

SINOPEC SHANGHAI PETROCHEMICAL CO LTD

Form 20-F

April 30, 2013

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 20-F**

.. **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2012

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

OR

.. **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

Date of event requiring this shell company report

For the transition period from                      to

Commission file number 1-12158

(Exact name of Registrant as specified in its charter)

**Sinopec Shanghai Petrochemical Company Limited**

(Translation of Registrant's name into English)

**The People's Republic of China**

(Jurisdiction of incorporation or organization)

**No. 48 Jinyi Road, Jinshan District, Shanghai, PRC 200540**

(Address of principal executive offices)

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(Name, Telephone, Email and/or Facsimile number and Address of Company Contact Person)

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**Securities registered or to be registered pursuant to Section 12(b) of the Act.**

Title of each class	Name of each exchange on which registered
<b>American Depositary Shares, each representing 100 H Shares, par value RMB1.00 per Share</b>	<b>New York Stock Exchange</b>
<b>H Shares, par value RMB1.00 per Share</b>	<b>The Stock Exchange of Hong Kong Limited</b>

**Securities registered or to be registered pursuant to Section 12(g) of the Act.**

None

(Title of Class)

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.**

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

**2,330,000,000 H Shares, par value RMB1.00 per Share**

**4,870,000,000 domestic shares, par value RMB1.00 per Share**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or (15) (d) of the Securities Exchange Act of 1934. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232,405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

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Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP

International Financial Reporting Standards as issued

Other

by the International Accounting Standards Board

If  Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.  Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

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**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This annual report includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, included in this annual report that address activities, events or developments which we expect or anticipate will or may occur in the future are hereby identified as forward-looking statements for the purpose of the safe harbor provided by Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. The words such as believe, intend, expect, anticipate, project, estimate, predict, plan and similar expressions are also intended to identify forward-looking statements. Forward-looking statements address, among others, such issues as:

amount and nature of future development,

future prices of and demand for our products,

future earnings and cash flow,

capital expansion programs,

future plans and capital expenditures,

expansion and other development trends of the petrochemical industry,

expected production or processing capacities, including expected rated capacities and primary distillation capacities, of units or facilities not yet in operation,

expansion and growth of our business and operations; and

our prospective operational and financial information.

These statements are based on assumptions and analyses made by us in light of our experience and our perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in particular circumstances. However, whether actual results and developments will meet our expectations and predictions depends on a number of risks and uncertainties which could cause actual results to differ materially from our expectations, including the risks set forth in Item 3. Key Information Risk Factors and the following:

fluctuations in crude oil and natural gas prices,

fluctuations in prices of our products,

failures or delays in achieving production from development projects,

potential acquisitions and other business opportunities,

continued availability of capital and financing;

general economic, market and business conditions, including volatility in interest rates, changes in foreign exchange rates and volatility in commodity markets; and

other risks and factors beyond our control.

Consequently, all of the forward-looking statements made in this annual report are qualified by these cautionary statements and readers are cautioned not to place undue reliance on these forward-looking statements. These forward-looking statements should be considered in light of the various important factors set forth above and elsewhere in this annual report. In addition, we cannot assure you that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected effect on us or our business or operations.

### EXCHANGE RATES

Unless otherwise specified, references in this annual report to U.S. Dollars or U.S.\$ are to United States Dollars, references to HK dollars or HK\$ are to Hong Kong dollars and references to Renminbi or RMB are to Renminbi yuan, the legal tender currency of the PRC.

We publish our financial statements in Renminbi. Unless otherwise indicated, all translations from Renminbi to U.S. Dollars have been made at a rate of RMB6.2301 to U.S.\$1.00, the noon buying rate on December 31, 2012 as set forth in the H.10 statistical release of the U.S. Federal Reserve Board. We do not represent that Renminbi or US dollar amounts could be converted into U.S. Dollars or Renminbi, as the case may be, at any particular rate.



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**CERTAIN TERMS AND CONVENTIONS**

References to we or us or Company are references to Sinopec Shanghai Petrochemical Company Limited and our subsidiaries, unless the context requires otherwise. Before our formation, these references relate to the petrochemical businesses carried on by the Complex.

References to Sinopec Corp. are references to China Petroleum & Chemical Corporation, the controlling shareholder of the Company.

References to the Sinopec Group are references to China Petrochemical Corporation, the controlling company of Sinopec Corp.

References to the Complex are references to Shanghai Petrochemical Complex, our predecessor founded in 1972.

References to China or the PRC are references to The People's Republic of China which, for the purpose of this annual report and for geographical reference only, excludes Hong Kong, Macau and Taiwan.

References to our A Shares are references to 720,000,000 of our domestic shares, par value RMB1.00 per share, which are ordinary shares subscribed for and traded exclusively on the Shanghai Stock Exchange by and between Chinese investors.

References to ADSs are references to our American Depositary Shares, which are listed and traded on the New York Stock Exchange. Each ADS represents 100 H Shares.

References to our domestic shares are references to all of our domestic shares, par value RMB1.00 per share, which are ordinary shares held by Chinese investors.

References to our H Shares are references to our overseas-listed foreign ordinary shares, par value RMB1.00 per share, which are listed and traded on the Stock Exchange of Hong Kong Limited ( HKSE ) under the number 338 .

Rated Capacity is the output capacity of a given production plant or, where appropriate, the throughput capacity, calculated by estimating the number of days in a year that the production plant is expected to operate, including downtime for regular maintenance, and multiplying that number by an amount equal to the plant optimal daily output or throughput, as the case may be.

All references to tons are to metric tons.

Unless otherwise noted, references to sales volume are to sales to entities other than us or our divisions and subsidiaries.

**Table of Contents****PART I****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS.**

Not applicable.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE.**

Not applicable.

**ITEM 3. KEY INFORMATION.****A. Selected Financial Data.**

Our selected consolidated statements of operations data (except for ADS data) and cash flows data for each of the years ended December 31, 2010, 2011 and 2012 and our selected consolidated balance sheets data as of December 31, 2011 and 2012 are derived from our consolidated financial statements included in Item 17. Financial Statements. Our selected consolidated statements of operations data and cash flows data for the years ended December 31, 2008 and 2009 and our consolidated balance sheets data as of December 31, 2008, 2009 and 2010 are derived from our consolidated financial statements not included in this annual report. Our selected consolidated financial data should be read in conjunction with our consolidated financial statements, and the notes thereto, and Item 5. Operating and Financial Review and Prospects. Our consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ( IFRS ), as issued by the International Accounting Standards Board.

**Selected Consolidated Financial Data****(in thousands, except per share and per ADS data)**

	Years Ended December 31,				
	2008 (RMB)	2009 (RMB)	2010 (RMB)	2011 (RMB)	2012 (RMB)
<b>CONSOLIDATED STATEMENTS OF OPERATIONS DATA</b>					
Net sales:					
Synthetic fibers	3,662,023	2,823,663	3,906,636	4,150,231	3,313,318
Resins and plastics	14,850,284	12,263,540	14,900,012	16,418,559	14,706,350
Intermediate petrochemicals	10,271,840	8,421,035	17,206,440	19,023,204	17,993,493
Petroleum products	27,552,859	18,917,890	28,733,890	37,350,244	38,301,388
Trading of petrochemical products	2,813,200	4,623,989	6,565,793	11,616,999	12,020,651
Others	179,565	295,147	783,111	950,416	882,074
(Loss)/profit from operations	(7,820,762)	2,019,978	2,963,594	1,059,824	(1,772,446)
(Loss)/earnings before income tax	(8,017,936)	2,163,011	3,529,878	1,296,706	(2,016,473)
Net (loss)/income attributable to equity shareholders of the Company	(6,241,067)	1,588,365	2,769,023	956,106	(1,528,397)
Net income attributable to non-controlling interests	36,717	64,471	25,358	30,416	23,255
Basic (loss)/earnings per share(a)	(0.87)	0.22	0.38	0.13	(0.21)
Basic (loss)/earnings per ADS(a)	(86.68)	22.06	38.46	13.28	(21.23)

(a)

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The calculation of earnings per share is based on the weighted average number of shares outstanding of 7,200,000,000 in each of 2008, 2009, 2010, 2011 and 2012, respectively. Earnings per ADS are calculated on the basis that one ADS is equivalent to 100 H Shares.

	Years Ended December 31,				
	2008	2009	2010	2011	2012
	(RMB)	(RMB)	(RMB)	(RMB)	(RMB)
<b>CONSOLIDATED STATEMENTS OF CASH FLOWS DATA</b>					
Net cash (used in)/generated from operating activities	(3,986,490)	3,346,890	3,973,719	2,219,994	(2,066,385)
Capital expenditure	1,511,072	2,120,292	1,356,845	3,481,235	4,259,859

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	Years Ended December 31,				
	2008 (RMB)	2009 (RMB)	2010 (RMB)	2011 (RMB)	2012 (RMB)
Net proceeds/ (repayment) related to corporate bonds		1,000,000		(1,000,000)	
Proceeds from loans and borrowings	32,528,758	29,211,434	39,355,780	35,106,127	53,365,372
Repayment of loans and borrowings	27,377,610	31,849,620	42,631,344	32,791,261	46,779,614

	Years Ended December 31,				
	2008 (RMB)	2009 (RMB)	2010 (RMB)	2011 (RMB)	2012 (RMB)

**CONSOLIDATED BALANCE SHEETS DATA**

Current assets	6,511,351	9,061,425	8,531,841	9,665,814	12,891,424
Property, plant and equipment	13,272,899	14,977,205	13,570,559	12,501,980	17,468,748
Total assets	27,667,066	30,039,902	28,697,535	30,718,865	36,462,546
Short term debt(a)	9,372,725	7,774,673	4,395,438	5,512,074	11,023,877
Current liabilities	13,342,720	14,304,925	10,573,225	12,271,832	18,927,257
Long term debt (excluding current portion)	429,021	304,258	175,000	160,050	1,231,340
Total equity attributable to equity shareholders of the Company	13,630,972	15,136,434	17,689,457	17,925,563	16,037,166

(a) Including corporate bonds and current portion of long term debt.

*Dividends*

The following table sets forth certain information concerning the dividends since January 1, 1994:

Dividend Period	Dividend per Share
January 1, 1994-June 30, 1994	RMB0.04 (U.S.\$0.0064)
July 1, 1994-December 31, 1994	RMB0.085 (U.S.\$0.0136)
January 1, 1995-June 30, 1995	RMB0.04 (U.S.\$0.0064)
July 1, 1995-December 31, 1995	RMB0.09 (U.S.\$0.0144)
January 1, 1996-June 30, 1996	RMB0.04 (U.S.\$0.0064)
July 1, 1996-December 31, 1996	RMB0.08 (U.S.\$0.0128)
January 1, 1997-December 31, 1997	RMB0.06 (U.S.\$0.0096)
January 1, 1998-December 31, 1998	RMB0.03 (U.S.\$0.0048)
January 1, 1999-December 31, 1999	RMB0.05 (U.S.\$0.0080)
January 1, 2000-December 31, 2000	RMB0.06 (U.S.\$0.0096)
January 1, 2001-December 31, 2001	No dividend
January 1, 2002-December 31, 2002	RMB0.05 (U.S.\$0.0080)
January 1, 2003-December 31, 2003	RMB0.08 (U.S.\$0.0128)
January 1, 2004-December 31, 2004	RMB0.20 (U.S.\$0.0321)
January 1, 2005-December 31, 2005	RMB0.10 (U.S.\$0.0161)
January 1, 2006-December 31, 2006	RMB0.04 (U.S.\$0.0064)
January 1, 2007-December 31, 2007	RMB0.09 (U.S.\$0.0144)
January 1, 2008-December 31, 2008	No dividend
January 1, 2009-December 31, 2009	RMB0.03 (U.S.\$0.0048)
January 1, 2010-December 31, 2010	RMB0.10 (U.S.\$0.0161)
January 1, 2011-December 31, 2011	RMB0.05 (U.S.\$0.0080)
January 1, 2012-December 31, 2012	No dividend

See also [Item 8. Financial Information](#) — [A. Consolidated Statements and Other Financial Information](#) — [Dividend Policy](#).



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The Chinese government controls its foreign currency reserves in part through direct regulation of the conversion of Renminbi into foreign exchange and through restrictions on foreign trade. See [Item 10. Additional Information – D. Exchange Controls](#).

The following table sets forth information concerning exchange rates between Renminbi and U.S. Dollars for the periods indicated:

Period	Noon Buying Rates (RMB/U.S.\$)			
	Period End	Average <sup>(1)</sup>	High	Low
2008	6.8225	6.9477	7.2946	6.7899
2009	6.8259	6.8307	6.8470	6.8176
2010	6.6000	6.7696	6.8330	6.6000
2011	6.2939	6.4630	6.6364	6.2939
2012	6.2301	6.3093	6.3879	6.2221
October 2012	6.2372	6.2627	6.2877	6.2372
November 2012	6.2265	6.2338	6.2454	6.2221
December 2012	6.2301	6.2328	6.2502	6.2251
January 2013	6.2186	6.2215	6.2303	6.2134
February 2013	6.2213	6.2323	6.2438	6.2213
March 2013	6.2108	6.2154	6.2246	6.2105

Source: The sources of the exchange rates are: (i) with respect to any period ending on or prior to December 31, 2008, the Federal Reserve Bank of New York, and (ii) with respect to any period ending on or after January 1, 2009, the H.10 statistical release of the Federal Reserve Board.

Note: (1) Determined by averaging the rates on the last business day of each month during the respective period.

***B. Capitalization and Indebtedness.***

Not applicable.

***C. Reasons for the Offer and Use of Proceeds.***

Not applicable.

***D. Risk Factors.***

*An investment in our ADSs involves significant risks. The risks and uncertainties described below are not the only ones we face. You should consider carefully all of the information in this annual report, including the risks and uncertainties described below and our consolidated financial statements and related notes, before making an investment in our ADSs. Any of the following risks could have a material adverse effect on our business, financial condition and results of operations. In any such case, the market price of our ADSs could decline, and you may lose all or part of your investment.*

*Our operations may be adversely affected by the cyclical nature of the petroleum and petrochemical market and by the volatility of prices of crude oil and petrochemical products.*

Most of our revenues are attributable to the sale of refined oil and petrochemical products, which have historically been cyclical and sensitive to the availability and price of raw materials and general economic conditions. Markets for many of our products are sensitive to changes in industry capacity and output levels, changes in regional and global economic conditions, the price and availability of substitute products and changes in consumer demand, which from time to time have had a significant impact on our product prices in the regional and global markets. Due to the decrease in tariff charges, the removal of other restrictions on importation and the Chinese government's gradual relaxation of its control of the allocation of products and pricing, many of our products have become increasingly vulnerable to the cyclical nature of regional and global petroleum and petrochemical markets, which may adversely affect our operations.

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We consume large amounts of crude oil to manufacture our products of which more than 90% is imported. In 2012, crude oil costs accounted for RMB55.54 billion, or 62.67% of our annual cost of sales. As a result, changes in crude oil prices can affect our profitability. In recent years, due to various reasons, the price of crude oil has fluctuated significantly. We cannot rule out the possibility of the occurrence of certain global emergencies which might disrupt our crude oil supply. We expect that the volatility and uncertainty of the prices of crude oil and petrochemical products will continue, and that increasing crude oil prices and declines in prices of petrochemical products may adversely affect our business, financial condition and results of operations.

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*Some of our products are subject to government price controls, and we are not able to pass on all cost increases from rising crude oil prices through higher product prices.*

We consume large amounts of crude oil to manufacture our products of which more than 90% is imported. We attempt to mitigate the effect of increased costs due to rising crude oil prices. However, our ability to pass on these increased costs to our customers is dependent on market conditions and government regulations. Given that the increase of the sales prices of our products may lag behind the increase of crude oil costs, we may fail to completely cover the increased costs by increasing our sales prices, particularly where government regulations restrict the prices of certain of our fuel products. In particular, gasoline, diesel and jet fuel, and liquefied petroleum gas are subject to government price controls at present. In 2010, 2011 and 2012, approximately 34.41%, 36.70% and 40.09% of our net sales were from such products subject to price controls. In 2012, the domestic prices of refined oil products were not brought into line with the prices of crude oil on the international markets in a timely manner due to various policy concerns, *e.g.*, the government's desire to control the high inflation rate in China, which resulted in a decline of RMB539.7 million of the operating profit of our refining business over the previous year. Although the current price-setting mechanism for refined petroleum products in China allows the Chinese government to adjust price in the PRC market when the average international crude oil price fluctuates beyond certain levels within a certain time period (see Item 4. Information on the Company B. Business Overview Product Pricing), the Chinese government still retains discretion as to whether or when to adjust the prices of the refined oil products. The Chinese government generally exercises certain price control over refined oil products once international crude oil prices experience a sustained rise or become significantly volatile. For instance, some of our fuel products are required to be sold to designated distributors (such as the subsidiaries of Sinopec Corp.). Because we cannot freely sell our fuel products to take advantage of opportunities for higher prices, we may not be able to fully cover increases in crude oil prices by increasing the sale prices of our products, which has had and will possibly continue to have a material adverse effect on our financial condition, results of operations and cash flows.

*Our development and operation plans have significant capital expenditure and financing requirements, which are subject to a number of risks and uncertainties.*

The petrochemical business is a capital intensive business. Our ability to maintain and increase our revenues, net income and cash flows depends upon continued capital spending. Our current business strategy contemplates capital expenditure for 2013 of approximately RMB2.6 billion (U.S.\$417.3 million), which will be provided through financing activities and use of our own capital. Our actual capital expenditures may vary significantly from these planned amounts, subject to our ability to generate sufficient cash flows from operations, investments and other factors that may be beyond our control. In addition, there can be no assurance as to whether, or at what cost, our capital projects will be completed or the success of these projects if completed.

As of March 31, 2013, we had an aggregate outstanding indebtedness of approximately RMB9.526 billion (U.S.\$1.529 billion). Most of our loans are with state-controlled banks in China and structured as short term debt obligations with payment due in one year or less. These banks have generally been willing to provide new short term loans while we pay off existing loans. Sinopec Corp., our controlling shareholder, did not provide any guarantee or credit support for our debt for the year ended December 31, 2012 and for the three-month period ended March 31, 2013.

Our ability to obtain external financing in the future and our ability to make timely repayments of our debt obligations are subject to a variety of uncertainties, including: our future results of operations, financial condition and cash flows; the condition of the economy in China and the condition of markets for our products; the cost of financing and the condition of financial markets; the issuance of relevant government approvals and other project risks associated with the development of infrastructure in China; and the continuing willingness of banks to provide new loans as we pay down existing debt.

While we anticipate that we will rely less on debt to finance capital expenditures and operations as the global economic outlook continues to improve, our business, results of operations and financial condition could be adversely affected if we fail to obtain sufficient funding for our operations or development plans.

*We could face increasing competition.*

Our principal market, Eastern China, which is comprised of Shanghai, Shandong, Jiangsu, Anhui, Zhejiang, Jiangxi and Fujian, has enjoyed stronger economic growth and a higher demand for petrochemical products than other regions of China. As a result, we believe that our competitors will try to expand their sales and build up their distribution networks in our principal market. We believe this will have an adverse impact on the production and sale of our major products. Moreover, Chinese private enterprises have gradually overcome technological and funding barriers to extend their business from the downstream processing sector to the upstream petrochemical field. These enterprises have advantages in many areas such as flexibility in operation costs, preferential policy treatments and regional presence, and may use these advantages to compete with us in our target market.





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*We are controlled by Sinopec Corp., whose interests may not be aligned with yours.*

As of March 31, 2013, Sinopec Corp. owned 55.56% of our shares. Accordingly, it has voting and management control over us, and its interests may be different from the interests of our other shareholders. Subject to our Articles of Association and applicable laws and regulations, Sinopec Corp. will be in a position to cause us to declare dividends, determine the outcome of corporate actions requiring shareholder approval or effect corporate transactions without the approval of the holders of the H shares and ADSs. Any such increase in our dividend payout would reduce funds available for reinvestment in our business and any such actions or transactions could adversely affect us or our minority shareholders. Sinopec Corp. may also experience changes in its own business strategy and policies. Although we are not currently aware of any specific changes, Sinopec Corp. may change its policies or practices toward us in ways that we cannot predict, with corresponding unpredictable consequences for our business. Additionally, Sinopec Corp. may leverage its controlling shareholder position to influence our decisions with regard to the manufacturing and operation, allocation of financial resources and appointment and removal of senior managements, which could adversely affect us or our minority shareholders.

We have also engaged from time to time and will continue to engage in a variety of transactions with Sinopec Corp., Sinopec Group, the controlling company of Sinopec Corp., and their various subsidiaries or affiliates which provide a number of services to us, including the supply of raw materials, product distribution and sales agency, project design and installment service, petrochemical industry related insurance and financial services. We also sell oil and petrochemical products to Sinopec Corp. and its affiliates. Our transactions with these companies are governed by a Mutual Product Supply and Sales Services Framework Agreement with Sinopec Corp. and a Comprehensive Services Framework Agreement with Sinopec Group, the terms of which were negotiated on an arm's length basis, see [Item 7. Related Party Transactions – B. Intercompany Service Agreements and Business-related Dealings](#). Our business and results of operations could be adversely affected if Sinopec Corp. or Sinopec Group refuses to engage in such transactions or if they seek to amend the contracts between the parties in a way adverse to us. In addition, Sinopec Corp. has interests in businesses which compete or are likely to compete, either directly or indirectly, with our businesses. Because Sinopec Corp. is our controlling shareholder and its interests may conflict with our own interests, Sinopec Corp. may take actions that favor itself over our interests.

*Our business operations may be adversely affected by present or future environmental regulations.*

We are subject to extensive environmental protection laws and regulations in China. These laws and regulations permit:

the imposition of fees and penalties for the discharge of waste substances;

the levy of payments and fines for damages for environmental offenses; and

the government to close or suspend any facility which fails to comply with orders and require it to correct or stop operations causing environmental damage.

Our production operations produce substantial amounts of waste materials (*i.e.*, waste water, waste gas and waste residue). In addition, our production and operations require permits that are subject to renewal, modification and revocation. At present, we believe that our operations substantially comply with all applicable Chinese environmental laws and regulations as they have been previously interpreted and enforced. The Chinese government (including the local governments), however, has moved, and may move further, toward the adoption of more regulations and more stringent environmental standards. Chinese national or local authorities may also apply more rigorous enforcement of such regulations which would require additional expenditures on environmental matters.

*Our operations are exposed to risks relating to operating hazards and production safety and we have limited insurance coverage for resulting losses.*

Our operations involve the handling and storage of explosives and other hazardous articles. In addition, our operations involve the use of heavy machinery, which involves inherent risks that cannot be entirely eliminated through our preventive efforts. As a result, we may encounter fires, explosions and other unexpected incidents during our operations, which may cause personal injuries or death, property damage, environmental damage, interruption of operations and reputational damages to us. Each of such incidents could have a material adverse impact on our business, financial condition and results of operations.



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We maintain a package of insurance coverage plan through Sinopec Group on our property, facilities and inventory. In addition, we maintain insurance policies for such assets as the engineering construction projects and products in transit with third-party's commercial insurance company. We do not carry any third party liability insurance to cover claims in respect of personal injury, property or environmental damage arising from accidents on our property or relating to our operations other than on our transportation vehicles. Our insurance coverage may not be sufficient to cover all the financial losses caused by the operating hazards. Resulting losses required to be compensated or otherwise paid by us due to such operating hazards that are not fully insured may have a material adverse effect on our financial condition and results of operations.

*Our business may be limited or adversely affected by government regulations.*

The Chinese central and local governments continue to exercise a certain degree of control over the petrochemical industry in China by, among other things:

mandating distribution channels for our fuel products;

setting allocations and pricing of certain resources, products and services;

assessing taxes and fees payable;

setting import and export quotas and procedures; and

setting safety, environmental and quality standards.

As a result, we may face significant constraints on our flexibility and ability to expand our business operations or to maximize our profitability. In addition, we have in the past benefited from favorable regulatory policies that have, for example, reduced the competition we face from illegal imports of petroleum products. Existing policies that favor our industry may change in the future and our business could be adversely affected by any such changes.

*Our development plans may require regulatory approval.*

We are currently engaged in a number of construction and expansion projects. Most of our projects are subject to governmental review and approval. The timing and cost of completion of these projects will depend on numerous factors, including approvals from relevant governmental authorities and general economic conditions in China.

While in general we attempt to obtain governmental approval as far in advance as practicable, we are unable to predict the timing and outcome of such governmental reviews and approvals. If any of our projects required for our future growth are not approved, or not approved on a timely basis, our results of operations and financial condition could be adversely affected.

*China's entry into the World Trade Organization, or WTO, may significantly increase foreign competition in our lines of business.*

China joined the WTO on December 11, 2001 and had committed to eliminate some tariff and non-tariff barriers to foreign competitions in the domestic petrochemical industry that benefited us in the past. In particular, China:

has reduced tariffs on imported petrochemical products that compete with ours;

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increased levels of permitted foreign investment in the domestic petrochemical industry, allowing foreign investors to own 100% of a domestic petrochemicals company from December 11, 2004;

has gradually relaxed restrictions on the import of crude oil by non-state owned companies;

has granted foreign-owned companies the right to import petrochemical products; and

has permitted foreign-owned companies to distribute and market fuel products in both retail and wholesale markets in China. As a result of these measures, we face increased competition from foreign companies and imports. In 2013, we expect the global financial crisis to continue to have a negative effect on the market for petrochemical products, and in turn our business. The petrochemical industry has experienced a slow recovery. In addition, competition for our products has increased, as many overseas companies have switched their focus to sales in China. In addition, tariff reductions could reduce our profit margins or otherwise negatively impact our revenue from certain products, including a small number of significant products. The Chinese government may also reduce the tariffs imposed on production equipment that we may import in the future.

*Political and economic policies in China could affect our business in unpredictable ways.*

The economy of China differs from the economies of most countries belonging to the Organization for Economic Co-operation and Development in a number of respects, including:

structure;

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level of government involvement;

level of development;

level of capital reinvestment;

control of foreign exchange; and

allocation of resources.

Before its adoption of reform and open-door policies beginning in 1978, China was primarily a planned economy. Since that time, the Chinese government has been reforming the Chinese economic system, and has also begun reforming the government structure. These reforms have resulted in significant economic growth and social progress. Although the Chinese government still owns a significant portion of the productive assets in China, economic reform policies since the late 1980s have emphasized autonomous enterprises and the utilization of market mechanisms. We expect that the Chinese government will continue these reforms, further reduce government intervention and rely more heavily on market mechanisms to allocate resources. Although we believe these reforms will have a positive effect on our overall long term development, we cannot predict whether changes to China's political, economic and social conditions, laws, regulations and policies will have any adverse effect on our current or future business or results of operations.

*If the Chinese government changes current regulations that allow us to make payments in foreign currencies, we may be unable to obtain the foreign currency necessary for our business.*

The Renminbi currently is not a freely convertible currency. We receive most of our revenue in Renminbi. A portion of our Renminbi revenue must be converted into other currencies to meet our foreign currency obligations. We have substantial requirements for foreign currencies, including:

debt service costs on foreign currency-denominated debt;

purchases of imported equipment;

payment of any cash dividends declared in respect of the H shares and the ADSs; and

import of crude oil and other materials.

Under existing foreign exchange regulations in China, we may undertake current account foreign exchange transactions, including the payment of dividends, without prior approval from the State Administration of Foreign Exchange (SAFE) by producing commercial documents evidencing the foreign exchange transactions, provided that they are processed through Chinese banks licensed to engage in foreign exchange transactions. The Chinese government has stated publicly that it intends to eventually make the Renminbi freely convertible. However, uncertainty exists as to whether the Chinese government may restrict access to foreign currency for current account transactions if foreign currency becomes scarce in China.

Foreign exchange transactions under the capital account (international revenues and expenditures that increase or decrease debt or equity, including principal payments in respect of foreign currency-denominated obligations) continue to be subject to limitations and require the prior approval of the SAFE. These limitations could affect our ability to obtain foreign exchange through debt financing, or to make capital expenditures in foreign currency.

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If the Chinese government restricts our ability to make payments in foreign currency, we may be unable to obtain the foreign currency necessary for our business. In that case, our business may be materially adversely affected, and we may default on our obligations.

*The change of currency policy and the fluctuation of Renminbi might adversely affect our business and operation results.*

The exchange rate between the Renminbi and the U.S. Dollar or other foreign currencies might fluctuate and be affected by the change in Chinese political and economic conditions. In July 2005, the Chinese government changed its policy of pegging the Renminbi to the U.S. Dollar. Under the new policy, the Renminbi is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. Since the adoption of this new policy, the value of the Renminbi has fluctuated daily within a narrow band against the U.S. Dollar. Nevertheless, the Chinese government continues to receive significant international pressures to further liberalize its currency policy which could result in China adjusting its currency policy further.

A small portion of our cash and cash equivalents is denominated in foreign currencies (including the U.S. Dollar). The appreciation in the value of Renminbi against foreign currencies (including the U.S. Dollar) may cause a decrease in the Renminbi value of our cash and cash equivalents that are denominated in foreign currencies. In addition, the appreciation of Renminbi may harm the exports of our downstream manufacturers, thus adversely affecting the market demand for our products.

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As most of our revenue is denominated in Renminbi, and most of our purchase of crude oil and some equipment and certain loan repayments are made in foreign currencies, any depreciation of the Renminbi would increase our cost and adversely affect our capacity of making profits. In addition, any depreciation of the Renminbi could adversely affect the value of the dividends of our H shares and ADSs, which we declare in Renminbi and pay in foreign currencies.

*The rejection of the proposed share reforms required of companies listed on the Shanghai Stock Exchange may adversely affect our market image and our ability to effectuate future transactions such as public offerings on the Shanghai Stock Exchange.*

Pursuant to regulations issued by the China Securities Regulatory Commission (the CSRC), we were required to obtain shareholder approval for and implement certain share reforms in 2006. Under the share reform plans proposed by holders of our non-circulating A Shares in October 2006 and December 2007, respectively, all non-circulating A Shares would be converted into circulating A Shares and may be sold publicly on the Shanghai Stock Exchange subject to any applicable lock-up period under the condition that holders of our non-circulating A Shares transfer a portion of their A Shares to holders of our circulating A Shares. However, holders of our circulating A Shares rejected both share reform plans for various reasons. We are uncertain as to when such share reforms will be completed. On January 8, 2007, the Shanghai Stock Exchange began to impose stricter regulations on its listed companies that are required but unable to complete the share reforms, including imposing a cap and a basket on the price fluctuation rate set at 5% daily, stricter trading information disclosure requirements that are similarly applicable to ST and \*ST shares and more restrictions on future financing abilities. Since March 26, 2007, the Shanghai Stock Exchange has required us to make public announcements periodically regarding the status of our share reforms. In addition, the CSRC is expected to impose stricter scrutiny on any securities-related applications filed by publicly listed PRC companies that are required to but have failed to complete such share reforms, their major shareholders and ultimate beneficial owners. The failure to complete the proposed share reforms may adversely affect our market image, the environment of our operation and our ability to effectuate future transactions such as public offerings on the Shanghai Stock Exchange. The possibility that the CSRC and the Shanghai Stock Exchange will impose more restrictions cannot be eliminated.

*Interpretation and enforcement of Chinese laws and regulations is uncertain.*

The Chinese legal system is based on statutory law. Under this system, prior court decisions may be cited as persuasive authority, but do not have the binding effect of precedents. Since 1979, the Chinese government has been developing a comprehensive system of commercial laws and considerable progress has been made in the promulgation of laws and regulations dealing with economic matters, such as corporate organization and governance, foreign investment, commerce, taxation and trade. Because these laws, regulations and legal requirements are relatively new and not all accessible to the public and because prior court decisions have little precedential value, the interpretation and enforcement of these laws, regulations and legal requirements involve greater uncertainty than in other jurisdictions.

*You may not enjoy shareholders' protections that you would be entitled to in other jurisdictions.*

As most of our business is conducted in China, our operations are governed principally by the laws of China. Despite the ceaseless improvement of the PRC Company Law and Securities Law, Chinese legal provisions for the protection of shareholders' rights and access to information are different from those applicable to companies formed in the United States, Hong Kong, the United Kingdom and other developed countries or regions. You may not enjoy shareholders' protections under Chinese law that you would be entitled to in other jurisdictions.

*Our Articles of Association require you to submit your disputes with us and other persons defined by our Articles of Associations regarding the Company's affairs to arbitration. You will have no legal right to a court proceeding.*

Our Articles of Association require holders of our H shares or ADSs having a claim against, or a dispute with, us, our directors, supervisors, executive officers or a holder of our domestic shares relating to any rights or obligations conferred or imposed by our Articles of Association, the Chinese Company Law or other relevant Chinese laws or regulations relating to our affairs, to submit such claim or dispute to arbitration with the China International Economic and Trade Arbitration Commission or to the Hong Kong International Arbitration Center. Our Articles of Association further provide that any arbitration decisions with respect to such disputes or claims shall be final and binding on all parties. As a result, you will have no legal right to a court proceeding.

*Currently, United States financial regulatory and law enforcement agencies, including but not limited to the SEC, PCAOB, U.S. Department of Justice and NYSE, have limited or may have no ability to conduct investigations within the PRC concerning the Company, its officers, directors, auditors, market research services or other professional services or experts based in the PRC.*





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The Company's operations and assets are physically located in the PRC. The PRC has limited or no agreements in place to facilitate cooperation with the SEC Division of Enforcement and other U.S. regulatory agencies charged with protecting investors for investigations within its jurisdiction. This may result in U.S. financial regulators, including but not limited to the SEC, the Public Company Accounting Oversight Board ( PCAOB ) and the U.S. Department of Justice, having limited access to the Company's books, records, testimony, on-site investigations of operations, subpoena power and other investigative actions, including those stemming from investor tips, complaints and referrals. Such limitations may result in the Company's investors receiving less protection from U.S. regulators than investors in companies operating in other jurisdictions because the Company and its service providers, particularly its auditors, are subject to less scrutiny than companies and service providers that are subject to regular investigations and inspections by U.S. regulators. For example, the PCAOB is currently unable to conduct independent regulatory inspections of PCAOB-registered firms' audit work related to a company's operations in China where the documentation of the audit work is located in China. As a result, our investors may be deprived of the benefits of the PCAOB's oversight of our independent registered public accounting firm through such inspections.

*We may be or become a passive foreign investment company, which could result in adverse U.S. federal income tax consequences to U.S. investors.*

We may be classified as a passive foreign investment company ( PFIC ) by the U.S. Internal Revenue Service ( IRS ) for U.S. federal income tax purposes. Such characterization could result in adverse U.S. federal income tax consequences to you if you are a U.S. investor. For example, U.S. investors who owned our H Shares or ADSs during any taxable year in which we were a PFIC generally are subject to increased U.S. tax liabilities and reporting requirements for that taxable year and all succeeding years, regardless of whether we actually continue to be a PFIC, although a shareholder election to terminate such deemed PFIC status may be available in certain circumstances. We do not intend to provide information to permit you to make a qualified electing fund election to avoid the adverse U.S. tax consequences described above. The same adverse U.S. federal income tax consequences will apply to U.S. investors who acquire our H Shares or ADSs during the current taxable year or any subsequent taxable year if we are treated as a PFIC for that taxable year.

The determination of whether or not we are a PFIC is made on an annual basis and depends on the composition of our income and assets, from time to time. Specifically, we will be classified as a PFIC for U.S. tax purposes for a taxable year if either (a) 75% or more of our gross income for such taxable year is passive income, or (b) 50% or more of the average percentage of our assets during such taxable year either produce passive income or are held for the production of passive income. For such purposes, if we directly or indirectly own 25% or more of the shares of another corporation, we generally will be treated as if we (a) held directly a proportionate share of the other corporation's assets, and (b) received directly a proportionate share of the other corporation's income.

We do not believe that we are currently a PFIC. However, because the PFIC determination is highly fact intensive and made at the end of each taxable year, there can be no assurance that we will not be a PFIC for the current or any future taxable year or that the IRS will not challenge our determination concerning our PFIC status. For further discussion of the adverse U.S. federal income tax consequences of our possible classification as a PFIC, see Item 10. Additional Information E. Taxation U.S. Taxation.

*We have in the past sourced a small portion of crude oil from Iran that may be targeted by economic sanctions under relevant U.S. laws, and if such activities are determined by the U.S. governmental authorities as sanctionable activities, we could be sanctioned or otherwise penalized.*

The United States has adopted a number of measures since 1996 that provide for the possible imposition of sanctions against non-U.S. companies engaged in certain activities in and with Iran in the energy sector, including the Executive Order 13622 issued on July 30, 2012 and the Iran Threat Reduction and Syria Human Rights Act of 2012 ( ITRSHRA ) issued on August 10, 2012. The sanctionable activities include certain investments, the provision of goods, services, technology, or support that could contribute to the development of petroleum and petrochemical resources or the production of refined petroleum products in Iran, the exportation of refined petroleum products to Iran, the transportation of crude oil from Iran, or the engagement in a significant transaction for the purchase or acquisition of petroleum or petroleum products from Iran.

We have sourced a small portion of our crude oil from Iran in the past through a wholly-owned subsidiary of Sinopec Corp., our controlling shareholder, and we may continue to purchase crude oil from Iran. In addition, Sinopec Corp., our current controlling shareholder, and Sinopec Group, the controlling shareholder of Sinopec Corp., have engaged in operations in or purchasing crude oil sourced from Iran and may continue to do so in the future. Furthermore, we have no control over the activities of Sinopec Group or Sinopec Corp. in connection with any activities that they may conduct in Iran.

If our purchases of crude oil from Iran are determined to be sanctionable activities by the U.S. President and/or the relevant U.S. governmental authorities, we may be subject to one or more of the twelve sanctions options available under the Iran Sanctions Act of 1996 (as amended) and the ITRSHRA, which include restrictions on bank financing, outright blocking of the Company's property within U.S. jurisdiction and prohibition of U.S. persons from investing or purchasing a significant amount of equity or debt instruments of the Company. In addition, many

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states in the United States have adopted legislation requiring state pension funds to divest themselves of securities in any company with active business operations in Iran. We cannot assure that we or any of our affiliates will not be sanctioned by the U.S. President and/or the relevant U.S. governmental authorities in light of the activities by us or our affiliates in Iran. The imposition of any such sanctions on us or our affiliates will have a negative impact on our business, reputation or stock price.

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*Sinopec Group, the controlling shareholder of Sinopec Corp. which is our current controlling shareholder, or its affiliates' current or future activities in certain countries are the subject of economic sanctions under relevant U.S. laws and could result in negative media and investor attention to us and possible imposition of sanctions on Sinopec Group, which could materially and adversely affect our shareholders*

Sinopec Group undertakes, from time to time and without our involvement, overseas investments and operations in the oil and gas industry, including the exploration and production of oil and gas, refining and Liquefied Natural Gas, or LNG, projects. Sinopec Group's overseas asset portfolio includes oil and gas development projects in Iran, Sudan and Syria, which countries are on the sanction list published and administered by the U.S. Department of the Treasury's Office of Foreign Assets Control, or OFAC. We cannot predict the interpretation or implementation of government policy at the U.S. federal, state or local levels with respect to any current or future activities by Sinopec Group or its affiliates in countries or with individuals or entities that are the subject of U.S. sanctions. Similarly, we cannot predict whether U.S. sanctions will be further tightened, or the impact that such actions may have on Sinopec Group. It is possible that the United States could subject Sinopec Group to sanctions due to these activities. Certain U.S. state and local governments and colleges have restrictions on the investment of public funds or endowment funds, respectively, in companies that are members of corporate groups with activities in certain countries that are the subject of U.S. sanctions. These investors may not wish to invest, and may divest their investment, in us because of our relationship with Sinopec Group and its investments and activities in those OFAC sanctioned countries. It is possible that, as a result of activities by Sinopec Group or its affiliates in countries that are the subject of U.S. sanctions, we may be subject to negative media or investor attention, which may distract management, consume internal resources and affect investors' perception of our company.

Further, the Iran Sanctions Act of 1996 (as amended) authorizes the imposition of sanctions on companies that engage in certain activities in and with Iran, especially in Iran's energy sector. It is possible that Sinopec Group or its affiliates engage in activities that are targeted for sanction purposes by ISA. It is possible that the U.S. government would determine, and in the event that the U.S. government so determines, that Sinopec Group, or an entity it owns or controls, had engaged in any such activities and if the most extreme sanction under the ISA, blocking, were applied to Sinopec Group's property, including controlled subsidiaries, Sinopec Group could be prohibited from engaging in business activities in the United States or with U.S. individuals or entities, and U.S. transactions in our securities and distributions to U.S. individuals and entities with respect to our securities could also be prohibited.

## **ITEM 4. INFORMATION ON THE COMPANY.**

### ***A. History and Development of the Company***

#### *General Information*

We were established in the People's Republic of China as a joint stock limited company under the Chinese Company Law on June 29, 1993 as Shanghai Petrochemical Company Limited. On October 12, 2000, we changed our name to Sinopec Shanghai Petrochemical Company Limited. Our registered office is at No. 48 Jinyi Road, Jinshan District, Shanghai, China 200540. Our telephone number there is (86-21) 5794-1941.

#### *Our Predecessor*

Our predecessor, Shanghai Petrochemical Complex (the "Complex"), was founded in 1972 as one of the first large scale Chinese petrochemical enterprises using advanced imported technology and equipment. Prior to June 29, 1993, the Complex was wholly-owned by Sinopec Group, at the time a ministerial level enterprise (before its restructuring in 1998, Sinopec). The Complex's location was chosen because of accessibility by water and land transportation to Shanghai, a major industrial city of China, and the availability of reclaimable land. The Complex was initially under the administration of the Ministry of Textile Industry and in 1983 was placed under the administration of Sinopec.

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### ***Construction Projects***

The Complex and we, as its successor, have completed five major stages of construction. The first stage of construction (1972-1976) included reclamation of land and the installation of 18 production units. The second stage of construction (1980-1986) increased the Complex's capacity for processing crude oil and doubled its capacity for synthetic fiber production. The third stage of construction (1987-1992) primarily consisted of the installation of a 300,000 ton Rated Capacity ethylene unit, an additional crude oil refining unit and other units for the production of petrochemical products. The third stage of construction completed our transition from a synthetic fiber producer to a highly integrated producer of a wide variety of petrochemical products. The fourth stage of construction (2000-2002) mainly included the 700,000 ton Ethylene Expansion Project and Coal-Fired Power Plant Expansion Project. The fifth stage of construction (2003-2009) was mainly designed to optimize our structure and realize sustainable development, and mainly included 3,300,000t/a diesel hydrogenation unit, 1,200,000t/a delayed coking unit and other projects implemented for removing bottlenecks in refinery, the building of new 600,000t/a PX hydrocarbon complex unit, 150,000t/a C5 segregation unit, 380,000t/a ethane unit, etc.

The Company commenced the sixth stage of construction in 2010 ( Phase 6 Project ) and completed in December 2012. The purpose of the Phase 6 Project was to improve the Company's overall industrial structure and core competitiveness and its capability of maintaining sustainable developments. The Phase 6 Project focused on utilizing intensively natural resources and forming a complete set of facilities in accordance with the fundamental industrial model of integrating oil refining and petrochemical. It was expected to further achieve the reform of oil refining and to strengthen and expand the Company's core business while continuing to explore the development of fine chemicals and products with high added value. Phase 6 Project consisted of refining capacity expansion projects, technology development and fine chemicals projects, see [Item 4. Information on the Company – D. Property, Plant and Equipment – Capital Expansion Program](#).

Over the past 39 years, the Company has established its own infrastructure system to support its production needs. The Company has its own facilities to supply water, electricity, steam and other utilities and to treat waste water, as well as ocean and inland waterway wharfs and railroad and road transportation facilities.

### ***Our Initial Public Offering and Listing***

We were established as a subsidiary of Sinopec on June 29, 1993. In preparation for our initial public offering of ordinary shares, all assets and liabilities of the Complex were transferred either to us or to Sinopec Shanghai Jinshan Industrial Company ( JI ), a separate subsidiary of Sinopec. The Complex's non-core businesses and assets, such as housing, stores, schools, transportation and medical services were transferred to JI. The Complex's core business and assets was transferred to us. The Complex then ceased to exist as a legal entity. In 1998, Sinopec was restructured into a limited liability company under the name of China Petrochemical Corporation ( Sinopec Group ). On February 25, 2000, Sinopec Group transferred its interest in us to its subsidiary, Sinopec Corp. In 1997, JI was restructured and its subsidiaries were either transferred to Sinopec or Shanghai Jinshan District. Sinopec Group now provides community services to us that were formerly provided by JI.

Our H Shares were listed on the HKSE on July 26, 1993. Our ADSs, each representing 100 H Shares, are listed on the New York Stock Exchange ( NYSE ). Our A Shares are listed on the Shanghai Stock Exchange. We were the first Chinese joint stock limited company to have securities concurrently traded in Hong Kong, the United States and China. On November 8, 1993, our A Shares were included in the Shanghai Stock Exchange Stock Index.

### ***Description of Principal Capital Expenditures and Divestitures***

In the fourth quarter of 2001, we established Secco, together with BP Chemicals East China Investments Limited ( BP ) and Sinopec Corp. We own 20%, while BP and Sinopec Corp. own 50% and 30% of the equity interest of Secco, respectively. Secco was established to build and operate a 900,000 ton Rated Capacity ethylene petrochemical manufacturing facility in order to manufacture and market ethylene, polyethylene, styrene, polystyrene, propylene, acrylonitrile, polypropylene, butadiene, aromatics and by-products; provide related after-sales services and technical advice with respect to such petrochemical products and by products; and engage in polymers application development. Secco completed construction in 2005. Secco's registered capital is U.S.\$901,440,964 of which we were obligated to contribute an amount in Renminbi equivalent to U.S.\$180,287,952 prior to the end of 2005. As of December 31, 2005, we had contributed such amount in full. For a description of capital expansion projects related to our facilities, see [Item 4. Information on the Company – D. Property, Plant and Equipment – Capital Expansion Program](#).

