NOTES TO FINANCIAL STATEMENTS

1 CORPORATE INFORMATION

The Company was established in the People's Republic of China (the "PRC") on 3 July 2000 as a limited liability company under the name of CNOOC Chemical Limited (中海石油化學有限公司). The Company's name was changed to China BlueChemical Ltd. (中海石油化學股份有限公司) on 25 April 2006. The registered office of the Company is located at No. 1 Zhu Jiang South Street, Dongfang City, Hainan Province, the PRC.

Pursuant to a reorganisation notice, dated 13 February 2006, from its ultimate holding company, CNOOC, and a promotion agreement (the "Promotion Agreement") entered into between CNOOC and the Other Four Promoters (as defined hereinafter) dated 18 March 2006, details of which are further explained below, the Company underwent a corporate reorganisation (the "Reorganisation") to rationalise its business and to reorganise itself into a joint stock limited company. The Reorganisation involved the following steps:

(a) Pursuant to a reorganisation notice issued by CNOOC dated 13 February 2006, equity interests owned by the Company's wholly-owned fellow subsidiaries in the following companies (the "Relevant Companies") were transferred, effective on 31 December 2005 to the Company. These equity interests were transferred to the Company at an aggregate value of RMB15,777,000, representing the aggregate of the respective share of the net assets value, as determined in accordance with the PRC Accounting Standards for Business Enterprises and PRC Accounting System for Business Enterprises ("PRC GAAP"), in the Relevant Companies by these wholly-owned fellow subsidiaries as at 31 December 2005. The transfer of the equity interests in the Relevant Companies to the Company was treated as an additional capital contribution to the Company from CNOOC with an effective date of 31 December 2005.

	Percentage of equity interests transferred
Hainan CNOOC Plastic Company Limited ("Plastic Co.")	30.23%
Transportation Co.	40%
CNOOC (Hainan) E&P Gas Limited ("E&P Gas")	60%

As CNOOC ultimately controlled the Relevant Companies before the Reorganisation and continues to have ultimate control over the Group after the Reorganisation, the transfer of the equity interests in the Relevant Companies from the Company's wholly-owned fellow subsidiaries has been accounted for as a reorganisation of entities under common control in a manner similar to pooling of interests. As a consequence of the aforesaid transfer and after considering the equity interests already held by the Company in the Relevant Companies, Plastic Co. and Transportation Co. had been accounted for as a wholly-owned subsidiary and a 90%-owned subsidiary of the Company, respectively, from the outset while E&P Gas had been accounted for as a wholly-owned subsidiary of the Company since its establishment on 8 November 2004.

In addition, pursuant to the aforesaid reorganisation notice, the Company transferred its entire equity interests of 9.21%, 60% and 84% in Sanya Resort Co., Ltd., Haiwan Fudao Hotel and Hainan CNOOC Agriculture Co., Ltd., respectively at an aggregate value of RMB45,323,000, representing the aggregate of the Company's total costs of investment in Sanya Resort Co., Ltd. and Haiwan Fudao Hotel, and the Company's share of net assets value, as determined in accordance with PRC GAAP, in Hainan CNOOC Agriculture Co., Ltd. as at 31 December 2005, to a wholly-owned fellow subsidiary of the Company. The Company's investment in Sanya Resort Co., Ltd. and Haiwan Fudao Hotel were accounted for as available-for-sale equity investments while Hainan CNOOC Agriculture Co., Ltd. was accounted for as a subsidiary of the Company prior to the above transfer. Although the Group held a 60% equity interest in Haiwan Fudao Hotel, the Group had no effective control over Haiwan Fudao Hotel and therefore Haiwan Fudao Hotel has not been accounted for as a subsidiary of the Company.

The transfer of equity interests in the aforesaid companies to the Company's wholly-owned fellow subsidiary was treated as a reduction in capital contribution to the Company from CNOOC with an effective date of 31 December 2005.

(b) Pursuant to an equity transfer agreement dated 28 February 2006, the Company acquired a 30% equity interest in Hainan CNOOC Complex Fertiliser Co., Ltd. ("Complex Fertiliser") at a cash consideration of RMB2,363,000 from Hainan Agricultural Means of Production Group Limited. Pursuant to a resolution of the employee shareholders of Complex Fertiliser, who together held a 34.95% equity interest in Complex Fertiliser dated 6 March 2006, the Company acquired the 34.95% equity interest in Complex Fertiliser at a cash consideration of RMB2,752,000 from the employee shareholders of Complex Fertiliser. As a consequence of the above acquisitions, Complex Fertiliser became a wholly-owned subsidiary of the Company.

(c) Pursuant to the Promotion Agreement entered into among

Zhejiang AMP Incorporation, Guangdong Agricultural Means of Production Corporation, Shanghai Municipal Agricultural Means of Production Corporation and Transammonia Inc., (together the "Other Four Promoters") and CNOOC in relation to the reorganisation of the Company into a joint stock limited company dated 18 March 2006, each of the Other Four Promoters transferred their entire shareholding of 3.24% each in CNOOC Fudao Co., Limited ("Fudao") to the Company in exchange for a 0.83% equity interest each in the Company upon its reorganisation into a joint stock limited company. Upon the completion of the exchange of shares, Fudao became a wholly-owned subsidiary of the Company.

(d) Pursuant to an approval document Guo Zi Gai Ge [2006] No. 462 issued by the State-owned Assets Supervision and Administration Commission ("SASAC") of the State Council on 24 April 2006, the Company was reorganised into a joint stock limited company with a registered share capital of RMB3,000,000,000 on 25 April 2006. The name of the Company was also changed from CNOOC Chemical Limited to China BlueChemical Ltd. on the same date.

In September and October 2006, the Company issued an aggregate 1,610,000,000 new H shares at a price of HK$1.90 per share to the public and such H shares were listed on the Main Board of the Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Further details are set out in note 30 to the financial statements.

The Group is principally engaged in the manufacture and sale of fertilisers and methanol.

In the opinion of the directors, the ultimate holding company of the Company is CNOOC, a state-owned enterprise established in the PRC.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), which comprise standards and interpretations approved by the International Accounting Standards Board, and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee that remain in effect and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for derivative financial instruments and certain equity investments, which have been measured at fair value. These financial statements have been presented in Renminbi and all values are rounded to the nearest thousand (RMB'000) except otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company, its subsidiaries and jointly-controlled entity for the year ended 31 December 2006.

Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group.

The Group's interest in its jointly-controlled entity is accounted for by proportionate consolidation from the date on which joint control over the jointly-controlled entity are established, which involves recognising in the consolidated financial statements a proportionate share of the jointly-controlled entity's assets, liabilities, income and expenses with similar items on a line-by-line basis.

All significant intercompany transactions and balances, including any unrealised profits arising from intercompany transactions, have been eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the subsidiaries of the Company. Acquisitions of minority interests are accounted for using the entity concept method.

2.2 IMPACT OF NEW AND AMENDED IFRS

The principal accounting policies and basis of preparation used in the preparation of these financial statements are consistent with those adopted by the Group in preparing its financial statements for the year ended 31 December 2005, except that the Group has adopted the following new and amended IFRS and International Financial Reporting Interpretations ("IFRIC") during the year. Adoption of these revised standards and interpretations did not have any material effect on these financial statements of the Group.

IAS 1 and IAS 19 Amendments	Actuarial Gains and Losses, Group Plans and Disclosures
IAS 21 Amendment	The Effects of Changes in ForeignExchange Rates
IAS 39 Amendment	Cash Flow Hedge Accounting of Forecast Intra-group Transactions
IAS 39 Amendment	The Fair Value Option
IAS 39 and IFRS 4 Amendments	Financial Guarantee Contracts
IFRS 6	Exploration for and Evaluation of Mineral Resources
IFRIC 4	Determining whether an Arrangement Contains a Lease

2.2 IMPACT OF NEW AND AMENDED IFRS (continued)

IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
IFRIC 6	Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment

The principal changes in accounting policies are as follows:

(a) IAS 1 and IAS 19 Amendments *Actuarial Gains and Losses, Group Plans and Disclosures*

The amendment has allowed a new option to recognise actuarial gains and losses outside of the profit or loss (i.e. through equity), in addition to the previous options of recognising such gains and losses directly in profit or loss or using the corridor approach. This change has had no effect on these financial statements.

(b) IAS 21 Amendment *The Effects of Changes in Foreign Exchange Rates*

Upon the adoption of IAS 21 Amendment regarding a net investment in a foreign operation, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements irrespective of the currency in which the monetary item is denominated. As the Group currently has no such transactions, the amendment has had no effect on these financial statements.

(c) IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS4 *Insurance Contracts*

(i) *Amendment for Cash Flow Hedge Accounting of Forecast Intra-group Transactions*

This amendment has revised IAS 39 to permit the foreign currency risk of a highly probable intra-group forecast transaction to qualify as a hedged item in a cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the consolidated income statement. As the Group currently has no such transactions, the amendment has had no effect on these financial statements.

(ii)*Amendment for The Fair Value Option*

This amendment has changed the definition of a financial instrument classified as fair value through profit or loss and has restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through the income statement. The Group had not previously used this option, and hence the amendment has had no effect on these financial statements.

(iii)*Amendment for Financial Guarantee Contracts*

This amendment has revised the scope of IAS 39 to require financial guarantee contracts issued that are not considered insurance contracts, to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with IAS 37 *Provisions*, *Contingent Liabilities and Contingent Assets* and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 *Revenue*. The adoption of this amendment has had no material impact on these financial statements.

(d) IFRS 6 *Exploration for and Evaluation of Mineral Resources*

IFRS 6 has provided interim guidance for accounting for expenditures incurred in the exploration for and evaluation of mineral resources, while the IASB continues its project on extractive industries. IFRS 6 is limited to considering the nature of such costs that may be capitalised as assets and the facts and circumstances which indicate when such assets may be impaired and the level at which impairment is assessed. As the Group currently has no such transactions, IFRS 6 has had no effect on these financial statements.

(e) IFRIC 4 *Determining whether an Arrangement Contains a Lease*

The Group has adopted this interpretation as of 1 January 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial statements.

(f) IFRIC 5 *Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*

IFRIC 5 has set out the accounting treatment for interests in funds established to finance the decommissioning or restoration of assets or environmental rehabilitation (decommissioning costs). As the Group currently has no such transactions, this interpretation has had no effect on these financial statements.

(g) IFRIC 6 *Liabilities arising from Participating in a Specific Market-Waste Electrical and Electronic Equipment*

This interpretation has required that liabilities relating to waste management in respect of sales of historical household equipment as defined in the European Union Directive on Waste Electrical and Electronic Equipment to be recognised when the entity participates in the market during the relevant measurement period. As the Group currently has no such transactions, this interpretation has had no effect on these financial statements.

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE IFRS

The Group has not applied the following new and revised IFRS, that have been issued but are not yet effective, in these financial statements.

IAS 1 Amendment	Capital Disclosures
IFRS 7	Financial Instruments: Disclosures
IFRS 8	Operating Segments
IFRIC 7	Applying the Restatement Approach under IAS 29 *Financial Reporting in Hyperinflationary Economies*
IFRIC 8	Scope of IFRS 2
IFRIC 9	Reassessment of Embedded Derivatives
IFRIC 10	Interim Financial Reporting and Impairment
IFRIC 11	IFRS 2- Group and Treasury Share Transactions
IFRIC 12	Service Concession Arrangements

The IAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

IFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. The standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments and also incorporates many of the disclosure requirements of IAS 32.

IFRS 8 will replace IAS 14 *Segment Reporting* and has adopted a management approach to segment reporting. This IFRS shall be applied for annual periods beginning on or after 1 January 2009.

IFRIC 7, IFRIC 8, IFRIC 9, IFRIC 10, IFRIC 11 and IFRIC 12 shall be applied for annual periods beginning on or after 1 March 2006, 1 May 2006, 1 June 2006, 1 November 2006, 1 March 2007 and 1 January 2008, respectively.

The Group has commenced its assessment of the impact of these standards and interpretation but it is not yet in a position to state whether these standards and interpretation would have a material impact on its results of operations and financial position.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entity and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture is treated as:

(a) a subsidiary, if the Company, directly, or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board of directors;

(b) a jointly-controlled entity, if the Group does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;

(c) an associate, if the Group does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or

(d) an equity investment accounted for in accordance with IAS 39, if the Group holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

Jointly-controlled entity

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's interest in its jointly-controlled entity is accounted for by proportionate consolidation from the date on which joint control over the jointly-controlled entity are established, which involves recognising in the financial statements a proportionate share of the jointly-controlled entity's assets, liabilities, income and expenses with similar items on a line-by-line basis.

The results of the jointly-controlled entity are included in the Company's income statement to the extent of dividends received and receivable. The Company's investment in a jointly-controlled entity is treated as a non-current asset and is stated at cost less any impairment losses.

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long-term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Associates (continued)

consolidated reserves, respectively. The Group's interests in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

Excess over the cost of a business combination

Any excess of the Group's interest in the net fair value of the acquirees' identifiable assets, liabilities and contingent liabilities over the cost of acquisition of subsidiaries (previously referred to as negative goodwill), after reassessment, is recognised immediately in the consolidated income statement.

Impairment of non-financial assets

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, deferred tax assets and financial assets), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the consolidated income statement in the period in which it arises.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the consolidated income statement in the period in which it arises.

Related parties

A party is considered to be related to the Group if:

(a) the party directly, or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Company/Group; (ii) has an interest in the Company that gives it significant influence over the Company/Group; or (iii) has joint control over the Company/Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Company or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of employees of the Company/Group, or of any entity that is a related party of the Company/Group.

