

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

### DISCUSSION OF SEGMENT OPERATIONS

The Company divides its operations into five principal business segments, the exploration and production segment, the refining segment, the marketing and distribution segment and the chemicals segment, and also the corporate and others segment. Unless otherwise

indicated, inter-segment transactions have not been eliminated from the financial data discussed in this section and the operating revenue data for each of the business segments discussed in this section include other operating revenues from each segments.

The following table lists the operating

revenues by segments, the contribution of external sales and inter-segment sales as a percentage of operating revenues before the elimination of inter-segment sales, and the contribution of external sales as a percentage of consolidated operating revenues, for the period indicated (i. e., after elimination of inter-segment sales).

	First half, 2001 RMB billions	First half, 2000 RMB billions	Proportion of Total Operating Revenues Before Elimination of Inter-segment Sales		Proportion of Consolidated Operating Revenues After Elimination of Inter-segment Sales	
			First half, 2001	First half, 2000	First half, 2001	First half, 2000
<b>Operating revenues</b>						
Exploration and Production Segment						
External sales <sup>(1)</sup>	6.6	4.4	2%	2%	4%	3%
Inter-segment sales	21.7	21.2	8%	9%		
<b>Total operating revenues</b>	<b>28.3</b>	<b>25.6</b>	<b>10%</b>	<b>11%</b>		
Refining Segment						
External sales <sup>(1)</sup>	27.7	30.8	10%	13%	17%	21%
Inter-segment sales	81.6	68.0	30%	28%		
<b>Total operating revenues</b>	<b>109.3</b>	<b>98.8</b>	<b>40%</b>	<b>41%</b>		
Marketing and Distribution Segment						
External sales <sup>(1)</sup>	93.9	78.0	33%	32%	57%	52%
Inter-segment sales	1.4	0.3	1%			
<b>Total operating revenues</b>	<b>95.3</b>	<b>78.3</b>	<b>34%</b>	<b>32%</b>		
Chemicals Segment						
External sales <sup>(1)</sup>	27.7	28.4	10%	11%	17%	19%
Inter-segment sales	2.9	1.5	1%	1%		
<b>Total operating revenues</b>	<b>30.6</b>	<b>29.9</b>	<b>11%</b>	<b>12%</b>		
Corporate and others						
External sales <sup>(1)</sup>	8.4	7.8	3%	3%	5%	5%
Inter-segment sales	4.8	1.0	2%	1%		
<b>Total operating revenues</b>	<b>13.2</b>	<b>8.8</b>	<b>5%</b>	<b>4%</b>		
<b>Total operating revenue before elimination of Inter-segment sales</b>	<b>276.7</b>	<b>241.4</b>	<b>100%</b>	<b>100%</b>		
Elimination of Inter-segment sales	(112.4)	(92.0)				
<b>Consolidated operating revenues</b>	<b>164.3</b>	<b>149.4</b>			<b>100%</b>	<b>100%</b>

Note: (1) Including other operating revenues.

The following table lists the operating revenues, operating expenses and operating profit by segment before elimination of inter-segment transactions for the period indicated.

#### Exploration and production segment

The exploration and production segment consists of the activities related to exploring, developing, producing and selling crude oil and natural gas.

The operating revenues for the exploration and production segment during the first half of 2001 was RMB 28.3 billion, up 10.5% over the same period in 2000.

The actual average selling price of crude oil was RMB 1,472 per tonne, down 1% from RMB 1,487 per tonne in the same period last year, while internal and external sales went up 2.9% from 16.46 million tonnes in the first half of last year to 16.94 million tonnes.

The operating expenses for the exploration and production segment during the first half of 2001 were RMB 16.7 billion, up 15.2% compared with the same period in 2000. The exploration and production segment's lifting cost per barrel for oil and gas was reduced by US\$0.63 per barrel and was down from US\$7.26 per barrel in the first half of last year to US\$6.63 per barrel.