### ***B. Business Overview***

We are one of the largest petrochemical companies in China based on 2012 net sales and ethylene production. Our highly integrated petrochemical complex processes crude oil into a broad range of products in four major product areas:

synthetic fibers,

resins and plastics,

intermediate petrochemicals, and

petroleum products.

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Based on 2012 sales volumes, we are a leading Chinese producer of synthetic fibers and resins and plastic products. We believe that we are also a leading competitor in sales of petroleum products and intermediate petrochemicals in our regional markets.

Our net sales by business lines as a percentage of total net sales in each of 2010, 2011 and 2012 are summarized as follows:

**Net Sales of RMB72,095.9 million in 2010**

Synthetic fibers	5.42%
Resins and plastics	20.67%
Intermediate petrochemicals	23.87%
Petroleum products	39.86%
Trading of petrochemical products	9.11%
Others	1.07%
<b>Total</b>	<b>100.00%</b>

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Synthetic fibers	4.64%
Resins and plastics	18.34%
Intermediate petrochemicals	21.25%
Petroleum products	41.73%
Trading of petrochemical products	12.98%
Others	1.06%
<b>Total</b>	<b>100.00%</b>

**Net Sales of RMB87,217.3 million in 2012**

Synthetic fibers	3.80%
Resins and plastics	16.86%
Intermediate petrochemicals	20.63%
Petroleum products	43.92%
Trading of petrochemical products	13.78%
Others	1.01%
<b>Total</b>	<b>100.00%</b>

We derive a substantial portion of our revenues from customers in Eastern China (comprising Shanghai and its six neighboring provinces), an area that has experienced economic growth above the national average in recent years. We believe that we are well-positioned to take advantage of opportunities which may arise through the economic growth of China generally and in this area in particular. Shown by geographic region and exports, our net sales by business lines as a percentage of total net sales for each of 2010, 2011 and 2012 are as follows:

**2010 Net Sales by Region (%)**

	Eastern China	Other parts of China	Exports
Synthetic fibers	85.05	14.08	0.87
Resins and plastics	87.20	12.80	0
Intermediate petrochemicals	83.07	14.08	2.85
Petroleum products	99.55	0.45	0
Trading of petrochemical products	88.90	0.36	10.74
Total net sales	92.32	7.01	0.67

**2011 Net Sales by Region (%)**

	Eastern China	Other parts of China	Exports
Synthetic fibers	83.27	16.20	0.53
Resins and plastics	87.77	12.22	0.01
Intermediate petrochemicals	85.68	12.44	1.88
Petroleum products	99.70	0.30	0
Trading of petrochemical products	89.43	0.79	9.78
Total net sales	93.25	6.32	0.43





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	Eastern China	Other parts of China	Exports
Synthetic fibers	84.61	14.83	0.56
Resins and plastics	86.50	13.50	0
Intermediate petrochemicals	89.32	9.31	1.37
Petroleum products	97.94	2.06	0
Trading of petrochemical products	92.54	0.58	6.88
Total net sales	94.18	4.68	1.14

**Business Strategy**

In 2013, we aim to develop the Company into a leading oil refining petrochemical enterprise. We will continue to focus on the improvement of quality and efficiency of developments, the adjustment of structure, the furtherance of reform and the improvement of management. We will proactively work on our underlying competitiveness, production and operation competence, management capabilities, research and development strength, the team of employees and the improvement of environment. We strive to utilize our advantages deriving from the launching of the Refinery Revamping and Expansion Project and the technological advancement programs and improve our economic returns.

To achieve its business objectives in 2013, the Company plans to carry out tasks in the following areas:

(a) Strengthening management of safety and environmental protection and promoting safe, green and low carbon development.

The Company will implement a green and low-carbon development strategy to further improve safety management and environmental protection. This includes diversifying safety management measures, actively launching safety competitions, and strengthening the grid management at construction sites, health, safety and environment ( HSE ) supervision and management during the direct operation process, the emergency response management and HSE supervision over outsourcing contractors. The Company will take greater efforts and establish a long-term mechanism to protect the environment. In addition, we will further and expand deodorizing programs in the manufacturing sites, continue to decrease the disposal of solid wastes, enhance the emergency response management with regard to the protection of water resources, the prevention and control of air pollution and the improvement of air quality, and get prepared for the measurement of carbon emissions.

(b) Enhancing plant operation capacity to ensure a safe, stable, long-cycle and full capacity operation of the plants.

The Company will bring in advanced management concepts in order to improve the plant operation management. We will strengthen the management of plant operation and manage to run well the newly built plants of Phase 6 Project. We will improve the organization and coordination of major production operations, and continue to organize special competitions for a safe, stable, long-cycle and full capacity operation among the production units. Furthermore, we will implement the unified management on the dispatch of production, electrical power and thermal power. In order to increase the Company's energy resources utilization efficiency, we will promote the energy conservation and the reduction of feedstock consumption, finish power balance tests on 20 integrated units and implement energy performance contracting. We will also improve our comprehensive capability for equipment management, implement plans for the long-cycle operation of the plants and strengthen the management of scheduled inspection and repair so as to lead the safe, stable, long-cycle, full capacity and good operation of the plants to a higher level.

(c) Further optimizing production operation and realizing the potential of economic returns.

The Company will closely monitor the market, optimize business operation and endeavor to utilize the advantage deriving from the integrated refining and chemical operation in order to improve the operational capability. We will improve the oil price trend analysis and increase the extent of centralization in terms of crude oil procurement in order to optimize the crude oil procurement and increase the economic return and we plan to fully utilize the facilities' potential capacities. With regard to the optimization of intermediate raw materials and our product mix, we will endeavor to achieve the optimized selection of raw materials, optimize the balance of materials and the adjustment of refined oil structure and increase the output of products, which will create economic returns. With regard to the sales, we will optimize the sales strategies and the material supply model, and endeavor to increase the market share of Shanghai IV refined oil products. Efforts will be made with respect to the sale of new products and the construction of a logistics line which allows delivery within 2 to 3 hours. We will also implement the low inventory strategy. As to the cost control, we will continue to leverage off the launching of the Refinery Revamping and Expansion Project and the optimization of the refinery and chemical system, implement various measures to decrease costs and fees, further emphasize the cost management among employees, and strictly control the expenditures. We will also establish a scientific and efficient strategy regarding

equipment repair and reduce the unreasonable inspection and repair expenses. Furthermore, we will strengthen the capital management and optimize the use of capital.

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(d) Pushing forward technological advancement and informationization in order to support future growth.

The Company will continue to explore a technological innovation system featured by a combination of production and study as well as research and utilization in order to accelerate the informationization progress and improve technologies. With regard to the further development of new products and technologies, we will speed up the technological breakthrough for a new carbon fiber, launch a pilot project with a capacity of 1,000 tons for norbornene/ethylidene norbornene and hydrogenated petroleum resins, and push forward the development and utilization of new environmental protection technologies. Efforts will be made to improve the marketing and stable expansion of production of new products, including specialized materials for binary random copolymer, fire-retardant polyester series, NEP polyester chips, gel dyed acrylic and precursor liquid coloring acrylic. As parts of our efforts to push forward the informationization progress, we will launch APC systems for various plants such as those for online blending of diesel, aromatics complex, CDU and EO/EG plant, and the construction of process simulation systems for various plants, such as No. 3 diesel hydrogenation plant and butadiene plant. We aim to establish a production and operation monitoring and analysis system in order to enhance our utilization of information systems.

(e) Strengthening corporate management and improving scientific management skill.

In order to improve the scientific management skill, the Company will specify measures to be taken to fulfill each working assignment, establish a working system for the benchmarking management, and standardize the process management. We will increase the operational level of our integrated management system so as to promote the standardized operation. As parts of our efforts to enhance the effect of performance tests, we will establish and improve a goal oriented performance test system, adequately exert the orientation and incentive effect of performance tests and improve the correlation between the organizational performance and individual employee performance.

(f) Strengthening team building and creating a stable and harmonious environment for developments.

In order to build a first-class workforce, we will carry out the medium and long-term human resources planning, improve the setup of channels catering to the growth of various types of competent staff from time to time, and improve the staff training and the optimization of human resources. As parts of our efforts to create a great environment for developments, we will further refine and enrich the essence of our company's culture, actively cultivate our company's core values, take care for the staff's welfare and livelihood and push forward the healthy, stable and harmonious development of the Company.

*Principal Products*

We produce four principal types of products with different specifications, including synthetic fibers, resins and plastics, intermediate petrochemicals and petroleum products. We use many of the important petroleum products and intermediate petrochemicals we produce in producing our own downstream products.

In 2012, the volume of our physical production remained stable, with a total volume of products amounting to 11,844,100 tons, representing a decrease of 1.31% over the previous year. The Company processed 11,193,500 tons of crude oil (including 563,000 tons of crude oil processed on a sub-contract basis), representing an increase of 3.01%. Total production output of refined oil, including gasoline, diesel and jet fuel was 5,878,800 tons, representing an increase of 2.32%, among which the Company produced 1,020,300 tons of gasoline, 4,027,900 tons of diesel and 830,600 tons of jet fuel, representing an increase of 5.35%, 1.21% and 4.18%, respectively. The Company produced 914,700 tons of ethylene and 504,400 tons of propylene, representing an increase of 0.51% and 4.71%, respectively. The Company produced 866,200 tons of paraxylene, representing a decrease of 6.16%. The Company also produced 1,087,500 tons of synthetic resins and copolymers (excluding polyesters and polyvinyl alcohol), representing a decrease of 0.95%; 1,015,600 tons of synthetic fiber monomers, representing an increase of 7.33%; 636,100 tons of synthetic fiber polymers, representing a decrease of 4.23%; and 251,600 tons of synthetic fibers, representing an increase of 0.64%. We continue to produce premium products of a stable quality.

The following table shows our 2012 net sales by major products as a percentage of total net sales together with the typical uses of these products.

Product	% of net sales	Typical Use
<b>SYNTHETIC FIBERS</b>		
Polyester staple fiber	0.72%	Textiles and apparel
Acrylic staple fiber	2.84%	Woven into fabrics or blended with other material fabrics to make fabric or acrylic top
Others	0.24%	

<b>Sub-total</b>	3.80%	
<b>RESINS AND PLASTICS</b>		
Polyester chips	4.81%	Polyester fibers, films and containers
PE pellets	6.42%	Films, ground sheeting, wire and cable compound and other injection molding products such as housewares and toys

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<b>Product</b>	<b>% of net sales</b>	
PP pellets	4.93%	Extruded films or sheets, injection molded products such as housewares, toys and household electric appliance and automobile parts
PVA	0.45%	PVA fibers, building coating materials and textile starch
Others	0.25%	
<b>Sub-total</b>	<b>16.86%</b>	
<b>INTERMEDIATE PETROCHEMICALS</b>		
Ethylene	1.06%	Feedstock for polyethylene, EG, PVC and other intermediate petrochemicals which can be further processed into resins, plastics and synthetic fiber.
Ethylene oxide	1.73%	Intermediate for chemical and pharmaceutical industry, dyes, detergents and auxiliary agents
Benzene	3.33%	Intermediate petrochemical products, styrene, plastics, explosives, dyes, detergents, epoxies and nylon
Paraxylene	6.64%	Intermediate petrochemicals and polyester
Butadiene	2.44%	Synthetic rubber and plastics
Ethylene glycol	2.16%	Fine chemicals
Others	3.27%	
<b>Sub-total</b>	<b>20.63%</b>	
<b>PETROLEUM PRODUCTS</b>		
Gasoline	7.95%	Transportation fuels
Diesel	24.95%	Transportation fuels and agricultural fuels
Jet Fuel	4.05%	Transportation fuels
Others	6.97%	
<b>Sub-total</b>	<b>43.92%</b>	
<b>TRADING OF PETROCHEMICAL PRODUCTS</b>		
	13.78%	
<b>OTHERS</b>		
	1.01%	
<b>Total</b>	<b>100.00%</b>	

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*Production Processes*

The key sectors in our vertically integrated production plants are the ethylene units which produce ethylene and propylene, and our aromatics plants which principally produce paraxylene ( PX ) and benzene. Ethylene is a major raw material in the production of polyethylene ( PE ) and monoethylene glycol ( MEG ) which, together with pure terephthalic acid ( PTA ), is used to manufacture polyester. Propylene is a major raw material in the production of acrylonitrile and polypropylene ( PP ). These products are produced through the processing of a series of petrochemical units from crude oil. Our production processes are shown in the flow chart below.

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Our refinery units refine crude oil into five basic components: (1) naphtha, (2) kerosene, (3) atmospheric gas oil ( AGO ), (4) VGO, and (5) residual oil. Part of the Naphtha and part of the AGO is fed to the ethylene units primarily to produce ethylene and propylene. Part of the Naphtha is fed to the reforming prehydrogenation units to produce refined Naphtha which shall be used for the production of Aromatics. The other part of the AGO is processed into diesel oil, and kerosene is fed to the jet fuel sweetening unit to produce jet fuel. Part of the VGO is further processed in a hydrocracking unit producing mainly light and heavy naphtha, liquefied petroleum gas ( LPG ), diesel oil, various aromatic hydrocarbon products and jet fuel. The other part of the VGO and residual oil can be further processed into gasoline, diesel oil, LPG, propylene and other products.

### ***Intermediate Petrochemicals***

**Ethylene** Ethylene is either directly processed into PE resins or processed into other intermediate petrochemicals. The most important of these is MEG. MEG is a key ingredient in polyester. It is produced by oxidizing ethylene in the ethylene oxide ( EO )/ethylene glycol ( EG ) unit. Ethylene is also used to produce vinyl acetate which is processed into PVA.

**Propylene** Propylene is either processed directly into PP resins or is further processed into other intermediate petrochemicals such as acrylonitrile, acetonitrile, hydroxyl acetonitrile and sodium cyanide. Acrylonitrile is used in producing acrylics.

**Vacuum gas oil** VGO is passed through the hydrocracker, and the resulting heavy naphtha is fed into the aromatics plants to produce PX and benzene. PX is processed into PTA, one of the principal raw materials in producing polyester.

### ***Resins and Plastics and Synthetic Fibers***

We process our intermediate petrochemical products into five kinds of synthetic fiber raw materials: (1) polyester, (2) acrylonitrile, (3) PP, (4) PE and (5) PVA. Each of these five products has its own production line or lines. We further process polyester and acrylonitrile into various types of synthetic fibers.

**Polyester** MEG and PTA are fed into a polymerization unit which produces polyester chips and polyester melt. Both chips and melt are used as raw materials in the production of polyester staple and filaments. Some chips are also sold to third parties.

Polyester staple fiber is a multi-strand fiber cut into short lengths which can be spun into fabric on its own or blended with cotton, wool or flax to produce textiles. Polyester filaments are a class of more highly processed polyester materials which have been drawn and oriented to produce a long thread-like fiber.

**Acrylonitrile** We produce polyacrylonitrile by feeding acrylonitrile into a polymerization unit. By passing the polyacrylonitrile through the fiber unit, acrylic fiber and acrylic staple fiber are produced, including cotton and wool type staple fibers. Wool acrylic staple fiber can be processed into acrylic wool strips.

**Polypropylene** We produce PP resins by feeding propylene into a polymerization unit. Our fiber grade PP resin is the main ingredient for PP fiber production.

**Polyethylene** We have three sets of units producing PE, two of which produce LDPE using the kettle type process, and the other unit produces all density PE products using the Borstar bimodal process.

**Polyvinyl acetate** PVA granules are produced from vinyl acetate ( VAC ), derived from ethylene.

### ***Raw Materials***

We optimized the composition of crude oil resources with the establishment of a mechanism for measuring crude oil optimization level. Furthermore, we optimized the raw materials of ethylene, aromatic and the composition of raw materials and fuels for the production of hydrogen. The cost of raw materials was reduced and the utilization rate of resources was increased. The Company realized a value of RMB690 million due to these arrangements.

### ***Crude Oil***

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Crude oil is our primary raw material and the most significant raw material we purchase from outside sources. In 2012, crude oil accounted for approximately 62.67% of our total cost of sales. Accordingly, the supply and price of crude oil are key factors in determining our profitability.

*Supply and Transportation* All crude oil required by us, whether from domestic or foreign sources, is purchased through the channels of Sinopec Corp. as an agent. During 2012, we did not experience any significant problems in obtaining sufficient crude oil to meet our production needs.

Sinopec Group is responsible for preparing an annual plan on demand and supply for crude oil and petroleum products that forms the basis of the Chinese government's annual balancing plan which effectively dictates our planned volume of crude oil processing in each year. Likewise, under the balancing plan, some of our petroleum products are designated for sale to the subsidiaries of Sinopec Group or other designated customers at market prices and we must consult with Sinopec Group in order to sell elsewhere.

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We have received confirmation from Sinopec Corp. that it will purchase on our behalf 15.5 million tons of imported crude oil and nil tons of domestic offshore crude oil in 2013. Sinopec Corp. has further confirmed that, subject to China's national crude oil policy and our actual production needs, it will continue to purchase on our behalf sufficient quantities and appropriate kinds of crude oil, including domestic offshore and imported crude oil, to satisfy our anticipated annual needs. We anticipate fully utilizing our 2013 supply of crude oil. We believe that the mix of crude oil feedstocks currently available is sufficient for our 2013 production capacity and targets. Additionally, as part of China's commitment at its accession into WTO, certain non-state-owned enterprises have been granted an increasing quota to import crude oil. Although we do not expect to obtain crude oil through this channel in the foreseeable future due to the current crude oil supply system, this may provide us with an alternative source of crude oil supply.

*Crude Oil Mix* Our refining equipment is designed to process certain grades of crude oil. Therefore, the origin and quality of the crude oil available can be important to our business. We believe, as we are significantly increasing usage of imported crude oil, we will continue to be able to obtain from the market such imported crude oil that is compatible with our refining equipment. The overall mix of foreign versus domestic crude oil we process in 2013 will depend on a variety of factors, including the amount of future supply of domestic offshore crude oil and the availability, price, quality, processing profitability and compatibility with our refining capabilities of imported crude oil. Provided there are no significant modifications to the existing channels of crude oil acquisition, we believe that sufficient supplies of crude oil will be available on the domestic or international markets for our 2013 production capacity and goals.

In 2012, our crude oil was sourced as follows:

Domestic offshore crude oil	2.89%
Imported crude oil	97.11%
<b>Total:</b>	<b>100.00%</b>

As a result of a consistent decrease in the supply of domestic crude oil, we expect that we will continue to rely principally on foreign sources for our crude oil supply. However, we believe that we will be able to maintain our processing efficiency through technological adjustments of our equipment and quality control, and that our increased use of imported crude oil will not materially and adversely impact our business and results of operations.

Foreign and domestic offshore crude oil is supplied by tanker and pipeline to our oil terminal wharf and oil storage tank. See [Item 4.D. Property, Plants and Equipment -Wharfs](#).

In the past, we have not experienced disruption in our crude oil supply. We have on-site crude oil storage tanks at Chenshan wharf capable of storing approximately 300,000 cubic meters of crude oil, primarily to provide crude oil to our No. 2 atmosphere vacuum distillation facility. This crude oil storage can provide us with approximately a 2-week supply of crude oil. The crude oil for our No. 3 atmosphere vacuum distillation facility is mainly supplied from the Ningbo-Shanghai-Nanjing oil pipeline. Due to our ability to obtain crude oil from multiple sources, we are able to meet our normal requirements for crude oil.

*Pricing* The price of domestic offshore crude oil is controlled by China National Offshore Oil Corporation ( CNOOC ) and Sinopec Group based on government pricing policies and by reference to the price of crude oil of the same quality in the international market, while imported crude oil is generally sold to us at prevailing international market prices. The average cost of imported crude oil and domestic offshore crude oil in 2012 was RMB5,228.58 (U.S.\$839.24) per ton and RMB5,090.85 (U.S.\$817.14) per ton, respectively. In 2012, we processed 10,869,500 tons of imported crude oil and 324,000 tons of domestic offshore crude oil (including 563,000 tons of crude oil processed on a sub-contract basis).

Until March 2001 the Chinese government implemented a unified pricing system for crude oil. Each month, the National Development and Reform Commission ( NDRC ) would establish an indicative price for each grade of domestic onshore crude oil based on comparable international market prices, inclusive of any duties that would have been imposed had the oil been imported. The actual price for domestic onshore oil would be such indicative price plus a surcharge. This surcharge was determined by China National Petroleum Corporation ( CNPC ) and Sinopec Group to reflect any transportation and other miscellaneous costs that would have been incurred in having the oil delivered to various refineries. Beginning March 2001, the NDRC ceased publishing such indicative price. Instead, the indicative price for domestic onshore oil is calculated and determined directly by CNPC and Sinopec Group based on the principles and methods formerly applied by the NDRC.

On March 26, 2013, the NDRC announced adjustments to the existing refined oil pricing mechanism, which include, among other things, (i) shortening of price reference period from 22 working days to 10 working days; (ii) lifting the 4% downward and upward fluctuation cap on

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benchmark crude oil prices; (iii) adjusting the composition of domestic benchmark crude oil types in response to changes of types of imported crude oil and crude oil trading in the overseas market. In the cases of changes such as significant increase in domestic prices or significant fluctuations of crude oil price, NDRC may issue additional procedural guidelines, such as implementing ad hoc suspension or delay of price adjustment upon approval by the State Council.

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We purchase crude oil through Sinopec Corp. and its affiliates in sources selected and quantities confirmed by the Company at market prices. On this basis, we believe that changes in crude oil prices should not have a material effect on our competitiveness with other domestic producers. Nevertheless, any increase in the price of crude oil could have an adverse impact on our profitability to the extent that we are unable to pass cost increases on to our customers.

Changes in crude oil prices can affect the Company's profitability. In 2012, international crude oil prices fluctuated at a high level, primarily due to geopolitical risks in the Middle East, the European and US macroeconomic outlook and the occurrence of material changes to the demand and supply of US crude oil, and . In 2012, the price of West Texas Intermediate ( WTI ) crude oil on the New York Mercantile Exchange fluctuated within a broad range of U.S.\$77-U.S.\$109/barrel (U.S.\$75-U.S.\$114/barrel in 2011), with peak and the bottom closing prices of U.S.\$109.77/barrel and U.S.\$77.69/barrel, respectively (U.S.\$113.93/barrel and U.S.\$75.67/barrel, respectively in 2011), for the year. The peak and the bottom closing prices of Brent crude oil futures on the London Intercontinental Exchange were U.S.\$126.22/barrel and U.S.\$89.23/barrel, respectively (U.S.\$126.64/barrel and U.S.\$93.33/barrel, respectively in 2011), for the year. In 2012, the average price of WTI crude oil on the New York Mercantile Exchange was U.S.\$94.145/barrel, an decrease of U.S.\$0.969 or 1% from U.S.\$95.114 in 2011; the average price of Brent crude oil on the London Intercontinental Exchange was U.S.\$111.673/barrel, an increase of U.S.\$0.761, or 0.7% from U.S.\$110.95 in 2011; and the average price of a package of OPEC oil was U.S.\$109.461/barrel, an increase of 1.9% compared to the daily average price of U.S.\$107.47 in 2011, reaching a record high. In 2012, we processed 11,193,500 tons of crude oil (including 563,000 tons of crude oil processed on a sub-contract basis), representing an increase of 326,800 tons over the previous year or 3.01%. The volumes of imported crude oil and domestic offshore crude oil processed by us were 10,869,500 tons and 324,000 tons, respectively. As a result, the average unit cost of crude oil we processed (for our own account) increased by 3.56% from RMB5,044.64 (U.S.\$809.72) per ton in 2011 to RMB5,224.38 (U.S.\$838.57) per ton in 2012. Our total costs of crude oil processing reached RMB55,538.0 million (U.S.\$8,914.5 million) in 2012, a slight increase of 3.77%, or RMB2,016.1million (U.S.\$323.6 million), compared to RMB53,521.9 million (U.S.\$8,590.9 million) for 2011, which represent 62.67% of our total cost of sales.

### ***Coal***

Most of the coal used for our electricity generation is purchased through a unified system of procurement administered by Sinopec Corp., and the rest is purchased directly by us from mines. Coal is transported by rail from the mines to Qinhuangdao port and shipped by barge to Jinshanwei where it is delivered to the plant via a wharf and a conveyer system. Our cost of coal is primarily dependent on coal price and transportation charges. Although coal may be purchased from alternative sources, railroad transportation must be obtained by allocation from the Chinese government on a monthly basis.

We expect that our total requirement for coal to generate electricity in 2013 will be approximately 2.01 million tons. In 2012, we consumed approximately 2.13 million tons of coal, an increase from 2011 of 0.03 million tons.

### ***Other Raw Materials***

We produce most of the raw materials used as feedstock for our operations. If any of these raw materials, other than ethylene, becomes unavailable from internal production, we believe that there are sufficient alternative sources at reasonable prices and the unavailability of raw materials from internal sources will not have a significant effect on our operations and profitability.

We purchase some ancillary raw materials from outside sources. These raw materials include natural gas, MX, methanol, ammonia, sodium hydroxide, sulfur, acetone, acrylonitrile, PTA, propylene and a variety of catalytic agents. In 2012, the total cost of these materials accounted for approximately 14.05% of our total cost of sales. We do not expect any difficulties in obtaining a supply of any of these ancillary raw materials in amounts sufficient to meet our needs in the foreseeable future.

### ***Sales and Marketing***

#### ***Distribution***

The distribution of our fuel products is subject to government regulations. We are required to sell certain refined products to the subsidiaries of Sinopec Group or customers designated by Sinopec Group. Since the second half of 2005, Sinopec Group has executed reforms to its system of selling petrochemical products and implemented what it refers to as a "Five Consolidations" strategy featuring consolidated marketing strategy, consolidated promotion, consolidated logistics optimization, consolidated sales and consolidated branding . As a result, the sales of our major petrochemical products are now conducted in a consolidated manner by sales agents designated by Sinopec Group. However, we have the autonomy to decide on the distribution method of our other products in accordance with market conditions. The products we sold in 2012 that were subject to planned distribution by Sinopec Group, sales by agents and sales based on our own discretion accounted for 51.16%, 43.32% and

5.52%, respectively, of the total products we sold.

We generally sell our products to large trading companies and industrial users with whom we have long-standing relationships, including Sinopec Group or customers designated by Sinopec Group. We believe that the transition to sales of major petrochemical products by agents designated by Sinopec Group will increase our distribution efficiency, reduce horizontal competition and enhance our overall bargaining power, by allowing us to benefit from Sinopec Group's extensive and highly specialized sales network. It will also allow us to focus more of our resources on reducing production costs and enhancing our technical support.

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We use long term contracts to sell most of our products. We did not experience significant write-offs or defaults on our accounts receivable or other trade accounts in 2012. In general we managed to keep a stable link between production and sales in 2012.

### ***Product breakdown***

***Synthetic Fibers*** In 2012, 9.49% of our synthetic fiber products were purchased by provincial and municipal government trading companies that act as intermediaries between us and end-users. No single customer accounted for more than 13.77% of our sales of synthetic fibers in 2012.

***Resins and Plastics*** In 2012, approximately 4.74% of our resins and plastics sales were to provincial and municipal government trading companies and approximately 63.68% were sold to industrial users. No single customer accounted for more than 3.22% of our sales of resins and plastics in 2012.

***Intermediate Petrochemicals*** We sell a variety of intermediate petrochemical products, none of which were sold in substantial quantities.

Sinopec Yizheng Chemical Fibre Company Limited ( *Yizheng* ) and Oriental Petrochemical (Shanghai) Corporation ( *Oriental* ) are the principal outside consumers of our paraxylene. In 2012, we sold 112.3 thousand tons and 148.9 thousand tons of paraxylene, representing 12.96% and 17.19% of our total 2012 production of such product, to Yizheng and Oriental respectively, at prices mutually agreed upon by the relevant parties.

***Petroleum Products*** In 2012, our primary gasoline and diesel customer was Sinopec Huadong Sales Company Limited.

***Trading of Petrochemical Products*** In 2012, our primary trading customer was Sinopec Chemical Commercial Holding Company Limited.

### ***Product Pricing***

Most of our products are permitted to be sold at market prices. However, four types of petroleum products (gasoline, diesel and jet fuel, and liquefied petroleum gas) that we sell are subject to varying degrees of government pricing control and are, accordingly, sold at prices set by the Chinese government, which may sometimes be below our costs. In 2010, 2011 and 2012, approximately 34.41%, 36.70% and 40.09% of our net sales were from products subject to price controls. In 2012, the domestic prices of refined oil products were not brought into line with the prices of crude oil on the international markets in a timely manner due to various policy concerns, e.g., the government's desire to control the high inflation rate in China, which resulted in the decline of RMB539.7 million of the operating profit of our refining business over the previous year. Price controls may apply to these products in various ways. Such price controls are sometimes applied exclusively to our products, exclusively to our competitors' products or sometimes applied to neither our products nor our competitors' products. The Chinese government has adopted changes to the pricing mechanism for domestic refined oil to be indirectly aligned with international crude oil prices in a controlled manner through use of certain formula(s).

For products that are not subject to price controls, we set our prices with reference to prices in the major Chinese chemical commodities markets in Shanghai and other parts of China. We also monitor pricing developments in major international commodities markets, particularly in Southeast Asia. In most cases, we revise product prices each month, or more frequently during periods of price volatility. Due to our economies of scale, brand recognition and high quality of products, we believe that we can continue to price our products competitively.

### ***Competition***

We compete principally in the Chinese domestic market where 98.86% of our products in volume were sold in 2012. In addition, the limited transportation infrastructure in China and the difficulties involved in transporting petrochemical products force companies to compete primarily on a regional basis. In 2012, 94.18% of our net sales were made to customers in Eastern China.

### ***Our Competitive Advantages***

We believe our primary competitive advantages are quality of product, pricing, brand recognition, geographic location and vertical integration. We have received many prizes and awards from both central and local government authorities for high product quality. Furthermore, our location on the outskirts of the densely populated and highly industrialized Shanghai area places us in close proximity to many of our customers. This location also gives us convenient access to ocean transport and inland waterways, which results in a competitive advantage in terms of transportation cost and reliability and punctuality of product delivery.





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We believe that our vertical integration represents a significant competitive advantage over non-integrated competitors in China, both in terms of reliability in delivery and price. For most downstream products, our vertical integration results in significant savings on transportation and storage costs which would be incurred by less vertically integrated facilities.

### ***The Domestic Competitive Environment***

Prior to 1993, because distribution and pricing of our products were determined in accordance with the State Plan, we did not operate in a competitive environment. With the liberalization of control over pricing and product allocation by the Chinese government, competition in the domestic market has been gradually increasing. At the same time, Chinese private enterprises have gradually overcome technological and funding barriers to extend their business from the downstream processing sector to the upstream petrochemical field. These enterprises have advantages in many areas such as flexibility in operation costs, preferential policy treatment and regional presence, and may use these advantages to compete with us in markets for our products.

### ***Foreign Competition and the World Trade Organization***

China joined the WTO on December 11, 2001. As part of its membership commitments, China agreed to eliminate certain tariff and non-tariff barriers to foreign competition in the domestic petrochemical industry that benefited us in the past. In accordance with its WTO commitments, China:

has reduced tariffs on imported petrochemicals products that compete with ours;

increased levels of permitted foreign investment in the domestic petrochemicals industry, allowing foreign investors to own 100% of a domestic petrochemicals company from December 11, 2004;

has gradually relaxed restrictions on the import of crude oil by non-state owned companies;

has granted foreign-owned companies the right to import petrochemical products; and

has permitted foreign-owned companies to distribute and market fuel products in both retail and wholesale markets in China. As a result of these measures, we are facing increasing competition from foreign companies and imports, but, we think that China's WTO entry will also create substantial amounts of new investment and business in China, with a corresponding increase in sales opportunities for us.

### ***Our Competitive Position***

In the following discussion, internal consumption of resins and intermediate petrochemicals produced by integrated manufacturers in the production of downstream products are treated as sales.

#### ***Synthetic Fibers***

In 2012, we had an approximate 0.87% share and imports had an approximate 1.45% share of total domestic polyester and acrylic consumption.

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The following table summarizes the competitive position of our principal synthetic fibers according to domestic sales in 2012.

Product	Our share of domestic consumption (%)	Our competitive ranking	Location of principal domestic competitor	Principal domestic competitor's share of consumption (%)	Imports share of consumption (%)
Acrylic	19.00%	1	Jilin Province	28.00%	21.39%

Sources: Statistics provided to us by Sinopec Group and the China National Council of Textiles.

*Resins and Plastics*

In 2012, we had an approximate 3.64% share and imports had an approximate 28.08% share of total domestic resins and plastics consumption. The following table summarizes the competitive position of our principal resins and plastics products according to domestic sales in 2012.

Product	Our share of domestic consumption (%)	Our competitive ranking	Location of principal domestic competitor	Principal Domestic competitor's share of consumption (%)	Imports share of consumption (%)
Polyester chips	5.19%	30	Jiangsu Province	12.00%	2.02%
PE	3.33%	3	Guangdong Province	5.18%	44.07%
PP	2.95%	5	Guangdong Province	3.50%	26.80%

*Intermediate Petrochemicals*

In 2012, we were one of the largest sellers of intermediate petrochemicals in China, holding an approximate 2.74% share of total domestic consumption, while imports had an approximate 27% share of domestic consumption. Ethylene glycol, paraxylene, benzene and butadiene are our major intermediate petrochemical products. In 2012, we were a major producer of ethylene glycol, paraxylene and benzene in China. The following table summarizes the competitive position of our principal intermediate petrochemicals according to domestic sales in 2012.

Product	Our share of domestic consumption (%)	Our competitive ranking	Location of principal domestic competitor	Principal Domestic competitor's share of consumption (%)	Imports share of consumption (%)
Ethylene glycol	4.32%	1	Zhejiang Province	15.00%	73.40%
Paraxylene	6.57%	2	Jiangsu Province	9.21%	47.68%
Benzene	5.61%	1	Jiangsu Province	5.30%	6.26%
Butadiene	4.95%	12	Zhejiang Province	5.78%	12.84%

*Petroleum Products*

In 2012, we had an approximate 1.95% share of total domestic petroleum products market while imports had an approximate 3.48% share. Although we have one of the largest refining capabilities in China, we use most of our refining capacity to produce feedstock for our own downstream processing of petrochemical products.

The domestic markets for each of our major petroleum products are geographically concentrated because these markets tend to be highly localized with individual producers controlling a large share of the markets in their locality. In 2012, we sold approximately 97.94% of our

petroleum products in Eastern China.

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**Table of Contents***Investments*

We established Secco, a Sino-foreign equity joint venture, in late 2001 with BP and Sinopec Corp., primarily to build and operate a 900,000 ton Rated Capacity ethylene petrochemical manufacturing facility. Secco completed construction and commenced its manufacturing operations in 2005. In 2009, Secco had expanded the capacity of certain facilities to 1,090,000 tons of ethylene per annum. We own 20% of the equity interest of Secco.

In 2012, Secco achieved a sales revenue of RMB27.158 billion (U.S.\$4.36 billion), representing a decrease of 1.93% from its sales revenue of RMB27.693 billion (U.S.\$4.45 billion) in 2011. The decrease of sales revenue was primarily attributable to the relatively lower market demand in the second half of 2012, in correspondence to which Secco selected to control the production capacity of manufacturing facilities. Secco produced 1,040.9 thousand tons of ethylene in 2012, representing a decrease of 24.3 thousand tons over the previous year, down by 2.28%. Secco achieved a net loss of RMB349.03 million (U.S.\$56.02 million) in 2012, as compared to a net profit of RMB17.04 million (U.S.\$2.74 million) in 2011. The decrease in net profit was primarily due to the fluctuations of international crude oil price and the continuous increase in the price of naphtha raw material. The prices of the majority of domestic petrochemical products fell during 2012, in particular, the price of polyolefin products was at a low level. All the above reasons contributed to Secco's net loss in 2012.

*Environmental Protection*

We are subject to national and local environmental protection regulations, which currently impose a graduated schedule of fees for the discharge of waste substances, require the payment of fines for pollution and provide for the forced closure of any facility that fails to comply with orders requiring it to cease or cure certain environmentally damaging practices. We have established environmental protection systems which consist of pollution control facilities to treat certain of our waste materials and to safeguard against accidents. Because of the nature of our business, however, we store a significant amount of waste substances in the plants and discharge them into the environment after such waste substances are processed and meet the discharge standards. During 2012, we were assessed a total of RMB30.77 million (U.S.\$4.94 million) in fees for discharges of waste substances. As of March 31, 2013, we had not been assessed any fines for environmental violations and there were no actions pending or, to our knowledge, threatened which would result in the assessment of such a fine.

We believe our environmental protection facilities and systems are adequate for the existing national and local environmental protection regulations. In 2012, the Company continued to carry out various energy-saving and emissions reduction measures in accordance with the relevant domestic energy conservation and emissions reduction requirements, and achieved all energy-saving and emissions reduction goals set by the Chinese government during the year. In 2012, the Company's overall level of energy consumption per RMB10,000 product value was 0.998 ton of standard coal on a par with that for 2011. Furthermore, the Company provided 57,344,700 tons of water for production (2011: 58,069,200 tons), representing a decrease of 724,500 tons, or 1.25% year-on-year, while the recycling rate of industrial water reaching 96.90%. The use volume of fresh water decreased by 2.40%. The total volume of each COD, solid wastes, industrial waste water and SO<sub>2</sub> discharge declined by 2.97%, 18.10%, 1.53% and 6.65% respectively. Various indices, such as waste water discharge compliance rate and the hazardous waste treatment ratio, comply with environmental protection requirements. The average heat efficiency rate of heaters was 91.89%, increased by 0.27 percentage points over the previous year. In 2012, the Company's various projects, such as the Flue-gas Desulphurisation Project for Furnaces of Coal-fired Power Plants, the Removal of Foul Gas from the De-aeration Pool of the Waste Water Treatment Plants, Tail Gas Regenerative Thermal Oxidation Facilities at PTA Plants, Flare Gas Recovery System and the addition of Recycled Hydrogen Desulfurization Unit to the Diesel Hydrogenation Plant (with a capacity 550,000 tons/year), played an effective role in the energy conservation and emissions reduction.

Despite our continuous efforts to protect the environment and save energies, there can be no assurance that Chinese national or local authorities will not impose additional regulations that would require additional expenditures in respect of environmental matters in the future.

*Insurance*

We currently participate in a package of insurance coverage plan through Sinopec Group as its controlled subsidiary, which, as of December 31, 2012, was approximately RMB32.964 billion (U.S.\$5.29 billion) on our property and facilities and approximately RMB3.511 billion (U.S.\$0.56 billion) on our inventory. In addition, we maintain insurance policies for such assets as the engineering construction projects and products in transit with third-party's commercial insurance company. The Sinopec Group insurance coverage is compulsory and applies to all enterprises controlled by Sinopec Group, pursuant to guidelines of Sinopec Group which may not be legally enforceable against Sinopec Group. Thus, there are uncertainties under Chinese law as to what percentage insurance claims we may demand against Sinopec Group.



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We do not carry any third party liability insurance to cover claims in respect of personal injury, property or environmental damage arising from accidents on our property or relating to our operations other than on our transportation vehicles. We have not had a third party liability claim filed against us during the last five years. Since business interruption insurance is not customary in China, we do not carry such insurance.

*Government Regulations*

Following the development of several major oil fields and a growth in demand for petroleum and petrochemical products in China in the early 1970 s, the Chinese government organized petroleum refining and petrochemical production and processing plants into large complexes that would permit integrated production of petroleum products, intermediate petrochemicals, resins and plastics, and synthetic fibers.

Although the Chinese government is liberalizing its control over the petroleum and petrochemical industries in China, significant government regulations that limit the business strategies available to us remain. Central government agencies and their local or provincial level counterparts do not own or directly control our production plants. However, they exercise significant control over the petrochemical industry in areas such as pricing, production quotas, quality standards, allocation of raw materials and finished products, allocation of foreign exchange and Renminbi loans for capital construction projects. The Chinese government s intentions with respect to the development objectives and policies for the petrochemical industry are stated as part of the Five Year Plans for National Economic and Social Development formulated every five years. These plans at both the national and Shanghai municipality level have identified the petrochemical industry as a development industry .

Historically, we were supervised by Sinopec, a ministry-level enterprise under the direct supervision of the State Council, China s highest administrative body. As a result of a governmental restructuring in 1998, we became subject to the administration of the State Bureau of Petroleum and Chemical Industry. After its functions were terminated in March 2001, we became subject to the administration of the State Economic and Trade Commission. The State Economic and Trade Commission was dissolved in March 2003 and its function in directing the reform and management of state-owned enterprises were assumed by the State-owned Assets Supervision and Administration Commission, its function in industry planning and policy making were assumed by NDRC, and its functions in administering domestic trade, coordinating and implementing import and export plans of critical industrial products and raw materials were assumed by the Ministry of Commerce. Since then, we have been subject to the industrial oversight of these three new governmental agencies at the national level.

As part of this restructuring, Sinopec was also restructured in July 1998. The succeeding entity, Sinopec Group, was authorized to conduct a petrochemical business and to control the exploration of crude oil and natural gas and crude oil refining, mainly in the southern and eastern regions of China. China Petroleum and Natural Gas Corporation, another major state-owned petrochemical company, was also restructured, renamed China National Petroleum Corporation and authorized to conduct the same type of business, mainly in the northern and western regions of China. On December 31, 1999, Sinopec Group completed a reorganization pursuant to which certain of its core oil and gas and chemical operations and businesses and related assets and liabilities were transferred to its subsidiary, Sinopec Corp., currently our controlling shareholder.

*Business Operations Relating to Iran Threat Reduction and Syria Human Rights Act of 2012*

In 2012, we sourced a small amount of crude oil from Iran through a wholly-owned subsidiary of Sinopec Corp., our controlling shareholder, and such amount represented 6.3% of our total purchase volume of crude oil in 2012. Details of our 2012 purchase volume and purchase expenses are provided below:

	Volume (thousand tons)	% of total	Amount (RMB billion)	% of total
<b>Iran</b>	722.2	6.33	3.59	6.05
<b>Others</b>	10,681.0	93.67	55.78	93.95
<b>Total</b>	11,403.2	100.00	59.37	100.00

In addition, based on feedback to our inquiries to Sinopec Group, the controlling shareholder of Sinopec Corp., Sinopec Group, directly or indirectly, engaged in a small amount of business activities in Iran such as providing engineering support and designs. Sales revenue from these business activities accounted for 0.08% of Sinopec Group s total unaudited sales revenue in 2012. No profits were generated from these business activities in 2012.

We have no performance obligations under any contract to continue to purchase crude oil sourced from Iran in 2013.



**Table of Contents****C. Organizational Structure.***Our Subsidiaries*

Our significant subsidiaries are listed below. All of the subsidiaries named below are incorporated in China.

Subsidiary Name	Our ownership interest and voting power (%)
Shanghai Petrochemical Investment Development Company Limited	100.00
China Jinshan Associated Trading Corporation	67.33
Shanghai Jinchang Engineering Plastics Company Limited	74.25
Shanghai Golden Phillips Petrochemical Company Limited	60.00
Zhejiang Jin Yong Acrylic Fiber Company Limited	75.00
Shanghai Golden Conti Petrochemical Company Limited	100.00

*Sinopec Corp.*

We are a member of a group (defined as a parent and all its subsidiaries) for purposes of the disclosure rules of the Securities and Exchange Commission. The parent company of this group is Sinopec Corp., our controlling shareholder. Sinopec Corp. is operated by separate management and from time to time uses its interest as a shareholder to direct our policies and management. We have extracted the following information regarding Sinopec Corp. from its public filings:

**Overview**

Sinopec Corp. is an integrated petroleum and petrochemical company with upstream, midstream and downstream operations. Based on trading volume in 2012, Sinopec Corp. is one of the largest publicly listed companies in China and one of the largest petroleum and petrochemical companies in both China and Asia. Sinopec Corp. is one of the largest refiners, distributors and marketers of gasoline, diesel, jet fuel and most other major refined products in China and Asia with principal markets in the eastern and southern regions of China. Sinopec Corp. is also a producer and distributor of petrochemicals in China and additionally explores, develops and produces crude oil and natural gas principally to supply its refining and chemical operations.

**Subsidiaries**

Details of Sinopec Corp.'s principal subsidiaries are given in the table below. Except for Sinopec Kantons Holdings Limited and Sinopec (Hong Kong) Limited, which are incorporated in Bermuda and Hong Kong respectively, all of the below principal subsidiaries are incorporated in China.