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the consolidated income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment and the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Buildings	2.57% to 8.33%
Plant and machinery	5.00% to 20.00%
Motor vehicles	6.00% to 20.00%
Computer and electronic equipment	18.00% to 20.00%
Office and other equipment	18.00% to 50.00%

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the consolidated income statement in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents the items of property, plant, machinery and equipment under construction and pending installation, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Investment properties

Investment properties are interests in buildings held to earn rental income and/or for capital appreciation, rather than for use in the production or supply of goods or services or for administrative purposes; or for sale in the ordinary course of business. Such properties are stated at cost, including transaction costs, less accumulated depreciation and any impairment losses.

Any gains or losses on the retirement or disposal of an investment property are recognised in the consolidated income statement in the year of the retirement or disposal.

Leases

Leases that transfer substantially all the rewards and risks of ownership of assets to the Group, other than legal title, are accounted for as finance leases. At the inception of a finance lease, the cost of the leased asset is capitalised at the present value of the minimum lease payments and recorded together with the obligation, excluding the interest element, to reflect the purchase and financing. Assets held under capitalised finance leases are included in property, plant and equipment, and depreciated over the shorter of the lease terms and the estimated useful lives of the assets. The finance costs of such leases are charged to the consolidated income statement so as to provide a constant periodic rate of charge over the lease terms.

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rentals receivable under the operating leases are credited to the consolidated income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the consolidated income statement on the straight-line basis over the lease terms.

Prepaid land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms.

Intangible assets

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Computer software

Computer software is stated at cost less any impairment losses and is amortised on the straight-line basis over their estimated useful lives of five years.

Patents and licences

Purchased patents and licences are stated at cost less any impairment losses and are amortised on the straight-line basis over their estimated useful lives of ten years.

Trademark

Trademark is stated at cost and is amortised on the straight-line basis over the registered term of usage of seven years.

Investments and other financial assets

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, or available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date. The Group considers whether a contract contains an embedded derivative when the Group first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

All regular way purchases and sales of financial assets are recognised on the trade date that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Derivatives, including separate embedded derivatives, are also classified as held for trading unless they are designated and effective hedging instruments. Gains or losses on investments held for trading are recognised in the consolidated income statement.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in listed and unlisted equity securities that are designated as available-for-sale or are not classified in any of the other two categories. After initial recognition, available-for-sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the consolidated income statement.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; a discounted cash flow analysis and option pricing models.

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the consolidated income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the consolidated income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Group will not be able to collect all of the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

Assets carried at cost

If there is objective evidence that an impairment loss on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the consolidated income statement. Impairment losses on equity instruments classified as available-for-sale are not reversed through the consolidated income statement.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

• the rights to receive cash flows from the asset have expired;

• the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or

• the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, where the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities at amortised cost (including interest-bearing loans and borrowings)

Financial liabilities including trade and other payables, an amount due to the ultimate holding company and interest-bearing loans and borrowings are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

Gains and losses are recognised in the consolidated income statement when the liabilities are derecognised as well as through the amortisation process.

Financial guarantee contracts

Financial guarantee contracts in the scope of IAS 39 are accounted for as financial liabilities. A financial guarantee contract is recognised initially at its fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial guarantee contract, except when such contract is recognised at fair value through profit or loss. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 *Revenue*.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the consolidated income statement.

Derivative financial instruments and hedging

The Group uses derivative financial instruments such as a cross currency interest rate swap contract to partially offset its risks associated with interest rate and foreign currency fluctuations. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The Group's derivative financial instruments do not qualify for hedge accounting and any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to the consolidated income statement in the year they arise.

The fair value of a cross currency interest rate swap contract is calculated by using valuation technique.

Inventories

Inventories are valued at the lower of cost and net realisable value.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

Raw materials	Purchase cost on the weighted average basis
Finished goods and work in progress	Cost of direct materials and labour and an appropriate proportion of overheads

Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short-term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and cash equivalents (contined)

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including time deposits, which are not restricted as to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the consolidated income statement.

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the consolidated income statement, or in equity if it relates to items that are recognised directly in equity in the same or a different period.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

• where the deferred tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

• in respect of taxable temporary differences associated with investments in subsidiaries, a jointly-controlled entity and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised, except:

• where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

• in respect of deductible temporary differences associated with investments in subsidiaries, a jointly-controlled entity and associates, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to a deferred income account and is released to the consolidated income statement over the expected useful life of the relevant asset by equal annual instalments.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) from the rendering of services, when the provision of services is started and completed within the same financial year, revenue is recognised at the time of completion. When the provision of services is started and completed in different accounting years and the outcome of the transaction can be estimated reliably, revenue is recognised at the balance sheet date on the percentage of completion basis; when the outcome of a transaction cannot be estimated reliably, revenue is recognised only to the extent of costs incurred that are expected to be recoverable;

(c) rental income, on a time proportion basis over the lease terms;

(d) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset; and

(e) dividend income, when the shareholders' right to receive payment has been established.

Employee benefits

Retirement benefits

The Group, its jointly-controlled entity and associates participate in a government-regulated defined contribution pension scheme, under which the Group, its jointly-controlled entity and associates make contributions into a government-regulated pension scheme at a fixed percentage of wages and salaries of the existing full time employees in the PRC and have no further legal or constructive obligations to make additional contributions. The contributions are charged as an expense to the consolidated income statement as incurred.

In addition to the benefits under the government-regulated defined contribution pension scheme above, Inner Mongolia Tianye Chemical Industry Limited ("Tianye"), the Company's 90%-owned subsidiary, also paid supplementary pensions to early retirees in accordance with an internal retirement plan and allowances to retired employees in accordance with the local labour regulations. As detailed in note 32 to the financial statements, such supplementary pensions and post employment allowances payables as at 31 December 2006 were assessed using the projected unit credit method; the cost of providing such pensions and allowances to the qualifying employees, including the active employees, is charged to the consolidated income statement as shown in the actuarial reports which contained full valuations of the obligations for the relevant accounting periods. These obligations are measured at the present value of the estimated future cash outflows using interest rates of the government securities which have terms to maturity similar to the terms of the related liability. To the extent that any cumulative unrecognised actuarial gains or losses exceed ten percent of the present value of the obligation at a disclosure date, that portion is recognised in the consolidated income statement over the expected average remaining working lives of the active employees. Otherwise the actuarial gains or losses are not recognised and deferred.

Details of the government-regulated pension scheme and the supplementary pension benefits are set out in note 8 to the financial statements.

Medical benefit costs

The Group, its jointly-controlled entity and associates participate in government-organised defined contribution medical benefit plans, under which the Group, its jointly-controlled entity and associates make contributions into a government-organised medical benefit plan at a fixed percentage of wages and salaries of the existing full time employees in the PRC and have no further legal or constructive obligations to make additional contributions.

The contributions are charged as an expense to the consolidated income statement as incurred. Details of the medical benefit plan are set out in note 8 to the financial statements.

Housing fund

The Group contributes on a monthly basis to a defined contribution housing fund plan organised by the PRC government. Contributions to these plans by the Group are expensed as incurred. Details of the housing fund plans are set out in note 8 to the financial statements.

Cash housing subsidies costs

Cash housing subsidies represent payments to the housing subsidy plan implemented by the Group. Cash housing subsidies are charged as an expense to the consolidated income statement as incurred. Details of the cash housing subsidy plan are set out in note 8 to the financial statements.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e. assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs capitalised.

All other borrowing costs are recognised as expenses in the period in which they are incurred.

Dividends

Dividends are recognised as a liability in the period in which they are approved by the shareholders and declared.

Foreign currencies

The financial records of the Group, its jointly-controlled entity and associates are maintained and these financial statements are stated in Renminbi ("RMB"), which is the functional currency of the Group, its jointly-controlled entity and associates.

Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

3 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in these financial statements:

Reclassification from construction in progress to property, plant and equipment

During the year, the Group has reclassified a significant amount of construction in progress to the appropriate category of property, plant and equipment when completed and ready for use.

The Group determines when the construction in progress is in the location and condition intended to be operated in the manner intended by management (i.e. ready for use) and has developed criteria in making that judgement on an individual asset basis.

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Deferred tax

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised. Where the actual or expected tax positions of the relevant companies of the Group in future are different from the original estimate, such differences will impact the recognition of deferred tax assets and income tax charge in the period in which such estimate has been changed.

(b) Write-down of inventories to net realisable value

Write-down of inventories to net realisable value is made based on the estimated net realisable value of the inventories. The assessment of the write-down required involves management's judgement and estimates. Where the actual outcome or expectation in future is different from the original estimate, such differences will have impact on the carrying amounts of the inventories and the write-down charge/write-back in the period in which such estimate has been changed.

(c) Provision for bad and doubtful receivables

Provision for bad and doubtful receivables is made based on the assessment of the recoverability of trade receivables and other receivables. The identification of doubtful receivables requires management's judgement and estimates. Where the actual outcome or expectation in future is different from the original estimate, such differences will have impact on the carrying amounts of the receivables and doubtful debt expenses/write-back in the period in which such estimate has been changed.

(d) Impairment of items of property, plant and equipment

The carrying amounts of items of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying amounts may not be recoverable in accordance with the accounting policy as disclosed in the relevant part of note 2.4 to the financial statements. The recoverable amount of property, plant and equipment is calculated as the higher of its fair value less costs to sell and value in use, the calculations of which involve the use of estimates.

(e) Depreciation of property, plant and equipment

The cost of items of property, plant and equipment is depreciated on a straight-line basis over their estimated useful lives. Management estimates the useful lives of plant and machinery to be 5 to 18 years, and other assets ranging from 2 to 35 years.

Changes in the expected level of usage and technological developments could impact the economic useful lives and the residual values of these assets, therefore depreciation charges might be revised in future.

4 SEGMENT INFORMATION

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately, according to the nature of their operations and the products and services they provided. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments.

Summary details of the business segments are as follows:

(i) the fertilisers segment is engaged in the manufacture and sale of nitrogenous fertilisers and compound fertilisers;

(ii) the methanol segment is engaged in the manufacture and sale of methanol; and

(iii) the "others" segment mainly comprises segments engaged in port operation, the provision of transportation services and the manufacture and sale of woven plastic bags.

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets. No geographical segments based on the location of the assets are presented as over 90% of the Group's assets are located in the PRC.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

Business segments

The following tables present revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the years ended 31 December 2006 and 2005.

4 SEGMENT INFORMATION (continued)

Business segments

	Fertilisers	Methanol	Others	Elimination	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Year ended 31 December 2006					
Segment revenue:					
Sales to external customers	2,989,161	308,700	167,920	-	**3,465,781**
Intersegment sales	-	-	83,897	(83,897)	**-**
Other income	99,223	-	484	-	**99,707**
Total	3,088,384	308,700	252,301	(83,897)	**3,565,488**
Segment results	1,082,254	123,775	21,944	-	**1,227,973**
Interest and dividend income and unallocated gains					**145,755**
Corporate and other unallocated expenses					**(94,621)**
Finance costs					**(61,738)**
Exchange loss, net					**(1,500)**
Share of profits of associates	1,779	-	57	-	**1,836**
Excess over the cost of a business combination					**577,619**
Profit before tax					**1,795,324**
Income tax expense					**(120,102)**
Profit for the year					**1,675,222**
As at 31 December 2006					
Segment assets	5,613,626	1,331,566	958,152	(21,737)	**7,881,607**
Investments in associates	7,590	-	1,056	-	**8,646**
Corporate and other unallocated assets					**1,220,629**
Total assets					**9,110,882**
Segment liabilities	(592,448)	(196,869)	(374,654)	21,737	**(1,142,234)**
Corporate and other unallocated liabilities					**(919,736)**
Total liabilities					**(2,061,970)**
Other segment information:					
Depreciation and amortisation	446,356	54,482	14,304	-	**515,142**
Write-back of impairment losses recognised in the consolidated income statement	(7,962)	-	-	-	**(7,962)**
Other non-cash expenses	2,580	-	237	-	**2,817**
Capital expenditure	124,454	301,983	163,241	-	**589,678**

	Fertilisers	Methanol	Others	Elimination	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Year ended 31 December 2005					
Segment revenue:					
Sales to external customers	2,259,876	-	111,123	-	2,370,999
Intersegment sales	-	-	55,532	(55,532)	-
Other income	543	-	370	-	913
Total	2,260,419	-	167,025	(55,532)	2,371,912
Segment results	960,476	-	2,368	-	962,844
Interest and dividend income and unallocated gains					25,173
Corporate and other unallocated expenses					(133,263)
Finance costs					(15,532)
Exchange gain, net					189,536
Share of profits of associates	1,892	-	21	-	1,913
Profit before tax					1,030,671
Income tax expense					(47,516)
Profit for the year					983,155
As at 31 December 2005					
Segment assets	4,362,105	454,336	883,099	(3,661)	5,695,879
Investments in associates	5,811	-	999	-	6,810
Corporate and other unallocated assets					450,335
Total assets					6,153,024
Segment liabilities	(167,125)	(54,947)	(398,495)	3,661	(616,906)
Corporate and other unallocated liabilities					(1,458,525)
Total liabilities					(2,075,431)
Other segment information:					
Depreciation and amortisation	253,489	-	12,785	-	266,274
Impairment losses recognised in the consolidated income statement	-	-	1,605	-	1,605
Other non-cash expenses	(1,221)	-	(1,028)	-	(2,249)
Capital expenditure	79,615	324,206	57,949	-	461,770

4 SEGMENT INFORMATION (continued)

Geographical segments

The following table presents revenue information for the Group's geographical segments for the years ended 31 December 2006 and 2005:

	2006	2005
	RMB'000	RMB'000
Sales to external customers:		
- PRC	**3,393,877**	2,020,564
- United States of America	**-**	350,435
- Others	**71,904**	-
	3,465,781	2,370,999

5 REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the invoiced values of goods sold, net of value-added tax ("VAT"), after allowances for returns and discounts; and the value of services rendered, net of business taxes and surcharges during the year.

