HK$'000

Management's Discussion and Analysis

FINANCIAL REVIEW

Group's financial results:

Operating results and ratios	Year ended 31 December		
	2006	2005 Restated	Increase/ (decrease)
Revenue	**7,503,428**	5,786,386	29.7%
Gross profit	**528,830**	410,309	28.9%
Profit attributable to shareholders (Note)	**200,815**	221,703	(9.4%)
Earnings per share	**HK 4.65 cents**	HK 5.14 cents	(9.5%)
Gross profit margin [1]	**7.0 %**	7.1%	
Inventory turnover [2]	**7.9 times**	7.7 times	

Financial position and ratios	31 December		
	2006	2005	Increase/ (decrease)
Cash and bank balances	**850,744**	1,519,595	(44.0%)
Total assets	**9,328,361**	6,020,027	55.0%
Bank and other loans	**3,802,562**	1,905,616	99.5%
Equity attributable to shareholders	**3,225,343**	2,941,773	9.6%
Current ratio [3]	**1.7 times**	2.0 times	
Gearing ratio [4]	**54.1%**	39.3%	

1 gross profit / revenue x 100%
2 cost of sales / [(opening inventories + closing inventories) / 2]
3 current assets / current liabilities
4 bank and other loans / (equity attributable to shareholders of the Company + bank and other loans) x 100%

(Note) There was a gain on sales of coal exploration interests of HK$78.5 million (after tax: HK$55.0 million) in 2005. If only the profits arising from the ordinary activities are compared, there was an increase of 20.5% in 2006.

Management's Discussion and Analysis

FINANCIAL REVIEW (CONTINUED)

The Group has achieved a satisfactory financial performance for 2006. The delivery of its business strategy as an integrated provider of key natural resources continued and there were a number of encouraging initiatives and developments during the year.

The businesses and interests in Australia, including aluminium smelting, coal, import and export of commodities, continue to be the principal contributors and formed the basis for the satisfactory results of the Group in 2006. The manganese business has made a welcome contribution to the profits of the Group since the 2Q of 2006 when the Group completed the acquisition of such business.

Investment in oil has been identified as a particular focus for the Group. In November 2006, the Group has concluded the acquisition of a 51% participating interest in the production sharing contract relating to an oilfield in the Seram Island Non-Bula Block, Indonesia (the "Seram Oilfield"). One notable aspect of this acquisition is that the Group also became the operator responsible for managing and operating exploration and development at the Seram Oilfield which marks a change in the Group's strategy for oil investments from passive holdings to an involvement.

The Group plans to increase its oil production capacity through development of existing interests and through acquisitions.

The following is a comparison of the results of each segment between 2005 and 2006.

Aluminium smelting

- Revenue ▲ 40%
  Net profit after tax (from ordinary activities) ▼ 20%

- Revenue was driven by higher selling prices, though it was partly offset by a drop in sales volume. The production in 2006 was slightly affected by the problem of the rectifier experienced in November 2005 which caused damages to some pots. The production was fully recovered in the 4Q of 2006. Insurance claim of HK$26.0 million was received.

- The decrease in net profit was mainly caused by the loss arising from the revaluation of the embedded derivatives. As a consequence of the adoption of Hong Kong Financial Reporting Standards, a component of the Electricity Supply Agreement (the "ESA") which is linked to the market price of aluminium is considered as a financial instrument embedded in the ESA. Such embedded derivatives need to be marked to market at the balance sheet date based on the future aluminium prices. As the future aluminium price has increased, the revaluation of the embedded derivatives resulted in unrealised losses of HK$111.7 million (2005: HK$13.2 million) and they were included in "Cost of sales" in the consolidated income statement.

  Another key reason for the drop in the net profit was the hedge loss of HK$162,522,000 (2005: HK$31,678,000). Such was also included in "Cost of sales" in the consolidated income statement.

  The underlying operation performed better than 2005 though there were increases in production costs, particularly for alumina and electricity which are linked to the market price of aluminium.

