III. Management discussion and analysis

1. Analysis of International and Domestic Shipping Markets during the Reporting Period

The Group's principle operation is ocean cargo shipping. Cargo shipping mainly consists of the shipment of oil and dry bulk cargoes (primarily coal) along the coastal region of the PRC and internationally.

In the first half of 2007, the world economy sustained a steady growth, and international trade as well as domestic demands in the PRC have been growing rapidly. The global shipping industry kept improving, and market continued to flourish, with sub-markets developing in different trends.

In the first half year, with the rapid increase in the demands for bulk cargoes (such as iron ore, coal etc), demand in the international dry bulk cargo shipping market continued to be strong. The shortage of shipping capacities has led freight rates to remain high. The average of the Baltic Dry Bulk Freight Rate Index (the "BDI") was 5,310 points, representing a significant increase of 113% as compared with the same period of last year. At the same time, due to the sustained growth in the economy of the PRC, coastal shipment of coal was growing rapidly, and the coastal bulk freight index increased by 17.7% as compared with the same period in 2006. The all-year base freight rate in respect of thermal coal for the contract of affreightment with the major customers increased by 14.1% as compared with 2006.

In the first half year, under the impact of a warmer winter in the northern hemisphere and production reduction by OPEC, overall demand in international oil market was inadequate. At the same time, surplus of new shipping capacities launched, which exceeded demands, has caused the freight rates to move downwards. In the first half year of 2007, the international crude oil composite freight rate indicator averaged at 1,161 points, representing a decrease of 9.1% as compared with the same period in 2006. Of these, the World Scale Index ("WS") for the shipping route from the Middle East to Japan, being one of the freight rate indicators for very large crude oil carriers ("VLCC") averaged at 71 points, a decrease of 26% as compared with last year. Oil shipment market in domestic trade remained stable.

2. Principle Operations of the Group during the Reporting Period

In the first half year of 2007, the Group persisted in taking oil shipping and domestic coastal coal shipping business as its core business, paying close attention on the market trends, and made efforts to enhance various cost control measures. Benefiting from the successful acquisition of the 42 dry bulk cargo vessels from China Shipping (Group) Company, the Company's controlling shareholder, and its subsidiaries, and the uprising in the international dry bulk cargo and coastal coal freight rate in the PRC, the profits of the Company increased significantly as compared with the same period in 2006. During the Reporting Period, the shipping volume achieved by the Group was 110.71 billion tonne-nautical miles, and the total revenue derived from shipment was approximately RMB5,527 million, representing an increase of 27.9% and 27.5% as compared with the first half in 2006 respectively. Cost of operations was approximately RMB3,074 million, an increase of 10.05% as compared with the same period in 2006. Net profit recorded was approximately RMB2,204 million, and earnings per share was approximately RMB0.663, representing an increase of 70.3% as compared with the same period in 2006.

An analysis of the principal operations in terms of products transported (Unit: RMB'000) is set out as follows:

Description	Revenue	Operating costs	Gross profit margin (%)	Increase/ (decrease) in revenue as compared with the same period of last year (%)	Increase/ (decrease) in operating costs as compared with the same period of last year (%)	Increase/ (decrease) in gross profit margin as compared with the same period of last year (%)
Oil transportation	2,349,436	1,547,066	34.15	(8.55)	(7.15)	(1.00)
Coal transportation	2,454,571	1,209,855	50.71	84.76	38.83	16.30
Others	723,469	316,809	56.21	64.89	24.03	14.43

An analysis of the principal operations in terms of geographical regions (RMB'000) is set out as follows:

Regions	Revenue	Increase/(decrease) in revenue as compared with the same period last year
Domestic transportation	3,527,980	45.49
International transportation	1,999,496	4.61

Dry bulk cargo shipping

In light of the favourable market opportunities and benefiting from the acquisition of the 42 dry bulk cargo vessels at the end of 2006 which have all been put into operation early this year, the Group's revenue derived from the dry bulk cargo shipping in the first half of 2007 increased significantly. In the first half of 2007, the Group has achieved a shipping volume of approximately 61.54 billion tonne-nautical miles of dry bulk cargo, and derived a revenue of approximately RMB3.18 billion, representing increases of 49.8% and 79.6% as compared with the same period in 2006 respectively. Of these, the shipping capacity of the 42 dry bulk cargo vessels acquired amounted to 1,406,000 DWT, representing 34.9% of the Company's existing shipping capacity of dry bulk cargo. Shipping volume achieved by the 42 vessels in the first half of 2007 was approximately 20.2 billion tonne-nautical miles, revenue generated was approximately RMB1,051 million, and the gross profit achieved was approximately RMB515 million, with gross profit margin of 49.0%.

