General

Mr. Xu Hongxing
Executive Director
and General Manager

This following analysis should be read in conjunction with the information in the audited financial statements contained in this annual report. The information presented below interprets the Company's financial statements prepared in accordance with IFRS. The Company will file an annual report in Form 20-F with the Securities and Exchange Commission before 30 June 2004. A copy of which will be provided to any shareholder upon written request.

The information set out in this management's discussion and analysis does not form part of the financial statements audited by KPMG, the auditors of the Company, and is included for information purposes only.

Overview

The Company is one of the largest producers of ethylene, resins and plastics in the PRC. The vast majority of the Company's products fall within three principal product groups: (i) resins and plastics, (ii) synthetic rubber, and (iii) basic organic chemical products. In 2003, the Company accounted for approximately 11.8% of the total ethylene production in the PRC. The Company is a leading producer in the PRC of LDPE, cis-polybutadiene rubber, butyl rubber, phenol, acetone, SBS and polypropylene.

All of the Company's products are used in the production of a wide range of manufactured products, such as houseware, household electric appliances, toys, packaging materials and tires. Accordingly, the Company is subject to broad changes in China's economy and benefits from China's consistently strong economic growth, but the Company generally does not suffer from cyclical or other downturns in any particular segment of the economy. However, the Company is sensitive to price fluctuations of crude oil, which directly affect the prices it pays for raw materials.

The Company's principal raw material is cracking feedstock, substantially all of which is purchased from the Parent Company. The Company mainly uses light industrial oil as its cracking feedstock. The Company also uses naphtha, and VGO, cracking wax oil and hydrogenated raffinate oil, which the Company has developed and uses as substitutes of light industrial oil. Since the establishment of the Sinopec Group in 1998, prices of light industrial oil and naphtha have been determined jointly by the National and Development and Reform Commission of the PRC and the Sinopec Group. During the reporting period, the average state price of light industrial oil fluctuated in line with the crude oil price and such average state price of light industrial oil for 2003 increased by 14.0%, as compared with the price in 2002. This increase has put pressure on the Company's margins.

Since the costs of raw materials are effectively beyond the Company's control, the Company generally seeks to increase profits through a combination of increased production volume, more efficient use of raw materials by adopting more efficient procedures and technologies, by shifting production to higher margin products, and by strengthening its marketing efforts, particularly to minimize the lag between changes in customer demand and changes in the Company's production. In 2003, the Company was able to complete a plant overhaul during a one-month shutdown at the tail-end of the SARS outbreak. The shutdown did reduce production during 2003, but the overhaul eliminated production bottlenecks and resulted in increased production capacity without major capital investment. These factors, together with strong price increases for the Company's products, more than offset the rise in raw material prices, resulting in positive results for 2003.

Critical Accounting Policies

The Company's critical accounting policies are set out in note 2 of its financial statements. IFRS requires that the Company adopts the accounting policies and estimation techniques that are most appropriate in the circumstances for the purpose of giving a true and fair view of its results and financial condition. However, different policies, estimation techniques and assumptions in critical areas could lead to materially different results. In particular:

a. Impairments

If circumstances indicate that the net book value of an asset may not be recoverable, this asset may be considered "impaired", and an impairment loss may be recognized in accordance with IAS 36 "Impairment of Assets". The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to recoverable amount. The amount of impairment loss is the difference between the carrying amount of the asset and its recoverable amount. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for the Company's assets are not readily available. In determining the value in use, expected cash flows generated by the asset are discounted to their present value, which requires significant judgement in relation to sales volume, selling price and amount of operating costs.