Management's Discussion and Analysis

FINANCIAL REVIEW (CONTINUED)

Coal

- Revenue ▲ 6%
  Net profit after tax (from ordinary activities) ▲ 31%

- The sale volume was slightly lower in 2006 compared to 2005 while the average selling price was similar between two years. Much of the increase in revenue was due to the appreciation of the Australian dollars.

- Despite the significant cost pressures across the mining industry, increase in mining costs was contained to around 6%. The Group received higher dividend payments from Macarthur Coal Limited. In 2006, the dividend income was HK$55.1 million (2005: HK$19.8 million)

Import and export of commodities

- Revenue ▲ 18%
  Net profit after tax (from ordinary activities) ▲ 10%

  The following table shows a breakdown of revenue and net profit before tax for 2006 and a comparison with 2005:

			Exports					
		Total	**Alumina**	**Iron ore**	**Steel**	**Others**	**Imports**	**Others**
Revenue	HK$ million	**5,074.1**	1,070.8	1,471.9	922.4	57.0	883.7	668.3
	Compare to 2005	**▲ 18%**	▼ 36%	▼ 9%	new line	▼ 66%	▲ 24%	▲412%
Net profit before tax	HK$ million	**79.6**	43.3	7.6	2.6	0.6	25.2	0.3
	Compare to 2005	**▲ 10%**	▲ 37%	▲ 21%	new line	▼ 87%	▲ 16%	▼ 96%

- The increase in revenue and net profit was partly due to the appreciation of the Australian dollars.

- Exported products include alumina and iron ore sourced from Australia and other countries exported to the People's Republic of China (the "PRC"). Alumina exports remained the largest contributor to the net profit though revenue largely decreased due to tight supply in early 2006. Significant profits were achieved on some cargoes in the early 2006, before the spot alumina prices dropped sharply from the 2Q of 2006.

  Iron ore exports decreased in terms of volume. Despite such, the profit margins improved, reflecting firmer iron ore prices and continued demand from the steel mills in the PRC. Iron ore was sourced from various origins including Australia, India, South Africa and Brazil.

  A positive development has been the commencement in the 1H of 2006 of a new trading line exporting Chinese steel to Europe and the Middle East, which largely offset the lower alumina and iron ore sales.

  CITIC Australia Trading Limited ("CATL") has been proactively working on sourcing products to support its export business and now have in place long term off-take contracts for alumina and iron ore. It is positive about its long term prospects of increasing iron ore sales particularly into the PRC market to become a major trading line alongside its alumina exports. CATL is encouraged by the commencement of exports of Chinese steel during 2006 and hopes to develop this into a regular and profitable trading line.

Management's Discussion and Analysis

FINANCIAL REVIEW (CONTINUED)

Imports continued to increase their contribution to overall profit. The steel and battery divisions performed strongly while the tyre and wheel imports faced increasing competition. The continued profit growth of the import division is very encouraging.

- CATL continues its strategy of diversification by developing multiple trading lines to reduce its relative reliance upon earnings from alumina. Alumina spot prices were extremely volatile during the year, but have experienced a strong recovery since the beginning of 2007. The iron ore market has been steady. The steel market has seen some moderate strengthening. CATL is monitoring developments in each of its trading lines and stays cautious.

- While trading is volatile in its nature, CATL's experienced trading team consistently and continuously strives to identify and capture profitable trading opportunities that balance minimum risk and maximum returns for its shareholders.

Manganese

- In February 2006, the formation of a sino-foreign equity joint venture to undertake the business of manganese mining and processing was completed. The newly established joint venture company, namely, CITIC Dameng Mining Industries Limited (the "Manganese Company"), became a non-wholly-owned subsidiary of the Group from then. As the Company has controlling interest in the Manganese Company, the financial results of the Manganese Company were consolidated into the accounts of the Group as from the 2Q of 2006. Since then, it has made a welcome contribution to the profits of the Group.

- The Manganese Company will be endeavouring to obtain greater efficiency and productivity in the future.

