

Management Discussion and Analysis

The management of the Group sincerely reports the discussion and analysis of 2006 operating results.

OPERATING RESULTS

In 2006, the management fully and seriously implemented various resolutions of the shareholders' meetings and the Board, and has captured favorable opportunity of rising commodity prices, carefully organized production, and recorded sales income of RMB10,678,810,000 in the year, representing an increase of RMB7,642,595,000, or 251.71% over the previous year. Among the growth, 12.69% was attributable to growth in new business, 15.64% was attributable to growth in the increase of price, and 71.67% was attributable to growth in production volume.

The table below sets out the sales by products for the two years ended 31 December 2005 and 2006:

Product	2006			2005		
	Unit price RMB	Volume	Amount/ RMB'000	Unit price RMB	Volume	Amount/ RMB'000
Gold	157.19/g	46,776.75 kg	7,352,810	119.25/g	20,155 kg	2,403,434
Gold concentrates	131.23/g	1,795.39 kg	235,609	108.37/g	892 kg	96,688
Copper concentrates	44,591/t	32,003.5 t	1,427,068	23,476/t	17,067 t	400,667
Copper cathodes	51,336.74/t	6,710.75 t	344,508	33,608/t	1,125 t	37,809
Zinc bullions	26,829/t	36,151 t	969,884	–	–	–
Zinc concentrates	16,179/t	11,365 t	183,875	8,965/t	1,418 t	12,713
Iron concentrates	360.13/t	486,682.69 t	175,270	332.13/t	335,025 t	111,272
Others			88,805			6,191
Less: Sales						
Tax and levies			(99,019)			(32,559)
Total			10,678,810			3,036,215

Note: The sales of gold include refined and processed gold of 28,510 kg.

Management Discussion and Analysis

The Group's revenue in 2006 has increased by 251.71% over 2005, which was mainly attributable to (i) gold sales increased by 214% in which, the production of gold at Zijinshan Gold Mine was increased by 14%, the sales of gold in Guizhou Zijin and Hunchun Zijin have increased by 26% and 8.36% respectively, and that Luoyang Yinhui sold 27,660 kg gold was the main reason of the growth; (ii) Xinjiang Ashele Copper Mine and the successful commencement of the operation of Zijinshan Copper Mine recorded increase in sales of copper concentrates and copper cathodes by 112.81%; (iii) the average sales price of gold and copper cathodes increased by 32% and 52.75% respectively; (iv) the commencement of operation of zinc refinery in Inner Mongolia additionally increased RMB969 million in sales of zinc ingot.

AN ANALYSIS OF GROSS PROFIT AND GROSS PROFIT MARGIN

The Group is mainly engaged in mine development. The Group's cost of sales mainly includes mining, processing, and refining costs, ore transportation cost, raw materials consumption, public management expenses, salaries and depreciation of fixed assets employed for production. The table below sets out details of the gross profit margin for the two years ended 31 December 2005 and 2006.

Product	2006 %	2005 %
Gold (gold produced from ores)	73.66	66.02
Gold (processed gold)	0.52	0.51
Gold concentrates	51.7	51.51
Copper concentrates	83.25	62.88
Copper cathodes	73.86	50.63
Zinc concentrates	76.83	–
Zinc bullions	35.9	–
Iron concentrates	56.64	59.32
Others	–	–
Total (included processed gold)	37.08	48.51
Total (excluded processed gold)	63.59	59.66

The Group's overall gross profit margin decreased from 48.51% in 2005 to 37.08% in 2006, which was mainly attributable to the gold processed business recording higher operating income and lower gross profit margin. The overall gross profit margin (excluded processed gold) could maintained at a high level of 63.59%. The increase of gross profit margin was mainly attributable to the growth in copper and zinc business and the rising of metal prices. In 2006, the average sales price of gold is RMB157.19/g and the average sales price of copper cathodes is RMB51,336.74/tonne.

Management Discussion and Analysis

SELLING AND DISTRIBUTION COSTS

The Group's selling and distribution costs have increased by 116% from RMB66.06 million in 2005 to RMB143.07 million in 2006, which was mainly attributable to the increase in transportation costs resulting from the increase in the sales of copper concentrates, iron concentrates, and zinc. All these costs are directly recorded under selling and distribution costs.

ADMINISTRATION EXPENSES

The Group's administration expenses in 2006 amounted to RMB417.51 million, representing an increase of 70.49% over last year. Due to the expansion in production, it caused a substantial increase in management expenses in Shanghang Zijinshan Gold Copper Mine, Ashele Copper Mine, Guizhou Zijin, and Hunchun Zijin. At the same time, the staff salaries have been increased under the good performance of the Group and it represented 63.32% of the increase of administrative expenses. Also, the recognition of the expenses of 9 new subsidiaries, substantially increased the administrative expenses. It represented 36.68% of the total increase of expenses.

OTHER OPERATING EXPENSES

The Group's other operating expenses is RMB673.17 million in 2006 which increased by RMB604.68 million over RMB68.49 million in 2005. The increase was mainly attributable to the increase in donation amounting to RMB117.45 million and the increase of loss in derivative financial instruments amounting to RMB484.29 million.

DERIVATIVE FINANCIAL INSTRUMENTS

As at 31 December 2006, the Group and the Company recognized a loss of RMB494.577 million in forward contracts selling gold and copper cathodes (after deducting the provision in 2005). The actual effect to the net profit of the equity holders is RMB296,027,025.