b. Depreciation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account their estimated residual value. The Company reviews the estimated useful lives of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives are based on the Company's historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

c. Provision for Doubtful Debts

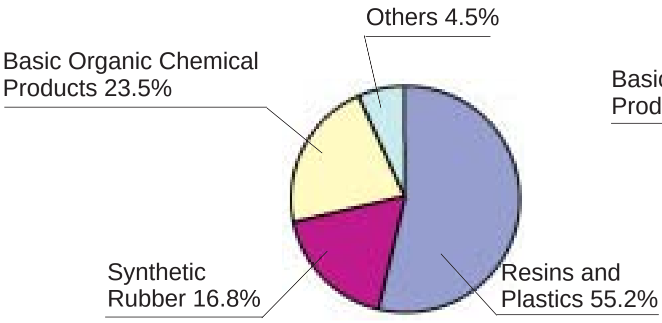
The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make the required payments. The Company bases its estimates on the ageing of its accounts receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of the Company's customers were to deteriorate, actual write-offs might be higher than expected.

Operating Results

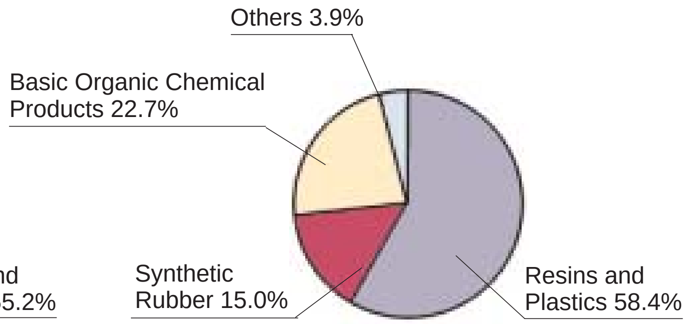
For the year ended 31 December 2003, the Company's turnover increased to RMB 11,473.9 million in 2003 from RMB 9,443.1 million in 2002, representing an increase of 21.5%. This increase in turnover was largely attributable to the substantial increase in the market prices of principal products of the Company in 2003. Due to strong market demand and an increase in the prices of raw materials, petrochemical products in China maintained at a high price level in 2003, which resulted in an increase of 25.9% in the weighted average sales price of the eight principal products of the Company as compared with that of 2002 (representing 79.1% and 78.6% of the total sales revenue of 2002 and 2003, respectively). The sales volume of the eight principal products of the Company decreased by approximately 4.1% in 2003 as compared with that of 2002 due to the one-month shutdown and overhaul; nevertheless, the Company's sales revenue increased significantly. During the reporting period, the profit of the Company before taxation was RMB 877.1 million, a 165.2% increase (in the amount of RMB 546.4 million) as compared with the profit before taxation of RMB 330.7 million recorded in 2002. The Company recorded a net profit of RMB 633.9 million in 2003, a 203.2% increase (in the amount of RMB 424.8 million) as compared with the net profit of RMB 209.1 million in 2002.

The following table sets forth a summary of the income statements for the years of 2003 and 2002:

	2003	2002
	RMB'000	RMB'000
Turnover	**11,473,928**	9,443,061
Cost of sales	**(9,723,562)**	(8,368,029)
Gross profit	**1,750,366**	1,075,032
Selling, general and administrative expenses	**(721,418)**	(530,571)
Other operating income/(expenses), net	**14,095**	(2,903)
Profit from operations	**1,043,043**	541,558
Net financing costs	**(165,936)**	(210,830)
Profit from ordinary activities before taxation	**877,107**	330,728
Income tax expense	**(243,222)**	(121,629)
Profit attributable to shareholders	**633,885**	209,099
Basic earnings per share	**RMB 0.19**	RMB 0.06
Basic earnings per ADS	**RMB 9.39**	RMB 3.10



2003 Turnover



2002 Turnover

The following table sets forth a summary of the financial data of the Company for the past five years, respectively:

	2003	2002	2001	2000	1999
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Total assets	**9,545,311**	10,259,807	10,758,196	8,649,826	8,534,176
Total liabilities	**3,889,479**	5,237,860	5,945,348	3,429,551	3,470,192
Net assets	**5,655,832**	5,021,947	4,812,848	5,220,275	5,063,984
Turnover	**11,473,928**	9,443,061	5,975,255	7,852,913	6,489,746
Profit/(loss) from operations	**1,043,043**	541,558	(350,644)	623,056	631,839
Profit/(loss) attributable to shareholders	**633,885**	209,099	(272,467)	358,731	357,393
Dividends attributable to the year	**168,700**	No dividend declared	No dividend declared	134,960	202,440