Crude Oil

- Oilfield in the PRC
  In February 2006, the Group exercised its option to convert its 40% participating interest in the Kongnan Block within the Dagang Oilfield in the PRC into common shares in the share capital of Ivanhoe Energy Inc. ("Ivanhoe") and a loan repayable by Ivanhoe. There were some gains in the disposal of the Ivanhoe shares.

- Oilfield in Indonesia
  In November 2006, CITIC Seram Energy Limited ("CITIC Seram"), an indirect wholly-owned subsidiary of the Group, concluded the acquisition of a 51% participating interest in the production sharing contract relating to the Seram Oilfield. In 2006, the average production of oil from the Seram Oilfield was above 4,700 barrels per day. From the completion date of the acquisition to the end of the year, no sales were recorded. Similar to other jointly-controlled assets of the Group, the Group's share of the revenue, expenses, assets and liabilities in the Seram Oilfield are taken into the accounts of the Group as from December 2006.

Management's Discussion and Analysis

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

Cash

As at 31 December 2006, the Group had a cash balance of HK$850.7 million.

In February and April 2007, the Company has allotted and issued totaling 700,000,000 new shares at a price of HK$2.46 per new share. The net proceeds of the subscription amounted to HK$1,683.0 million.

Borrowings

As at 31 December 2006, the Group had outstanding borrowings of HK$3,802.6 million, which comprised secured bank loans of HK$878.7 million, unsecured bank loans of HK$2,465.0 million and unsecured other loans of HK$458.9 million. The secured bank loans were secured by the Group's 22.5% participating interest in the Portland Aluminium Smelter joint venture, the fixed assets, prepaid land lease premiums, letter of credit and mining right of the manganese coal mines, and guarantees mostly provided by Guangxi Dameng Manganese Industry Co., Ltd. The bank trade finance facilities available to CATL are guaranteed by CITIC Resources Australia Pty Limited.

Most transactions of CATL are debt funded, which means CATL is highly geared. However, in contrast to term loans, CATL's borrowings are transaction specific and of short duration, matching the term of the underlying trade. When sales proceeds are received at the completion of a transaction, the related borrowings are repaid accordingly.

As at 31 December 2006, there was an increase in the Group's total outstanding borrowings caused by the growth of the business, the gearing ratio of the Group was 54.1%. Of the total outstanding borrowings, HK$1,588.0 million was repayable within one year. There was no adverse change to the financial position of the Group.

Share Capital

In a special general meeting of the Company held on 20 March 2007, an ordinary resolution was passed that the authorized share capital of the Company of HK$300 million divided into 6,000,000,000 ordinary shares of HK$0.05 each be and is hereby increased to HK$500 million divided into 10,000,000,000 ordinary shares of HK$0.05 each.

Financial risk management

The Group's diversified business is exposed to a variety of financial risks, such as market risks (including foreign exchange risk, commodity price risk and interest rate risk), credit risk and liquidity risk. The management of such risks is dictated by a set of internal policies and procedures designed to minimize potential adverse effects to the Group. The policies and procedures have proven to be effective. Further details are set out in note 44 to the financial statements.

The Group enters into derivative transactions, including principally forward currency, commodity contracts and interest rate swap. The purpose of these transactions is to manage the currency, commodity price and interest rate risks arising from the Group's operations and its sources of finance.

Management's Discussion and Analysis

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE (CONTINUED)

New investments

- In February 2006, the formation of the Manganese Company as a sino-foreign equity joint venture to undertake the business of manganese mining and processing was completed. The Manganese Company became a non-wholly-owned subsidiary of the Group from then. The joint venture enables the Group to manage and operate the largest manganese mine in the PRC and one of the largest manufacturers and suppliers of manganese products in the world.

  The Manganese Company was established in August 2005 and is owned as to 40% by Guangxi Dameng Manganese Industry Co., Ltd. ("Guangxi Dameng", a state-owned enterprise in the PRC) and as to 60% by CITIC Dameng Investments Limited ("CITIC Dameng"). CITIC Dameng is ultimately owned as to 80% by the Group and as to 20% by CITIC United Asia Investments Limited, an indirect wholly-owned subsidiary of CITIC Group. Before the end of 2005, CITIC Dameng has paid its capital contribution in cash of RMB300 million (HK$288.5 million) and Guangxi Dameng has paid its capital contribution in form of the contributed assets as approved by the relevant authorities of the PRC in the amount of RMB200 million (HK$192.3 million). The contributed assets include the land use rights and mining rights in respect of two manganese mines in Guangxi and the related operational assets and liabilities. Further details of the transaction are set out in the circular of the Company dated 24 August 2005.