Name of Company	Particulars of issued capital (millions)	Type of legal entity	Percentage of equity held by Sinopec Corp. and its subsidiary (%)	Principal activities
China Petrochemical International Company Limited	RMB1,400	Limited company	100.00	Trading of petrochemical products
Sinopec Chemical Commercial Holding Company Limited	RMB1,000	Limited company	100.00	Marketing and distribution of petrochemical products



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Sinopec Qingdao Petrochemical Company Limited	RMB1,595	Limited company	100.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Sales Company Limited	RMB1,700	Limited company	100.00	Marketing and distribution of refined petroleum products
Sinopec Yangzi Petrochemical Company Limited	RMB13,203	Limited company	100.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec Zhongyuan Petrochemical Company Limited	RMB2,400	Limited company	93.51	Manufacturing of petrochemical products
Fujian Petrochemical Company Limited	RMB5,019	Limited company	50.00	Manufacturing of plastics, intermediate petrochemical products and petroleum products

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Name of Company	Particulars of issued capital (millions)	Type of legal entity	Percentage of equity held by Sinopec Corp. and its subsidiary (%)	Principal activities
Sinopec Shanghai Petrochemical Company Limited	RMB7,200	Limited company	55.56	Manufacturing of synthetic fibers, resin and plastics, intermediate petrochemical products and petroleum products
Sinopec Kantons Holdings Limited	HK\$207	Limited company	72.34	Trading of crude oil and petroleum products
Sinopec Yizheng Chemical Fiber Company Limited	RMB4,000	Limited company	42.00	Production and sale of polyester chips and polyester fibers
Sinopec International Petroleum Exploration and Production Company Limited	RMB8,000	Limited company	100.00	Investment in exploration, production sales, etc. of petroleum and nature gas
Sinopec Shell (Jiangsu) Petroleum Marketing Company Limited	RMB830	Limited company	60.00	Marketing and distribution of refined petroleum products
BP Sinopec (Zhejiang) Petroleum Company Limited	RMB800	Limited company	60.00	Marketing and distribution of petroleum refined products
Sinopec Qingdao Refining and Chemical Company Limited	RMB5,000	Limited company	85.00	Manufacturing of intermediate petrochemical products and petroleum products
China International United Petroleum & Chemical Co., Ltd.	RMB3,000	Limited company	100.00	Trading of crude oil and petrochemical products
Sinopec Hainan Refining & Chemical Company Limited	RMB3,986	Limited company	75.00	Manufacturing of intermediate petrochemical products and petroleum products
Sinopec (Hong Kong) Limited	HK\$5,477	Limited company	100.00	Trading of crude oil and petrochemical products
Sinopec Senmei (Fujian) Petroleum Ltd.	RMB1,840	Limited Company	55.00	Marketing and distribution of refined petroleum products
Sinopec Fuel Oil Sales Company Limited	RMB2,200	Limited Company	100.00	Marketing and distribution of refined petroleum products

**D. Property, Plant and Equipment.***Real Property*

Our corporate headquarters and production facilities, occupying an area of approximately 7.03 square kilometers, are located in Jinshanwei, approximately 75 kilometers from downtown Shanghai. The total gross floor area of all our production and other facilities is approximately 2 million square meters. We own all of the buildings and facilities located at the site. We have the right to use the land upon which our buildings and facilities are located for a term of 50 years beginning in 1993 without the payment of any rent or usage fees other than land use taxes. We also have the right to transfer our land use rights to third parties without any payment to the Chinese government, so long as the use of the land remains the same as when the land use right was granted to us and the terms of the land use right we received will be applicable to any transferees.



**Table of Contents***Plants and Facilities*

The following tables set forth the Rated Capacities of our principal production units. The actual production capacity of a production unit can exceed the Rated Capacity and may be further increased without increasing the Rated Capacity through technical improvements or expansion of such unit. The utilization rate of a production unit is based upon the Rated Capacity rather than actual production capacity and may vary with technical enhancements, changes in production management and scheduling of maintenance.

The following table sets forth the Rated Capacities and weighted average utilization rates of our principal production units for petroleum products and intermediate petrochemicals in 2012:

<b>Production Unit (number of units)</b>	<b>Rated Capacity (tons)</b>	<b>Utilization Rate (%)</b>
Crude oil distillation units (2)	14,000,000	79.95
Hydrocracker (2)	3,000,000	89.36
Ethylene units (2)	850,000	108.25
Aromatics unit	835,000	103.74
PTA unit	400,000	95.47
EO/EG unit (2)	525,000	100.88
Acrylonitrile unit	130,000	105.47
*Cracking and catalyzing (2)	4,500,000	86.32
Delayed Coking (2)	2,200,000	105.41
Reforming prehydrogenation unit	750,000	85.71
C5 segregation unit (2)	205,000	121.45

\* For cracking and catalyzing units, the utilization rate of 86.32% only applies to one unit. The second unit was launched for operation in the beginning of 2013, as such its utilization rate is not available as the date of this annual report.

Our two crude oil distillation units were designed and built in China. In 2012, the actual quantity of crude oil we processed was approximately 11.1935 million tons. Our hydrocracker uses technology from United Oil Products Corporation of the United States. Our first ethylene unit uses technology from Mitsubishi Petrochemical Corporation of Japan. The second ethylene unit uses technology from ABB Lummus Global Inc. of the United States. The aromatics unit uses technology from Universal Oil Products Corporation of the United States. The PTA unit uses technology from Mitsui Petrochemical Corporation of Japan. The EO/EG unit was constructed using technology from Scientific Design Corporation of the United States.

The following table sets forth the Rated Capacities and weighted average utilization rates of our principal production units for resins and plastics and synthetic fibers in 2012:

<b>Production Unit (number of units)</b>	<b>Rated Capacity (tons)</b>	<b>Utilization Rate (%)</b>
Polyester units (3)	550,000	107.71
Polyester staple units (2)	154,000	42.61
Polyester filament units	21,000	88.87
Acrylic staple fiber units (4)	141,000	117.66
PE units (3)	408,000	109.60
PP units (3)	400,000	108.27
Vinyl acetate unit (2)	102,000	91.33

Our polyester units use technology from Kanebo Corporation of Japan and E.I. Dupont DeNemours & Co. Inc. ( Dupont ) of the United States. The polyester staple units use technology from Teijin of Japan and Jima of Germany as well as Chinese technology. The polyester filament units use technology from Murata Manufacturing Company Limited and Teijin Corporation of Japan, Barmag AG of Germany and Dupont. We produce polyethylene in three units, two LDPE units which use technology from Mitsubishi Petrochemical Corporation of Japan and BASF LDPE of Germany and one HDPE unit uses the Borstar bimodal polyethylene technology from Northern European Chemical Engineering Company.

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The acrylic fiber units were built domestically, based on the design of equipment which was imported into China in the 1960s and that we substantially improved. In 1996, we acquired two additional acrylic fiber units which use technology from Kawasaki Corporation of Japan. We produce PP in three identical units using technology from Himont Corporation of Italy. The PVA unit uses technology acquired from Kuraray Corporation of Japan.

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### *Power Facilities*

Our electricity requirements are currently supplied by our own 425 megawatt coal-fired power plant and petroleum coke power plant. These power plants are designed to provide sufficient power supply needed by our facilities. We are connected to the Eastern China electricity grid, which provides a back-up source of power in case of a shortfall in our self-generated power supply.

### *Other Facilities*

We also have facilities to produce industrial water, steam, hydrogen, oxygen and nitrogen which we use in our production facilities.

### *Maintenance*

We engage in production stoppages for facility maintenance and repairs and implement our routine monthly maintenance and repair plans according to the needs of our production facilities, our requirements for product quality, and our commitment to security and environmental protection. The technicians in our facility management department have responsibility for the daily management of maintenance and repair work. We also outsource facility maintenance and repair projects to qualified contractors.

In 2012, the Company prioritized the HSE works, and implemented an HSE accountability system at each working level to ensure a sound safety and environment friendly practice. There were no accidents involving serious consequences such as major fires, explosions or environmental pollution during the year. Overall production remained stable. Both the number of times and the duration of unplanned shutdowns of the major production plants decreased by 49.12% and 46.42%, respectively. Important technical and economic indicators were improved, with 62.26% of such indicators reflecting a stronger performance than the previous year, and 33.02% of such indicators reaching the advanced industrial level.

### *Transportation-Related Fixtures*

Crude oil, our principal raw material, is transported by pipeline and oil tanker to a crude oil terminal wharf and storage tanks. Our products leave the factory by water, rail, road and pipeline. In 2012, approximately 54.07% of our products by sales volume were collected by customers from our premises, and we delivered the balance. Our major ethylene customer is supplied via a pipeline. Some of the products collected by customers were also transported using our facilities.

### *Wharfs*

We own one chemical wharf at Jinshan with five berths of 2,000, 5,000, 8,000, 10,000 and 25,000 tons. We also own a connecting pipeline capable of loading up to approximately 1.4 million tons of chemical products annually onto ocean-going barges and ships. In 2012, products representing 15.17% of total sales volume were shipped from the wharf. We also have a facility to load ships and barges which use the region's inland waterways. In 2012, products representing 2.78% of total sales volume were shipped from these facilities. We believe that we have a competitive advantage because a greater proportion of our products are shipped by water as opposed to rail and truck, which is subject to capacity constraints on China's rail and highway networks. Additionally, we own facilities for receiving crude oil and coal at docks that we own and transporting such materials by pipeline or conveyor to our production facilities.

We own an oil terminal wharf at Chenshan in Zhejiang Province, which is comprised of four berths, among which each of two berths is capable of handling 80,000 ton vessels, one is capable of handling 15,000 ton vessels and the other 50,000 ton vessels. Two 25 kilometer pipelines connect this oil terminal wharf with our facilities.

### *Rail*

We own a railroad loading depot with an annual capacity of 500,000 tons. The depot provides access via a spur line to the Chinese national railway system. In 2012, products representing 1.53% of total sales volume were transported from the factory by rail. Our ability to transport products by rail is limited because of China's overburdened railway system, the allocation of use of which remains strictly controlled by the Chinese government.

**Table of Contents***Capital Expansion Program*

Our principal capital expansion projects for the near term are summarized in the table and further described below. In aggregate, we expect that total investment in the projects described will be approximately RMB2.6 billion in 2013. This amount will be funded by our own capital and by bank loans.

<b>Name of Project</b>	<b>Rated Capacity (tons/year)</b>	<b>Start Date</b>	<b>Expected Completion Date</b>	<b>Status</b>
The Carbon Fiber Project with a capacity of 1,500 tons/year	1,500	2010	Phase I 2012	Phase I completed
The No. 2 and No. 3 Aromatics Complexes Energy-saving Up-grade Project	N/A	2012	2014	Under construction
The SL-2 Cracking Furnace of No. 2 Ethylene Unit Transformation for Improving Energy Efficiency	N/A	2012	2013	Under construction
The Transformation for Improving Manufacturing Capacity for Epoxy Ethane	N/A	2012	2013	Under construction

N/A not applicable.

In 2010, 2011 and 2012, we invested RMB1.357 billion, RMB3.225 billion and RMB3.811 billion respectively, in capital expansion projects.

*Refining Capacity Expansion*

With a view to accommodating the need to adjust our product mixes, we adhere to the direction of purchasing more heavy and low-quality crude oil, improve the overall processing procedures, enhance our reprocessing capacity, and continuously increase the operating adaptability and overall efficiency of our refining facilities. The construction of the Phase 6 Project, which follows the direction of giving considerations to both low cost and product diversity, and to both mass and refined production, emphasizes low cost and mass production in the upstream supply and high added value and refined production in the downstream production, and focuses on the reconstruction of refining facilities, fine chemicals, structure adjustment and system perfection, has been substantially completed. The construction of the Refinery Revamping and Expansion Project was completed and the relevant facilities were put into operation in December 2012.

*Expansion of New and Existing Downstream Petrochemical Products*

As an integrated petrochemical complex, we produce a wide range of intermediate and downstream petrochemical products. We plan to utilize our currently available resources and develop higher-margin downstream products and fine chemicals, with raw materials including cracking carbon 5, carbon 4, epoxy ethane, vinyl acetate and acrylonitrile. With a view towards enhancing our competitive power and the ability to keep sustainable development, we plan to further increase the overall resource utility rate and adjust and improve our company's industrial structure through the measures discussed below.

To take advantage of our expertise in producing acrylics fiber and to improve our industrial structure and upgrade certain products, we plan to construct a carbon fiber project with a capacity of 1,500 tons/year. Sinopec Corp. approved the basic design for this project in December 2010; pile foundation construction was commenced in December 2010; civil engineering was commenced in February 2011 and one series of facilities under phase I were launched for trial operation in 2012.

We plan to construct a new 100,000t/a EVA production unit with imported technology. The revised feasibility study report for this project was submitted to Sinopec Corp. for approval in September 2011. The construction of this project is scheduled to be commenced in 2013 and completed in 2015.

We plan to adjust the production structure to improve No. 1 glycol unit's capacity of producing epoxyethane by utilizing SD technology. Sinopec Corp. approved the feasibility study report for this project in April 2011. The construction was commenced in August 2012 and is scheduled to be completed in June 2013.





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### ***Other Projects***

The basic design for the Up-grading Project for the Optimization of the system and reduction in energy and feedstock consumption of the No.2 PTA Plan was approved by Sinopec Corp. in May 2010. The Company started civil engineering in 2010 and the project was completed and put into operation in 2012. The feasibility study report for No. 2 and No. 3 aromatic hydrocarbon unit transformation for improving energy efficiency was approved by Sinopec Corp. in April 2011; and this project is scheduled to be commenced in 2013 and completed in 2014. The feasibility study report for No. 2 combined heat and power furnace transformation project for the purpose of achieving industrial standards and efficiency improvement was approved by Sinopec Corp. on October 28, 2011. The basic design was approved in July 2012 and the construction was completed in 2012. The feasibility study report for SL-2 cracking furnace of No. 2 ethylene unit transformation for improving energy efficiency was submitted to Sinopec Corp. for approval in July 2011. The construction was commenced in September 2012 and is scheduled to be completed in 2013.

In order to further our capacity of maintaining sustainable development and to echo the government's requirement of protecting the environment, we planned the No.5 and No. 6 Furnace Secondary Desulfurisation Project for Department of Thermoelectric. The basic design of the project was approved by Sinopec Corp. in June 2011. The construction commenced in September 2011 and was completed in June 2012. We also plan to commence the project of dust abatement and denitrification unit construction for No. 3 and No. 4 furnaces. The feasibility study report of the project was submitted to Sinopec Corp. for approval on December 29, 2011. The construction was commenced in December 2012 and is scheduled to be completed in August 2013.

### **ITEM 4A. UNRESOLVED STAFF COMMENTS.**

None.

### **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS.**

#### ***General***

Our financial performance has been affected by factors arising from operating in a planned economy which are beyond our control. However, with China's WTO accession, the impact of these factors has gradually been decreasing.

You should read the following discussion and analysis in conjunction with our audited financial statements and our selected financial data, in each case, together with the accompanying notes included elsewhere in this annual report. Our audited financial statements have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board.

#### ***Critical Accounting Policies***

The following discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements. The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during 2012. Our financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of our financial statements. We based our assumptions and estimates on historical experience and on various other assumptions that we believe to be reasonable and which form the basis for making judgments about matters that are not readily apparent from other sources. On an on-going basis, our management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

Our principal accounting policies are set forth in Note 2 to our consolidated financial statements included in [Item 17. Financial Statements](#). The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing our financial statements. We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our financial statements.

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**Table of Contents*****Impairments for long-lived assets***

If circumstances indicate that the net book value of a long-lived asset may not be recoverable, the asset may be considered impaired, and an impairment loss may be recognized in accordance with International Accounting Standard No. 36 Impairment of Assets. Long-lived assets are reviewed for indication of impairment at the end of each reporting period or whenever events or changes in circumstance have indicated that their carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the 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 prices because quoted market prices for our assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgment relating to level of sale volume, selling price and amount of operating costs. We use all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of sale volume, selling price and amount of operating costs. During the years ended December 31, 2010, 2011 and 2012, we recognized impairment charges on property, plant and equipment of RMB238 million, RMB11 million and RMB nil, respectively.

***Depreciation***

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual values. We review the estimated useful lives of the assets annually in order to determine the amount of depreciation expense to be recorded during any reporting period. The useful lives are based on our historical experience with similar assets, taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates. There were no significant changes in these estimates during the years ended December 31, 2010, 2011 and 2012.

***Impairment for bad and doubtful debts***

We estimate impairment losses for bad and doubtful debts resulting from the inability of the customers to make the required payments. We base the estimates on the aging of the accounts receivable balance, customer credit-worthiness and historical write-off experience. If the financial condition of the customers were to deteriorate, actual impairment losses would be higher than estimated. Impairment provisions for bad and doubtful debts were a reversal of RMB3 million, a reversal of RMB2 million and a provision of RMB0.2 million, during the years ended December 31, 2010, 2011 and 2012, respectively.

***Inventory management***

At the beginning of every year, the management team determines the appropriate levels of inventories to maintain on the basis of annual production and operating plans, financial budgets and market conditions. Every six months, the management team conducts an inventory status analysis in conjunction with its supply, production, marketing, financial and other departments and develops a plan for keeping inventories at an appropriate level.

Management assesses the realizability of our inventories based on the estimates of the net realizable value of the inventories at the end of each reporting period. Net realizable value represents the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. We base the estimates on all available information, including the current market prices of the finished goods and raw materials and historical operating costs. Any excess of the cost over the net realizable value of each item of inventories is recognized as a provision for diminution in the value of inventories. If the actual selling prices were to be lower or the costs of completion were to be higher than the estimates, the actual allowance for diminution in value of inventories could be higher than estimated. In addition, management periodically reviews inventory aging information to assess if any obsolete inventories are required to be written down at the period end. Based on our assessments, we recorded write-down of inventories of RMB12 million, RMB110 million and RMB204 million respectively for the years ended December 31, 2010, 2011 and 2012. Barring unforeseeable changes that may occur to the current economic environment in either China or worldwide, our management does not anticipate encountering major difficulties with our attempt to realize by the end of 2013 the bulk of our inventories as of December 31, 2012 after deducting for diminution in values.

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**Table of Contents****Income tax**

In June 2007, the State Administrative of Taxation issued a tax circular (Circular No.664) to the local tax authorities requesting the relevant local tax authorities to rectify the applicable enterprise income tax ( EIT ) for nine listed companies, which included us. After the notice was issued, we were required by the relevant tax authority to settle the EIT for 2007 at a rate of 33 percent. To date, we have not been requested by the tax authorities to pay additional EIT in respect of any years prior to 2007. There is no further development of this matter during the year ended December 31, 2012. No provision has been made in the financial statements at December 31, 2012 for this uncertainty because we believe it is not probable that the Company will be required to pay additional EIT for tax years prior to 2007.

**Recognition of deferred tax assets**

Deferred tax assets are recognized in respect of temporary deductible differences and the carryforward of unused tax losses. We recognize deferred tax assets only to the extent that it is probable that future taxable profit will be available against the assets which can be realized or utilized. At the end of each reporting period, we assess whether previously unrecognized deferred tax assets should be recognized. The Company recognizes a previously unrecognized deferred tax asset to the extent that it is probable that future taxable profit will allow the deferred tax asset to be utilized. In addition, we assess the carrying amount of deferred tax assets that are recognized at the end of each reporting period. The Company reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available for the deferred tax asset to be utilized.

In making the assessment of whether it is probable the Company will realize or utilize the deferred tax assets, we primarily rely on the generation of future taxable income to support the recognition of deferred tax assets. In order to fully utilize the deferred tax assets recognized at December 31, 2012, the Company would need to generate future taxable income of at least RMB4,210 million, of which RMB1,497 million is required to be generated by 2013 prior to the expiration of the unused tax losses incurred in 2008 and RMB2,260 million is required to be generated by 2017 prior to the expiration of the unused tax losses incurred in the current year.

Management believes that it is probable that the Company will generate sufficient taxable income before the unused tax losses expire. Favorable factors include the enlargement of crude oil refinery capacity of the Company and the new pricing mechanism in the PRC for setting gasoline and diesel prices to more closely track crude oil costs. Uncertainties which could affect the estimated taxable income include various factors such as the volatility of international crude oil prices and the cyclical nature of the petroleum and petrochemical industry. Upon changes in facts and circumstances, management may conclude that deferred tax assets may not be realizable in future periods, resulting in a future reduction in the carrying amount of a deferred tax asset.

**Government Policies**

The impact of government economic, fiscal, and monetary policies can materially affect our financial condition, results of operations, and cash flows (see [Item 3. Key Information D. Risk Factors](#)).

In particular, we consume large amounts of crude oil to manufacture our products of which more than 90% is imported. We attempt to mitigate the effect of increased costs due to rising crude oil prices. However, our ability to pass on these increased costs to our customers is dependent on government regulations, among other factors. Given that the increase of the sales prices of our products can lag behind the increase of crude oil costs, we sometimes fail to completely cover the increased costs by increasing our sales prices, particularly where government regulations restrict the prices of certain of our fuel products such as gasoline, diesel and jet fuel, and liquefied petroleum gas. In 2010, 2011 and 2012, approximately 34.41%, 36.70% and 40.09% of our net sales were from such products subject to price controls. In 2012, the domestic prices of refined oil products were not brought into line with the prices of crude oil in the international markets in a timely manner due to various policy concerns, e.g., the government's desire to control the high inflation rate in China, which resulted in the decline of RMB539.7 million of the operating profit of our refining business over the previous year. Although the current price-setting mechanism for refined petroleum products in China allows the Chinese government to adjust price in the PRC market when the average international crude oil price fluctuates beyond certain levels within a certain time period (see [Item 4. Information on the Company B. Business Overview Product Pricing](#)), the Chinese government still retains discretion as to whether or when to adjust the prices of the refined oil products. The Chinese government generally exercises certain price control over refined oil products once international crude oil prices experience a sustained rise or become significantly volatile. Moreover, the Chinese government controls the distribution of many fuel products in China. For instance, some of our fuel products are required to be sold to designated distributors (such as the subsidiaries of Sinopec Corp.). Because we cannot freely sell our fuel products to take advantage of opportunities for higher prices we may not be able to fully cover increases in crude oil prices by increases in the sale prices of our products, which has had and will continue to have a material adverse effect on our financial condition, results of operations and cash flows.



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In addition, the exchange rates between the Renminbi and the U.S. Dollar or other foreign currencies are affected by Chinese government policies. In particular, the value of the Renminbi is only permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. The Chinese government continues to receive significant international pressure to liberalize its currency policy. Most of our revenue is denominated in Renminbi, and most of our purchase of crude oil and some equipment and certain loan repayments are made in foreign currencies. In general, the trend for appreciation of the Renminbi has been helpful to us since our imported crude oil purchases constitute such a large portion of our total costs. By contrast, any depreciation of the Renminbi would increase our costs and adversely affect our capacity of making profits. In addition, any depreciation of the Renminbi could adversely affect the value of the dividends of our H shares and ADSs, which we pay in foreign currencies. Further appreciation in the value of Renminbi against foreign currencies (including the U.S. Dollar) may cause a decrease in the value of our cash and cash equivalents that are denominated in foreign currencies.

**Summary**

The following table sets forth our sales volumes and net sales for the years indicated:

	For the year ended December 31,								
	Sales Volume ( 000 tons)	2010 Net Sales (Millions of RMB)	% of Total Net Sales	Sales Volume ( 000 tons)	2011 Net Sales (Millions of RMB)	% of Total Net Sales	Sales Volume ( 000 tons)	2012 Net Sales (Millions of RMB)	% of Total Net Sales
Synthetic fibers	255.9	3,906.6	5.4	250.9	4,150.2	4.6	253.3	3,313.3	3.8
Resins and plastics	1,620.2	14,900.0	20.7	1,590.7	16,418.6	18.3	1,582.8	14,706.3	16.9
Intermediate petrochemicals	2,386.5	17,206.4	23.9	2,246.7	19,023.2	21.3	2,209.2	17,993.5	20.6
Petroleum products	6,342.8	28,733.9	39.9	6,968.1	37,350.2	41.7	6,921.0	38,301.4	43.9
Trading of petrochemical products		6,565.9	9.1		11,617.0	13.0		12,020.7	13.8
Others		783.1	1.0		950.5	1.1		882.1	1.0
<b>Total</b>	<b>10,605.4</b>	<b>72,095.9</b>	<b>100.0</b>	<b>11,056.4</b>	<b>89,509.7</b>	<b>100.0</b>	<b>10,966.3</b>	<b>87,217.3</b>	<b>100.0</b>

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The following table sets forth a summary statement of the Company's consolidated statements of operations for the years indicated:

	For the year ended December 31,					
	2010		2011		2012	
	Millions of RMB	% of Net sales	Millions of RMB	% of Net sales	Millions of RMB	% of Net sales
<b>Synthetic fibers</b>						
Net sales	3,906.6	5.4	4,150.2	4.6	3,313.3	3.8
Operating expenses	(3,471.0)	(4.8)	(3,848.9)	(4.3)	(3,718.6)	(4.3)
Segment profit/(loss)	435.6	0.6	301.3	0.3	(405.3)	(0.5)
<b>Resins and plastics</b>						
Net sales	14,900.0	20.7	16,418.6	18.3	14,706.3	16.9
Operating expenses	(13,908.9)	(19.3)	(16,406.6)	(18.3)	(15,997.7)	(18.4)
Segment profit/(loss)	991.1	1.4	12.0	0.0	(1,291.4)	(1.5)
<b>Intermediate petrochemicals</b>						
Net sales	17,206.4	23.9	19,023.2	21.3	17,993.5	20.6
Operating expenses	(16,841.3)	(23.4)	(17,874.6)	(20.0)	(17,160.8)	(19.6)
Segment profit	365.1	0.5	1,148.6	1.3	832.7	1.0
<b>Petroleum products</b>						
Net sales	28,733.9	39.9	37,350.2	41.7	38,301.4	43.9
Operating expenses	(27,593.6)	(38.3)	(37,803.6)	(42.2)	(39,294.4)	(45.0)
Segment profit/(loss)	1,140.3	1.6	(453.4)	(0.5)	(993.0)	(1.1)
<b>Trading of petrochemical products</b>						
Net sales	6,565.9	9.1	11,617.0	13.0	12,020.7	13.8
Operating expenses	(6,551.8)	(9.1)	(11,602.0)	(13.0)	(11,974.3)	(13.7)
Segment profit	14.1	0.0	15.0	0.0	46.4	0.1
<b>Others</b>						
Net sales	783.1	1.0	950.5	1.1	882.1	1.0
Operating expenses	(765.7)	(1.0)	(914.2)	(1.0)	(843.9)	(1.0)
Segment profit	17.4	0.0	36.3	0.1	38.2	0.0
<b>Total</b>						
Net sales	72,095.9	100.0	89,509.7	100.0	87,217.3	100.0
Operating expenses	(69,132.3)	(95.9)	(88,449.9)	(98.8)	(88,989.7)	(102.0)
Profit/(loss) from operations	2,963.6	4.1	1,059.8	1.2	(1,772.4)	(2.0)
Net financing (costs)/income	(95.2)	(0.1)	83.5	0.1	(283.3)	(0.3)
Investment income	0.2	0.0	0.7	0.0	6.4	0.0
Share of profit of associates and jointly controlled entities	661.3	0.9	152.7	0.1	32.8	0.0
Earnings/(loss) before income tax	3,529.9	4.9	1,296.7	1.4	(2,016.5)	(2.3)
Income tax	(735.5)	(1.0)	(310.2)	(0.3)	511.4	0.6

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Net income/(loss)	2,794.4	3.9	986.5	1.1	(1,505.1)	(1.7)
<b>Attributable to:</b>						
Equity shareholders of the Company	2,769.0	3.8	956.1	1.0	(1,528.4)	(1.8)
Non-controlling interests	25.4	0.1	30.4	0.1	23.3	0.1
Net income/(loss)	2,794.4	3.9	986.5	1.1	(1,505.1)	(1.7)

Net sales represent sales revenue of the respective segments after sales taxes and surcharges. Operating expenses represent cost of sales, selling and administrative expenses and other operating expenses /income, as allocated to respective segments.

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**Table of Contents*****A. Results of Operations***

In 2012, we witnessed a sluggish recovery of the global economy, an economic downturn in the developed countries, a general slowdown of the economic growth in the emerging economies and a significant decline in the growth of international trade. Conditions were further complicated by the severe volatility in the prices of major commodities and ups and downs in the global financial market. The world's petrochemical industry stayed at a relatively low stage of the cycle marked by a slower rate of growth in the demand for petrochemical products and diminishing gross profits in the industry. Economic growth in China was slowing down while remaining stable due to the policy of maintaining growth and adjusting the structure of the economy. China recorded an annual GDP growth of 7.8%, which suggests a further slowdown in the growth of economy. The operation of China's petrochemical industry remained steady in general, albeit with a decline in its growth rate. The overall profitability across the industry declined significantly, due to a number of factors such as increased downward pressure on the economy growth, weakened growth in demand, high business costs, excessive growth of capacity expansion, and intensified competition in the market of homogeneous goods.

In 2012, the international market price of crude oil fluctuated violently at high levels, which resulted in the increase of our operating costs. The Company's oil refining business suffered losses due to the State policy related factors. The prices of petrochemical products fell sharply, and the output decreased due to the maintenance of certain production facilities. The foregoing contributed to a substantial loss of RMB1,528.4 million attributable to our shareholders for 2012.

In 2012, our turnover amounted to RMB93,008.3 million, representing a decrease of 2.63% from 2011. Our production/sale ratio was 100.06%, the receivable recovery rate was 100.05%. Our total amount of import and export was U.S.\$9,016 million, representing an increase of 18.40% from 2011.

*Year ended December 31, 2012 compared with year ended December 31, 2011*

***Net sales***

Against the backdrop of the slackened economic growth at home and abroad in 2012, the overall operation of the petrochemical industry tended to decline. The excessively expanded production capacity of bulk petrochemical products and the declined rate of growth in the demand in domestic and international markets led to a more intense market competition and a substantial fall in the market prices of petrochemical products. Domestic oil consumption continued to grow while the supply of refined oil products could easily satisfy the consumption demand. In 2012, our net sales amounted to RMB87,217.3 million, representing a decrease of 2.56% from RMB89,509.7 million in 2011. For the year ended December 31, 2012, the weighted average prices (excluding tax) of our synthetic fibers, resins and plastics, and intermediate petrochemical products decreased by 20.92%, 9.98%, and 3.81%, respectively, over the previous year, while the weighted average price (excluding tax) of petroleum products increased by 3.24%.

***(i) Synthetic fibers***

In 2012, the net sales of synthetic fibres amounted to RMB3,313.3 million, representing a decrease of 20.17% compared to RMB4,150.2 million in the previous year. The weighted average sales price of synthetic fibres decreased by 20.92% as compared to the previous year. In particular, the weighted average sales prices of acrylic fibre and polyester fibre, the principal products of synthetic fibres, decreased by 23.54% and 16.66% over the previous year, respectively. The sales of acrylic fibre and polyester fibre accounted for 74.66% and 19.01% of the total sales of synthetic fibres, respectively.

Net sales of synthetic fibre products accounted for 3.80% of total net sales in 2012, representing a decrease of 0.80 percentage points as compared to the previous year.

***(ii) Resins and plastics***

The net sales of resins and plastics amounted to RMB14,706.3 million in 2012, representing a decrease of 10.43% as compared to RMB16,418.6 million in 2011, which is mainly driven by a 9.98% decrease of the weighted average sales prices of resins and plastics in 2012. Among resins and plastics products, the weighted average sales price of polyethylene for 2012 decreased by 6.68%; the weighted average sales price of polypropylene for 2012 decreased by 8.15%; the weighted average sales price of polyester pellet for 2012 decreased by 16.35%. The sales of polyethylene, polypropylene and polyester pellet accounted for 38.01%, 29.29% and 28.57% of the total sales of resins and plastics, respectively.



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The net sales of resins and plastics accounted for 16.86% of total net sales in 2012, representing a decrease of 1.44 percentage points as compared to the previous year.

### *(iii) Intermediate petrochemicals*

The net sales of intermediate petrochemical products amounted to RMB17,993.5 million in 2012, representing a decrease of 5.41% as compared to RMB19,023.2 million in 2011, with the weighted average sales price of intermediate petrochemical products decreased by 3.81% as compared to the previous year while the sales volume decreased by 1.67%. Among the intermediate petrochemical products, weighted average sales prices of paraxylene, butadiene and ethylene glycol decreased by 5.25%, 12.22% and 13.90%, respectively, while the weighted average sales price of benzene increased by 10.32%. The sales of paraxylene, butadiene, ethylene glycol and benzene accounted for 32.19%, 11.83%, 10.46% and 16.16% of the total sales of intermediate petrochemical products, respectively.

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The net sales of intermediate petrochemical accounted for 20.63% of total net sales in 2012, representing a decrease of 0.67 percentage points as compared to the previous year.

### *(iv) Petroleum products*

The net sales of petroleum products amounted to RMB38,301.4 million in 2012, representing an increase of 2.55% as compared to RMB37,350.2 million in the previous year. The weighted average sales price increased by 3.24%, while the sales volume decreased by 0.68%.

The net sales of petroleum products accounted for 43.92% of total net sales in 2012, representing an increase of 2.22 percentage points as compared to the previous year.

### *(v) Trading of petrochemical products*

The net sales of the trading of petroleum products amounted to RMB12,020.7 million in 2012, representing an increase of 3.48% as compared to RMB11,617.0 million in the previous year. Such increase in the net sales was mainly attributable to a slight increase in the trading volume of petrochemical products as compared to the previous year.

The net sales of trading of petrochemical products accounted for 13.78% of total net sales in 2012, representing an increase of 0.78 percentage points as compared to the previous year.

### *(vi) Others*

The net sales of others amounted to RMB882.1 million in 2012, representing a decrease of 7.20% as compared to RMB950.5 million in the previous year. Such decrease in the net sales was mainly attributable to a decrease in our business of crude oil processed on a sub-contract basis.

The net sales of others accounted for 1.01% of the Company's total net sales in 2012, basically at par with the previous year.

## ***Operating expenses***

Our operating expenses consist of cost of sales, selling and administrative expenses, other operating expenses and other operating income.

Our operating expenses were RMB88,989.7 million in 2012, representing a slight increase as compared to RMB88,449.9 million in 2011. Our operating expenses of petroleum products in 2012 were RMB39,294.4 million, representing an increase of 3.94% as compared to the previous year, primarily due to an increase of 3.56% in the average unit cost of crude oil processed. Our operating expenses of the trading of petrochemical products in 2012 were RMB11,974.3 million, representing an increase of 3.21% as compared to the previous year, primarily due to a slight increase in the trading volume of petrochemical products as compared to the previous year. Our operating expenses of synthetic fibres, resins and plastics, intermediate petrochemicals and others in 2012 amounted to RMB3,718.6 million, RMB15,997.7 million, RMB17,160.8 million, and RMB843.9 million, representing a decrease of 3.39%, 2.49%, 3.99%, and 7.69% as compared to the previous year, respectively, which was primarily due to decreases in both the sales volume and prices of certain petrochemical raw materials.

### ***Cost of sales***

Our cost of sales amounted to RMB88,617.8 million in 2012, basically as par with RMB87,881.2 million in 2011. Cost of sales accounted for 101.61% of the net sales for 2012.

### ***Selling and administrative expenses***

Our selling and administrative expenses amounted to RMB649.9 million in 2012, representing a decrease of 3.83% as compared to RMB675.8 million in the previous year, mainly due to a decrease in sales agency fees with respect to sales to Sinopec Chemical Commercial Holding Company Limited in line with the decrease in sales volume.

***Other operating income***

Our other operating income amounted to RMB333.8 million in 2012, representing an increase of 103.16% as compared to RMB164.3 million in the previous year, mainly due to an increase of RMB144.1 million of government grants recognized in profit or loss after fulfilling the conditions in 2012 as compared to the previous year.

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### ***Other operating expenses***

Our other operating expenses were RMB55.8 million in 2012, basically at par with RMB57.2 million in 2011.

### ***Profit/loss from operations***

Our loss from operations amounted to RMB1,772.4 million in 2012, as compared to profit from operations of RMB1,059.8 million in the previous year. Below are the major reasons for the loss.

In 2012, the domestic prices of refined oil products were not brought into line with the prices of crude oil on the international markets in a timely manner due to various policy concerns, *e.g.*, the government's desire to control the high inflation rate in China, which resulted in a decline of RMB539.7 million of the operating profit of our refining business over the previous year.

The operation of our petrochemical business suffered a loss of RMB864.0 million, representing a decrease in profit of RMB2,325.9 million compared to the previous year. The loss in our petrochemical business was mainly attributable to the slackened growth of domestic demand, the excessive expansion of production capacity, the sluggish market, the further intensified market competition and the substantial fall in the prices of petrochemical products.

### ***Net financing costs/income***

Our net financing costs were RMB283.3 million in 2012, while there was a net financing income of RMB83.5 million in 2011. The change was mainly due to a decrease of RMB213.4 million in net foreign exchange income during the reporting period as compared to the previous year resulting from the stability in the US Dollar to Renminbi exchange rate. Furthermore, a substantial amount of new borrowings was made by the Company, resulting in an increase of RMB140.6 million in interest expense.

### ***Share of profit of associates and jointly controlled entities***

In 2012, the Company's share of profit of associates and jointly controlled entities amounted to RMB32.8 million (2011: share of profit of RMB152.7 million), representing a decrease of 78.52%, among which, the share of loss of Secco amounted to RMB75.3 million (2011: share of profit of RMB9.8 million).

### ***Earnings/loss before income tax***

Our loss before income tax was RMB2,016.5 million in 2012, as compared to earnings before income tax of RMB1,296.7 million in the previous year.

### ***Income tax***

Our income tax credit was RMB511.4 million in 2012, while the Company's income tax expense was RMB310.2 million in the previous year. The change was primarily attributable to the deferred assets recognized in respect of the unused tax loss generated by the Company in 2012. The effective tax rate (excluding the share of profit of associates and jointly controlled entities) was 25.0% (2011: 27.1%).

In accordance with the PRC Enterprise Income Tax Law (as amended) which took effect from 1 January 2008, the income tax rate of the Company in 2012 was 25% (2011: 25%).

### ***Net income/loss***

Our net loss was RMB1,505.1 million in 2012, as compared to net income of RMB986.5 million in the previous year.

*Year ended December 31, 2011 compared with year ended December 31, 2010*

### ***Net sales***

In 2011, our net sales amounted to RMB89,509.7 million, representing an increase of 24.15% from RMB72,095.9 million in 2010. For the year ended December 31, 2011, the weighted average prices (excluding tax) of our synthetic fibers, resins and plastics, intermediate petrochemical

products and petroleum products increased by 8.35%, 12.23%, 17.44% and 18.32%, respectively, over the previous year. The net sales of the trading of petrochemical products amounted to RMB11,617.0 million in 2011, representing an increase of 76.93% as compared to RMB6,565.9 million in the previous year.

*(i) Synthetic fibers*

In 2011, the net sales of synthetic fiber products amounted to RMB4,150.2 million, representing a 6.24% increase from RMB3,906.6 million in the previous year. The weighted average price of synthetic fibers increased by 8.35% over the previous year. In particular, the weighted average prices of acrylic fiber and polyester fiber, the principal product of synthetic fiber of the Company, increased by 5.78% and 20.31% over the previous year, respectively. The sales of acrylic fiber and polyester fiber accounted for 74.67% and 19.78% of the total sales of synthetic fibers respectively.

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Net sales of synthetic fiber products accounted for 4.60% of our total net sales in 2011, representing a decrease of 0.80 percentage point as compared to the previous year.

### *(ii) Resins and plastics*

The net sales of resins and plastics amounted to RMB16,418.6 million in 2011, representing an increase of 10.19% from RMB14,900.0 million in 2010. The weighted average price of resins and plastics in 2011 increased by 12.23%, while the sales volume in 2011 decreased by 1.82%. Among resins and plastics products, the weighted average price of polyethylene increased by 7.03% and sales volume decreased by 2.57%, and the weighted average price of polyester pellet for 2011 increased by 22.34% and sales volume decreased by 0.02%. The sales of polypropylene and polyester pellet accounted for 36.02% and 31.49% of the total sales of resins and plastics respectively.

Net sales of resins and plastics accounted for 18.30% of our total net sales in 2011, representing a decrease of 2.40 percentage points as compared to the previous year.

### *(iii) Intermediate petrochemicals*

The net sales of intermediate petrochemical products amounted to RMB19,023.2 million in 2011, representing an increase of 10.56% from RMB17,206.4 million in 2010, with the weighted average price of intermediate petrochemical products increased by 17.44% and sales volume decreased by 5.86% as compared to the previous year. Among the intermediate petrochemical products, the weighted average prices of paraxylene, butadiene and benzene increased by 31.33%, 30.50% and 11.57%, respectively. The sales of paraxylene, butadiene and benzene accounted for 34.70%, 11.74% and 14.28% of the total sales of intermediate petrochemical products, respectively.

Net sales of intermediate petrochemical accounted for 21.30% of our total net sales in 2011, representing a decrease of 2.60 percentage points as compared to the previous year.

### *(iv) Petroleum products*

The net sales of petroleum products amounted to RMB37,350.2 million in 2011, representing an increase of 29.99% from RMB28,733.9 million in the previous year, with the weighted average product prices increased by 18.32% and sales volume increased by 9.86% as compared to 2010. Due to the impact of an increase in demand from the domestic market, the market demand for diesel and gasoline increased as compared to the previous year which led to increases of 13.72% and 2.25% in the Company's sales volume of diesel and gasoline respectively. The increase in our sales in 2011 was also in part due to the production of Shanghai IV refined oil and the introduction of 30,000 tons of Euro V diesel to the Hong Kong market. The sales of diesel and gasoline accounted for 59.90% and 17.78% of the total sales of petroleum products respectively.

Net sales of petroleum products accounted for 41.70% of our total net sales in 2011, representing an increase of 1.80 percentage points as compared to the previous year.

### *(v) Trading of petrochemical products*

The net sales of the trading of petrochemical products amounted to RMB11,617.0 million in 2011, representing an increase of 76.93% as compared to RMB6,565.9 million in the previous year. Such increase in the net sales was mainly attributed to a significant increase in the trading volume of petrochemical products as compared to the previous year.

Net sales of the trading of petrochemical products accounted for 13.00% of our total net sales in 2011, representing an increase of 3.90 percentage points as compared to the previous year.

### *(vi) Others*

The net sales of other activities amounted to RMB950.5 million in 2011, representing an increase of 21.38% as compared to RMB783.1 million in the previous year. Such increase in the net sales was mainly attributed to the expansion in the processing-on-sub-contract business as compared to the previous year.

Net sales of others accounted for 1.10% of our total net sales in 2011, basically at par with the previous year.



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### ***Operating expenses***

Our operating expenses are comprised of cost of sales, selling and administrative expenses, other operating expenses and other operating income.

Our operating expenses increased by RMB19,317.6 million, or 27.94%, from RMB69,132.3 million in 2010 to RMB88,449.9 million in 2011. The operating expenses of synthetic fibers, resins and plastics, intermediate petrochemicals, petroleum products, trading of petrochemical products and others amounted to RMB3,848.9 million, RMB16,406.6 million, RMB17,874.6 million, RMB37,803.6 million, RMB11,602.0 million and RMB91,420.0 million, representing an increase of 10.89%, 17.96%, 6.14%, 37.00%, 77.08% and 19.39% as compared to the previous year, respectively.

#### ***(i) Synthetic fibers***

The operating expenses of synthetic fibers in 2011 increased by RMB377.9 million as compared to the previous year, which was primarily due to increased unit prices for raw materials (*e.g.*, acrylonitrile) for producing synthetic fibers.

#### ***(ii) Resins and plastics***

Our operating expenses of resins and plastics in 2011 increased by RMB2,497.7 million as compared to the previous year, which was primarily due to increased unit costs for raw materials such as ethylene and propylene.

#### ***(iii) Intermediate petrochemicals***

The operating expenses of intermediate petrochemicals in 2011 increased by RMB1,033.3 million as compared to the previous year. The significant increase in costs and expenses of intermediate petrochemical products was attributable to the increase in unit cost of intermediate petrochemical products along with the increase in average unit cost of crude oil during 2011.

#### ***(iv) Petroleum products***

The operating expenses of petroleum products in 2011 increased by RMB10,210.0 million as compared to the previous year, primarily due to the increase in crude oil prices (which was the major raw material of the Company) and increased processing volume.

#### ***(v) Trading of petrochemical products***

The operating expenses of trading of petrochemical products in 2011 increased by RMB5,050.2 million as compared to the previous year, primarily due to the significant increase in the Company's trading volume of petrochemical products as compared to the previous year.

#### ***(vi) Other activities***

The operating expenses of other activities in 2011 increased by RMB148.5 million as compared to the previous year, primarily due to an increase in the cost of crude oil processed on a sub-contract basis.

### ***Cost of sales***

The cost of sales amounted to RMB87,881.2 million in 2011, representing a significant increase of 28.64% compared to RMB68,317.4 million in 2010. Cost of sales accounted for 98.18% of the net sales for 2011, primarily due to an increase in crude oil prices in 2011 which was the Company's major raw material.

### ***Selling and administrative expenses***

Selling and administrative expenses amounted to RMB675.8 million in 2011, representing an increase of 7.47% from RMB628.8 million in the previous year, primarily due to an increase in sales related transportation expenses as a result of increased sales volume of the Company in 2011.



and an increase in agency fees with respect to sales to Sinopec Chemical Commercial Holding Company Limited.

***Other operating income***

Other operating income amounted to RMB164.3 million in 2011, representing an increase of 49.64% from RMB109.8 million in the previous year, primarily due to an increase of RMB39.8 million in the government subsidies received in 2011 as compared to the previous year.

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### ***Other operating expenses***

Other operating expenses decreased from RMB296.0 million in the previous year to RMB57.2 million in 2011, representing a decrease of 80.68%, mainly due to a decrease of RMB227.6 million in the Company's impairment losses of fixed assets in 2011 as compared to the previous year.

### ***Profit from operations***

Profit from operations amounted to RMB1,059.8 million in 2011, representing a decrease of RMB1,903.8 million as compared to RMB2,963.6 million in the previous year. In particular, the operating profit of our refining business decreased by RMB1,593.6 million over the previous year, because the domestic prices of refined oil products were not brought into line with the prices of crude oil on the international markets in a timely manner due to various policy concerns, e.g., the high inflation rate in China. In addition, the operating profit of the Company's petrochemical business decreased by RMB329.9 million as compared to the previous year, which is attributable to the decline in the prices of petrochemical products since the fourth quarter of 2011 and the intensifying market competition.

### ***Net financing income***

Our net financing income was RMB83.5 million in 2011, while the net financing costs of 2010 amounted to RMB95.2 million. The change was primarily attributable to an increase of RMB58.6 million in net foreign exchange gain of the Company in 2011, a decrease of RMB58.2 million in interest expenses, and an increase of RMB62.0 million in interest income as compared to the previous year.

### ***Investment income***

Our investment income was RMB0.7 million in 2011. In 2010 our investment income was RMB0.2 million. Our investment income represents gain on disposal of available-for-sale financial assets.

### ***Earnings before income tax***

Our earnings before income tax were RMB1,296.7 million in 2011, representing a decrease of RMB2,233.2 million as compared to RMB3,529.9 million in the previous year.

