

DIRECTORS' REPORT

To all shareholders:

The Board of Directors (the "Board") of Harbin Power Equipment Company Limited (the "Company") is pleased to announce the audited consolidated interim results of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2001.

RESULTS

For the six months ended 30 June 2001, the Group recorded a turnover of RMB1,170.3 million, a decrease of 16.29 per cent over the same period last year. The profit after taxation and minority interests was RMB19.11 million, an increase of 90.59 per cent over the same period last year and the earnings per share was RMB0.0161.

As at 30 June 2001, the Group's total assets were valued at RMB9,348.69 million, an increase of 7.5 per cent over that at 31 December 2000. Total liabilities amounted to RMB6,415.77 million, an increase of 11.87 per cent over that at 31 December 2000. The net assets per share reached RMB2.46.

INTERIM DIVIDEND

The Board does not recommend an interim dividend for the period under review.

MANAGEMENT DISCUSSION AND ANALYSIS

INDUSTRY DEVELOPMENT

In the first half of 2001, the gross domestic product of China grew by 7.9 per cent and the electricity consumption increased 11.2 per cent. The macro-economy continued to head to positive direction. The "Tenth Five-year Plan" has started up. The strategy of "actively developing hydropower and large pit-mouth thermal power units, restricting small thermal power units, moderately developing nuclear power, encouraging co-generation units and comprehensively-utilized generation and actively developing new energy and renewable energy generation" and big west development strategy with transporting electricity from west to east as key item has been carried out, which will remarkably increase new power plant construction projects. The power equipment industry of China is welcoming a new and important development era.

BUSINESS DEVELOPMENT

As at 30 June 2001, new orders secured by the Group totalled RMB4.46 billion, an increase of RMB2.48 billion, 125.3 per cent over the same period of last year. The growth in new orders is mainly attributable to the start-up of the "Tenth Five-

year Plan”, the carrying out of the big west development strategy and especially, the Group’s efforts in marketing. The export orders and orders in the western provinces increased. The major new orders include the El Gaili Combined-cycle Power Station in Sudan (2X206B), turbine island and boiler island engineering project for the Hancheng Power Plant in Shanxi (2X600MW), thermal power main units for the Pingliang Power Plant in Gansu (2X300MW), turbine and turbine generator for the Zhuzhou Power Plant in Hunan (2X300MW), hydropower turbine for the Gongboxia Hydropower Station in Qinghai (5X300MW) and hydropower turbine for the Hongjiadu Hydropower Station in Guizhou (3X200MW). Among which the El Gaili combined-cycle project was significant to the Group, being the first EPC project of the Group in Africa. During the period under review, the Group also secured orders for 6 sets of 100MW class circulated fluidised bed boilers (CFB). So far the Group has secured the orders for accumulated 29 sets CFB boilers and the Group’s market share of 100MW CFB boilers in China is about 80 per cent. The manufacturing technology of 100MW class CFB boilers of the Group has been proved and mature and the Group has remarkable strength in this field.

RESEARCH AND DEVELOPMENT

According to the development trends of power generation equipment market, the Group enhanced its research and development and made certain progress on some products.

- As for large sub-critical thermal power units, the Group succeeded in developing new-generation 300MW sub-critical turbine, which reached the international advanced level. The Group is now developing and designing new-generation 600MW sub-critical turbine, which is expected to be finished during the year.
- As for large air-cooling units, the design of 300MW and 600MW air-cooling turbines were completed.
- As for clean coal combustion technology, the Group succeeded in developing, introducing and producing 100MW class CFB boilers. And the Group has begun to introduce the technology for 300MW class CFB boilers.
- As for hydropower equipment, the subject of “the Three Gorges units research and production” has been reviewed and accepted by the relevant authorities, which laid a foundation for the localization of the Three Gorges units.
- As for the pumped storage units, integrating with the Henan Huilong Power Station (2X60MW), the Group designed the model runner, conducted hydraulic testing and began the design task.

PRODUCTION AND SERVICES

During the period under review, the Group's output in hydropower turbine generator units amounted to 240MW, a decrease of 42.9 per cent over the same period last year. As for thermal power main units, the output of power plant boilers was 775MW, an increase of 24 per cent over the same period last year. The output in power plant turbine and turbine generator was 825MW and 583MW, a decrease of 6.3 per cent and 2.8 per cent over the same period last year respectively. The decrease of product output was mainly because the production cycle of the Group is long, the products manufactured by the Group in the first half of the year were mostly small- and medium-sized (most large units will be produced in the second half of the year) and the production of the components for the Three Gorges Project was not included in the output. During the period under review, the Group increased the production of spare parts and components and work-in-progress. The actual production completed increased by about 20 per cent over the same period last year, which created the conditions for the output increase in the second half of the year and the next year. The production for the Three Gorges Project proceeded as scheduled. The manufacturing of the stay ring for the turbine and the stator frame for the generator was finished during the period and these components have been delivered to the site.