An analysis of revenue, other income and gains is as follows:

	2006	2005
	RMB'000	RMB'000
Revenue		
Sale of goods	**3,303,539**	2,264,210
Rendering of services	**162,242**	106,789
	3,465,781	2,370,999
Other income and gains		
Dividend income from unlisted investments	**-**	223
Dividend income from listed investments	**360**	-
Subsidy income (Note)	**89,259**	-
Fair value gains on derivative financial instruments	**24,992**	-
Gain on dissolution of a subsidiary	**586**	-
Income from the sale of other materials	**6,652**	1,117
Others	**3,796**	305
	125,645	1,645

Note:

Pursuant to documents Cai Shui (2004) No. 33 and Cai Shui (2005) No. 9 issued by the Ministry of Finance and the State Administration of Taxation (the "SAT") on 17 January 2004 and 26 January 2005, respectively, manufacturers of urea products in Mainland China were entitled to a refund of 50% of the net VAT paid on the sale of urea products during the period from 1 January 2004 to 31 December 2005. In October 2005, the Group received approval documents from the local finance authority of Hainan Province, the PRC for the refund of 50% of the net VAT paid by the Group on the sale of urea products, amounting to RMB65,768,000, for the year ended 31 December 2004. In addition, in January 2006, the Group also received approval documents from the local finance authority of Hainan Province, the PRC for the refund of 50% of the net VAT paid by the Group on the sale of urea products, amounting to RMB53,243,000, for the six-month period ended 30 June 2005. Pursuant to the payment notifications issued by the Hainan provincial government on 22 May 2006, the Group received cash refund of RMB89,259,000 in May 2006. The remaining VAT refund of RMB29,752,000 has yet to be received by the Group and will be recognised as subsidy income when there is reasonable assurance that the VAT refund will be received by the Group.

Pursuant to a document Cai Shui (2005) No. 87 issued by the Ministry of Finance and the SAT on 26 May 2005, the sale of urea products by manufacturers of urea products in Mainland China were no longer entitled to receive a refund of 50% of the net VAT paid on the sale of urea products from 1 July 2005 as they are exempt from VAT with effect from 1 July 2005.

6 FINANCE REVENUE

Finance revenue represents interest income earned for the years ended 31 December 2006 and 2005.

7 FINANCE COSTS

	2006 RMB'000	2005 RMB'000
Interest on bank loans and other loans wholly repayable within five years	**76,465**	15,801
Less: Interest capitalised in construction in progress	**(14,727)**	(269)
	61,738	15,532

8 PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging/(crediting):

	2006 RMB'000	2005 RMB'000
Cost of inventories sold	**2,036,846**	1,212,716
Cost of services provided	**127,318**	80,379
Depreciation	**506,650**	264,362
Amortisation of a trademark	**311**	-
Amortisation of patents and licences	**26**	25
Amortisation of other intangible assets	**114**	114
Amortisation of prepaid land lease payments	**8,041**	1,773
Fair value losses on derivative financial instruments *	**-**	67,937
Write-down/(write-back) of inventories to net realisable value	**467**	(1,426)
Auditors' remuneration	**2,100**	736
Employee benefits expense (including directors' and supervisors' remuneration – note 9 below):		
Wages and salaries	**202,939**	122,566
Defined contribution pension scheme (note (i))	**26,359**	12,885
Early retirement benefits and post-employment allowances (note (ii))	**2,918**	-
Medical benefit costs (note (iii))	**12,117**	8,008
Housing fund (note (iv))	**8,242**	3,594
Cash housing subsidies costs (note (v))	**-**	46
	252,575	147,099
Foreign exchange differences, net	**1,500**	(189,536)
Provision/(write-back of provision) for bad and doubtful receivables *	**2,350**	(823)
Impairment/(write-back of impairment) of items of property, plant and equipment *	**(7,962)**	1,605
Dividend income from unlisted investments	**-**	(223)
Dividend income from listed investments	**(360)**	-
Loss on disposal of items of property, plant and equipment *	**2,865**	156

*These items are included in "Other expenses" on the face of the consolidated income statement.

8 PROFIT BEFORE TAX (continued)

Notes:

(i)Defined contribution pension scheme

All of the Group's employees in the PRC are covered by a government-regulated scheme and are entitled to an annual pension determined by their basic salaries upon their retirement. The PRC government is responsible for the pension liabilities to these retired employees. The Group is required to make annual contributions to the government-regulated pension scheme at 20% of the employees' salaries. This defined contribution pension scheme continued to be available to the Group's employees for the years ended 31 December 2006 and 2005. The related pension costs are expensed as incurred.

In addition to the government-regulated scheme, commencing from 1 January 2005, the Group operates a supplementary defined contribution retirement benefits scheme for those employees who are eligible to participate in this scheme. Contributions are made based on a percentage of the employee's basic salaries and are charged to the consolidated income statement as they become payable in accordance with the rules of the scheme. The assets of this scheme are held separately from those of the Group in an independently administered fund.

(ii)Early retirement benefits and post-employment allowances

Tianye, the Group's 90%-owned subsidiary, paid supplementary pensions to early retirees and allowances to retired employees in addition to the benefits under the government-regulated defined contribution pension scheme above. The benefits are assessed using the projected unit credit method and are charged to the consolidated income statement as shown in the actuarial reports which contained full valuations of the obligations for each of the relevant accounting periods. Details of the early retirement benefits are set out in note 32 to the financial statements.

(iii)Medical benefit costs

The Group contributes on a monthly basis to defined contribution medical benefit plans organised by the PRC government. The PRC government undertakes to assume the medical benefit obligations of all existing and retired employees under these plans. Contributions to these plans by the Group are expensed as incurred. The Group has no further obligations for medical benefits for their qualified employees under these plans.

(iv)Housing fund

The Group contributes on a monthly basis to a defined contribution housing fund plan organised by the PRC government. Contributions to these plans by the Group are expensed as incurred.

(v)Cash housing subsidies costs

Cash housing subsidies represent payments to the housing subsidy plan implemented by the Group. Cash housing subsidies are charged as an expense to the consolidated income statement as incurred.

9 DIRECTORS' AND SUPERVISORS' REMUNERATION

Details of the directors' and supervisors' remuneration for the year disclosed pursuant to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules") and Section 161 of the Companies Ordinance are as follows:

	Directors	
	2006	2005
	RMB'000	RMB'000
Fees	**-**	-
Other emoluments:		
Salaries, housing benefits, other allowances and benefits in kind	**776**	328
Discretionary bonuses	**751**	524
Pension scheme contributions	**80**	48
	1,607	900

	Supervisors	
	2006	2005
	RMB'000	RMB'000
Fees	**-**	-
Other emoluments:		
Salaries, housing benefits, other allowances and benefits in kind	**86**	142
Discretionary bonuses	**128**	124
Pension scheme contributions	**13**	17
	227	283

The remuneration of each of the directors and supervisors of the Company for the year ended 31 December 2006 is set out below:

	Salaries, housing benefits, other allowances and benefits in kind	Discretionary bonuses	Pension scheme contributions	Total
	RMB'000	RMB'000	RMB'000	RMB'000
Directors				
Non-executive director				
Wu Mengfei	15	-	-	15
Executive directors				
Yang Yexin	200	273	30	503
Fang Yong	140	226	21	387
Chen Kai	181	252	29	462
Wang Zhongan*	-	-	-	-
Cao Xinghe*	-	-	-	-
Zheng Baoguo *	-	-	-	-
Cheng Chi *	-	-	-	-
	521	751	80	1,352
Independent non-executive directors				
Zhang Xinzhi	38	-	-	38
Wu Xiaohua	38	-	-	38
Tsui Yiu Wa, Alec	126	-	-	126
Wang Wenshan	38	-	-	38
	240	-	-	240
	776	**751**	**80**	**1,607**
Supervisors				
Yin Jihong	-	-	-	-
Qu Bin	49	120	10	179
Huang Jinggui	19	-	-	19
Yin Gang **	18	8	3	29
Zhou Shengwei *	-	-	-	-
Fu Maosheng *	-	-	-	-
	86	**128**	**13**	**227**

*These directors and supervisors have not been in office since March 2006.

**The remuneration of Yin Gang was for the period from 1 January 2006 to 28 February 2006, the date of his resignation as a supervisor.

9 DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

The remuneration of each of the directors and supervisors of the Company for the year ended 31 December 2005 is set out below:

	Salaries, housing benefits, other allowances and benefits in kind	Discretionary bonuses	Pension scheme contributions	Total
	RMB'000	RMB'000	RMB'000	RMB'000
Directors				
Yang Yexin	195	276	29	500
Fang Yong	133	248	19	400
Wu Zhenfang	-	-	-	-
Sun Guofu	-	-	-	-
Wang Zhongan	-	-	-	-
Zheng Baoguo	-	-	-	-
Cao Xinghe	-	-	-	-
Cheng Chi	-	-	-	-
	328	524	48	900
Supervisors				
Zhou Shengwei	-	-	-	-
Fu Maosheng	-	-	-	-
Yin Gang	142	124	17	283
	142	124	17	283

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration during the year (2005: Nil).

10 FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees of the Group during the years ended 31 December 2006 and 2005 are analysed as follows:

	2006	2005
Directors and supervisors	**3**	2
Non-director and non-supervisor employees	**2**	3
	5	5

Details of the remuneration of the above non-director and non-supervisor, highest paid employees during the years ended 31 December 2006 and 2005 are as follows:

	2006	2005
	RMB'000	RMB'000
Salaries, housing benefits, other allowances and benefits in kind	**244**	427
Discretionary bonuses	**426**	600
Pension scheme contributions	**38**	63
	708	1,090

The remuneration of all of these non-director and non-supervisor, highest paid employees fell within the band from nil to HK$1,000,000 for the years ended 31 December 2006 and 2005.

11 INCOME TAX EXPENSE

Major components of income tax expense for the years ended 31 December 2006 and 2005 are as follows:

Group

	2006	2005
	RMB'000	RMB'000
Current - PRC		
Charge for the year	**115,399**	49,309
Deferred (note 23)	**4,703**	(1,793)
Total tax charge for the year	**120,102**	47,516

(a) *Corporate income tax*

Under the relevant PRC Income Tax Law and the respective regulations, except for certain preferential tax treatment available to the Company, its subsidiaries and its jointly-controlled entity, the entities within the Group are subject to corporate income tax ("CIT") at the rate of 33%.

The Company, its subsidiaries and its jointly-controlled entity registered in Hainan Province or Pudong New Area, Shanghai, the PRC are entitled to a preferential CIT rate of 15%.

A two-year income tax exemption followed by a three-year 50% reduction in the applicable tax rate for CIT based on a CIT rate of 15% commencing from the first profitable year is applicable to the Company and all its subsidiaries in Hainan, the PRC. In addition, the Company is entitled to a further three-year 50% reduction in the applicable tax rate for CIT for the three years ending 31 December 2011 as it was assessed as a high-technology enterprise.

Hainan Basuo is entitled to exemption from CIT for the five years ending 31 December 2009 and a 50% reduction in the applicable tax rate for CIT for the five years ending 31 December 2014 as it is engaged in infrastructure development and operation business.

CNOOC Kingboard Chemical Limited ("CNOOC-KB"), the Company's jointly-controlled entity, is a foreign investment enterprise and is entitled to exemption from CIT for its first two profitable years and a 50% reduction in the applicable tax rate for CIT for the subsequent three years. According to the PRC Income Tax Law for Enterprises with Foreign Investment and Foreign Enterprises, enterprises with foreign investment which commence operations in the middle of a year and earn profits may, where the actual period of operations is less than six months, elect to use the following year as the first period to be entitled to the tax exemptions. However, in such circumstances, income tax shall be paid in accordance with the Tax Law on the assessable profits earned in the first profitable year. CNOOC-KB has elected to enjoy the tax holiday starting from the year ending 31 December 2007 and this has been approved by the local tax bureau of Dongfang city of Hainan Province, the PRC.

Tianye is entitled to a preferential income tax treatment by way of a three-year exemption from CIT of 33% starting from the year ended 31 December 2005 in relation to the conversion of its facilities to use natural gas instead of residual oil as a raw material for its urea production.

(b) *Hong Kong profits tax*

No provision for Hong Kong profits tax has been made as the Group had no assessable profits arising in Hong Kong for the years ended 31 December 2006 and 2005, respectively.

A reconciliation of the income tax expense applicable to profit before tax using the statutory rates for the country in which the Group and its jointly-controlled entity are domiciled to the income tax expense at the effective tax rates is as follows:

	2006	2005
	RMB'000	RMB'000
Profit before tax	**1,795,324**	1,030,671
Tax at the statutory tax rate of 33%	**592,457**	340,121
Lower tax rate for specific provinces/ districts or concessions	**(431,359)**	(291,695)
Effect on opening deferred tax of increase in tax rates	**-**	(70)
Profits attributable to associates	**(267)**	(287)
Income not subject to tax (Note)	**(43,322)**	-
Expenses not deductible for tax	**919**	114
Tax losses not recognised	**92**	489
Others	**1,582**	(1,156)
Income tax expense reported in the consolidated income statement	**120,102**	47,516
The Group's effective income tax rate	**6.7%**	4.6%

Note:

Income not subject to tax is made up of the excess over the cost of a business combination which is exempt from CIT.

