

Report of the PRC Auditors



All Shareholders of Sinopec Yizheng Chemical Fibre Company Limited (“the Company”):

We have audited the accompanying financial statements of the Company, which comprise the consolidated balance sheet and balance sheet as at 31 December 2006, and the consolidated income and profit appropriation statement, income and profit appropriation statement, consolidated cash flows statement and cash flow statement for the year then ended, and notes to the financial statements.

MANAGEMENT’S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Company’s management is responsible for the preparation of these financial statements in accordance with the Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises issued by the Ministry of Finance of the People’s Republic of China. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITORS’ RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with China’s Auditing Standards for the Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors’ judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity’s preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the financial statements comply with the requirements of the Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises issued by the Ministry of Finance of the People’s Republic of China and present fairly, in all material respects, the consolidated financial position and financial position of the Company as at 31 December 2006, the consolidated results of operations, results of operations, consolidated cash flows and cash flows of the Company for the year then ended.

KPMG Huazhen

Beijing, The People’s Republic of China

*Certified Public Accountants
Registered in The People’s Republic of China*

Hu Qiong

Yu Xiao-jun

30 March 2007



Consolidated Balance Sheet

As at 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Assets			
Current assets			
Cash at bank and on hand	4	1,059,263	398,533
Bills receivable	5	983,526	820,731
Accounts receivable	6	302,635	189,407
Other receivables	7	80,908	111,881
Payments in advance	8	66,159	17,328
Inventories	9	1,383,553	1,287,936
Total current assets		<u>3,876,044</u>	<u>2,825,816</u>
Long-term investments			
Long-term equity investments	10	<u>-</u>	<u>62,500</u>
Fixed assets			
Cost		13,036,964	14,064,457
Less: Accumulated depreciation		<u>7,136,432</u>	<u>7,152,305</u>
Net book value before provision for impairment		5,900,532	6,912,152
Less: Provision for impairment of fixed assets		<u>25,362</u>	<u>417,621</u>
Carrying amount	11	5,875,170	6,494,531
Construction in progress	12	<u>121,818</u>	<u>270,963</u>
Total fixed assets		<u>5,996,988</u>	<u>6,765,494</u>
Intangible assets			
	13	<u>168,925</u>	<u>247,655</u>
Deferred taxation			
Deferred tax assets	3(e)	<u>73,646</u>	<u>83,410</u>
Total assets		<u><u>10,115,603</u></u>	<u><u>9,984,875</u></u>

The notes on pages 112 to 148 form part of these financial statements.

Consolidated Balance Sheet

As at 31 December 2006

(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Liabilities and shareholders' funds			
Current liabilities			
Short-term loans	14	82,500	82,591
Bills payable	15	-	5,501
Accounts payable	15	1,144,022	507,729
Receipts in advance	15	320,542	343,802
Accrued payroll		155,143	164,279
Staff welfare payable		60,215	54,430
Taxes payable	3(d)	(161,070)	12,931
Other payables	16	12,013	22,799
Other creditors	15	167,491	354,590
Accrued expenses	17	-	279
Long-term liabilities due within one year	18	6,079	97,431
Total current liabilities		<u>1,786,935</u>	<u>1,646,362</u>
Long-term liabilities			
Long-term loans	19	-	50,000
Long-term payables	20	6,755	12,834
Total long-term liabilities		<u>6,755</u>	<u>62,834</u>
Total liabilities		<u>1,793,690</u>	<u>1,709,196</u>
Minority interests			
		<u>47,652</u>	<u>52,104</u>
Shareholders' funds			
Share capital	21	4,000,000	4,000,000
Capital reserve	22	3,116,808	3,103,537
Surplus reserve	23	1,456,004	1,456,004
Accumulated losses		(298,551)	(335,966)
Total shareholders' funds		<u>8,274,261</u>	<u>8,223,575</u>
Total liabilities and shareholders' funds		<u>10,115,603</u>	<u>9,984,875</u>

These financial statements have been approved by the Board of Directors of the Company on 30 March 2007.

Qian Heng-ge
Chairman
(Legal Representative)

Xiao Wei-zhen
Vice Chairman
and General
Manager

Li Jian-ping
Chief Financial
Officer

Xu Xiu-yun
Supervisor of the
Asset and Accounting
Department

The notes on pages 112 to 148 form part of these financial statements.



Balance Sheet

As at 31 December 2006

(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Assets			
Current assets			
Cash at bank and on hand	4	910,845	281,947
Bills receivable	5	904,599	748,856
Accounts receivable	6	296,588	171,848
Other receivables	7	69,988	319,226
Payments in advance	8	62,233	3,923
Inventories	9	1,321,150	1,157,898
		<u>3,565,403</u>	<u>2,683,698</u>
Total current assets			
Long-term investments			
Long-term equity investments	10	412,703	352,187
Receivables due after 1 year	10(c)	-	2,712
		<u>412,703</u>	<u>354,899</u>
Total long-term investments			
Fixed assets			
Cost		12,763,541	12,635,784
Less: Accumulated depreciation		7,101,928	6,536,333
		<u>5,661,613</u>	<u>6,099,451</u>
Net book value before provision for impairment			
Less: Provision for impairment of fixed assets		25,362	25,860
		<u>5,636,251</u>	<u>6,073,591</u>
Carrying amount	11		
Construction in progress	12	114,037	269,215
		<u>5,750,288</u>	<u>6,342,806</u>
Total fixed assets			
Intangible assets			
	13	146,976	224,351
Deferred taxation			
Deferred tax assets	3(e)	73,646	83,410
Total assets			
		<u>9,949,016</u>	<u>9,689,164</u>

The notes on pages 112 to 148 form part of these financial statements.

Balance Sheet

As at 31 December 2006

(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Liabilities and shareholders' funds			
Current liabilities			
Accounts payable	15	1,141,057	499,199
Receipts in advance	15	328,650	347,299
Accrued payroll		145,992	155,720
Staff welfare payable		51,926	47,165
Taxes payable	3(d)	(174,509)	4,638
Other payables	16	10,901	21,842
Other creditors	15	162,768	235,767
Accrued expenses	17	-	279
Long-term liabilities due within one year	18	-	90,000
Total current liabilities		1,666,785	1,401,909
Long-term liabilities			
Long-term loans	19	-	50,000
Total liabilities		1,666,785	1,451,909
Shareholders' funds			
Share capital	21	4,000,000	4,000,000
Capital reserve	22	3,126,453	3,113,182
Surplus reserve	23	1,456,004	1,456,004
Accumulated losses		(300,226)	(331,931)
Total shareholders' funds		8,282,231	8,237,255
Total liabilities and shareholders' funds		9,949,016	9,689,164

These financial statements have been approved by the Board of Directors of the Company on 30 March 2007.

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The notes on pages 112 to 148 form part of these financial statements.

Consolidated Income and Profit Appropriation Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Sales from principal activities	24	17,027,846	15,798,665
Less: Cost of sales from principal activities	24	16,450,738	15,246,152
Business taxes and surcharges	3(c)	31,170	38,555
Profit from principal activities		545,938	513,958
Less: Loss/(profit) from other operations		1,323	(2,288)
Operating expenses		200,936	210,503
General and administrative expenses		300,868	394,391
Add: Net financial income/(financial expenses)	25	2,723	(56,630)
Operating profit/(loss)		45,534	(145,278)
Add: Investment income	26	15,039	36,491
Non-operating income	27	53,095	23,088
Less: Non-operating expenses	28	52,926	911,550
Profit/(loss) before income tax		60,742	(997,249)
Less: Income tax	3(b)	22,912	(42,485)
Minority interests		415	(485)
Net profit/(loss) for the year		37,415	(954,279)
Add: (Accumulated losses)/retained earnings at the beginning of the year		(335,966)	718,313
Accumulated losses attributable to shareholders		(298,551)	(235,966)
Less: Cash dividends appropriated to shareholders		-	100,000
Accumulated losses at the end of the year		(298,551)	(335,966)
Supplementary information:			
Item	Note	2006 Rmb'000	2005 Rmb'000
Loss on disposal of a subsidiary	10(c)	1,920	-

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The notes on pages 112 to 148 form part of these financial statements.

Income and Profit Appropriation Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

	Note	2006 Rmb'000	2005 Rmb'000
Sales from principal activities	24	16,287,590	14,797,740
Less: Cost of sales from principal activities	24	15,762,953	14,290,048
Business taxes and surcharges	3(c)	29,859	37,341
Profit from principal activities		494,778	470,351
Add: Profit from other operations		4,597	5,945
Less: Operating expenses		156,212	170,981
General and administrative expenses		271,570	343,036
Add: Net financial income/(financial expenses)	25	7,463	(46,533)
Operating profit/(loss)		79,056	(84,254)
Less: Investment loss	26	28,609	503,551
Add: Non-operating income	27	35,666	24,031
Less: Non-operating expenses	28	44,644	453,026
Profit/(loss) before income tax		41,469	(1,016,800)
Less: Income tax	3(b)	9,764	(59,902)
Net profit/(loss) for the year		31,705	(956,898)
Add: (Accumulated losses)/retained earnings at the beginning of the year		(331,931)	724,967
Accumulated losses attributable to shareholders		(300,226)	(231,931)
Less: Cash dividends appropriated to shareholders		-	100,000
Accumulated losses at the end of the year		(300,226)	(331,931)
Supplementary information:			
Item	Note	2006 Rmb'000	2005 Rmb'000
Loss on disposal of a subsidiary	10(c)	1,920	-

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The notes on pages 112 to 148 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

Note to the
cash flow
statement

Cash flows from operating activities:

Cash received from sale of goods and rendering of services	20,551,719
Refund of taxes	1,697
Other cash received relating to operating activities	32,948

Sub-total of cash inflows	<u>20,586,364</u>
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Cash paid for goods and services	(18,127,316)
Cash paid to and for employees	(641,224)
Cash paid for all types of taxes	(712,657)
Other cash paid relating to operating activities	(312,559)

Sub-total of cash outflows	<u>(19,793,756)</u>
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Net cash inflow from operating activities	(i) <u>792,608</u>
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Cash flows from investing activities:

Cash received from disposal of a subsidiary	(iii) 9,626
Cash received from disposal of investments	83,505
Net cash received from disposal of fixed assets	20,802
Other cash received relating to investing activities	17,479
Other cash received relating to investing activities by a jointly controlled entity	62

Sub-total of cash inflows	<u>131,474</u>
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Cash paid for acquisition of fixed assets	(87,211)
Other cash paid for acquisition of fixed assets and intangible assets by a jointly controlled entity	(18,688)

Sub-total of cash outflows	<u>(105,899)</u>
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Net cash inflow from investing activities	<u>25,575</u>
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Cash flows from financing activities:

Cash received from bank loans	119,609
Cash received from bank loans by a jointly controlled entity	390,000

Sub-total of cash inflows	<u>509,609</u>
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Cash repayment of borrowings	(294,700)
Cash paid for dividends distribution and interest expenses	(14,406)
Cash repayment of borrowings by a jointly controlled entity	(355,000)
Cash paid for interest expenses by a jointly controlled entity	(2,956)

Sub-total of cash outflows	<u>(667,062)</u>
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Net cash outflow from financing activities	<u>(157,453)</u>
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Net increase in cash and cash equivalents	(iv) <u>660,730</u>
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The notes on pages 112 to 148 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

Notes to the consolidated cash flow statement

(i) Reconciliation of net profit to net cash inflow from operating activities:

	2006 Rmb'000
Net profit	37,415
Add: Provision for bad and doubtful debts	3,971
Write-back of provision for bad and doubtful debts	(1,017)
Provision for inventories	38,482
Write-back of provision for inventories	(35,261)
Depreciation of fixed assets	687,702
Amortisation of intangible assets	7,623
Gains arising from investments	(15,039)
Financial expenses	(2,721)
Net losses on disposal of fixed assets	19,396
Decrease in deferred tax assets	9,764
Increase in gross inventories	(143,224)
Increase in gross operating receivables	(149,229)
Increase in operating payables	334,331
Minority interests	415
Net cash inflow from operating activities	792,608

(ii) Investing activities not requiring the use of cash or cash equivalents:

Consideration for disposal of a subsidiary not settled by cash	166,400
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(iii) Cash received from disposal of a subsidiary:

	2006	
	The Group Rmb'000	The Company Rmb'000
Cash consideration	23,050	23,050
Less: Cash held by a subsidiary disposed of	13,424	-
Cash received from disposal of a subsidiary	9,626	23,050

Details of financial position and results of operations of the subsidiary disposed of are set out in note 10 (c).

(iv) Net increase in cash and cash equivalents:

	2006 Rmb'000
Cash and cash equivalents at the end of the year (note 4)	1,059,263
Less: Cash and cash equivalents at the beginning of the year (note 4)	398,533
Net increase in cash and cash equivalents	660,730

These financial statements have been approved by the Board of Directors of the Company on 30 March 2007.

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The notes on pages 112 to 148 form part of these financial statements.

Cash Flow Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

Note to the
cash flow
statement

Cash flows from operating activities:

Cash received from sale of goods and rendering of services	18,911,968
Refund of taxes	1,697
Other cash received relating to operating activities	29,595

Sub-total of cash inflows	18,943,260
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Cash paid for goods and services	(16,764,738)
Cash paid to and for employees	(611,982)
Cash paid for all types of taxes	(689,328)
Other cash paid relating to operating activities	(145,447)

Sub-total of cash outflows	(18,211,495)
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Net cash inflow from operating activities	(i) 731,765
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Cash flows from investing activities:

Cash received from disposal of a subsidiary	(iii) 23,050
Cash received from disposal of investments	82,000
Net cash received from disposal of fixed assets	8,583
Other cash received relating to investing activities	14,935

Sub-total of cash inflows	128,568
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Cash paid for acquisition of fixed assets	(83,269)
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Sub-total of cash outflows	(83,269)
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Net cash inflow from investing activities	45,299
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Cash flows from financing activities:

Cash received from bank loans	117,000
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Sub-total of cash inflows	117,000
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Cash repayment of borrowings	(257,000)
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Cash paid for interest expenses	(8,166)
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Sub-total of cash outflows	(265,166)
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Net cash outflow from financing activities	(148,166)
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Net increase in cash and cash equivalents	(iv) 628,898
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The notes on pages 112 to 148 form part of these financial statements.

Cash Flow Statement

For the year ended 31 December 2006
(Prepared in accordance with PRC Accounting Rules and Regulations)

Notes to the cash flow statement

	2006 Rmb'000
(i) Reconciliation of net profit to net cash inflow from operating activities:	
Net profit	31,705
Add: Provision for bad and doubtful debts	2,245
Write-back of provision for bad and doubtful debts	(593)
Provision for inventories	23,873
Write-back of provision for inventories	(23,873)
Depreciation of fixed assets	658,645
Amortisation of intangible assets	6,268
Losses arising from investments	28,609
Financial expenses	(7,048)
Net losses on disposal of fixed assets	12,368
Decrease in deferred tax assets	9,764
Increase in gross inventories	(163,252)
Increase in gross operating receivables	(227,252)
Increase in operating payables	380,306
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Net cash inflow from operating activities	731,765
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(ii) Investing activities not requiring the use of cash or cash equivalents:	
Consideration for disposal of a subsidiary not settled by cash	166,400
Conversion of other receivables into investment in a jointly controlled entity	120,252
(iii) Cash received from disposal of a subsidiary:	
Please see note (iii) to the consolidated cash flow statement.	
(iv) Net increase in cash and cash equivalents:	
Cash and cash equivalents at the end of the year (note 4)	910,845
Less: Cash and cash equivalents at the beginning of the year (note 4)	281,947
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Net increase in cash and cash equivalents	628,898
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These financial statements have been approved by the Board of Directors of the Company on 30 March 2007.

Qian Heng-ge
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The notes on pages 112 to 148 form part of these financial statements.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

1. COMPANY STATUS

Sinopec Yizheng Chemical Fibre Company Limited (the “**Company**”) was established in the People’s Republic of China (“**PRC**”) on 31 December 1993 as a joint stock limited company as part of the restructuring of the Yihua Group Corporation (“**Yihua**”). On the same date, the principal business undertakings of Yihua together with the relevant assets and liabilities were taken over by the Company.

Pursuant to the directives on the reorganisation of certain companies involving the Company and Yihua as issued by the State Council and other governmental authorities of the PRC, China Eastern United Petrochemical (Group) Company Limited (“**CEUPEC**”) became the largest shareholder of the Company on 19 November 1997, holding the 1,680,000,000 A shares (representing 42% of the Company’s issued share capital) previously held by Yihua. China International Trust and Investment Corporation (“**CITIC**”) continues to hold the 18% of the Company’s issued share capital (in the form of A shares) that it held prior to the reorganisation, and the balance of 40% remains in public hands in the form of A shares and H shares.

Following the State Council’s approval of the reorganisation of China Petrochemical Corporation (“**CPC**”) on 21 July 1998, CEUPEC joined CPC. As a result of the reorganisation, Yihua replaced CEUPEC as the holder of the 42% of the Company’s issued share capital, and CEUPEC dissolved.

The reorganisation of CPC was completed on 25 February 2000 and CPC set up a joint stock limited company, China Petroleum & Chemical Corporation (“**Sinopec Corp**”), in the PRC. From that date, the 1,680,000,000 A shares (representing 42% of the issued share capital of the Company), which were previously held by Yihua, were transferred to Sinopec and Sinopec became the largest shareholder of the Company.

By a special resolution passed in the Shareholders’ Meeting on 18 October 2000, the name of the Company was changed from “Yizheng Chemical Fibre Company Limited” to “Sinopec Yizheng Chemical Fibre Company Limited”.

The principal activities of the Company, its subsidiaries and its jointly controlled entity (the “**Group**”) are the manufacturing and sale of chemical fibre and chemical fibre raw materials.

2. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted by the Group in the preparation of the financial statements conform to the Accounting Standards for Business Enterprises, the Accounting Regulations for Business Enterprises and other relevant regulations issued by the Ministry of Finance of the PRC (“**MOF**”).

(a) Accounting year

The accounting year of the Group is from 1 January to 31 December.

(b) Basis of consolidation

The Group’s consolidated financial statements are prepared in accordance with the Accounting Regulations for Business Enterprises and Cai Kuai Zi [1995] No.11 “Temporary regulations on consolidated financial statements” issued by the MOF.

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries and its jointly controlled entity. Subsidiaries are those entities in which the Company directly or indirectly, holds more than 50% (not including 50%) of the issued share capital, or has the power to control despite the issued share capital held by the Company is equal to or less than 50%. The results of the subsidiaries during the period in which the Company holds more than 50% of the issued share capital or the Company has the power to control despite the issued share capital held by the Company is equal to or less than 50%, are included in the consolidated income statement of the Company. The effect of minority interests on equity and profit/loss attributable to minority interests are separately shown in the consolidated financial statements.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Basis of consolidation (Continued)

A jointly controlled entity is an entity over which the Group can exercise joint control with other ventures. Joint control is the contractually agreed sharing of control over an economic activity. Investments in jointly controlled entities are accounted for on a proportionate consolidation basis. Under this method, the Group combines its proportionate share of the jointly controlled entity's turnover and expenses with each major turnover and expense caption of the Group's income statement and combines its proportionate share of the jointly controlled entity's assets and liabilities with each major asset and liability caption of Group's balance sheet.

Where the accounting policies adopted by the subsidiaries and the jointly controlled entity are different from the policies adopted by the Company, the financial statements of the subsidiaries and the jointly controlled entity have been adjusted in accordance with the accounting policies adopted by the Company on consolidation. All significant inter-company balances and transactions, and any unrealised gains arising from inter-company transactions, have been eliminated on consolidation.

Details of the Company's principal subsidiary and the jointly controlled entity are disclosed in note 10(a).

(c) Basis of preparation and measurement basis

The financial statements of the Group have been prepared on an accrual basis. Unless otherwise stated, the measurement basis used is historical cost.

(d) Reporting currency

The Group's reporting currency is the Renminbi.