The following table sets forth the Company's turnover, net of value-added tax ("VAT"), by principal product groups for the years of 2003 and 2002:

	2003		2002	
	Turnover RMB'000	**Percentage of Turnover**	Turnover RMB'000	Percentage of Turnover
Resins and Plastics	**6,332,332**	**55.2**	5,514,147	58.4
Synthetic Rubber	**1,923,773**	**16.8**	1,418,899	15.0
Basic Organic Chemical Products	**2,700,036**	**23.5**	2,140,185	22.7
Others	**517,787**	**4.5**	369,830	3.9
Total	**11,473,928**	**100.0**	9,443,061	100.0

The following table sets forth the Company's sales, net of VAT, by geographical analysis for the years of 2003 and 2002:

	2003		2002	
	Turnover (RMB Million)	**Percentage of Turnover**	Turnover (RMB Million)	Percentage of Turnover
Northeastern China	**218.0**	**1.9**	160.5	1.7
Northern China	**6,586.0**	**57.4**	5,316.5	56.3
Eastern China	**3,430.7**	**29.9**	2,889.6	30.6
Central-southern China	**814.6**	**7.1**	47.2	0.5
Northwestern China	**22.9**	**0.2**	198.3	2.1
Southwestern China	**252.5**	**2.2**	698.8	7.4
Exports	**149.2**	**1.3**	132.2	1.4
Total	**11,473.9**	**100.0**	9,443.1	100.0

The following table sets forth the percentages of total turnover of the principal operating expenses associated with the Company's business:

	2003	2002
	Percentage	Percentage
Turnover	**100.0**	100.0
Less expenditure		
Raw materials	**(59.2)**	(62.4)
Utility (fuels and power) expenses	**(10.7)**	(12.9)
Depreciation	**(7.8)**	(8.5)
Wages and bonus	**(2.5)**	(2.5)
Other overheads	**(5.1)**	(2.9)
Selling, general and administrative expenses	**(5.7)**	(5.0)
Other operating income/(expenses), net	**0.1**	(0.1)
Operating margin	**9.1**	5.7

Raw material expenses were the largest component of the Company's operating expenses. In 2003 and 2002, 51.2% and 52.2%, respectively, of the cost of sales were expenses relating to purchases of cracking feedstock. In 2003, the total cracking feedstock expense was RMB 4,975.6 million, as compared with RMB 4,365.8 million in 2002, representing an increase of RMB 609.8 million, or 14.0%. This increase was largely due to the significant increase in the price of cracking feedstock in 2003. Along with the changes in the prices of crude oil and domestic finished oil, the price of light industrial oil, the principal raw material of the Company, increased from RMB 2,575 per ton at the beginning of 2003 to RMB 2,670 per ton (including 17% VAT) at the end of 2003, and the average price of the cracking feedstock in 2003 increased by 14.3% as compared with the price in 2002.

The following table sets forth the changes in the state price of light industrial oil, the principal raw material of the Company, in 2003 and 2002 (including VAT):

Unit: RMB per ton

Month / Year	1	2	3	4	5	6	7	8	9	10	11	12
2002	1,670	1,795	1,925	2,185	2,325	2,325	2,375	2,375	2,375	2,575	2,575	2,575
2003	2,575	2,765	2,765	2,765	2,475	2,475	2,475	2,475	2,475	2,475	2,475	2,670

Since significant portions of the Company's expenses were either fixed (as in the case of depreciation expense for a given piece of equipment) or consisted of stable unit costs (as in the case of cracking feedstock), fluctuations in sales (particularly those principally caused by changes in sales volume) or raw material prices caused fluctuations in profitability. In 2003, due to the large increase in the sales volume of the Company as well as the significant increase in the price of principal products of the Company, the operating margin of the Company increased from 5.7% in 2002 to 9.1% in 2003.