### ***Income tax***

Our income tax expense was RMB310.2 million in 2011, representing a decrease of RMB425.3 million from RMB735.5 million in the previous year. The change was in line with the decrease on taxable income. The effective tax rate (excluding the share of profit of associates and jointly controlled entities) was 27.1% (2010: 25.6%). The difference with the statutory tax rate of 25.0% mainly included permanent tax differences such as the non-deductible staff welfare and entertainment expenses.

In accordance with the PRC Enterprise Income Tax Law (as amended) which took effect from 1 January 2008, the income tax rate of the Company in 2011 was 25% (2010: 25%).

### ***Net income***

Our net income was RMB986.5 million in 2011, representing a decrease of RMB1,807.9 million from RMB2,794.4 million in the previous year.

## ***B. Liquidity and Capital Resources.***

We strive to have sufficient liquidity at all times to meet our liabilities when due, preparing for both normal and stressed conditions, without incurring unacceptable losses or risking damage to our reputation.

Our primary sources of funding have been cash provided by our operating activities, short term and long term loans. Our primary uses of cash have been for cost of sales, other operating expenses and capital expenditures. We prepare monthly cash flow budgets to ensure that we will always have sufficient liquidity to meet our financial obligations as they become due. We arrange and negotiate financing with financial institutions and maintain a certain level of standby credit facilities to reduce liquidity risk. We believe that our current cash on hand, expected cash flows from operations and available standby credit facilities from financial institutions will be sufficient to meet our working capital requirements and repay our short term debts and obligations when they become due. In addition, we will continue to optimize our fund raising

strategy from short and long term perspectives to take advantage of low interest rates by issuing corporate bonds or debts with low financing costs.

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The following table sets forth a condensed summary of our consolidated statement of cash flows for the year ended December 31, 2011 and 2012.

Cash flow data	Year Ended December 31,	
	2011	2012
	(Millions of RMB)	
Net cash generated from/(used in) operating activities	2,220.0	(2,066.4)
Net cash used in investing activities	(2,810.2)	(4,062.1)
Net cash generated from financing activities	581.8	6,198.1
Net (decrease)/increase in cash and cash equivalents	(8.4)	69.6

***Net cash generated from/used in operating activities***

The net cash used in operating activities amounted to RMB2,066.4 million in 2012, representing a decrease in cash inflows of RMB4,286.4 million as compared to the net cash inflows of RMB2,220.0 million in the previous year, due to: (i) affected by the decline in our profit from operations during the reporting period, net cash outflows from loss before taxation (net of depreciation and impairment losses on property, plant and equipment) amounted to RMB333.4 million in 2012, representing a decrease of RMB3,264.4 million of cash inflows compared to net cash inflows of RMB2,931.0 million in the previous year; (ii) our increased inventory balance led to a decrease in operating cash inflow of RMB3,366.0 million in 2012 (as compared to a decrease in operating cash inflow of RMB230.1 million due to increased inventory balance at the end of the previous year); (iii) decreases in the balances of debtors, bills receivable and prepayments led to an increase in operating cash inflow of RMB992.2 million in 2012 (as compared to a decrease in operating cash inflow of RMB1,015.4 million as a result of increases in such year-end balances of the previous year).

***Net cash used in investing activities***

Our net cash used in investing activities increased from RMB2,810.2 million in 2011 to RMB4,062.1 million in 2012. This was primarily due to (i) an increase in capital expenditure of RMB778.6 million, and (ii) a decrease in dividend income received of RMB521.2 million.

***Net cash generated from financing activities***

Our net cash generated from financing activities was RMB6,198.1 million in 2012, while our net cash generated from financing activities was RMB581.8 million in 2011. This was primarily due to the increase in cash inflow of RMB18,259.2 million in proceeds from loans and borrowings and a decrease in cash outflow in dividends paid of RMB345.4 million, offset by an increase in cash outflow of RMB12,988.3 million in repayment of loans, borrowing and corporate bonds.

***Borrowings and banking facilities***

Due to the Company's net loss and the increasing capital expenditure for the implementation of Phase 6 Project, the Company had to take on an increased amount of borrowings in 2012 in order to maintain the balance of cash and cash equivalents at a safe level. Our total borrowing at the end of 2012 amounted to RMB12,255.2 million, representing an increase of RMB6,583.1 million as compared to the end of the previous year, of which short term debts increased by RMB5,511.8 million, and long term debts increased by RMB1,071.3 million. We have generally been able to arrange short term loans with several PRC financial institutions as necessary. The debt obligations, as of December 31, 2011 and 2012 were as follows.

Debt instruments	Year Ended December 31,	
	2011	2012
	(Millions of RMB)	
Short term bank loans (1)	4,852.1	10,803.9
Short term loans from a related party (2)	660.0	220.0
Long term bank loans (1)	160.0	1,231.3
	5,672.1	12,255.2

- (1) As of December 31, 2012, no loans and borrowings were secured by the way of property, plant and equipment. We obtained a credit rating of AA- for financing loans, assessed by Centrus Business Credit Consulting Co., Ltd, a credit rating agency authorized by the People's Bank of China. As of December 31, 2012, we had standby credit facilities of RMB18,196.0 million, which are effective until the end of 2013. Out of the total banking facilities granted, amounts totaling RMB7,850.0 million was unutilized as of December 31, 2012. We believe that we will be able to renew these facilities when they expire based on our well-established relationships with various lenders.
- (2) We borrowed short term loans from a subsidiary of Sinopec Group, Sinopec Finance Company Limited, on terms no less favorable to us than terms available from the other commercial banks in China. We have entered into the Comprehensive Services Framework Agreement with Sinopec Group so as to obtain financial services from Sinopec Finance Company Limited for the three years ending December 31, 2011, 2012 and 2013.

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Our ability to renew our short term loans and obtain additional external financing in the future and the cost of such financing are subject to a variety of uncertainties, including:

the cost of financing and the condition of financial markets;

our future operating performance, financial condition and cash flows; and

potential changes in monetary policy of the Chinese government with respect to bank interest rates and lending practices.

If we fail to rollover, extend or refinance our short term debts as necessary in a timely manner, we may be unable to meet our obligations in connection with debt servicing, trade and bills payable and/or other liabilities when they become due. See also Item 3. Key Information D. Risk Factors - Our development and operation plans have significant capital expenditure and financing requirements, which are subject to a number of risks and uncertainties.

In light of our good credit standing and various financing channels, we believe that we will not experience any difficulty in obtain sufficient financing for our operations.

We managed to maintain our asset-liability ratio at a safe level by enhancing controls over both liabilities (including borrowings) and financing risks. We generally do not experience any seasonality in borrowings. However, due to the nature of the capital expenditures plan, long term bank loans can be arranged in advance of expenditures while short term borrowings are used to meet operational needs. The terms of our existing borrowings do not restrict its ability to pay dividends on its shares.

**Liability-to-asset ratio**

As at December 31, 2012, our liability-to-asset ratio was 55.29% (2011: 40.77%). The ratio is calculated by dividing total liabilities by total assets.

**Capital expenditure**

In 2012, our capital expenditure amounted to RMB3,811.0 million, representing an increase of 18.17% as compared to RMB3,225.0 million in capital expenditure in 2011. Major projects include the following:

<b>Project</b>	<b>Total project investment RMB million</b>	<b>Project progress as at December 31, 2012</b>
The Refinery Revamping and Expansion Project	6,267.0	Completion and commencement of operation
The Carbon Fiber Project with a capacity of 1,500 tons/year	848.0	Phase I completed and commencement of trial operation
The Up-grading Project for the optimization of the system and reduction in energy and feedstock consumption of the No. 2 PTA Plant	186.0	Completion and commencement of operation
The No.5 and No. 6 Furnace Secondary Desulfurisation Project for Department of Thermoelectric	129.0	Completion and commencement of operation
	954.0	Under construction

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The No. 2 and No. 3 Aromatics Complexes  
Energy-saving Up-grade Project

The SL-2 Cracking Furnace of No. 2 Ethylene  
Unit Transformation for Improving Energy  
Efficiency

115.0

Under construction

Total

8,499.0

Our capital expenditure for 2013 is estimated at approximately RMB2,600.0 million.

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### *C. Research and Development, Patents and Licenses, etc.*

We have a number of technology development units, including the Petrochemical Research Institute, the Plastics Research Institute, the Polyester Fiber Research Institute, the Acrylic Fiber Research Institute and the Environmental Protection Research Institute. These units are charged with various research and development tasks with respect to new technology, new products, new production processes and equipment and environmental protection. Our research and development expenditures in 2010, 2011 and 2012 were RMB58.2 million, RMB79.6 million and RMB72.2 million, respectively, all representing approximately 0.1% of the total sales for each of those years.

In 2012, the Company engaged in the technical development of new products and developed a batch of new products such as polyethylene specialized materials with a high crystallization rate for heat shrinkable films, moisture absorbing and quick-drying polyester, and superfine antipilling acrylic. The Company strived to adjust its product mix and to increase the production of various high value-added products such as ternary random copolypropylene and binary random polypropylene. The high-performance PBO fiber project and industrial tests on the treatment of ethylene glycol wastewater using large biological fluidized bed have passed their examinations. Significant achievements were made in the industrial applications of YS-8810 silver catalysts. A total of 400,900 tons of new products were produced during the year, with a total product differential rate of 59.26%. A total of 44 patent applications were submitted and 10 patent licenses were awarded. Shanghai Municipal Government granted us special financial supports with an aggregate amount of RMB21.4 million with regard to 15 new and high-tech achievement projects.

The Company continued to push forward the construction of its information system and increase the level of informationization. The APC for four plants Coking Plant 2, Acrylonitrile Plant, Polyester Plant 1 and Polyester Plant 2 was completed and put into operation. The establishment of a process simulation system for three plants the residue hydrogenation, catalytic cracking and gasoline adsorptive desulfurization plants was completed. The scope of implementation and application of the ERP system was extended to the whole Company. The application of information systems such as APC, HR and EM was further enhanced. The Company maintains a leadership in the industry in this regard.

We are not, in any material aspect, dependant on any patents, licenses, industrial, commercial or financial contracts, or new production processes.

### *D. Trend Information*

In 2013, the world economy will remain complex and challenging and will face increasing uncertainty, characterized by an obvious emergence in various forms of protectionism, and the increasing pressure of the potential inflation and asset bubbles. The world economy has entered into a period of intensive transformation and adjustment from a period of rapid growth before the world economic recession hits and continues to grow slowly. China's economy is still in an important strategic period with opportunities. China will maintain the general macro-economic control policy featured by promoting growth while ensuring stability, continue to implement the proactive fiscal policy and the prudent monetary policy, and boost the domestic demand. China's economy is expected to maintain a stable growth.

The development landscape of the worldwide petrochemical industry is undergoing major changes as the industry will be greatly affected by the reduction of costs of energy resources and chemical raw materials as a result of the large-scale development of shale gas in North America and the challenges to the traditional petrochemical industry posed by the development of the coal chemical industry. The competition in the petrochemical industry will be further intensified. The outlook of the international crude oil price is uncertain, which is attributable to various factors, including the uncertainties with regard to the international crude oil market and the international economic growth, the change of oil supply pattern, and social and civil unrest in the West Asia and the North Africa. The demand of energy resources may continue to decline due to the European debt crisis and the slow recovery of American economy. The crude oil prices may remain at high levels due to the geopolitical risks in the Middle East intertwine with the worldwide relaxing currency policies. The overall demand and supply structure of the international crude oil market is expected to be stable. Overall, China's domestic consumer market will maintain stable growth. The market demand for energies and major bulk chemicals will increase and the investment in the petrochemical industry will continue to enjoy a fast growth. The operation of the petroleum and chemical industries is expected to maintain stable overall, and will pick up growth momentum as part of a steady and positive development trend.

### *E. Off-balance Sheet Arrangements*

As of December 31, 2012, we had no contingent liabilities in respect of guarantees issued to banks in favor of our associated companies and other unlisted investments (December 31, 2011: nil). Other than our capital commitments and contingencies disclosed in Note 23 in our consolidated financial statements included in [Item 17. Financial Statements](#), we do not have any other off-balance sheet arrangements.





**Table of Contents***F. Contractual Obligations and Commercial Commitments*

The following table sets forth our obligations to make future payments under contracts effective as of December 31, 2012.

	As of December 31, 2012 Payment Due by Period				
	Total (RMB 000)	Within 1 year or on demand (RMB 000)	More than 1 year but within 2 years (RMB 000)	More than 2 years but within 5 years (RMB 000)	More than 5 years (RMB 000)
<b>Contractual obligations</b>					
Short term loans	11,023,877	11,023,877			
Long term loans	1,231,340		370,560	860,780	
Total contractual obligations	12,255,217	11,023,877	370,560	860,780	
<b>Estimated future interest payments</b>					
Fixed rate	57,300	57,300			
Variable rate <sup>(1)</sup>	201,251	103,554	57,738	39,959	
<b>Total estimated future interest payments</b>	<b>258,551</b>	<b>160,854</b>	<b>57,738</b>	<b>39,959</b>	
<b>Other commercial commitments</b>					
Capital commitments <sup>(2)</sup>	1,485,573	1,485,573			
Total commercial commitments	1,485,573	1,485,573			

(1) The average interest rates for variable rate loans are calculated based on the year end indices.

(2) Capital commitments refer to commitments for purchase of property, plant and equipment.

*G. Other Information***Employees**

Our staff costs for 2012 were RMB1,740.2 million.

As at December 31, 2012, we had 15,007 employees in total, among whom there were 8,689 production staff, 4,701 sales representatives, financial personnel and other personnel and 1,617 administrative staff. 41.33% of our employees had tertiary qualifications or above. The company has 14,910 retired employees who are under retirement insurance plans, details of which are provided under Item 6. D. Employees. As of December 31, 2012, we have terminated employment with 648 persons (including the retired and voluntary leave), accounting for 4.14% of 15,655 employees we had as of January 1, 2012.

**Purchase, Sale and Investment**

Except as disclosed in this report, during the year ended December 31, 2012, we engaged in no material purchase or sale of our subsidiaries or associated companies or any other material investments.

**Pledge of Assets**

As of December 31, 2012, we had not pledged any of our property or equipment.



**Table of Contents****ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES.****A. Directors and Senior Management.**

The following table sets forth certain information concerning our directors, executive officers and members of our supervisory committee (Supervisory Committee). The current term for our directors, executive officers and members of our Supervisory Committee is three years, which term will end in June 2014.

<b>Name</b>	<b>Age</b>	<b>Position</b>
<u>Directors</u>		
Wang Zhiqing (1)	50	Vice Chairman of the Board of Directors and President
Wu Haijun	50	Vice Chairman of the Board of Directors
Li Honggen	56	Director and Vice President
Ye Guohua	44	Director and Chief Financial Officer
Lei Dianwu	50	External Director
Xiang Hanyin	58	External Director
Shen Liqiang	56	Independent Director
Jin Mingda	62	Independent Director
Wang Yongshou	72	Independent Director and Director of the Remuneration and Appraisal Committee
Cai Tingji	58	Independent Director and Director of the Audit Committee
<u>Other Executive Officers</u>		
Shi Wei	53	Vice President
Zhang Zhiliang	59	Vice President
Zhang Jianping	50	Vice President
Jin Qiang	47	Vice President
Gao Jinping	46	Vice President
Guo Xiaojun	43	Vice President
Zhang Jingming	55	Secretary of the Company and General Legal Counsel
<u>Supervisory Committee</u>		
Zuo Qiang	50	Supervisor
Li Xiaoxia	43	Supervisor
Zhai Yalin	48	External Supervisor
Wang Liqun	55	External Supervisor
Chen Xinyuan	48	Independent Supervisor
Zhou Yunnong	70	Independent Supervisor

(1) Mr. Wang Zhiqing was nominated by the board of directors of the Company as the Chairman of the Board of Directors in the board meeting on April 19, 2013. The nomination will need to be reviewed and approved by the Company's 2012 general shareholders meeting on June 6, 2013. Mr. Wang Zhiqing will perform the duties and powers of the Chairman of the Board of Directors before the nomination is approved.

*Directors*

**Wang Zhiqing**, 50, currently Vice Chairman, President and Deputy Secretary of the Communist Party Committee of the Company. Mr. Wang was appointed as a member of and nominated as the Chairman of the board and as the Chairman of the Nomination Committee of the Company in the board meeting on April 19, 2013. His nomination as the Chairman of the board and as the Chairman of the Nomination Committee needs to be reviewed and approved by the Company's 2012 general shareholders meeting on June 6, 2013. Mr. Wang commenced work in 1983 and held various positions including Deputy Leader of preparatory team for the chemical fiber plant of Luoyang Petrochemical Complex, Deputy Chief Engineer of Luoyang Petrochemical Complex cum Officer-in-Charge of the preparatory team for the complex's chemical fiber plant, and then Deputy Chief Engineer of the complex cum Director of the chemical fiber plant. From June 1999 to December 2001, Mr. Wang was Chief Engineer of Luoyang Petrochemical Complex. From February 2000 to December 2001, Mr. Wang was Vice President cum Chief Engineer of Sinopec Luoyang Company. From December 2001 to October 2006, Mr. Wang was President of Sinopec Luoyang Company. From July 2005 to May 2007, Mr. Wang was the Leader of the preparatory team for a Sinopec refinery project in Guangxi. From October 2006 to December 2008, Mr. Wang was President of Sinopec Jiujiang Company. From December 2008 to July 2010, Mr. Wang was President of Sinopec Jiujiang Company. Mr. Wang was appointed President and Deputy Secretary of the Communist Party Committee of the Company in July 2010. Mr. Wang was appointed Director and Vice Chairman of the Company in December 2010. In February 2011, Mr. Wang was appointed the Director and Chairman of the board of Secco. Mr. Wang graduated from the East China Petroleum Institute with a Bachelor of Engineering in

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1983, majoring in refinery engineering, and graduated from China University of Petroleum (East China) with a Doctorate in Engineering in 2006, majoring in chemical engineering and technology. He is a senior engineer by professional title.

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**Wu Haijun**, 50, currently Vice Chairman of the Company, Director and Vice President of Secco. Mr. Wu joined the Complex in 1984 and held various positions including Deputy Director and Director of the Company's No.2 Chemical Plant as well as manager of the Chemical Division. He was Vice President of the Company from May 1999 to March 2006 and Director of the Company from June 2004 to June 2006. He was manager and Secretary of the Communist Party Committee of the Chemical Sales Branch Office of Sinopec Corp. from December 2005 to March 2008. From December 2005 to April 2010, he was Director of the Chemical Business Department of Sinopec Corp. In April 2010, he was appointed as Director of Secco. From April 2010 to February 2011, he served as the General Manager of Secco. In June 2010, he was appointed Director and Vice Chairman of the Company. In February 2011, Mr. Wu was appointed Vice President of Secco. Mr. Wu graduated from the East China Institute of Chemical Technology in 1984, majoring in chemical engineering, and obtained a Bachelor of Engineering degree. In 1997, he obtained an MBA from the China Europe International Business School. He is a senior engineer by professional title.

**Li Honggen**, 56, is Executive Director and Vice President of the Company. Mr. Li joined the Complex in 1973 and has held various positions including Deputy Director of No. 1 Chemical Plant of the Complex, Deputy Director and Director of the Ethylene Plant of the Company and Deputy Manager and Manager of the Refining and Chemical Division of the Company. From August 2000 to December 2003, he served as Vice President of Shanghai Chemical Industrial Park Development Company Limited. From August 2002 to January 2006, he served as Vice President of Secco. In March 2006, he was appointed Vice President of the Company. In June 2006, he was appointed Director of the Company. In August 2008, he was concurrently appointed Director of Shanghai Chemical Industrial Park Development Company Limited. Mr. Li graduated from East China Institute of Chemical Technology majoring in engineering management and completed a post-graduate course majoring in engineering management at East China University of Science and Technology in 1998. He is an engineer by professional title.

**Shi Wei**, 53, is Vice President of the Company and the leader of the preparatory group of Zhijin coal chemical project of Sinopec Corp. in Guizhou. Mr. Shi joined the Complex in 1982 and has held various positions including Assistant to the Manager, Deputy Manager of the Refining and Chemical Division of the Company, Manager of the Environmental Department, Secretary of the Communist Party Committee and manager of the Refining and Chemical Division of the Company. In October 2003, Mr. Shi was appointed Vice President of the Company. In June 2005, he was appointed Director of the Company. In May 2012, Mr. Shi was appointed the leader of the preparatory group of Zhijin coal chemical project of Sinopec Corp. in Guizhou. In 1982, Mr. Shi graduated from East China University of Science and Technology majoring in oil refining engineering and obtained a bachelor's degree in engineering. Mr. Shi completed post-graduate studies in Business Management at East China University of Science and Technology in 1998. Mr. Shi is a senior engineer by professional title.

**Ye Guohua**, 44, is Chief Financial Officer of the Company. Mr. Ye joined Shanghai Gaoqiao Petrochemical Company in 1991 and has held various positions, including Deputy Chief and Chief of the Cost Accounting Section of the Finance Office, Director of the Finance Office of the Refinery Plant of Shanghai Gaoqiao Petrochemical Company and Deputy Chief Accountant and Director of the Finance Department of Sinopec Shanghai Gaoqiao Company. In October 2009, Mr. Ye was appointed Chief Financial Officer of the Company. Mr. Ye graduated with a major in accounting from the Shanghai University of Finance and Economics in July 1991. He is a senior accountant by professional title.

*External Directors*

**Lei Dianwu**, 50, is Assistant to the General Manager of Sinopec Group, Vice President and Director of Development and Planning Division of Sinopec Corp. In June 2005, Mr. Lei was elected External Director of the Company. Mr. Lei has held various positions including Deputy Director of Planning Division of Yangzi Petrochemical Company, Director of the Preparation Office of the Joint Venture of Yangzi Petrochemical Company, Vice President and Manager of production division of Yangzi BASF Styrene Company Limited. He acted as Deputy Manager and Deputy Director of the Joint Venture Office at Yangzi Petrochemical Company, Director of Project Development Department of China Dong Lian Petrochemical Limited Liabilities Company, Deputy General Manager of Yangzi Petrochemical Limited Liabilities Company and Deputy Director of Development and Planning Division of Sinopec Corp. From March 2001, he assumed the current position of Director of Development and Planning Division of Sinopec Corp. From March 2009, he assumed the current position of Assistant to General Manager of Sinopec Corp. From May 2009, he assumed the position of Vice President of Sinopec Corp. Mr. Lei has rich experience in enterprise planning and investment development management. In 1984, Mr. Lei graduated from the East China Petroleum Institute with a major in basic organic chemicals and obtained a bachelor's degree in engineering. He is a senior engineer by professional title.

**Xiang Hanyin**, 58, is Deputy Director of Chemical Division of Sinopec Corp. In June 2005, Mr. Xiang was elected External Director of the Company. Mr. Xiang commenced work in February 1982 and was Deputy Director of the Chemical Plant of Yizheng Chemical Fiber Company and Director of Chemical Plant of Yizheng Chemical Fiber Co., Ltd. In February 2000, he assumed the current position of Deputy Director of the Chemical Division of Sinopec Corp. Mr. Xiang has rich experience in the management of production and operation of chemical enterprises. Mr. Xiang graduated from Nanjing Chemical College with a major in basic organic chemicals and a bachelor's degree in engineering in 1982. In 2000, he completed post-graduate studies in enterprise management at Nanjing University. He is a senior engineer by professional title.



**Table of Contents***Independent Directors*

**Shen Liqiang**, 56, is President and Secretary of the Communist Party Committee of the Shanghai Branch of the Industrial and Commercial Bank of China ( ICBC ). Mr. Shen was appointed as the Independent Director of the Company in June 2011. Mr. Shen has been engaged in financial business since December 1976, and has held various positions, including Deputy Director and Director of the Hangzhou Business Department of the ICBC; Deputy Director of the Accounting and Cashier Department, Deputy Director and Director of the Savings Department, Director of the Personnel Department and Assistant to the President cum Director of Personnel Department of the Zhejiang Branch of the ICBC; Vice President of the Zhejiang Branch of the ICBC; Vice President cum General Manager and Secretary of the Communist Party Committee of the Banking Department of the Zhejiang Branch of the ICBC. He was Vice President and Deputy Secretary of the Communist Party Committee of the Zhejiang Branch of the ICBC from October 2005 to March 2007, and was appointed President and Secretary of the Communist Party Committee of the Hebei Branch of the ICBC from March 2007 to June 2009. He has been President and Secretary of the Communist Party Committee of the Shanghai Branch of the ICBC since June 2009. Mr. Shen has long been engaged in banking business management and has both in-depth expertise on finance theory and extensive experience in finance practice. Mr. Shen holds a Master's Degree in Economics and is a senior accountant by professional title. His current term of office is from June 2011 to June 2014.

**Jin Mingda**, 62, is Chairman and Secretary of the Communist Party Committee of Shanghai Huayi (Group) Company. Mr. Jin was appointed as the Independent Director of the Company in June 2011. Mr. Jin started working in October 1968 and has held various positions, including Deputy Secretary of the Communist Party Committee, Deputy Director, Secretary of the Communist Party Committee and Director of Shanghai Power Station Auxiliary Equipment Works Co., Ltd; General Manager and Deputy Secretary of the Communist Party Committee of Shanghai Boiler Works Co., Ltd; Vice President of Shanghai Electric (Group) Corporation; Vice President of Shanghai Electric Group Co., Ltd.; and President and Secretary of the Communist Party Committee of Shanghai Mechanical & Electrical Industry Co., Ltd. He served as Director, President and Deputy Secretary of the Communist Party Committee of Shanghai Huayi (Group) Company from November 2005 to October 2007, and Chairman and Secretary of the Communist Party Committee of Shanghai Huayi (Group) Company from October 2007. He was appointed Independent Director of Shanghai Electric Power Co., Ltd in November 2009. Mr. Jin has extensive experience in business decision-making and management of conglomerates. He possesses postgraduate qualifications and is a senior economist by professional title. His current term of office is from June 2011 to June 2014.

**Wang Yongshou**, 72. Mr. Wang was appointed as the Independent Director of the Company in June 2011. Mr. Wang started working in September 1964 and has held various positions, including Deputy Secretary of the Communist Party Committee, Deputy Director and Director of Plastics Factory of the Complex; Chief Economist of the Complex and Deputy President of JI. He served as President of Shanghai Jinshan Industrial Investment and Development Co., Ltd. from September 1997 to November 2001. Mr. Wang has extensive experience in corporate operation and management. Mr. Wang graduated from Zhejiang Institute of Chemical Technology in September 1964, and is a senior engineer by professional title. His current term of office is from June 2011 to June 2014.

**Cai Tingji**, 58, is a Fellow of the Hong Kong Institute of Certified Public Accountants, a member of the Committee of the Chinese People's Political Consultative Conference of Jing'an District, Shanghai, and Honorary Vice-Chairman of the Federation of Returned Overseas Chinese of Jing'an District, Shanghai. Mr. Cai was appointed as the Independent Director of the Company in June 2011. Mr. Cai graduated from the Department of Accounting, Hong Kong Polytechnic University in 1978. He joined KPMG in the same year and has held various positions, including Deputy Manager and Manager of the audit department of KPMG Hong Kong Office, Managing Partner of KPMG Shanghai Office, Senior Partner of KPMG Huazhen Shanghai Office as well as Senior Partner of KPMG Huazhen in Eastern and Western China. Mr. Cai retired from KPMG Huazhen in April 2010. Mr. Cai was responsible for IPO projects for a number of large Chinese domestic enterprises in China, Hong Kong or overseas, as well as for various projects for listed companies. He possesses a wealth of professional knowledge and experience. His current term of office is from June 2011 to June 2014.



**Table of Contents***Supervisory Committee*

The Company has a Supervisory Committee whose primary duty is to supervise senior management of the Company that includes the Board of Directors, managers and senior officers. The function of the Supervisory Committee is to ensure that senior management of the Company act in the interests of the Company, its shareholders and employees and in compliance with PRC law. The Supervisory Committee reports to the shareholders in the general meeting. The Articles of Association provide the Supervisory Committee with the right to investigate the business and the financial affairs of the Company and to convene shareholders' meetings from time to time. The Supervisory Committee currently comprises of six members, two of whom are employee representatives and four of whom are external supervisors, including two independent supervisors.

**Zuo Qiang**, 50, is the Supervisor, Vice Secretary of the Discipline Supervisory Committee, Director of the Supervisory Office, Director of the office of the Supervisory Committee and Secretary of the Discipline Supervisory Committee of the Headquarter of the Company. Mr. Zuo joined the Complex in 1981 and has held various positions, including archivist of the Command Division for the construction of Phase II of No. 1 Chemical Plant, Head of archives of the ethylene plant, Secretary of the Youth League Committee of the ethylene plant, Secretary of the Youth League Committee of the Refining and Chemical Division of the Complex, Secretary of the Youth League Committee of the Refining and Chemical Division, Secretary of General Branch of the Communist Party Committee of Ethylene Plant No. 1 of the Refining and Chemical Division of the Company and Deputy Director of the Supervisory Office of the Company. He was appointed Secretary of the Discipline Supervisory Committee of the Headquarter of the Company in August 2008. He has been serving as Director of the Supervisory Office of the Company since April 2011. Mr. Zuo was appointed Supervisor of the Company and the Director of the office of the Supervisory Committee in June 2011. In October 2011, he was appointed the Vice Secretary of the Discipline Supervisory Committee. Mr. Zuo graduated from the Correspondence College of the Communist Party Committee School of the Central Committee in June 1993 with a major in Party & Administrative management. He is an ideologist by professional title.

**Li Xiaoxia**, 43, is the Supervisor and the Vice President of the Labor Union of the Company. Ms. Lee joined the Complex in 1991 and has held various positions, including Controller of the operation zone of the marine terminal of the Company, Assistant to the Workshop Director, Deputy Workshop Director and Deputy Section Chief of Storage and Transportation Area No. 2 of the Refining and Chemical Division, Deputy Secretary of the Youth League Committee of the Company and Secretary of Chief Branch of Communist Party of the Labor Union for Staff Exchange and Relocation Centre. She was appointed Secretary of the Communist Party Committee and Deputy Manager of the Refining Division of the Company in June 2008. She was appointed Supervisor of the Company in June 2011 and Vice President of the Labor Union of the Company in December 2011. Ms. Li graduated from Liaoning University of Petroleum and Chemical Technology in August 1991 with a major in petroleum and natural gas transportation. She is a senior specialist technician by professional title.

*External Supervisors*

**Zhai Yalin**, 48, is Deputy Director of the Auditing Bureau of Sinopec Group and Deputy Director of Auditing Department of Sinopec Corp. and has served as External Supervisors of the Company since June 2008. Mr. Zhai began his career in 1986 and has been successively Deputy Head of the Head Office and Director of the Auditing Department of Qianguo Refinery, Deputy Director of the General Office of Sinopec Huaxia Auditing Company, Deputy Director of the General Administrative Office of the Auditing Bureau of Sinopec Group, Director of the General Administrative Office of the Auditing Bureau of Sinopec Group, and Director of the General Administrative Office of the Auditing Bureau of Sinopec Group (Auditing Department of Sinopec Corp.). Since December 2001, Mr. Zhai has been holding concurrently the positions of Deputy Director of the Auditing Bureau of Sinopec Group and Deputy Director of Auditing Department of Sinopec Corp. Mr. Zhai graduated from Jilin Siping Normal College in 1986 and is a senior economist by professional title.

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**Wang Liqun**, 55, is Deputy Chief of the Supervisory Bureau of Sinopec and Deputy Director of the Supervisory Department of Sinopec Corp. In June 2011, he was appointed the External Supervisor of our Company. Mr. Wang started working in 1976 and has held various positions, including Deputy Director of the Manager's Office of Beijing Yanshan Petrochemical Corporation, Director of the Personnel Department, Deputy Head and Head of the Department for Cadres of Beijing Yanshan Petrochemical Co., Ltd. He served as a member of the Standing Committee of the Communist Party Committee and Chairman of the Labor Union of Beijing Yanshan Petrochemical Co., Ltd. from August 2008 to April 2010. He has been serving as Deputy Chief of the Supervisory Bureau of Sinopec and Deputy Director of the Supervisory Department of Sinopec Corp. from April 2010. Mr. Wang graduated from Beijing Federation of Labor Unions University for Workers and Staff in 1984 with a major in environmental protection (Diploma), and graduated from Beijing University of Technology in 1997 with a major in business management (Bachelor). He is a senior economist by professional title.

*Independent Supervisors*

**Chen Xinyuan**, 48, is Dean, Professor and Tutor to doctoral students of the College of Accounting, Shanghai University of Finance and Economics. Mr. Chen was appointed the Independent Supervisor of the Company in June 2011. After graduation from the Accounting Faculty, Hangzhou College of Commerce in July 1985, Mr. Chen undertook post-graduate studies at the Accounting Faculty of Shanghai University of Finance and Economics and continued as a lecturer. He commenced his doctoral studies in accounting while teaching and received his doctorate in June 1994. He has been a tutor to doctoral students since December 1998. From June 2000 to June 2003, Mr. Chen was Independent Supervisor of the Company. From June 2003 to June 2011 Mr. Chen was appointed Independent Non-executive Director of the Company. Mr. Chen has also studied in West Germany for one year. He is an expert in financial reporting and accounting, given his experience in the academic aspects of accounting and notable achievements in accounting research. He is also experienced in business management.

**Zhou Yunnong**, 70. Mr. Zhou was appointed Independent Supervisor of the Company in June 2011. Mr. Zhou joined the Complex in October 1972 and held various positions including Deputy President of the Complex, Deputy Director of the Human Resource Department of Sinopec Group, Deputy Secretary of Communist Party Committee of the Complex, Vice President of the Company, Secretary of the Communist Party Committee of Sinopec Jinshan Industrial Company and the Governor of Jinshan District of Shanghai. From November 1999 to April 2002 he was a Senior Advisor to Shanghai Jinshan District. From June 2003 to June 2005, Mr. Zhou was Independent Supervisor of the Company. From June 2005 to June 2011, Mr. Zhou was Independent Non-executive Director of the Company. Mr. Zhou has extensive experience in business management and public administration management. Mr. Zhou graduated from East China Normal University in August 1964, majoring in radio. He is a senior engineer by professional title.

*Senior Management*

**Zhang Zhiliang**, 59, is a Vice President of the Company. Mr. Zhang joined the Complex in 1977 and held various positions including Deputy Director and Director of the No. 1 Chemical Plant of the Complex, as well as assistant manager and manager of the Company's Refining and Chemical Division. He was Vice President of the Company from April 1997 to March 2006. He was Director of the Company from June 1997 to June 2003. He was Director of Secco from November 2002 to April 2010, and Vice President of Secco from January 2006 to November 2006. He was President of Secco from November 2006 to April 2010. In April 2010, he was appointed as a Vice President of the Company. Mr. Zhang graduated from Fudan University in 1977, majoring in high molecular chemistry. He graduated from Shanghai No. 2 Industrial University in 1999, majoring in Applied Computer Management. He is a senior cadre of professorate rank.

**Zhang Jianping**, 50, is a Vice President of the Company. Mr. Zhang was nominated as the director of the Company in the board meeting on April 19, 2013. His nomination as the director of the Company needs to be reviewed and approved by the Company's 2012 general shareholders meeting on June 6, 2013. He joined the Complex in 1987, and successively held the positions of Deputy Chief Engineer of the Aromatics Plant of the Refining and Chemical Division, Deputy Director of the Plastic Plant, Deputy Manager of Plastics Division of the Company, Director of the Petrochemical Research Institute, Director of the Production Division of the Company, Assistant to President of the Company and Director of the Production Division. In July 2004, he was appointed Vice President of our Company. Mr. Zhang graduated in 1984 from East China Institute of Chemical Technology specializing in Petroleum Refinery and received a Master's Degree in Petroleum Processing from the same institute in 1987. He is a qualified senior engineer by professional title.

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**Jin Qiang**, 47, is Vice President of the Company. Mr. Jin joined Zhenhai General Petrochemical Works in 1986 and held various positions including Deputy Chief of the atmosphere and vacuum distillation unit and Deputy Chief of the heavy oil catalytic cracking plant. He then became Deputy Head and Head of the Machinery and Power Section of the Refinery Plant of Zhenhai Refining & Chemical Co., Ltd. He was appointed Deputy Director of the Utilities Department of Sinopec Zhenhai Refining & Chemical Co., Ltd ( ZRCC ) from June 2002 to April 2004, Deputy Director of the Machinery and Power Division of ZRCC from April 2004 to July 2005, Director of the Machinery and Power Division of ZRCC from July 2005 to October 2006, Director of the Machinery and Power Division of Zhenghai Refining & Chemical branch of Sinopec Corp. from October 2006 to March 2007 and Deputy Chief Engineer of Zhenghai Refining & Chemical branch of Sinopec Corp. from March 2007 to November 2011. Mr. Jing was appointed as the Vice President of the Company in November 2011. Mr. Jin graduated in July 1986 from the East China Institute of Chemical Technology specializing in chemical machinery, and graduated in July 2007 from the Graduate School of Central Party School specializing in economic management. He is a senior engineer by profession title.

**Gao Jinping**, 46, is the Vice President, Deputy Secretary of the Communist Party Committee, Secretary of the Communist Party Discipline Supervisory Committee of the Company and Chairman of the Labor Union of the Company. Mr. Gao was nominated as the director of the Company in the board meeting on April 19, 2013. His nomination as the director of the Company needs to be reviewed and approved by the Company's 2012 general shareholders meeting on June 6, 2013. Mr. Gao joined the Complex in 1990 and has held various positions including Deputy Secretary of the Communist Youth League of the Company, Deputy Secretary of the Communist Party Committee of the Experimental Plant and Chemical Division of the Company and Director of the Propaganda Division of the Company. In May 2003, Mr. Gao was appointed Deputy Secretary of the Communist Party Committee of the Company and Chairman of the Labor Union of the Company. From June 2004 to June 2006, Mr. Gao served as Director of the Company. In April 2006, Mr. Gao was appointed Secretary of the Communist Party Discipline Supervisory Committee of the Company. In June 2006, Mr. Gao was appointed Supervisor and Chairman of the Supervisory Committee of the Company. He rendered his resignation as the supervisor and Chairman of the Supervisory Committee with effect as of April 18, 2013. Mr. Gao graduated from the Food Processing Faculty of Shanghai Aquatic Products University with a major in cooling and cold storage technology and obtained a bachelor's degree in engineering in July 1990. In 2001, he completed his post-graduate studies in business administration in the aspect of industrial economics at Shanghai Academy of Social Sciences. He has senior professional title.

**Guo Xiaojun**, 43, is the Vice President, the Deputy Chief Engineer and Director of the Production Department of the Company. He joined the Company in 1991 and has held various positions, including Deputy Director of the Polypropylene Workshop in the Plastics Plant of the Company, Deputy Director of the Polypropylene Plant and Director of the Polyolefin Integrated Plant in the Plastics Division as well as Deputy Chief Engineer and Assistant to the Manager of the Plastics Division. He was Deputy Manager of the Company's Plastics Division from July 2008 to July 2009, Manager and Deputy Secretary of the Communist Party Committee of the Company's Plastics Division from July 2009 to March 2011, and has been serving as the Deputy Chief Engineer and Director of the Production Department of the Company since March 2011. He graduated with a major in basic organic chemical engineering from the East China University of Science and Technology in July 1991, and obtained a master's degree majoring in chemical engineering from the East China University of Science and Technology in April 2008. He is a senior engineer by professional title.

**Zhang Jingming** (FCIS, FCS), 55, is the Secretary of the Board of Directors, General Legal Counsel and Director of the Strategy Office of the Company. Mr. Zhang joined the Complex in 1978 and has held various positions including Project Manager and Deputy Director of the International Department, Securities Affairs Representative in Hong Kong and Deputy Director of the Board Secretariat. In June 1999, Mr. Zhang was appointed as Secretary to the Board of Directors. From June 1999 to June 2011, he concurrently served as Director of the Board Secretariat. In June 2001, Mr. Zhang was appointed Director of Strategy Research Department of the Company. In January 2005, Mr. Zhang was appointed General Counsel of the Company. In 1987, Mr. Zhang graduated from the Shanghai International Studies University majoring in English. During the period from 1992 to 1993, he was enrolled in graduate courses for the fourth Sino-British joint MBA program at Northwestern Polytechnic University and later on, Mr. Zhang went to the University of Hull in the United Kingdom for further study to earn an MBA degree and was granted the degree by the University of Hull in the United Kingdom in July 1995. In 2002, Mr. Zhang completed his graduate courses in international economic law at East China University of Political Science and Law. He is a senior economist by professional title.

### ***B. Compensation.***

The aggregate amount of cash compensation we paid to our directors, supervisors and executive officers during the year ended December 31, 2012 was approximately RMB7.598 million. In addition, directors and supervisors who are also officers or employees receive certain other benefits-in-kind, such as subsidized or free health care services, housing and transportation, which large Chinese enterprises customarily provide to their employees. No benefits are payable to members of the board or the Supervisory Committee or the executive officers upon termination of their relationship with us.



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The following table sets forth the compensation on an individual basis for our directors, supervisors and executive officers who received compensation from us in 2012.

Name	Position with the Company	Remuneration in 2012 (RMB 000) (before tax)
Rong Guangdao (1)	Former Chairman of the Board of Directors	688
Wang Zhiqing	Vice Chairman of the Board of Directors and President	688
Wu Haijun	Vice Chairman of the Board of Directors	
Li Honggen	Director and Vice President	602
Shi Wei	Vice President and Former Director	645
Ye Guohua	Director and Chief Financial Officer	586
Lei Dianwu	External Director	
Xiang Hanyin	External Director	
Shen Liqiang	Independent Director	
Jin Mingda	Independent Director	150
Wang Yongshou	Independent Director and Director of the Remuneration and Appraisal Committee	150
Cai Tingji	Independent Director and Director of the Audit Committee	150
Gao Jinping (2)	Vice President	586
Zuo Qiang	Supervisor	358
Li Xiaoxia	Supervisor	365
Zhai Yalin	External Supervisor	
Wang Liqun	External Supervisor	
Chen Xinyuan	Independent Supervisor	
Zhou Yunnong	Independent Supervisor	
Zhang Zhiliang	Vice President	631
Zhang Jianping	Vice President	586
Tang Chengjian (3)	Former Vice President	392
Jin Qiang	Vice President	586
Zhang Jingming	Company Secretary and General Legal Counsel	437

- (1) Rong Guangdao received compensation as Chairman of the Company in 2012 but no longer serves that position as the date of this annual report.
- (2) Gao Jinping received compensation as the supervisor and the Chairman of the Supervisory Committee of the Company in 2012 but no longer serves those positions as the date of this annual report.
- (3) Tang Chengjian received compensations as a Vice President of the Company in 2012 but no longer serves that position as the date of this annual report.

**C. Board Practices.***Board of Directors*

Our board of directors consists of twelve members. Our directors are elected at meetings of our shareholders, and, unless they resign at an earlier date, are deceased or removed, will serve three-year terms. The directors shall be eligible for reelection upon expiry of their terms of office, however, the combined tenure of an independent director may not exceed a total of six years. The term of our current board of directors will expire in 2014. None of our directors have entered into any service contracts with us or any of our subsidiaries providing for benefits upon termination of appointment or employment (with the exception of compensation required by Chinese labor law).

*Supervisory Committee*

The Supervisory Committee is responsible for ensuring that our directors and senior officers act in the interests of our company or those of our shareholders or employees and that they do not abuse their positions and powers. The Supervisory Committee has no power to overturn the

decisions or actions of our directors or officers and may only recommend that they correct any acts that are harmful to our interests or the interests of our shareholders or employees. The Supervisory Committee is currently composed of six members appointed for a three year term. The term of the current members will expire in June 2014. Supervisory Committee members have the right to attend meetings of our board of directors, inspect our financial affairs and perform other supervisory functions.

**Table of Contents***Audit Committee*

Pursuant to Paragraph 14 of the Code of Best Practices set out in Appendix 14 of the Rules Governing the Listing of Securities on The HKSE, we formed an audit committee on June 15, 1999 which consists of three directors. The current members are Cai Tingji, Shen Liqiang and Wang Yongshou according to the Resolutions of the First Meeting of the Seventh Session of the Board of Directors. The principal duty of the audit committee is to review and supervise our financial reporting process and internal controls. The members of the audit committee will hold office for the same term as their directorships which will expire in 2014.

*Remuneration Committee*

We formed a remuneration committee on December 25, 2001 which consists of three directors. The current members are Wang Yongshou, Jing Mingda and Ye Guohua according to the Resolutions of the First Meeting of the Seventh Session of the Board of Directors. The key responsibility of the Remuneration Committee is to formulate and review the remuneration policy and plan for the directors and executive officers, formulate the standards for evaluation of the directors and executive officers and conduct such evaluations.

*Summary Corporate Governance Differences*

There are significant differences between our corporate governance practices and those of U.S. issuers listed on the NYSE. Pursuant to Section 303A.11 of the NYSE listing Manual, we have disclosed certain of these differences on our website at [www.spc.com.cn/enspc/spc/newsroomlook.php?Did=1650&cid=69dD1ev=5](http://www.spc.com.cn/enspc/spc/newsroomlook.php?Did=1650&cid=69dD1ev=5).

**D. Employees.**

As of December 31, 2012, we had 15,007 employees.

The following table shows the approximate number of employees we had at the end of our last three years by the principal business function they performed:

	December 31,		
	2010	2011	2012
Management	1,332	1,632	1,617
Engineers, technicians and factory personnel	9,023	8,857	8,689
Accounting, marketing and others	6,014	5,166	4,701
Total	16,369	15,655	15,007

Approximately 41.33% of our work force are graduates with a tertiary degree or higher. In addition, we offer our employees opportunities for education and training based upon our development and the individual performance of each employee.

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A system of labor contracts has been adopted in our company. The contract system imposes discipline, provides incentives to adopt better work habits and gives us greater management control over our work force. We believe that by linking remuneration to productivity, the contract system has also improved employee morale. As of December 31, 2012, almost all of the work force was employed pursuant to labor contracts which specify the employee's position, responsibilities, remuneration and grounds for termination. The contracts generally have short terms of one to five years and may be renewed with the agreement of both parties. The remaining personnel are employed for an indefinite term.