- In November 2006, the Group completed the acquisition of a 51% participating interest in the production sharing contract relating to the Seram Oilfield for a purchase price of HK$875.0 million, subject to adjustment.

  The agreement was signed in July 2006 with KUFPEC (Indonesia) Limited ("KUFPEC"). Further details of the transaction are set out in the circular of the Company dated 28 September 2006.

- In October 2006, the Company had entered into a memorandum of understanding with CITIC Group pursuant to which CITIC Group had granted to the Group the right to purchase the Kazakhstan oil assets (the "Purchase Right").

  The Company may elect to exercise the Purchase Right by giving notice in writing to CITIC Group during the period of one year commencing from 29 December 2006. To ensure that the Company could act expeditiously in relation to its review and assessment of an investment in the Kazakhstan oil assets, the Company has placed as earnest money an amount equal to US$200 million with CITIC Group in October 2006. Further details of the transaction are set out in the announcement of the Company dated 1 November 2006.

Management's Discussion and Analysis

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE (CONTINUED)

Changes to investments

- In February 2006, the Group exercised its option to convert its 40% participating interest in the Kongnan Block within the Dagang Oilfield in the PRC, with a then carrying value of US$27,386,135 (HK$213,612,000), into 8,591,434 common shares in the share capital of Ivanhoe and a 3-year non-interest bearing, unsecured loan of US$7,386,135 (HK$57,612,000) repayable by Ivanhoe. The loan is repayable by 36 monthly instalments and the first instalment was due and received in March 2006.

  The 8,591,434 common shares represent about 3.7% of the total issued and outstanding share capital of Ivanhoe following completion of the conversion. There are limits on the sales of the shares during the period of 12 months following the date of conversion. During 2006, some of the shares were sold and as at 31 December 2006, the Company still held 7,160,271 shares, being about 2.9% of the total issued and outstanding share capital of Ivanhoe. Further details of the transaction are set out in the circular of the Company dated 13 March 2006.

- With effect from 7 June 2006, the agreement signed between the Group and a Chevron Corporation subsidiary in January 2005 to form a joint venture to develop a regional network of Caltex branded service stations in Southern China and to explore development possibilities in the Yangtze river delta lapsed. The required PRC approval was not obtained.

Opinion

The Board is of the opinion that after taking into account the existing available borrowing facilities and internal resources, the Group has sufficient resources to meet its foreseeable working capital requirements and there will be no adverse change to its financial position.

Management's Discussion and Analysis

EMPLOYEES AND REMUNERATION POLICIES

As at 31 December 2006, the Group had around 3,100 full time employees, including management and administrative staff. Most of the employees are employed in the PRC and Australia while the others are employed in Indonesia and Hong Kong.

The employees' remuneration, promotion and salary increment are assessed based on an individual's performance, professional and working experience and by reference to prevailing market practice and standards. Rent-free quarters are provided to the Group's PRC employees.

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for those employees who are eligible to participate in the MPF Scheme. The employees of the Group's subsidiaries which operate in the PRC are required to participate in a central pension scheme operated by the local municipal government. The Group also operates a defined contribution retirement benefits scheme (the "RB Scheme") under the superannuation legislation of the Australian government for those employees in Australia who are eligible to participate.

Contributions are made based on a percentage of the employees' basic salaries. The assets of the MPF Scheme and the RB Scheme are held separately from those of the Group in an independently administered fund. The Group's contributions as an employer vest fully with the employees when contributed into the MPF Scheme and the RB Scheme.

The Group's PRC subsidiaries are required to contribute a certain percentage of their payroll costs to the central pension scheme.

The Company and CATL operate share option schemes for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations.