over the previous year. It was mainly due to the fact that our production capacity had been fully utilized, the unit energy consumption decreased and the slight decrease in the price of coal.

Cost breakdown for 2006



Cost breakdown for 2005



During the Reporting Period, given the rise in selling price of our products and the full utilization of production capacity as well as the decrease in costs, both the Group's revenue and gross profit margin increased by a huge margin. In this regard, the year-on-year increase of revenue for cement was 50.77%, and gross profit margin increased by 6.31 percentage points; the year-on-year increase of revenue for clinker was 15.41%, and gross profit margin increased by 6.54 percentage points.

2006 gross profit by products and comparison

Product type	Sales from principal operations	Cost of principal operations	Gross profit margin	Changes in income from principal operations over last year	Changes in cost from principal operations over last year	Change of percentage points in gross profit margin over last year
	(RMB million)	(RMB million)	(%)	(%)	(%)	
Cement	11,733	8,294	29.31	50.77	38.42	6.31
Clinker	3,513	2,450	30.26	15.41	5.51	6.54
Total	**15,246**	**10,744**	**29.53**	**40.83**	**29.23**	**6.33**

During the Reporting Period, the three major expenses decreased slightly over last year as cost control had been better implemented. Increase in the total operating expenses was mainly due to the significant increase in export volume and increase in the sales of bagged cement.

Changes in major expenses items prepared in accordance with the PRC Accounting Standards

			Percentage to sales from principal activities	
Expenses for the period	**2006**	2005	**2006**	2005
	(RMB'000)	(RMB'000)	**(%)**	(%)
Selling expenses	**1,148,673**	832,756	**7.53**	7.69
Administrative expenses	**498,708**	354,671	**3.27**	3.28
Net financial expenses	**529,251**	445,260	**3.47**	4.11

ANALYSIS OF FINANCIAL POSITION

Assets and Liabilities Structure

Changes in assets and liabilities prepared in accordance with the PRC Accounting Standards

Item	2006 (RMB'000)	2005 (RMB'000)	Increase/ (decrease) (RMB'000)	Changes (%)
Fixed assets	**17,650,876**	15,091,128	2,559,748	16.96
Current and other assets	**4,654,649**	4,150,898	503,751	12.14
Total assets	**22,305,525**	19,242,026	3,063,499	15.92
Current liabilities	**6,559,531**	7,397,025	-837,494	-11.32
Non-current liabilities	**7,206,485**	4,990,774	2,215,711	44.40
Minority interests	**1,487,803**	1,142,793	345,010	30.19
Shareholders equity	**7,051,706**	5,711,434	1,340,272	23.47
Total liabilities and Shareholders' equity	**22,305,525**	19,242,026	3,063,499	15.92

During the Reporting Period, with the further optimization of the loan structure of the Group, the gradual completion of projects and rise in profit, improvements on our financial position was shown.

As at 31 December 2006, the Group's total assets prepared in accordance with the PRC Accounting Standards amounted to RMB22.306 billion; the Group's net assets amounted to RMB7.052 billion; the Group's total liabilities amounted to RMB13.766 billion, an increase of RMB1.378 billion over the end of last year.

As at 31 December 2006, the Group's non-current liabilities increased by RMB2.216 billion over the end of last year. It was mainly due to the increase in long-term borrowings.

As at 31 December 2006, the Group's total current assets amounted to RMB3,830.31 million, and the Group's total current liabilities amounted to RMB6,559.53 million, and the current ratio arrived at by dividing current assets by current liabilities was 0.58:1.

As at 31 December 2006, the Group's gearing ratio was 61.72%, representing a decrease of 2.66 percentage points over last year, and the net debt ratio calculated in accordance with the IFRS was 1.14, representing a slight decrease over last year.

During the Reporting Period, the Group was committed to improve its loan structure and enhance its current ratio as well as to strictly control its financial risks. Since the Group aimed at meeting the requirements for our normal operations and the needs of capital expenditure by reasonable financing, the interest coverage ratio rose significantly higher than that of last year to 5.62.

Liquidity and funding

Maturity analysis of the Group's bank loans and other borrowings as at 31 December 2006:

	As at 31 December 2006 (RMB'000)	As at 31 December 2005 (RMB'000)
Due within 1 year	**3,457,380**	4,706,360
Due after 1 year but within 2 years	**2,408,939**	2,185,380
Due after 2 years but within 5 years	**3,779,800**	1,959,800
Due after 5 years	**980,000**	730,000
Total	**10,626,119**	9,581,540

During the Reporting Period, percentage of the Group's long-term loans increased from 51% in 2005 to 68% in 2006.

Comparison of net cash flow prepared in accordance with the PRC Accounting Standards

	2006 (RMB'000)	2005 (RMB'000)
Net cash flows from operating activities	**2,926,949**	1,523,523
Net cash flows from investment activities	**(3,333,368)**	(3,284,168)
Net cash flows from financing activities	**365,639**	1,312,206
Decrease in cash and cash equivalents	**(40,780)**	(448,439)
Cash and cash equivalents at the beginning of the year	**1,178,390**	1,626,829
Cash and cash equivalents at the end of the year	**1,137,610**	1,178,390

In 2006, the cement market saw rises in its steady development, and the Group seized the opportunity and fully utilized our production capacity to expand the scale of our sales. The marked increase in sales volume and rise in prices resulted in the significant increase in cash inflow from operations, and the modest decrease in the purchasing cost of raw materials resulted in a more efficient control of our cash expenses for operations; as a result of the aforesaid factors, the Group's net cash inflow from operations increased significantly. During the Reporting Period, the Group's net cash inflow from operations amounted to RMB2,926.95 million, representing an increase by RMB1,403.43 million. Net cash and cash equivalents decreased by RMB40.78 million. It was mainly due to the relatively large amount of capital committed in project construction.

Capital Expenditure

During the Reporting Period, the aggregate amount of investment activities and capital expenditure of the Group amounted to RMB3,333 million, which was used in the construction of cement and clinker production lines and the residual heat power generation project. During the Reporting Period, our new loans amounted to RMB1,044 million, which was mainly used in the construction of projects.

As at 31 December 2006, the Group's investment in associates amounted to RMB163.22 million.

As at 31 December 2006, capital commitment in respect of the acquisition of machinery and equipment for suppliers that were committed but have not been provided for in the financial statements were as follows:

	As at 31 December 2006 (RMB'000)	As at 31 December 2005 (RMB'000)
Contracted for	**2,210,776**	1,466,180
Authorized but not contracted for	**2,262,920**	1,129,017
Total	**4,473,696**	2,595,197

EFFECTS OF THE NEW ACCOUNTING STANDARDS

As from 1 January 2007, the Company implemented the New Accounting Standards for Enterprises ("New Accounting Standards") issued by the Ministry of Finance in 2006. Having implemented the New Accounting Standards, the effects on our accounting policy, accounting estimated changes and their effects to our operating results and financial position are as follows:

In relation to the differences in shareholders' equity calculated in accordance with the existing accounting standards and the New Accounting Standards upon the initial implementation of the New Accounting Standards on 1 January 2007:

1. **Difference in long-term investment**
   According to the New Accounting Standards, as at 1 January 2007, for long-term investment in equity arising from the combination of businesses under common control, difference in investment in equity not yet amortized was to be fully written off with retained profit adjusted, which led to a reduction of minority interests of RMB3.482 million.

2. **Income tax**
   According to the requirements of the New Accounting Standards, the Company re-designed its accounting policy and changed the accounting treatment of income tax from the payable tax approach to taxation effect approach. On 1 January 2007, provision for deferred income tax assets was made for the temporary difference arising from the difference between the bad debt provision for receivables, provision for impairment of inventory and internal unrealized gross profit and the basis of calculation, resulting in an increase in shareholders' equity of RMB45.03 million.

3. **Minority interests**
   In accordance with the requirements of the New Accounting Standards, as at 1 January 2007, the minority interests of RMB1,487.80 million as at 31 December 2006 in the combined financial statement prepared in accordance with the existing accounting standards were stated as shareholders' equity.

Possible effects on our accounting policy, accounting estimated changes and the operating results and financial position of our Company upon the implementation of the New Accounting Standards are as follows:

1) In accordance with the requirements No. 2 of the New Accounting Standards on long-term investment in equity in subsidiaries by the parent company shall be dealt with by the cost approach, as such, the Company has changed the existing accounting policy of using the equity approach for subsidiaries to cost approach, which will affect the current investment gains of the parent company but not the consolidated financial statements.

2) In accordance with the requirements No. 18 of the New Accounting Standards on income tax, the Company shall recognize the temporary difference between the book value of its assets or liabilities and the basis for taxation assessment as deferred income tax assets or deferred income tax liabilities, the change of which will affect the current taxation of the Company, which in turn will affect the Company's net profit and consolidated shareholders' equity.