	First half, 2001 RMB billions	First half, 2000 RMB billions	Percentage change between first half 2001 and same period 2000
Exploration and production segment			
Operating revenues	28.3	25.6	10.5%
Operating expenses	16.7	14.5	15.2%
<b>Total operating profit</b>	<b>11.6</b>	<b>11.1</b>	<b>4.5%</b>
Refining Segment			
Operating revenues	109.3	98.8	10.6%
Operating expenses	106.5	100.4	6.1%
<b>Total operating profit</b>	<b>2.8</b>	<b>(1.6)</b>	<b>275.0%</b>
Marketing and distribution segment			
Operating revenues	95.3	78.3	21.7%
Operating expenses	94.3	75.1	25.6%
<b>Total operating profit</b>	<b>1.0</b>	<b>3.2</b>	<b>(68.8%)</b>
Chemicals Segment			
Operating revenues	30.6	29.9	2.3%
Operating expenses	30.4	27.9	9.0%
<b>Total operating profit</b>	<b>0.2</b>	<b>2.0</b>	<b>(90.0%)</b>
Corporate and others			
Operating revenues	13.2	8.8	50.0%
Operating expenses	12.8	8.8	45.5%
<b>Total operating profit</b>	<b>0.4</b>	<b>0.0</b>	

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The operating profit for the exploration and production segment during the first half of 2001 was RMB 11.6 billion, up 4.5% compared with the same period in 2000.

### Refining Segment

The refining segment's activities consist of purchasing crude oil from the Company's exploration and production segment and from third parties, processing crude oil into refined oil products, selling refined oil products to bulk customers and to the Company's marketing and distribution segment.

The operating revenues from the refining segment in the first half of 2001 were RMB 109.3 billion, up 10.6% compared with the first half of last year, largely due to the increased sales of gasoline, diesel, chemical feedstocks and other refined oil products.

- The refining segment's sales of gasoline in the first half of 2001, which constituted approximately 23% of the segment's total operating revenues for the period, increased 13.8% compared with the first half of 2000 to RMB 24.7 billion, largely due to the increased selling price of RMB 2,560 per tonne in the first half of 2001, up 13% compared with the first half of 2000, and the increased sales volume of 9.66 million tonnes in the first half of 2001, up 1% compared with the first half of 2000.
- The refining segment's sales of diesel in the first half of 2001, which constituted approximately 39% of the segment's total operating revenues for the period, increased 14% compared

with the first half of 2000 to RMB 42.5 billion, largely due to the increased selling price of RMB 2,260 per tonne in the first half of 2001, up 7% compared with the first half of 2000, and the increased sales volume of 18.79 million tonnes in the first half of 2001, up 6% compared with the first half of 2000.

- The refining segment's sales of chemical feedstocks and other refined oil products in the first half of 2001, which constituted approximately 20% of the segment's total operating revenues for the period, went up 30% compared with the first half of 2000 to RMB 22 billion, largely due to the increased selling price of RMB 2,037 per tonne in the first half of 2001, up 8% compared with the first half of 2000 and the increased sales volume of 10.78 million tonnes in the first half of 2001, up 20% compared with the first half of 2000.

In order to enable the refining segment and marketing and distribution segment to operate more efficiently on an integrated basis, the Company intends to gradually redirect substantially all (with the exception of certain amounts which will be retained by the refining segment for certain special customers and for exports) of the refining segment's sales of gasoline and diesel to the marketing and distribution segment which conducts external sales.

In the first half of 2001, the operating expenses of the refining segment were RMB 106.5 billion, up 6% compared with the same period in 2000, largely due to increased expenses for the

purchase of crude oil, oil feedstock, catalysts and auxiliary materials.

In the first half of 2001, the Company's refining margin (defined as sales revenues less crude oil expenses and oil feedstock expenses, divided by the corresponding volume of crude oil and oil feedstock processed) was US\$3.67 per barrel, an increase over the same period last year. The main reasons for that increase were the increased sales revenues while the crude oil processing throughput remained unchanged. The Company's cash operating costs (defined as the segment's operating expenses less the sum of purchased crude oil and oil feedstock expenses, depreciation and amortisation, taxes other than income tax and other operating expenses, divided by the volume of crude oil and corresponding oil feedstocks processed) in the first half of 2001 were US\$2.07 per barrel, down US\$0.19 per barrel from the same period in 2000.

The operating profit of the Company's refining segment in the first half of 2001 was RMB 2.8 billion, up 275% over the same period last year, largely due to the fact that the level of the increase in operating revenues exceeded the level of the increase in operating expenses.

### Marketing and Distribution Segment

The marketing and distribution segment consists of the purchasing of refined oil products from the refining segment and third parties and selling and distributing such refined oil products, wholesale to bulk customers and retail through the Company's retail distribution network and related activities.

The operating revenues from the marketing and distribution segment in the first half of 2001 were RMB 95.3 billion, up 21.7% compared with the first half of last year, largely due to increases in the selling prices and volumes of gasoline and diesel.