Year ended 31 December 2003 compared with year ended 31 December 2002

Turnover increased to RMB 11,473.9 million in 2003 from RMB 9,443.1 million in 2002, representing an increase of RMB 2,030.8 million, or 21.5%. The increase in the turnover was mainly due to the large increase in the prices of the principal products of the Company in 2003. Due to strong market demand and an increase in the prices of raw materials, petrochemical products in China maintained at a high price level in 2003, which resulted in an increase of 25.9% in the weighted average sales price of the eight principal products of the Company as compared to that of 2002 (representing 79.1% and 78.6% of the total sales revenue of 2002 and 2003, respectively). The sales volume of the eight principal products of the Company decreased by approximately 4.1% in 2003 as compared with that of 2002 due to the one-month shutdown and overhaul; nevertheless, the Company's sales revenue increased significantly.

Sales of resins and plastics, which accounted for 55.2% of the Company's total sales, increased by 14.8% from RMB 5,514.1 million in 2002 to RMB 6,332.3 million in 2003. This increase was primarily attributable to the 21.2% increase in the weighted average price for resin and plastic products of the Company in 2003 as compared to that of 2002.

Sales of synthetic rubber, which accounted for 16.8% of the Company's total sales, increased by 35.6% from RMB 1,418.9 million in 2002 to RMB 1,923.8 million in 2003. This increase was primarily due to a 26.6% increase in the sales price of synthetic rubber products in 2003 as compared to that of 2002.

In 2003, sales of basic organic chemical products, which accounted for 23.5% of the Company's total sales, increased by 26.2% from RMB 2,140.2 million in 2002 to RMB 2,700.0 million in 2003. This increase was primarily a result of an increase in the price of the basic organic chemical products of the Company.

Sales of other products, which accounted for 4.5% of the Company's total sales, increased by 40.0% to RMB 517.8 million in 2003 from RMB 369.8 million in 2002.

Cost of sales increased by 16.2% to RMB 9,723.6 million in 2003, up from RMB 8,368.0 million in 2002. This increase was mainly due to the increase in the prices for raw materials and the increased overhead costs resulting from normal shutdown and overhaul. The Company's gross profit increased by 62.8% from RMB 1,075.0 million in 2002 to RMB 1,750.4 million in 2003, as gross margin rose from 11.4% in 2002 to 15.3% in 2003.

Selling, general and administrative expenses increased by RMB 190.8 million (36.0%) to RMB 721.4 million in 2003 from RMB 530.6 million in 2002. This increase in selling, general and administrative expenses was primarily due to the increase in research and development expenses and other expenses.

The Company's profit from 2003 operations was RMB 1,043.0 million, representing an increase of 92.6% when compared with the RMB 541.6 million from 2002 operations. The Company's operating margin increased to 9.1% in 2003, as compared with 5.7% in 2002. The increase in operating margin reflects improvement of the market operating situation as well as a realization of the benefits from the economies of scale of the Company.

Net financing costs in 2003 decreased by RMB 44.9 million from RMB 210.8 million in 2002 to RMB 165.9 million in 2003. This decrease was primarily due to the repayment of certain bank loans in 2003 along with the increase of cash generated from operating activities and the corresponding significant decrease in expenditure of loan interest.

In 2003, the Company recorded a profit before taxation of RMB 877.1 million, representing an increase of 165.2% when compared with the profit before taxation of RMB 330.7 million in 2002. The Company's net profit for 2002 was RMB 209.1 million, and the net profit for 2003 was RMB 633.9 million, representing an increase of 203.2% when compared to that of 2002. The net profit margin for 2003 increased to 5.5% compared to 2.2% for 2002.

Liquidity and Capital Resources

The Company has principally relied on cash generated from operating activities, bank loans and share capital to finance its capital expenditures and working capital.