For shipment of coal, the Group has achieved a total shipping volume of 40.14 billion tonne-nautical miles in the first half of 2007, and generated revenue of approximately RMB2,455 million, representing an increase of 56.1% and 85.0% as compared with the same period in 2006 respectively. Of these, domestic trade coal shipment was 36 billion tonne-nautical miles, and revenue achieved was approximately RMB2,254 million, representing increases of 69.3% and 86.2% as compared with the same period in 2006 respectively. International trade coal shipment was 4.14 billion tonne-nautical miles, representing a decrease of 7.0% as compared with the same period in 2006, and revenue achieved was approximately RMB201 million, representing an increase of 72.7% as compared with the same period in 2006.

For shipment of other dry bulk cargoes, the Group has achieved a total shipping volume of approximately 21.40 billion tonne-nautical miles in the first half of 2007, and achieved a shipping revenue of approximately RMB723 million, representing increases of 39.1% and 63.3% as compared with the same period in 2006 respectively. Of these, international trade shipping volume achieved was 17.73 billion tonne-nautical miles, and revenue achieved was approximately RMB512 million, representing increases of 33.5% and 64.1% as compared with the same period in 2006 respectively. Domestic trade shipping volume achieved was 3.67 billion tonne-nautical miles, and revenue achieved was approximately RMB211 million, representing increases of 74.1% and 61.2% as compared with the same period in 2006 respectively.

Oil shipment

Oil shipment is one of the Group's principle operations. In the first half of 2007, facing with the changes in the international and domestic oil shipping markets, the Group carefully organised the shipment and production, and made efforts in conducting safety management and cost control. In the first half of 2007, the Group achieved a shipping volume of approximately 49.17 billion tonne-nautical miles of oil shipment, representing an increase of 8.2% as compared with the same period in 2006, and revenue achieved was approximately RMB2,349 million, representing a decrease of 8.5% as compared with the same period in 2006.

For shipment of domestic trade oil, the Group has achieved a shipping volume of approximately 8.52 billion tonne-nautical miles of domestic trade oil shipment, representing a decrease of 18% as compared with the same period in 2006, and revenue achieved was approximately RMB1,060 million, representing a decrease of 1.8% as compared with the same period in 2006. In the first half year, of the domestic trade oil shipment, offshore oil shipping, transhipment of imported crude oil and refined oil shipping showed varied performances. The Group achieved a shipping volume of approximately 4.96 billion tonne-nautical miles of offshore oil shipping, representing a decrease of 7.0% as compared with the same period in 2006, and achieved a shipping revenue of approximately RMB546 million, representing an increase of 13.1% as compared with the same period in 2006. The Group achieved a shipping volume of approximately 2.20 billion tonne-nautical miles of transhipment of imported crude oil, and revenue of approximately RMB3,490 million, representing increases of 4.3% and 3.3% as compared with the same period in 2006 respectively. In the first half year, the Group continued to put efforts in the disposal of old tankers. Due to the impact caused by reduction in shipping capacity, the Group has achieved a shipping volume of 1.11 billion tonne-nautical miles of domestic trade refined oil shipment, and revenue gererated was approximately RMB116 million, representing decreases of 61.7% and 53.3% as compared with the same period in 2006 respectively.