In the first half of 2001, external sales of gasoline were approximately RMB 30.4 billion, up 21% compared with the first half of 2000, largely due to:

- The average realised retail price was up 15% over the same period in 2000 to RMB 3,212 per tonne and sales volume was up 45.2% to 5.06 million tonnes compared with the first half of 2000. The increase in retail sales volumes was as a result of the expansion of the Company's retail network and improved management.
- The average realised direct sales price to bulk customers was up 17% over the same period in 2000 to RMB 2,614 per tonne and the sales volume was up 634% to 459,000 tonnes compared with the first half of 2000. The large increase in direct sales volume to bulk customers was as a result of the shift of direct sales of gasoline from the Company's refining segment to the marketing and distribution segment, effective 2001.

External sales of diesel in the first half of 2001 were RMB 53.4 billion, up 23% compared with RMB 43.5 billion in the first half of 2000, largely due to:

- The average realised retail price was up 4% over the same period in 2000 to RMB 2,661 per tonne and the sales volume was up 55.3% to 7.41 million tonnes compared with the first half of 2000.
- The average realised direct sales price to bulk customers was up 18% over the same period in 2000 to RMB 2,305 per tonne and the sales volume was up 1.4% to 2.59 million tonnes compared with the first half of 2000.

The operating expenses of the marketing and distribution segment in the first half of 2001 were RMB 94.3 billion, up 25.6% from RMB 75.1 billion compared with the first half of 2000. The operating expenses of gasoline and diesel accounted for 82.3% of the total operating expenses of the marketing and distribution segment in the first half of 2001. The average costs for gasoline and diesel in the first half of 2001 were RMB 2,693 per tonne and RMB 2,332 per tonne, up 16% and 10% respectively against the same period in 2000.

The operating profit from the marketing and distribution segment in the first half of 2001 was RMB 1 billion, down 68.8% compared with the first half of 2000, largely due to oversupply in regional markets and the fact that wholesale and retail prices did not reach expected levels, and, although operating turnover increased in the first half of the year compared to the same period last year, the increase in operating expenses exceeded the increase in operating turnover, causing a reduction in operating profits.

The marketing and distribution segment's cash operating costs (defined as operating expenses less the purchase expenses of goods, taxes other than income tax, and depreciation and amortisation, divided by sales volume) was down RMB 8 per tonne compared with the same period in 2000 to RMB 166 per tonne.

#### **Chemicals Segment**

The chemicals segment consists of producing, marketing and distributing petrochemical and inorganic chemical products.

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The operating revenues of the chemicals segment in the first half of 2001 were up 2% from RMB 29.9 billion in the first half of 2000 to RMB 30.6 billion, of which RMB 27.7 billion was from external sales, down RMB 700 million or 2%, compared with RMB 28.4 billion in the first half 2000. The main reason was because of the global economic slow-down and the drop in the international prices for petrochemical products which led to a drop in the domestic prices for domestic chemical products other than synthetic rubber.

The operating expenses of the chemicals segment in the first half of 2001 were RMB 30.4 billion, up 9% from RMB 27.9 billion in the first half of 2000. This was largely due to the fact that since June last year, prices for chemical feedstocks such as naphtha have been closely linked to international prices, and due to the effect of high international oil prices in the first half of this year, which remain at high price level, and due to increased consumption of raw materials in line with increases in production.

The operating profit from the chemicals segment in the first half of 2001 was RMB 200 million, down RMB 1.8 billion or 90%, compared with RMB 2 billion in the first half of 2000.

### Corporate and Other Segment

The operating revenues from the corporate and other segment in the first half of 2001 were RMB 13.2 billion, up 50.0% compared with RMB 8.8 billion in the first half of 2000. The operating expenses were RMB 12.8 billion, up 45.5% from RMB 8.8 billion in the first half of 2000. The increase in operating

revenues and expenses was 45.5%, largely due to the increase in the trading volume of Sinopec International Company Limited, one of the subsidiaries of the Company, turning the operating results of the corporate and other segment from a breakeven into a profit of RMB 400 million.

### CASH FLOW AND SOURCE OF CAPITAL

The following table is extracted from the Company's consolidated statement of cash flows for the relevant period indicated.