The share of tax attributable to associates amounting to RMB10,000 (2005: RMB8,000) is included in "Share of profits of associates" on the face of the consolidated income statement.

12 PROFIT FOR THE YEAR ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The consolidated profit for the year attributable to equity holders of the parent for the year ended 31 December 2006 includes a profit of RMB1,190,051,000 (2005:RMB693,463,000) dealt with in the financial statements of the Company (note 31).

13 DIVIDENDS

		2006	2005
	Notes	RMB'000	RMB'000
Special Dividend to CNOOC	(i)	-	1,210,801
Pre-establishment Distribution	(ii)	**264,538**	-
Pre-IPO Profit	(iii)	**302,142**	-
Proposed final – RMB1.5 cent (2005: Nil) per ordinary share	(iv)	**69,150**	-
Dividend to other equity holders of the Relevant Companies	(v)	-	1,012
		635,830	1,211,813

Notes:

(i) On 6 March 2006, the directors proposed to declare a dividend of RMB1,210,801,000 (the "Special Dividend") to CNOOC, which was approved in the shareholders' meeting on the same date.

(ii) In accordance with the Provisional Regulations Relating to Corporate Reorganisation of Enterprises and Related Management of State-owned Capital and Financial Treatment notice (財政部關于印發«企業公司制改建有關國有資本管理與財務處理的暫行規定»的通知) issued by the Ministry of Finance (English title is a direct translation of Chinese title of the notice), which became effective from 27 August 2002, the Company is required to make a distribution (the "Pre-establishment Distribution") to CNOOC in an amount equal to its net profit, as determined in accordance with PRC GAAP, of the Company, generated from 1 January 2006 to 24 April 2006, the date immediately prior to the date on which the Company was reorganised into a joint stock limited company.

Pursuant to a supplementary agreement to the Promotion Agreement dated 10 July 2006, the Company's promoters (i.e. CNOOC and the Other Four Promoters) agreed to distribute a Pre-establishment Distribution of RMB264,538,000 to CNOOC, which was paid in full during the year.

(iii) On 25 April 2006, the promoters of the Company unanimously resolved that they will be entitled to, in the same proportion as their respective shareholdings in the Company, all of the undistributed profit (the "Pre-IPO Profit"), as determined in accordance with PRC GAAP, of the Company for the period from 25 April 2006, the date of the Company's reorganisation into a joint stock limited company, to the last day of the month immediately preceding the listing of the Company's H shares on the Stock Exchange (i.e. 31 August 2006). On 30 December 2006, the directors resolved to distribute an aggregate amount of RMB302,142,000 to the promoters as the Pre-IPO Profit which was paid in full during the year.

(iv) The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

(v) An aggregate amount of RMB1,012,000 was declared and paid by the Relevant Companies to their respective equity holders, other than the Company, for the year ended 31 December 2005.

Upon listing of the Company's shares on the Stock Exchange, the Company may not distribute dividends exceeding the lower of the profit after tax as determined under PRC GAAP and IFRS. Further details are set out in note 31 to the financial statements.

14 EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

	2006	2005
	RMB'000	RMB'000
Earnings		
Net profit for the year attributable to equity holders of the parent	**1,645,819**	943,830

	Number of shares	
	'000	'000
Shares		
Weighted average number of shares in issue during the year	**3,400,438**	3,000,000

The Company's weighted average number of shares in issue during the years ended 31 December 2006 and 2005 used in the basic earnings per share calculation is determined on the assumption that 3,000,000,000 Domestic Shares of RMB1 each issued as a result of the Reorganisation had been in issue throughout the years ended 31 December 2006 and 2005 and as adjusted to add the 1,610,000,000 H shares of RMB1 each issued to the public upon the listing of the Company's H shares on the Stock Exchange. Further details are set out in note 1 to the financial statements.

Diluted earnings per share amounts for the years ended 31 December 2006 and 2005 have not been disclosed as no diluting events existed during these years.

15 PROPERTY, PLANT AND EQUIPMENT

Group

	Buildings	Plant and machinery	Motor vehicles	Computer and electronic equipment	Office and other equipment	Construction in progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
As at 31 December 2005:							
Cost	947,794	3,211,272	46,470	32,436	4,733	478,517	4,721,222
Accumulated depreciation and impairment	(165,079)	(1,040,103)	(21,877)	(13,664)	(1,366)	-	(1,242,089)
Net carrying amount	782,715	2,171,169	24,593	18,772	3,367	478,517	3,479,133
Cost as at 1 January 2006, net of accumulated depreciation and impairment	782,715	2,171,169	24,593	18,772	3,367	478,517	**3,479,133**
Additions	26,850	22,200	8,159	21,397	644	432,836	**512,086**
Acquisition of a subsidiary (note 39(e))	681,508	1,138,063	2,932	14,904	10,810	519,216	**2,367,433**
Disposals	-	(636)	(365)	(355)	(2,689)	-	**(4,045)**
Dissolution of a subsidiary (note 39(d))	(415)	-	-	-	(606)	-	**(1,021)**
Transfers	323,103	932,045	-	14,199	893	(1,270,240)	**-**
Write-back of impairment /(impairment)	2,678	5,340	-	-	(56)	-	**7,962**
Depreciation for the year	(101,896)	(376,860)	(11,463)	(15,219)	(1,212)	-	**(506,650)**
Cost as at 31 December 2006, net of accumulated depreciation and impairment	1,714,543	3,891,321	23,856	53,698	11,151	160,329	**5,854,898**
As at 31 December 2006:							
Cost	2,532,158	6,312,343	74,745	325,090	42,496	160,329	**9,447,161**
Accumulated depreciation and impairment	(817,615)	(2,421,022)	(50,889)	(271,392)	(31,345)	-	**(3,592,263)**
Net carrying amount	1,714,543	3,891,321	23,856	53,698	11,151	160,329	**5,854,898**

15 PROPERTY, PLANT AND EQUIPMENT (continued)

Group (continued)

	Buildings	Plant and machinery	Motor vehicles	Computer and electronic equipment	Office and other equipment	Construction in progress	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
As at 31 December 2004:							
Cost	685,083	3,147,171	33,742	24,830	4,337	77,502	3,972,665
Accumulated depreciation	(126,322)	(825,269)	(16,639)	(11,492)	(804)	-	(980,526)
Net carrying amount	558,761	2,321,902	17,103	13,338	3,533	77,502	2,992,139
Cost as at 1 January 2005, net of accumulated depreciation	558,761	2,321,902	17,103	13,338	3,533	77,502	2,992,139
Additions	269	2,067	8,637	6,645	283	441,034	458,935
Formation of a subsidiary (note39(a))	267,015	25,406	4,140	1,145	113	-	297,819
Disposals	-	(143)	-	(25)	-	-	(168)
Transfer of a subsidiary to a CNOOC group company (note39(b))	(3,256)	(301)	(68)	-	-	-	(3,625)
Transfers	1,068	38,869	82	-	-	(40,019)	-
Impairment	-	-	(1,605)	-	-	-	(1,605)
Depreciation for the year	(41,142)	(216,631)	(3,696)	(2,331)	(562)	-	(264,362)
Cost as at 31 December 2005, net of accumulated depreciation and impairment	782,715	2,171,169	24,593	18,772	3,367	478,517	3,479,133
As at 31 December 2005:							
Cost	947,794	3,211,272	46,470	32,436	4,733	478,517	4,721,222
Accumulated depreciation and impairment	(165,079)	(1,040,103)	(21,877)	(13,664)	(1,366)	-	(1,242,089)
Net carrying amount	782,715	2,171,169	24,593	18,772	3,367	478,517	3,479,133

As at 31 December 2006, the net book value of the Group's property, plant and equipment held under finance leases amounted to RMB2,297,000 (2005: Nil).

Details of the Group's property, plant and equipment pledged to secure the Group's bank borrowings are set out in note 33 to the financial statements.

As at 31 December 2006, the Group has yet to obtain building ownership certificates for certain buildings with net book value of approximately RMB34,952,000.

Company

	Buildings RMB'000	Plant and machinery RMB'000	Motor vehicles RMB'000	Computer and electronic equipment RMB'000	Office and other equipment RMB'000	Construction in progress RMB'000	Total RMB'000
As at 31 December 2005:							
Cost	449,940	1,668,286	20,934	16,570	4,133	17,722	2,177,585
Accumulated depreciation	(79,745)	(237,516)	(10,304)	(3,334)	(1,273)	-	(332,172)
Net carrying amount	370,195	1,430,770	10,630	13,236	2,860	17,722	1,845,413
Cost as at 1 January 2006, net of accumulated depreciation	370,195	1,430,770	10,630	13,236	2,860	17,722	**1,845,413**
Additions	151	8,170	106	636	54	592	**9,709**
Disposals	(2,251)	-	(122)	(72)	-	-	**(2,445)**
Transfers	15,330	948	-	997	139	(17,414)	**-**
Depreciation for the year	(27,043)	(112,667)	(1,994)	(3,264)	(372)	-	**(145,340)**
Cost as at 31 December 2006, net of accumulated depreciation	356,382	1,327,221	8,620	11,533	2,681	900	**1,707,337**
As at 31 December 2006:							
Cost	463,168	1,677,404	19,825	17,718	4,326	900	**2,183,341**
Accumulated depreciation	(106,786)	(350,183)	(11,205)	(6,185)	(1,645)	-	**(476,004)**
Net carrying amount	356,382	1,327,221	8,620	11,533	2,681	900	**1,707,337**
As at 31 December 2004:							
Cost	449,532	1,653,600	15,496	11,551	4,122	4,948	2,139,249
Accumulated depreciation	(56,889)	(120,763)	(8,732)	(2,293)	(781)	-	(189,458)
Net carrying amount	392,643	1,532,837	6,764	9,258	3,341	4,948	1,949,791
Cost as at 1 January 2005, net of accumulated depreciation	392,643	1,532,837	6,764	9,258	3,341	4,948	1,949,791
Additions	119	2,123	5,356	5,203	11	27,136	39,948
Disposals	-	(143)	-	(25)	-	-	(168)
Transfers	289	13,991	82	-	-	(14,362)	-
Depreciation for the year	(22,856)	(118,038)	(1,572)	(1,200)	(492)	-	(144,158)
Cost as at 31 December 2005, net of accumulated depreciation	370,195	1,430,770	10,630	13,236	2,860	17,722	1,845,413
As at 31 December 2005:							
Cost	449,940	1,668,286	20,934	16,570	4,133	17,722	2,177,585
Accumulated depreciation	(79,745)	(237,516)	(10,304)	(3,334)	(1,273)	-	(332,172)
Net carrying amount	370,195	1,430,770	10,630	13,236	2,860	17,722	1,845,413

16 INVESTMENT PROPERTIES

	As at 31 December 2006 RMB'000
Additions and carrying amounts at end of year	**17,422**

Included in the Company's investment properties are buildings situated in the PRC, which are leased to its subsidiaries under operating leases. Further details are set out in note 40 to the financial statements.

In the opinion of the directors, the carrying amounts of the Company's investment properties approximate their fair values.

17 PREPAID LAND LEASE PAYMENTS

Group

	2006 RMB'000	2005 RMB'000
Carrying amount at 1 January	**118,857**	65,325
Additions	**61,956**	2,835
Formation of a subsidiary (note 39(a))	**-**	57,407
Acquisition of a subsidiary (note 39(e))	**249,659**	-
Transfer of a subsidiary to a CNOOC group company (note 39(b))	**-**	(4,937)
Amortisation for the year	**(8,041)**	(1,773)
Carrying amount at 31 December	**422,431**	118,857
Current portion included in prepayments, deposits and other receivables	**(8,569)**	-
Non-current portion	**413,862**	118,857

As at 31 December 2006, the Group has yet to obtain the land use right certificate for a piece of land amounting to approximately RMB10,047,000 where Tianye's production facilities for the manufacture of methanol are located. Pursuant to a State-owned Land Use Right Grant Contract dated 30 June 2006 entered into between Tianye and the State-owned Land Resources Bureau of Huhhot City, this piece of land has been granted to Tianye for a term of 50 years.

