





# Chairman's Statement

Dear Shareholders,

On 22 August 2006, China National Coal Group Corporation established China Coal Energy Company Limited ("China Coal Energy" or the "Company") in the capacity of sole promoter. China Coal Energy was successfully listed on the Hong Kong Stock Exchange on 19 December 2006. In 2006, all businesses of the Company continued to grow rapidly and sustainably. The Company achieved outstanding operational results and have built up tremendous growth momentum thanks to the hard work and dedication by all members of staff. China Coal Energy firmly believes in the slogan "safety is of paramount importance, life is most valuable", and therefore, the Company strives to eliminate gas accidents in coal mines and major accidents which will result in casualties. The Company has maintained the rate of fatality per million tons of production at 0.076, which is much lower than the national average rate of fatality per million tons of production of 2.041. The Company highly values the harmonious development of the enterprise along with environmental protection. The Company exerts tremendous efforts in building mining areas that are designed to conserve resources and are environmentally friendly, and actively performs its social responsibility with a view to contributing to the building of a harmonious society.

I hereby present the 2006 annual report to all shareholders on behalf of the board of directors.

## Remarkable Financial Performance

China Coal Energy is the second largest coal enterprise in China. The Company reduced the cost of sales of coal and improved its profitability by increasing the production of raw coal and refining the coal sales structure, resulting in a remarkable improvement in the quality of corporate growth. For the year ended 31 December 2006, revenue of the Company was RMB30.227 billion. From the perspective of revenue composition, revenue from coal production and trading operations amounted to RMB23.832 billion, accounting for 78.8% of the total revenue, of which revenue from the sales of commercial coal amounted to RMB18.882 billion, representing an increase of 7.3% over last year; revenue from coking operations amounted to RMB2.035 billion, representing an increase of 27.9% over last year; revenue from coal mining equipment manufacturing operations amounted to RMB2.346 billion, representing an increase of 24.1% over last year; and revenue from coal mine design services and other operations amounted to RMB2.014 billion, representing an increase of 40.7% over last year.

The Company strives to lower costs. Aggregated cost of sales for the year 2006 amounted to RMB23.681 billion, representing a decrease of RMB757 million, or 3.1% from last year. The cost of sales for coal production and sales and coal trading amounted to RMB18.480 billion, representing a decrease of 9.4% from last year. The average unit cost of sales for coal from the Company's own mines amounted to RMB243.79 per ton, representing a decrease of RMB11.36 per ton, or 4.5% from last year. The average unit cost of sales of coal produced by the Pingshuo Mining Area was RMB193.27 per ton, representing a decrease of RMB23.23 per ton, or 10.7% from last year.

The Company has achieved favorable operating results due to the growth in revenue and cost reduction. Gross profit for 2006 was RMB6.546 billion, representing an increase of 16.4% over last year, of which gross profit from coal production and sales and coal trading operations amounted to RMB5.564 billion, representing an increase of 12.0% over last year. Earnings before interest, tax, depreciation and amortization (EBITDA) was RMB6.263 billion, representing an increase of 15.3% over last year; net profit amounted to RMB3.172 billion which exceeded the profit forecast target budgeted for 2006. Basic earnings per share was RMB0.39 while the rate of return on the shareholder's equity was 24.9%.



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China Coal Energy emphasizes the enhancement of shareholders' value. Prices of the Company's shares have been rising steadily since its listing. As at 31 December 2006, the total market capitalization of the Company amounted to HK\$59.253 billion, representing an increase of HK\$11.733 billion compared with the market capitalization of HK\$47.520 billion (valued at the issue price) on 19 December 2006 when the Company was listed, representing an increase of 24.7%, which surpassed the rise of the Hang Seng China Enterprises Index by 12.8% over the same period. The market capitalization of the Company as at 31 March 2007 was HK\$97.973 billion, representing a sharp rise of HK\$50.453 billion compared with the market capitalization of the Company on 19 December 2006 when the Company was listed, resulting in an appreciation rate of 106.2%, while the appreciation rate for the Hang Seng China Enterprises Index over the same period was 4.1%.

## The Company maintained its leading position in terms of growth in production capacity of coal

From 2003 to 2005, the coal production capacity of China Coal Energy had grown at an annual compound rate of 22.8%, setting the highest record in the PRC coal industry. In 2006 the Company has utilized its mining capacity in full, stepped up the construction of new projects, upgrade and renovation projects that enabled continuous rapid expansion of coal production volume. The annual raw coal production volume in 2006 was 79.04 million tons, of which coal from the Company's own mines was 66.49 million tons, representing an increase of 16.37 million tons or an increase of 32.7% compared with 50.12 million tons produced in 2005 and the growth rate in coal production volume continued to be at the top among national levels. Sales volume of commercial coal for the year was 88.45 million tons, of which coal from the Company's own mines was 57.15 million tons, representing an increase of 6.16 million tons. The Company improved the sales structure of coal to raise profit margin from sales. Gross profit margin for the production and trading in coal was 23.1%, representing an increase of 350 basis points over last year. EBITDA ratio of the Company was 20.7%, representing an increase of 260 basis points over last year.



Coal production in the Pingshuo Mining Area which is the largest mining area in the Jinbei coal base, reached 59.96 million tons, representing an increase of 15.25 million tons compared to last year, and production efficiency of the Pingshuo Mining Area continued to improve, with an average production efficiency reaching 92.5 tons per worker-shift, representing an increase of 17.2 tons per worker-shift, or 22.8% compared with the rate of last year. Amongst these mining areas, Anjialing Open Pit Mine and Antaibao Open Pit Mine maintained their reputation as safe and highly efficient premier mines. Monthly production for a single working panel in Anjialing underground coal mine exceeded 1 million tons.

As at 31 December 2006, the Company has proved and probable reserves of 3.513 billion tons and resources of 9.46 billion tons according to JORC standards, which provides a solid base for the continuous development of the Company's core coal business.

### Leading Coal Mining Equipment Manufacturer in China

The production volume of coal mining equipment of the Company in 2006 was approximately 160,000 tons, representing an increase of 14.3% over last year as the Company maintained its leading position in the domestic coal mining equipment manufacturing industry. The market shares of the Company for heavy duty curved armored face conveyors and hydraulic roof supports were 41% and 19% respectively, both having captured the top market shares amongst its peers. The Company succeeded in the development and manufacture of 3x855Kw and 3x1000Kw heavy duty curved armored face conveyors, of which the hourly conveyed volume of the 3x1000Kw



heavy duty curved armored face conveyor amounted to 4,500 tons, which currently is the most powerful conveyor in the world. The Company also succeeded in the development and manufacture of fully automatic coal ploughs for thin coal seams, which filled a market vacuum of such products produced in China and replaced the import of such products. The Company achieved a breakthrough in the sale of coal mining equipment, by exporting integrated sets of fully mechanized top caving equipment and technology to Russia. The Company also successfully acquired manufacturing technology, equipment and marketing channels from Parsons of the United Kingdom (英國帕森斯) which rendered the Company a leading global manufacturer of chains for mining use.

### The Largest Independent Coke Manufacturer in China

In 2006, production capacity of the Company for coke was 4.5 million tons, rendering the Company one of the top coke enterprises in China. Production volume of coke was 2.36 million tons, representing an increase of 67.5% over last year; export volume of coke was 0.6 million tons, which made the Company one of the top coke exporters in the country. Selling price of coke rebounded gradually, as a result of increasing demands from the steel industry. The Company believes that with its coke production facilities operating at full capacity, upgrading of the utilization of by-products from coke processing and extension of activities in different segments of the coke industry, its profit generating power in the coke business will continue to increase.



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## Immense Development Potential

The Company possesses ample reserves in coal resources. Its controlling shareholder, the China Coal Group, was granted the mining right in the Shuonan Mining Area in December 2006. The geological resources based on the reconnaissance survey was approximately 4 billion tons. The above mentioned resources may be developed by China Coal Energy directly, or may be injected into China Coal Energy after a new production facility has been built. In addition, China Coal Energy is arranging for 4 billion tons of coal resources for the ancillary chemical engineering of 3 million ton coal-based dimethylether in Erdos, which will provide assurance to the continuous development and enhance the efficiency of the Company.

The production volume of coal will increase rapidly. The Company will build on the foundation of rich coal resources, and focus on the core business of coal by increasing efforts in the building of a coal enterprise with a view to achieving an annual capacity of 100 million tons. The Company shall expand production capacity by focusing on the construction of key large scale coal mine projects, gradually acquiring local coal mines which have been acquired and consolidated by its controlling shareholder and participate in the development of superb quality overseas coal mines. In 2007, the Company's production capacity for coal is expected to reach 88.7 million tons. By 2008, production capacity for coal is expected to exceed 100 million tons. At present, the Company is in the process of renovating and expanding its mining facilities for the open pit mines at the Pingzhou Mining Area. Antaibao underground mine will commence production in 2007. Construction of the Eastern Open Pit Mine (東露天煤礦) will also commence during the year, construction work on the Wangjialing Mine of Huajin has officially commenced and the renovation and expansion project for Kongzhuang Mine at the Datun Mining Area is in progress, all of which will help lay a solid foundation for the Company's continuous development in the future.

The Company maintains its leadership position in the manufacturing of coal mining equipment. The growth in demand for coal in China has been very strong, which will drive the development of the coal mining equipment manufacturing sector. At the same time, the closing down of small coal mines in progress, the speeding up of elimination of outdated production facilities, the stepping up of the consolidation of coal resources in the country, the expansion in the scale of production by coal producing enterprises, the mechanization of coal mining technology and workflow by employing large machinery and the trend towards automation, all present development and growth opportunities for the China coal mining equipment manufacturing industry. Products of the Company including heavy duty curved armored face conveyors, hydraulic roof supports, coal ploughs for thin coal seam and mining chains, are all products with competitive advantages in the industry in China, laying down the solid foundation for achieving high yields and returns in the future. The Company aspires to upgrade the quality of mining machinery manufacturing in China, to strengthen research and development capability, and actively seeks new business opportunities for merger and acquisition and reorganization of related enterprises. The Company had reorganized Fushun Coal Mining Motor Plant and succeeded in establishing a foothold in the electric mining motor manufacturing industry. The Company endeavors to create a brand in the high end products by using its motto "The Top in China, First Class by global standards", and maintains its leading position in terms of market share in the domestic markets.





It is expected that the coal chemical industry will continue to establish a high standard and develop rapidly. The projects of China Coal Group in Heilongjiang are the coal-based methanol project and the coal mine oil shale retorting project. Preliminary works for the above projects have been completed as all necessary approvals have been obtained. In 2007, the Company will make direct investments to develop such projects, which will be another new business opportunity of the Company in the coal chemical industry. Pursuant to plans laid down by relevant departments of the PRC, China Coal Energy, with the support of the National Development and Reform Commission, will construct and develop 3 million tons of coal-based dimethylether ("DME") project in Erdos jointly with enterprises including China Petroleum & Chemical Corp and Shenenergy Group, so as to build an integrated project combining coal, chemical, electricity and transportation in a world class coal chemical project. That project has been classified as a national demonstration fuel project of coal-based methanol-dimethylether and a key construction project in the Inner Mongolia Autonomous Region. The overall development plan for this project will be completed by the Company during the year, causing the coal chemical industry to start growing rapidly at a high level. The above three coal chemical projects have gone through the corresponding preliminary procedures.

### Prospects

The Company believes the demand for energy will increase with the acceleration of industrialization, urbanization and modernization in China. The macro economy will continue its relatively fast development and there will be a sustained increase in economic growth. A diversified energy development based on coal resources is the fundamental policy and strategy of China's energy resource structure. Coal will maintain its fundamental role as the primary energy source for a long time and the coal industry in China is blessed with promising prospects, leaving plenty of room for rises in coal prices. As the second largest coal producer in China, China Coal Energy will strive to grow into a large internationally competitive energy company to achieve an annual production capacity of hundred-million tons during the 11th Five-Year Plan period. The Company shall focus on the development of the core coal business, mobilize its competitive edge in being the most comprehensive production chain with unique characteristics of the industry, raise its core competitive strengths, expand and strengthen its core businesses, emphasize on the comprehensive utilization of coal resources, implement the strategy of raw coal production as the core business while extending to and upgrading the coal chemical investments; to strengthen its management structure, system building and continuously improve the quality of corporate governance so as to implement refined management, strengthen its ability to improve efficiency and create favorable returns to its shareholders.

JING Tianliang  
Chairman  
Beijing, the PRC  
17 April 2007