#### Net cash generated from Operating Activities

The Company's net cash generated from operating activities in the first half of 2001 was RMB 6.612 billion, down RMB 3.897 billion compared with the first half of 2000. The key reasons are: (1) the increased operating profits resulting an increase in cash inflow of RMB 2.488 billion; (2) the increases in inventory, accounts receivable, notes receivable, payments in advance and other current assets which outweighed increases in accounts payable, notes payable,

provisions and other items, resulting an increase in a cash outflow of RMB 3.734 billion over the same period in 2000; (3) cash outflows for interest paid and income tax paid increased RMB3.05 billion against the first half of 2000. In the same period, interest received and profits on investment received were RMB0.399 billion which, after off-setting against cash outflows, reduced the increase of net cash outflows against the same period last year to RMB2.651 billion. The increase was mainly due to the fact that the Company paid income tax monthly in the first half of 2001, while in the year 2000, the Company only started to pay income tax in the second half of the year.

Cash flow per share for the first half of 2001 was RMB 0.08, down RMB 0.07 per share compared with the first half of 2000, largely due to the issue of H Shares in the second half of last year. In the first half of 2000, share capital was 68.8 billion shares, which increased to 83.9 billion shares in the first half of this year.

	First half, 2001 RMB billions	First half, 2000 RMB billions	Change between the first half of 2001 and the same period of 2000 RMB billions
Net cash generated from operating activities	6.612	10.509	(3.897)
Net cash generated from investment activities	(12.286)	(14.620)	(2.334)
Net cash generated from financing activities	14.899	8.366	6.533
Net increase of cash and cash equivalents	9.225	4.255	4.97

### Net Cash generated from Investment Activities

The generated net cash flows used in the first half of 2001 for the Company's investment activities were RMB 12.286 billion, down RMB 2.334 billion compared with the first half of 2000. The key reasons are: (1) RMB 11.976 billion cash inflow on the maturity of fixed term deposits resulting in an increase in cash inflow of RMB 9.057 billion compared with the first half of 2000; (2) cash payments of RMB 20.938 billion for the purchase and construction of fixed assets, resulting in an increase in cash outflow of RMB 5.728 billion compared with the first half of 2000; (3) RMB 1.691 billion of cash payments for investment activities, resulting in an increase in cash outflow of RMB 893 million compared with the first half of 2000.

### Net Cash generated from Financing Activities

The net cash income from financing activities in the first half of 2001 was RMB 14.899 billion, up RMB 6.533 billion compared with the first half of 2000. The key reasons are: (1) RMB 120.329 billion of cash from banks and other loans, resulting in an increase in cash inflow of RMB 59.217 billion compared with the first half of 2000; (2) the repayment of bank and other loans in the sum of RMB 105.196 billion resulting in an increase in cash outflow of RMB 53.824 billion compared with the first half of 2000; (3) repayment of bonds payable, which resulted in a decrease in cash outflows of RMB 683 million compared to the first half of 2000.

### Historical and Planned Capital Expenditures

The Company aims to increase return on capital employed and enhance its overall competitiveness. Based on its operating strategy, the Company has centralised the decision-making process in relation to investment, streamlined structure and rationalised projects.

The Company's original planned capital expenditure for the year 2001 is RMB 40.76 billion. Based on market conditions, the Company has adjusted this year's planned capital expenditure to RMB 42.76 billion (which does not include RMB 6.45 billion for the acquisition of Sinopec National Star); of which: Exploration and production segment RMB 14.09 billion; Refining segment RMB 6.62 billion; Marketing

and distribution segment RMB 11.39 billion; Chemicals segment RMB 10.3 billion, and Corporate and Others segment RMB 0.36 billion.

The Company's actual capital expenditures (the construction/acquisition of fixed assets, intangible assets) for the first half of 2001 were approximately RMB 20.7 billion, of which RMB 5.6 billion was spent in the exploration and production segment, RMB 2.8 billion in the refining segment, RMB 7.9 billion in the marketing and distribution segment, RMB 4.2 billion in the chemicals segment and RMB 210 million in the corporate and others segment. The following table sets forth the breakdown of the Company's capital expenditures program.

Capital expenditure	Planned figure for 2001 in RMB billion	Actual capital expenditure in the first half, 2001 in RMB billion	Proportion of planned figure constituted by actual expenditure
Exploration and Production Segment	14.09	5.57	39.53%
Refining Segment	6.62	2.81	42.45%
Marketing and Distribution Segment	11.39	7.91	69.45%
Chemicals Segment	10.3	4.19	40.68%
Corporate and others Segment	0.36	0.21	58.33%
Total	42.76	20.69	48.39%