As for engineering services project, the 95 per cent, 100 per cent and 81 per cent of the main equipment supply for the Iran MES, KRH and K3 Hydropower Stations has been completed respectively. Regarding the Tuoketuo Boiler Island Project (2X600MW), the procurement of auxiliaries and raw materials has come to the final stage and the manufacturing of most steel structure of the boiler proper has been completed and the installation is proceeding now. The Sudan El Gaili Combined-cycle Project (2X206B) has begun and the equipment supply and installation contracts have been signed.

TURNOVER AND PROFIT ANALYSIS

As at 30 June 2001, the Group recorded a turnover of RMB1,170.3 million, representing a decrease of 16.29 per cent over the same period last year. Among which turnover from thermal power main units was RMB700.49 million, an increase of 9.95 per cent over the same period last year, turnover from hydropower main units was RMB79.12 million, a decrease of 18.73 per cent and turnover from power plant engineering services was RMB243.49 million, a decrease of 47.79 per cent. And turnover from power plant auxiliaries and parts was RMB50.48 million, turnover from AC/DC motor and other products and services was RMB96.73 million, an increase of 193.34 per cent and a decrease of 46.26 per cent respectively. The turnover decrease of the Group was mainly due to the decrease in turnover from power plant engineering services.

During the period, export sales and sales denominated in foreign currencies of the Group amounted to USD25.25 million, representing 17.86 per cent of the Group's total turnover. The major export countries include Iran, Japan, Thailand, the United States of America and etc.

During the period under review, the profit after taxation and minority interests was RMB19.11 million, an increase of 90.59 per cent over the same period last year. The earnings per share was RMB0.0161. The increase in profit was mainly due to cost control and higher profit margin of some products.

During the period under review, the gross profits of the Group was RMB264.09 million, an increase of 3.69 per cent over the same period last year. The gross profit margin increased 4.35 per cent to 22.57 per cent compared to the same period last year, among which the profit margin of power plant engineering services, auxiliaries and parts and AC/DC motors and other product increased by a big margin.

COST AND EXPENSE ANALYSIS

During the period under review, the Group's operating costs were RMB906.21 million, a decrease of 20.74 per cent over the same period last year, which was mainly due to the decrease of turnover and the strengthened cost control.

The Group's expenses during the period were RMB274.71 million, a slight decrease over that of the same period last year.

FINANCIAL ANALYSIS

As at 30 June 2001, the total assets of the Group increased 7.54 per cent to RMB9,348.69 million as compared to that of 31 December 2000, which was mainly due to the increase of inventories and debtors. Among which the total current assets were RMB7,023.84 million, representing 75.13 per cent of the total assets. The total fixed assets were RMB2,229.95 million, representing 23.85 per cent of the total assets. Among current assets, the inventories were RMB2,406.09 million, an increase of 12.55 per cent compared to that of 31 December 2000, which was mainly due to the increase of raw materials and work-in-progress.

As at 30 June 2001, the Group's debtors, deposits and prepayment reached RMB2,595.84 million, an increase of RMB104.39 million as compared to that of 31 December 2000.

As at 30 June 2001, the total liabilities of the Group amounted to RMB6,415.77 million, an increase of 11.87 per cent compared to that of 31 December 2000, which was mainly due to the increase of loans for production and technical renovation.

As at 30 June 2001, the Group's borrowings due within one year was RMB2,124.06 million. The Group adopted the interest rate as stipulated by the State. The Group repays its debts on time. All debts of the Group were in Renminbi. The gearing ratio of the Group was 0.51:1.

As at 30 June 2001, the cash and cash equivalents of the Group was RMB584.3 million, an increase of RMB24.81 million compared to that of 31 December 2000.

So far the Group has not adopted hedging measures for exchange rate, the fluctuation of exchange rate has certain impact on the operating results of the Group.

INVESTMENT IN INFRASTRUCTURE CONSTRUCTION AND TECHNICAL UPGRADING

During the period under review, the total investment in infrastructure construction and technical upgrading amounted to RMB141 million, which was mainly used to enhance the manufacturing capability of large hydropower equipment, super critical, pumped storage, large rolling mill motor technical upgrading projects and turbine blade machining center project. Among which the technical upgrading project of turbine blade machining center project has been completed during the period. In the second half of the year, the Group will accelerate the investment in enhancing the manufacturing capability of large hydropower equipment.