(e) Translation of foreign currencies

Foreign currency transactions during the year are translated into Renminbi at the exchange rates quoted by the People's Bank of China ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Renminbi at the exchange rates quoted by the People's Bank of China ruling at the balance sheet date. Exchange gains and losses on foreign currency translation, except for the exchange gains and losses directly relating to the construction of fixed assets (see note 2(k)), are dealt with in the income statement.

Exchange differences which arise during the start-up period are aggregated in the long-term deferred expenses and are then fully charged to the income statement in the month of commencement of operations.

(f) Cash equivalents

Cash equivalents represent short-term, highly liquid investments which are readily convertible into known amounts of cash, and are subject to an insignificant risk of change in value.

(g) Provision for bad and doubtful debts

The provision for bad debt losses is estimated based on individual accounts receivable which show signs of uncollectibility and an aging analysis. Provision for other receivables is determined based on their specific nature and management's estimate of their collectibility.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(h) Inventories

Inventories, other than spare parts and consumables, are carried at the lower of cost and net realisable value.

Costs comprise all costs of purchase, costs of conversion and other costs. Inventories are measured at their actual cost upon acquisition. The cost of inventories is calculated using the weighted average method. In addition to the purchase cost of raw materials, work in progress and finished goods include direct labour costs and an appropriate allocation of manufacturing overheads.

Any excess of the cost over the net realisable value of each item of inventories is recognised as a provision for diminution in the value of inventories. Net realisable value is the estimated selling price in the normal course of business less the estimated costs to completion and the estimated expenses and related taxes necessary to make the sale.

Spare parts and consumables are stated at cost less any provision for obsolescence. Spare parts and consumables are amortised in full when received for use.

The Group adopts a perpetual inventory system.

(i) Long-term equity investments

Where the Group has the power to control, jointly control or exercise significant influence over an investee enterprise, the investment is accounted for under the equity method of accounting whereby the investment is initially recorded at cost and adjusted thereafter for any post acquisition change in the Group's share of the investors' equity in the investee enterprise.

Equity-investment difference, which is the difference between the initial investment cost and the Group's share of investors' equity in the investee enterprises, is accounted for as follows:

- Any excess of the initial investment cost over the Group's share of the investors' equity in the investee enterprise is amortised on a straight-line basis. The amortisation period is determined according to the investment period as stipulated in the relevant agreement, or 10 years if the investment period is not specified in the agreement. The unamortised balance is included in long-term equity investments at the year end.
- Any shortfall of the initial investment cost over the Company's share of the investors' equity in the investee enterprise is amortised on a straight-line basis if the investment was acquired before the MOF's issuance of the "Questions and answers on implementing Accounting Regulations for Business Enterprises and related accounting standards (II)" (Cai Kuai [2003] No. 10). The amortisation period is determined according to the investment period as stipulated in the relevant agreement, or 15 years if the investment period is not specified in the agreement. The unamortised balance is included in long-term equity investments at the year end. Such shortfalls are recognised in the "Capital reserve – reserve for equity investment" if the investment was acquired after the issuance of the Cai Kuai [2003] No.10.

Where the Company does not control, jointly control or exercise significant influence over an investee enterprise, the investment is accounted for under the cost method, stating it at the initial investment cost. Investment income is recognised once the investee enterprise declares a cash dividend or distributes profits.

Upon the disposal or transfer of long-term equity investments, the difference between the proceeds received and the carrying amount of the investments is recognised as profit or loss.

The Group makes provision for impairment losses on long-term equity investments (see note 2(m)).

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(j) Fixed assets

Fixed assets are assets with comparatively high unit values held by the Group for use in the production of goods, rendering of services and for administrative purposes. They are expected to be used for more than one year.

Fixed assets are stated in the balance sheet at cost or revalued amount less accumulated depreciation and impairment losses (see note 2(m)). The revalued amount refers to the fixed assets value, which have been adjusted to the revalued amounts according to the fixed assets valuation carried out in accordance with the relevant rules and regulations.

The Group's fixed assets are depreciated using the straight-line method over their estimated useful lives. The respective estimated useful lives and the estimated rate of residual values on cost for the Group's fixed assets are as follows:

	Estimated useful life	Estimated rate of residual value
Land and buildings	25 to 50 years	0%–3%
Machinery equipment	8 to 22 years	3%
Motor vehicles and other fixed assets	4 to 10 years	3%

(k) Construction in progress

Construction in progress is stated in the balance sheet at cost less impairment losses (see note 2(m)). All direct and indirect costs that are related to the construction of fixed assets and incurred before the assets are ready for their intended use are capitalised as construction in progress. Those costs include borrowing costs (including foreign exchange differences arising from the loan principle and the related interest) on specific borrowings for the construction of the fixed assets during the construction period.

Construction in progress is transferred to fixed assets when it is ready for its intended use. No depreciation is provided against construction in progress.

(l) Intangible assets

Intangible assets are stated in the balance sheet at cost less accumulated amortisation and impairment losses (see note 2(m)). The cost of the intangible assets is amortised on a straight-line basis. The amortisation period is determined according to the shorter of the contracted beneficial period and the effective period stipulated by law, or 10 years if the period is not specified in the contract or law.

(m) Provision for impairment

The carrying amounts of assets (including long-term investments, fixed assets, construction in progress and intangible assets) are assessed regularly to determine whether their recoverable amounts have declined below their carrying amounts. Assets are tested for impairment whenever events or changes in conditions indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount by which the carrying amount is reduced is the impairment loss.

The recoverable amount is the greater of the net selling price and the present value of the estimated future cash flows arising from the continuous use of the asset and from the disposal of the asset at the end of its useful life.

Provision for impairment is calculated on an item by item basis and recognised as an expense in the income statement. However, when a deficit between the initial investment cost and the Company's share of the investors' equity of the investee enterprise has been credited to the capital reserve, any impairment losses for long-term equity investment are firstly set off against the difference initially recognised in the capital reserve relating to the investment and any excess impairment losses are then recognised in the income statement.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(m) Provision for impairment (Continued)

If there is an indication that there has been a change in the factors used to determine the provision for impairment and as a result the estimated recoverable amount is greater than the carrying amount of the asset, the impairment loss recognised in prior years is reversed. Reversals of impairment losses are recognised in the income statement. An impairment loss is reversed only to the extent of the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. In respect of the reversal of an impairment loss for a long-term equity investment, the reversal starts with the impairment losses that had previously been recognised in the income statement and then the impairment losses that had been charged to capital reserve.

(n) Income tax

Income tax is recognised using the tax effect accounting method. Income tax for the year comprises current tax paid and payable and movements in deferred tax assets and liabilities.

Current tax is calculated at the applicable tax rate on taxable income.

Deferred tax is provided using the liability method for the differences between the accounting profits and the taxable profits arising from the timing differences in recognising income, expenses or losses between the accounting and tax regulations. When the tax rate changes or a new type of tax is levied, adjustments are made to the amounts originally recognised for the timing differences under the liability method. The current tax rates are used in arriving at the reversal amounts when the timing differences are reversed.

Deferred tax assets arising from tax losses, which are expected to be utilised against future taxable profits, are set off against the deferred tax liabilities (only for the same taxpayer within the same jurisdiction). When it is not probable that the tax benefits of deferred tax assets will be realised, the deferred tax assets are reduced to the extent that the related tax benefits are expected to be realised.

(o) Provisions and contingent liabilities

Provisions are recognised when the Group has a present obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligations and a reliable estimate can be made.

Where it is not probable that the settlement of the above obligation will cause an outflow of economic benefits, or the amount of the outflow cannot be estimated reliably, the obligation is disclosed as a contingent liability.

(p) Revenue recognition

When it is probable that the economic benefits will flow to the Group and the revenue and cost can be measured reliably, revenue is recognised in the income statement according to the following methods:

(i) Sales of goods

Sales revenue is recognised when the significant risks and rewards of the ownership of goods have been transferred to the buyers. No revenue is recognised if there are significant uncertainties regarding the receipt of the consideration and the return of goods, or when the revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(p) Revenue recognition (Continued)

(ii) Rendering of services

When the provision of service is started and completed within the same accounting year, revenue from the rendering of services is recognised in the income statement at the time of completion of the services. When the provision of service is started and completed in different accounting years, revenue from the rendering of services is recognised by reference to the stage of completion of the transaction based on the progress of work performed, to the extent that the outcome of a transaction involving the rendering of service can be estimated reliably. When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue is recognised only to the extent of cost incurred that are expected to be recoverable.

(iii) Interest income

Interest income is recognised on a time proportion basis with reference to the principal outstanding and the applicable rate.

(q) Research and development costs

Research and development costs are recognised as expenses in the income statement in the period in which they are incurred.

(r) Borrowing costs

Borrowing costs incurred on specific borrowings for the construction of fixed assets are capitalised into the cost of the fixed assets during the construction period until the fixed assets are ready for their intended uses.

Except for the above, other borrowing costs are recognised as financial expenses in the income statement when incurred.

(s) Repairs and maintenance expenses

Repairs and maintenance expenses are recognised in the income statement when incurred.

(t) Environmental preservation expenses

Environmental preservation expenses relating to circumstances arising as a result of the current or past businesses are recognised in the income statement when incurred.

(u) Dividends appropriated to shareholders

Cash dividends appropriated to the shareholders are recognised in the income and profit appropriation statement upon approval. Cash dividends approved after the balance sheet date, but before the date on which the financial statements are authorised for issue, are disclosed in the balance sheet as a separate component under shareholders' funds.

(v) Profit appropriation

Profit appropriation is made in accordance with the relevant rules and regulations set out in the Company Law of the PRC ("the Company Law") and the Articles of Association of the Company, its subsidiaries and the jointly controlled entity.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(w) Retirement benefits

Pursuant to the relevant laws and regulations in the PRC, the Group has joined a defined contribution retirement plan for the employees arranged by a governmental organisation. The Group makes contributions to the retirement scheme at the applicable rates based on the employees' salaries. The required contributions under the retirement plans are charged to the income statement.

(x) Related parties

If the Group has the power, directly or indirectly, to control, jointly control or exercise significant influence over another party, or vice versa, or where the Group and one or more parties are subject to common control from another party, they are considered to be related parties. Related parties may be individuals or enterprises.