The Group's leasehold land is situated in Mainland China and is held under the following lease terms:

	RMB'000
Long-term leases	**79,140**
Medium-term leases	**343,291**
	422,431

Company

	2006 RMB'000	2005 RMB'000
Carrying amount at 1 January	**37,907**	39,212
Additions	**5,591**	-
Amortisation for the year	**(515)**	(1,305)
Carrying amount at 31 December	**42,983**	37,907
Current portion included in prepayments, deposits and other receivables	**(592)**	-
Non-current portion	**42,391**	37,907

The Company's leasehold land is situated in Mainland China and is held under the following lease terms:

	RMB'000
Long-term leases	**8,847**
Medium-term leases	**34,136**
	42,983

18 INTANGIBLE ASSETS

Group

	Computer software	Patents and licences	Trademark	Total
	RMB'000	RMB'000	RMB'000	RMB'000
Cost as at 1 January 2006, net of accumulated amortisation	246	152	-	**398**
Additions	15,636	-	-	**15,636**
Acquisition of a subsidiary (note 39(e))	-	-	968	**968**
Amortisation for the year	(114)	(26)	(311)	**(451)**
Impairment	-	(126)	-	**(126)**
Cost as at 31 December 2006, net of accumulated amortisation and impairment	15,768	-	657	**16,425**
At 31 December 2006:				
Cost	16,207	253	2,299	**18,759**
Accumulated amortisation and impairment	(439)	(253)	(1,642)	**(2,334)**
Net carrying amount	15,768	-	657	**16,425**
Cost as at 1 January 2005, net of accumulated amortisation	360	177	-	537
Amortisation for the year	(114)	(25)	-	(139)
Cost as at 31 December 2005, net of accumulated amortisation	246	152	-	398
At 31 December 2005:				
Cost	571	253	-	824
Accumulated amortisation	(325)	(101)	-	(426)
Net carrying amount	246	152	-	398

18 INTANGIBLE ASSETS (continued)

Company

	Computer software RMB'000
Cost as at 1January 2006,net of accumulated amortisation	**246**
Additions	**15,636**
Amortisation for the year	**(114)**
Cost as at 31 December 2006, net of accumulated amortisation	**15,768**
As at 31 December 2006:	
Cost	**16,207**
Accumulated amortisation	**(439)**
Net carrying amount	**15,768**
Cost as at 1 January 2005, net of accumulated amortisation	360
Amortisation for the year	(114)
Cost as at 31 December 2005, net of accumulated amortisation	246
As at 31 December 2005:	
Cost	571
Accumulated amortisation	(325)
Net carrying amount	246

19 INTERESTS IN SUBSIDIARIES

	2006 RMB'000	2005 RMB'000
Unlisted investments, at cost	**2,206,154**	1,053,374
Loans to subsidiaries	**30,000**	-
	2,236,154	1,053,374

The Company's trade receivable, other receivable, loan receivable, other long-term liability, trade payable, and other payable balances with its subsidiaries are disclosed in notes 25, 27, 28, 34, 35 and 36 to the financial statements, respectively.

The loans to subsidiaries included in the interests in subsidiaries above are unsecured, bear interest at a rate of 5.2% per annum and are repayable on 27 April 2008.

Particulars of the principal subsidiaries of the Company are set out as follow:

Company name	Place and date of establishment	Registered capital	Percentage of equity interests attributable to the Company		Principal activities
		RMB'000			
CNOOC Fudao Limited* (海洋石油富島有限公司)	PRC 31 December 2001	463,000	Direct Indirect	100.00 -	Manufacture and sale of fertilisers
Hainan CNOOC Plastic Company Limited (海南中海石油塑編有限公司)	PRC 28 April 2002	12,716	Direct Indirect	100.00 -	Manufacture and sale of woven plastic bags
Hainan CNOOC Transportation Co., Ltd. (海南中海石油運輸服務有限公司)	PRC 22 October 2001	5,000	Direct Indirect	- 65.25	Provision of transportation services
CNOOC (Hainan) E&P Gas Limited (中海石油（海南）環保氣體有限公司)	PRC 8 November 2004	6,900	Direct Indirect	100.00 -	Manufacture and sale of liquid carbon dioxide
Hainan Basuo Port Limited (海南八所港務有限責任公司)	PRC 25 April 2005	518,356	Direct Indirect	72.50 -	Port operation
Inner Mongolia Tianye Chemical Industry Limited (內蒙古天野化工（集團）有限責任公司)	PRC 4 October 1991	1,981,690	Direct Indirect	90.00 -	Manufacture and sale of fertilisers and methanol
Inner Mongolia Hong Feng Packaging Co., Ltd. (內蒙古鴻豐包裝有限責任公司)	PRC 9 December 1999	3,297	Direct Indirect	- 63.54	Manufacture and sale of woven plastic bags

*Upon the Reorganisation of the Company into a joint stock limited company on 25 April 2006, Fudao was restructured from a joint stock limited company into a limited liability company under the name of CNOOC Fudao Limited and became a wholly-owned subsidiary of the Company.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affects the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

20 INVESTMENT IN A JOINTLY-CONTROLLED ENTITY

	2006	2005
	RMB'000	RMB'000
Unlisted investments, at cost	**300,000**	300,000

The Group and the Company's trade receivable, other receivable, other long-term liability, trade payable, and other payable balances with the jointly-controlled entity are disclosed in notes 25, 27, 34, 35 and 36 to the financial statements.

Particulars of the jointly-controlled entity of the Company and of the Group are set out as follows:

Company name	Place and date of establishment	Registered capital	Percentage of			Principal activities
			Ownership interest	Voting power	Profit sharing	
		RMB'000				
CNOOC Kingboard Chemical Limited (中海石油建滔化工有限公司)	PRC 31 October 2003	500,000	60.00	60.00	60.00	Manufacture and sale of methanol

20 INVESTMENT IN A JOINTLY-CONTROLLED ENTITY (continued)

The following table illustrates the summarised financial information of the Group's jointly-controlled entity:

	2006 RMB'000	2005 RMB'000
Share of the jointly-controlled entity's assets and liabilities:		
Non-current assets	**666,263**	386,230
Current assets	**212,515**	68,106
Non-current liabilities	**(311,452)**	(99,389)
Current liabilities	**(203,562)**	(54,947)
Net assets	**363,764**	300,000

Share of the jointly-controlled entity's results:

	2006	2005
Turnover	**106,562**	-
Other revenue	**-**	-
Total revenue	**106,562**	-
Total expenses	**(33,145)**	-
Tax	**(9,653)**	-
Profit after tax	**63,764**	-

21 INVESTMENTS IN ASSOCIATES

Group

	2006 RMB'000	2005 RMB'000
Share of net assets	**8,646**	6,810

The Group's other payable balances with its associates are disclosed in note 36 to the financial statements.

Particulars of the associates of the Group are set out as follows:

Company name	Place and date of establishment	Registered capital RMB'000	Percentage of ownership interest attributable to the Group		Principal activities
Guangxi Fudao Agricultural Means of Production Limited(廣西富島農業生產資料有限公司)	PRC 11 January 2003	11,800	Direct Indirect	- 30.00	Trading of fertilisers
China Basuo Oversea Shipping Agency Co., Ltd.(中國八所外輪代理有限公司)	PRC 24 May 2000	1,800	Direct Indirect	- 36.25	Provision of overseas shipping services

The following table illustrates the aggregate amounts of the assets, liabilities, revenues and profit of the Group's associates.

	2006 RMB'000	2005 RMB'000
Assets	**99,340**	90,472
Liabilities	**70,941**	69,103
Revenues	**504,673**	455,538
Profit	**6,044**	6,344

22 AVAILABLE-FOR-SALE EQUITY INVESTMENTS

Group

	2006	2005
	RMB'000	RMB'000
Unlisted equity investments, at cost	**600**	600
Listed equity securities in the PRC, at fair value	**8,865**	6,188
	9,465	6,788

The unlisted equity investments are accounted for at cost less accumulated impairment losses as such investments do not have quoted market prices in an active market and their fair values cannot be reliably measured.

23 DEFERRED TAXATION

The movements in deferred tax assets and liabilities of the Group and of the Company during the years ended 31 December 2006 and 2005 are as follows:

Group

Deferred tax assets

	Differences in depreciation and amortisation between tax regulations and accounting policies	Provision for impairment of assets	Others	Total
	RMB'000	RMB'000	RMB'000	RMB'000
As at 1 January 2006	2,469	2,203	-	**4,672**
Acquisition of a subsidiary (note 39(e))	-	27,225	625	**27,850**
Credited/(charged) to the consolidated income statement (note 11)	2,132	(6,835)	-	**(4,703)**
As at 31 December 2006	4,601	22,593	625	**27,819**
As at 1 January 2005	1,507	1,372	-	2,879
Credited to the consolidated income statement (note 11)	962	831	-	1,793
As at 31 December 2005	2,469	2,203	-	4,672

Deferred tax liabilities

	Fair value adjustments arising from acquisition of a subsidiary
	RMB '000
As at 1 January 2006	**-**
Acquisition of a subsidiary (note 39(e))	**61,017**
As at 31 December 2006	**61,017**

23 DEFERRED TAXATION (continued)

Company

Deferred tax assets

	Differences in depreciation and amortisation between tax regulations and accounting policies	Provision for impairment of assets	Total
	RMB'000	RMB'000	RMB'000
As at 1 January 2006	1,285	583	**1,868**
Credited/(charged) to the income statement	687	(465)	**222**
As at 31 December 2006	1,972	118	**2,090**
As at 1 January 2005	643	-	643
Credited to the income statement	642	583	1,225
As at 31 December 2005	1,285	583	1,868

24 INVENTORIES

Group

	2006	2005
	RMB'000	RMB'000
Raw materials	**252,387**	121,768
Work in progress	**50,732**	25,549
Finished goods	**29,565**	14,742
Net book value	**332,684**	162,059

Company

	2006	2005
	RMB'000	RMB'000
Raw materials	**77,879**	50,249
Work in progress	**13,594**	10,310
Finished goods	**30**	2,727
Net book value	**91,503**	63,286

25 TRADE RECEIVABLES

Sales of the Group's fertilisers are normally settled on an advance receipt basis whereby the customers are required to pay in advance either by cash or by bank acceptance drafts. However, in the case of long-standing customers with bulk purchases and a good repayment history, the Group may agree that the sales can be settled by commercial acceptance drafts. In the case of export sales, the Group may also accept irrevocable letters of credit issued in its favour.

The trading terms of the Group with its methanol customers are mainly on credit. The credit period is generally one month.

An aged analysis of the trade receivables, based on invoice date and net of provision for bad and doubtful debts, of the Group and of the Company is as follows:

Group

	2006	2005
	RMB'000	RMB'000
Within six months	**127,212**	168,830
Over six months but within one year	**166**	2,135
Over one year but within two years	**6,179**	18
Over two years but within three years	**-**	600
Over three years	**-**	69
	133,557	171,652

As at 31 December 2006, the amount due from a jointly-controlled entity included in the above trade receivable balances was RMB4,308,000 (2005: Nil). The amounts due are unsecured, non-interest-bearing and repayable on similar credit terms to those offered to the major customers of the Group.

Company

	2006 RMB'000	2005 RMB'000
Within six months	**7,753**	125,420

As at 31 December 2006, the amounts due from subsidiaries of the Company included in the above trade receivable balances were RMB1,378,000 (2005: RMB835,000). The amounts due are unsecured, non-interest-bearing and repayable on similar credit terms to those offered to the major customers of the Company.

26 BILLS RECEIVABLE

The bills receivable of the Group and of the Company as at 31 December 2006 and 2005 are all matured within six months.

27 PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

Group

	2006 RMB'000	2005 RMB'000
Prepayments	**47,040**	59,283
Deposits and other receivables	**39,113**	109,240
	86,153	168,523

The amounts due from CNOOC group companies and a jointly-controlled entity included in the above can be analysed as follows:

	2006 RMB'000	2005 RMB'000
CNOOC group companies	**6,166**	12,094
A jointly-controlled entity	**5,405**	1,226
	11,571	13,320

The amounts due are unsecured, non-interest-bearing and have no fixed terms of repayment.

Company

	2006 RMB'000	2005 RMB'000
Prepayments	**3,650**	16,219
Deposits and other receivables	**145,259**	38,220
	148,909	54,439

The amounts due from CNOOC group companies, a jointly-controlled entity and subsidiaries of the Company included in the above can be analysed as follows:

	2006 RMB'000	2005 RMB'000
CNOOC group companies	**5,666**	2,094
A jointly-controlled entity	**7,014**	3,065
Subsidiaries	**113,368**	13,546
	126,048	18,705

Included in the amount due from the Company's subsidiaries as at 31 December 2006 was a dividend receivable from Fudao of RMB96,293,000(2005:Nil).

The amounts due are unsecured, non-interest-bearing and have no fixed terms of repayment.

28 LOANS RECEIVABLE

As at 31 December 2006, loans receivable represented an entrusted loan with a contract amount of RMB600,000,000 which was provided to Tianye during the year and is unsecured, bears interest at a rate of 5.27% per annum and is repayable on 15 June 2007.

The balance as at 31 December 2005 represented an entrusted loan to another subsidiary which was unsecured, bore interest at a rate of 4.5% per annum. The amount was repaid in full during the year.

29 CASH AND CASH EQUIVALENTS AND PLEDGED BANK DEPOSITS

Group

	2006	2005
	RMB'000	RMB'000
Cash and bank balances	**1,908,363**	1,551,752
Time deposits	**298,160**	398,000
	2,206,523	1,949,752
Less: Pledged bank deposits	**(10,904)**	-
Cash and cash equivalents in the consolidated balance sheet	**2,195,619**	1,949,752
Less: Non-pledged time deposits with original maturity of three months or more when acquired	**(146,160)**	(230,000)
Cash and cash equivalents in the consolidated cash flow statements	**2,049,459**	1,719,752

As at 31 December 2006, the Group's pledged time deposits of RMB 10,904,000 (2005: Nil) were deposited to banks for issuing letters of credit in relation to the purchase of machinery and equipment.

The Group's cash and bank balances are denominated in RMB as at 31 December 2006 and 2005, except for amounts of RMB171,000 (2005: RMB49,088,000) which is translated from U.S.$22,000 (2005: U.S.$6,083,000); RMB4,707,000 (2005: Nil) which is translated from JPY71,727,000 (2005: Nil); and RMB12,448,000 (2005: Nil) which is translated from HK$12,390,000 (2005: Nil).

