

5. MANAGEMENT DISCUSSION AND ANALYSIS

(1) Analysis of the principal operational results and financial position of the Company (prepared under PRC accounting standards):

Items	Amount (RMB'000)		Change%
	For the six months ended 30 June 2002	For the six months ended 30 June 2001	
Revenue from principal activities	252,482	177,294	42.41
Profit from principal activities	69,643	26,865	159.23
Net profit	(29,732)	(70,509)	57.83
Decrease in cash and cash equivalents	(159,314)	(8,146)	(1855.73)

Items	Amount (RMB'000)		Change%
	As of 30 June 2002	As of 31 December 2001	
Total assets	2,601,231	2,578,023	0.90
Shareholders' funds	856,489	885,832	(3.31)

Analysis:

- (1) An increase in revenues from principal activities is mainly attributable to the implementation of the “Tenth Five Year Plan” in full swing, the strategic implementation of the State Western Region Development Strategy, commencement of a series of constructions of power-generating projects and an increase of orders received by the Company. Therefore, there were increases in manufacturing activities and sales volume of products.
- (2) An increase in profits from principal activities is mainly attributable to a faster growth in revenues from principal activities of the Company during the reporting period, revenues from the Three Gorges project and products with high gross profit margin such as steam turbine generators with generation capacity of 200MW or more.
- (3) There was a decrease in loss in the reporting period compared to the corresponding period of last year, mainly because there was an increase in profits from principal activities in the reporting period.
- (4) There was a larger deficit in cash flow in the reporting period, mainly because there was a greater increase in expenditure from purchase of products and repayment of loans in the reporting period.
- (5) As at 30 June 2002, the gearing ratio of the Company was 67.03%, approximately the same as the corresponding period of last year. Borrowing bearing fixed interest rate amounted to RMB822,458,000, RMB282,100,000 of which was short-term loans, RMB101,358,000 of which was due within one year, RMB439,000,000 of which was long-term loans. All loans were repaid at maturity.
- (6) The Company purchased raw materials from overseas and sold its products to overseas. Certain machineries and processing equipment were imported for large power station project to be completed in 2003. Recently, average of foreign exchange balance was approximately US\$ 30,000,000. Therefore, there was a certain degree of risk in foreign exchange.
- (7) As at 30 June 2002, the shareholders’ funds of the Company was as follows: capital amounted to RMB450,000,000; capital surplus amounted to RMB606,569,000; statutory common reserve fund amounted to RMB53,590,000; accumulated deficit amounted to RMB253,670,000.

(2) Operations of the Company in the reporting period

The principal operations of the Company include hydro turbine generators, steam turbine generators, A.C. and D.C. motors and control equipment.

The Company recorded loss in the year of 2001. Based on the business plan of 2002, the Board of Directors determined to tackle the problem in an effort to rebound the Company from the trough and make a turnabout from recording loss to profits. In the first half of the year, the Company completed the objectives set for the first half of the year, further approaching a health-growing stage in pursuit of the completion of objectives for the full year. In the first half of the year, the Company built 5 hydro turbine generator sets with generation capacity of 297MW; 8 sets of auxiliary equipment for the Three Gorges project; 7 steam turbine generators with generation capacity of 1,328MW. Orders received by the Company amounted to approximately RMB 590 million.

Segment information:

	Hydro turbine generators	Steam turbine generators	A.C. and D.C. motors	Other	Total
Revenue from principal activities	110,018	98,250	22,451	21,763	252,482
Costs from principal activities	87,934	66,851	20,005	8,049	182,839
Segmental results	22,084	31,399	2,446	13,714	69,643

(Unit: RMB'000)

During the currently period and previous period, the Group's revenues were mainly derived from the PRC. Since revenues derived from overseas were negligible, no gains and results based on geographical segments by location of customers were presented.

During the reporting period, the Company has no other operation which has significant impact on net profits in the reporting period.

(3) Use of proceeds

In compliance with the purpose stipulated in the Company's prospectus for the issue of A Shares and H Shares, the proceeds of approximately RMB752,548,300 from the share offer of A Shares and H Shares has been applied in four major technological reform projects on improving the production capacity of hydro turbine generator sets. The use of proceeds in the four projects as at 30 June 2002 was as follows:

Projects undertaken in prospectus:

- (1) It was planned to invest RMB 670 million in the technological reform project for improving production capacity of hydro generator sets and the actual investment was RMB226,089,000. In the first half of the year, there was a total investment of RMB14,364,000. Through the implementation of the technological reform, the production capacity and technology level of hydro and steam turbine generator sets have been enhanced, thus improving its ability to seize market share and its competitiveness. However, in view of the present market situation of generator equipment, the Company is prudent in making technological reform.
- (2) It was planned to invest RMB 160 million as capital input of the Sino partner in joint venture projects for the production of large hydro turbine generator sets and steam turbine generators. On 6 March 2001 and 27 May 2002, the Company held an Extraordinary General Meeting and the 2001 Annual General Meeting respectively to approve the change of use of the proceeds of RMB160 million which were initially intended to be utilized as capital input in joint venture projects for the production of large hydro turbine generator sets and steam turbine generators as additional working capital of the Company. Currently, such change in the use of proceeds has been implemented.
- (3) It was planned to invest RMB 150 million as additional working capital and the actual investment was RMB 150 million. This project was completed.
- (4) It was planned to invest RMB 75 million as repayment of the loans for technological reform under the Seventh Five-year Plan and Eighth Five-year Plan and the actual investment was RMB 88,449,000. The project was completed.

As at 30 June 2002, the balance of unused proceeds amounted to approximately RMB 128.01 million. The Company has deposited the unused proceeds with banks in the PRC.

(4) Employees of the Company

As of 30 June 2002, there were 7,518 employees in the Company, 3,979 of which were engaged in production, 131 of which were engaged in sales, 1,254 of which were engaged in technology, 84 of which were engaged in finance, 569 of which were engaged in administration. As for training of employees, the Company provided various training programs, actively establishing performance evaluation and awarding-penalizing system. Quality of employees as a whole will be improved through the combination of training and evaluation.

(5) Plans for the second half of the year

Following the implementation of the “Tenth Five Year Plan” in full swing, the “Electricity transmission from western China to eastern China” project under the State Western Region Development Strategy and commencement of a series of large-scale power projects, resulted in lucrative prospects for power-generating equipment. In view of the market circumstances, the Company determined to rebound the Company from the trough and make a turnabout from recording loss to profits. In order to accomplish such objectives, the Company would endeavor to complete the following important tasks:

1. To consolidate management and control of the implementation of contracts throughout the whole process, actively improve management model for production organization and perform professional synergy, ensuring completion of production tasks for the whole year.
2. To seize the market opportunities, maintain important tasks and keep the positive ordering trend of products;
3. To focus on important tasks, implement catching-up procedures and enhance the core competitiveness;
4. To continue to improve quality, enhance management of process and finish quality control objectives;
5. To consolidate cost-management, further implement cost-cutting procedures and efficiency-enhancing policies and control of target costs;
6. To further consolidate management, organize management behavior and carry out informational management.

However, fluctuation of prices of raw materials and uncertainty about whether application for export tax refund for various items by the Company can be approved within this year may have influence on the economic results of the Company for the year.

(6) It is estimated that during the period from January to September 2002, the Company would still record loss in the accumulated results, details of the figures will be disclosed in the financial report for the 3rd quarter.