In the international trade oil shipping market, to cope with the overall market depressed situation, the Group put emphasis in market research, and focused on cargo soliciting on key VLCC, Aframax and Handy-size tankers, and made efforts in finalising cargo sources during the periodical high positions. In the first half of 2007, the Group has achieved a shipping volume of approximately 40.7 billion tonne-nautical miles of international trade oil, representing an increase of 16% as compared with the same period in 2006, and revenue achieved was approximately RMB1,289 million, representing a decrease of 13.4% as compared with the same period in 2006. Of these, the shipping volume of international crude oil was approximately 22.56 billion tonne-nautical miles, representing an increase of 24.4% as compared with the same period in 2006, and revenue achieved was approximately RMB422 million, representing a decrease of 17.2% as compared with the same period in 2006. The shipping volume of international refined oil was approximately 18.09 billion tonne-nautical miles, representing an increase of 6.9% as compared with the same period in 2006, and revenue achieved was approximately RMB867 million, representing a decrease of 11.6% as compared with the same period in 2006.

3. Cost Analysis

In the first half year, there was a slight reduction in the daily average price of international crude oil. However, since June, under the impact of factors such as local politics and production reduction by OPEC, coupled with the arrival of the summer peak season of oil consumption in the European and American countries, prices of international crude oil increased rapidly and shipping enterprises were still facing with significant cost pressure.

In the first half of 2007, while adopting effective measures to increase revenue from principal operations, the Group continued to enhance overall control on various major costs, and has effectively controlled the major costs in fuel expenses, port expenses, repair expenses through advanced control and management in various aspects. The total operating cost incurred in the first half of 2007 was RMB3,074 million, an increase of 10.05% as compared with the same period in 2006, lower than the growth of 27.5% in the reveneue generated form operating activities. The cost compositions are specifically analysed as follows:

a. Fuel cost: the Group's fuel expenses in the first half of 2007 was approximately RMB1,356 million, an increase of 12.8% as compared with the same period in 2006, representing 44.11% of the total operating cost, and an increase of 1.0 percentage points over the corresponding period last year. However, at the same time, the Group further enhanced its fuel saving, and with a growth of 27.9% in its shipping volume as compared with the same period last year, there was only a growth of 18.9% in the fuel consumption, representing a reduction of 7.1% in fuel consumption per thousand nautical miles as compared with the same period last year.

b. Port cost: port expenses incurred in the first half of 2007 was approximately RMB315 million, an increase of 16.6% as compared with the same period in 2006, representing 10.24% of the total operating cost.

c. Labor cost: the Group's total labor cost in the first half of 2007 was approximately RMB378 million, an increase of 6.78% as compared with the same period in 2006, representing 12.3% of the total operating cost.

d. Depreciation: the Group's depreciation expenses incurred in the first of 2007 amounted to approximately RMB447 million, a decrease of 4.28% as compared with the same period in 2006, representing 14.54% of the total operating cost.

e. Repair expenses: the Group's repair expenses incurred in the first half of 2007 amounted to approximately RMB197 million, an increase of 9.4% as compared with the same period in 2006, representing 6.4% of the total operating cost.

4. Financial analysis

a. Net cash inflow

During the Reporting Period, the net cash inflow from operating activities of the Group increased from approximately RMB1,471,039,000 for the corresponding period in the previous year to approximately RMB2,694,043,000, representing an increase of 83.14%.

b. Commitments on capital expenditures

As at 30 June 2007, the commitments on capital expenditures for the Group amounted to approximately RMB15,375,664,000 (31 December 2006: approximately RMB8,864,108,000). The source of funding was mainly financed by the Company's working capital and bank loans.

c. Capital structure

As at 30 June 2007, the equity attributable to equity holders of the Company, bank loans, other interest-bearing borrowings and finance leases payable amounted to approximately RMB13,783,693,000, approximately RMB3,356,790,000 and approximately RMB9,916,000 respectively. The debt-to-equity ratio was 42.38% (31 December 2006: 34.99%).

d. Borrowings

As at 30 June 2007, the Group's total borrowing (excluding finance leases payable) was approximately RMB3,356,790,000. Borrowings repayable within one year amounted to approximately RMB253,389,000. Bank loans amounting to approximately RMB1,640,612,000 were pledged by 7 vessels owned by the Company. As at 30 June 2007, the total net book value of such vessels were approximately RMB2,065,316,000. Interests of the above loans were calculated at the annual rate from 5.670% to 6.156% and libor+0.42% to 0.85%. The Group's debt ratio was 29.76%, calculated by dividing total liabilities over total assets of the Group.

e. Risk on foreign currency

As at 30 June 2007, the Group's foreign exchange liabilities mainly comprised of bank loans payable in US Dollars equivalent to approximately RMB1,278,967,000 and finance lease rental payable in EURO dollars equivalent to approximately RMB9,916,000.