The RMB is not freely convertible into other currencies. However, under the PRC Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

As at 31 December 2006, included in the Group's cash and cash equivalents was RMB259,866,000 (2005: RMB1,098,690,000) deposited in CNOOC Finance Corporation Ltd. ("CNOOC Finance"). The deposits with CNOOC Finance are entitled to interest at the rates similar to the prevailing bank deposit rates and are held for terms ranging from one day to six months.

Company

	2006	2005
	RMB'000	RMB'000
Cash and bank balances	**1,528,618**	1,174,271
Less: Pledged bank deposits	**(2,413)**	-
	1,526,205	1,174,271

As at 31 December 2006, the Company's pledged time deposits of RMB 2,413,000 (2005: Nil) were deposited to banks for issuing letters of credit in relation to the purchase of machinery and equipment.

The Company's cash and bank balances are denominated in RMB as at 31 December 2006 and 2005, except for amounts of RMB23,000 (2005:RMB1,565,000) which is translated from US$3,000 (2005: U.S.$194,000); RMB4,707,000 (2005: Nil) which is translated from JPY71,727,000 (2005: Nil); and RMB12,448,000 (2005: Nil) which is translated from HK$12,390,000 (2005: Nil). The Company is subject to the same exchange control requirements as the Group as detailed above.

As at 31 December 2006, included in the Company's cash and cash equivalents was RMB62,757,000 (2005: RMB766,949,000) deposited in CNOOC Finance. The deposits with CNOOC Finance are entitled to interest at the rates similar to the prevailing bank deposit rates and are held for terms ranging from one day to six months.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term time deposits are made for varying periods of between one day and six months depending on the immediate cash requirements of the Group and the Company, and earn interest at the respective short-term time deposit rates. The carrying amounts of the cash and cash equivalents and the pledged bank deposits approximate to their fair values.

30 PAID-UP CAPITAL

	Number of shares	Nominal value
	'000	RMB'000
Registered capital	4,610,000	4,610,000
Issued and fully paid:		
Domestic Shares of RMB1 each, currently not listed:		
- State-owned shares	2,739,000	2,739,000
- Other legal person shares	75,000	75,000
Unlisted Foreign Shares of RMB1 each	25,000	25,000
H shares of RMB1 each	1,771,000	1,771,000
As at 31 December 2006	**4,610,000**	**4,610,000**

A summary of the movements in the Company's issued share capital for the period from 25 April 2006, the date on which the Company was reorganised into a joint stock limited company, to 31 December 2006 is as follows:

	Notes	Domestic Shares	H shares	Total
		RMB'000	RMB'000	RMB'000
Reorganised as a joint stock limited company on 25 April 2006	(i)	3,000,000	-	**3,000,000**
Issue of new shares upon listing	(ii)	-	1,610,000	**1,610,000**
Domestic Shares converted into H shares	(ii)	(161,000)	161,000	-
		2,839,000	1,771,000	**4,610,000**

Notes:

(i) On 25 April 2006, the Company was reorganised into a joint stock limited company with a registered share capital of RMB3,000,000,000, divided into 3,000,000,000 shares with a nominal value of RMB1 each.

The Company issued 2,900,000,000 Domestic Shares to CNOOC, 25,000,000 Domestic Shares to each of Zhejiang AMP Incorporation, Guangdong Agricultural Means of Production Corporation and Shanghai Municipal Agricultural Means of Production Corporation, and 25,000,000 Unlisted Foreign Shares to Transammonia Inc., representing approximately 96.68%, 0.83%, 0.83%, 0.83% and 0.83%, respectively, of the Company's issued share capital as at 25 April 2006.

The Domestic Shares rank pari passu, in all material respects, with the H shares.

(ii) In September 2006, the Company issued 1,400,000,000 new H shares to the public at a price of HK$1.90 per share and such H shares were listed on the Main Board of the Stock Exchange on 29 September 2006. In addition, 140,000,000 shares converted from certain Domestic Shares held by CNOOC were transferred to the National Council of the Social Security Fund of the PRC (the "NSSF").

In October 2006, as a result of the exercise of the over-allotment option as detailed in the Company's prospectus dated 18 September 2006, the Company issued 210,000,000 new H shares to the public at a price of HK$1.90 per share and such H shares were listed on the Main Board of the Stock Exchange on 16 October 2006. In addition, 21,000,000 shares converted from certain Domestic Shares held by CNOOC were transferred to the NSSF.

After deducting the share issue expenses of approximately RMB174,158,000, the Company raised net proceeds of approximately RMB2,932,336,000 from issuing the total of 1,610,000,000 H shares. The excess of the net proceeds over the paid-up capital of RMB1,610,000,000, amounting to RMB1,322,336,000, was credited to capital reserve (note 31).

The Company is in the process of registering the increase in the registered and paid-up capital from RMB 3,000,000,000 to RMB 4,610,000,000 with the Ministry of Commerce of the PRC.

31 RESERVES

Group

The amounts of the Group's reserves and the movements therein for the years ended 31 December 2006 and 2005 are presented in the consolidated statement of changes in equity set out on pages 56 to 58 of the financial statements.

Company

	Notes	Statutory surplus reserves	Capital reserve	Retained profits/ (accumulated losses)	Proposed dividend	Total
		RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
		(Note a)	(Note b)	(Note a)		
As at 1 January 2005		135,291	-	381,587	-	516,878
Net profit for the year	12	-	-	693,463	-	693,463
Proposed Special Dividend	13	-	-	(1,210,801)	1,210,801	-
Transfer from retained profits		137,845	-	(137,845)	-	-
On capitalisation of retained profits		-	-	(209,207)	-	(209,207)
As at 31 December 2005 and 1 January 2006		273,136	-	(482,803)	1,210,801	1,001,134
Net profit for the year	12	-	-	1,190,051	-	1,190,051
Capital contribution	(c)	-	7,607	-	-	7,607
Capitalisation as a result of the Reorganisation	(d)	(273,136)	(220,308)	-	-	(493,444)
Special Dividend declared	13	-	-	-	(1,210,801)	(1,210,801)
Pre-establishment Distribution declared	13	-	-	(264,538)	-	(264,538)
Pre-IPO Profit declared	13	-	-	(302,142)	-	(302,142)
Proposed 2006 final dividend		-	-	(69,150)	69,150	-
Transfer from retained profits		68,732	-	(68,732)	-	-
Share premium arising from the issuance of H shares	30	-	1,496,494	-	-	1,496,494
Share issue expenses	30	-	(174,158)	-	-	(174,158)
As at 31 December 2006		**68,732**	**1,109,635**	**2,686**	**69,150**	**1,250,203**

Notes:

(a) In accordance with the articles of association of the Company approved by the relevant government authorities on 25 April 2006, the profit after tax of the Company for the purpose of profit distribution will be deemed to be the lesser of (i) the net profit determined in accordance with PRC GAAP and (ii) the net profit determined in accordance with IFRS following the listing of the Company's shares on the Stock Exchange. On this basis, the net profit available for distribution (after the Pre-establishment Distribution and the Pre-IPO Profit and the appropriation of reserves, as further explained below) was approximately RMB71,836,000, being the amount determined in accordance with IFRS.

Under the PRC Company Law and the Company's articles of association approved on 25 April 2006, net profit after tax could only be distributed as dividends after an allowance has been made for the following:

(i) Making up prior years' cumulative losses, if any;

(ii) Allocations to the statutory common reserve fund of at least 10% of profit after tax, until the fund aggregates to 50% of the Company's share capital. For the purpose of calculating the amount of transfer to reserves, the profit after tax shall be the amount determined under PRC GAAP. The transfer to this reserve must be made before any distribution of dividends to shareholders; and

(iii) Allocations to the discretionary common reserve if approved by the shareholders.

The above reserves cannot be used for purposes other than those for which they are created and are not distributable as cash dividends.

For dividend distribution purposes, the amount which the Company's subsidiaries and its jointly-controlled entity can legally distribute by way of a dividend is determined with reference to their profits available for distribution as reflected in their respective PRC statutory financial statements, which are prepared in accordance with PRC GAAP. These profits may differ from those reflected in this report which is prepared in accordance with IFRS.

(b) As at 31 December 2006, the capital reserve account balance included the Company's share premium of RMB 1,322,336,000 (note 30).

(c) The details are set out in note (b) to the consolidated statement of changes in equity on pages 56 to 58 of the financial statements.

(d) The details are set out in note (c) to the consolidated statement of changes in equity on pages 56 to 58 of the financial statements.

32 BENEFITS LIABILITY

Tianye, the Company's 90%-owned subsidiary, provides post-employment allowances covering substantially all of its employees, and also early retirement benefits to qualifying retirees.

The following tables summarise the components of net benefits expense recognised in the consolidated income statement and amounts recognised in the consolidated balance sheet.

The details of net benefits expense by each type of benefits for the year ended 31 December 2006 are as follows:

Group

	Early retirement benefits	Post-employment allowances	Total
	RMB'000	RMB'000	RMB'000
Current service cost	1,196	600	1,796
Interest cost on benefits obligation	679	522	1,201
Net actuarial gain recognised for the year	(45)	(34)	(79)
Net benefits expense	**1,830**	**1,088**	**2,918**

The details of benefits liability by each type of benefits as at 31 December 2006 are as follows:

	Early retirement benefits	Post-employment allowances	Total
	RMB'000	RMB'000	RMB'000
Defined benefit obligation	39,948	29,978	69,926
Unrecognised net actuarial gain	10,455	(423)	10,032
Benefits liability	**50,403**	**29,555**	**79,958**

The details of changes in present value of the defined benefit obligation by each type of benefits during the year are as follows:

	Early retirement benefits	Post-employment allowances	Total
	RMB'000	RMB'000	RMB'000
At beginning of year	-	-	-
Acquisition of a subsidiary	39,814	30,033	69,847
Current service cost	1,196	600	1,796
Interest cost	679	522	1,201
Benefits paid	(1,741)	(1,177)	(2,918)
Actuarial gains on obligation	10,455	(423)	10,032
At end of year	**50,403**	**29,555**	**79,958**

The Group is expected to incur a net benefits expense of RMB 8,660,000 for the year ending 31 December 2007.

The principal assumptions used in determining the early retirement benefits obligation and post-employment allowances of the Group as at 31 December 2006 are shown below:

Discount rate	4.00%
Early retirement rate	1.00%
Inflation rate	4.00%

The directors have reviewed the actuarial valuation as at 31 December 2006 which was performed by Watson Wyatt Consultant (Shanghai) Ltd., an independent actuary service provider, using the valuation method detailed under the heading "Employee Benefits" in note 2.4 to the financial statements, and considered that the Group's current provision for the net benefits expenses were adequate for the year ended 31 December 2006.

33 INTEREST-BEARING BANK AND OTHER BORROWINGS

Group

	Effective interest rate (%)	Maturity	2006	2005
			RMB'000	RMB'000
Current				
Bank loans				
- Unsecured				
- Yen loan	LIBOR+0.6	2007	**146,056**	152,926
- U.S.$ loan	LIBOR+0.5 – LIBOR+0.65	2007	**23,909**	119,225
- RMB loan	5.2 - 5.8	2007	**303,074**	3,714
			473,039	275,865
Other loans				
- Obligations under finance lease (note 38)	2.25 – 6.03	2007	**908**	-
- Secured	4.7	2006	**-**	57,015
- Unsecured	5.0 - 5.5	2007	**2,632**	2,500
			3,540	59,515
			476,579	335,380
Non-current				
Bank loans				
- Secured	6.1	2007	**-**	2,300
- Unsecured				
- Yen loan	LIBOR+0.6	2008	**73,106**	917,535
- U.S.$ loan	LIBOR+0.65	2014	**239,023**	99,389
- RMB loan	5.2 - 5.8	2016	**38,999**	7,428
			351,128	1,026,652
Other loans				
- Obligations under finance lease (note 38)	2.25 – 6.03	2008	**236**	-
- Unsecured	5.2 - 5.5	2016	**33,429**	3,750
			33,665	3,750
			384,793	1,030,402
			861,372	1,365,782

Group (continued)

	2006 RMB'000	2005 RMB'000
Analysed into:		
Bank loans repayable:		
Within one year or on demand	**473,039**	275,865
In the second year	**115,878**	181,321
In the third to fifth years, inclusive	**128,318**	539,486
Beyond five years	**106,932**	305,845
	824,167	1,302,517
Other loans repayable:		
Within one year or on demand	**3,540**	59,515
In the second year	**5,379**	3,750
In the third to fifth years, inclusive	**15,429**	-
Beyond five years	**12,857**	-
	37,205	63,265
	861,372	1,365,782

As at 31 December 2005, certain of the Group's bank borrowings were secured by certain of the Group's buildings and machinery, which had an aggregate net carrying amount of RMB8,462,000. The pledges were released in full upon the repayment of the related bank borrowings for the year ended 31 December 2006.

As at 31 December 2006, the Group had an outstanding loan of RMB36,060,000 (2005: RMB6,250,000), which was obtained from CNOOC Finance. The loan is unsecured, bears interest at rate of 5.5% per annum (2005: 5.0%-5.2% per annum) and is repayable by 2016. As at 31 December 2006, the obligations under finance lease of RMB1,144,000 (2005: Nil) were due to a CNOOC group company. Further details are set out in note 38 to the financial statements.

As at 31 December 2005, included in the above secured other loans of the Group were short-term loans of RMB57,015,000 obtained by discounting the commercial acceptance drafts with recourse. CNOOC Finance provided services for discounting the commercial acceptance drafts to the Group with terms similar to those offered by other financial institutions. As at 31 December 2006, there were no short-term loans from discounting the commercial acceptance drafts with recourse.

Details of corporate guarantees provided by the Group's related companies in connection with the bank borrowings obtained by the Group in prior year are set out in note 42 to the financial statements.

Company

	Effective interest rate (%)	Maturity	2006 RMB'000	2005 RMB'000
Current				
Unsecured bank loans	LIBOR+0.6 – 5.2	2007	**446,056**	152,926
Secured other loans	4.7	2006	-	38,716
			446,056	191,642
Non-current				
Unsecured bank loans	LIBOR+0.6	2008	**73,106**	917,535
			519,162	1,109,177
Analysed into:				
Bank and other loans repayable:				
Within one year or on demand			**446,056**	191,642
In the second year			**73,106**	152,923
In the third to fifth years, inclusive			-	458,767
Beyond five years			-	305,845
			519,162	1,109,177

As at 31 December 2005, certain of the Company's bank and other borrowings with an aggregate carrying amount of RMB1,070,461,000 were guaranteed by the Company's ultimate holding company. The guarantees provided by the ultimate holding company were released in full during the year.

As at 31 December 2005, included in the above secured other loans of the Company were short-term loans of RMB38,716,000 obtained by discounting the commercial acceptance drafts with recourse. CNOOC Finance provided services for discounting the commercial acceptance drafts to the Company with terms similar to those offered by other financial institutions. As at 31 December 2006, there were no short-term loans from discounting the commercial acceptance drafts with recourse.

As at 31 December 2006, the carrying amounts of the Group's and the Company's bank and other borrowings approximate their fair values.

34 OTHER LONG-TERM LIABILITIES

Group

As at 31 December 2006, other long-term liabilities of the Group mainly represented a government grant of RMB25,470,000 (2005: RMB15,790,000) received by Hainan Basuo from the Ministry of Communication of the PRC and deferred rental income of RMB5,654,000 (2005: Nil), after elimination of the Group's 60% interest therein, received from the Group's jointly-controlled entity.

The government grant is for the specific purpose of the future renovation of the port facilities operated by Hainan Basuo.

Company

As at 31 December 2006, other long-term liabilities of the Company mainly represented deferred rental income of RMB 21,295,000 (2005: Nil) received from its subsidiaries and its jointly-controlled entity.

35 TRADE PAYABLES

The trade payables are non-interest-bearing and are normally settled from thirty to sixty days. An aged analysis of trade payables, based on invoice dates, of the Group and of the Company is as follows:

	2006	2005
	RMB'000	RMB'000
Within six months	**89,021**	39,270
Over six months but within one year	**348**	2,924
Over one year but within two years	**2,753**	615
Over two years but within three years	**1,778**	354
Over three years	**786**	4,886
	94,686	48,049

As at 31 December 2006, the amounts due to CNOOC group companies and a jointly-controlled entity included in the above trade payable balances were RMB54,041,000 (2005: RMB31,969,000) and RMB1,265,000 (2005: Nil), respectively.

The amounts due are unsecured, non-interest-bearing and have no fixed terms of repayment.

Company

	2006	2005
	RMB'000	RMB'000
Within six months	**42,077**	35,370
Over six months but within one year	**-**	-
Over one year but within two years	**-**	5
Over two years but within three years	**-**	192
Over three years	**68**	6,281
	42,145	41,848

The amounts due to CNOOC group companies, subsidiaries and a jointly-controlled entity included in the above can be analysed as follows:

	2006	2005
	RMB'000	RMB'000
CNOOC group companies	**34,375**	31,969
Subsidiaries	**2,314**	190
A jointly-controlled entity	**3,162**	-
	39,851	32,159

The amounts due are unsecured, non-interest-bearing and have no fixed terms of repayment.

36 OTHER PAYABLES AND ACCRUALS

Group

	2006	2005
	RMB'000	RMB'000
Advances from customers	**146,878**	19,235
Accruals	**10,336**	74,044
Other payables	**645,195**	487,644
Due to the ultimate holding company	-	2,172
Due to CNOOC group companies	**42,119**	3,772
Due to an associate	**5,303**	1,669
Due to a jointly-controlled entity	**132**	-
	849,963	588,536

Company

	2006	2005
	RMB'000	RMB'000
Advances from customers	**28,992**	9,436
Accruals	**3,915**	24,779
Other payables	**82,412**	55,077
Due to the ultimate holding company	**-**	2,172
Due to CNOOC group companies	**2,466**	2,654
Due to an associate	**4,925**	500
Due to subsidiaries	**84,703**	5,086
Due to a jointly-controlled entity	**331**	-
	207,744	99,704

The amounts due are unsecured, non-interest-bearing and have no fixed terms of repayment.

37 DERIVATIVE FINANCIAL INSTRUMENTS

In 2001, the Company entered into a cross currency interest rate swap contract with a financial institution to sell United States dollars ("U.S.$") in exchange for Japanese Yen ("JPY") in order to partially offset the potential fluctuation in future repayments of certain Japanese Yen denominated loans (the "Japanese Yen loans") and their related interest payments in U.S.$ equivalent. The Japanese Yen loans are subject to floating six-month LIBOR plus 0.6% per annum while the interest rate stipulated in this swap contract for the U.S.$ is fixed at a rate of 3.93% per annum. The contractual exchange rate is JPY124/U.S.$1.

This swap contract did not meet the criteria for hedge accounting of IAS 39 as the Company did not prepare the required formal designation and documentation specifying how the hedge effectiveness would be assessed throughout the life of hedge relationship from the outset. As such, changes in the fair values of this non-hedging cross currency interest rate swap contract have been reported as other income and gains or other expenses in the consolidated income statement for the years ended 31 December 2006 and 2005.

The notional/contract amount of this swap contract indicates the volume of transaction outstanding as at the balance sheet date i.e. the outstanding Japanese Yen loan amounts or their U.S.$ equivalents as at that date. The notional amount changes according to a fixed amortised schedule with a notional amount of U.S.$116,970,000 or JPY13,353,571,000 as at 31 December 2006 and amortised subsequently to U.S.$97,434,000 or JPY11,127,257,000 in the last coupon period before it matures on 20 June 2008. The cross currency interest rate swap contract is carried as an asset when the fair value is positive and a liability when the fair value is negative as at each balance sheet date. The fair value of the cross currency interest rate swap contract as of 31 December 2006 and 2005 is detailed as follows:

Group and Company

	2006	2005
	RMB'000	RMB'000
Cross currency interest rate swap contract	**(25,641)**	(50,634)

38 OBLIGATIONS UNDER FINANCE LEASE

The Group has finance lease contracts for certain computer equipment with a CNOOC group company. The lease has a term of renewal, but no purchase option and escalation clauses. Renewals are at the option of the Group.

At 31 December 2006, the future minimum lease payments under finance lease and the present value of the minimum lease payments are as follows:

	Minimum lease payments	Present value of minimum lease payments
	RMB'000	RMB'000
Amounts payable:		
Within one year	**939**	**908**
In the second year	**251**	**236**
Total minimum finance lease payments	**1,190**	**1,144**
Future finance charges	**(46)**	
Total net finance lease payables	**1,144**	
Portion classified as current liabilities (note 33)	**(908)**	
Non-current portion (note 33)	**236**	

39 NOTES TO THE CONSOLIDATED CASH FLOW STATMENT

(a) Formation of a subsidiary

In 2005, the Company and SASAC of Hainan Province, the PRC ("Hainan SASAC") established Hainan Basuo, which was engaged in port operation. The Group contributed cash of RMB304,200,000 into Hainan Basuo, representing a 72.5% equity interest in Hainan Basuo while Hainan SASAC contributed net assets.

The carrying amounts of the net assets contributed by Hainan SASAC at the date of formation of Hainan Basuo were as follows:

	Notes	RMB'000
Property, plant and equipment	15	297,819
Prepaid land lease payments	17	57,407
Available-for-sale equity investments		12,167
Investment in an associate		978
Trade receivables		35,097
Prepayments, deposits and other receivables		79,040
Tax recoverable		25
Cash and bank balances		11,938
Other payables and accruals		(358,175)
Interest-bearing bank and other borrowings		(20,896)
		115,400

(b) Transfer of a subsidiary to a CNOOC group company

The Group transferred its entire equity interest of 84% in Hainan CNOOC Agriculture Co., Ltd. to a CNOOC group company, which was treated as a reduction in capital contributed by CNOOC with an effective date of 31 December 2005. Further details are set out in note 1 to the financial statements.

The carrying amounts of the assets and liabilities of Hainan CNOOC Agriculture Co., Ltd. as at the date of the equity transfer were as follows:

	Notes	RMB'000
Net assets transferred:		
Property, plant and equipment	15	3,625
Prepaid land lease payments	17	4,937
Other long-term assets		512
Trade receivables		136
Prepayments, deposits and other receivables		340
Cash and bank balances		1
Trade payables		(1,652)
Income tax payable		(99)
Other payables and accruals		(2,097)
Interest-bearing bank and other borrowings		(2,772)
Minority interests		(482)
		2,449

An analysis of the net outflow of cash and cash equivalents in respect of the transfer of a subsidiary to a CNOOC group company is as follows:

	2005
	RMB'000
Cash consideration	-
Cash and bank balances	(1)
Net outflow of cash and cash equivalents in respect of the transfer of a subsidiary	(1)

The results of the subsidiary transferred in the year ended 31 December 2005 had no significant impact on the Group's consolidated revenue or profit after tax for that year.

(c) Transfer of available-for-sale equity investments

The Group has transferred available-for-sale equity investments which included amounts of RMB27,874,000 and RMB15,000,000 invested in Haiwan Fudao Hotel and Sanya Resort Co., Ltd., respectively, to a CNOOC Group company. The transfer of these investments was treated as a reduction in capital contributed by CNOOC with an effective date of 31 December 2005. Further details are set out in note 1 to the financial statements.

(d) Dissolution of a subsidiary

Subsequent to the acquisition of Tianye, one of its subsidiaries, namely Inner Mongolia Jie Da Chemical Co., Ltd. ("Jie Da"), was declared bankrupt in March 2006. As at the date of Jie Da's bankruptcy, the carrying amounts of the assets and liabilities of Jie Da were as follows:

	Notes	RMB'000
Net liabilities disposed of:		
Property, plant and equipment	15	1,021
Trade receivables		220
Prepayments, deposits and other receivables		361
Inventories		246
Trade payables		(3,656)
Other payables and accruals		(1,338)
		(3,146)
Group's receivables written off		2,539
Gain on dissolution of a subsidiary	5	586
Net outflow of cash and cash equivalents from dissolution of a subsidiary		(21)

(e) Business combination

In November and December 2005, the Company entered into an equity transfer agreement with each of the four equity holders of Tianye to acquire a 90% equity interest in Tianye for an aggregate cash consideration of RMB964,641,000 (the "Acquisition"). The cash consideration was payable to three of the equity holders which together held 80.92% equity interests in Tianye. The remaining 9.08% equity interest in Tianye was transferred from the SASAC of the Inner Mongolia Autonomous Region People's Government to the Company at nil consideration. The transfer of the 9.08% equity interest in Tianye has given rise to a PRC corporate income tax provision of RMB8,120,000, which was capitalised as part of the Company's investment in Tianye.

Out of the total cash consideration of RMB964,641,000 paid for the acquisition of equity interests in Tianye by the Company, an amount of RMB891,118,000 for the acquisition of a 74.74% equity interest in Tianye from an equity holder was paid on 19 January 2006. The remaining cash consideration of RMB73,523,000 for the acquisition of a combined 6.18% equity interest in Tianye from the other two equity holders was fully paid on 7 March 2006.

Tianye recorded an amount of interest-bearing bank loans denominated in Japanese Yen borrowed from the Export-Import Bank of China (the "Japanese Yen Loans"), related penalty interest and late fee payables thereon due to the late repayment of the Japanese Yen Loans (collectively the "Japanese Yen Loan Obligations") as at 19 January 2006. In addition, it also had an amount due to the Inner Mongolia Finance Bureau (the "Finance Bureau") as at 19 January 2006 arising from the previous settlement of part of the Japanese Yen Loan obligations with the Export-Import Bank of China by the Finance Bureau on behalf of Tianye. Pursuant to the document Caijin [2006] No.3 issued by the Ministry of Finance on 12 January 2006 (the "MOF Document"), there was a waiver of the entire penalty interest and late fee payables, and 50% of certain related bank charges included in Tianye's Japanese Yen Loan Obligations as at 31 December 2005 (the "Waiver"). In connection with the Acquisition, and pursuant to the MOF Document, on 28 February 2006, Tianye entered into four tripartite loan transfer agreements with the Export-Import Bank of China and the Finance Bureau under which it transferred its Japanese Yen Loan Obligations to the Finance Bureau. After the completion of the above-mentioned transfer, Tianye, however, was required to pay the Finance Bureau 50% of the Japanese Yen Loan Obligations after the Waiver. Consequently, the Finance Bureau has in effect agreed to assume 50% of Tianye's Japanese Yen Loan Obligations after the Waiver. In addition, in connection with the four tripartite loan transfer agreements, the Finance Bureau has waived 50% of the amount due to it by Tianye arising from its previous settlement of part of the Japanese Yen Loan obligations on behalf of Tianye.

Upon completion of the aforesaid four tripartite loan transfer agreements and as a result of the waivers by the Finance Bureau, in February 2006, the total obligations of Tianye in respect of the Japanese Yen Loans, related penalty interest and late fee payables, and the amount due to the Finance Bureau were reduced by a total amount of RMB1,019,296,000, from an aggregate amount of RMB1,917,822,000 as at 19 January 2006 to RMB898,526,000, which was fully repaid to the Finance Bureau during the year.