The Company's net cash flow derived from operating activities is generally much higher than its net profit, mainly due to substantial depreciation. In 2003, the Company's net cash flow from operating activities was RMB 1,616.6 million, with an increase of RMB 579.5 million as compared with the RMB 1,037.1 million net cash flow in 2002. The net cash flow in 2003 was primarily adjusted by (i) profit before taxation of RMB 877.1 million; (ii) depreciation expenses of RMB 890.8 million; and (iii) interest expenditure of RMB 142.8 million. As of 31 December 2003, the accounts receivable and bills receivable of the Company amounted to RMB 423.1 million, equivalent to a sales volume of approximately 14 days in 2003.

In 2003, the net cash used in investing activities amounted to RMB 348.6 million. The funds were mainly used in the technical improvement of phenol-acetone and ethylene glycol units.

The Company's short-term and long-term loans are primarily obtained from PRC financial institutions. In 2003, the Company repaid a total of RMB 3,065.1 million of its short-term loans and RMB 719.8 million of its long-term loans, while it borrowed RMB 2,560 million in short-term loans and RMB 205.7 million in long-term loans. As of 31 December 2003, the Company's total loans taken from banks was RMB 2,684.8 million (including RMB 1,070.0 million in short-term loans and RMB 18.4 million in long-term loans due within one year), a 27.5% decrease from the RMB 3,703.9 million in bank loans (including RMB 1,575.0 million in short-term loans and RMB 201.4 million in long-term loans due within one year) as of 31 December 2002. This was primarily due to the substantial decrease in bank loans resulting from repayment, an increase in the net cash generated from operating activities, and a decrease in cash expenditure for investment as the Company did not carry out any project involving large capital expenditure in 2003.

The Company expects to incur capital expenditures of RMB 300.0 million in 2004 and of RMB 400.0 million in each of 2005 and 2006. These capital expenditures will mainly be used for the technical improvement projects of the Company. The Company believes that its net cash flow from operating activities and new bank loans will be sufficient to cover the Company's expected capital expenditures for the above periods.

Gearing Ratio

The Company's gearing ratio was 47.5% in 2003, compared with 73.8% in 2002. Such decrease was mainly due to the decrease in both long-term and short-term debts caused by repayment of certain bank loans and an increase in net cash generated from operating activities in 2003.

The gearing ratio is calculated by dividing the total amount of both long-term and short-term bank loans by the shareholders' equity.

Dividend Policy

Following the establishment of the Company as a joint stock limited company in April 1997, the distribution of the Company's dividends is considered annually by the Board of Directors and decided by the shareholders' general meeting. Payment of future dividends will depend on the profits, financial conditions, future earnings and other factors of the Company.

Contingent Liabilities

As of 31 December 2003, the Company had no significant contingent liabilities.

Purchase, Sale and Investment

For the year ended 31 December 2003, there was no material purchase, sale or investment in connection with the Company's subsidiaries and associates.

Pledges of Assets

As of 31 December 2003, there was no significant pledge of assets by the Company.

Exposure to Fluctuations in Exchange Rates and Any Related Hedges

The Company is exposed to exchange rate risks primarily due to its foreign currency denominated long-term debt and, to a limited extent, its cash and cash equivalents being denominated in foreign currencies. The Company had not been engaged in any foreign currency hedging activities for the year ended 31 December 2003.

Contractual Obligations

The following table sets forth the Company's obligations to make future payments under contracts as of 31 December 2003:

	As of 31 December 2003 payment due by period			
	Total	2004	2005	2006
	RMB'000	RMB'000	RMB'000	RMB'000
Contractual obligations (1):				
Short-term debts	1,170,000	1,170,000	-	-
Long-term debts	1,614,760	18,401	709,193	887,166
Total contractual obligations	2,784,760	1,188,401	709,193	887,166

(1) Contractual obligations represent on-balance sheet contractual liability as of 31 December 2003.

Reconciliation to Accounting Principles Generally Accepted in the United States of America ("US GAAP")

The Company prepares a set of financial statements in compliance with IFRS, which differs in certain significant respects from US GAAP. Please refer to "Supplementary Information for North American Shareholders" for the nature and effect of differences in connection with the accounting policies.