We have a labor union that protects employees' rights, aims to assist in the fulfillment of our economic objectives, encourages employee participation in management decisions and assists in mediating disputes between us and union members. We have not been subject to any strikes or other labor disturbances which have interfered with our operations, and we believe that our relations with our employees are good.

Total remuneration of our employees includes salary and bonuses. Employees also receive certain benefits in terms of housing, education and health services that we subsidize, and other miscellaneous subsidies. In 2012, we incurred RMB1,740.2 million in employment costs.

In compliance with Shanghai regulations, we and our employees participate in a defined contribution government pension scheme under which all employees upon retirement are entitled to receive pensions. In order to protect and properly enhance the living level of retired employees and improve the middle and long term incentive system, the company established an enterprise annuity plan. According to the plan, to the extent that the employees volunteer for the related payments and have been with the Company for one year or more, such employees are entitled to participate in the enterprise annuity plan. We will make payments to match the payments made by the employees after giving considerations to our profitability, the employee's work responsibilities, contributions, and treatments post retirement based on the principle of universal benefits. The company has 14,910 retired employees under the above retirement insurance plans.

In addition to the pension benefits, pursuant to the relevant laws and regulations of the PRC, we and our employees participate in defined social security contributions for employees, such as a housing fund, basic medical insurance, supplementary medical insurance, unemployment insurance, injury insurance and maternity insurance.



**Table of Contents****E. Share Ownership.**

The following table shows the ownership interests of our Directors, Supervisors and senior officers in our shares as of March 31, 2013. All shares indicated are A shares and are directly owned by the relevant persons. In each case, they represent less than 1% of the outstanding A shares. No change in shareholdings occurred. Except as disclosed below, none of the Directors, Supervisors or senior officers or their affiliates had any other beneficial interest in our issued share capital as of March 31, 2013.

<b>Name</b>	<b>Position</b>	<b>Shares held at March 31, 2013</b>
Rong Guangdao	Former Chairman	3,600
Wang Zhiqing	Vice Chairman and President	0
Wu Haijun	Vice Chairman	0
Li Honggen	Director and Vice President	0
Shi Wei	Vice President and Former Director	0
Ye Guohua	Director and Chief Financial Officer	0
Lei Dianwu	External Director	0
Xiang Hanyin	External Director	0
Shen Liqiang	Independent Director	0
Jin Mingda	Independent Director	0
Wang Yongshou	Independent Director and Director of the Remuneration and Appraisal Committee	3,600
Cai Tingji	Independent Director and Director of the Audit Committee	0
Gao Jinping	Former Chairman of Supervisory Committee	0
Zuo Qiang	Supervisor	0
Li Xiaoxia	Supervisor	0
Zhai Yalin	External Supervisor	0
Wang Liqun	External Supervisor	0
Chen Xinyuan	Independent Supervisor	0
Zhou Yunnong	Independent Supervisor	0
Zhang Zhiliang	Vice President	0
Zhang Jianping	Vice President	0
Jin Qiang	Vice President	0
Zhang Jingming	Company Secretary and General Legal Counsel	0

We have no employee share purchase plan, share option plan or other arrangement that involves employees in our share capital.

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Sinopec Corp. owns 55.56% of our share capital and is able to exercise all the rights of a controlling shareholder, including the election of directors and voting on amendments to our Articles of Association.

The table below sets forth information regarding ownership of our capital stock as of March 31, 2013 by (i) all persons who we know own more than five percent of our capital stock and (ii) our officers and directors as a group. We are not aware that any such shareholders have voting rights different from those of our other shareholders.

Title of Class	Identity of Person or Group	Number of Shares Held	Percent of Total Share Capital
Domestic Shares	Sinopec Corp.	4,000,000,000	55.56%
H Shares	HKSCC nominees Ltd.	2,294,740,101	31.87%
A Shares	Directors and Officers	7,200	less than 1%

As of March 31, 2013, a total of 2,330,000,000 H Shares were outstanding. A total of 720,000,000 circulating A Shares were outstanding on March 31, 2013.

As of March 31, 2013 a total of 1,798,984 ADSs were registered in the name of The Bank of New York Mellon, the depository under our ADS deposit agreement. The Bank of New York Mellon has advised us that, as of March 31, 2013, 1,798,984 ADSs, representing the equivalent of 179,898,400 H Shares, were held of record by 89 other registered shareholders domiciles in and outside of the United States. We have no further information as to our shares held, or beneficially owned, by U.S. persons.

To the best of our knowledge, except as disclosed above, we are not directly or indirectly controlled by another corporation, any foreign government, or any other natural or legal person, severally or jointly.

We are not aware of any arrangement that may at a subsequent date result in a change of control of our company.

**B. Related Party Transactions.***Intercompany service agreements and business-related dealings*

During 2012, pursuant to the Mutual Product Supply and Sales Service Framework Agreement entered into by the Company and Sinopec Corp., we purchased raw materials from, and sold petroleum products and petrochemicals as well as leased properties to, Sinopec Corp. and its associates, and Sinopec Corp. and its associates acted as sales agents for our petrochemical products. Under the Comprehensive Services Framework Agreement entered into by the Company and Sinopec Group, we accepted construction and installation, engineering design, insurance agency and financial services relating to the petrochemical industry provided by Sinopec Group and its associates. The relevant connected transactions were conducted in accordance with the terms of the Mutual Product Supply and Sales Services Framework Agreement and the Comprehensive Services Framework Agreement. As the Mutual Product Supply and Sales Service Framework Agreement and the Comprehensive Services Framework Agreement were set to expire on December 31, 2010, we renewed these agreements with Sinopec Corp. and Sinopec Group respectively upon approval and authorization at the 2010 Extraordinary General Meeting held on December 28, 2010. At the 2010 Extraordinary General Meeting, our shareholders also approved certain caps on the annual transaction values of certain ongoing continuing connected transactions for the years ending December 31, 2011, December 31, 2012 and December 31, 2013. The transaction amounts of the relevant connected transactions in 2012 did not exceed such caps.

The purchases by us of crude oil and related materials from, and sales of petroleum products by us to, Sinopec Corp. and its associates were conducted in accordance with the State's relevant policy and applicable State tariffs or State guidance prices. As long as the State does not lift its control over purchases of crude oil, sales of petroleum products and pricing thereof, such connected transactions will continue to occur. We sell petrochemicals to Sinopec Corp. and its associates and Sinopec Corp. and its associates act as agents for the sales of petrochemicals in order to reduce our inventories, expand their trading, distribution and sales networks and improve our bargaining power with our customers. We lease part of the properties to Sinopec Corp. and its associates in consideration of their good financial background and credit standing. We accept

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construction and installation, engineering design, insurance agency and financial services relating to the petrochemical industry from Sinopec Group and its associates in order to secure steady and reliable services at reasonable prices.

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The prices of the continuing connected (*i.e.*, related-party) transactions conducted between the Company and Sinopec Group, Sinopec Corp. and its associates are determined by the parties involved after consultation pursuant to (1) the fixed price of the state; or (2) the guiding price of the state; or (3) market prices, and the conclusion of agreements for the connected transactions are in compliance with the needs of the Company's production and operation. Therefore the above continuing connected transactions do not cause a material impact on the Company's independence.

Type of major transactions	Connected parties	Annual cap for 2012	Transaction Amount during The reporting Period	Unit: RMB '000 Percentage Of the total Amount of the same type of transaction (%)
<b>Mutual Product Supply and Sales Services Framework Agreement</b>				
Purchases of raw materials	Sinopec Corp. and its associates	57,700,000	52,230,820	63.30
Sales of petroleum products	Sinopec Corp. and its associates	52,000,000	37,618,198	40.42
Sales of petrochemical products	Sinopec Corp. and its associates	17,400,000	13,722,908	14.74
Property leasing	Sinopec Corp. and its associates	31,000	23,976	51.66
Agency sales of petrochemical products	Sinopec Corp. and its associates	310,000	160,903	100.00
<b>Comprehensive Services Framework Agreement</b>				
Construction, installation and engineering design services	Sinopec Group and its associates	640,000	436,082	38.88
Petrochemical industry insurance services	Sinopec Group and its associates	141,000	115,918	65.92
Financial services	Sinopec Group and its associates	229,000	29,761	6.37

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*Other related party transactions*

We transferred to Sinopec Corp. an 81.97% equity interest owned by our wholly owned subsidiary Shanghai Petrochemical Investment Development Company Limited in Shanghai Jin Hua Industrial Company Limited for a consideration of RMB61,600,400. The relevant transfer agreement was entered into on February 8, 2006. The transaction generated a gain of RMB24,307,946 in 2006. The pricing principle was determined on the basis of a valuation report prepared by a qualified asset valuation company independent of the Company and Sinopec Corp. and upon arm's length negotiations between the parties. On the asset disposal date, the book value of the assets was RMB37,292,454, while the appraised value of the assets was RMB53,600,422 as at March 31, 2005.

We entered into equity transfer agreements with Sinopec Finance Company Limited to transfer our respective equity interests in China Everbright Bank and Bank of Shanghai to Sinopec Finance Company Limited. The considerations for the China Everbright Bank transfer and Bank of Shanghai transfer were RMB66,993,800 and RMB14,729,600, respectively. The relevant transfer agreements were entered into on December 7, 2006. As at the asset appraisal date, the book value of the equity interests held by the respective parties in China Everbright Bank and Bank of Shanghai totaled RMB55,449,641. The increase in the fair value of those equity interests of RMB26,228,500 as a result of the above transaction was recognized in the reserve, net of deferred tax, in 2006. The transaction prices were determined by way of a bidding process on the China Beijing Equity Exchange. The transfer of equity interest in China Everbright Bank was completed in April 2007. The transfer of equity interest in Bank of Shanghai was completed in July 2007.

We signed an agreement on December 30, 2005 to transfer our 2% equity interest in Sinopec Finance Company Limited to Sinopec Corp. for a purchase price of RMB82,000,000. In accordance with the payment terms of the agreement, we were paid the consideration on February 28, 2006.

We paid an amount of RMB164,763,000 to Sinopec Corp. and its subsidiary which consisted of equipment pre-payments and progress payments for the 380,000 tons per year glycol project and the long-cycle facility of the 3,300,000 tons per year diesel hydrogenation project. Both facilities were delivered in the first half of the year in 2006.

He Fei, a non-executive Director prior to June 18, 2002, is a partner of Haiwen & Partners, our legal advisor on Chinese laws, which has received and will continue to receive legal fees in connection with their representation of us.

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### *Equity joint venture*

Late in 2001, we established Secco, a Sino-foreign equity joint venture, together with BP and Sinopec Corp. We own a 20% interest in Secco, while BP and Sinopec Corp. own 50% and 30% interests in Secco, respectively. Secco was established to build and operate a 900,000 ton Rated Capacity ethylene petrochemical manufacturing facility to manufacture and market ethylene, polyethylene, styrene, polystyrene, propylene, acrylonitrile, polypropylene, butadiene, aromatics and by-products; provide related after-sales services and technical advice with respect to such petrochemical products and by products; and engage in polymers application development. Secco completed construction in 2005. Secco's total registered capital is U.S.\$901,440,964, of which we provided the Renminbi equivalent of U.S.\$180,287,952.

### *HKSE connected transactions rules*

We are required by HKSE listing rules to obtain advance shareholder approval for certain transactions with related parties such as Sinopec Group, Sinopec Corp., or its associates. We comply with such HKSE listing rules by obtaining advance shareholder approval at least every three years for the renewal of our framework agreements (*e.g.*, the Mutual Product Supply and Sales Services Framework Agreement and the Comprehensive Services Framework Agreement) with Sinopec Corp. and Sinopec Group for setting maximum aggregated annual values spent on the supply of products and services under these agreements. The independent non-executive directors will need to confirm each year, upon reviewing our continuing connected transaction, that these transactions are conducted in the ordinary and usual course of our business, on normal commercial terms and in accordance with the terms of these agreements.

### ***C. Interests of Experts and Counsel.***

Not applicable.

## **ITEM 8. FINANCIAL INFORMATION.**

### ***A. Consolidated Statements and Other Financial Information.***

Please see [Item 17. Financial Statements](#) for our audited consolidated financial statements filed as part of this annual report.

### *Export Sales*

In 2012, export sales accounted for RMB994.3 million (U.S.\$159.6 million) or 1.14% of our total net sales.

### *Litigation*

Neither we nor any of our subsidiaries is a party to, nor is any of our or their property the subject of any legal or arbitration proceedings which may have significant effects on our financial position or profitability. We are not aware of any litigation or arbitration proceedings in which any of our directors, any member of our senior management or any of our affiliates is an adverse party or has a material adverse interest.

### *Dividend Policy*

Our board of directors may propose dividend distributions subject to the approval of the shareholders. The Articles of Association also provide that, the aggregate profits distributed in cash in the recent three years shall not be less than 30% of the average distributable profits per year realized within the same period. Shareholders receive dividends in proportion to their shareholdings.

The Articles of Association require that cash dividends and other distributions in respect of H shares be declared in Renminbi and paid by us in Hong Kong dollars while cash dividends and other distributions in respect of our domestic shares be paid in Renminbi. If we record no profit for the year, we may not distribute dividends in such year.

We expect to continue to pay dividends, although there can be no assurance as to the particular amounts that might be paid from year to year. Payment of future dividends will depend upon our revenue, financial condition, future earnings and other factors. See [Item 5. Operating and Financial Review and Prospects](#) and [Item 3. Key Information A. Selected Financial Data Dividends](#).

***B. Significant Changes.***

No significant change has occurred since the date of the financial statements included in this annual report.

**Table of Contents****ITEM 9. THE OFFER AND LISTING.****A. Offer and Listing Details**

Set forth below is certain market information relating to our H Shares, ADSs and A Shares for the periods indicated.

	The Stock Exchange of Hong Kong		The New York Stock Exchange		The Shanghai Stock Exchange	
	High	Low	High	Low	High	Low
2008	4.88	1.10	61.88	14.50	13.64	3.58
2009	4.13	1.61	52.09	20.75	12.48	5.06
2010	4.11	2.58	52.27	33.13	11.11	7.16
2011	4.98	2.45	63.05	32.24	10.89	5.80
2012	3.20	1.88	41.43	24.64	6.76	4.68
2011						
First Quarter	4.98	3.62	63.05	47.01	9.58	7.74
Second Quarter	4.14	3.13	51.80	40.53	10.89	8.09
Third Quarter	3.55	2.45	45.24	32.24	9.06	6.96
Fourth Quarter	3.22	2.51	43.00	32.36	7.44	5.80
2012						
First Quarter	3.20	2.59	41.43	34.62	6.72	5.72
Second Quarter	2.83	2.13	36.54	27.39	6.76	5.73
Third Quarter	2.43	1.88	30.17	24.64	6.38	5.07
Fourth Quarter	2.77	1.97	36.31	25.29	5.55	4.68
2013						
First Quarter	3.75	2.55	48.24	33.18	6.74	5.04
Most Recent Six Months						
October 2012	2.38	1.97	30.89	25.29	5.55	5.27
November 2012	2.34	2.19	30.15	28.18	5.48	4.69
December 2012	2.77	2.24	36.31	29.15	5.32	4.68
January 2013	2.89	2.55	37.49	33.18	5.35	5.04
February 2013	3.57	2.83	44.44	37.63	6.08	5.18
March 2013	3.75	3.00	48.24	40.38	6.74	5.96

**B. Plan of Distribution**

Not applicable.

**C. Markets**

The principal trading market for our H Shares is the HKSE. The ADSs, each representing 100 H Shares, have been issued by The Bank of New York Mellon as a depository under a Deposit Agreement with us and are listed on the NYSE under the symbol SHI. We have also listed our A Shares on the Shanghai Stock Exchange. Prior to our initial public offering on July 26, 1993 and subsequent listings on the HKSE and NYSE, there was no market for our H Shares or the ADSs. Public trading in our A Shares commenced on November 8, 1993.

**D. Selling Shareholders**

Not applicable.

**E. Dilution**



Not applicable.

***F. Expenses of the Issuer***

Not applicable.

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### **ITEM 10. ADDITIONAL INFORMATION.**

#### ***A. Share Capital***

Not applicable.

#### ***B. Memorandum and Articles of Association.***

The following is a summary based upon provisions of our Articles of Association as currently in effect, the Company Law of the People's Republic of China (1993) (as amended) and other selected laws and regulations applicable to us. You should refer to the text of the Articles of Association and to the texts of applicable laws and regulations for further information.

We are a joint stock limited company established in accordance with the Company Law and certain other laws and regulations of the PRC. We are registered with the Shanghai Administration of Industry and Commerce with business license number 310000000021453. Our Articles of Association provide, at article 11, that our purpose is:

to build and operate a diversified industrial company which will be one of the world's leading petrochemical companies;

to promote the development of the petrochemical industry in China through the production of a broad variety of outstanding products; and

to practice advanced, scientific management and apply flexible business principles, and to develop overseas markets for our products so that we and our shareholders receive reasonable economic benefits.

Our scope of business is limited to matters approved by Chinese authorities. Article 12 provides that our primary business scope includes:

Refining crude oil, petroleum products, petrochemical products, synthetic fibers and monomers, plastic products, raw materials for knitting and textile products, preparation of catalysts and recover waste catalysts, power, heat, water and gas supply, water treatment, railway cargo loading and unloading, inland water transport, wharf operation, warehousing, design, research and development, technology development, transfer, consultancy and other services, property management, lease of self-owned premises, internal staff training, design and fabrication of various advertisements, and release of advertisements on self-owned media (administrative license should be obtained when required). We may adjust these subject to approval by governmental authorities.

The following discussion primarily concerns our shares and the rights of our shareholders. Holders of our ADSs will not be treated as our shareholders and will be required to surrender their ADSs for cancellation and withdrawal from the depository facility in which the H shares are held in order to exercise shareholder rights in respect of H shares.

Domestic shares and overseas-listed foreign invested H shares are both ordinary shares in our share capital. Domestic shares are shares we issue to domestic Chinese investors for subscription in Renminbi, while H shares are shares we issue for subscription in other currencies to investors from Hong Kong, Macau, Taiwan and outside of China.

#### ***Sources of Shareholders' Rights***

China's legal system is based on written statutes and is a system in which decided legal cases have little precedent value. China's legal system is similar to civil law systems in this regard. In 1979, China began the process of developing its legal system by undertaking to promulgate a comprehensive system of laws. In December 1993, the Standing Committee of the 8th National People's Congress adopted the Chinese Company Law. Although the Chinese Company Law is expected to serve as the core of a body of regulatory measures, which will impose a uniform standard of corporate behavior on companies and their directors and shareholders, only a limited portion of this body of regulatory measures has so far been promulgated.

Currently, the primary sources of shareholder rights are the Articles of Association, the Chinese Company Law and the HKSE listing rules, which, among other things, impose standards of conduct, fairness and disclosure on us, our directors and our controlling shareholder. To facilitate the offering and listing of shares of Chinese companies overseas, and to regulate the behavior of companies whose shares are listed

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overseas, the former State Council Securities Committee and the former State Commission for Restructuring the Economic System issued the Mandatory Provisions for articles of association of Companies Listing Overseas on August 27, 1994. These provisions have been incorporated into our Articles of Association and any amendment to those provisions will only become effective after approval by the companies approval department authorized by the State.

In addition, upon the listing of and for so long as the H shares are listed on the HKSE, we will be subject to those relevant ordinances, rules and regulations applicable to companies listed on the HKSE, the Securities and Futures Ordinance and the Codes on Takeovers and Mergers and Share Repurchases.

Unless otherwise specified, all rights, obligations and protections discussed below derive from our Articles of Association and/or the Chinese Company Law.

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### *Enforceability of Shareholders' Rights*

There has not been any public disclosure in relation to the enforcement by holders of H shares of their rights under the charter documents of joint stock limited companies or the Chinese Company Law or in the application or interpretation of the Chinese or Hong Kong regulatory provisions applicable to Chinese joint stock limited companies.

In most states of the United States, shareholders may sue a corporation derivatively. A derivative suit involves the commencement by a shareholder of a corporate cause of action against persons who have allegedly wronged the corporation, where the corporation itself has failed to enforce the claims directly. This would include suits against corporate officers, directors, or controlling shareholders. This type of action is brought based upon a primary right of the corporation, but is asserted by a shareholder on behalf of the corporation. In accordance with the Company Law of the People's Republic of China, if a company incurs losses due to the violation of any provision of laws, administrative regulations or the company's articles of association by any of its directors, supervisors and officers during his/her discharge of duties entrusted by the company, or due to any other person's infringement of the company's legal rights or interests, the shareholders of the company may take legal action before a court under the Company Law of the People's Republic of China.

Our Articles of Association provide that all differences or claims

between a holder of H shares and us;

between a holder of H shares and any of our directors, supervisors, manager or other senior officers; or

between a holder of H shares and a holder of domestic shares, involving any right or obligation provided in the Articles of Association, the Chinese Company Law or any other relevant law or administrative regulation which concerns our affairs must, with certain exceptions, be referred to arbitration at either the China International Economic and Trade Arbitration Commission in China or the Hong Kong International Arbitration Center. Our Articles of Association also provide that the arbitration will be final and conclusive. On June 21, 1999, an arrangement was made between Hong Kong and China for the summary mutual enforcement of each other's arbitration awards in a manner consistent with the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards and practices that occurred before the handover of Hong Kong to China. This arrangement was approved by the Supreme Court of China and the Hong Kong Legislative Council, and became effective on February 1, 2000.

All of our directors and officers reside outside the United States (principally in China) and substantially all of our assets and of those persons are located outside the United States. Therefore, you may not be able to effect service of process within the United States against any of those persons. In addition, China does not have treaties providing for the reciprocal recognition and enforcement of judgments of courts within the United States or most other countries that are members of the Organization for Economic Cooperation and Development. This means that administrative actions brought by regulatory authorities such as the Securities and Exchange Commission, and other actions which result in foreign court judgments could only be enforced in China if the judgments or rulings do not violate the basic principles of the law of China or the sovereignty, security and social public interest of the society of China, as determined by a People's Court of China which has jurisdiction for recognition and enforcement of judgments. We have been advised by our Chinese counsel, Haiwen & Partners, that there is doubt as to the enforceability in China of any actions to enforce judgments of United States courts arising out of or based on the ownership of our H shares or ADSs, including judgments arising out of or based on the civil liability provisions of United States federal or state securities laws.

### *Restrictions on Transferability and the Share Register*

All fully paid up H shares will be freely transferable in accordance with the Articles of Association unless otherwise prescribed by law and/or administrative regulations. Under current laws and regulations, H shares may be traded only among investors who are not Chinese persons, and may not be sold to Chinese investors. Consequences under Chinese law of a purported transfer of H shares to Chinese investors are unclear.

As provided in our Articles of Association, we may refuse to register a transfer of H shares without providing any reason unless:

all relevant transfer fees and stamp duties are paid;

the instrument of transfer is accompanied by the share certificates to which it relates and any other evidence reasonably required by our board to prove the transferor's right to make the transfer;

there are no more than four joint holders as transferees; and

the H shares are free from any lien of ours.

Additionally, no transfers of shares may be registered within the 30 days prior to a shareholders' general meeting or within five days before we decide on the distribution of dividends.

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We are required to keep a register of our shareholders which shall be comprised of various parts, including one part which is to be maintained in Hong Kong in relation to H shares listed on the HKSE. Shareholders have the right to inspect the share register. For a reasonable fee, shareholders may copy any part of the share register, obtain background information regarding our directors, supervisors, manager and other senior officers, minutes of shareholder general meetings and reports regarding our share capital and any share repurchases in the prior year.

### *Dividends*

Upon approval by ordinary resolution at a shareholders' meeting, our Board of Directors may propose dividend distribution at any time. The Articles of Association permits dividends issued in the form of cash or shares. Special resolution of the shareholders' general meeting is required for dividends issued in the form of shares.

Dividends may only be distributed, however, after allowance has been made for:

recovery of losses, if any;

allocations to the statutory common reserve fund; and

allocations to a discretionary common reserve fund.

The Articles of Association require us to appoint on behalf of the holders of H shares a receiving agent which is registered as a trust corporation under the Trustee Ordinance of Hong Kong to receive dividends we declare in respect of the H shares on behalf of the H shareholders. The Articles of Association require that cash dividends and other distributions in respect of H shares be declared in Renminbi and paid by us in Hong Kong dollars while cash dividends and other distributions of the domestic shares shall be paid in Renminbi.

If we record no profit for the year, we may not normally distribute dividends for the year.

Dividend payments may be subject to Chinese withholding tax. See [Item 10. Additional Information](#) **E. Taxation**.

### *Voting Rights and Shareholders' Meetings*

Our board of directors must convene a shareholders' annual general meeting once every year within six months from the end of the preceding financial year. Our board must convene an extraordinary general meeting within two months of the occurrence of any one of the following events:

where the number of directors is less than five as required by the Chinese Company Law or two-thirds of the number specified in our Articles of Association;

where our unrecovered losses reach one-third of the total amount of our share capital;

where shareholder(s) holding 10% or more of our issued and outstanding voting shares request(s) in writing; or

whenever our board deems necessary or our Supervisory Committee so requests.

Meetings of a special class of shareholders must be called in specified situations when the rights of the holders of that class of shares may be varied or abrogated, as discussed below. The Board of Directors, the Supervisory Committee, and shareholders individually or collectively holding 3% or more of our total voting shares are entitled to make written proposals to a shareholders' meeting. Shareholders individually or

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collectively holding more than 3% of our total shares may submit written interim proposals to the convener of a shareholders meeting ten days before the meeting.

All shareholders meetings must be convened by our board by notice given to shareholders by personal service, mail or announcement in the newspaper not less than 45 days before the meeting. Based on the written replies we receive 20 days before a shareholders meeting, we will calculate the number of voting shares represented by shareholders who have indicated that they intend to attend the meeting. We can convene the shareholders general meeting if the number of voting shares represented by those shareholders is more than one-half of our total voting shares. Otherwise, we shall, within five days, inform the shareholders again of the motions to be considered and the date and venue of the meeting by way of public announcement. After the announcement is made, the shareholders meeting may be convened. Our accidental omission to give notice of a meeting to, or the non-receipt of notice of a meeting by, a shareholder will not invalidate the proceedings at that shareholders meeting. However, an extraordinary shareholders meeting cannot conduct any business not contained in the notice of meeting.

Shareholders at meetings have the power, among other things, to decide on our operational policies and investment plans, to approve or reject our proposed annual budget, approve our profit distribution plans, an increase or decrease in share capital, the issuance of debentures, our merger or liquidation and any amendment to our Articles of Association. Shareholders also have the right to review any proposals by a shareholder owning 3% or more of our shares.

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In general, holders of H shares and domestic shares vote together as a single class at all meetings and on all matters. However, the rights of a class of shareholders may not be varied or abrogated, unless approved by both a special resolution of all shareholders at a general shareholders meeting and by a special resolution of shareholders of that class of shares at a separate meeting. Our Articles of Association specify, without limitation, that the following amendments would be deemed to be a variation or abrogation of the rights of a class of shareholders:

increasing or decreasing the number of shares of a class or of a class having voting or distribution rights or privileges equal or superior to that class;

removing or reducing rights to receive dividends in a particular currency;

creating shares with voting or distribution rights superior to shares of that class;

restricting or adding restrictions to the transfer of ownership of shares of that class;

allotting and issuing rights to subscribe for, or to convert into, shares of that class or another class;

increasing the rights or privileges of any other class; or

modifying the provision of our Articles of Association that specifies which amendments would be deemed a variation or abrogation of the rights of a class of shareholder.

For votes on any of these matters, or any other matter that would vary or abrogate the rights of the domestic shares or H shares, the holders of domestic shares and H shares are deemed to be separate classes and vote separately. However, Interested Shareholders are not entitled to vote at class meetings. The meaning of Interested Shareholder depends on the proposal to be voted on at the class meeting:

If the proposal is for us to repurchase our shares either from all shareholders proportionately or by purchasing share on a stock exchange, an Interested Shareholder is our controlling shareholder;

If the proposal is for us to repurchase our shares from a shareholder by a private contract, an Interested Shareholder is the shareholder whose shares would be repurchased;

If the proposal is for our restructuring, an Interested Shareholder is any shareholder that has an interest in the restructuring different from the other shareholders of the class or who bears a burden under the proposed restructuring that is less than proportionate to his shareholdings of the class.

Our Articles of Association specifically provide that an issue of up to 20% of domestic and H shares would not be a variation or abrogation of the rights of domestic shareholders or H shareholders, therefore, separate approval of the domestic shareholders or H Shareholders would not be required.

Each share is entitled to one vote on all matters submitted to a vote of our shareholders at all shareholders meetings, except for meetings of a special class of shareholders where only holders of shares of the affected class are entitled to vote on the basis of one vote per share of the affected class.



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Shareholders are entitled to attend and vote at meetings either in person or by proxy. Proxy authorization forms must be in writing and deposited at our company's principal offices, or at such other place specified in the notice of shareholders meeting not less than 24 hours before the time that such meeting will be held or the time appointed for passing upon the relevant resolutions. If a proxy authorization form is signed by a third party on behalf of the relevant shareholder, then such proxy authorization form must be accompanied by the signature authorization letter or other such document authorizing such third party to sign on behalf of the shareholder.

Except for those actions discussed below, which require supermajority votes, or special resolutions, resolutions of the shareholders are passed by a simple majority of the voting shares held by shareholders who are present in person or by proxy. Special resolutions must be passed by more than two-thirds of the voting rights represented by shareholders who are present in person or by proxy.

The following decisions must be adopted by special resolution:

an increase or reduction of our share capital or the issue of shares of any class, warrants and other similar securities;

the issue of our debentures;

our division, merger, dissolution and liquidation;

amendments to our Articles of Association;

significant acquisition or disposal of material assets or provision of guarantees conducted within the period of one year with a value exceeding 30% of our latest audited total assets;

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share incentive schemes; and

any other matters considered by the shareholders in a general meeting and which they have resolved by way of an ordinary resolution to be material and should be adopted by special resolution.

All other actions taken by the shareholders, including the appointment and removal of our directors and independent auditors and the declaration of normal dividend payments, will be decided by an ordinary resolution of the shareholders.

Our listing agreement with the HKSE provides that we may not permit amendments to certain sections of our Articles of Association that are subject to the Mandatory Provisions. These sections include provisions relating to (i) varying the rights of existing classes of shares, (ii) voting rights, (iii) our ability to purchase our own shares, (iv) rights of minority shareholders and (v) procedures on liquidation. In addition, certain amendments to the Articles of Association require the approval and assent of Chinese authorities.

### *Board of Directors*

Our Articles of Association authorize up to 12 directors. Directors are elected by shareholders at a general meeting for a three year term from among candidates nominated by the board of directors or by shareholders holding 3% or more of our shares (independent directors may be nominated by shareholders each holding 1% or more of our shares). Because our directors do not serve staggered terms, the entire board of directors will stand for election, and could be replaced, every three years. Our directors are not required to hold any shares in us, and there is no age limit requirement for the retirement or non- retirement of our directors.

In addition to obligations imposed by laws, administrative regulations or the listing rules of the stock exchanges on which our shares are listed, the Articles of Association place on each of our directors, supervisors, manager and any other senior officers a duty to each shareholder, in the exercise of our functions and powers entrusted to them:

not to cause us to exceed the scope of business stipulated in our business license;

to act honestly in what he considers our best interests;

not to expropriate our assets in any way, including (without limitation) usurpation of opportunities which may benefit us; and

not to expropriate the individual rights of shareholders, including (without limitation) rights to distributions and voting rights, except according to a restructuring which has been submitted to the shareholders for their approval in accordance with the Articles of Association.

Our Articles of Association further place on each of our directors, supervisors, manager and other senior officers:

a duty, in the exercise of their powers and discharge of their duties, to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances;

a fiduciary obligation, in the discharge of his duties, not to place himself or herself in a position where his or her interests may conflict with his or her duty to us; and

a duty not to cause a person or an organization related or connected to him or her in specified relationships to do what they are prohibited from doing.

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We pay all expenses that our directors incur for their services as directors. Directors also receive compensation for their services under service contracts that are negotiated by the board of directors and approved by the shareholders.

Subject to the stipulations of relevant laws and regulations, the shareholders in a general meeting may by ordinary resolution remove any director before the expiration of his term of office. Except for the restrictions placed on controlling shareholders, discussed below, our shareholders in general meeting have the power to relieve a director or supervisor from liability for specific breaches of duty.

Cumulative voting is required for a meeting of shareholders held for the election of two or more of our directors or supervisors as long as more than 30% of our outstanding shares are held by a single shareholder. Cumulative voting allows shareholders to cast a number of votes for a candidate equal to the number of shares held multiplied by the number of directors being elected at the shareholders' meeting. If a shareholder attempts to cast more votes than he is entitled to under this system, all of the shareholder's votes will be invalid and will be deemed an abstention.

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More than one third of our directors of board must be independent from our shareholders and not hold any office with us (each, Independent Director ). At least one Independent Director must be an accounting professional and all Independent Directors must possess a basic knowledge of the operations of a listed company and be familiar with relevant laws and rules and have at least five years working experience in law, economics or other area required for the fulfillment of responsibilities as an Independent Director. Independent Directors may not serve for terms exceeding six years. In addition, there are specific persons who are disqualified from acting as Independent Director. These include:

immediate family members of persons who work for us or our associated entities;

persons or their immediate family who hold one percent or more of our shares or are among our ten largest shareholders;

any persons that satisfied the foregoing conditions within the past one year;

persons providing financial, legal, consultation or other services to us or our associated entities;

persons who already serve as Independent Director for five other listed companies; and

anyone identified by the CSRC as unsuitable for serving as an Independent Director.

If the resignation of an Independent Director would cause our Board of Directors to have less than one third Independent Directors, the resignation will only become effective after a new Independent Director has been appointed.

Our Board will be required to meet at least four times each year. Directors who miss two consecutive Board meetings without appointing an alternate director to attend on their behalf will be proposed for removal at the next shareholders meeting, provided that Independent Directors may miss three consecutive meetings in person before being proposed for removal.

Directors may not vote on any matter in which he has a material interest, nor will he be counted for purposes of forming a quorum on such a matter.

Board resolutions are passed by a simple majority of the Directors except for the following matters which require the consent of more than two thirds of the Directors:

proposals for our financial policies;

the increase or reduction of our registered capital;

the issue of securities of any kind and their listing;

any repurchase of our shares;

significant acquisitions or disposals;

our merger, division or dissolution; and

any amendment to our Articles of Association.

Our Board of Directors or Supervisory Committee may nominate candidates for our Board of Directors and Supervisory Committee. In addition, shareholders holding one percent or more of our shares have the right to nominate candidates for Independent Director or Independent Supervisor and shareholders holding three percent or more of our shares have the right to nominate other candidates for Director or Supervisor. For candidates for Director, the nominator and candidates will be responsible for providing truthful and complete information about the candidate for disclosure. Candidates for Independent Director must publicly declare that there does not exist any relationship between himself and us that may influence his independent, objective judgment. The CSRC may veto any candidate for Independent Director.

Any material connected transactions are subject to prior approval by our Independent Directors. Connected transactions are those defined by the HKSE and by Chinese rules and regulations, but would generally include transactions with any of the following:

any company that, directly or indirectly, controls us or is under common control with us;

any shareholders owning 5% or more of our shares;

our directors, supervisors and other senior management;

any of our key technical personnel or key technology suppliers; and

any close relative or associate of any of the above.

Our independent directors can also propose to the Board of Directors the appointment or removal of our auditors, the convening of a Board meeting, independently appoint external auditors, solicit votes from shareholders and report circumstances directly to shareholders, Chinese securities regulatory authorities or other government departments. Two or more may request that the Board convene an extraordinary meeting of shareholders.

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Our Independent Directors will have to express their opinion on specified matters to the Board or to the shareholders at a shareholders meeting, either by a single unanimous statement or individually. These matters are:

the nomination, removal and remuneration of directors or senior management;

any major loans or financial transactions with our shareholders or related enterprises and whether we have taken adequate steps to ensure repayment;

matters that the Independent Director believes may harm the rights and interests of minority shareholders; and

any other matter that they are required to opine on by applicable law or rules.

These opinions must be expressed as either, agree, qualified agreement, opposition or unable to form an opinion. All but agreement must also be accompanied by a supporting explanation. If public disclosure of the matter is required, we must also disclose the opinions of our Independent Directors.

Any Independent Director may engage independent institutions to provide independent opinions as the basis of their decision. We must arrange the engagement and bear any costs.

### *Supervisory Committee*

The Supervisory Committee is responsible for supervising our directors and senior officers and preventing them from abusing their positions and powers or infringing upon the rights and interests of our company or those of our shareholders and employees. The Supervisory Committee has no power over the decisions or actions of our directors or officers except for requesting the directors or officers to correct any acts that are harmful to our interests. The Supervisory Committee is currently composed of six members appointed for a three year term. It has the right to:

attend the meetings of our board of directors;

inspect our financial affairs;

supervise and evaluate the conduct of our directors, general manager and other senior officers in order to determine whether they violate any laws, regulations or the Articles of Association in performing their duties;

require our directors, general manager or other senior officers to correct any act harmful to our interests and those of our shareholders and employees;

verify financial reports, accounting reports, business reports, profit distribution plans and other financial information proposed to be tabled at the shareholders general meeting, and entrust registered accountants and practising accountants to re-review such documents upon its discovery of any problems;

require the board of directors to convene an extraordinary general meeting of shareholders;

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represent us in negotiations with directors or in initiating legal proceedings against a director on our company's behalf;

conduct investigation into any identified irregularities in our operations, and where necessary, to engage accountants, legal advisers or other professionals to assist in the investigation; and

any other matters authorized by the Articles of Association.

No less than 1/3rd of the Supervisory Committee must be employee representatives appointed by our employees. The remaining members are appointed by the shareholders in a general meeting, provided that our directors, general manager and senior officers are not eligible to serve as supervisors. The Supervisory Committee must meet at least once a year. Decisions of the Supervisory Committee must be made by a one-half vote. We will pay all reasonable expenses incurred by the Supervisory Committee in appointing professional advisors, such as lawyers, accountants or auditors.

### *Liquidation Rights*

In the event of our liquidation, payment of debts out of our remaining assets will be made in the order of priority prescribed by applicable laws and regulations. After payment of debts, we will distribute the remaining property to shareholders according to the class and proportion of their shareholdings. For this purpose, the H shares will rank equally with the domestic shares.

### *Obligation of Shareholders*

Shareholders are not obligated to make any further contributions to our share capital other than as agreed by the subscriber of the relevant shares on subscription. This provision means that holders of ADSs will also not be obligated to make further contributions to our share capital.

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### *Duration*

We are organized as a joint stock limited company of indefinite duration.

### *Increase in Share Capital*

The Articles of Association require that approval by a resolution of the shareholders be obtained prior to issuing new shares. New issues of shares must also be approved by the relevant Chinese authorities.

### *Reduction of Share Capital and Purchase by Us of Our Shares*

We may reduce our registered share capital only upon obtaining the approval of the shareholders and, when applicable, relevant Chinese authorities. Repurchases may be made either by way of a general offer to all shareholders in proportion to their shareholdings, by purchasing our shares on a stock exchange or by an off-market contract with individual shareholders.

### *Restrictions on Large or Controlling Shareholders*

Our Articles of Association provide that, in addition to any obligation imposed by laws and administrative regulations or required by the listing rules of the stock exchanges on which our shares are listed, a controlling shareholder cannot exercise voting rights in a manner prejudicial to the interests of the shareholders generally or of some part of the shareholders:

to relieve a director or supervisor from his or her duty to act honestly in our best interest;

to approve the expropriation by a director or supervisor (for his or her own benefit or for the benefit of another person) of our assets in any way, including, without limitation, opportunities which may benefit us; or

to approve the expropriation by a director or supervisor (for his or her own benefit or for the benefit of another person) of the individual rights of other shareholders, including, without limitation, rights to distributions and voting rights (but not according to a restructuring of our company which has been submitted for approval by the shareholders in a general meeting in accordance with our Articles of Association).

A controlling shareholder, however, will not be precluded by our Articles of Association or any laws and administrative regulations or the listing rules of the stock exchanges on which our shares are listed from voting on these matters.

A controlling shareholder is defined by our Articles of Association as any person who, acting alone or together with others:

has the power to elect more than one-half of the board of directors;

has the power to exercise, or to control the exercise of, 30% or more of our voting rights;

holds 30% or more of our issued and outstanding shares; or

has *de facto* control of us in any other way.

*Minutes, Accounts and Annual Report*



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Our shareholders may inspect copies of the minutes of the shareholders' general meetings during our business hours free of charge. Shareholders are also entitled to receive copies of these minutes within seven days of receipt of the reasonable charges we may require.

Our fiscal year is the calendar year ending December 31. Each fiscal year, we must mail our financial report to shareholders not less than 21 days before the date of the shareholders' annual general meeting. These and any interim financial statements must be prepared in accordance with Chinese accounting standards and, for so long as H shares are listed on the HKSE, must also be prepared in accordance with or reconciled to either Hong Kong accounting standards or international accounting standards. The financial statements must be approved by an ordinary resolution of the shareholders at the annual general meeting.

Independent auditors are appointed each year by the shareholders at the annual meeting.

### *C. Material Contracts.*

We have not entered into any material contracts other than in the ordinary course of business and other than those described in Item 4. Information on the Company or elsewhere in this annual report on Form 20-F.

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### ***D. Exchange Controls.***

Our Articles of Association require that cash dividends on our H Shares be declared in Renminbi and paid in HK dollars. The Articles of Association further stipulate that such dividends must be converted to HK dollars at a rate equal to the average of the closing exchange rates for HK dollars as announced by the Chinese Foreign Exchange Trading Center for the calendar week preceding the date on which the dividends are declared.

The Renminbi currently is not a freely convertible currency. The SAFE, under supervision of the People's Bank of China ( PBOC ) controls the conversion of Renminbi into foreign currency. Although Chinese governmental policies were introduced in 1996 to reduce restrictions on the convertibility of Renminbi into foreign currency for current account items, conversion of Renminbi into foreign exchange for capital items, such as foreign direct investment, loans or securities, requires the approval of SAFE and other relevant authorities. These limitations could affect our ability to obtain foreign exchange through debt or equity financing, or to obtain foreign exchange for capital expenditures.

On July 21, 2005, the Chinese government changed its policy of pegging the Renminbi to the U.S. dollar. Under the new policy, the Renminbi is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. Since the adoption of this new policy, the value of the Renminbi has fluctuated daily within a narrow band, but overall has appreciated against the US dollar. Nevertheless, the Chinese government continues to receive significant international pressure to further liberalize its currency policy which could result in a further and more significant appreciation in the value of the Renminbi against the US dollar.

While the impact of the foregoing developments is not entirely clear, it appears that the trend in the Chinese government's foreign exchange policy is toward easier convertibility of the Renminbi.

The holders of the ADSs will receive the HK dollar dividend payments in U.S. Dollars at conversion rates related to market rates and subject to fees as set forth in our Deposit Agreement with The Bank of New York Mellon, as Depositary. The HK dollar is currently linked to and trades within a narrow band against the US dollar at a rate that does not deviate significantly from HK\$7.80 = U.S.\$1.00. The Hong Kong government has stated its intention to maintain such link, although there can be no guarantee that such link will be maintained.

### ***E. Taxation***

#### ***PRC Taxation***

The following is a summary of those taxes, including withholding provisions, to which United States security holders are subject under existing Chinese laws and regulations. The summary is subject to changes in Chinese law, including changes that could have retroactive effect. The summary does not take into account or discuss the tax laws of any country other than China, nor does it take into account the individual circumstances of a security holder. This summary does not purport to be a complete technical analysis or an examination of all potential tax effects under such laws and regulations.

#### ***Tax on Dividends***

##### ***For an Individual Investor***

According to the Individual Income Tax Law of the People's Republic of China, as amended on December 29, 2007 (the Individual Income Tax Law ) dividends paid by Chinese companies to individual investors are subject to Chinese withholding tax at a flat rate of 20%. As for a foreign individual investor that neither has a domicile nor resides in China, or that has no domicile and has resided in China for no more than one year, the dividends received by such an investor in China are generally subject to a withholding tax at a flat rate of 20% under the individual income tax law, subject to exemption or reduction by an applicable income tax treaty. According to the State Administration of Taxation's tax treatments with regard to the dividends of H shares paid by onshore non-foreign invested enterprises listed in HKEx, we will withhold and pay the individual income tax at the tax rate of 10% for individual shareholders who are residents of Hong Kong, Macau, or countries which have entered into tax treaties with mainland China, which provide for a 10% dividends tax rate, and we will temporarily withhold and pay the individual income tax at the tax rate of 10% for individual shareholders who are residents of countries which have entered into tax treaties with mainland China, which provide for a less than 10% dividends tax rate. Shareholders of H Shares may directly or through our Company apply to the in-charge tax authority for the preferential treatments provided by the relevant tax treaties. Upon the approval by the in-charge tax authority, the excessive amount being paid will be refunded. For individual shareholders who are residents of countries which have entered into tax treaties with mainland China providing for a more than 10% but less than 20% dividends tax rate, we will withhold and pay the individual income tax at the specific tax rate required therein. We will withhold and pay the individual income tax at the dividends tax rate of 20% for individual shareholders who are residents of countries which have not entered into any forms of tax treaties with mainland China or in circumstances other

than above described.