In addition, the Company would pay dividend of H shares in Hong Kong dollars.

In order to avoid the risk of Renminbi appreciation, the Group actively made adjustments to its debt structure, and the ratio in US dollar indebtedness increased from 37.64% at the beginning of the year to about 38.10%. Majority of US dollar income was used for overseas payments, and during the Reporting Period, foreign exchange income and expenses were basically equal.

Given the increasing significance of the Group's international shipping business, changes in exchange rate would have certain impacts on the Group's profitability. Therefore, in respect of the changes in exchange rate, the Group will study the impact of exchange rate mechanism on shipping enterprises. It will also implement effective measures proactively to minimize exchange risks.

5. Disposal of assets (Unit: Rmb'000)

Assets sold	Price of disposal	Profit arising from disposal of assets	Connected transaction (Yes/No)	Pricing policy
Jinquan	12,200	5,283	No	Marketprice
Haitang	7,600	(726)	No	Marketprice
Yongan4	173,829	55,060	No	Marketprice
Daqing44	18,262	16,292	No	Marketprice
Jianshe5	8,600	7,740	No	Marketprice
Jianshe6	8,800	7,934	No	Marketprice
Jianshe22	9,500	5,834	No	Marketprice
BeiJiXing	99,654	16,712	No	Marketprice
Jianshe4	7,000	6,764	No	Marketprice
Daqing51	22,162	19,614	No	Marketprice
Daqing61	26,426	18,345	No	Marketprice
Huaxi	29,015	26,864	No	Marketprice

6. Outlook and Focus in the Second Half of 2007

According to the forecast by International Monetary Fund, the growth rate of the world economy will reach approximately 4.9% in 2007, with a strong growing trend for the next five years. At the same time, the continuous development of the PRC economy will push the demand for energy resources such as oil, coal and iron ores, which will provide favourable conditions for the Group to capitalise on the advantages in both international and domestic trade operations, and develop healthily.

It is anticipated that during the second half of 2007, the international dry bulk cargo, oil shipping and domestic coastal oil and coal shipping markets will continue to maintain the developing trend as in the first half of 2007. In respect of international oil shipping, with the continued investment of new shipping capacities, it is expected that rebound of freight rates in the second half of 2007 will be limited, and in the overall, the market situation in the whole year will be lower than the average level of last year. In respect of international dry bulk cargo shipping, due to the major factors leading to the explosive growth in the BDI Index in the first half of 2007 such as strong demand in shipping capacity, inadequate growth in shipping capacity, extended shipping distances and congestion of ports still exist, it is expected that the freight rates for dry bulk cargo will remain at a high level in the second half of 2007.

6. Outlook and Focus in the Second Half of 2007 (continued)

To cope with the current market situation, the Group will continue to carry out the followings in the second half of 2007:

a. Continue to enhance cooperation with major customers. The Group will continue to explore for the strategic cooperation with major customers such as PetroChina, Sinopec, CNOOC, and continue to negotiate for long-term shipping contracts for imports of iron ores with domestic large iron and steel enterprises;

b. Further strengthen vessel chartering. The Company has recently established two professional vessel chartering companies in Hong Kong, aiming to make vessel chartering as a conventional mode for development of shipping capacity, and as an important supplementary resort for the implementation of the strategic planning of a “world class fleet”;

c. Continue with the disposal of old tankers, so as to optimise the structure of the tanker fleet, and enhance the shipping efficiencies of the vessels; and

d. Continue to finalise effective measures such as various energy saving measures, adopt enhancement in the management and supervision of fuel procurements, locking up of some of the fuel prices, so as to further control fuel and other various costs, making efforts to minimise the increase in costs.