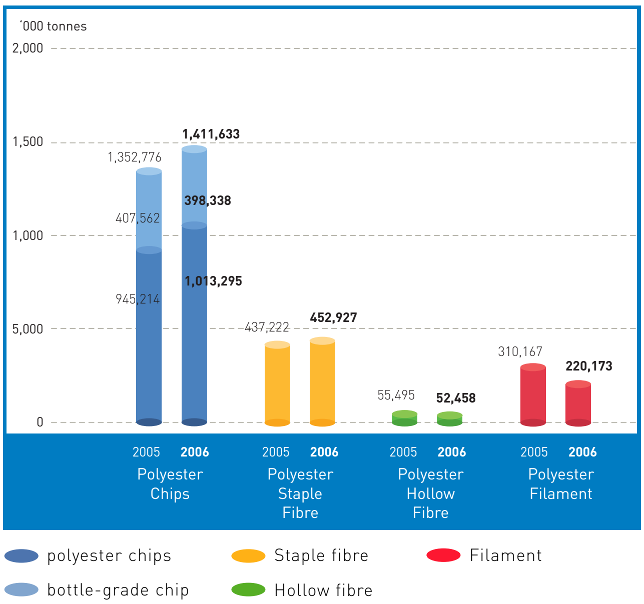
The information set out below does not constitute part of the financial statements audited by KPMG or KPMG Huazhen, as set out on pages 56 to 100 and pages 101 to 148, respectively, of this Annual Report, and is included for information purpose. This discussion and analysis should be read in conjunction with the information contained in the Consolidated Financial Statements and Notes thereto (the "Financial Statements") presented in this Annual Report. Financial figures, except for specifically noted, contained herein have been extracted from the financial statements prepared in accordance with the IFRSs.

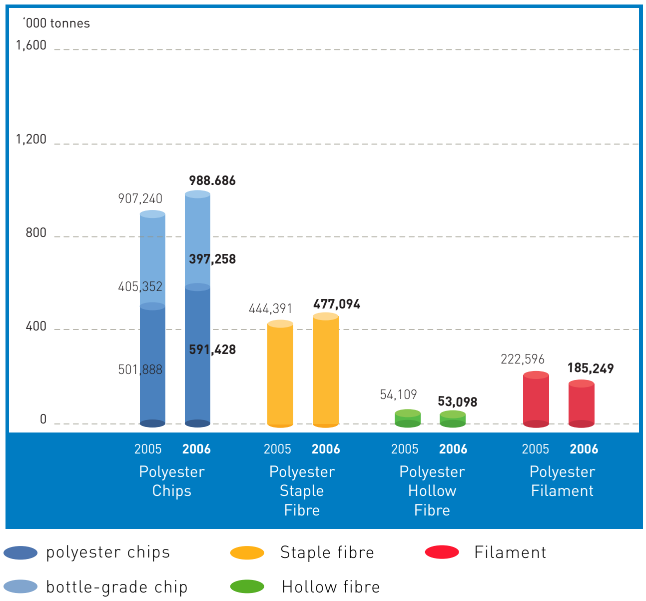
1. RESULTS OF OPERATIONS

In 2006, under the severe market condition, the Group put great efforts in extending reform adjustments, strengthening internal management, optimizing production and operations, further reducing costs and expenses, and optimizing products structure. As a result, the Group achieved positive development in various fields.

Production Volume



Sales Volume



(1) Turnover

In 2006, the Group's total production volume of polyester products was 2,137,191 tonnes, representing a decrease of 0.9 per cent as compared with that of 2,155,660 tonnes for last year. The decrease was mainly due to the establishment of the joint venture Yihua UNIFI in August 2005 and the completion of equity transfer of Tianma Chemical Fibre in 2006. Actually, the Company's production volume of polyester products increased as compared with that of 2005. The average capacity utilization rate reached 93.7 per cent. The total production volume of PTA amounted to 1,003,858 tonnes, an increase of 3.4 per cent as compared with that of 970,507 tonnes for last year. The production volume of PTA created the historical best level.

Production volume

	For the year ended 31 December			
	2006		2005	
	Production volume (tonnes)	**Per cent of total production volume (%)**	Production volume (tonnes)	Per cent of total production volume (%)
Polyester products				
Polyester chips	**1,411,633**	**66.0**	1,352,776	62.7
Of which: bottle-grade polyester chips	**398,338**	**18.6**	407,562	18.9
Staple fibre	**452,927**	**21.2**	437,222	20.3
Hollow fibre	**52,458**	**2.5**	55,495	2.6
Filament	**220,173**	**10.3**	310,167	14.4
Total	**2,137,191**	**100.0**	2,155,660	100.0

In 2006, the Group's total sales volume of the polyester products amounted to 1,704,127 tonnes, representing an increase of 4.7 per cent from 1,628,336 tonnes of 2005. The ratio of sales to production reached 100.1 per cent. Export sales of the polyester products amounted to 120,330 tonnes, representing an increase of 46.5 per cent as compared with the 82,142 tonnes for 2005. Due to the drive from the cost of polyester raw materials, the prices of polyester products increased. The weighted average prices (excluding VAT) of the Group's polyester products increased from Rmb 9,544/tonne to Rmb 9,706/tonne during the year, representing a 1.7 per cent increase. But the increase in prices of polyester products was obviously less than that of polyester raw material. As a result, the profit margin of polyester products was significantly compressed.

Sales volume

	For the year ended 31 December			
	2006		2005	
	Sales volume (tonnes)	**Per cent of total sales volume (%)**	Sales volume (tonnes)	Per cent of total sales volume (%)
Polyester products				
Polyester chips	**988,686**	**58.0**	907,240	55.7
Of which: bottle-grade polyester chips	**397,258**	**23.3**	405,352	24.9
Staple fibre	**477,094**	**28.0**	444,391	27.3
Hollow fibre	**53,098**	**3.1**	54,109	3.3
Filament	**185,249**	**10.9**	222,596	13.7
Total	**1,704,127**	**100.0**	1,628,336	100.0

Average Prices for products (excluding VAT) (Rmb/tonnes)

	For the year ended 31 December		
	2006	2005	Change (%)
Polyester products			
Polyester chips	**9,325**	9,067	2.8
Staple fibre	**9,924**	9,746	1.8
Hollow fibre	**10,494**	10,316	1.7
Filament	**10,946**	10,901	0.4
Weighted average price	**9,706**	9,544	1.7

Turnover

	For the year ended 31 December			
	2006		2005	
	Turnover Rmb'000	**Per cent of turnover %**	Turnover Rmb'000	Per cent of turnover %
Polyester products				
Polyester chips	**9,219,975**	**54.1**	8,225,566	52.1
Staple fibre	**4,734,752**	**27.8**	4,331,081	27.4
Hollow fibre	**557,208**	**3.3**	558,197	3.5
Filament	**2,027,667**	**11.9**	2,426,488	15.4
Others	**488,244**	**2.9**	257,333	1.6
Total	**17,027,846**	**100.0**	15,798,665	100.0

In 2006, the Group's turnover amounted to Rmb 17,027,846,000, representing an increase of 7.8 per cent as compared with Rmb 15,798,665,000 for last year. The increase was mainly due to the increase in sales volume, weighted average prices of polyester products (excluding VAT) and others' turnover by 4.7 per cent, 1.7 per cent and 89.7 per cent respectively as compared with last year.

(2) Cost of sales

In 2006, the Group's cost of sales amounted to Rmb 16,478,421,000, representing 96.8 per cent of the turnover, which decreased by 0.1 percentage points as compared with last year. Total costs of raw materials increased by Rmb 1,197,601,000 from Rmb 12,859,001,000 in 2005 to Rmb 14,056,602,000, which accounted for 85.3 per cent of cost of sales in 2006. The increase was mainly due to the increase in procurement and purchase cost of PTA and PX. The Group's weighted average purchase prices of polyester raw materials increased by 6.7 per cent as compared with last year. Of which, the average purchase costs of PTA and PX increased by 7.0 per cent and 19.2 per cent respectively as compared with last year. But the average purchase cost of MEG decreased by 8.1 per cent as compared with last year. To ease the increase in the cost of sale, the Group took measures to organize the safe and stable operation of facilities, reduce costs and expenses, increase PTA production volume and save energy consumption.

In 2006, although the turnover increased by 7.8 per cent as compared with last year, the Group's gross profit increased by Rmb 60,248,000 to Rmb 549,425,000 due to the increase in cost of sale by 7.6 per cent as compared with last year. The Group's gross margin was 3.2 per cent, representing a slight increase of 0.1 percentage points as compared with last year.

(3) Selling, administrative and financial expenses

	For the year ended 31 December		
	2006 Rmb'000	2005 Rmb'000	Change (%)
Selling expenses	**200,916**	210,503	(4.6)
Administrative expenses	**288,841**	365,543	(21.0)
Net finance (income)/costs	**(2,723)**	53,087	(105.1)
Total	**487,034**	629,133	(22.6)

In 2006, due to improve the proportion of direct selling, optimize the allocation of transportation resource and reduce intermediate expenses of sales, selling expenses decreased by Rmb 9,587,000 as compared with last year. Administrative expenses and net financing expenses decreased by Rmb 76,702,000 and Rmb 55,810,000 respectively as compared with last year. These saving are attributed to improvements to internal management, reductions in costs and expenses, a decrease in fixed assets depreciation as a result of asset structure adjustment and decrease in bank loans and discounted bills. The total reduction in selling expenses, administrative expenses and net finance costs was 22.6 per cent from that of 2005.

(4) Operating profit/(loss), profit/(loss)before taxation, profit/(loss) attributable to equity shareholders of the Company

	For the year ended 31 December		
	2006 Rmb'000	2005 Rmb'000	Change (%)
Operating profit/(loss)	**61,610**	(956,249)	Not applicable
Profit/(loss) before taxation	**64,333**	(1,009,336)	Not applicable
Income tax expense	**23,450**	(41,343)	Not applicable
Profit/(loss) attributable to equity shareholders of the Company	**40,468**	(967,508)	Not applicable
Earnings/(loss) per share(in Rmb)	**0.010**	(0.242)	Not applicable

In 2006, although the operational circumstances of the domestic polyester industry had not distinctly changed, the Group's operating profit and profit before taxation amounted to Rmb 61,610,000 and Rmb 64,333,000 respectively, achieved by exerting efforts to increase PTA production volume, strengthen internal management, exercise better control over costs and expenses, and optimising products mix. Profit attributable to equity shareholders of the Group amounted to Rmb 40,468,000.

(5) Statement of the principal operations by products

Polyester products contributed more than 10 percent of the Group's income from principal operations and profit from principal operations. The following is the statement of principal operations by products for the year ended 31 December 2006 in accordance with the PRC Accounting Rules and Regulations.

Products	Income from principal operations Rmb'000	Cost of principal operations Rmb'000	Gross profit margin %	Increase/ (decrease) in income from principal operations as compared to last year %	Increase/ (decrease) in cost of principal operations as compared to last year %	Gross margin ratio as compared to last year %
Polyester products	16,539,602	16,017,029	3.2	6.4	7.2	Decreased by 0.7 percentage points
Of which: connected transactions	215,024	205,230	4.6	(32.9)	(33.5)	Increased by 0.8 percentage points

During 2006, the Company did not sell any products to its controlling shareholders and their subsidiaries.

(6) Operations of principal subsidiaries in 2005

1. Yihua Kangqi Chemical Fibre Company Limited ("**Kangqi Company**") and its subsidiaries ("**Kangqi Group**"). The Company holds 100 per cent of the equity interest of Kangqi Company. Kangqi Company's registered capital is Rmb 60,000,000. Kangqi Company, through its 13 subsidiaries in major domestic markets, has established a sales network in the PRC. Kangqi Group's principal activities are sales of polyester fibre. As at 31 December 2006, the total assets of Kangqi Group were Rmb 354,866,000. For the year ended 31 December 2006, Kangqi Group made a net profit of Rmb 10,823,000.

2. Yihua UNIFI. The Company and UNIFI Asia holds 50 per cent of the equity interest of Yihua UNIFI respectively. Yihua UNIFI's registered capital is USD60,000,000 and a joint venture. Its principal activities are the production and sales of differential polyester filament and relative products, research and development of polyester and textile products, and after sales services for its products. As at 31 December 2006, the total assets of Yihua UNIFI were Rmb 614,972,000. For the year ended 31 December 2006, Yihua UNIFI made a loss of Rmb 76,678,000.

(7) Acquisition, divestment and investment

The Group did not make any material acquisition and investment in relation to any of its subsidiaries or associates in 2006. Details of divestment during the year of 2006 are set forth in item 5 of "Significant Events" of the Annual Report.

(8) Profit mix for the year 2006 and major reasons for the significant variance in the profit mix as compared with last year (extracted from the financial statements prepared in accordance with PRC Accounting Rules and Regulations)

In 2006, the percentages of profit from principal operations, expenses for the period and net non-operating expenses to total profit showed significant variance as compared with last year. Major reasons for the significant variance were the Group successfully erased the deficits and earned surpluses in its operational results in 2006.

(9) Possible changes in accounting policies and accounting estimates after the adoption of the new PRC Accounting Standards and their impact on the Company's financial position and results of operations

(1) In accordance with the requirements of the "Notice on the Release of 38 Accounting Standards for Business Enterprises" (Cai Kuai [2006] No.3) dated 15 February 2006, the Company should follow the New Accounting Standards from 1 January 2007. Upon application of the New Accounting Standards, the Company's consolidated shareholders' funds were increased by Rmb 64,251,000, from Rmb 8,274,261,000 to Rmb 8,338,512,000, with a portion of these funds reducing the accumulated losses by Rmb 16,599,000, and with the remainder comprising the minority interests of Rmb 47,652,000. The reconciliation of differences is explained below.

(i) Capitalisation of general borrowing costs

Under the "Accounting Standards for Business Enterprises No. 17 – Borrowing Cost," where funds are borrowed generally and used for acquiring a fixed asset that is qualified for capitalisation, their borrowing cost is capitalised as part of the asset's cost. The Company increased fixed assets amounting to Rmb 19,528,000 upon its adoption of the New Accounting Standards on 1 January 2007, by referring to the information relied upon by the Company in preparing the financial statements under IFRSs for the previous years. The Company reduced its accumulated losses amounting to Rmb 19,528,000 accordingly.

(ii) Income tax

Under the "Accounting Standards for Business Enterprises No. 18 – Income Tax," the Company increased the deferred tax liabilities amounting to Rmb 2,929,000 upon its adoption of the New Accounting Standards on 1 January 2007, which arose from the capitalization of general borrowing costs. The Company increased its accumulated losses amounting to Rmb 2,929,000 accordingly.

(iii) Minority interests

Under the "Accounting Standards for Business Enterprises No. 38 – First-Time Adoption of Accounting Standards for Business Enterprises" and the "Accounting Standards for Business Enterprises No. 33 – Consolidated Financial Statements," minority interests should be presented in the consolidated balance sheet as part of shareholders' funds instead of separately presented under the Old Accounting Standards. The Company's minority interests in the consolidated shareholders' funds amounted to Rmb 47,652,000 on 1 January 2007.

(2) Possible changes in accounting policies and accounting estimates after the adoption of the New Accounting Standards and their impact on the Company's financial status and operation results

(i) Under the "Accounting Standards for Business Enterprises No. 33 – Consolidated Financial Statements," the Company's jointly controlled entity which is proportionally combined in the Company's consolidated financial statements under the Old Accounting Standards, is accounted for using the equity method. The change of accounting policy will affect the Company's consolidated financial statements.

(ii) Under the "Accounting Standards for Business Enterprises No.2 – Long-term Equity Investments," the Company's subsidiaries, which are accounted for using the equity method in the Company's financial statements under the Old Accounting Standards, are accounted for using the cost method. The change of the accounting policy will lessen the impact of the subsidiaries' operating results on the Company's investment gain or loss for the current period, but will not affect the Company's consolidated financial statements.

(iii) Under the "Accounting Standards for Business Enterprises No. 6 – Intangible Assets," the Company will reclassify land use rights, which is accounted for fixed assets under the Old Accounting Standards to intangible assets. The Company's research expenditure and development expenditure will be accounted for separately. The development expenditure will be recognised as intangible assets if the criteria set in the New Accounting Standards are met.

The above differences and impacts may be adjusted in accordance with the Ministry of Finance's further guidelines of the New Accounting Standards.

2. FINANCIAL ANALYSIS

The Group's primary sources of funds come from operating activities, short-term and long-term borrowings, and the funds are primarily used for working capital, capital expenditures and repayment of short-term and long- term borrowings.

(1) Assets, liabilities and shareholders' equity analysis

	At 31 December 2006 Rmb'000	At 31 December 2005 Rmb'000	Changes in amount Rmb'000
Total assets	**10,155,439**	9,833,113	322,326
Current assets	**4,064,589**	2,980,642	1,083,947
Non-current assets	**6,090,850**	6,852,471	(761,621)
Total liabilities	**1,982,235**	1,709,196	273,039
Current liabilities	**1,982,235**	1,659,196	323,039
Non-Current liabilities	**–**	50,000	(50,000)
Minority interests	**47,652**	52,104	(4,452)
Shareholders' equity (excluding minority interests)	**8,125,552**	8,071,813	53,739

As at 31 December 2006, the Group's total assets were Rmb 10,155,439,000, total liabilities were Rmb 1,982,235,000, and shareholders' equity (excluding minority interests) were Rmb 8,125,552,000. Compared with the assets and liabilities as at 31 December 2005 (hereinafter referred to as "**as compared with the end of last year**"), the variations and main causes of such changes are described as follows:

Total assets were Rmb 10,155,439,000, an increase of Rmb 322,326,000 as compared with the end of last year. Current assets were Rmb 4,064,589,000, an increase of Rmb 1,083,947,000 as compared with the end of last year. The increase was mainly because the Group's cash and cash equivalents increased by Rmb 584,408,000 owing to abundant cash as a result of the rise in net cash inflow. Meanwhile, accounts receivable and bills receivable increased by Rmb 275,639,000 due to the increase in the Group's sales volume. Moreover, value added tax paid in advance increased by Rmb 188,545,000. Non-current assets were Rmb 6,090,850,000, a decrease of Rmb 761,621,000 as compared with the end of last year, which was mainly due to ordinary depreciation and amortisation.

Total liabilities were Rmb 1,982,235,000, an increase of Rmb 273,039,000 as compared with the end of last year. Current liabilities were Rmb 1,982,235,000, an increase of Rmb 323,039,000 as compared with the end of last year, which was mainly due to the increase of Rmb 586,531,000 in trade payables. Non-current liabilities were zero, a decrease of Rmb 50,000,000 as compared with the end of last year, which was mainly because the Group repaid long-term borrowings.

Shareholders' equity (excluding minority interests) was Rmb 8,125,552,000, an increase of Rmb 53,739,000 as compared with the end of last year, mainly due to Rmb 40,468,000 for profit attributable to equity shareholders of the Group.

As at 31 December 2006, total liabilities to total assets ratio was 19.5 per cent, and 17.4 per cent as at 31 December 2005.

(2) Cash flow analysis

At the end of 2006, cash and cash equivalents increased by Rmb 568,728,000, representing an increase from Rmb 372,535,000 as at 31 December 2005 to Rmb 941,263,000 as at 31 December 2006. The following table lists major items in the consolidated cash flow statement of the Group for the year 2006 and 2005.

Major items in cash flow statement	2006 Rmb'000	2005 Rmb'000	Change Rmb'000
Net cash flow from operating activities	**777,509**	577,510	199,999
Net cash flow from investing activities	**(66,427)**	86,290	(152,717)
Net cash flow from financing activities	**(142,354)**	(519,417)	377,063
Net increase in cash and cash equivalents	**568,728**	144,383	424,345
Cash and cash equivalents at the beginning of the year	**372,535**	228,152	144,383
Cash and cash equivalents at the end of the year	**941,263**	372,535	568,728

In 2006, the Group's net cash inflow from operating activities was Rmb 777,509,000, representing an increase of Rmb 199,999,000 as compared with last year. The main reasons were: (1) Gross profit was Rmb 549,425,000 in 2006, whereas, it was Rmb 489,177,000 in 2005. As a result, the net cash inflow from operating activities increased by Rmb 60,248,000. (2) Owing to the reduction in interest paid and income tax paid in 2006, the net cash inflow from operating activities increased by Rmb 82,612,000.

In 2006, the Group's net cash outflow from investing activities was Rmb 66,427,000, an increase of cash outflow by Rmb 152,717,000 as compared with last year. The main reasons were time deposits with banks and other financial institutions increased by Rmb 92,002,000, while the deposits in 2005 decreased by Rmb 104,836,000, which increased cash outflows by Rmb 196,838,000.

In 2006, the Group's net cash outflow from financing activities was Rmb 142,354,000, a decrease of cash outflow by Rmb 377,063,000 as compared with last year. The main reasons were that the amount of repayment in 2006 greatly decreased as a result of vigorously reducing loans in the recent two years.

In 2006, the Group's net cash inflow from operating activities was Rmb 777,509,000, while profit attributable to equity shareholders of the Group was Rmb 40,468,000. This significant difference was mainly due to ordinary depreciation and amortization and increase in trade and other payables.

(3) Bank borrowings

As at 31 December 2006, the Group's bank borrowings were Rmb 82,500,000, decreased by Rmb 105,000,000 compared with Rmb 187,500,000 as at 31 December 2005. The Group's major bank borrowings were denominated in Renminbi and all of the bank borrowings were charged at the fixed interest rate. The borrowing needs of the Group were not subject to seasonal changes.

(4) Assets charges

For the year ended 31 December 2006, there was not any charge on the Group's assets.

(5) Management of foreign exchange risk

Main receivables and payables items of the Group are dominated in Renminbi. Foreign currency used in the Group's operation was dominated in US dollars and were settled immediately under current items. Therefore, there is no material effect on the Group resulting from the fluctuations in foreign exchange rates.

(6) Debt-equity ratio

The debt-equity ratio of the Group was zero for 2006 (2005:0.6 per cent). The ratio is computed as long-term borrowings divided by the sum of long-term borrowings and shareholders' equity.

3. CAPITAL EXPENDITURE

In 2006, the Company's capital expenditure amounted to Rmb 73,600,000, which was mainly invested the projects such as saving energy consumption, safety and environment, and reducing costs and expenses.

The Company's capital expenditure for the year 2007 is expected to be approximately Rmb 621,440,000. In order to investment contribution maximise, the Company will strengthen investment management in accordance with the prudential principle. The planned capital expenditures will be funded from cash generated from operations and bank credit facilities.