As at 31 December 2006, the Group accumulatively settled 13,480 tonnes copper cathodes and 54,400 ounces gold (1,690 kg) forward selling contracts. The settlement caused a loss of RMB347.465 million (2005: nil).

As at 31 December 2006, the Group and the Company entered and held 2,245 tonnes of copper cathodes and 137,600 ounces of gold (4,280 kg) forward selling contracts. The Company recognized an unrealized investment loss of RMB147.112 million (2005: RMB10.287 million).

The conduction of gold and copper forward selling contracts is for the purpose of locking up the profit at certain reasonable prices. The Board has made adjustments on the transaction volume in 2007 which limits the transaction volume of copper cathodes not exceeding 25% of the total annual planned production and the total position of gold not exceeding 25% of total annual planned production from mines. The Board will prudently evaluate the relative risks and take necessary measures to reduce the risk.

Management Discussion and Analysis

DONATION AND SOCIAL RESPONSIBILITY

As at 31 December 2006, the Group donated RMB148.423 million (2005: RMB30.966 million) which included Xinjiang Ashele's donation of RMB114.78 million. The Board considered that it is the corporate responsibility to increase donation to build schools and improve the infrastructure and environment of the society especially in the time of high metal price and with great support from the local governments and people.

FINANCE COSTS

The Group's finance costs in 2006 amounted to RMB114.98 million, with an increase of 523.54% over RMB18.44 million in 2005, which was mainly attributable to an increase in external investment and the fact that the Company and subsidiaries increased the interests bearing bank loan. In comparison with the beginning of the reporting year, long term loan increased by RMB1,953.63 million and short term loan increased by RMB818.29 million, which caused a great increase in interest expenses (The debt/asset ratio is 55.47%).

WORKING CAPITAL AND CAPITAL RESOURCES

As at 31 December 2006, the Group's cash and cash equivalents amounted to RMB1,939.41 million, representing an increase of RMB933.61 million, or 93% over the previous year.

During the year, net cash inflow generated from the Group's operating activities amounted to RMB2,606.29 million, an increase of RMB1,478.38 million or 131% over the previous year. The main reasons for the increase in the cash-flow generated from the Group's operating activities were (i) the increase in sales volume and price in gold; (ii) the increase in the production and sales price of copper of the Company and its controlling subsidiaries; and (iii) the increase of sales price in other products like zinc and the increase of production volume in iron.

During the year, the net cash outflow generated from the Group's operating activities amounted to RMB3,615.14 million, an increase of RMB1,858.46 million or 105.79% over the previous year. The main reasons for the increase in investment activities were (i) the increase of the Group's acquisition of stakes in 11 subsidiaries and 1 associated company and 2 joint venture companies; and (ii) the Company's technology upgrade in gold and copper mines and the increase of input for the subsidiaries infrastructure.

During the year, net cash inflow generated from the Group's financing activities amounted to RMB1,946.18 million, an increase of RMB1,137.35 million or 141% over the previous year, which was mainly due to more bank loans required for increasing external investment and investment in fixed assets.

As at 31 December 2006, the Group's total borrowings amounted to RMB4,057.58 million (31 December 2005: RMB1,285.66 million) of which the amount repayable within two years was approximately RMB2,175.91 million, the amount repayable within two to five years was approximately RMB1,787.24 million, and the amount repayable in over five years was RMB94.43 million. All the bank borrowings bore interest rates between 2.55% to 6.696% (2005: 2.55% to 6.696%). The borrowings from financial institutions were mainly for the Group's holding subsidiaries.

Management Discussion and Analysis

The Group's daily capital requirements and capital expenditures were expected to be financed from its internal cashflow. The Group also possessed substantial amount of uncommitted short-term loan facilities provided by its major banks.

PROFITS ATTRIBUTABLE TO SHAREHOLDERS AND EARNINGS PER SHARE

The Group's profits attributable to shareholders as at 31 December 2006 were approximately RMB1,704.51 million, representing an increase of 142.24% over approximately RMB703.64 million in 2005.

For the year ended 31 December 2006, the Group's earnings per Share (basic) was RMB0.16, an increase of 142.24% over the previous year. The calculation of earnings per Share was based on the Group's profit attributable to shareholders of RMB1,704.51 million (2005: RMB703.64 million) and the weighted average number of 10,513,047,280 Ordinary Shares (2005: 10,513,047,280 Shares Adjusted) in issue during the year.

TAX

Income taxes of the Group for the years of 2006 and 2005 were set out in the table below:

	2006	2005
	RMB'000	RMB'000
Group:		
Current – Hong Kong	4,357	–
– Mainland China	592,369	277,867
Overprovision in prior years	(33,963)	(14,038)
Deferred	(51,942)	–
	510,821	263,829

Provision for Hong Kong profits tax has been provided at the rate of 17.5% on the assessable profits arising in Hong Kong for the year. No provision for Hong Kong tax was made in 2005 as the Group had no assessable profits arising in Hong Kong for that year. Provision for the PRC corporate income tax has been provided at the rate of 33% based on the taxable profits except for some subsidiaries enjoy tax concession.

Details of the income tax of the Group are set out in note 10 to the financial statements.