Upon the demand of the market development and integrating the power development trends during the "Tenth Five-year Plan" period, the Group will accelerate the investment in the following projects while completing the project of enhancing the manufacturing capability of large hydropower equipment. These projects include technical upgrading of super critical units, technology transfer and technical upgrading of large gas turbine, technical renovation of large air-cooling units and optimized 300MW and 600MW sub-critical turbine, technology transfer and technical upgrading of combined-cycle heat recovery steam generator, large pumped storage units and wet flue gas desulfurization and large enterprise information project. It is estimated that the total investment in these projects is about RMB1.5 billion. The Group will realize the investment by continuing to utilize the proceeds from H Share listing and through issuing domestic Renminbi denominated ordinary shares (A Share) in China and other financing channels. The implementation of these projects will accelerate the product replacement of the Group and enhance competitiveness.

USE OF LISTING PROCEEDS

In order to be adjusted to the requirements of the "Tenth Five-year Plan" and the big west development and the demand of the international market, the Group speeded up its technical upgrading and enhanced corresponding investment so

as to improve the competitiveness. During the period under review, the Group has utilized RMB136 million from H share listing proceeds. Among which RMB66 million was utilized in turbine blade machining center project and technical upgrading project of large rolling mill motor. And RMB70 million was utilized as working capital of the Group's associated companies.

As at 30 June 2001, the Group has used a total of RMB690 million from its H share listing proceeds. The Board has approved RMB317 million from H share listing proceeds to be invested in large hydropower renovation project, the construction of the National Engineering Research Center and other projects during the year. The remaining proceeds of RMB232 million are deposited in banks and will be used according to the prospectus of the Company for the issue of H Shares dated 5 December 1994.

PROSPECT

The performance of the Group will improve in the second half of 2001. The product output will remarkably increase and the results will continue to grow. Although the competition in power equipment market will still be fierce, the demand in the market will keep being vigorous with the start-up of the "Tenth Five-year Plan" and implementation of big west development strategy. The Group will mainly be engaged in the following tasks in the second half of the year:

- continue to enhance marketing, especially the marketing of large hydropower units, 300MW and 600MW thermal power units, air-cooling units and circulated fluidised bed boilers and try to secure more orders;
- enhance technical upgrading and investment in research and development, especially the technical upgrading of large hydropower units, technology transfer of super-critical units, technology transfer and technical upgrading of clean coal combustion and pumped storage units and investment in the Power Equipment National Engineering Research Center;
- actively push forward the A Share issue, expand financing channels, improve the structure of assets and liabilities in order to provide capital support to the development of the Company;
- further enhance internal administration, accelerate internal reforms, improve distribution system and bring every positive factor of employees into play.

According to the "Tenth Five-year Plan" of China, it is expected that the average growth speed of the national electricity demand is 5 per cent to 6 per cent. The newly increased installed capacity is 100 million kilowatt. Altogether 25000MW small units will be shut down. The power plants with total capacity of 100 million kilowatt are under construction and the construction of power plants with total capacity of 10000MW is under preparation during the "Tenth Five-year

Plan” period. The focal point of development of hydropower equipment during the “Tenth Five-year Plan” period will be put on the hydropower resources along the middle and upper reaches of the Yangze River and its main tributary, Hongshui River, the middle and lower reaches of Lancang River, Wu River and the upper reaches of the Yellow River. The seven large hydropower stations including Longtan, Xiaowan, Shuibuya, Goupitan, Sanbanxi, Gongboxia and Pubugou Power Stations with total capacity of 19000MW will begin construction. As for thermal power, the newly constructed coal-fired power plants will mainly adopt units with capacity of and above 300MW and with high parameters, high efficiency and good peak adjustment feature. Large-sized pit-mouth power plants will be set up in resource bases such as Shanxi, Shan’xi, the Inner Mongolia and the southwestern region and the electricity generated by these power plants will be transmitted to the eastern and coastal areas. The Group will also actively promote and develop super-critical units and push forward CFB boilers and other clean coal generation demonstration projects. The Board believes that the power equipment required by the “Tenth Five-year Plan” is just what the Group will mainly develop. The Group has strength in these fields. This is an important opportunity for the development of the Group. The Group will master this opportunity by accelerating technical advancement and upgrading, improving facilities and product quality in order to meet the demand of the power equipment market. The Board is confident of the bright future of the Group.

EXPORT VAT REBATE

Pursuant to the stipulations in the document Cai Shui Zi [1999] No. 17 of the PRC Ministry of Finance and the State Tax Bureau, the export VAT rebate application to the Group export products is 17 per cent. with effect from 1 January 1999.

INCOME TAX

The Group is a high technological enterprise and has been enjoying an income tax rate of 15 per cent.. So far the Group has not been informed of any changes regarding income tax.