39 NOTES TO THE CONSOLIDATED CASH FLOW STATMENT (continued)

(e) Business combination (continued)

The fair values of the identifiable assets and liabilities of Tianye as at the date of acquisition (i.e. 19 January 2006) and the corresponding carrying amounts immediately before the Acquisition were as follows:

	Notes	Fair value recognised on acquisition RMB'000	Carrying amount RMB'000
Property, plant and equipment	15	2,367,433	2,332,900
Prepaid land lease payments	17	249,659	80,624
Intangible assets	18	968	968
Deferred tax assets	23	27,850	27,850
Inventories		90,990	87,617
Trade receivables		11,158	11,158
Bills receivable		12,221	12,221
Prepayments, deposits and other receivables		12,204	12,204
Pledged bank deposits		20,918	20,918
Non-pledged time deposits with original maturity of three months or more when acquired		100,000	100,000
Cash and cash equivalents		72,396	72,396
Trade payables		(5,064)	(5,064)
Other payables and accruals		(1,087,772)	(1,087,772)
Interest-bearing bank and other borrowings		(1,346)	(1,346)
Benefits liability		(80,036)	(80,036)
Income tax payable		(6,466)	(6,466)
Deferred tax liabilities	23	(61,017)	-
Minority interests		(173,716)	(159,124)
		1,550,380	1,419,048
Excess over the cost of a business combination recognised in the consolidated income statement		(577,619)	
		972,761	
Satisfied by:			
Cash		964,641	
Income tax payable		8,120	
		972,761	

In the opinion of directors, the Waiver formed part of the acquisition of Tianye by the Company. Accordingly, the effect of the Waiver was taken into consideration in determining the fair values of the identifiable assets and liabilities of Tianye as at the date of the acquisition, thereby giving rise to the excess over the cost of a business combination recognised in the Acquisition of RMB577,619,000.

An analysis of the net outflow of cash and cash equivalents in respect of the Acquisition is as follows:

	RMB'000
Cash consideration	(964,641)
Cash and cash equivalents acquired	72,396
Net outflow of cash and cash equivalents in respect of the Acquisition	(892,245)

The results of Tianye have been consolidated into the Group since 19 January 2006. Since its acquisition, Tianye has contributed RMB 1,009,041,000 to the Group's consolidated turnover and RMB141,183,000 to the consolidated profit for the year ended 31 December 2006.

Had the business combination taken place at the beginning of the current year, the consolidated turnover and consolidated profit of the Group for the year ended 31 December 2006 would have been RMB3,533,506,000 and RMB1,676,534,000, respectively.

40 OPERATING LEASE ARRANGEMENTS

(i) As lessor

Group

As at 31 December 2006 and 2005, the Group had no significant future minimum lease receivables under non-cancellable operating leases.

Company

The Company leases certain of its buildings under operating lease arrangements with leases negotiated for terms from one year to twenty years to its subsidiaries.

As at 31 December 2006 and 2005, the Company had total future minimum lease receivables from the subsidiaries of the Company under non-cancellable operating leases falling due as follows:

	2006	2005
	RMB'000	RMB'000
Within one year	**536**	517
In the second to fifth years, inclusive	**2,143**	2,069
After five years	**5,021**	5,698
	7,700	8,284

(ii) As lessee

As at 31 December 2006 and 2005, the Group and the Company had no significant future minimum lease payments under non-cancellable operating leases.

41 COMMITMENTS AND CONTINGENT LIABILITIES

(i) Capital commitments

Group

	2006 RMB'000	2005 RMB'000
Contracted, but not provided for:		
- Acquisition of land and buildings	46,826	50,263
- Acquisition of plant and machinery	5,147	58
	51,973	50,321
Authorised, but not contracted for:		
- Acquisition of land and buildings	132,267	196,842
- Acquisition of plant and machinery	3,986,496	1,781
	4,118,763	198,623
	4,170,736	248,944

Company

	2006 RMB'000	2005 RMB'000
Contracted, but not provided for:		
- Acquisition of plant and machinery	5,043	-
Authorised, but not contracted for:		
- Acquisition of land and buildings	32,200	-
- Acquisition of plant and machinery	3,949,653	1,560
	3,981,853	1,560
	3,986,896	1,560

In addition, the Group's and the Company's share of the jointly-controlled entity's own capital commitments, which are not included in the above, is as follows:

	2006 RMB'000	2005 RMB'000
Contracted, but not provided for:		
- Acquisition of plant and machinery	-	265,735
Authorised, but not contracted for:		
- Acquisition of plant and machinery	-	260,613
	-	526,348

(ii) Contingent liabilities

Group

	2006 RMB'000	2005 RMB'000
Guarantees given to a bank in connection with banking facilities granted to and utilised by a CNOOC group company	-	294,000

Company

	2006 RMB'000	2005 RMB'000
Guarantees given to banks in connection with banking facilities granted to and utilised by :		
- A CNOOC group company	-	294,000
- Subsidiaries	-	7,183
- A jointly-controlled entity	341,066	99,389
	341,066	400,572

The guarantees given to a bank in connection with the banking facilities granted to and utilised by the CNOOC group company were released in full in June 2006.

42 RELATED PARTY TRANSACTIONS

During the year, the Group had the following material transactions with related parties:

(1) Recurring

	Notes	2006	2005
		RMB'000	RMB'000
Purchases of raw materials from CNOOC group companies	(i)	**433,032**	350,866
Sale of goods to associates	(i)	**260,346**	196,559
Sale of goods to a CNOOC group company	(i)	**14,361**	-
Provision of transportation services to an associate	(ii)	**11,361**	5,739
Interest income from a CNOOC group company	(iii)	**6,895**	11,356
Interest expense to a CNOOC group company	(iii)	**1,546**	124
Rental income from a jointly-controlled entity	(iv)	**132**	-
Rental fees to CNOOC group companies	(v)	**1,895**	250
Provision of construction and installation services from CNOOC group companies	(vi)	**94,760**	32,877
Provision of transportation services from CNOOC group companies	(vi)	**9,697**	-
Provision of human resource services from a CNOOC group company	(vi)	**8,233**	-
Use of CNOOC trademark	(vii)	**-**	-

Notes:

(i) These transactions were conducted in accordance with terms agreed between the Group, its associate and CNOOC group companies.

(ii) Transportation income was based on mutually agreed terms with reference to the market rate.

(iii) Interest income/expense was based on mutually agreed terms with reference to the market rate for corresponding amounts and periods.

(iv) Rental income was based on mutually agreed terms.

(v) Rental fees were based on mutually agreed terms with reference to the market rate.

(vi) These services were charged based on mutually agreed terms.

(vii) The CNOOC trademark owned by CNOOC was used by the Group at nil consideration.

The amounts of transactions with a jointly-controlled entity disclosed in the table above were arrived at after deducting the Group's share portion, which was eliminated in the proportionate consolidation of the Group's investment in the jointly-controlled entity.

Except for the rental income from a jointly-controlled entity, the sale of goods to associates and the provision of transportation services to an associate, the above recurring related party transactions also constitute continuing connected transactions as defined in Chapter 14A of the Listing Rules.

42 RELATED PARTY TRANSACTIONS (continued)

(2) Non-recurring

	Notes	2006	2005
		RMB'000	RMB'000
Provision of utilities to a CNOOC group company	(i)	**14,461**	12,536
Interest expense to the ultimate holding company	(ii)	**8,897**	-
Fees and charges to a CNOOC group company	(iii)	**5,569**	-
Sale of goods to the ultimate holding company	(iv)	**3,719**	-

Notes:

(i) The transaction was conducted in accordance with terms agreed between the Group and the CNOOC group company.

(ii) Interest expense was charged at a contract rate of 2.07% per annum.

(iii) Fees and charges were based on mutually agreed terms.

(iv) These transactions were conducted in accordance with terms agreed between the Group and its ultimate holding company.

(3) Guarantees provided by related parties of the Group

The Group's related parties have provided corporate guarantees, in connection with bank borrowings obtained by the Group, as follows:

	2006	2005
	RMB'000	RMB'000
Guarantees provided to the Group by :		
- the ultimate holding company	-	1,070,461
- CNOOC group companies	-	126,935
	-	1,197,396

The guarantees provided by the ultimate holding company and the CNOOC group companies to banks in connection with the banking facilities granted to and utilised by the Group were released in full in June 2006.

(4) Balances with related parties

Except for the balances with CNOOC Finance, one of the CNOOC group companies, the balances due from/to related parties of the Group mainly resulted from trading transactions and miscellaneous amounts reimbursable by/to these related parties. Further details are set out in notes 25, 27, 34, 35 and 36 to the financial statements.

As at 31 December 2006, the deposits placed by the Group and the Company with CNOOC Finance and the outstanding loans due to CNOOC Finance by the Group and the Company are summarised below:

Group

	2006 RMB'000	2005 RMB'000
Deposits placed with CNOOC Finance	**259,866**	1,098,690
Outstanding loans due to CNOOC Finance	**36,060**	63,265

Company

	2006 RMB'000	2005 RMB'000
Deposits placed with CNOOC Finance	**62,757**	766,949
Outstanding loans due to CNOOC Finance	**-**	38,716

Further details of the deposits placed with CNOOC Finance and the outstanding loans due to CNOOC Finance are set out in notes 29 and 33 to the financial statements, respectively.

(5) Compensation of key management personnel of the Group

	2006 RMB'000	2005 RMB'000
Short-term employee benefits	**4,696**	3,321
Post-employment benefits	**290**	188
Total compensation paid to key management personnel	**4,986**	3,509

Further details of directors' and supervisors' emoluments are set out in note 9 to the financial statements.

(6) Transactions with other state-owned enterprises in the PRC

The Group operates in an economic environment predominated by enterprises directly or indirectly owned or controlled by the PRC government through its numerous authorities, affiliates or other organisations (collectively the "State-owned Enterprises"). During the year, the Group had transactions with the State-owned Enterprises including, but not limited to, the sale of fertilisers and purchases of raw materials. The directors consider that transactions with such other State-owned Enterprises are activities in the ordinary course of the Group's business, and that the dealings of the Group have not been significantly or unduly affected by the fact that the Group and such other State-owned Enterprises are ultimately controlled or owned by the PRC government. The Group has also established pricing policies for products and services, and such pricing policies do not depend on whether or not the customers are State-owned Enterprises. Having due regard to the substance of the relationships, the directors are of the opinion that none of these transactions is a material related party transaction that requires separate disclosure.

43 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments other than derivatives, comprise bank loans, other interest-bearing loans and cash and short-term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities, such as trade receivables and trade payables, which arise directly from its operations.

The Group also enters into a cross currency interest rate swap contract, the purpose of which is to manage the exchange rate and interest rate risk arising from the Group's sources of finance.

The main risks arising from the Group's financial instruments are cash flow interest rate risk, foreign currency risk, credit risk and liquidity risk.

The Group does not have written risk management policies and guidelines. However, the management meets periodically to analyse and formulate measures to manage the Group's exposure to financial risk. Generally, the Group employs a prudent strategy regarding its risk management.

(i) Cash flow interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long-term debt obligations with a floating interest rate.

The Group monitors interest rate exposure and entered into a cross currency interest rate swap contract in which the Group agreed to exchange, at specified intervals, the difference between fixed and variable rate interest amounts calculated by reference to an agreed-upon notional principal amount, though the swap contract did not meet the criteria for hedge accounting. As at 31 December 2006, after taking into account the effect of the interest rate swaps, approximately 60% of the Group's borrowings are at fixed rate of interest.

The interest rates and the terms of repayment of the Group's bank and other borrowings are disclosed in note 33 to the financial statements.

(ii) Foreign currency risk

Foreign currency risk is the risk that the value of a financial instrument fluctuates because of the changes in foreign exchange rates.

The Group's monetary assets, loans and transactions are principally denominated in RMB, U.S.$ and JPY. The Group is exposed to foreign currency risk arising from the exposure of JPY and U.S.$ against RMB. At present, the Group reduces its exposure to JPY foreign exchange fluctuations by entering into a cross currency interest rate swap contract to partially offset against future repayments of certain Japanese Yen denominated loans and their related interest payments.

The Group will constantly review the economic situation and its foreign exchange risk profile, and will consider appropriate hedging measures in the future, as may be necessary.

(iii) Credit risk

The carrying amounts of cash and cash equivalents, available-for-sale equity investments, trade receivables, other receivables and other current assets except for prepayments and tax recoverable represent the maximum exposure of the Group to the credit risk in relation to financial assets. The majority of the Group's trade receivables are related to the sale of fertilisers which are normally settled on an advance receipt basis whereby the customers are required to pay in advance either by cash or by bank acceptance drafts.

The trading terms of the Group with its methanol customers are mainly on credit. The credit period is generally one month.

It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures and only long-standing customers are granted with credit terms. In addition, receivable balances are monitored on an ongoing basis and the Group's exposure to bad debts is not significant.

Since the Group trades only with recognised and creditworthy third parties, there is no requirement for collateral.

No other financial assets carry a significant exposure to credit risk.

(iv) Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans. In addition, banking facilities have been put in place for contingency purposes.

44 POST BALANCE SHEET EVENTS

During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law ("the New Corporate Income Tax Law") was approved and will become effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. Since the detailed implementation and administrative rules and regulations have not yet been announced, the financial impact of the New Corporate Income Tax Law to the Group cannot be reasonably estimated at this stage.

45 APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 3 April 2007.