**Table of Contents***For a Corporation*

According to the Enterprise Income Tax Law of the People's Republic of China ( Enterprise Income Tax Law ) and its implementation rules, effective January 1, 2008, dividends by Chinese resident enterprises to non-resident enterprises are ordinarily subject to a Chinese withholding tax levied at a flat rate of 10%. For purposes of the Enterprise Income Tax Law, a Chinese resident enterprise is an enterprise which is either (i) set up in China in accordance with PRC laws or (ii) set up in accordance with the laws of a foreign country (region) but whose actual administrative headquarters is in China. For purposes of the Enterprise Income Tax Law, a non-resident enterprise is an enterprise which is set up in accordance with the laws of a foreign country (region) and whose actual administrative headquarters is located outside China but which has either (i) set up a legal presence in China or (ii) has income originating from China despite not having formally set up a legal presence in China. The State Administration of Taxation issued a *Circular on Issues Relating to the Withholding of Enterprise Income Tax for Dividends Distributed by Resident Enterprises in China to Non-resident Enterprises Holding H-shares of the Enterprises* (Guo Shui Han [2008] No. 897)( Circular No. 897 ) on November 6, 2008, which further clarifies that Chinese resident enterprises should, in distributing dividends for 2008 or any year hereafter to non-resident enterprises holding H-shares of the Chinese resident enterprise, withhold enterprise income tax for such dividends at a tax rate of 10%. After receiving dividends, non-resident enterprises holding H-shares of any Chinese resident enterprise can, on their own or through an agent, file an application to the relevant taxation authorities for such dividends to be covered by any applicable tax treaty (or other arrangement). The relevant taxation authorities should, upon reviewing and verifying the application and supporting materials to be correct, refund the difference between the tax levied and the tax payable calculated at a tax rate specified by the applicable tax treaty (or other arrangement).

**Capital Gains Tax***For an Individual Investor*

So far as we are aware, in practice, capital gains derived by a foreign individual investor from the sale of overseas-listed shares are temporarily exempted from individual income tax.

*For a Corporation*

According to the Enterprise Income Tax Law and its implementation rules, a non-resident enterprise is subject to a 10% withholding tax for capital gains derived from the disposal of overseas-listed shares unless such payment is exempted or deducted pursuant to applicable double taxation treaties or otherwise. According to the Circular issued by the State Administration of Taxation on Issues regarding Income Tax Payable by Foreign Invested Enterprises, Foreign Enterprises and Individuals for Capital Gains Derived from the Disposal of Shares (Equity Interests) and Dividends (Guoshuifa [1993] No. 45), capital gains derived by a non-resident enterprise from the disposal of overseas-listed shares are temporarily exempted from withholding tax in China. However, this circular has been revoked in 2011. Therefore, technically, PRC withholding tax should be applied to non-resident enterprises on capital gains derived from the disposal of overseas-listed shares unless it is tax exempted under the applicable double tax treaty. So far as we are aware, practically, there is no consistent enforcement of the collection of such withholding tax in China at current stage. However, we are aware of cases where the PRC tax authorities try to levy PRC withholding tax when they became aware of the disposal of the overseas-listed shares that the profits from the disposal of shares are derived from China.

**Tax Treaties**

China has an income tax treaty with the United States that currently limits the rate of Chinese withholding tax to 10% for dividends paid to individuals and corporations that qualify for treaty benefits. However, this treaty does not offer reduced tax rates for capital gains.

However, if certain conditions under the double tax treaty are satisfied (*e.g.*, the shareholding in H-shares is less than 25% and the H-share company is not land rich ), the capital gains may be exempted from the 10% PRC withholding tax.

**Stamp Tax**

While no express exemption exists for the imposition of Chinese stamp tax on transfers of Overseas Shares pursuant to the Provisional Regulations of the People's Republic of China Concerning Stamp Tax effective on July 1, 1989, we are not aware of any circumstance under which Chinese stamp tax has actually been imposed on the transfer of Overseas Shares.

**Estate or Gift Tax**

China does not currently impose any estate or gift tax.



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*U.S. Taxation*

The following is a summary of the material U.S. federal income tax consequences of the ownership and disposition of H Shares or ADSs. The following discussion is not exhaustive of all possible tax considerations. This summary is based upon the Internal Revenue Code of 1986, as amended (the Code), regulations promulgated under the Code by the U.S. Treasury Department (including proposed and temporary regulations), rulings, current administrative interpretations and official pronouncements of the IRS, and judicial decisions, all as currently in effect and all of which are subject to differing interpretations or to change, possibly with retroactive effect. Such change could materially and adversely affect the tax consequences described below. No assurance can be given that the IRS will not assert, or that a court will not sustain, a position contrary to any of the tax consequences described below.

This discussion does not address state, local, or foreign tax consequences of the ownership and disposition of H Shares or ADSs. (See PRC Taxation above).

This summary is for general information only and does not address all aspects of U.S. federal income taxation that may be important to a particular holder in light of its investment or tax circumstances or to holders subject to special tax rules, such as: banks; financial institutions; insurance companies; dealers in stocks, securities, or currencies; traders in securities that elect to use a mark-to-market method of accounting for their securities holdings; tax-exempt organizations; real estate investment trusts; regulated investment companies; qualified retirement plans, individual retirement accounts, and other tax-deferred accounts; expatriates of the United States; persons subject to the alternative minimum tax; persons holding H Shares or ADSs as part of a straddle, hedge, conversion transaction, or other integrated transaction; persons who acquired H Shares or ADSs pursuant to the exercise of any employee stock option or otherwise as compensation for services; persons actually or constructively holding 10% or more of our voting stock; and U.S. Holders (as defined below) whose functional currency is other than the U.S. dollar.

**This discussion is not a comprehensive description of all of the U.S. federal tax consequences that may be relevant with respect to the ownership and disposition of H Shares or ADSs. We urge you to consult your own tax advisor regarding your particular circumstances and the U.S. federal income and estate tax consequences to you of owning and disposing of H Shares or ADSs, as well as any tax consequences arising under the laws of any state, local, or foreign or other tax jurisdiction and the possible effects of changes in U.S. federal or other tax laws.**

This summary is directed solely to persons who hold their H Shares or ADSs as capital assets within the meaning of Section 1221 of the Code, which generally means as property held for investment. For purposes of this discussion, the term U.S. Holder means a beneficial owner of H Shares or ADSs that is any of the following:

a citizen or resident of the United States or someone treated as a U.S. citizen or resident for U.S. federal income tax purposes;

a corporation (or other entity taxable as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the United States, any state thereof, or the District of Columbia;

an estate, the income of which is subject to U.S. federal income taxation regardless of its source;

a trust if a U.S. court can exercise primary supervision over the trust's administration and one or more U.S. persons have the authority to control all substantial decisions of the trust; or

a trust in existence on August 20, 1996 that has a valid election in effect under applicable Treasury Regulations to be treated as a U.S. person.

The term Non-U.S. Holder means a beneficial owner of H Shares or ADSs that is not a U.S. Holder. As described in Taxation of Non-U.S. Holders below, the tax consequences to a Non-U.S. Holder may differ substantially from the tax consequences to a U.S. Holder.

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If a partnership (including for this purpose any entity treated as a partnership for U.S. federal income tax purposes) is a beneficial owner of H Shares or ADSs, the U.S. federal income tax consequences to a partner in the partnership will generally depend on the status of the partner and the activities of the partnership. A holder of H Shares or ADSs that is a partnership and the partners in such partnership should consult their own tax advisors regarding the U.S. federal income tax consequences of the ownership and disposition of H Shares or ADSs.

### *ADSs*

As it relates to the ADSs, this discussion is based in part upon the representations of the depository and the assumption that each obligation in the deposit agreement and any related agreement will be performed in accordance with its terms.

Generally, a holder of ADSs will be treated as the owner of the underlying H Shares represented by those ADSs for U.S. federal income tax purposes. Accordingly, no gain or loss will be recognized if the holder exchanges ADSs for the underlying H Shares represented by those ADSs. The holder's adjusted tax basis in the H Shares will be the same as the adjusted tax basis of the ADSs surrendered in exchange therefor, and the holding period for the H Shares will include the holding period for the surrendered ADSs.

**Table of Contents***TAXATION OF U.S. HOLDERS*

The discussion in *Distributions on H Shares or ADSs* and *Dispositions of H Shares or ADSs* below assumes that we will not be treated as a PFIC for U.S. federal income tax purposes. For a discussion of the rules that apply if we are treated as a PFIC, see the discussion in *Passive Foreign Investment Company* below.

*Distributions on H Shares or ADSs*

*General.* Subject to the discussion in *Passive Foreign Investment Company* below, if you actually or constructively receive a distribution on H Shares or ADSs, you must include the distribution in gross income as a taxable dividend on the date of your (or in the case of ADSs, the depositary's) receipt of the distribution, but only to the extent of our current or accumulated earnings and profits, as calculated under U.S. federal income tax principles. Such amount must be included without reduction for any foreign taxes withheld. Dividends paid by us will not be eligible for the dividends received deduction allowed to corporations with respect to dividends received from certain domestic corporations. Dividends paid by us may or may not be eligible for preferential rates applicable to qualified dividend income, as described below.

To the extent a distribution exceeds our current and accumulated earnings and profits, it will be treated first as a non-taxable return of capital to the extent of your adjusted tax basis in the H Shares or ADSs, and thereafter as capital gain. Preferential tax rates for long term capital gain may be applicable to non-corporate U.S. Holders.

We do not intend to calculate our earnings and profits under U.S. federal income tax principles. Therefore, you should expect that a distribution will generally be reported as a dividend even if that distribution would otherwise be treated as a non-taxable return of capital or as capital gain under the rules described above.

*Qualified Dividend Income.* With respect to non-corporate U.S. Holders (*i.e.*, individuals, trusts, and estates), for taxable years beginning before January 1, 2013, dividends that are treated as qualified dividend income ( QDI ) are taxable at a maximum tax rate of 15% or 20%. In accordance with recent legislation, including the American Taxpayer Relief Act of 2012, for individuals earning U.S.\$400,000 or less per year or married couples filing jointly and earning U.S.\$450,000 or less per year, the maximum individual U.S. federal income tax rate applicable to QDI generally is 15%. For individuals earning more than U.S.\$400,000 per year or married couples filing jointly and earning more than U.S.\$450,000 per year, the maximum U.S. federal income tax rates will increase, effective January 1, 2013, to 20% for QDI. Among other requirements, dividends generally will be treated as QDI if either (i) our H Shares or ADSs are readily tradable on an established securities market in the United States, or (ii) we are eligible for the benefits of a comprehensive income tax treaty with the United States which includes an information exchange program and which is determined to be satisfactory by the U.S. Treasury. It is expected that our ADSs will be readily tradable as a result of being listed on the NYSE.

In addition, for dividends to be treated as QDI, we must not be a PFIC (as discussed below) for either the taxable year in which the dividend was paid or the preceding taxable year. We do not believe that we were a PFIC for the preceding taxable year or will be a PFIC for the current taxable year. However, please see the discussion under *Passive Foreign Investment Company* below. Additionally, in order to qualify for QDI treatment, you generally must have held the H Shares or ADSs for more than 60 days during the 121-day period beginning 60 days prior to the ex-dividend date. However, your holding period will be reduced for any period during which the risk of loss is diminished.

Moreover, a dividend will not be treated as QDI to the extent you are under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property. Since the QDI rules are complex, you should consult your own tax advisor regarding the availability of the preferential tax rates for dividends paid on H Shares or ADSs.

*Foreign Currency Distributions.* A dividend paid in foreign currency (*e.g.*, Hong Kong dollars or Chinese Renminbi) must be included in your income as a U.S. dollar amount based on the exchange rate in effect on the date such dividend is received, regardless of whether the payment is in fact converted to U.S. Dollars. If the dividend is converted to U.S. Dollars on the date of receipt, you generally will not recognize a foreign currency gain or loss. However, if you convert the foreign currency to U.S. Dollars on a later date, you must include in income any gain or loss resulting from any exchange rate fluctuations. The gain or loss will be equal to the difference between (i) the U.S. dollar value of the amount you included in income when the dividend was received and (ii) the amount that you receive on the conversion of the foreign currency to U.S. Dollars. Such gain or loss will generally be ordinary income or loss and U.S. source for U.S. foreign tax credit purposes.

*Foreign Tax Credits.* Subject to certain conditions and limitations, any foreign taxes paid on or withheld from distributions from us and not refundable to you may be credited against your U.S. federal income tax liability or, alternatively, may be deducted from your taxable income. This election is made on a year-by-year basis and applies to all foreign taxes paid by you or withheld from you that year.





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Distributions will constitute foreign source income for foreign tax credit limitation purposes. The foreign tax credit limitation is calculated separately with respect to specific classes of income. For this purpose, distributions characterized as dividends distributed by us will generally constitute passive category income or, in the case of certain U.S. Holders, general category income. Special limitations may apply if a dividend is treated as QDI (as defined above).

Since the rules governing foreign tax credits are complex, you should consult your own tax advisor regarding the availability of foreign tax credits in your particular circumstances.

### ***Dispositions of H Shares or ADSs***

Subject to the discussion in *Passive Foreign Investment Company* below, you generally will recognize taxable gain or loss realized on the sale or other taxable disposition of H Shares or ADSs equal to the difference between the U.S. dollar value of (i) the amount realized on the disposition (*i.e.*, the amount of cash plus the fair market value of any property received), and (ii) your adjusted tax basis in the H Shares or ADSs. Such gain or loss will be a capital gain or loss.

If you have held the H Shares or ADSs for more than one year at the time of disposition, such capital gain or loss will be long-term capital gain or loss. Preferential tax rates for long term capital gain will apply to non-corporate U.S. Holders. For individuals earning U.S.\$400,000 or less per year or married couples filing jointly and earning U.S.\$450,000 or less per year, the maximum individual U.S. federal income tax rate applicable to long term capital gain generally is 15%. For individuals earning more than U.S.\$400,000 per year or married couples filing jointly and earning more than U.S.\$450,000 per year, the maximum U.S. federal income tax rates will increase, effective January 1, 2013, to 20% for long term capital gain. If you have held the H Shares or ADSs for one year or less, such capital gain or loss will be short term capital gain or loss taxable as ordinary income at your marginal income tax rate. The deductibility of capital losses is subject to limitations.

Generally, any gain or loss recognized will not give rise to foreign source income for U.S. foreign tax credit purposes.

You should consult your own tax advisor regarding the U.S. federal income tax consequences if you receive currency other than U.S. Dollars upon the disposition of H Shares or ADSs.

### ***Passive Foreign Investment Company***

We generally will be a PFIC under Section 1297 of the Code if, for a taxable year, either (a) 75% or more of our gross income for such taxable year is passive income (the *income test*) or (b) 50% or more of the average percentage, generally determined by fair market value, of our assets during such taxable year either produce passive income or are held for the production of passive income (the *asset test*). Passive income includes, for example, dividends, interest, certain rents and royalties, certain gains from the sale of stock and securities, and certain gains from commodities transactions.

Certain *look through* rules apply for purposes of the income and asset tests described above. If we own, directly or indirectly, 25% or more of the total value of the outstanding shares of another corporation, we generally will be treated as if we (a) held directly a proportionate share of the other corporation's assets, and (b) received directly a proportionate share of the other corporation's income. In addition, passive income does not include any interest, dividends, rents, or royalties that are received or accrued by us from a *related person* (as defined in Section 954(d)(3) of the Code), to the extent such items are properly allocable to income of such related person that is not passive income.

Under the income and asset tests, whether or not we are a PFIC will be determined annually based upon the composition of our income and the composition and valuation of our assets, all of which are subject to change. In determining that we are not a PFIC, we are relying on our projected revenues and projected capital expenditures. If our actual revenues and capital expenditures do not match our projections, we may become a PFIC. For example, if we do not spend enough of the cash (a passive asset) we raise from any financing transactions we may undertake, the relative percentage of our passive assets will increase. In addition, our determination is based on a current valuation of our assets. We believe our valuation approach is reasonable. However, it is possible that the IRS will challenge the valuation of our assets, which may result in our being a PFIC.

We do not believe that we are currently a PFIC. However, because the PFIC determination is highly fact intensive and made at the end of each taxable year, there can be no assurance that we will not be a PFIC for the current or any future taxable year or that the IRS will not challenge our determination concerning our PFIC status.

*Default PFIC Rules under Section 1291 of the Code.* If we are treated as a PFIC with respect to a U.S. Holder, the U.S. federal income tax consequences to the U.S. Holder of the ownership and disposition of H Shares or ADSs will depend on whether such U.S. Holder makes an

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election to treat us as a qualified electing fund ( QEF ) under Section 1295 of the Code (a QEF Election ) or a mark-to-market election under Section 1296 of the Code (a Mark-to-Market Election ). A U.S. Holder owning H Shares or ADSs while we were or are a PFIC that has not made either a QEF Election or a Mark-to-Market Election will be referred to in this summary as a Non-Electing U.S. Holder.

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If you are a Non-Electing U.S. Holder, you will be subject to the default tax rules of Section 1291 of the Code with respect to:

any excess distribution paid on H Shares or ADSs, which means the excess (if any) of the total distributions received by you during the current taxable year over 125% of the average distributions received by you during the three preceding taxable years (or during the portion of your holding period for the H Shares or ADSs prior to the current taxable year, if shorter); and

any gain recognized on the sale or other taxable disposition (including a pledge) of H Shares or ADSs.

Under these default tax rules:

any excess distribution or gain will be allocated ratably over your holding period for the H Shares or ADSs;

the amount allocated to the current taxable year and any period prior to the first day of the first taxable year in which we were a PFIC will be treated as ordinary income in the current taxable year;

the amount allocated to each of the other years will be treated as ordinary income and taxed at the highest applicable tax rate in effect for that year; and

the resulting tax liability from any such prior years will be subject to the interest charge applicable to underpayments of tax.

In addition, notwithstanding any election you may make, dividends that you receive from us will not be eligible for the preferential tax rates applicable to QDI (as discussed above in *Distributions on H Shares or ADSs*) if we are a PFIC either in the taxable year of the distribution or the preceding taxable year, but will instead be taxable at rates applicable to ordinary income.

Special rules for Non-Electing U.S. Holders will apply to determine U.S. foreign tax credits with respect to foreign taxes imposed on distributions on H Shares or ADSs.

If we are a PFIC for any taxable year during which you hold H Shares or ADSs, we will continue to be treated as a PFIC with respect to you for all succeeding years during which you hold H Shares or ADSs, regardless of whether we actually continue to be a PFIC. If we are treated as a PFIC in any year with respect to you, you will be required to file an annual return on IRS Form 8621 regarding distributions received on H Shares or ADSs and any gain realized on the disposition of H Shares or ADSs.

*QEF Election.* We currently do not intend to furnish you annually with certain tax information that would permit you to make a QEF Election to avoid the adverse U.S. tax consequences associated with owning PFIC stock.

*Mark-to-Market Election.* U.S. Holders may make a Mark-to-Market Election, but only if the H Shares or ADSs are marketable stock. The H Shares or ADSs will be marketable stock as long as they are regularly traded on a qualified exchange. Stock is considered regularly traded for any calendar year during which it is traded (other than in de minimis quantities) on at least 15 days during each calendar quarter. Qualified exchanges include (a) a national securities exchange that is registered with the Securities and Exchange Commission, (b) the national market system established pursuant to section 11A of the Securities and Exchange Act of 1934, and (c) a foreign securities exchange that is regulated or supervised by a governmental authority of the country in which the market is located, provided that (i) such foreign exchange has trading volume, listing, financial disclosure, surveillance, and other requirements and the laws of the country in which such foreign exchange is located, together with the rules of such foreign exchange, ensure that such requirements are actually enforced, and (ii) the rules of such foreign exchange effectively promote active trading of listed stocks.

Since the H Shares are listed on a foreign exchange (*i.e.*, the HKSE Limited) and the IRS has yet to identify specific foreign exchanges that are qualified for this purpose, there can be no assurances that the H Shares will be marketable stock and will be regularly traded. As for the ADSs, they will be marketable stock as long as they remain listed on the NYSE and are regularly traded. There can be no assurances, however, that the

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ADSs will be treated, or continue to be treated, as regularly traded.

If you own (or owned) H Shares or ADSs while we are (or were) a PFIC and you make a Mark-to-Market Election, you generally will not be subject to the default rules of Section 1291 of the Code discussed above. Rather, you generally will be required to recognize ordinary income for any increase in the fair market value of the ADSs for each taxable year that we are a PFIC. You will also be allowed to deduct as an ordinary loss any decrease in the fair market value to the extent of net marked-to-market gain previously included in prior years. Your adjusted tax basis in the ADSs will be adjusted to reflect the amount included or deducted.

The Mark-to-Market Election will be effective for the taxable year for which the election is made and all subsequent taxable years, unless the ADSs cease to be marketable stock or the IRS consents to the revocation of the election. You should consult your own tax advisor regarding the availability of, and procedure for making, a Mark-to-Market Election.

Since the PFIC rules are complex, you should consult your own tax advisor regarding them and how they may affect the U.S. federal income tax consequences of the ownership and disposition of H Shares or ADSs.

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### ***3.8% Medicare tax on net investment income***

With respect to taxable years beginning after December 31, 2012, certain U.S. persons, including individuals, estates and trusts, will be subject to an additional 3.8% Medicare tax on unearned income. For individuals, the additional Medicare tax applies to the lesser of (i) net investment income or (ii) the excess of modified adjusted gross income over \$200,000 (\$250,000 if married and filing jointly or \$125,000 if married and filing separately). Net investment income generally equals the taxpayer's gross investment income reduced by the deductions that are allocable to such income.

You should consult your tax advisors regarding the implications of the additional Medicare tax resulting from your ownership and disposition of H Shares or ADSs.

### ***Information reporting regarding PFICs and specified foreign financial assets***

If we are treated as a PFIC in any year with respect to you, you will be required to file an annual return on IRS Form 8621 regarding distributions received on H Shares or ADSs and any gain realized on the disposition of H Shares or ADSs.

Certain U.S. Holders who are individuals (and under proposed regulations, certain entities) may be required to report information relating to an interest in our H Shares or ADSs, subject to certain exceptions (including an exception for shares held in accounts maintained by U.S. financial institutions). U.S. Holders are urged to consult their tax advisors regarding their information reporting obligations, if any, with respect to their ownership and disposition of our H Shares or ADSs. In the event a U.S. Holder does not file the information reports described above relating to ownership of a PFIC or disclosure of specified foreign financial assets, the statute of limitations on the assessment and collection of U.S. federal income taxes of such U.S. holder for the related tax year will not close before such report is filed.

If you are a U.S. Holder, you are urged to consult with your own tax advisor regarding the application of the PFIC and specified foreign financial assets information reporting requirements and related statute of limitations tolling provisions with respect to our common shares.

### ***Information Reporting and Backup Withholding***

Generally, information reporting requirements will apply to distributions on H Shares or ADSs or proceeds from the disposition of H Shares or ADSs paid within the United States (and, in certain cases, outside the United States) to a U.S. Holder unless such U.S. Holder is an exempt recipient, such as a corporation. Furthermore, backup withholding (currently at 28%) may apply to such amounts unless such U.S. Holder (i) is an exempt recipient that, if required, establishes its right to an exemption, or (ii) provides its taxpayer identification number, certifies that it is not currently subject to backup withholding, and complies with other applicable requirements.

A U.S. Holder may generally avoid backup withholding by furnishing a properly completed IRS Form W-9.

Backup withholding is not an additional tax. Rather, amounts withheld under the backup withholding rules may be credited against your U.S. federal income tax liability. Furthermore, you may obtain a refund of any excess amounts withheld by filing an appropriate claim for refund with the IRS and furnishing any required information in a timely manner.

## ***TAXATION OF NON-U.S. HOLDERS***

### ***Distributions on H Shares or ADSs***

Subject to the discussion in *Information Reporting and Backup Withholding* below, as a Non-U.S. Holder, you generally will not be subject to U.S. federal income tax, including withholding tax, on distributions received on H Shares or ADSs, unless the distributions are effectively connected with a trade or business that you conduct in the United States (and, if an applicable income tax treaty so requires, attributable to a permanent establishment that you maintain in the United States).

If distributions are effectively connected with a U.S. trade or business (and, if applicable, attributable to a U.S. permanent establishment), you generally will be subject to tax on such distributions in the same manner as a U.S. Holder, as described in *Taxation of U.S. Holders Distributions on H Shares or ADSs* above. In addition, any such distributions received by a corporate Non-U.S. Holder may also, under certain circumstances, be subject to an additional branch profits tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty.

*Dispositions of H Shares or ADSs*

Subject to the discussion in Information Reporting and Backup Withholding below, as a Non-U.S. Holder, you generally will not be subject to U.S. federal income tax, including withholding tax, on any gain recognized on a sale or other taxable disposition of H Shares or ADSs, unless (i) the gain is effectively connected with a trade or business that you conduct in the United States (and, if an applicable income tax treaty so requires, attributable to a permanent establishment that you maintain in the United States), or (ii) you are an individual and are present in the United States for at least 183 days in the taxable year of the disposition, and certain other conditions are met.

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If you meet the test in clause (i) above, you generally will be subject to tax on any gain that is effectively connected with your conduct of a trade or business in the United States in the same manner as a U.S. Holder, as described in *Taxation of U.S. Holders* *Dispositions of H Shares or ADSs* above. Effectively connected gain realized by a corporate Non-U.S. Holder may also, under certain circumstances, be subject to an additional *branch profits tax* at a 30% rate or such lower rate as may be specified by an applicable income tax treaty.

If you meet the test in clause (ii) above, you generally will be subject to tax at a 30% rate on the amount by which your U.S. source capital gain exceeds your U.S. source capital loss.

### ***Information Reporting and Backup Withholding***

Payments to Non-U.S. Holders of distributions on, or proceeds from the disposition of, H Shares or ADSs are generally exempt from information reporting and backup withholding. However, a Non-U.S. Holder may be required to establish that exemption by providing certification of non-U.S. status on an appropriate IRS Form W-8.

Backup withholding is not an additional tax. Rather, amounts withheld under the backup withholding rules may be credited against your U.S. federal income tax liability. Furthermore, you may obtain a refund of any excess amounts withheld by filing an appropriate claim for refund with the IRS and furnishing any required information in a timely manner.

### ***F. Dividends and Paying Agents.***

Not applicable.

### ***G. Statement by Experts.***

Not applicable.

### ***H. Documents on Display.***

We are subject to the periodic reporting and other informational requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Under the Exchange Act, we are required to file reports and other information with the Securities and Exchange Commission. Specifically, we are required to file annually a Form 20-F no later than four months after the close of each fiscal year, which is December 31 of each year. Copies of reports and other information, when so filed, may be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at 100 F Street, N.E., Washington, D.C. 20549. You can request copies of these documents upon payment of a duplicating fee, by writing to the SEC. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference rooms. The SEC also maintains a Web site at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short- swing profit recovery provisions contained in Section 16 of the Exchange Act.

## **ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

### ***Interest Rate Risk***

We are subject to risk resulting from fluctuations in interest rates. Our debts are fixed and variable rate bank and other loans, with original maturities ranging from 1 to 5 years. Accordingly, fluctuations in interest rates can lead to significant fluctuations in the fair value of such debt instruments. We had no program of interest rate hedging activities and did not engage in any such activities in 2011 or 2012.



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The following table provides information, by maturity date, regarding our interest rate sensitive financial instruments, which consist of fixed and variable rate short term and long term debt obligations, as of December 31, 2012 and 2011.

	As of December 31, 2012					Total Recorded Amount	Fair Value
	2013	2014	2015	2016	2017		
(RMB equivalent in thousands, except interest rates)							
<b>Fixed rate bank and other loans</b>							
In U.S. Dollars							
Average interest rate							
In RMB	3,183,998					3,183,998	3,183,998
Average interest rate <sup>(1)</sup>	4.95%					4.95%	
<b>Variable rate bank and other loans</b>							
In U.S. Dollars							
Average interest rate <sup>(1)</sup>	2.02%					2.02%	
In RMB		370,560	427,020	433,760		1,231,340	1,192,960
Average interest rate <sup>(1)</sup>		6.01%	6.01%	6.01%		6.01%	

(1) The average interest rates for variable rate bank and other loans are calculated based on the year end indices.

	As of December 31, 2011					Total Recorded Amount	Fair Value
	2012	2013	2014	2015	2016		
(RMB equivalent in thousands, except interest rates)							
<b>Fixed rate bank and other loans</b>							
In U.S. Dollars							
Average interest rate							
In RMB	889,500	125,000			35,050	1,049,550	1,048,221
Average interest rate <sup>(1)</sup>	5.54%	5.36%			6.89%	5.56%	
<b>Variable rate bank and other loans</b>							
In U.S. Dollars							
Average interest rate <sup>(1)</sup>	2.33%					2.33%	

(1) The average interest rates for variable rate bank and other loans are calculated based on the year end indices.

**Exchange Rate Risk**

We are also exposed to foreign currency exchange rate risk as a result of our foreign currency denominated short term debt and, to a limited extent, cash and cash equivalents denominated in foreign currencies. The following table provides information, by maturity date, regarding our foreign currency exchange rate sensitive financial instruments, which consist of cash and cash equivalents, short term debt obligations as of December 31, 2012 and 2011.

	As of December 31, 2012						Total Recorded Amount	Fair Value
	2013	2014	2015	2016	2017	Thereafter		
(RMB equivalent in thousands, except interest rates)								
<b>On-balance sheet financial instruments</b>								
Cash and cash equivalents:								

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In Hong Kong Dollars	780	780	780
In U.S. Dollars	148	148	148
In Euro			
In Japanese Yen			
In Swiss Frank			
Debt:			
Fixed rate bank and other loans in U.S. Dollars			
Average interest rate <sup>(1)</sup>			
Variable rate bank and other loans in U.S. Dollars	7,839,879	7,839,879	7,839,879
Average interest rate <sup>(1)</sup>	2.02%	2.02%	

(1) The average interest rates for variable rate bank and other loans are calculated based on the year end indices.

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	As of December 31, 2011					Total Recorded Amount	Fair Value
	2012	2013	2014	2015	2016 Thereafter		
(RMB equivalent in thousands, except interest rates)							
<b>On-balance sheet financial instruments</b>							
<b>Cash and cash equivalents:</b>							
In Hong Kong Dollars	669					669	669
In U.S. Dollars	1,471					1,471	1,471
In Euro							
In Japanese Yen							
In Swiss Frank	923					923	923
<b>Debt:</b>							
<b>Fixed rate bank and other loans in</b>							
<b>U.S. Dollars</b>							
Average interest rate							
<b>Variable rate bank and other loans in</b>							
<b>U.S. Dollars</b>							
Average interest rate <sup>(1)</sup>	4,622,574					4,622,574	4,622,574
	2.33%					2.33%	

(1) The average interest rates for variable rate bank and other loans are calculated based on the year end indices.

**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES.**

In connection with our ADS program, a holder of our ADSs may have to pay, either directly or indirectly, certain fees and charges, as described in Item 12.D.3. In addition, we receive fees and other direct and indirect payments from The Bank of New York Mellon that are related to our ADS as described in Item 12.D.4.

**12D.3 Fees and Charges that a holder of our ADSs May Have to Pay**

The Bank of New York Mellon collects its fees for delivery and surrender of ADSs directly from investors depositing shares or surrendering ADSs for the purpose of withdrawal or from intermediaries acting for them. The Bank of New York Mellon also collects fees for making distributions to investors by deducting those fees from the amounts distributed or by selling a portion of distributable property to pay the fees. The Bank of New York Mellon may collect its annual fee for depositary services by deductions from cash distributions.

**Persons depositing or withdrawing shares must pay:**

\$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)

A fee equivalent to the fee that would be payable if securities distributed to you had been shares and the shares had been deposited for issuance of ADSs

A fee of \$.05 (or less) per ADS (or portion thereof)

Registration or transfer fees

Expenses of The Bank of New York Mellon

**For:**

Issuance and withdrawal of ADSs, including issuances resulting from a distribution of shares or rights or other property

Distribution of securities distributed to holders of deposited securities which are distributed by The Bank of New York Mellon to ADS registered holders

Any cash distribution made pursuant to the Deposit Agreement

Transfer and registration of shares on our share register to or from the name of the depositary or its agent when you deposit or withdraw shares

Cable, telex and facsimile transmissions (when expressly provided in the Deposit Agreement);

Converting foreign currency to U.S. Dollars

As necessary

Taxes and other governmental charges The Bank of New York Mellon or the custodian have to pay on any ADS or share underlying an ADS, for example, stock transfer taxes, stamp duty or withholding taxes

Any charges incurred by The Bank of New York Mellon or its agents for servicing the deposited securities As necessary

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***12D.4 Fees and Other Payments Made by The Bank of New York Mellon***

From January 1, 2012 through March 31, 2013, a total of U.S.\$69,484.38 was paid by The Bank of New York Mellon on our behalf for our ADSs program. Specifically, the following fees were paid on our behalf: U.S.\$19,905.77 for standard out-of-pocket maintenance costs for the ADSs program (primarily consisting of expenses related to our Annual General Meeting), and U.S.\$49,578.61 for investor relations services from third party vendors.

**PART II**

**ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES.**

None.

**ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS.**

On May 11, 2011, we entered into an Amended and Restated Deposit Agreement with The Bank of New York Mellon, as Depositary (the Restated Deposit Agreement ), and updated the form of American Depositary Receipt (the ADR ) evidencing the ADSs issued under the terms of the Restated Deposit Agreement. The Restated Deposit Agreement restates our original Deposit Agreement with The Bank of New York (the predecessor of The Bank of New York Mellon), dated as of July 23, 1993 (as amended, the 1993 Deposit Agreement ), in its entirety.

We and The Bank of New York Mellon entered into the Restated Deposit Agreement to modify the ADSs voting process and to bring our arrangements with The Bank of New York Mellon in line with the current customary market practice regarding depositary arrangements.

By the Restated Deposit Agreement, subject to the Depositary's obligation to notice the owner of ADSs any meeting of holders of our shares or other deposited securities, and subject further to certain exceptions as provided therein, to the extent that no instructions are received by the Depositary from an owner of ADSs on or before the date established by the Depositary, the Depositary may deem instructions by the owner of the ADS have been given to give a discretionary proxy to a person designated by us to exercise voting rights in the meeting of holders of our shares or other deposited securities.

In addition, the Restated Deposit Agreement amends the 1993 Deposit Agreement, among other things, to (i) provide the American Depositary Shares may be uncertificated securities or certificated securities evidenced by ADRs, and (ii) change the fees and charges of the Depositary, see Item 12D.3 Fees and Charges that a holder of our ADSs May Have to Pay.

The foregoing descriptions of the Restated Deposit Agreement and the ADR do not purport to be complete and are qualified in their entirety by reference to the complete Restated Deposit Agreement and ADR which are incorporated herein by reference to Exhibit 2 and the forms filed on Form F-6 (File number 033-65616) on May 4, 2011.

**ITEM 15. CONTROLS AND PROCEDURES**

***A. Evaluation of disclosure controls and procedures.***

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. These rules refer to the controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods. This includes controls and procedures designed to ensure that information required to be disclosed is accumulated and communicated to our management, including our principal executive officer or officers and principal financial officer or officers, to allow timely decisions regarding required disclosure.

We maintain a written policy adopted by our board of directors that governs the collection, coordination and disclosure of information to our shareholders, the public and to governmental and other regulatory bodies. All such disclosures are coordinated by the Secretary and subject to execution by either the Chairman of the Board or, for disclosures by our Supervisory Board, the Chairman of the Supervisory Board. Under the policy, all material issues must be disclosed and our disclosures must be true, accurate, complete and timely without any false or misleading statements. Each of our departments and subsidiaries has their own supplemental policies which may be both written and unwritten.

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Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) of the Securities Exchange Act of 1934) as of the end of the fiscal year covered by this annual report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the fiscal year covered by this annual report, our disclosure controls and procedures were adequate and effective to ensure that information required to be disclosed in the reports we file under the Exchange Act is accumulated and communicated to the management to allow timely decisions to be made regarding required disclosures, and is recorded, processed, summarized and reported as and when required.

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***B. Management's assessment report on the internal control***

Our management is accountable for establishing and maintaining effective internal control over financial reporting (as defined in Rules 13a-15(f) of the Securities Exchange Act of 1934). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives and may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting based upon the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission as of December 31, 2012. Based on that evaluation, our management has concluded that our internal control over financial reporting was effective as of December 31, 2012 based on these criteria.

KPMG, an independent registered public accounting firm, has audited the consolidated financial statements included in this annual report on Form 20-F and, as part of the audit, has issued a report, included herein, on the effectiveness of our internal control over financial reporting.

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***C. Report of Independent Registered Public Accounting Firm.***

The Board of Directors and Shareholders of

Sinopec Shanghai Petrochemical Company Limited:

We have audited Sinopec Shanghai Petrochemical Company Limited's internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Sinopec Shanghai Petrochemical Company Limited's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the management's Assessment Report on the Internal Control. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Sinopec Shanghai Petrochemical Company Limited maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Sinopec Shanghai Petrochemical Company Limited and subsidiaries as of December 31, 2011 and 2012, and the related consolidated statements of operations, comprehensive income, changes in equity and cash flows for each of the years in the three-year period ended December 31, 2012, and our report dated March 27, 2013 expressed an unqualified opinion on those consolidated financial statements.

/s/ **KPMG**

Hong Kong, China

March 27, 2013



**Table of Contents*****D. Changes in internal control over financial reporting.***

For the year ended December 31, 2012, there have been no significant changes to our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

**ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

We currently have an audit committee financial expert, Cai Tingji, serving on our audit committee and he is an independent director as defined in 17 CFR 240.10A-3.

**ITEM 16B. CODE OF ETHICS**

We have not adopted a code of ethics as defined by the applicable U.S. securities regulations that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions since it is not a customary practice for a PRC company to adopt such code of ethics.

**ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The following table summarizes the fees charged by KPMG, our principal accountant, for certain services rendered to us during 2011 and 2012.

	<b>For the year ended December 31, (in thousands of RMB)</b>	
	<b>2011</b>	<b>2012</b>
Audit fees (1)	8,500	8,850
Audit-related fees (2)		
Tax fees (3)		
All other fees (4)		
<b>Total</b>	<b>8,500</b>	<b>8,850</b>

- (1) Audit fees means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors for the audit of our annual financial statements.
- (2) Audit-related fees means the aggregate fees billed in each of the fiscal years listed for assurance and related services rendered by our principal auditors for the audit of our financial information.
- (3) Tax fees means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors for tax compliance, tax advice and tax planning.
- (4) All other fees means the aggregate fees billed in each of the fiscal years listed for products and services provided by the our principal accountant, other than the services reported under audit fees, audit-related fees and tax fees.

***Audit Committee Pre-approval Policies and Procedures***

Our audit committee has adopted procedures which set forth the manner in which the committee will review and approve all audit and non-audit services to be provided by KPMG. The pre-approval procedures are as follows:

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Any audit or non-audit service to be provided to us by the independent accountant must be (i) pre-approved by the audit committee; or (ii) pre-approved by one or several committee members designated by the committee and rectified by the audit committee.

### **ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES.**

We have not been granted an exemption from the applicable listing standards for the audit committee of our board of directors.

### **ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS.**

None.

**ITEM 16F. CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT.**

KPMG has served as our principal accountants for the audit of our consolidated financial statements since 1993. On March 27, 2013, our board of directors approved the proposed change of our principal accountants, KPMG, after the completion of the audit of our consolidated financial statements for the year ended December 31, 2012 and the effectiveness of our internal control over financial reporting as of December 31, 2012, based on recommendation from our audit committee. Such change in our principal accountants is due to the relevant regulations issued by the Ministry of Finance and the State-owned Assets Supervision and Administration Commission of the PRC. According to the relevant regulations, there are certain limits to the number of years for which an auditor may continuously undertake financial auditing work in respect of a state-owned enterprise and its subsidiaries. As a result, KPMG will not be re-appointed as our principal accountants for the year ending December 31, 2013.

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The audit reports of KPMG on our consolidated financial statements as of and for the fiscal years ended December 31, 2011 and 2012 contain no adverse opinion or disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope, or accounting principles.

During the two fiscal years ended December 31, 2011 and 2012 and through April 30, 2013, there have been no disagreements with KPMG on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements if not resolved to the satisfaction of KPMG, would have caused them to make reference to the subject matter of the disagreement in connection with their report, nor have there been any reportable events (as defined in Item 16F(a)(1)(v) of Form 20-F). We have provided a copy of the foregoing disclosure to KPMG and requested that KPMG furnish a letter addressed to the SEC stating whether or not KPMG agrees with such disclosure. A copy of the letter from KPMG addressed to the SEC, dated April 30, 2013, is filed as Exhibit 15.1 to this Form 20-F.

With the approvals of our board and the audit committee, we resolved to appoint PricewaterhouseCoopers and PricewaterhouseCoopers Zhong Tian CPAs Limited Company (the name will be changed to PricewaterhouseCoopers Zhong Tian LLP), or PwC as our principal accountants for the year 2013, which is subject to the approval of shareholders at our forthcoming 2012 annual general meeting.

During the two most recent fiscal years and through April 30, 2013, neither we nor anyone on our behalf consulted PwC regarding either (i) the application of accounting principles to a specified transaction, either completed or proposed; or the type of audit opinion that might be rendered on the registrant's financial statements, or (ii) any matter that was either the subject of a disagreement (as defined in Item 16F(a)(1)(iv) of Form 20-F and related instructions to Item 16-F of Form 20-F) with PwC or a reportable event (as described in Item 16F(a)(1)(v) of Form 20-F). Also, during the two most recent fiscal years and through April 30, 2013, we have not obtained any written report or oral advice that PwC concluded was an important factor considered by us in reaching a decision as to the accounting, auditing or financial reporting issue.

**ITEM 16G. CORPORATE GOVERNANCE.**

Set forth below is a summary of the significant differences between the corporate governance rules of the NYSE and those of the People's Republic of China for listed companies:

	NYSE Corporate Governance Rules	The Company's Corporate Governance Practices
Director Independence	A listed company must have a majority of independent directors on its board of directors. The board of directors needs to affirmatively determine that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company). In addition, a director must meet certain standards to be deemed independent.	(which conform with the corporate governance rules for companies organized and listed in the People's Republic of China)  It is required in China that no less than 1/3rd of the board members of any listed company must be independent directors, and the listed company must set forth specific requirements for the qualification and election of independent directors in compliance with PRC laws. For example, an independent director shall not hold any other position in the listed company other than being a director and shall not be influenced by the main shareholders or the controlling persons of the listed company, or by any other entities or persons with whom the listed company has a significant relationship.

The Company has complied with the relevant Chinese corporate governance rules and has implemented internal rules governing the independence and responsibilities of independent directors. The Company determines the independence of independent directors every year.

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	The non-management directors of each listed company must meet at regularly scheduled executive sessions without management.	No similar requirements.
Nominating/Corporate Governance Committee	Listed companies must have a nominating/corporate governance committee composed entirely of independent directors.	The board of directors can establish a nominating committee if the shareholders pass resolutions to establish such a committee. A majority of the directors on the committee shall be independent directors, who shall act as the convener. The board of directors, which formulates relevant written guidelines with respect to the nomination of directors, has established a nominating committee with a majority of the members being independent directors.
	The nominating/corporate governance committee must have a written charter that addresses:	Relevant responsibilities of the nominating committee are similar to those stipulated by the NYSE rules, but the main responsibilities do not include the research and recommendation of corporate governance guidelines, the supervision of the evaluation of the board of directors and management, or the annual evaluation of the committee.
	(i) the committee's purpose and responsibilities - which, at minimum, must be to: identify individuals qualified to become board members, consistent with criteria approved by the board, and to select, or to recommend that the board select, the director nominees for the next annual meeting of shareholders; develop and recommend to the board a set of corporate governance guidelines applicable to the corporation; and oversee the evaluation of the board and management; and	
	(ii) an annual performance evaluation of the committee.	
Compensation Committee	Listed companies must have a compensation committee composed entirely of independent directors.	The board of directors can establish a compensation and assessment committee if the shareholders pass resolutions to establish such a committee. A majority of the directors on the committee shall be independent directors, who shall act as the convener.
	The purposes and responsibilities of the compensation committee stated in its charter must include:	The responsibilities of the compensation and assessment committee include:
	(1) reviewing and approving the corporate goals and objectives associated with the CEO's compensation, evaluate the performance of the CEO in fulfilling these goals and objectives, and, either as a committee or together with the other independent directors (as directed by the	(1) reviewing the standards for the evaluation of directors and management, evaluate directors and management and report the results of such evaluation to the board of directors; and

board), determine and approve the CEO's compensation level based on such evaluation; (2) reviewing compensation policies and benefit plans for directors and executive officers.