IMPACT OF CURRENT ECONOMIC SITUATION

The PRC will join the World Trade Organization (WTO) soon. The Board believes that the PRC’s admission to WTO will have no material negative impact on the Group.

With the carrying out of the strategies of the “Tenth Five-year Plan” and the “Big West Development”, the domestic power equipment market will welcome a new era of fast development. The Group will benefit from this.

SALE OF STAFF QUARTERS

The Group did not sell any staff quarters, as it did not have any during the period under review.

ENTRUSTED DEPOSITS AND OVERDUE TIME DEPOSITS

As at 30 June 2001, the Company had no entrusted deposits in commercial banks or non-bank financial institutions and had no deposits that become due but have not been withdrawn.

SHARE CAPITAL STRUCTURE

As at 30 June 2001, the share capital of the Company comprised of 1,189,151,000 shares is as follows:

	Shares	Percentage in total Share capital (%)
(1) State shares (not circulated)	720,000,000	60.55
(2) H shares (circulated and listed on the HKSE)	469,151,000	39.45
Total	<u>1,189,151,000</u>	<u>100</u>

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2001, the Company's major shareholders included:

Shareholder	Share category	Share number	Percentage in total share capital (%)
Harbin Power Plant Equipment Company Corporation	State share	720,000,000	60.55
HKSCC Nominees Limited	H share	456,120,789	38.36

Other than disclosed above, the Board of Directors of the Company has not been notified of any other interests directly or indirectly representing 10 percent. Or more of the Company's issued share capital, which should be recorded in share registrar pursuant to section 16(1) of the SDI Ordinance in Chapter 396 of the Hong Kong Ordinance, or should be applied and reported to relevant authorities in compliance with relative regulations of the PRC.

DIRECTOR'S, SUPERVISOR'S AND SENIOR MANAGEMENT'S INTERESTS IN THE SHARE CAPITAL OF THE COMPANY

As at 30 June 2001, none of the Directors, Supervisors or senior management, or any of their connected persons had any interests in any shares, debentures or options of the Company or any of the subsidiaries. None of them was given preferential purchase right by the Company.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the period, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities.

CODE OF BEST PRACTICE

None of the Directors is aware of any information that would reasonably indicate that the Company is not, or was not for any part of the six months ended 30 June 2001, in compliance with Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

DISCLOSURE OF SIGNIFICANT EVENTS

In March 2001, altogether 42 items of 9 specialized subjects of the "Three Gorges 700MW hydropower units research and development" project have been reviewed and accepted by the relevant authorities. Some of which have reached international advanced level. The manufacturing of the stay ring for turbine and stator frame for the first unit of the Three Gorges Project has been completed and these components have been delivered to the site during the period under review.

During the period under review, the Group signed EPC contract for the Sudan El Gaili Combined-cycle Power Station (2X206B), which is the first EPC project that the Group has ever obtained in Africa.

During the period under review, the Group signed boiler island and turbine island EPC contract for the Shanxi Hancheng Power Plant (2X600MW), which is the second 600MW class island by island EPC project that the Group has ever obtained.

Other than disclosed above, the Group did not have other disclosable significant events in the period under review.

SHAREHOLDERS' MEETING

The Company's 2000 Annual General Meeting was held on 22 June 2001 in Harbin city, during which all resolutions set out in the Company's Notice of Annual General Meeting dated 23 April 2001 were passed.

Other than disclosed above, no extraordinary general meeting was held during the period under review.

POST BALANCE SHEET EVENT-PROPOSED ISSUE OF A SHARES

On 4 August 2001, the Board of the Company passed a resolution on proposed issue of not more than 144 million domestic Renminbi denominated ordinary shares (A share) in the PRC and application to the Shanghai Stock Exchange for the listing of such A Shares on the Shanghai Stock Exchange in order to expand financing channels, provide capital support to technical upgrading and product replacement, improve the competitiveness of the Group, meet the market demand and improve the structure of assets of liabilities of the Group. The proposal upon the approval from the Board is still subject to the approval of the Company's Extraordinary General Meeting which will be held on 22 September 2001 and the approval of the China Securities Regulatory Commission. The relevant preparation is proceeding as planned. For detailed information, please refer to the announcement of the Company published on the Hong Kong Economy Daily and South China Morning Post (English edition) on 6 August 2001.

REFERENCE DOCUMENT

The interim report and financial statements for the six months ended 30 June 2001 of the Company are available for inspection at Block B, 95 Daqing Road, Dongli District, Harbin, Heilongjiang, the PRC.

By order of the Board

Geng Lei

Chairman

Harbin, the PRC, 24 August 2001