3. TAXATION

- (a) The types of tax applicable to the Group's sale of goods and rendering of services include value added tax ("VAT"), business tax, city development tax and education surcharge.

The VAT rate is 17%.

The business tax rate is either 3% or 5%.

City development tax is paid at a rate of 7% of the sum of business tax payable and VAT payable.

Education surcharge is paid at a rate of 4% of the sum of business tax payable and VAT payable.

(b) Income tax

Income tax in the income statement represents:

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Provision for income tax for the year	10,970	10,615	-	-
Under provision for income tax in respect of preceding year	2,178	1,774	-	601
	13,148	12,389	-	601
Reversal/(origination) of deferred tax assets	9,764	(54,874)	9,764	(60,503)
Total	22,912	(42,485)	9,764	(59,902)

Pursuant to the directive "Cai Shui Zi [1994] No. 17" issued by the MOF and the State Administration of Taxation of the PRC on 18 April 1994, the Company's applicable income tax rate is 15%.

The income tax rate applicable to the Group's jointly controlled entity, Yihua UNIFI Fibre Industry Company Limited ("Yihua UNIFI") is 27%. Pursuant to the PRC Foreign Investment Enterprises and Foreign Enterprises Income Tax, starting from the year in which a taxable income is made after the offset of deductible losses incurred in prior years, the jointly controlled entity is entitled to a tax holiday of a tax free period for the first and second years and a 50% reduction in the income tax rate for the third to fifth years.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

3. TAXATION (Continued)

(b) Income tax (Continued)

Except for the following subsidiary granted with tax concession, the income tax rate applicable to the Group's other principal subsidiaries is 33%.

The subsidiary granted with tax concession is set out below:

Name of subsidiary	Preferential tax rate	Reason for granting concession
Yizheng Chemical Fibre Xiamen Kangqi Co., Ltd.	15%	Enterprise in Xiamen special economic zone

(c) Business taxes and surcharges

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
City development tax	19,835	24,536	19,001	23,763
Education surcharge	11,335	14,019	10,858	13,578
	<u>31,170</u>	<u>38,555</u>	<u>29,859</u>	<u>37,341</u>

(d) Taxes payable

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Income tax payable	8,356	9,785	-	2,112
City development tax payable	5,841	25,051	5,463	24,769
VAT payable/(recoverable)	4,548	(33,910)	-	(34,159)
Prepaid VAT	(188,545)	-	(188,545)	-
Others	8,730	12,005	8,573	11,916
	<u>(161,070)</u>	<u>12,931</u>	<u>(174,509)</u>	<u>4,638</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

3. TAXATION (Continued)

(e) Deferred tax assets and liabilities

Deferred tax assets

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Provision for bad and doubtful debts	1,041	1,375	1,041	1,375
Provision for inventories	8,679	8,679	8,679	8,679
Provision for impairment of fixed assets	3,804	3,879	3,804	3,879
Difference in depreciation	6,953	4,942	6,953	4,942
Tax loss	53,169	64,535	53,169	64,535
	<u>73,646</u>	<u>83,410</u>	<u>73,646</u>	<u>83,410</u>

Deferred tax liabilities

The Group has no significant deferred tax liability.

4. CASH AT BANK AND ON HAND

	The Group 2006		
	Original currency '000	Exchange rate	Rmb/ Rmb/ equivalent '000
<i>Cash on hand</i>			
Renminbi			26
<i>Cash at bank</i>			
Renminbi			988,256
Hong Kong Dollars	631	1.005	634
US Dollars	1,099	7.809	8,584
			<u>997,500</u>
Cash at bank and on hand			997,500
Deposits with related companies			
Renminbi			61,763
			<u>61,763</u>
Cash and cash equivalents			<u>1,059,263</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

4. CASH AT BANK AND ON HAND (Continued)

	Original currency '000	The Group 2005 Exchange rate	Rmb/ Rmb equivalent '000
<i>Cash on hand</i>			
Renminbi			31
<i>Cash at bank</i>			
Renminbi			300,455
Hong Kong Dollars	2,738	1.040	2,848
US Dollars	365	8.070	2,946
Cash at bank and on hand			306,280
Deposits with related companies			
Renminbi			92,253
Cash and cash equivalents			<u>398,533</u>

As at 31 December 2006 and 2005, the time deposits held by the Group were not pledged as security.

	The Company 2006		Rmb/ Rmb equivalent '000
	Original currency '000	Exchange rate	
<i>Cash on hand</i>			
Renminbi			16
<i>Cash at bank</i>			
Renminbi			846,423
Hong Kong Dollars	137	1.005	138
US Dollars	1,086	7.809	8,484
Cash at bank and on hand			855,061
Deposits with related companies			
Renminbi			55,784
Cash and cash equivalents			<u>910,845</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

4. CASH AT BANK AND ON HAND (Continued)

	The Company 2005		Rmb/ Rmb equivalent '000
	Original currency '000	Exchange rate	
<i>Cash on hand</i>			
Renminbi			15
<i>Cash at bank</i>			
Renminbi			191,813
Hong Kong Dollars	136	1.040	141
US Dollars	62	8.070	497
			<hr/>
Cash at bank and on hand			192,466
Deposits with related companies			
Renminbi			89,481
			<hr/>
Cash and cash equivalents			<u>281,947</u>

The deposits with related companies represent deposits with China CITIC Bank and Sinopec Finance Company Limited ("Sinopec Finance"). Deposit interest is calculated at market rate. Details are set out in note 29.

5. BILLS RECEIVABLE

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Bank acceptance bills	<u>983,526</u>	<u>820,731</u>	<u>904,599</u>	<u>748,856</u>

As at 31 December 2006 and 2005, the above bank acceptance bills were not pledged.

Included in the above balances, there were no bills receivable due from shareholders who hold 5% or more of the voting shares of the Company.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

6. ACCOUNTS RECEIVABLE

The ageing analysis of accounts receivable is as follows:

	The Group							
	2006				2005			
	Amount Rmb'000	Percentage of total amount	Bad debt provision Rmb'000	Rate of provision %	Amount Rmb'000	Percentage of total amount	Bad debt provision Rmb'000	Rate of provision %
		%				%		
Within 1 year	301,092	93	-	-	184,730	85	-	-
Between 1 to 2 years	2,138	1	813	38	20,912	10	17,023	81
Between 2 to 3 years	16,621	5	16,403	99	3,819	2	3,190	84
Over 3 years	4,540	1	4,540	100	5,464	3	5,305	97
	<u>324,391</u>	100	<u>21,756</u>	7	<u>214,925</u>	100	<u>25,518</u>	12
Net balance	<u>302,635</u>				<u>189,407</u>			

	The Company							
	2006				2005			
	Amount Rmb'000	Percentage of total amount	Bad debt provision Rmb'000	Rate of provision %	Amount Rmb'000	Percentage of total amount	Bad debt provision Rmb'000	Rate of provision %
		%				%		
Within 1 year	296,315	100	-	-	169,692	98	-	-
Between 1 to 2 years	437	-	164	38	2,867	2	859	30
Between 2 to 3 years	46	-	46	100	371	-	223	60
Over 3 years	279	-	279	100	-	-	-	-
	<u>297,077</u>	100	<u>489</u>	-	<u>172,930</u>	100	<u>1,082</u>	1
Net balance	<u>296,588</u>				<u>171,848</u>			

The analysis of provision for bad and doubtful debts is as follows:

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Opening balance as at 1 January	25,518	28,088	1,082	9,996
Add: Charge for the year	1,157	6,744	-	392
Less: Reversal during the year	1,017	-	593	-
Write-off during the year	3,047	9,314	-	9,306
Transfer out due to disposal of a subsidiary	855	-	-	-
Closing balance as at 31 December	<u>21,756</u>	<u>25,518</u>	<u>489</u>	<u>1,082</u>

During the year ended 31 December 2006, the Group and the Company had no individually significant accounts receivable been fully or substantially provided for.

During the year ended 31 December 2006, the Group and the Company had no individually significant write off or write back of bad and doubtful debts which had been fully or substantially provided for in the prior years.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

6. ACCOUNTS RECEIVABLE (Continued)

Accounts receivable due from shareholders who hold 5% or more of the voting shares of the Company are disclosed in note 29.

As at 31 December 2006, the amount and proportion of the Group's five largest accounts receivable over the total accounts receivable were as follows:

	2006 Rmb'000	2005 Rmb'000
Total of the five largest accounts receivable	144,149	110,928
Proportion over the total accounts receivable	44%	52%

7. OTHER RECEIVABLES

The ageing analysis of other receivables is as follows:

	The Group							
	2006		Bad debt provision Rmb'000	Rate of provision %	2005		Bad debt provision Rmb'000	Rate of provision %
Amount Rmb'000	Percentage of total amount %	Amount Rmb'000			Percentage of total amount %			
Within 1 year	70,699	69	-	-	101,096	73	-	-
Between 1 to 2 years	4,740	5	-	-	4,593	3	-	-
Between 2 to 3 years	87	-	-	-	238	-	-	-
Over 3 years	26,603	26	21,221	80	33,199	24	27,245	82
	102,129	100	21,221	21	139,126	100	27,245	20
Net balance	80,908				111,881			

	The Company							
	2006		Bad debt provision Rmb'000	Rate of provision %	2005		Bad debt provision Rmb'000	Rate of provision %
Amount Rmb'000	Percentage of total amount %	Amount Rmb'000			Percentage of total amount %			
Within 1 year	69,666	50	-	-	310,767	80	-	-
Between 1 to 2 years	235	-	-	-	4,455	1	-	-
Between 2 to 3 years	87	-	-	-	238	-	-	-
Over 3 years	69,823	50	69,823	100	73,589	19	69,823	95
	139,811	100	69,823	50	389,049	100	69,823	18
Net balance	69,988				319,226			

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

7. OTHER RECEIVABLES (Continued)

The analysis of provision for bad and doubtful debts is as follows:

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Opening balance as at 1 January	27,245	27,240	69,823	69,823
Add: Charge for the year	2,814	5	2,245	–
Less: Write-off during the year	2,250	–	2,245	–
Transfer out due to disposal of a subsidiary	6,588	–	–	–
Closing balance as at 31 December	<u>21,221</u>	<u>27,245</u>	<u>69,823</u>	<u>69,823</u>

During the year ended 31 December 2006, the Group and the Company had no individually significant other receivables been fully or substantially provided for.

During the year ended 31 December 2006, the Group and the Company had no individually significant write off or write back of bad and doubtful debts which had been fully or substantially provided for in the prior years.

Other receivables due from shareholders who hold 5% or more of the voting shares of the Company are disclosed in note 29.

As at 31 December 2006, the amount and proportion of the Group's five largest other receivables over the total other receivables were as follows:

	2006 Rmb'000	2005 Rmb'000
Total of the five largest other receivables	<u>70,502</u>	<u>93,961</u>
Proportion over the total other receivables	<u>69%</u>	<u>68%</u>

8. PAYMENTS IN ADVANCE

All payments in advance aged within one year.

Balances due from shareholders who hold 5% or more of the voting shares of the Company are disclosed in note 29.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

9. INVENTORIES

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Raw materials	534,986	659,803	531,195	621,110
Work in progress	100,382	118,725	97,650	111,307
Finished goods	293,719	334,296	241,001	254,863
Goods in transit	326,972	23,301	326,972	23,301
Spare parts and consumables	186,779	232,261	182,195	205,180
	<u>1,442,838</u>	<u>1,368,386</u>	<u>1,379,013</u>	<u>1,215,761</u>
Less: Provision for diminution in value of inventories				
Raw materials	4,974	11,197	4,600	4,600
Finished goods	5,571	5,513	4,523	4,523
Spare parts and consumables	48,740	63,740	48,740	48,740
	<u>59,285</u>	<u>80,450</u>	<u>57,863</u>	<u>57,863</u>
	<u>1,383,553</u>	<u>1,287,936</u>	<u>1,321,150</u>	<u>1,157,898</u>

Provision for diminution in value of inventories:

	The Group			
	Raw materials Rmb'000	Finished goods Rmb'000	Spare parts and consumables Rmb'000	Total Rmb'000
As at 1 January 2006	11,197	5,513	63,740	80,450
Add: Provision made during the year	16,001	18,481	4,000	38,482
Less: Transfer out due to sales during the year	17,945	17,316	-	35,261
Transfer out due to disposal of a subsidiary	4,279	1,107	19,000	24,386
As at 31 December 2006	<u>4,974</u>	<u>5,571</u>	<u>48,740</u>	<u>59,285</u>

	The Company			
	Raw materials Rmb'000	Finished goods Rmb'000	Spare parts and consumables Rmb'000	Total Rmb'000
As at 1 January 2006	4,600	4,523	48,740	57,863
Add: Provision made during the year	10,440	13,433	-	23,873
Less: Transfer out due to sales during the year	10,440	13,433	-	23,873
As at 31 December 2006	<u>4,600</u>	<u>4,523</u>	<u>48,740</u>	<u>57,863</u>

All the above inventories are purchased from others or self-manufactured.

During the year ended 31 December 2006, the Group and the Company recognised the cost of inventories as costs and expenses, are Rmb 16,453,959,000 (2005: Rmb 15,269,720,000) and Rmb 15,762,953,000 (2005: Rmb 14,292,629,000) respectively.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS

Long-term equity investments

	The Group Other unlisted equity investment
	Rmb'000 note (b(i))
As at 1 January 2006	62,500
Decrease during the year	(62,500)
As at 31 December 2006	-

	The Company			Total
	Investments in subsidiaries	Investment in a jointly controlled entity	Other unlisted equity investment	
	Rmb'000 note (a)	Rmb'000 note (a)	Rmb'000 note (b(i))	Rmb'000
As at 1 January 2006	179,584	110,103	62,500	352,187
Increase in investment cost	3,456	120,252	-	123,708
Investment income accounted for under the equity method	39,562	(38,339)	-	1,223
Decrease during the year	(1,915)	-	(62,500)	(64,415)
As at 31 December 2006	220,687	192,016	-	412,703

- (a) The particulars of the major subsidiary and the jointly controlled entity, both of which are companies established and operating in the PRC, which principally affected the results or assets of the Group as at 31 December 2006 are as follows:

Name of company	Registered capital '000	Percentage of equity held		Types of legal entity	Principal activity	Registered place
		directly by the Company	by subsidiary			
Subsidiary						
Yihua Kangqi Chemical Fibre Company Limited ("Yihua Kangqi") (i)	Rmb 60,000	100%	-	Limited company	Investment holding and trading of polyester chips and polyester fibre	Jiangsu, PRC
Jointly controlled entity						
Yihua UNIFI (ii)	USD 60,000	50%	-	Limited company	Manufacturing and processing of differentiated polyester textile filament products; conducting research in polyethylene textile products; sales of self-produced products; and provision of after-sales service	Jiangsu, PRC

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS (Continued)

(a) The particulars of the major subsidiary and the jointly controlled entity, both of which are companies established and operating in the PRC, which principally affected the results or assets of the Group as at 31 December 2006 are as follows: (Continued)

- (i) Pursuant to the equity transfer agreement signed on 8 September 2006, Yizheng Chemical Fibre Investment Management Company Limited, a subsidiary of Yihua Group, sold 5% equity interest in Yihua Kangqi to the Company. The purchase cost of the investment was Rmb 6,652,000 and an equity-investment difference of Rmb 3,196,000 arose accordingly. Management considered that the above equity-investment difference would not generate future profit for the Company, and fully amortised it in 2006 (note 26). After this equity transfer, the percentage of the Company's equity interest in Yihua Kangqi increased from 95% to 100%.
- (ii) Pursuant to the equity joint venture contract signed between the Company and UNIFI Asia Holding SRL ("**UNIFI Asia**") dated 10 June 2005 and Yihua UNIFI's board resolution dated 7 June 2006, the Company and UNIFI Asia, had agreed to convert the amounts of Rmb 120,252,000 (equivalent to USD15,000,000) and USD 15,000,000 respectively due from Yihua UNIFI to Yihua UNIFI's paid in capital. The registered capital of Yihua UNIFI was increased from USD 30,000,000 to USD 60,000,000. Yue Hua Certified Public Accountants has verified the above capital contributions, and issued related capital verification report on 25 July 2006 (Yue Hua Su Yan Zi [2006] No. 013).
- (iii) In view of the current market condition of the polyester fibre industry, the Group disposed of its entire equity interests in Foshan Chemical Fibre United Company Limited and Foshan Tianma Chemical Fibre Company Limited ("**Tianma Chemical Fibre**").

(b) **Other unlisted equity investment**

- (i) Pursuant to the equity transfer agreement dated 20 March 2006, the Company sold its entire 2% equity interest in Sinopec Finance to CPC for a cash consideration of Rmb 82,000,000. The consideration was based on the audited shareholders' funds of Sinopec Finance attributable to the Company as at 30 September 2005 (approximately Rmb 82 million). The gain on disposal of the investment is Rmb 19,500,000 (note 29(c)), which has been recognised in the Group's and the Company's income statements for the year ended 31 December 2006.
- (ii) Pursuant to the equity transfer agreement dated 26 March 2006, Yihua Kangqi, a subsidiary of the Company, sold its 5% equity interest in each of Yizheng Chemical Fibre Ningbo Kangqi Co., Ltd. and Yizheng Chemical Fibre Qindao Kangqi Co., Ltd. to their minority shareholders for a cash consideration of Rmb 1,505,000. The total gain on disposal of these investments is Rmb 655,000, which has been recognised in the Group's income statement for the year ended 31 December 2006.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS (Continued)

(c) Receivables due after 1 year

	The Company
	Rmb'000
Amount due from a subsidiary:	
Cost	
As at 1 January 2006	800,000
Disposal during the year	(800,000)
	<hr/>
As at 31 December 2006	-

Less: Provision for impairment	
As at 1 January 2006	(797,288)
Written back during the year	10,628
Disposal during the year	786,660
	<hr/>
As at 31 December 2006	-

Carrying amount	
As at 31 December 2006	-
	<hr/> <hr/>
As at 31 December 2005	2,712
	<hr/> <hr/>

The Company has advanced Rmb 800 million to Tianma Chemical Fibre to support its operating working capital on a going concern basis.

The Group's management made a decision on 28 October 2005 to dispose of its entire equity interest in Tianma Chemical Fibre together with the amount due from Tianma Chemical Fibre. Based on management's assessment of the recoverable amount, determined by reference to the selling price agreed with two independent third-party co-purchasers in the conditional sale and purchase agreement dated 24 March 2006, the Company recognised a provision of Rmb 797,288,000 as at 31 December 2005. The provision included employee reduction expense of Rmb 67,000,000, which should be paid to Tianma Chemical Fibre's employees. Based on the negotiation result between the Company and the relevant local government authority in April 2006, the employee reduction expense paid and payable to Tianma Chemical Fibre's employees reduced from Rmb 67,000,000 to Rmb 52,924,000. The Company has written back the over-provision for impairment of Rmb 14,076,000 (note 27) in the income statement for the year ended 31 December 2006.

However, one of the purchasers revoked the above sale and purchase agreement and forfeited the deposit of Rmb 14,950,000 paid to the Group (included in "Non-operating income" (note 27)). On 14 August 2006, the Group entered into a new conditional sale and purchase agreement with the remaining purchaser mentioned above and two other new third-party purchasers to dispose of its 100% equity interest in Tianma Chemical Fibre together with the amount due from Tianma Chemical Fibre, with a net consideration of Rmb 189,450,000.

The disposal was approved by the Company's shareholders and directors. The Company also obtained the approval from the Ministry of Commerce of the People's Republic of China.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS (Continued)

(c) Receivables due after 1 year (Continued)

As at 14 August 2006 and 31 December of 2005, the assets and liabilities of Tianma Chemical Fibre were as follows:

	As at	2005
	14 August 2006	Rmb'000
	Rmb'000	Rmb'000
	(unaudited)	
Assets		
Current assets		
Cash at bank and on hand	13,424	15,680
Bills receivable	1,156	3,292
Accounts receivable	5,701	13,454
Other receivables	352	3,376
Payments in advance	7,429	1,072
Inventories	44,386	51,918
	<u>72,448</u>	<u>88,792</u>
Total current assets	-----	-----
Fixed assets		
Cost	1,137,693	1,102,297
Less: Accumulated depreciation	604,797	557,458
	<u>532,896</u>	<u>544,839</u>
Net book value before provision for impairment	532,896	544,839
Less: Provision for impairment of fixed assets	391,761	391,761
	<u>141,135</u>	<u>153,078</u>
Carrying amount	141,135	153,078
Construction in progress	1,748	1,748
	<u>142,883</u>	<u>154,826</u>
Total fixed assets	-----	-----
Total assets	-----	-----
	215,331	243,618
Liabilities		
Short-term loans	-	35,091
Bills payable	-	5,501
Accounts payable	8,049	3,464
Receipts in advance	10,486	6,191
Accrued payroll	1,547	-
Taxes payable	1,844	2,898
Other creditors	2,035	2,444
	<u>23,961</u>	<u>55,589</u>
Total liabilities	-----	-----
Net assets	<u>191,370</u>	<u>188,029</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS (Continued)

(c) Receivables due after 1 year (Continued)

The results of operations of Tianma Chemical Fibre for the period from 1 January 2006 to 14 August 2006 and for the year ended 31 December 2005 were as follows:

	For the period ended 14 August 2006	2005
	Rmb'000	Rmb'000
	(unaudited)	
Sales from principal activities	261,874	796,873
Less: Cost of sales from principal activities	<u>273,585</u>	<u>830,450</u>
Loss from principal activities	(11,711)	(33,577)
Add: Profit from other operations	1,228	4,031
Less: Operating expenses	1,475	2,793
General and administrative expenses	9,748	28,847
Financial expenses	<u>4,330</u>	<u>8,987</u>
Operating loss	(26,036)	(70,173)
Add: Non-operating income	194	34
Less: Non-operating expenses	<u>1,188</u>	<u>391,902</u>
Loss before income tax	(27,030)	(462,041)
Less: Income tax	<u>-</u>	<u>-</u>
Net loss for the period/year	<u>(27,030)</u>	<u>(462,041)</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

10. LONG-TERM INVESTMENTS (Continued)

(c) Receivables due after 1 year (Continued)

Net loss from disposal of Tianma Chemical Fibre is as follows:

	The Group
	2006
	Rmb'000
Consideration	
Cash	23,050
Bills receivable	139,860
Other receivables	26,540
	<hr/>
	189,450
	<hr/>
Less: Net assets of Tianma Chemical Fibre as at 14 August 2006	191,370
	<hr/>
Net loss	<u>(1,920)</u>
	<hr/>
	The Company
	2006
	Rmb'000
Consideration	
Cash	23,050
Bills receivable	139,860
Other receivables	26,540
	<hr/>
	189,450
	<hr/>
Less: Receivables due after 1 year as at 14 August 2006	
– Cost	800,000
– Provision	(786,660)
Other receivables	178,030
	<hr/>
	191,370
	<hr/>
Net loss	<u>(1,920)</u>
	<hr/>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

11. FIXED ASSETS

	The Group			Total Rmb'000
	Land and buildings Rmb'000	Machinery equipment Rmb'000	Motor vehicles and other fixed assets Rmb'000	
Cost or valuation:				
As at 1 January 2006	2,521,772	10,993,552	549,133	14,064,457
Additions				
– attributable to the jointly controlled entity	–	10	–	10
– others	–	45,759	10,009	55,768
Transferred from construction in progress (note 12)				
– attributable to the jointly controlled entity	867	2,105	494	3,466
– others	8,794	153,984	30,146	192,924
Reclassifications (note (d))	190,557	(503,052)	312,495	–
Disposals				
– attributable to the jointly controlled entity	–	–	(250)	(250)
– transfer out due to disposal of a subsidiary	(284,337)	(819,766)	(33,590)	(1,137,693)
– others	(21,576)	(46,335)	(73,807)	(141,718)
As at 31 December 2006	2,416,077	9,826,257	794,630	13,036,964
Accumulated depreciation:				
As at 1 January 2006	824,395	5,812,102	515,808	7,152,305
Charge for the year	96,856	526,463	64,383	687,702
Reclassifications (note (d))	16,980	(80,013)	63,033	–
Written back on disposal				
– attributable to the jointly controlled entity	–	–	(15)	(15)
– transfer out due to disposal of a subsidiary	(83,255)	(495,495)	(26,047)	(604,797)
– others	(6,203)	(35,316)	(57,244)	(98,763)
As at 31 December 2006	848,773	5,727,741	559,918	7,136,432
Provision for impairment:				
As at 1 January 2006	78,424	337,182	2,015	417,621
Write off on disposal				
– write off on disposal of a subsidiary	(77,971)	(312,520)	(1,270)	(391,761)
– others	(453)	(31)	(14)	(498)
As at 31 December 2006	–	24,631	731	25,362
Carrying amount:				
As at 31 December 2006	1,567,304	4,073,885	233,981	5,875,170
As at 31 December 2005	1,618,953	4,844,268	31,310	6,494,531

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

11. FIXED ASSETS (Continued)

	The Company			Total Rmb'000
	Land and buildings Rmb'000	Machinery equipment Rmb'000	Motor vehicles and other fixed assets Rmb'000	
Cost or valuation:				
As at 1 January 2006	2,140,307	10,003,335	492,142	12,635,784
Additions	–	42,030	9,796	51,826
Transferred from construction in progress (note 12)	8,794	153,984	30,146	192,924
Reclassifications (note (d))	190,557	(503,052)	312,495	–
Disposals	(5,031)	(46,335)	(65,627)	(116,993)
As at 31 December 2006	<u>2,334,627</u>	<u>9,649,962</u>	<u>778,952</u>	<u>12,763,541</u>
Accumulated depreciation:				
As at 1 January 2006	735,212	5,317,057	484,064	6,536,333
Charge for the year	89,720	506,993	61,932	658,645
Reclassifications (note (d))	16,980	(80,013)	63,033	–
Written back on disposal	(1,019)	(35,316)	(56,715)	(93,050)
As at 31 December 2006	<u>840,893</u>	<u>5,708,721</u>	<u>552,314</u>	<u>7,101,928</u>
Provision for impairment:				
As at 1 January 2006	453	24,662	745	25,860
Write off on disposal	(453)	(31)	(14)	(498)
As at 31 December 2006	<u>–</u>	<u>24,631</u>	<u>731</u>	<u>25,362</u>
Carrying amount:				
As at 31 December 2006	<u>1,493,734</u>	<u>3,916,610</u>	<u>225,907</u>	<u>5,636,251</u>
As at 31 December 2005	<u>1,404,642</u>	<u>4,661,616</u>	<u>7,333</u>	<u>6,073,591</u>

(a) All the Group's buildings are located in the PRC.

(b) As at 31 December 2006, the original cost of fully depreciated fixed assets in use was Rmb 1,773,866,000 (2005:Rmb 1,008,286,000).

(c) The Group obtained land use rights through purchase and contribution from its shareholder.

(d) Pursuant to the finalised completion report of the 450,000-tonne PTA plant and its associated projects ("completion report of the 450,000-tonne PTA plant"), the Company reclassified the original estimated cost of fixed assets and recalculated depreciation accordingly during the year ended 31 December 2006.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

12. CONSTRUCTION IN PROGRESS

As at 31 December 2006, the Group's and the Company's major construction in progress were as follows:

Project	Budgeted amount Rmb'000	Balance as at	Additions Rmb'000	Transferred to fixed assets	Transferred out due to disposal of a subsidiary	Balance as at 31 December 2006	Source of fund	Percentage of completion	Interest capitalised during the year Rmb'000
		1 January 2006 Rmb'000		(Note 10)	(Note 10(c))	Rmb'000			
Improvement of air compression system of a power plant	16,825	14,693	1,427	(16,120)	-	-	Own fund	100%	-
Upgrade of ERP system	14,500	13,902	12	(13,914)	-	-	Own fund	100%	-
Upgrade of heat coal stove	9,928	3,936	4,063	-	-	7,999	Own fund	81%	-
Optimisation of supply chain	12,000	8,255	15	-	-	8,270	Own fund	69%	-
Improvements and expansion of existing plants and equipment	316,569	226,747	32,229	(161,208)	-	97,768	Own fund	82%	-
Other construction projects	3,775	1,682	-	(1,682)	-	-	Own fund	100%	-
Total for the Company		269,215	37,746	(192,924)	-	114,037			
Miscellaneous projects of the subsidiaries and the jointly controlled entity		1,748	11,247	(3,466)	(1,748)	7,781	Own fund	-	-
Total for the Group		270,963	48,993	(196,390)	(1,748)	121,818			

No borrowing costs of the Group for the year were capitalised in 2006 (2005: Rmb nil).

13. INTANGIBLE ASSETS

	Technology right Rmb'000	The Group Patent right Rmb'000	Total Rmb'000
Cost			
As at 1 January 2006	304,317	142,435	446,752
Disposal during the year (note (a))	(71,107)	-	(71,107)
As at 31 December 2006	233,210	142,435	375,645
Accumulated amortisation			
As at 1 January 2006	64,013	135,084	199,097
Charge for the year	21,212	1,377	22,589
Written back on disposal (note (a))	(14,966)	-	(14,966)
As at 31 December 2006	70,259	136,461	206,720
Carrying amount			
As at 31 December 2006	162,951	5,974	168,925
As at 1 January 2006	240,304	7,351	247,655

In 2005, the Group's jointly controlled entity, Yihua UNIFI, acquired technology licence for producing differentiated polyester filament products from UNIFI Manufacturing INC., and its remaining amortisation period is 39 years.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

13. INTANGIBLE ASSETS (Continued)

	Technology right Rmb'000	The Company Patent right Rmb'000	Total Rmb'000
Cost			
As at 1 January 2006	280,000	142,435	422,435
Disposal during the year (note (a))	(71,107)	-	(71,107)
As at 31 December 2006	208,893	142,435	351,328
Accumulated amortisation			
As at 1 January 2006	63,000	135,084	198,084
Charge for the year	19,857	1,377	21,234
Written back on disposal (note (a))	(14,966)	-	(14,966)
As at 31 December 2006	67,891	136,461	204,352
Carrying amount			
As at 31 December 2006	141,002	5,974	146,976
As at 1 January 2006	217,000	7,351	224,351

- (a) Pursuant to the completion report of the 450,000-tonne PTA plant, the Company revised the cost of technology right and recalculated the accumulated amortisation accordingly during 2006.
- (b) In 2004, the Company acquired technology licences to operate the 450,000-tonne PTA plant from third parties, and their average remaining amortisation period is 7 years.
- (c) The Company acquired patent rights from third parties in 2001 and 2005 respectively, and their average remaining amortisation period is 4 years.

14. SHORT-TERM LOANS

The Group's short-term loans were bank loans denominated in Renminbi, of which weighted average interest rates per annum were 3.3% as at 31 December 2006 (2005: 4.1%). All the Group's short-term bank loans are credit loans, unsecured and not guaranteed. As at 31 December 2006 and 31 December 2005, the Group and the Company had no significant overdue short-term bank loans.

Short-term bank loans from shareholders who hold 5% or more of the voting shares of the Company are disclosed in note 29.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

15. BILLS PAYABLE, ACCOUNTS PAYABLE, RECEIPTS IN ADVANCE AND OTHER CREDITORS

Bills payable are mainly issued for the purchase of raw materials, goods or products by the Group, with the repayment terms generally ranging from three to six months:

	The Group			
	2006		2005	
	Rmb'000	%	Rmb'000	%
Bills payable				
Bank acceptance bills	-	-	5,501	100

Bills payable aged within one year.

As at 31 December 2006, there was no individually significant balance aged over three years included in the Group's and the Company's accounts payable and other creditors.

As at 31 December 2006, there was no individually significant balance aged over one year included in the Group's and the Company's receipts in advance.

In the accounts of accounts payable, receipts in advance and other creditors, balances due to shareholders who hold 5% or more of the voting shares of the Company are disclosed in note 29.

16. OTHER PAYABLES

	Charge rate	The Group		The Company	
		2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Education surcharge	note 3(a)	1,965	22,386	1,768	21,759
Basic pension insurance		8,091	-	8,091	-
Unemployment insurance		867	-	867	-
Others		1,090	413	175	83
Total		12,013	22,799	10,901	21,842

17. ACCRUED EXPENSES

Accrued expenses represent interest accrual.

18. LONG-TERM LIABILITIES DUE WITHIN ONE YEAR

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Bank loans				
– Rmb loans (note 19)	-	90,000	-	90,000
Other long-term payables (note 20)	6,079	7,431	-	-
Total	6,079	97,431	-	90,000

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

19. LONG-TERM LOANS

Lender	Period	Interest rate	Interest type	The Group and the Company	
				2006 Rmb'000	2005 Rmb'000
Industrial and Commercial Bank of China	Due in 2006	4.94%~5.18%	Fixed	-	90,000
China Construction Bank	Due in 2007	4.94%~5.18%	Fixed	-	50,000
Total long-term bank loans				-	140,000
Less: Long-term bank loans (current portion) (note 18)				-	90,000
Long-term bank loans (long-term portion)				-	50,000

The above long-term bank loans are denominated in Renminbi.

The repayment terms of the long-term bank loans are as follows:

	The Group and the Company	
	2006 Rmb'000	2005 Rmb'000
Due within 1 year	-	90,000
Due between 1 to 2 years	-	50,000
Total	-	140,000

20. LONG-TERM PAYABLES

	The Group Payable for technology right Rmb'000
As at 1 January 2006	20,265
Repayment during 2006	(7,431)
Total	12,834
Less: Long-term payables due within 1 year (note 18)	(6,079)
	6,755

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

20. LONG-TERM PAYABLES (Continued)

According to the relevant contract, the repayment terms of the above long-term payables are as follows:

	The Group	
	2006	2005
	Rmb'000	Rmb'000
Due within 1 year	6,079	7,431
Due between 1 to 2 years	4,728	6,079
Due between 2 to 3 years	2,027	4,728
Due between 3 to 4 years	-	2,027
Total	<u>12,834</u>	<u>20,265</u>

In the above balance, there is no amount due to shareholders who hold 5% or more of the voting shares of the Company.

21. SHARE CAPITAL

	The Group and the Company	
	2006	2005
	Rmb'000	Rmb'000
Registered, issued and paid up capital:		
2,400,000,000 "Domestic non-public legal person A" shares of Rmb 1.00 each	2,400,000	2,400,000
200,000,000 "Social public A" shares of Rmb 1.00 each	200,000	200,000
1,400,000,000 "H" shares of Rmb 1.00 each	1,400,000	1,400,000
Total	<u>4,000,000</u>	<u>4,000,000</u>

All the "Domestic non-public legal person A", "Social public A" and "H" shares rank pari passu in all material respects.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

22. CAPITAL RESERVE

	The Group		
	As at 1 January 2006 Rmb'000	Addition during the year Rmb'000	As at 31 December 2006 Rmb'000
Share premium	3,078,825	–	3,078,825
Reserve for equity investment	9,644	–	9,644
Other capital reserve	15,068	13,271	28,339
Total	<u>3,103,537</u>	<u>13,271</u>	<u>3,116,808</u>

	The Company		
	As at 1 January 2006 Rmb'000	Addition during the year Rmb'000	As at 31 December 2006 Rmb'000
Share premium	3,078,825	–	3,078,825
Reserve for equity investment	19,289	–	19,289
Other capital reserve	15,068	13,271	28,339
Total	<u>3,113,182</u>	<u>13,271</u>	<u>3,126,453</u>

23. SURPLUS RESERVE

	The Group and the Company			Total Rmb'000
	Statutory surplus reserve Rmb'000	Statutory public welfare fund Rmb'000	Discretionary surplus reserve Rmb'000	
As at 1 January 2005 and as at 31 December 2005	513,046	348,411	594,547	1,456,004
Statutory public welfare fund transferred to statutory surplus reserve (note(b))	348,411	(348,411)	–	–
As at 31 December 2006	<u>861,457</u>	<u>–</u>	<u>594,547</u>	<u>1,456,004</u>

(a) Transfers from the distributable profits to the above surplus reserve were made in accordance with the relevant rules and regulations set out in the Company Law and the Articles of Association of the Company, its subsidiaries and its jointly controlled entity.

(b) Pursuant to the relevant requirements set out in No.167 of the Company Law which was effective since 1 January 2006, the Company, its subsidiaries and its jointly controlled entity are no longer required by law to make profit appropriations to the statutory public welfare fund.

Furthermore, in accordance with the relevant requirements set out in "Notice on accounting issues relating to the implementation of the Company Law" issued by the MOF of the PRC, the balance of the statutory public welfare fund amounting to Rmb 348,411,000 as at 31 December 2005 was transferred to the statutory surplus reserve.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

24. SALES AND COST OF SALES FROM PRINCIPAL ACTIVITIES

The Group and the Company are principally engaged in the production and sale of chemical fibre and chemical fibre raw materials. The Group's and the Company's sales and cost of sales from principal activities represent income earned and cost incurred in relation to sale of chemical fibre and chemical fibre raw materials.

The Group's profit is primarily attributable to the production and sales of chemical fibre and chemical fibre raw materials in the PRC. Accordingly, no segmental analysis is provided by the Group.

During the year ended 31 December 2006, revenue from sales to the top five customers is Rmb 1,419,000,000 (2005: Rmb 1,565,000,000) which accounts for 8% (2005: 10%) of the total sales from principal activities of the Group.

25. NET FINANCIAL INCOME/(FINANCIAL EXPENSES)

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Interest expense incurred	(14,820)	(60,129)	(7,887)	(54,365)
Interest income	17,541	4,509	14,935	9,816
Net exchange gains	2,075	1,356	2,063	67
Other financial expenses	(2,073)	(2,366)	(1,648)	(2,051)
Total	<u>2,723</u>	<u>(56,630)</u>	<u>7,463</u>	<u>(46,533)</u>

26. INVESTMENT INCOME/(LOSSES)

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Accounted for under the equity method (note 10)	-	-	1,223	(37,213)
Provision for impairment for receivables due after 1 year (note 10(c))	-	-	(42,296)	(499,179)
Gains on transfer of long-term equity investments	655	3,650	-	-
Amortisation of equity-investment difference (note 10(a))	(3,196)	-	(3,196)	-
Net gains on disposal of long-term investments	17,580	-	15,660	-
Decrease in equity-investment difference	-	29,341	-	29,341
Dividend from other equity investment	-	3,500	-	3,500
Total	<u>15,039</u>	<u>36,491</u>	<u>(28,609)</u>	<u>(503,551)</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

27. NON-OPERATING INCOME

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Forfeited deposit (note 10(c))	14,950	-	14,950	-
Write-back of employee reduction expenses over-accrued in prior year (note 10(c))	14,076	-	-	-
Compensation income	6,110	-	6,110	-
Gains on disposal of fixed assets	6,071	305	6,071	305
Safety security compensation income	-	19,652	-	19,652
Other	11,888	3,131	8,535	4,074
	53,095	23,088	35,666	24,031

28. NON-OPERATING EXPENSES

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Losses on disposal of fixed assets	25,467	29,272	18,439	29,093
Employee reduction expenses	10,450	90,939	10,404	23,939
Flood prevention fees	10,939	7,000	9,741	7,000
Compensation loss	3,000	-	3,000	-
Provision for impairment of fixed assets	-	783,621	-	391,860
Donations	400	500	400	500
Others	2,670	218	2,660	634
Total	52,926	911,550	44,644	453,026

In accordance with the Group's and the Company's employee reduction plans, the Group and the Company had incurred Rmb 10,450,000 and Rmb 10,404,000 respectively (2005: Rmb 90,939,000 and Rmb 23,939,000 respectively) on the reduction of 170 and 164 respectively (2005: 1,814 and 490 respectively) employees for the year ended 31 December 2006.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

29. RELATED PARTIES AND RELATED PARTY TRANSACTIONS

(a) Related party with controlling relationship

Name of Company:	Sinopec Corp
Registered Address:	No. 6 Hui Xin Dong Jie Jia, Chao Yang Qu, Beijing
Principal activities:	Exploring for, extracting and selling crude oil and natural gas; oil refining; production, sale and transport of petro-chemical, chemical fibres and other chemical products; pipe transport of crude oil and natural gas; research, development and application of new technologies and information
Relationship with the Company:	The immediate holding company
Types of legal entity:	Joint stock limited company
Legal representative:	Chen Tong-hai
Registered capital:	Rmb 86.7 billion

The above mentioned related party, having the ability to control the Group, has registered share capital of Rmb 86,702,439,000. There was no change during the year.

The equity interest held by the related party having the ability to control the Group is as follows:

	Number of shares	Percentage
As at 31 December 2006 and 2005	<u>1,680,000,000</u>	<u>42%</u>

The major related parties controlled by the Company are disclosed in note 10(a).

(b) Relationships between the Company and related parties without controlling relationships

Name of company	Relationship with the Company
CPC	Ultimate holding company
CITIC	Shareholder
Yihua	With a common ultimate holding company
Sinopec Yangzi Petrochemical Company Limited ("Yangzi")	With a common immediate holding company
Sinopec Finance	With a common ultimate holding company
China CITIC Bank	Subsidiary of CITIC
China Petroleum & Chemical Corporation, Zhenhai Branch ("Zhenhai")	With a common immediate holding company
Sinopec International Company Limited	With a common immediate holding company
Yihua UNIFI	Jointly controlled entity

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

29. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

(c) Significant transactions between the Group and the related parties are summarised as follows:

	2006 Rmb'000	2005 Rmb'000
Sinopec Corp and its subsidiaries		
Purchases of raw materials	8,431,148	6,519,226
Including: Yangzi	4,608,171	3,364,716
Zhenhai	3,005,402	2,637,487
Service charges for the purchases of raw materials	<u>23,971</u>	<u>19,226</u>
CPC and its subsidiaries (excluding Yihua and its subsidiaries ("Yihua Group"), Sinopec Corp and its subsidiaries and Sinopec Finance)		
Purchases of raw materials and spare parts	-	35,191
Insurance premium	18,765	25,730
Safety security compensation income	-	19,652
Investment income (note 10(b))	<u>19,500</u>	<u>-</u>
Yihua Group		
Sales	260,491	385,778
Purchases	-	113,070
Miscellaneous service fee charges (see note below)	11,654	20,000
Loss on acquisition of investment (note 10(a))	3,196	-
Gains on transfer of investment	<u>-</u>	<u>3,650</u>
Note: The above service fee charges were paid in accordance with the terms of the agreements dated 19 February 2005 and 20 January 2006 signed between the Company and Yihua.		
Sinopec Finance		
Interest income	872	79
Interest expense	<u>22</u>	<u>1,606</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

29. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

(c) Significant transactions between the Group and the related parties are summarised as follows: (Continued)

	2006 Rmb'000	2005 Rmb'000
China CITIC Bank		
Interest income	1,388	32
Interest expense	795	10,938
Bills custody fee	123	3,030
	<u>1,388</u>	<u>14,000</u>
Yihua UNIFI		
Sales of fixed assets	-	371,116
Sales of finished goods	414,178	232,098
Purchases of finished goods	101,279	36,769
	<u>515,457</u>	<u>639,983</u>

The Directors of the Company are of the opinion that the above transactions were carried out in the normal course of business and on normal commercial term.

(d) Deposits with and loans from Sinopec Finance

	2006 Rmb'000	2005 Rmb'000
Cash at bank	48,518	66,661
Short-term loans	10,000	-
	<u>58,518</u>	<u>66,661</u>

(e) Deposits with and loans from China CITIC Bank

	2006 Rmb'000	2005 Rmb'000
Cash at bank	13,245	25,592
Short-term loans	15,000	10,000
	<u>28,245</u>	<u>35,592</u>

(f) Details of amounts due from/(to) Yihua UNIFI are as follows:

	2006 Rmb'000	2005 Rmb'000
Accounts receivable	167	-
Other receivables	1,465	60,792
Payments in advance	1,523	1,260
Other creditors	(3,154)	-
	<u>1</u>	<u>62,052</u>

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

29. RELATED PARTIES AND RELATED PARTY TRANSACTIONS (Continued)

(g) Details of amounts due from/(to) CPC and its subsidiaries (excluding Yihua Group) are as follows:

	2006 Rmb'000	2005 Rmb'000
Amounts receivable	18,416	-
Payments in advance	63,983	6,533
Other receivables	431	1,747
Accounts payable	(76,457)	(30,633)
Other creditors	(1,612)	-
Receipts in advance	(161)	(862)
	<u>4,600</u>	<u>(23,215)</u>

(h) Details of amounts due from/(to) Yihua Group are as follows:

	2006 Rmb'000	2005 Rmb'000
Accounts receivable	3,704	5,157
Other receivables	20	6,650
Accounts payable	-	(12,740)
Receipts in advance	(7,233)	(3,459)
Other creditors	(5,045)	(10)
	<u>(8,554)</u>	<u>(4,402)</u>

30. CAPITAL COMMITMENTS

Capital commitments relate primarily to construction of building, plant, machinery and purchases of equipment. The Group and the Company had capital commitments outstanding as at 31 December 2006 as follows:

	The Group		The Company	
	2006 Rmb'000	2005 Rmb'000	2006 Rmb'000	2005 Rmb'000
Contracted for	-	-	-	121,584
Authorised but not contracted for	<u>81,590</u>	<u>186,358</u>	<u>81,590</u>	<u>186,358</u>
	<u>81,590</u>	<u>186,358</u>	<u>81,590</u>	<u>307,942</u>

31. CONTINGENCIES

The Group and the Company had no material contingencies as at 31 December 2006 and 2005.

Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

32. RETIREMENT BENEFITS

As stipulated by the regulations of the PRC, the Company and its jointly controlled entity in the PRC participate in basic defined contribution retirement schemes organised by their respective municipal governments under which they are governed. Details of these schemes of the Company and its jointly controlled entity – Yihua UNIFI, are as follows:

Administrator	Beneficiary	Contribution rate	
		2006	2005
Yizheng Municipal Government Jiangsu Province	Employees of the Company	20%	19%
Yizheng Municipal Government Jiangsu Province	Employees of Yihua UNIFI	20%	19%

All employees are entitled to retirement benefits equal to a fixed proportion of their salaries and benefits in kind prevailing at their normal retirement ages.

Other than the above, pursuant to a document "Lao Bu Fa [1995] No.464" dated 29 December 1995 issued by the Ministry of Labour of the PRC, the Company has set up a supplementary defined contribution retirement scheme for its employees. The assets of the scheme are held separately from those of the Company in an independent fund administered by representatives from the Company. The scheme is funded by contributions from the Company which are calculated at a rate based on the basic salaries of its employees. The contribution rate for 2006 was 9% (2005: 9%).

The Group has no other material obligation for payment of retirement benefits beyond the annual contributions which are calculated at a rate based on the salaries, bonuses and certain allowances of its employees as described above.

33. NON-RECURRING ITEMS

In accordance with "Standard questions and answers on the preparation of information disclosures by companies publicly issuing securities, No. 1 – Non-recurring items" (2004 Revised), the Group's and the Company's non-recurring items are summarised as follows:

	The Group	
	2006 Rmb'000	2005 Rmb'000
Non-recurring items for the year		
Net gains on disposal or transfer of long-term investments	(18,235)	–
Forfeited deposit	(14,950)	–
Write-back of employee reduction expenses over-accrued in prior year	(14,076)	–
Compensation income	(6,110)	–
Safety security compensation income	–	(19,652)
Other non-operating income (excluding forfeited deposit, write-back of employee reduction expenses over-accrued in prior year, compensation income, safety security compensation income and gains on disposal of fixed assets)	(11,888)	(3,134)
Net losses on disposal of fixed assets	19,396	28,967
Employee reduction expenses	10,450	90,939
Flood prevention fees	10,939	7,000
Compensation loss	3,000	–
Other non-operating expenses (excluding losses on disposal of fixed assets and employee reduction expenses, flood prevention fees, compensation loss and provision for impairment of fixed assets)	3,070	718
	(18,404)	104,838
Less: Tax effect on above items	2,761	(15,726)
Total	(15,643)	89,112



Notes on the Financial Statements

(Prepared in accordance with PRC Accounting Rules and Regulations)

33. NON-RECURRING ITEMS (Continued)

	The Company	
	2006 Rmb'000	2005 Rmb'000
Non-recurring items for the year		
Net gains on disposal of long-term investments	(15,660)	-
Forfeited deposit	(14,950)	-
Compensation income	(6,110)	-
Safety security compensation income	-	(19,652)
Other non-operating income (excluding forfeited deposit, compensation income, safety security compensation income, and gains on disposal of fixed assets)	(8,535)	(4,074)
Net losses on disposal of fixed assets	12,368	28,788
Employee reduction expenses	10,404	23,939
Flood prevention fees	9,741	7,000
Compensation loss	3,000	-
Other non-operating expenses (excluding losses on disposal of fixed assets and employee reduction expenses, flood prevention fees, compensation loss and provision for impairment of fixed assets)	3,060	1,134
	(6,682)	37,135
Less: Tax effect on above items	1,002	(5,570)
Total	(5,680)	31,565

34. POST BALANCE SHEET EVENT

- (a) With effect from 1 January 2007, the Company adopted the Accounting Standards for Business Enterprises issued by the MOF of the PRC on 15 February 2006 ("**New Accounting Standards**"); and it does not need to comply with the Accounting Standards for Business Enterprises and the Accounting Regulations for Business Enterprises ("**Existing Accounting Standards**"). After adopting the New Accounting Standards, the Company may change its accounting policies and accounting estimates based on the Existing Accounting Standards. Hence this may have effects on the financial position and the results of operations of the Company.
- (b) Pursuant to the PRC enterprise income tax law passed by the Fifth Plenary Session of the Tenth National People's Congress on 16 March 2007, the new enterprise income tax rates for domestic and foreign enterprises are unified at 25% and will be effective from 1 January 2008. The impact of such change of enterprise income tax rate on the Group's consolidated financial statements will depend on detailed pronouncements that are subsequently issued. Since implementation and transitional guidance applicable to the Group has not yet been announced, the Group cannot reasonably estimate the financial impact of the new tax law to the Group at this stage.