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	<p>(2) making recommendations to the board with respect to non-CEO executive officer compensation, and incentive-compensation and equity-based plans that are subject to board approval; and</p> <p>(3) producing a committee report on executive compensation as required by the SEC to be included in the annual proxy statement or annual report filed with the SEC. The charter must also include the requirement for an annual performance evaluation of the compensation committee.</p>	<p>Unlike the NYSE rules, the PRC rules do not require the committee to produce a report on the executive compensation or make an annual performance evaluation of the committee. In addition, the compensation committee evaluates and reviews the compensation of directors as well as executive officers.</p> <p>The board of directors of the Company has established a compensation evaluation committee with a majority of the members being independent directors who act as the convener, and the committee has established a written charter complying with the domestic corporate governance rules.</p>
<p>Audit Committee</p>	<p>Listed companies must have an audit committee that satisfies the requirements of Rule 10A-3 of the Securities Exchange Act of 1934, as amended (the Exchange Act ). It must have a minimum of three members, and all audit committee members must satisfy the requirements for independence set forth in Section 303A.02 of the NYSE Corporate Governance Rules and , in the absence of an applicable exemption, Rule 10A-3b(1) of the Exchange Act.</p> <p>The written charter of the audit committee must specify that the purpose of the audit committee is to assist the board oversight of the integrity of financial statements, the company's compliance with legal and regulatory requirements, the qualifications and independence of the independent auditors, the performance of the listed company's internal audit function and independent auditors.</p> <p>The written charter must also require the audit committee to prepare an audit committee report as required by the SEC to be included in the listed company's annual proxy statement as well as an annual performance evaluation of the audit committee.</p> <p>The written charter must also address the duties and responsibilities of the audit committee as required under Section 303A.07 of the NYSE Corporate Governance Rules. Each listed company must maintain an internal audit function to provide management and the audit committee with ongoing assessments of the listed company's risk management processes and system of internal controls.</p>	<p>The board of directors of a listed company can, through the resolution of the shareholders' meeting, establish an audit committee composed entirely of directors, of which the independent directors are the majority and act as the convener, and, at minimum, one independent director is an accounting professional.</p> <p>The purpose, authority and responsibilities of the audit committee are similar to those stipulated by the NYSE rules, but according to customary practices in China, the Company is not required to make an annual performance evaluation of the audit committee, and the audit committee is not required to prepare an audit report to be included in the Company's annual proxy statement. The board of directors of the Company has established an audit committee that satisfies Rule 10A-3 under the Securities Exchange Act of 1934, as amended and relevant domestic requirements. The audit committee has a written charter.</p> <p>China has a similar regulatory provision, and the Company has an internal audit department.</p>





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Equity Compensation	Shareholders must be given the opportunity to vote on all equity compensation plans and material revisions thereto, except for employment inducement awards, certain grants, plans and amendments in the context of mergers and acquisitions, and certain specific types of plans as described under Section 303A.08 of the NYSE Corporate Governance Rules.	The relevant regulations of China require the board of directors propose plans on the amount and types of director compensation for the shareholders meeting to approve. The compensation plan of executive officers shall be approved by the board and announced at the shareholders meeting and disclosed to the public upon the approval of the board of directors.
Corporate Governance Guidelines	Listed companies must adopt and disclose corporate governance guidelines involving director qualification standards, director responsibilities, director compensation, director access to management and, as necessary and appropriate, independent advisors, director orientation and continuing education and management succession. The board should conduct a self-evaluation at least annually to determine whether it and its committees are functioning effectively.  A listed company must make its corporate governance guidelines available on or through its website.	The China Securities Regulatory Commission (the CSRC ) has issued the Corporate Governance Rules, prescribing detailed guidelines on directors of the listed companies, including director selection, the structure of the board of directors and director performance evaluation.  The Company has complied with the above mentioned rules.
Code of Ethics for Directors, Officers and Employees	Listed companies must adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers. Each listed company may determine its own policies, but all listed companies should address the most important topics, including, among others, conflicts of interest, corporate opportunities, confidentiality, fair dealing, protection and proper use of listed company assets, compliance with laws, rules and regulations (including insider trading laws), and encouraging the reporting of any illegal or unethical behavior.  Each listed company CEO must certify to the NYSE each year that he or she is not aware of any violation by the company of NYSE corporate governance listing standards and he or she must promptly notify the NYSE in writing of any non-compliance with any applicable provisions of Section 303A.	There is no such requirement for a code for ethics in China. As the directors and officers of the Company have all signed a Director Service Agreement, however, they are bound by their fiduciary duties to the Company. In addition, the directors and officers must perform their legal duties in accordance with the Company Law of the PRC, relevant requirements of CSRC and Mandatory Provisions to the Charter of Companies Listed Overseas.  No similar requirements.

**ITEM 16H. MINE SAFETY DISCLOSURE.**  
Not applicable.

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**PART III**

**ITEM 17. FINANCIAL STATEMENTS.**

See pages F-1 to F-68.

**ITEM 18. FINANCIAL STATEMENTS.**

We have elected to provide the financial statements and related information specified in Item 17 in lieu of the information called for by this Item 18.

**ITEM 19. EXHIBITS**

<b>No.</b>	<b>Exhibit</b>
1.1	Translation of the amended and restated Articles of Association of Sinopec Shanghai Petrochemical Company Limited (incorporated by reference to Exhibit 1.1 of our annual report on Form 20-F (File No. 001-12158) filed with the Commission on June 27, 2011).
2.	Amended and Restated Deposit Agreement between Sinopec Shanghai Petrochemical Company Limited and The Bank of New York Mellon dated May 11, 2011 (incorporated by reference to Exhibit 2 of our annual report on Form 20-F (File No. 001-12158) filed with the Commission on April 30, 2012).
4.1	Translation of the Product Supply and Sales Services Framework Agreement between Sinopec Shanghai Petrochemical Company Limited and China Petroleum & Chemical Corporation (incorporated by reference to Exhibit 4.1 of our annual report on Form 20-F (File No. 001-12158) filed with the Commission on June 27, 2011).
4.2	Translation of the Comprehensive Services Framework Agreement between Sinopec Shanghai Petrochemical Company Limited and China Petrochemical Corporation (incorporated by reference to Exhibit 4.2 of our annual report on Form 20-F (File No. 001-12158) filed with the Commission on June 27, 2011).
8	A list of subsidiaries of Sinopec Shanghai Petrochemical Company Limited.
12.1	Certification of President Required by Rule 13a-14(a).
12.2	Certification of Chief Financial Officer Required by Rule 13a-14(a).
13.1	Certification of President Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
13.2	Certification of Chief Financial Officer Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
15.1	Letter from KPMG regarding Item 16F of this annual report.

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**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

**SINOPEC SHANGHAI PETROCHEMICAL**

**COMPANY LIMITED**

Date: April 30, 2013

*/s/ WANG ZHIQING*  
**Wang Zhiqing, President**

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**Sinopec Shanghai Petrochemical Company Limited**

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**Years Ended December 31, 2010, 2011 and 2012**

**Consolidated Financial Statements of Sinopec Shanghai Petrochemical Company Limited**

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders of

Sinopec Shanghai Petrochemical Company Limited:

We have audited the accompanying consolidated balance sheets of Sinopec Shanghai Petrochemical Company Limited and subsidiaries (the Group) as of December 31, 2011 and 2012, and the related consolidated statements of operations, comprehensive income, changes in equity, and cash flows for each of the years in the three-year period ended December 31, 2012. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sinopec Shanghai Petrochemical Company Limited and subsidiaries as of December 31, 2011 and 2012, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2012, in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Sinopec Shanghai Petrochemical Company Limited's internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 27, 2013 expressed an unqualified opinion on the effectiveness of Sinopec Shanghai Petrochemical Company Limited's internal control over financial reporting.

/s/ **KPMG**

Hong Kong, China

March 27, 2013

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Balance Sheets

As of December 31, 2011 and 2012

(Amounts in thousands)

		December 31,	
		2011	2012
	Note	Renminbi	Renminbi
<u>Assets</u>			
Current assets:			
Cash and cash equivalents		91,346	160,962
Inventories	12	5,582,425	8,938,077
Amounts due from related parties	13, 25(c)	639,286	1,052,842
Trade debtors, net	13	121,936	93,484
Bills receivable	13	2,988,010	2,046,657
Other debtors and prepayments	14	242,811	599,402
Total current assets		9,665,814	12,891,424
Non-current assets:			
Property, plant and equipment, net	15(a)	12,501,980	17,468,748
Investment property	16	452,555	439,137
Construction in progress	17	3,852,692	612,388
Lease prepayments and other assets		825,250	1,131,123
Interest in associates and jointly controlled entities	18	2,901,305	2,867,153
Deferred tax assets	8(b)	519,269	1,052,573
Total non-current assets		21,053,051	23,571,122
Total assets		30,718,865	36,462,546

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Balance Sheets

As of December 31, 2011 and 2012

(Amounts in thousands)

		December 31,	
		2011	2012
	Note	Renminbi	Renminbi
<u>Liabilities and Shareholders' Equity</u>			
<b>Current liabilities:</b>			
Loans and borrowings	19	5,512,074	11,023,877
Amounts due to related parties	25(c)	2,242,868	3,411,279
Trade creditors		3,126,495	2,886,616
Bills payable		15,688	
Other creditors		1,352,367	1,603,022
Income tax payable		22,340	2,463
<b>Total current liabilities</b>		<b>12,271,832</b>	<b>18,927,257</b>
<b>Non-current liabilities:</b>			
Loans and borrowings	19	160,050	1,231,340
Deferred income	20	91,319	
<b>Total non-current liabilities</b>		<b>251,369</b>	<b>1,231,340</b>
<b>Total liabilities</b>		<b>12,523,201</b>	<b>20,158,597</b>
<b>Shareholders' equity:</b>			
Share capital	21	7,200,000	7,200,000
Reserves	22	10,725,563	8,837,166
<b>Total equity attributable to equity shareholders of the Company</b>		<b>17,925,563</b>	<b>16,037,166</b>
Non-controlling interests		270,101	266,783
<b>Total equity</b>		<b>18,195,664</b>	<b>16,303,949</b>
<b>Total liabilities and shareholders' equity</b>		<b>30,718,865</b>	<b>36,462,546</b>

See accompanying notes to consolidated financial statements.



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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Operations

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands, except per share data)

	Note	Years ended December 31,		
		2010 Renminbi	2011 Renminbi	2012 Renminbi
Sales	26(b)	77,520,699	95,518,856	93,008,338
Less: Sales taxes and surcharges		(5,424,817)	(6,009,203)	(5,791,064)
Net sales		72,095,882	89,509,653	87,217,274
Cost of sales	4	(68,317,413)	(87,881,160)	(88,617,789)
Gross profit/(loss)		3,778,469	1,628,493	(1,400,515)
Selling and administrative expenses		(628,761)	(675,771)	(649,906)
Other operating income	5	3,149,708	952,722	(2,050,421)
Other operating expenses	6	109,842	164,286	333,754
		(295,956)	(57,184)	(55,779)
Profit/(loss) from operations		2,963,594	1,059,824	(1,772,446)
Financing income		178,462	299,036	86,545
Financing expenses		(273,681)	(215,494)	(369,802)
Net financing (costs)/income	7	(95,219)	83,542	(283,257)
Investment income		215	685	6,446
Share of profit of associates and jointly controlled entities		661,288	152,655	32,784
Earnings/(loss) before income tax		3,529,878	1,296,706	(2,016,473)
Income tax	8(a)	(735,497)	(310,184)	511,331
Net income/(loss)		2,794,381	986,522	(1,505,142)
Attributable to:				
Equity shareholders of the Company		2,769,023	956,106	(1,528,397)
Non-controlling interests		25,358	30,416	23,255
Net income/(loss)		2,794,381	986,522	(1,505,142)
Earnings/(loss) per share	9			
Basic		RMB 0.38	RMB 0.13	RMB (0.21)
Diluted		RMB 0.38	RMB 0.13	RMB (0.21)

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

	Note	Years ended December 31,		
		2010	2011	2012
		Renminbi	Renminbi	Renminbi
Net income/(loss)		2,794,381	986,522	(1,505,142)
Other comprehensive income for the year	11			
Total comprehensive income/(loss) for the year		2,794,381	986,522	(1,505,142)
Attributable to:				
Equity shareholders of the Company		2,769,023	956,106	(1,528,397)
Non-controlling interests		25,358	30,416	23,255
Total comprehensive income/(loss) for the year		2,794,381	986,522	(1,505,142)

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Changes in Equity

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

	Attributable to equity shareholders of the Company						Total
Note	Share capital Renminbi	Share premium Renminbi	Reserves Renminbi	Retained earnings Renminbi	Total Renminbi	Non-controlling interests Renminbi	Equity Renminbi
<b>Balance at January 1, 2010</b>	7,200,000	2,420,841	4,805,946	709,647	15,136,434	294,285	15,430,719
Changes in equity for 2010:							
Net income for the year				2,769,023	2,769,023	25,358	2,794,381
Other comprehensive income							
Total comprehensive income for the year				2,769,023	2,769,023	25,358	2,794,381
Dividends approved in respect of the previous year	10(b)			(216,000)	(216,000)		(216,000)
Appropriation of profits			279,548	(279,548)			
Dividends paid by subsidiaries to non-controlling shareholders						(59,790)	(59,790)
<b>Balance at December 31, 2010</b>	7,200,000	2,420,841	5,085,494	2,983,122	17,689,457	259,853	17,949,310

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Changes in Equity

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

	Attributable to equity shareholders of the Company						Total
Note	Share capital Renminbi	Share premium Renminbi	Reserves Renminbi	Retained earnings Renminbi	Total Renminbi	Non-controlling interests Renminbi	Equity Renminbi
<b>Balance at January 1, 2011</b>	7,200,000	2,420,841	5,085,494	2,983,122	17,689,457	259,853	17,949,310
Changes in equity for 2011:							
Net income for the year				956,106	956,106	30,416	986,522
Other comprehensive income							
Total comprehensive income for the year				956,106	956,106	30,416	986,522
Dividends approved in respect of the previous year	10(b)			(720,000)	(720,000)		(720,000)
Appropriation of profits	22		70,456	(70,456)			
Appropriation of safety production fund	22		21,777	(21,777)			
Dividends paid by subsidiaries to non-controlling shareholders						(20,168)	(20,168)
<b>Balance at December 31, 2011</b>	7,200,000	2,420,841	5,177,727	3,126,995	17,925,563	270,101	18,195,664

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Changes in Equity

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

	Note	Attributable to equity shareholders of the Company				Total Renminbi	Non-controlling interests Renminbi	Total Equity Renminbi
		Share capital Renminbi	Share premium Renminbi	Reserves Renminbi	Retained earnings Renminbi			
<b>Balance at January 1, 2012</b>		7,200,000	2,420,841	5,177,727	3,126,995	17,925,563	270,101	18,195,664
Changes in equity for 2012:								
Net (loss)/income for the year					(1,528,397)	(1,528,397)	23,255	(1,505,142)
Other comprehensive income								
Total comprehensive (loss)/income for the year					(1,528,397)	(1,528,397)	23,255	(1,505,142)
Dividends approved in respect of the previous year	10(b)				(360,000)	(360,000)		(360,000)
Utilization of safety production fund	22			(13,598)	13,598			
Dividends paid by subsidiaries to non-controlling shareholders							(26,573)	(26,573)
<b>Balance at December 31, 2012</b>		7,200,000	2,420,841	5,164,129	1,252,196	16,037,166	266,783	16,303,949

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

	Note	Years ended December 31,		
		2010	2011	2012
		Renminbi	Renminbi	Renminbi
Net cash generated from/(used in) operating activities	(a)	3,973,719	2,219,994	(2,066,385)
<b>Cash flows from investing activities:</b>				
Interest income received		37,375	99,345	86,545
Dividend income received		89,817	588,118	66,936
Proceeds from disposal of property, plant and equipment and other long term assets		66,347	70,344	24,504
Proceeds from disposal of investments		700,000	700,000	49,743
Capital expenditure		(1,356,845)	(3,481,235)	(4,259,859)
Purchase of investments and interests in associates			(786,751)	(30,000)
Net cash used in investing activities		(463,306)	(2,810,179)	(4,062,131)
<b>Cash flows from financing activities:</b>				
Proceeds from loans and borrowings		39,355,780	35,106,127	53,365,372
Proceeds from issuance of corporate bonds		1,000,000		
Repayment of loans and borrowings		(42,631,344)	(32,791,261)	(46,779,614)
Redemption of corporate bonds		(1,000,000)	(1,000,000)	
Dividends paid to equity shareholders of the Company		(200,510)	(712,891)	(361,051)
Dividends paid by subsidiaries to non-controlling shareholders		(59,790)	(20,168)	(26,573)
Net cash (used in)/generated from financing activities		(3,535,864)	581,807	6,198,134
Net (decrease)/increase in cash and cash equivalents		(25,451)	(8,378)	69,618
Cash and cash equivalents at the beginning of year		125,917	100,110	91,346
Effect of exchange rate fluctuations on cash held		(356)	(386)	(2)
Cash and cash equivalents at the end of year		100,110	91,346	160,962

See accompanying notes to consolidated financial statements.

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## SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

## AND SUBSIDIARIES

## Notes to the Consolidated Statements of Cash Flows

For the years ended December 31, 2010, 2011 and 2012

(Amounts in thousands)

## (a) Reconciliation of earnings/(loss) before income tax to net cash generated from/(used in) operating activities

	Years ended December 31,		
	2010 Renminbi	2011 Renminbi	2012 Renminbi
Earnings/(loss) before income tax	3,529,878	1,296,706	(2,016,473)
Interest income	(37,375)	(99,345)	(86,545)
Share of profit of associates and jointly controlled entities	(661,288)	(152,655)	(32,784)
Gain on disposal of investment by a subsidiary			(6,446)
Gain on sale of available-for-sale financial assets	(215)	(685)	
Interest expense	273,681	215,494	356,103
Depreciation of property, plant and equipment	1,641,961	1,610,450	1,669,778
Depreciation of investment property	13,256	13,250	13,250
Impairment losses on property, plant and equipment	238,200	10,552	
Amortization of lease prepayments	19,573	18,401	18,323
Unrealized exchange gain	(29,845)	(50,480)	(16,887)
Loss on disposal of property, plant and equipment and other long term assets, net	34,635	18,006	20,765
Decrease/(increase) in inventories	1,531,533	(230,124)	(3,366,017)
(Increase)/decrease in debtors, net, bills receivable and prepayments	(1,571,121)	(1,015,449)	992,248
Increase in trade creditors, other creditors and bills payable	1,161,697	297,014	131,269
(Decrease)/increase in balances due to related parties, net	(1,881,447)	573,783	754,855
<b>Cash generated from/(used in) operations</b>	<b>4,263,123</b>	<b>2,504,918</b>	<b>(1,568,561)</b>
Interest paid	(270,113)	(261,437)	(454,864)
Income tax paid	(19,291)	(23,487)	(42,960)
<b>Net cash generated from/(used in) operating activities</b>	<b>3,973,719</b>	<b>2,219,994</b>	<b>(2,066,385)</b>

See accompanying notes to consolidated financial statements.



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SINOPEC SHANGHAI PETROCHEMICAL COMPANY LIMITED

AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(All Renminbi amounts in thousands, except per share data and except otherwise stated)

**1. ORGANIZATION, PRINCIPAL ACTIVITIES AND BASIS OF PREPARATION**

Sinopec Shanghai Petrochemical Company Limited ( the Company ), formerly Shanghai Petrochemical Company Limited, was established in the People s Republic of China ( the PRC or the State ) on June 29, 1993 as a joint stock limited company to hold the assets and liabilities of the production divisions and certain other units of the Shanghai Petrochemical Complex ( SPC ). SPC was established in 1972 and owned and managed the production divisions as well as the related housing, stores, schools, hotels, transportation, hospitals and other municipal services in the community of Jinshanwei.

The Company s former controlling shareholder, China Petrochemical Corporation ( CPC ) completed its reorganization on February 25, 2000 in which its interests in the Company were transferred to its subsidiary, China Petroleum & Chemical Corporation ( Sinopec Corp ). In connection with the reorganization, CPC transferred the ownership of its 4,000,000,000 of the Company s state owned legal shares, which represented 55.56 percent of the issued share capital of the Company, to Sinopec Corp. On October 12, 2000, the Company changed its name to Sinopec Shanghai Petrochemical Company Limited.

The principal activity of the Company and its subsidiaries (the Group ) is the processing of crude oil into petrochemical products for sale. The Group is one of the largest petrochemical enterprises in the PRC, with a highly integrated petrochemical complex which processes crude oil into a broad range of synthetic fibers, resins and plastics, intermediate petrochemicals and petroleum products. Substantially all of its products are sold in the PRC domestic market.

These financial statements have been approved by the Board of Directors on March 27, 2013.

**Table of Contents****1. ORGANIZATION, PRINCIPAL ACTIVITIES AND BASIS OF PREPARATION** *(continued)*

At December 31, 2012, the following list contains the particulars of subsidiaries, all of which are limited companies established and operating in the PRC, which principally affected the results and assets of the Group.

Company	Registered Capital	Percentage of equity held by the Company %	Percentage of equity held by subsidiaries %	Principal activities
Shanghai Petrochemical Investment Development Company Limited	RMB 1,000,000	100		Investment management
China Jinshan Associated Trading Corporation	RMB 25,000	67.33		Import and export of petrochemical products and equipment
Shanghai Jinchang Engineering Plastics Company Limited	US\$ 9,154		74.25	Production of polypropylene compound products
Shanghai Golden Phillips Petrochemical Company Limited	US\$ 50,000		60	Production of polyethylene products
Zhejiang Jin Yong Acrylic Fibre Company Limited	RMB 250,000	75		Production of acrylic fiber products
Shanghai Golden Conti Petrochemical Company Limited	RMB 545,776		100	Production of petrochemical products

None of the subsidiaries have issued any debt securities.

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### **1. ORGANIZATION, PRINCIPAL ACTIVITIES AND BASIS OF PREPARATION** *(continued)*

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ( IFRS ) as issued by the International Accounting Standards Board ( IASB ).

The consolidated financial statements are prepared on the historical cost basis except for available-for-sale financial assets (see note 2(b)) which are stated at fair value.

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of IFRS that have significant effect on the financial statements and major sources of estimation uncertainty are disclosed in note 27.

### **2. PRINCIPAL ACCOUNTING POLICIES**

#### (a) Basis of consolidation

##### (i) Subsidiaries and non-controlling interests

The consolidated financial statements of the Group include the financial statements of the Company and all of its principal subsidiaries. Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(a) Basis of consolidation *(continued)*

(i) Subsidiaries and non-controlling interests *(continued)*

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-group balances and transactions and any unrealized profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealized losses resulting from intra-group transactions are eliminated in the same way as unrealized gains but only to the extent that there is no evidence of impairment.

Non-controlling interests represent the equity in a subsidiary not attributable directly or indirectly to the Company, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. For each business combination, the Group can elect to measure any non-controlling interests either at fair value or at their proportionate share of the subsidiary's net identifiable assets.

Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity shareholders of the Company. Non-controlling interests in the results of the Group are presented on the face of the consolidated statements of operations and the consolidated statements of comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the Company. Loans from holders of non-controlling interests and other contractual obligations towards these holders are presented as financial liabilities in accordance with notes 2(i) or 2(j) depending on the nature of the liability.

Changes in the Group's interests in a subsidiary that do not result in a loss of control are accounted for as equity transactions, whereby adjustments are made to the amounts of controlling and non-controlling interests within consolidated equity to reflect the change in relative interests, but no adjustments are made to goodwill and no gain or loss is recognized.

When the Group loses control of a subsidiary, it is accounted for as a disposal of the entire interest in that subsidiary, with a resulting gain or loss being recognized in profit or loss. Any interest retained in that former subsidiary at the date when control is lost is recognized at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see note 2(b)) or, when appropriate, the cost on initial recognition of an investment in an associate or jointly controlled entity (see note 2(a)(ii)).

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(a) Basis of consolidation *(continued)*

(ii) Associates and jointly controlled entities

An associate is an entity in which the Group has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

A jointly controlled entity is an entity which operates under a contractual arrangement between the Group and other parties, where the contractual arrangement establishes that the Group and one or more of the other parties share joint control over the economic activity of the entity.

An investment in an associate or a jointly controlled entity is accounted for in the consolidated financial statements under the equity method. Under the equity method, the investment is initially recorded at cost, adjusted for any excess of the Group's share of the acquisition-date fair values of the investee's identifiable net assets over the cost of the investment (if any). Thereafter, the investment is adjusted for the post-acquisition change in the Group's share of the investee's net assets and any impairment loss relating to the investment (see note 2(s)). Any acquisition-date excess over cost, the Group's share of the post-acquisition, post-tax results of the investees and any impairment losses for the year are recognized in the consolidated statements of operations, whereas the Group's share of the post-acquisition post-tax items of the investees other comprehensive income is recognized in the consolidated statements of comprehensive income. For the periods presented, no adjustments have been made (or are necessary) to conform the associate's or jointly controlled entity's accounting policies to those of the Group as there are no material differences between the accounting policies adopted by the associate and the jointly controlled entity and the Group.

When the Group's share of losses exceeds its interest in the associate or the jointly controlled entity, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee. For this purpose, the Group's interest is the carrying amount of the investment under the equity method together with the Group's long term interests that in substance form part of the Group's net investment in the associate or the jointly controlled entity.

Unrealized profits and losses resulting from transactions between the Group and its associates and jointly controlled entities are eliminated to the extent of the Group's interest in the investee, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in profit or loss.

**Table of Contents****2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*(a) Basis of consolidation *(continued)*(ii) Associates and jointly controlled entities *(continued)*

When the Group ceases to have significant influence over an associate or joint control over a jointly controlled entity, it is accounted for as a disposal of the entire interest in that investee, with a resulting gain or loss being recognized in profit or loss. Any interest retained in that former investee at the date when significant influence or joint control is lost is recognized at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see note 2(b)) or, when appropriate, the cost on initial recognition of an investment (see note 2(b)).

(b) Other investments

The Group's policies for other investments, other than investments in associates and jointly controlled entities, are as follows:

Investments in available-for-sale financial assets are carried at fair value with any change in fair value recognized in other comprehensive income and accumulated separately in equity in the fair value reserve. When these investments are derecognized or impaired, the cumulative gain or loss is reclassified from equity to profit or loss. Investments in equity securities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognized in the balance sheet at cost less impairment losses (see note 2(s)).

(c) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses (see note 2(s)).

The cost of self-constructed assets includes the cost of materials, direct labor, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads and borrowing costs.

Gains or losses arising from the retirement or disposal of items of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the items and are recognized in profit or loss on the date of retirement or disposal.

Depreciation is calculated to write off the costs of property, plant and equipment over their estimated useful lives on a straight-line basis, after taking into account their estimated residual values, as follows:

Buildings	12 to 40 years
Plant and machinery	5 to 20 years
Vehicles and other equipment	4 to 20 years

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(c) Property, plant and equipment *(continued)*

Where parts of an item of property, plant and equipment have different useful lives, the cost of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. The depreciation method, useful life and the residual value of an asset are reviewed annually.

(d) Investment property

Investment properties are properties which are owned or held under a leasehold interest either to earn rental income and / or for capital appreciation.

Investment properties are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 2(s)). Depreciation is provided over their estimated useful lives on a straight-line basis, after taking into account their estimated residual values. Estimated useful life of the investment property is 40 years.

(e) Lease prepayments and other assets

Lease prepayments and other assets mainly represent prepayments for land use rights and catalysts used in production. The assets are carried at cost less accumulated amortization and impairment losses (see note 2(s)). Lease prepayments and other assets are written off on a straight-line basis over the respective periods of the rights and the estimated useful lives of the catalysts.

(f) Construction in progress

Construction in progress represents buildings, various plant and equipment under construction and pending installation, and is stated at cost less government grants that compensate the Group for the cost of construction, and impairment losses (see note 2(s)). Cost comprises direct costs of construction as well as interest charges, and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest charges, during the period of construction.

Construction in progress is transferred to property, plant and equipment when the asset is substantially ready for its intended use.

No depreciation is provided in respect of construction in progress.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(g) Inventories

Inventories, other than spare parts and consumables, are carried at the lower of cost and net realizable value. Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Costs of conversion of inventories include cost directly related to the units of production as well as allocation of production overheads. The allocation of fixed production overhead to the costs of conversion is based on normal operating capacity of the production facilities, whereas variable production overheads are allocated to each unit of production on the basis of the actual use of the production facilities. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of the inventories is recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realizable value and all losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

Spare parts and consumables are stated at cost less any provision for obsolescence.

(h) Trade receivables, bills and other receivables

Trade receivables, bills and other receivables are initially recognized at fair value and thereafter stated at amortized cost using the effective interest method less allowance for impairment of doubtful debts (see note 2(s)), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less allowance for impairment of doubtful debts.

Trade receivables, bills and other receivables are derecognized if the Group's contractual rights to the cash flows from these financial assets expire or if the Group transfers these financial assets to another party without retaining control or substantially all risks and rewards of the assets.



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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(i) Interest-bearing borrowings

Interest-bearing borrowings are recognized initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortized cost with any difference between the amount initially recognized and redemption value being recognized in profit or loss over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

(j) Trade and other payables

Trade and other payables are initially recognized at fair value and thereafter stated at amortized cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(k) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand and time deposits with banks and other financial institutions with an initial term of less than three months at acquisition. Cash equivalents are stated at cost, which approximates fair value.

(l) Translation of foreign currencies

Foreign currency transactions during the year are translated into Renminbi at the applicable exchange rates ruling at the transaction dates.

Monetary assets and liabilities denominated in foreign currencies are translated into Renminbi at rates quoted by the People's Bank of China at the balance sheet date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated into Renminbi at the closing foreign exchange rate ruling at the date of the transaction.

Foreign currency translation differences relating to funds borrowed to finance the construction of property, plant and equipment to the extent that they are regarded as an adjustment to interest costs are capitalized during the construction period. All other exchange gains and losses are dealt with in profit or loss.

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### **2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

#### **(m) Revenue recognition**

Revenues associated with the sale of petroleum and chemical products are recognized in profit or loss when the significant risks and rewards of ownership have been transferred to the buyer. Revenue excludes value added tax and is after deduction of any trade discounts and returns. No revenue is recognized if there are significant uncertainties regarding recovery of the consideration due to the possible return of goods, or when the amount of revenue and the costs incurred or to be incurred in respect of the transaction cannot be measured reliably.

The Group provides pipeline transportation services to customers. Revenues associated with transportation services are recognized by reference to the stage of completion (that is, when the services are rendered) of the transaction at the end of the reporting period and when the outcome of the transaction can be estimated reliably. The outcome of the transaction can be estimated reliably when the amount of revenue, the costs incurred and the stage of completion can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group.

Dividend income is recognized in profit or loss on the date the shareholder's right to receive payment is established.

Gains or losses arising from the disposal of unlisted investments are determined as the difference between the net disposal proceeds and the carrying amount of the investment and are recognized in profit or loss on the date of disposal.

Rental income from investment property is recognized in profit or loss on a straight-line basis over the term of the lease.

#### **(n) Government grants**

Government grants are recognized in the balance sheet initially when there is reasonable assurance that they will be received and that the Group will comply with the conditions attaching to them. Grants that compensate the Group for expenses incurred are recognized as revenue in profit or loss on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the Group for the cost of an asset are deducted from the carrying amount of the asset and consequently are effectively recognized in profit or loss over the useful life of the asset by way of reduced depreciation expense.

#### **(o) Net financing (costs)/income**

Net financing (costs)/income comprise interest payable on borrowings calculated using the effective interest rate method, interest income on bank deposits, foreign exchange gains and losses and bank charges.

Interest income from bank deposits is recognized in profit or loss as it accrues using the effective interest method.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(o) Net financing (costs)/income (continued)

All interest and other costs incurred in connection with borrowings are expensed as incurred and included as part of net financing costs, except to the extent that they are capitalized as being directly attributable to the acquisition or construction of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

(p) Repairs and maintenance expenses

Repairs and maintenance expenses are charged to profit or loss as and when they are incurred.

(q) Research and development costs

Research and development costs comprise all costs that are directly attributable to research and development activities or that can be allocated on a reasonable basis to such activities. Because of the nature of the Group's research and development activities, no development costs satisfy the criteria for the recognition of such costs as an asset. Both research and development costs are therefore recognized as expenses in the period in which they are incurred.

(r) Employee benefits

The contributions payable under the Group's retirement plans are charged to the profit or loss on an accrual basis according to the contribution determined by the plans. Further information is set out in note 24.

Termination benefits are recorded as employee reduction expenses in the profit or loss, and are recognized when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(s) Impairment loss

- (i) Trade accounts receivable, bills and other receivables and investments in equity securities other than investments in associates and jointly controlled entities, that do not have a quoted market price in an active market are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, an impairment loss is determined and recognized.

The impairment loss is measured as the difference between the asset's carrying amount and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material, and is recognized as an expense in the profit or loss. Impairment losses for trade accounts receivable, bills and other receivables are reversed through the profit or loss if in a subsequent period the amount of the impairment loss decreases. Impairment losses for investments in equity securities carried at cost are not reversed.

For investments in associates and jointly controlled entities recognized using the equity method (note 2(a)(ii)), the impairment loss is measured by comparing the recoverable amount of the investment as a whole with its carrying amount in accordance with note 2(s)(ii). The impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount in accordance with note 2(s)(ii).

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(s) Impairment loss *(continued)*

(ii) Impairment of other long-lived assets is accounted for as follows:

The carrying amounts of other long-lived assets, including property, plant and equipment, construction in progress, lease prepayments, other assets and investments in associates and jointly controlled entities, are reviewed at each balance sheet date to identify indications that the asset may be impaired. 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 the recoverable amount.

The recoverable amount is the greater of the fair value less costs to sell and the value in use. In determining the value in use, expected future cash flows generated by the asset are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

The amount of the reduction is recognized as an expense in the profit or loss. Impairment losses recognized in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit and then, to reduce the carrying amount of the other assets in the unit on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

Management assesses at each balance sheet date whether there is any indication that an impairment loss recognized for an asset, except in the case of goodwill, in prior years may no longer exist. An impairment loss is reversed if there has been a favorable change in the estimates used to determine the recoverable amount. A subsequent increase in the recoverable amount of an asset, when the circumstances and events that led to the write-down or write-off cease to exist, is recognized in profit or loss. The reversal is reduced by the amount that would have been recognized as depreciation had the write-down or write-off not occurred. An impairment loss in respect of goodwill is not reversed.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(t) Dividends payable

Dividends are recognized as a liability in the period in which they are declared.

(u) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized in other comprehensive income or directly in equity, in which case the relevant amounts of tax are recognized in other comprehensive income or directly in equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, except differences relating to goodwill not deductible for tax purposes and the initial recognition of assets or liabilities which affect neither accounting nor taxable income. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. The effect on deferred tax of any changes in tax rates is charged or credited to the profit or loss, except for the effect of a change in tax rate on the carrying amount of deferred tax assets and liabilities which were previously charged or credited directly to equity upon initial recognition, in such case the effect of a change in tax rate is also charged or credited to equity.

A deferred tax asset is recognized only to the extent that it is probable that future taxable income will be available against the assets which can be realized or utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(v) Provisions and contingent liabilities

Provisions are recognized for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(w) Related parties

(i) A person, or a close member of that person's family, is related to the Group if that person:

(1) has control or joint control over the Group;

(2) has significant influence over the Group; or

(3) is a member of the key management personnel of the Group or the Group's parent.

(ii) An entity is related to the Group if any of the following conditions applies:

(1) The entity and the Group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(2) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

(3) Both entities are joint ventures of the same third party.

(4) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(5) The entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group.

(6) The entity is controlled or jointly controlled by a person identified in (i).

- (7) A person identified in (i)(1) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.



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**2. PRINCIPAL ACCOUNTING POLICIES** *(continued)*

(x) Segment reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the Group's chief operating decision maker for the purposes of allocating resources to, and assessing the performance of the Group's various lines of business.

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**Table of Contents****3. CHANGES IN ACCOUNTING POLICIES**

The IASB has issued a few amendments to IFRS that are first effective for the current accounting period of the Group. None of the developments are relevant to the accounting policies applied in the financial statements for the years presented.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

**4. COST OF SALES**

Cost of sales represents:

	Years ended December 31,		
	2010	2011	2012
Costs of raw materials			
-crude oil	39,694,617	53,521,866	55,537,991
-other ancillary materials	14,699,011	14,846,848	12,457,296
Depreciation of property, plant and equipment	1,640,877	1,609,656	1,669,376
Depreciation of investment property	13,256	13,250	13,250
Repairs and maintenance	1,016,530	1,093,339	984,486
Research and development	58,242	79,573	72,174
Employees' pension costs			
-municipal retirement scheme costs	209,133	221,573	249,115
-supplementary retirement scheme costs	52,974	54,002	62,189
Staff costs	1,404,129	1,662,559	1,704,330
Amortization of lease prepayments	19,573	18,401	18,323
Fuel and power	2,197,707	2,683,934	2,754,267
Costs of merchandise	6,502,085	11,480,908	11,886,346
Others	809,279	595,251	1,208,646
	68,317,413	87,881,160	88,617,789

**5. OTHER OPERATING INCOME**

Other operating income represents:

	Years ended December 31,		
	2010	2011	2012
Income from pipeline transportation services	15,074	17,108	17,502
Gain on disposal of property, plant and equipment	2,425	3,119	3,905
Rental income from investment property	39,662	41,758	46,413
Government grants	27,211	66,965	211,044
Others	25,470	35,336	54,890
	109,842	164,286	333,754

**Table of Contents****6. OTHER OPERATING EXPENSES**

Other operating expenses represent:

	Years ended December 31,		
	2010	2011	2012
Loss on disposal of property, plant and equipment	37,060	21,125	24,670
Employee reduction expenses	3,646	9,758	7,388
Impairment losses on property, plant and equipment (note 15(c))	238,200	10,552	
Others	17,050	15,749	23,721
	295,956	57,184	55,779

**7. NET FINANCING (COSTS)/ INCOME**

Net financing (costs)/income represent:

	Years ended December 31,		
	2010	2011	2012
Interest income	37,375	99,345	86,545
Net foreign exchange gain	141,087	199,691	
Financing income	178,462	299,036	86,545
Net foreign exchange loss			(13,699)
Interest on loans and borrowings	(274,511)	(246,326)	(466,409)
Less: Borrowing costs capitalized as construction in progress*	830	30,832	110,306
Financing expenses	(273,681)	(215,494)	(369,802)
Net financing (costs)/income	(95,219)	83,542	(283,257)

\* The borrowing costs during 2012 have been capitalized at a rate of 2.98%-6.21% per annum (2011: 2.75%-4.86%; 2010: 2.00%-3.25%) for construction in progress.

**Table of Contents****8. INCOME TAX**

(a) Taxation in the consolidated statements of operations represents:

	Years ended December 31,		
	2010	2011	2012
Current tax			
- Provision for PRC income tax for the year	22,523	30,280	21,841
- Under/(over)-provision in respect of prior years	3,453	(436)	132
Deferred taxation	709,521	280,340	(533,304)
<b>Total income tax</b>	<b>735,497</b>	<b>310,184</b>	<b>(511,331)</b>

A reconciliation of the expected income tax calculated at the applicable tax rate with the actual income tax is as follows:

	Years ended December 31,		
	2010	2011	2012
Earnings/(loss) before income tax	3,529,878	1,296,706	(2,016,473)
Expected PRC income tax at the statutory tax rate of 25% (2011: 25%; 2010: 25%)	882,469	324,177	(504,118)
Tax effect of non-deductible expenses	6,240	22,604	3,386
Tax effect of non-taxable income	(225)	(3,957)	(3,968)
Under/(over)-provision in prior years	3,453	(436)	132
Tax effect of share of profit recognized under the equity method	(165,322)	(38,164)	(8,196)
Tax effect of unused tax losses not recognized	12,324	10,582	7,455
Others	(3,442)	(4,622)	(6,022)
<b>Actual income tax</b>	<b>735,497</b>	<b>310,184</b>	<b>(511,331)</b>

The Group did not carry out business overseas and therefore does not incur overseas income taxes.

**Table of Contents****8. INCOME TAX (continued)**

(b) Deferred taxation:

(i) Deferred tax assets and deferred tax liabilities are attributable to items detailed in the tables below:

	Assets		Liabilities		Net balance	
	December 31,		December 31,		December 31,	
	2011	2012	2011	2012	2011	2012
<i>Current</i>						
Provisions	42,123	32,301			42,123	32,301
<i>Non-current</i>						
Provision for impairment losses	112,297	87,983			112,297	87,983
Capitalization of borrowing costs			(20,395)	(17,431)	(20,395)	(17,431)
Tax losses carried forward	374,186	939,359			374,186	939,359
Others	11,058	10,361			11,058	10,361
Deferred tax assets / (liabilities)	539,664	1,070,004	(20,395)	(17,431)	519,269	1,052,573

(ii) Movements in deferred tax assets and liabilities are as follows:

	<i>Balance</i>	<i>The Group</i>	<i>Balance</i>
	<i>at January 1,</i>	<i>Recognized</i>	<i>at December 31,</i>
	<i>2010</i>	<i>in consolidated</i>	<i>2010</i>
		<i>statements of</i>	
		<i>operations</i>	
<i>Current</i>			
Provisions	36,778	(15,239)	21,539
<i>Non-current</i>			
Provision for impairment losses	85,112	54,267	139,379
Capitalization of borrowing costs	(26,322)	2,874	(23,448)
Tax losses carried forward	1,401,978	(750,449)	651,529
Others	11,584	(974)	10,610
Net deferred tax assets	1,509,130	(709,521)	799,609

**Table of Contents****8 INCOME TAX (continued)**

(b) Deferred taxation (continued):

(ii) Movements in deferred tax assets and liabilities are as follows (continued):

	<i>Balance at January 1, 2011</i>	<i>The Group Recognized in consolidated statements of operations</i>	<i>Balance at December 31, 2011</i>
<i>Current</i>			
Provisions	21,539	20,584	42,123
<i>Non-current</i>			
Provision for impairment losses	139,379	(27,082)	112,297
Capitalization of borrowing costs	(23,448)	3,053	(20,395)
Tax losses carried forward	651,529	(277,343)	374,186
Others	10,610	448	11,058
Net deferred tax assets	799,609	(280,340)	519,269

	<i>Balance at January 1, 2012</i>	<i>The Group Recognized in consolidated statements of operations</i>	<i>Balance at December 31, 2012</i>
<i>Current</i>			
Provisions	42,123	(9,822)	32,301
<i>Non-current</i>			
Provision for impairment losses	112,297	(24,314)	87,983
Capitalization of borrowing costs	(20,395)	2,964	(17,431)
Tax losses carried forward	374,186	565,173	939,359
Others	11,058	(697)	10,361
Net deferred tax assets	519,269	533,304	1,052,573

**Table of Contents**

**8. INCOME TAX** *(continued)*

(b) Deferred taxation *(continued)*:

(ii) Movements in deferred tax assets and liabilities are as follows *(continued)*:

The Group recognizes deferred tax assets only to the extent that it is probable that future taxable income will be available against which the assets can be utilized. Based on the level of historical taxable income and projections for future taxable income over the periods which the deferred tax assets will be utilized, management believes that it is probable the Group will realize the benefits of these temporary differences.

(iii) Deferred tax assets not recognized:

As at December 31, 2012, a subsidiary of the Company did not recognize the deferred tax assets in respect of the impairment losses on property, plant and equipment amounting to RMB 432,579 (2011: RMB 432,579; 2010: RMB 432,579) and the unused tax losses carried forward for PRC income tax purpose amounting to RMB 426,685 (2011: RMB 465,414; 2010: RMB 452,443), because it was not probable that the related tax benefit will be realized. The unused tax losses carried forward of RMB 197,952, RMB 107,292, RMB 49,294, RMB 42,328 and RMB 29,819 will expire in 2013, 2014, 2015, 2016 and 2017, respectively.

**9. LOSS/EARNINGS PER SHARE**

The calculation of basic loss/earnings per share is based on the loss attributable to equity shareholders of the Company of RMB 1,528,397 (2011: profit of RMB 956,106; 2010: profit of RMB 2,769,023) and 7,200,000,000 (2011: 7,200,000,000; 2010: 7,200,000,000) shares in issue during the year.

The amount of diluted loss/earnings per share is not presented as there were no dilutive potential ordinary shares for either year.

**Table of Contents****10. DIVIDENDS**

- (a) Dividends attributable to the year

	Years ended December 31,		
	2010	2011	2012
Final dividend proposed after the balance sheet date of RMB nil per share (2011: RMB 0.05 per share; 2010: RMB 0.10 per share)	720,000	360,000	

No final dividend was proposed after the balance sheet date in respect of the year ended December 31, 2012(2011: RMB 360,000, 2010: RMB 720,000).

- (b) Dividends attributable to the previous financial year, approved during the year

	Years ended December 31,		
	2010	2011	2012
Final dividend in respect of the previous financial year, approved during the year, of RMB 0.05 per share (2011: RMB 0.10 per share; 2010: RMB 0.03 per share)	216,000	720,000	360,000



**Table of Contents****11. OTHER COMPREHENSIVE INCOME**

Reclassification adjustments relating to components of other comprehensive income

	Years ended December 31,		
	2010	2011	2012
<b><i>Available-for-sale financial assets:</i></b>			
Changes in fair value recognized during the year	215	685	
Reclassification adjustments for amounts transferred to profit or loss - gain on disposal	(215)	(685)	

Net movement in fair value reserve during the year recognized in other comprehensive income

**12. INVENTORIES**

(a) Inventories in the balance sheet comprise:

	December 31,	
	2011	2012
Raw materials	2,042,098	5,491,654
Work in progress	1,980,028	1,995,301
Finished goods	1,167,872	1,056,490
Spare parts and consumables	392,427	394,632
	5,582,425	8,938,077

(b) The analysis of the amount of inventories recognized as an expense is as follows:

The cost of inventories recognized as an expense in the consolidated statements of operations amounted to RMB 88,617,789 for the year ended December 31, 2012 (2011: RMB 87,881,160; 2010: RMB 68,317,413), which included the write-down of inventories of RMB 203,556 (2011: RMB 109,666; 2010: RMB 11,921).

**Table of Contents****13. TRADE DEBTORS, BILLS RECEIVABLE AND AMOUNTS DUE FROM RELATED PARTIES**

	December 31,	
	2011	2012
Trade debtors	126,671	94,366
Less: Impairment losses for bad and doubtful debts	(4,735)	(882)
	121,936	93,484
Bills receivable	2,988,010	2,046,657
Amounts due from related parties	639,286	1,052,842
	3,749,232	3,192,983

Amounts due from related parties mainly represent trade-related balances.

The aging analysis of trade debtors, bills receivable and amounts due from related parties (net of impairment losses for bad and doubtful debts) is as follows:

	December 31,	
	2011	2012
Invoice date:		
Within one year	3,748,135	3,192,974
Between one and two years	1,097	9
	3,749,232	3,192,983

Impairment losses for bad and doubtful debts are analyzed as follows:

At January 1, 2010	12,634
Reversal during the year	(2,916)
Write-off	(1,881)
At December 31, 2010	7,837
Reversal during the year	(1,927)
Write-off	(1,175)
At December 31, 2011	4,735
Provision for the year	237
Write-off	(4,090)
At December 31, 2012	882

**Table of Contents****13. TRADE DEBTORS, BILLS RECEIVABLE AND AMOUNTS DUE FROM RELATED PARTIES** *(continued)*

Bills receivable represent short term banker acceptance receivable that entitle the Group to receive the full face amount of the receivables from the banks at maturity, which generally ranges from one to six months from the date of issuance. Historically, the Group had experienced no credit losses on bills receivable.

Sales are generally on a cash basis. Subject to negotiation, credit is generally only available for major customers with well-established trading records.

**14. OTHER DEBTORS AND PREPAYMENTS**

Other debtors and prepayments comprise:

	December 31,	
	2011	2012
Purchase deposits	39,270	48,891
Tax recoverables	44,639	396,991
Sundry debtors	158,902	153,520
	242,811	599,402

**Table of Contents****15. PROPERTY, PLANT AND EQUIPMENT**

(a) Property, plant and equipment comprise:

	Buildings	Plant and machinery	Vehicles and other equipment	Total
<b>Cost:</b>				
At January 1, 2011	5,732,894	25,806,799	6,896,432	38,436,125
Additions		131,945	55,792	187,737
Transferred from construction in progress (note 17)	12,221	349,348	29,467	391,036
Disposal	(5,175)	(274,098)	(76,734)	(356,007)
At December 31, 2011	5,739,940	26,013,994	6,904,957	38,658,891
At January 1, 2012	5,739,940	26,013,994	6,904,957	38,658,891
Reclassification	(2,154,455)	7,123,424	(4,968,969)	
Additions		117,126	41,606	158,732
Transferred from construction in progress (note 17)	110,431	6,402,975	27,302	6,540,708
Disposal	(19,467)	(266,885)	(77,574)	(363,926)
At December 31, 2012	3,676,449	39,390,634	1,927,322	44,994,405
<b>Accumulated depreciation and impairment losses:</b>				
At January 1, 2011	3,761,918	16,193,524	4,910,124	24,865,566
Charge for the year	140,673	1,185,535	284,242	1,610,450
Impairment loss	542	8,629	1,381	10,552
Written back on disposal	(3,519)	(252,859)	(73,279)	(329,657)
At December 31, 2011	3,899,614	17,134,829	5,122,468	26,156,911
At January 1, 2012	3,899,614	17,134,829	5,122,468	26,156,911
Reclassification	(1,867,526)	5,449,167	(3,581,641)	
Charge for the year	95,919	1,504,491	69,368	1,669,778
Impairment loss				
Written back on disposal	(10,181)	(219,834)	(71,017)	(301,032)
At December 31, 2012	2,117,826	23,868,653	1,539,178	27,525,657
<b>Net book value:</b>				
At December 31, 2012	1,558,623	15,521,981	388,144	17,468,748
At December 31, 2011	1,840,326	8,879,165	1,782,489	12,501,980

**Table of Contents****15. PROPERTY, PLANT AND EQUIPMENT** *(continued)*

(b) The analysis of net book value of properties is as follows:

	December 31,	
	2011	2012
<b>In mainland China</b>		
medium term leases	1,812,123	1,531,605
<b>In Hong Kong</b>		
medium term leases	28,203	27,018
	<b>1,840,326</b>	<b>1,558,623</b>

(c) Impairment losses

2010

Impairment losses recognized on property, plant and equipment of the synthetic fibres segment were RMB 92 million for the year ended December 31, 2010, which represented impairment losses in respect of certain filament production facilities. The primary factor resulting in the impairment losses on the filament production facilities is the high operating and production costs caused by the increase in the raw material price that are not expected to be covered through an increase in selling price of those products in the foreseeable future. These assets were tested for impairment in accordance with the Company's accounting policy described in note 2(s)(ii) to the consolidated financial statements. The recoverable amounts of these production facilities were estimated based on their value in use. The estimate of value in use was determined using a pre-tax discount rate of 10%.

Impairment losses recognized on certain idle facilities of the resins and plastics segment were RMB 26.3 million for the year ended December 31, 2010. These facilities were abandoned and tested for impairment in accordance with the Company's accounting policy described in note 2(s)(ii) to the consolidated financial statements. The estimated recoverable amounts were based on the assets' fair value less costs to sell, which were determined by reference to the recent observable market prices for similar assets within the same industry.

Impairment losses recognized on property, plant and equipment of the intermediate petrochemicals segment were RMB 119.9 million for the year ended December 31, 2010, which mainly represented impairment losses of RMB 89.9 million in respect of a newly constructed facility that has not started production as it cannot meet the local environmental requirement. The asset was tested for impairment in accordance with the Company's accounting policy described in note 2(s)(ii) to the consolidated financial statements. The estimated recoverable amounts was based on the asset's fair value less costs to sell, which was determined by reference to the recent observable market prices for similar assets within the same industry.

2011

Impairment losses recognized on certain idle facilities of the intermediate petrochemicals segment were RMB 10.6 million for the year ended December 31, 2011. These facilities were tested for impairment in accordance with the Company's accounting policy described in note 2(s)(ii) to the consolidated financial statements. The estimated recoverable amounts were based on the assets' fair value less costs to sell, which were determined by reference to the recent observable market prices for similar assets within the same industry.

(d) The carrying value of the above assets prior to the impairment losses and the carrying value of the assets subsequent to the impairment losses by asset category for the year ended December 31, 2011 are presented as follows:

2011

Asset Category

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	<i>Original cost</i>	<i>Net book value before impairment</i>	<i>Impairment loss recognized</i>	<i>Net book value after impairment</i>
Buildings	3,363	647	(542)	105
Plant and machinery	114,303	12,145	(8,629)	3,516
Vehicles and other equipment	13,831	1,650	(1,381)	269
Total	131,497	14,442	(10,552)	3,890

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**Table of Contents****16. INVESTMENT PROPERTY**

	2011	2012
<b>Cost:</b>		
At January 1	546,412	546,412
Disposal		(208)
At December 31	546,412	546,204
<b>Accumulated depreciation:</b>		
At January 1	80,607	93,857
Charge for the year	13,250	13,250
Written back on disposal		(40)
At December 31	93,857	107,067
<b>Net book value:</b>		
At December 31	452,555	439,137

Investment property represents certain floors of an office building leased to other entities including related parties.

The fair value of the investment property of the Group as at December 31, 2012 was estimated by the directors to be approximately RMB 970,565 by reference to market values of similar properties in the relevant region (2011: RMB 964,816). The investment property has not been valued by an external independent valuer.

Rental income of RMB 46,413 was received by the Group during the year ended December 31, 2012 (2011: RMB 41,758; 2010: RMB 39,662).

**Table of Contents****17. CONSTRUCTION IN PROGRESS**

	2011	2012
At January 1	1,139,239	3,852,692
Additions	3,104,489	3,656,121
Transferred to property, plant and equipment (note 15)	(391,036)	(6,540,708)
Transferred to other assets - catalysts		(355,717)
At December 31	3,852,692	612,388

**18. INTEREST IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES**

	December 31,	
	2011	2012
Interest in associates	2,777,292	2,744,248
Interest in jointly controlled entities	124,013	122,905
	2,901,305	2,867,153

The above amount represents the share of net assets of the Group's interest in its associates and jointly controlled entities.



**Table of Contents****18. INTEREST IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES** *(continued)*

The particulars of the significant associates and jointly controlled entities, which are limited companies established and operating in the PRC, and which principally affected the results or assets of the Group at December 31, 2012 are as follows:

Company	Registered Capital	Percentage of equity held by the Company %	Percentage of equity held by subsidiaries %	Principal activities
Shanghai Chemical Industry Park Development Company Limited	RMB 2,372,439	38.26		Planning, development and operation of the Chemical Industry Park in Shanghai, PRC
Shanghai Secco Petrochemical Company Limited	US\$ 901,441	20		Manufacturing and distribution of chemical products
Shanghai Jinsen Hydrocarbon Resins Company Limited	US\$ 23,395		40	Production of resins products
Shanghai Azbil Automation Company Limited	US\$ 3,000		40	Service and maintenance of building automation systems and products
BOC-SPC Gases Company Limited	US\$ 32,000	50		Production and sales of industrial gases

Summary financial information of the associates and jointly controlled entities is as follows:

	Assets	Liabilities	Equity	Revenues	Net income/(loss)
2011					
100 percent	24,339,685	11,867,334	12,472,351	30,222,018	353,774
Group's effective interest	6,574,718	3,673,413	2,901,305	6,558,197	152,655
2012					
100 percent	22,225,085	9,995,489	12,229,596	29,487,156	(108,583)
Group's effective interest	5,808,515	2,941,362	2,867,153	6,362,905	32,784

For the periods presented, no adjustments have been made (or are necessary) to conform the associates' and jointly controlled entities' accounting policies to those of the Group as there are no material differences between the accounting policies adopted by the associates and jointly controlled entities and the Group.

**Table of Contents****19. LOANS AND BORROWINGS**

Short term loans consist of:

	December 31,	
	2011	2012
Bank loans	4,852,074	10,803,877
Loans from a related party	660,000	220,000
	5,512,074	11,023,877

At December 31, 2012, no loans and borrowings were secured by the way of pledge of property, plant and equipment (2011: nil). The Group's weighted average short term interest rates were 2.75% and 3.62% at December 31, 2011 and 2012, respectively.

The Group's long term loans consist of:

Final maturity date	Interest rate at December 31, 2012	Interest type	December 31,	
			2011	2012
<b>Arranged by the Company:</b>				
Renminbi denominated:				
2013	5.36%	Floating	125,000	
2014	5.76%-6.21%	Floating		360,000
2015-2017	5.76%-6.21%	Floating	10,000	840,000
<b>Arranged by subsidiaries:</b>				
Renminbi denominated:				
2014	6.40%-6.90%	Floating		10,560
2015-2016	6.40%-6.90%	Floating	25,050	20,780
Total long term loans outstanding			160,050	1,231,340
Less: Amounts due within one year				
Amounts due after one year			160,050	1,231,340

Included in loans and borrowings are the following amounts denominated in currencies other than the functional currency of the entity to which they relate:

	December 31,	
	2011	2012
United States Dollars	USD 733,637	USD 1,247,296

**Table of Contents****20. DEFERRED INCOME**

Government grants of RMB 91,319 received in 2011 was recognized in profit or loss during 2012 in accordance with the accounting policy adopted for government grants set out in note 2(n).

**21. SHARE CAPITAL**

Share capital represents:

	December 31,	
	2011	2012
Registered, issued and paid up capital:		
4,870,000,000 A shares of RMB 1.00 each	4,870,000	4,870,000
2,330,000,000 H shares of RMB 1.00 each	2,330,000	2,330,000
	7,200,000	7,200,000

All the A and H shares rank pari passu in all respects.

**Capital management**

Management optimizes the structure of its capital, comprising equity and loans. In order to maintain or adjust the capital structure, management may cause the Group to issue new shares, adjust the capital expenditure plan, sell assets to reduce debt, or adjust the proportion of short term and long term loans. Management monitors capital on the basis of debt-to-equity ratio, which is calculated by dividing loans and borrowings by the total equity attributable to equity shareholders of the Company, and liability-to-asset ratio, which is calculated by dividing total liabilities by total assets. Management's strategy is to make appropriate adjustments according to the operating and investment needs and changes in market conditions, and to maintain the debt-to-equity ratio and the liability-to-asset ratio at a range considered reasonable by management. As at December 31, 2012, the debt-to-equity ratio and the liability-to-asset ratio of the Group were 76.42% (2011: 31.64%) and 55.29% (2011: 40.77%), respectively. The Group's exposure to liquidity risk and the management policies and practices used by the Group are disclosed in note 28.

The schedules of the contractual maturities of loans and commitments are disclosed in notes 19 and 23, respectively.

There were no changes in the management approach to capital management of the Group during the year. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

**Table of Contents****22. RESERVES**

Movements on reserves comprise:

	2011	2012
<b>Share premium</b>		
Balance at January 1 and December 31(note (a))	2,420,841	2,420,841
<b>Statutory surplus reserve</b>		
Balance at January 1	3,800,800	3,871,256
Appropriation(note (b))	70,456	
Balance at December 31 (note (b))	3,871,256	3,871,256
<b>Capital reserve</b>		
Balance at January 1 and December 31(note (c))	4,180	4,180
<b>Discretionary surplus reserve</b>		
Balance at January 1 and December 31(note (d))	1,280,514	1,280,514
<b>Specific reserve for safety production fund</b>		
Balance at January 1		21,777
Appropriation/(utilization)	21,777	(13,598)
Balance at December 31(note (e))	21,777	8,179
<b>Retained earnings</b>		
Balance at January 1	2,983,122	3,126,995
Net income/(loss) for the year attributable to the equity shareholders of the Company	956,106	(1,528,397)
Dividend approved in respect of previous year	(720,000)	(360,000)
Appropriation of profits	(70,456)	
(Appropriation)/utilization of safety production fund	(21,777)	13,598
Balance at December 31(note (f))	3,126,995	1,252,196
	10,725,563	8,837,166

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**22. RESERVES** *(continued)*

Note (a):

The application of the share premium account is governed by Sections 178 and 179 of the PRC Company Law.

Note (b):

According to the Company's Articles of Association, the Company is required to transfer 10% of the Company's profit after taxation, as determined under China Accounting Standards for Business Enterprises, to a statutory surplus reserve. The transfer to this reserve is made before distribution of a dividend to shareholders.

The statutory surplus reserve can be used to make good of previous years' losses, if any, and may be converted into share capital by the issue of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of the registered capital.

Note (c):

This reserve represents gifts or grants received from China Petrochemical Corporation, the ultimate parent company and which are required to be included in this reserve fund by PRC regulations.

Note (d):

The transfer to this reserve from the retained profits is subject to the approval by shareholders at general meetings. Its usage is similar to that of statutory surplus reserve.

Note (e):

According to the relevant PRC regulations, the Group is required to transfer an amount to specific reserve for the safety production fund based on the turnover of certain refining and chemicals products. This reserve represents unutilized safety production fund.

Note (f):

According to the Company's Articles of Association, the reserve available for distribution is the lower of the amount determined under China Accounting Standards for Business Enterprises and the amount determined under IFRS. No final dividend (2011: RMB 360,000) in respect of the financial year 2012 was declared after the balance sheet date.

**Table of Contents****23. COMMITMENTS AND CONTINGENCIES**

## (a) Capital commitments

The Group had capital commitments outstanding at December 31 not provided for in the financial statements as follows:

	December 31,	
	2011	2012
<u>Property, plant and equipment</u>		
Contracted but not provided for	2,817,581	123,310
Authorized but not contracted for	2,708,271	1,362,263
	5,525,852	1,485,573

## (b) Contingent liabilities

## (i) Income tax differences

In June 2007, the State Administrative of Taxation issued a tax circular (Circular No.664) to the local tax authorities requesting the relevant local tax authorities to rectify the applicable enterprise income tax ( EIT ) for nine listed companies, which included the Company. After the notice was issued, the Company was required by the relevant tax authority to settle the EIT for 2007 at a rate of 33 percent. To date, the Company has not been requested by the tax authorities to pay additional EIT in respect of any years prior to 2007. There is no further development of this matter during the year ended December 31, 2012. No provision has been made in the financial statements at December 31, 2012 for this uncertainty because management believes it is not probable that the Group will be required to pay additional EIT for tax years prior to 2007.

- (ii) Except for the above, there are no contingent liabilities for which the possibility of any outflow of resources is other than remote and the Group is not a party to any business operation contingencies.

**Table of Contents****24. RETIREMENT SCHEMES**

As stipulated by the regulations of the PRC, the Group participates in a defined contribution retirement plan organized by the Shanghai Municipal Government for its staff. The Group is required to make contributions to the retirement plan at a rate of 22% of the salaries, bonuses and certain allowances of its staff in 2012 (2011: 22%).

In addition, pursuant to a document Order of the Ministry of Labour and Social Security No.20 dated January 6, 2004 issued by the Ministry of Labour of the PRC, the Group has set up a supplementary defined contribution retirement plan for the benefit of employees. Employees who have served the Group for more than one year may participate in this plan. The Group and participating employees make defined contributions to their pension saving accounts according to the plan. The assets of this plan are held separately from those of the Group in an independent fund administered by a committee consisting of representatives from the employees and the Group.

A member of the above plans is entitled to a pension amount equal to a fixed proportion of the salary prevailing at his or her retirement date. Both the Group and participating employees make defined contributions to the above two retirement plans. The Group has no other material obligation for the payment of pension benefits associated with these plans beyond the annual contributions described above. For the year ended December 31, 2012, the Group's contribution to the above two plans amounted to RMB 264,160 and RMB 68,763 respectively (2011: RMB 235,013 and RMB 59,922 respectively; 2010: RMB 209,752 and RMB 57,867 respectively).

**25. RELATED PARTY TRANSACTIONS**

The following is a list of the Group's major related parties:

Names of related parties	Relationship with the Company
China Petrochemical Corporation ( Sinopec Group Company )	Ultimate parent company
China Petroleum & Chemical Corporation ( Sinopec Corp )	Immediate parent company
Sinopec Huadong Sales Company Limited	Subsidiary of the immediate parent company
China International United Petroleum and Chemical Company Limited	Subsidiary of the immediate parent company
China Petrochemical International Company Limited	Subsidiary of the immediate parent company
Sinopec Chemical Commercial Holding Company Limited	Subsidiary of the immediate parent company
Sinopec Yizheng Chemical Fibre Company Limited	Subsidiary of the immediate parent company
Sinopec Finance Company Limited ( Sinopec Finance )	Subsidiary of the ultimate parent company
Shanghai Secco Petrochemical Co., Ltd.	Associate
BOC-SPC Gases Co., Ltd.	Jointly controlled entity

**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*

- (a) Most of the transactions undertaken by the Group during the year ended December 31, 2012 have been affected on such terms as determined by Sinopec Corp and relevant PRC authorities.

Sinopec Corp negotiates and agrees the terms of crude oil supply with suppliers on a group basis, which is then allocated among its subsidiaries, including the Group, on a discretionary basis. Sinopec Corp also owns a widespread petroleum products sales network and possesses a fairly high market share in domestic petroleum products market, which is subject to extensive regulation by the PRC government.

The Group has entered into a mutual product supply and sales services framework agreement with Sinopec Corp. Pursuant to the agreement, Sinopec Corp provides the Group with crude oil, other petrochemical raw materials and agent services. On the other hand, the Group provides Sinopec Corp with petroleum products, petrochemical products and property leasing services.

The pricing policy for these services and products provided under the agreement is as follows:

if there are applicable State (central and local government) tariffs, the pricing shall follow the State tariffs;

if there are no State tariffs, but there are applicable State's guidance prices, the pricing shall follow the State's guidance prices;  
or

if there are no State tariffs or State's guidance prices, the pricing shall be determined in accordance with the prevailing market prices (including any bidding prices).

Transactions between the Group and Sinopec Corp, its subsidiaries and jointly controlled entities were as follows:

	Years ended December 31,		
	2010	2011	2012
Sales of petroleum products	30,352,483	36,585,798	37,618,198
Sales other than petroleum products	8,982,711	14,117,834	11,975,071
Purchases of crude oil	24,555,912	35,795,694	41,173,864
Purchases other than crude oil	7,296,474	7,816,204	8,261,218
Sales commissions	168,896	195,606	160,903
Rental income	26,942	23,246	23,976



**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*

- (b) Other transactions between the Group and Sinopec Group Company and its subsidiaries, associates and jointly controlled entities of the Group were as follows:

	Years ended December 31,		
	2010	2011	2012
<b>Sales of goods and service income</b>			
Sinopec Group Company and its subsidiaries	307,658	279,289	430,089
Associates and jointly controlled entities of the Group	1,279,154	2,299,800	2,548,068
	1,586,812	2,579,089	2,978,157
<b>Purchases</b>			
Sinopec Group Company and its subsidiaries	45,773	42,858	24,445
Associates and jointly controlled entities of the Group	5,702,541	4,154,093	3,519,612
	5,748,314	4,196,951	3,544,057
<b>Insurance premiums</b>			
Sinopec Group Company and its subsidiaries	96,712	115,910	115,918
<b>Interest income</b>			
Sinopec Finance	570	859	555
<b>Loans borrowed</b>			
Sinopec Finance	5,160,000	4,790,000	3,361,740
<b>Loans repayment</b>			
Sinopec Finance	4,990,000	4,540,000	3,801,740
<b>Interest expense</b>			
Sinopec Finance	29,029	22,148	29,716
<b>Construction and installation cost</b>			
Sinopec Group Company and its subsidiaries	88,586	286,023	436,082

The directors of the Company are of the opinion that the transactions with Sinopec Corp, its subsidiaries and jointly controlled entities, Sinopec Group Company and its subsidiaries, associates and jointly controlled entities of the Group as disclosed in notes 25(a) and 25(b) were conducted in the ordinary course of business, on normal commercial terms and in accordance with the agreements governing such transactions.

**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*

- (c) The relevant amounts due from/to Sinopec Corp, its subsidiaries and jointly controlled entities, Sinopec Group Company and its subsidiaries, associates and jointly controlled entities of the Group, arising from purchases, sales and other transactions as disclosed in notes 25(a) and 25(b), are summarized as follows:

	December 31,	
	2011	2012
<b>Amounts due from related parties</b>		
Sinopec Corp, its subsidiaries and jointly controlled entities	553,562	867,960
Sinopec Group Company and its subsidiaries	1,910	3,884
Associates and jointly controlled entities of the Group	83,814	180,998
<b>Total</b>	<b>639,286</b>	<b>1,052,842</b>
<b>Amounts due to related parties</b>		
Sinopec Corp, its subsidiaries and jointly controlled entities	2,027,816	3,211,906
Sinopec Group Company and its subsidiaries	10,081	5,894
Associates and jointly controlled entities of the Group	204,971	193,479
<b>Total</b>	<b>2,242,868</b>	<b>3,411,279</b>
<b>Cash deposits, maturing within 3 months</b>		
Sinopec Finance	1,093	1,933
<b>Short term loans</b>		
Sinopec Finance	660,000	220,000

Amounts due from / to related parties are unsecured and interest free.

**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*

## (d) Key management personnel compensation and post-employment benefit plans

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and supervisors of the Group. The key personnel compensations are as follows:

	Years ended December 31,		
	2010	2011	2012
Short term employee benefits	6,318	6,973	7,428
Post-employment benefits	190	147	170
	6,508	7,120	7,598

Post-employment benefits are included in contributions to defined contribution retirement plans as disclosed in note 25(e).

## (e) Contributions to defined contribution retirement plans

The Group participates in defined contribution retirement plans organized by municipal governments for its staff. The contributions to defined contribution retirement plans are as follows:

	Years ended December 31,		
	2010	2011	2012
Municipal retirement scheme costs (note 24)	209,752	235,013	264,160
Supplementary retirement scheme costs (note 24)	57,867	59,922	68,763

At December 31, 2010, 2011 and 2012, there was no material outstanding contribution to the above defined contribution retirement plans.

**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*

## (f) Transactions with other state-owned entities in the PRC

The Group is a state-controlled enterprise and operates in an economic regime currently dominated by entities directly or indirectly controlled by the PRC government (collectively referred to as state-controlled entities ) through its government authorities, agencies, affiliations and other organizations.

Apart from transactions with related parties, the Group has transactions with other state-controlled entities which include, but are not limited to, the following:

sales and purchases of goods and ancillary materials;

rendering and receiving services;

lease of assets, purchase of property, plant and equipment;

placing deposits and obtaining finance; and

use of public utilities.

These transactions are conducted in the ordinary course of the Group's business on terms comparable to those with other entities that are not state controlled. The Group has established its procurement policies, pricing strategy and approval process for purchases and sales of products and services which do not depend on whether the counterparties are state-controlled entities or not.

Having considered the transactions potentially affected by related party relationships, the entity's pricing strategy, procurement policies and approval processes, and the information that would be necessary for an understanding of the potential effect of the related party relationship on the financial statements, the directors are of the opinion that the following transactions require disclosure of the related amounts.

## (i) Transactions with other state-controlled energy and chemical companies

The Group's major domestic suppliers of crude oil are China National Offshore Oil Corporation and its subsidiaries and Sinochem Group and its subsidiaries, which are state-controlled entities.

The aggregate amount of crude oil purchased by the Group from the above state-controlled energy and chemical companies are as follows:

	Years ended December 31,		
	2010	2011	2012
Purchases of crude oil	13,474,022	16,987,956	13,243,442

As at December 31, 2012, there was no outstanding balance with the above state-controlled energy and chemical companies arising from purchases of crude oil (2011: prepayments of RMB 8,747).

**Table of Contents****25. RELATED PARTY TRANSACTIONS** *(continued)*(f) Transactions with other state-owned entities in the PRC *(continued)*

(ii) Transactions with state-controlled banks

The Group deposits its cash with several state-controlled banks in the PRC. The Group also obtains short term and long term loans from these banks in the ordinary course of business. The interest rates of the bank deposits and loans are regulated by the People's Bank of China. The Group's interest income from and interest expense to these state-controlled banks in the PRC are as follows:

	Years ended December 31,		
	2010	2011	2012
Interest income	20,379	18,885	17,192
Interest expense	245,482	224,178	436,693

The amounts of cash deposited at and loans from state-controlled banks in the PRC are summarized as follows:

	December 31,	
	2011	2012
Cash and cash equivalents at state-controlled banks in the PRC	90,253	159,029
Short term loans and current portion of long term loans	4,852,074	10,803,877
Long term loans excluding current portion of long term loans	160,050	1,231,340
Total loans from state-controlled banks in the PRC	5,012,124	12,035,217

(g) Commitments with related parties

	December 31,	
	2011	2012
Construction and installation cost:		
Sinopec Group Company and its subsidiaries	408,664	53,690

Except for the above, the Group had no other material commitments with related parties at December 31, which are contracted, but not included in the financial statements.

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### **26. SEGMENT REPORTING**

The Group manages its business by divisions, which are organized by business lines. In view of the fact that the Company and its subsidiaries operate mainly in the PRC, no geographical segment information is presented.

In a manner consistent with the way in which information is reported internally to the Group's chief operating decision maker for the purposes of resource allocation and performance assessment, the Group has identified the following five reportable segments. No operating segments have been aggregated to form the following reportable segments.

The Group principally operates in five operating segments: synthetic fibres, resins and plastics, intermediate petrochemicals, petroleum products and trading of petrochemical products. Synthetic fibres, resins and plastics, intermediate petrochemicals, petroleum products are produced through intermediate steps from the principal raw material of crude oil. The specific products of each segment are as follows:

- (a) The synthetic fibers segment produces primarily polyester and acrylic fibers, which are mainly used in the textile and apparel industries.
- (b) The resins and plastics segment produces primarily polyester chips, polyethylene resins and plastics, polypropylene resins and PVA granules. The polyester chips are used to produce polyester fibres, coating and containers. Polyethylene resins and plastics are used to produce insulated cable, mulching films and moulded products such as housewares and toys. Polypropylene resins are used for films, sheets and moulded products such as housewares, toys, consumer electronics and automobile parts.
- (c) The intermediate petrochemicals segment primarily produces p-xylene, benzene and butadiene. The intermediate petrochemicals produced by the Group are both served as raw materials in the production of other petrochemicals, resins, plastics and synthetic fibres, and sold to outside customers.
- (d) The Group's petroleum products segment is equipped with crude oil distillation facilities used to produce vacuum and atmospheric gas oils used as feedstocks of the Group's downstream processing facilities. Residual oil and low octane gasoline fuels are co-products of the crude oil distillation process. Part of the residual oil is further processed into qualified refined gasoline and diesel oil. In addition, the Group produces a variety of fuels for transportation, industry and household heating usage, such as diesel oil, jet fuel, heavy oil and liquefied petroleum gas.

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**26. SEGMENT REPORTING** *(continued)*

- (e) The Group's trading of petrochemical products segment is primarily engaged in importing and exporting of petrochemical products. The products are sourced from international and domestic suppliers.
  
- (f) Other operating segments represent the operating segments which do not meet the quantitative threshold for determining reportable segments. These include sales of consumer products and services and a variety of other commercial activities, which are not allocated to the above five operating segments.

*(a)* Segment results, assets and liabilities

In accordance with IFRS 8, segment information disclosed in the annual financial statements has been prepared in a manner consistent with the information used by the Group's chief operating decision maker for the purposes of assessing segment performance and allocating resources of the segments. In this regard, the Group's chief operating decision maker monitors the results, assets and liabilities attributable to each reportable segment on the following bases:

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest in associates or jointly controlled entities, deferred tax assets, cash and cash equivalents, investment property and related revenues (such as share of profit of associates and jointly controlled entities, interest income and investment income), interest-bearing loans, borrowings and interest expense, and corporate assets and expenses.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

**Table of Contents****26. SEGMENT REPORTING** (continued)

(b) Reportable information on the Group's operating segments is as follows:

	Years ended December 31,		
	2010	2011	2012
<b>Sales</b>			
<b>Manufactured products</b>			
Synthetic fibers			
External sales	3,955,396	4,198,251	3,344,190
Intersegment sales	82	118	93
Total	3,955,478	4,198,369	3,344,283
Resins and plastics			
External sales	15,065,276	16,589,438	14,828,298
Intersegment sales	118,699	136,352	108,618
Total	15,183,975	16,725,790	14,936,916
Intermediate petrochemicals			
External sales (note a)	17,399,592	19,242,850	18,161,380
Intersegment sales (note b)	18,583,283	19,498,129	19,085,952
Total	35,982,875	38,740,979	37,247,332
Petroleum products			
External sales (note a)	33,734,607	42,896,821	43,754,793
Intersegment sales	2,678,172	5,156,614	5,618,459
Total	36,412,779	48,053,435	49,373,252
Trading of petrochemical products			
External sales (note a)	6,567,757	11,620,440	12,025,361
Intersegment sales	1,878,590	3,385,692	3,423,818
Total	8,446,347	15,006,132	15,449,179
Others			
External sales (note a)	798,071	971,056	894,316
Intersegment sales	688,715	814,281	718,864
Total	1,486,786	1,785,337	1,613,180
Elimination of intersegment sales	(23,947,541)	(28,991,186)	(28,955,804)
<b>Consolidated sales</b>	<b>77,520,699</b>	<b>95,518,856</b>	<b>93,008,338</b>



**Table of Contents****26. SEGMENT REPORTING** (continued)

	Years ended December 31,		
	2010	2011	2012
<b>Segment profit/(loss)</b>			
Synthetic fibers	435,594	301,334	(405,349)
Resins and plastics	991,091	11,994	(1,291,393)
Intermediate petrochemicals	365,124	1,148,572	832,675
Petroleum products	1,140,268	(453,368)	(993,026)
Trading of petrochemical products	14,085	14,969	46,448
Others	17,432	36,323	38,199
<b>Consolidated profit/(loss) from operations</b>	2,963,594	1,059,824	(1,772,446)
<b>Net financing (costs)/income</b>	(95,219)	83,542	(283,257)
<b>Investment income</b>	215	685	6,446
<b>Share of profit of associates and jointly controlled entities</b>	661,288	152,655	32,784
<b>Earnings/(loss) before income tax</b>	3,529,878	1,296,706	(2,016,473)

Note (a): External sales include sales to Sinopec Corp, its subsidiaries and jointly controlled entities as follows:

	Years ended December 31,		
	2010	2011	2012
<b>Sales to Sinopec Corp, its subsidiaries and jointly controlled entities</b>			
Intermediate petrochemicals	3,838,121	4,851,962	4,355,455
Petroleum products	30,352,483	36,585,798	37,618,198
Trading of petrochemical products	4,668,546	8,721,026	6,999,471
Others	476,044	544,846	620,145
<b>Total</b>	39,335,194	50,703,632	49,593,269

Note (b): Intermediate petrochemicals intersegment sales for each of the other reportable segments are as follows:

	Years ended December 31,		
	2010	2011	2012
Synthetic fibers	3,366,715	3,160,141	3,483,378
Resins and plastics	14,938,149	16,037,690	15,302,334
Petroleum products	278,419	300,298	300,240
<b>Total</b>	18,583,283	19,498,129	19,085,952

**Table of Contents****26. SEGMENT REPORTING** (continued)

	December 31,	
	2011	2012
<b>Assets</b>		
<b>Segment assets</b>		
Synthetic fibers	1,615,153	1,689,429
Resins and plastics	1,162,060	1,100,082
Intermediate petrochemicals	6,628,962	6,811,409
Petroleum products	14,401,380	18,661,951
Trading of petrochemical products	547,692	451,111
Others	2,238,739	2,715,605
<b>Total segment assets</b>	<b>26,593,986</b>	<b>31,429,587</b>
<b>Unallocated:</b>		
Interest in associates and jointly controlled entities	2,901,305	2,867,153
Deferred tax assets	519,269	1,052,573
Investment property	452,555	439,137
Others	251,750	674,096
<b>Consolidated assets</b>	<b>30,718,865</b>	<b>36,462,546</b>

	December 31,	
	2011	2012
<b>Liabilities</b>		
<b>Segment liabilities</b>		
Synthetic fibers	257,964	232,135
Resins and plastics	1,019,349	1,029,297
Intermediate petrochemicals	1,182,389	1,260,661
Petroleum products	3,795,554	4,927,935
Trading of petrochemical products	411,433	388,810
Others	70,729	62,079
<b>Total segment liabilities</b>	<b>6,737,418</b>	<b>7,900,917</b>
<b>Unallocated:</b>		
Loans and borrowings-current	5,512,074	11,023,877
Loans and borrowings-non-current	160,050	1,231,340
Others	113,659	2,463
<b>Consolidated liabilities</b>	<b>12,523,201</b>	<b>20,158,597</b>

**Table of Contents****26. SEGMENT REPORTING** *(continued)*

	Years ended December 31,		
	2010	2011	2012
<b>Depreciation and amortization</b>			
Synthetic fibers	126,929	120,257	143,742
Resins and plastics	171,111	165,499	161,764
Intermediate petrochemicals	570,670	572,200	583,280
Petroleum products	624,190	601,196	614,812
Trading of petrochemical products	830	601	330
Others	167,804	169,098	184,173
<b>Segment depreciation and amortization</b>	<b>1,661,534</b>	<b>1,628,851</b>	<b>1,688,101</b>
<b>Unallocated</b>	<b>13,256</b>	<b>13,250</b>	<b>13,250</b>
<b>Consolidated depreciation and amortization</b>	<b>1,674,790</b>	<b>1,642,101</b>	<b>1,701,351</b>

	Years ended December 31,		
	2010	2011	2012
<b>Impairment losses on long-lived assets</b>			
Synthetic fibers	92,000		
Resins and plastics	26,300		
Intermediate petrochemicals	119,900	10,552	
<b>Consolidated impairment losses on long-lived assets</b>	<b>238,200</b>	<b>10,552</b>	

	Years ended December 31,		
	2010	2011	2012
<b>Capital expenditure for segment long-lived assets</b>			
Synthetic fibers	154,149	549,058	101,260
Resins and plastics	15,179	72,571	46,509
Intermediate petrochemicals	197,774	298,880	918,826
Petroleum products	825,494	2,212,855	2,571,457
Trading of petrochemical products			650
Others	164,249	347,871	621,157
<b>Consolidated capital expenditure for segment long-lived assets</b>	<b>1,356,845</b>	<b>3,481,235</b>	<b>4,259,859</b>

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### **27. ACCOUNTING JUDGMENTS AND ESTIMATES**

The Group's financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of the financial statements. Management bases the assumptions and estimates on historical experience and on various other assumptions that management believes to be reasonable and which form the basis for making judgments about matters that are not readily apparent from other sources. On an on-going basis, management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing the financial statements. The principal accounting policies are set forth in note 2. Management believes the following critical accounting policies involve the most significant judgments and estimates used in the preparation of the financial statements.

#### **Impairments for long-lived assets**

If circumstances indicate that the net book value of a long-lived asset may not be recoverable, the asset may be considered impaired, and an impairment loss may be recognized in accordance with IAS 36 Impairment of Assets. Long-lived assets are reviewed for impairment at the end of each reporting period or whenever events or changes in circumstances have indicated that their carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to 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 Group's assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgment relating to level of sale volume, selling price and amount of operating costs. Management uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of sale volume, selling price and amount of operating costs.

#### **Depreciation**

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

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**27. ACCOUNTING JUDGMENTS AND ESTIMATES** *(continued)*

**Impairment for bad and doubtful debts**

Management estimates impairment losses for bad and doubtful debts resulting from the inability of the customers to make the required payments. Management bases the estimates on the ageing of the accounts receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of the customers were to deteriorate, actual impairment losses would be higher than estimated.

**Allowance for diminution in value of inventories**

If the costs of inventories become higher than their net realizable values, an allowance for diminution in value of inventories is recognized. Net realizable value represents the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. Management bases the estimates on all available information, including the current market prices of the finished goods and raw materials, and historical operating costs. If the actual selling prices were to be lower or the costs of completion were to be higher than estimated, the actual allowance for diminution in value of inventories could be higher than estimated.

**Recognition of deferred tax assets**

Deferred tax assets are recognized in respect of temporary deductible differences and the carryforward of unused tax losses. Management recognizes deferred tax assets only to the extent that it is probable that future taxable profit will be available against the assets which can be realized or utilized. At the end of each reporting period, management assesses whether previously unrecognized deferred tax assets should be recognized. The Group recognizes a previously unrecognized deferred tax asset to the extent that it is probable that future taxable profit will allow the deferred tax asset to be utilized. In addition, management assesses the carrying amount of deferred tax assets that are recognized at the end of each reporting period. The Group reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available for the deferred tax asset to be utilized.

In making the assessment of whether it is probable the Group will realize or utilize the deferred tax assets, management primarily relies on the generation of future taxable income to support the recognition of deferred tax assets. In order to fully utilize the deferred tax assets recognized at December 31, 2012 the Group would need to generate future taxable income of at least RMB 4,210 million, of which RMB 1,497 million is required to be generated by 2013 prior to the expiration of the unused tax losses incurred in 2008 and RMB 2,260 million is required to be generated by 2017 prior to the expiration of the unused tax losses incurred in the current year. Based on estimated forecast and historical experience, management believes that it is probable that the Group will generate sufficient taxable income before the unused tax losses expire.

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### **28. FINANCIAL INSTRUMENTS**

#### ***Overview***

Financial assets of the Group include cash and cash equivalents, other investments, trade debtors, bills receivable, other debtors and amounts due from related parties. Financial liabilities of the Group include loans and borrowings, trade creditors, bills payable, other creditors and amounts due to related parties.

The Group has exposure to the following risks from its use of financial instruments:

credit risk;

liquidity risk; and

market risk

The Board of Directors has overall responsibility for the establishment, oversight of the Group's risk management framework, and developing and monitoring the Group's risk management policies.

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations. Internal audit department undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Group's audit committee.

#### ***Credit risk***

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's deposits placed with financial institutions and receivables from customers. The majority of the Group's trade debtors and amounts due from related parties relate to sales of petroleum and chemical products to third parties and related parties operating in the petroleum and chemical industries. Management performs ongoing credit evaluations of its customers' financial condition and generally does not require collateral on trade debtors and related parties. The Group maintains an impairment loss for doubtful accounts and actual losses have been within management's expectations. The details of the Group's credit policy and quantitative disclosures in respect of the Group's exposure on credit risk for trade debtors are set out in note 13.

The carrying amounts of other investments, trade debtors, bills receivable, other debtors, and amounts due from related parties, represent the Group's maximum exposure to credit risk in relation to financial assets.

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**28. FINANCIAL INSTRUMENTS** *(continued)*

*Liquidity risk*

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. Management's approach in managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. Management prepares monthly cash flow budget to ensure that they will always have sufficient liquidity to meet its financial obligation as they fall due. Management arranges and negotiates financing with financial institutions and maintains a certain level of standby credit facilities to reduce the liquidity risk.

At December 31, 2012, the Group's current liabilities exceeded its current assets by RMB 6,035,833. The liquidity of the Group is primarily dependent on its ability to maintain adequate cash inflow from operations, the renewal of its short term bank loans and on its ability to obtain adequate external financing, to support its working capital and meet its debt obligation when they become due. At December 31, 2012, the Group had standby credit facilities with several PRC financial institutions which provided the Group to borrow up to RMB 18,196,000, of which RMB 7,850,000 was unutilized.

Management has carried out a detailed review of the cash flow forecast of the Group for the twelve months ending December 31, 2013. Based on such forecast, management believes that adequate sources of liquidity exist to fund the Group's working capital and capital expenditure requirements, and meet its short term debt obligations as they become due. In preparing the cash flow forecast, management has considered historical cash requirements of the Group as well as other key factors, including the availability of the above-mentioned banking facilities which may impact the operations of the Group during the next twelve-month period. Management is of the opinion that the assumptions used in the cash flow forecast are reasonable.

The following table sets out the remaining contractual maturities at the balance sheet date of the Group's financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on prevailing rates current at the balance sheet date) and the earliest date the Group would be required to repay:

**Table of Contents****28. FINANCIAL INSTRUMENTS** *(continued)**Liquidity risk (continued)*

	Carrying amount	Total contractual undiscounted cash flow	2011		
			Within 1 year or on demand	More than 1 year but less than 2 years	More than 2 years but less than 5 years
Loans and borrowings (current)	5,512,074	5,603,336	5,603,336		
Loans and borrowings (non-current)	160,050	183,933	9,054	133,393	41,486
Trade creditors	3,126,495	3,126,495	3,126,495		
Bills payable	15,688	15,688	15,688		
Other creditors	1,352,367	1,352,367	1,352,367		
Amounts due to related parties	2,242,868	2,242,868	2,242,868		
	12,409,542	12,524,687	12,349,808	133,393	41,486

	Carrying amount	Total contractual undiscounted cash flow	2012		
			Within 1 year or on demand	More than 1 year but less than 2 years	More than 2 years but less than 5 years
Loans and borrowings (current)	11,023,877	11,110,694	11,110,694		
Loans and borrowings (non-current)	1,231,340	1,403,074	74,037	428,298	900,739
Trade creditors	2,886,616	2,886,616	2,886,616		
Other creditors	1,603,022	1,603,022	1,603,022		
Amounts due to related parties	3,411,279	3,411,279	3,411,279		
	20,156,134	20,414,685	19,085,648	428,298	900,739



**Table of Contents****28. FINANCIAL INSTRUMENTS** *(continued)***Market risk**

Market risk is the risk relating to changes in market prices, such as foreign exchange rates and interest rates. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

## (a) Currency risk

Currency risk arises on financial instruments that are denominated in a currency other than the functional currency in which they are measured. The Group's currency risk exposure primarily relates to short term debts denominated in US dollars.

The following table details the Group's exposure at the balance sheet date to currency risk, which mainly arises from short term loans and borrowings denominated in a currency other than the functional currency of the entity to which they relate.

	December 31,	
	2011	2012
Gross exposure arising from loans and borrowings	USD 733,637	USD1,247,296

A 5 percent strengthening / weakening of Renminbi against USD at December 31, 2012 would have increased / decreased net income for the year and retained earnings of the Group by approximately RMB 293,995 (2011: RMB 173,347; 2010: RMB 94,854). This analysis has been determined assuming that the change in foreign exchange rates had occurred at the end of the reporting period and the change was applied to the foreign currency balances at that date to which the Group has significant exposure as stated above, and that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2011 and 2010.

Other than the amounts as disclosed above, the amounts of other financial assets and liabilities of the Group are substantially denominated in the functional currency of respective entity of the Group.

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**28. FINANCIAL INSTRUMENTS** *(continued)*

***Market risk*** *(continued)*

(b) Interest rate risk

The Group's interest rate risk exposure arises primarily from its short term and long term loans. Loans carrying interest at variable rates and at fixed rates expose the Group to cash flow interest rate risk and fair value interest rate risk respectively. The interest rates of loans and borrowings of the Group are disclosed in note 19.

As at December 31, 2012, it is estimated that a general increase/decrease of 100 basis points in variable interest rates, with all other variables held constant, would decrease/increase the Group's net income for the year and retained earnings by approximately RMB 66,827 (2011: RMB 35,185; 2010: RMB 19,808). This sensitivity analysis has been determined assuming that the change in interest rates had occurred at the end of the reporting period and the change was applied to the Group's debts outstanding at that date with exposure to cash flow interest rate risk. The impact on the Group's net income for the year and retained earnings is estimated as an annualized impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis for 2011 and 2010.

***Fair value***

The disclosures of the fair value estimates, methods and assumptions, set forth below for the Group's financial instruments, are made to comply with the requirements of IFRS 7 and IAS 39 and should be read in conjunction with the Group's consolidated financial statements and related notes. The estimated fair value amounts have been determined by management using market information and valuation methodologies considered appropriate. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Group could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

**Table of Contents****28. FINANCIAL INSTRUMENTS** *(continued)**Fair value (continued)*

The fair value of long term loans is estimated by discounting future cash flows thereon using current market interest rates offered to the Group for loans with substantially the same characteristics and maturities ranging from 5.76% to 6.40% (2011: 5.90% to 6.21%). The following table presents the carrying amounts and fair values of the Group's long term loans at December 31, 2011 and 2012.

	2011		2012	
	Carrying amount	Fair value	Carrying amount	Fair value
<b>Liabilities</b>				
Long term loans	160,050	158,721	1,231,340	1,192,960

Unquoted equity investments are individually and in the aggregate not material to the Group's financial condition or results of operations. There are no listed market prices for such interests in the PRC and, accordingly, a reasonable estimate of fair value could not be made without incurring excessive costs.

The fair values of all other financial instruments approximate their carrying amounts due to the short term maturity of these instruments.

**29. POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDED DECEMBER 31, 2012**

Up to the date of issue of these financial statements, the IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended December 31, 2012 and which have not been adopted in these financial statements.

Management is in the process of making an assessment of what the impact of these amendments and new standards is expected to be in the period of initial application and has so far concluded that the adoption of them is unlikely to have a significant impact on the Group's results of operations and financial position.

**30. PARENT COMPANIES**

The directors consider the immediate parent company and the ultimate parent company at December 31, 2012 to be China Petroleum & Chemical Corporation and China Petrochemical Corporation, respectively, which are incorporated in the PRC. China Petroleum & Chemical Corporation produces financial statements available for public use.

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**Exhibit Index**

<b>No.</b>	<b>Exhibit</b>
8	A list of subsidiaries of Sinopec Shanghai Petrochemical Company Limited.
12.1	Certification of President Required by Rule 13a-14(a).
12.2	Certification of Chief Financial Officer Required by Rule 13a-14(a).
13.1	Certification of President Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
13.2	Certification of Chief Financial Officer Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
15.1	Letter from KPMG regarding Item 16F of this annual report.