3) In accordance with the requirements No. 20 of the New Accounting Standards on the combination of businesses, the difference on the debit side of investment in equity arising from the combination of businesses not under common control shall be recognized as goodwill without amortization, but impairment test shall be conducted every year. The matter does not affect the consolidated balance sheet at the initial implementation, but will affect the net profit and consolidated shareholders' equity of the Company in subsequent years.

4) In accordance with the requirements No. 33 of the New Accounting Standards on consolidated financial statements, in the consolidated balance sheet, minority interests shall no longer be individually stated, instead, minority interests are treated as part of the equity holders and are stated under the item of equity holders as "minority interests"; in the consolidated profit statement, minority interests shall no longer be stated in the debit side of net profit, and are assigned to the respective profit and loss of the parent company and minority interests under net profit. The matter will increase the net profit and shareholders' equity of the Company.

5) In accordance with the requirements of the practice guidelines of the New Accounting Standards, the preliminary fees of the Company are charged directly to the current administrative expenses as incurred and will not be deferred for one-off calculation until the commencement of operations of the company. Balance of the preliminary fees as at 31 December 2006 shall be entirely recognized as administrative expenses in the first accounting period after the first implementation date. The matter will affect the net profit and shareholders' equity of the Company.

OUTLOOK FOR 2007

In 2007, the economy of the PRC is expected to continue to sustain robust growth, and the PRC will continue to pursue a prudent and sound financial and currency policy, which will in turn facilitate the further economic structural adjustment and changes in the manner of economic growth. Investment in fixed assets is expected to go back to a rational manner, however, the total investment and scale of investment will continue to be massive, especially with the confirmation of the policy for the central regions of the PRC, the construction of the new socialist rural areas and the acceleration of construction of inter-city railways in East and South China regions will be implemented, which is likely to become the momentum for the demand for cement.

In order to put into practice the binding indicators as proposed by the "Eleventh Five-Year Plan (Outlines)" of the State on energy consumption and the total emission volume of pollutants, in February 2007, the National Development and Reform Commission of the PRC issued the Notice on Efforts to Phase Out Obsolete Cement Production Capacity, whereby schedules for phasing out obsolete cement production capacity from 2007 to 2010 for both the whole nation and the provinces were handed down, and governments at different levels shall within 2007 sign the performance pledge for phasing out obsolete cement production capacity during the "Eleventh Five-Year Plan" period, which will facilitate the further structural adjustments of the cement industry to lead to a more balanced supply and demand relationship in the cement market, and will afford a favourable opportunity for the Group to proceed with another round of development.

In 2007, the Group will speed up the implementation of the development and planning strategy under the "Eleventh Five-Year Plan", whereby the Group will fully leverage on our advantage in scale, technology, management and resources to expedite the construction of new projects and expansion of existing projects; at the same time, the Group does not rule out the means of acquisitions and mergers in order to expand production scale and to increase our share of the market. Moreover, the Group will continue to increase its investment scale in the residual heat power generation project so as to increase our profitability.

Production capacity of the Group's clinker and cement is expected to grow continuously in 2007. In 2007, the Group will have seven production lines of 5,000 tonnes/day for clinker at Wuhu Conch, etc, and 20 cement mills at Ninghai Qiangjiao Conch Cement Company Limited ("Qiangjiao Conch"), etc, which, upon completion and put into operation, the Group plans to have newly added production capacity for clinker of 11.55 million tonnes, and 15 million tonnes for cement. At present, the Group has completed the production base for clinker of 10 million tonnes at Tongling Conch, and planning for two production bases, namely Chizhou Conch and Wuhu Conch has been completed and construction is underway.

Moreover, the Group is constructing 26 residual heat power generation units at Baimashan Cement Plant, Wuhu Conch and Xuancheng Conch Cement Company Limited ("Xuancheng Conch"), which will add 128,000 kw to the Group's power generation capacity in 2007, which will further reduce the operation cost and upgrade the operation quality.

In 2007, the Group plans to arrange for a capital expenditure of approximately RMB5.37 billion. The aforesaid capital will mainly come from internal resources of the Group and bank loans. At present, the average interest rate of the bank loans of the Group is about 5.4%.

The management is also aware that the rise in the prices of energy and resources will continue to exert pressure on the Company's operating costs. The RMB appreciation and lower export tax rebate rate will also affect export of the Company's products to a certain extent. In response, the management will strengthen the management of integrated resources utilisation by intensifying technological upgrade and investment in its energy saving facilities, in order to minimise its energy consumption, increase resources utilisation, with the aim of enhancing the Company's overall operation quality and creating excellent value for shareholders.

Office of Chizhou Conch