



中化香港控股有限公司

SINOCEM HONG KONG HOLDINGS LIMITED



## Nurturing China's Agriculture Sector



2006 Interim Results  
September 2006

## Disclaimer

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### ■ 2H2006 Outlook



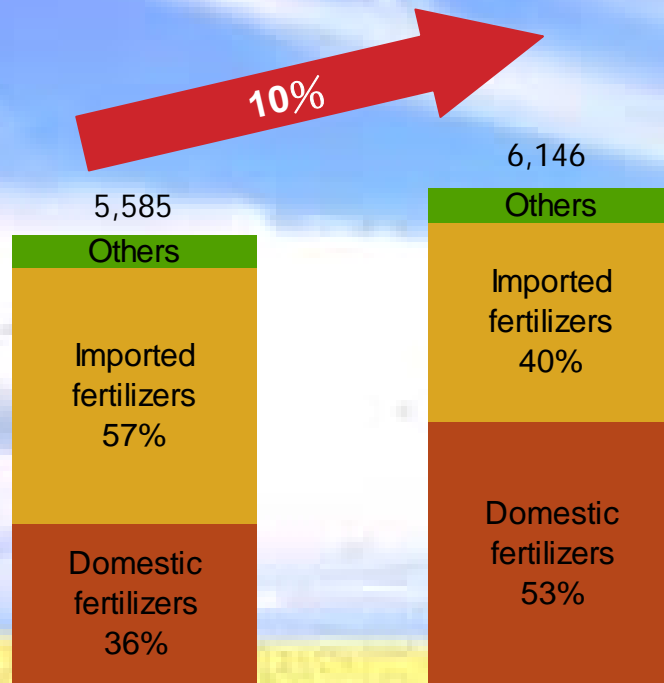
# 1H 2006 Financial Highlights: High Growth, High Returns

(HK\$ '000)	1H 2005 <sup>(1)</sup>	1H 2006	Change
Sales volume (Kt)	5,585	6,146	+10%
<b>Turnover</b>	<b>9,624,333</b>	<b>10,305,707</b>	<b>+7%</b>
Gross profit	771,397	838,856	+9%
Profit before tax	464,979	554,332	+19%
<b>Net profit</b>	<b>389,711</b>	<b>465,318</b>	<b>+19%</b>
<b>EPS (HK cents)</b>	<b>7.25</b>	<b>8.01</b>	<b>+11%</b>
ROE	11%	12%	
Debt-to-equity ratio	34%	20%	

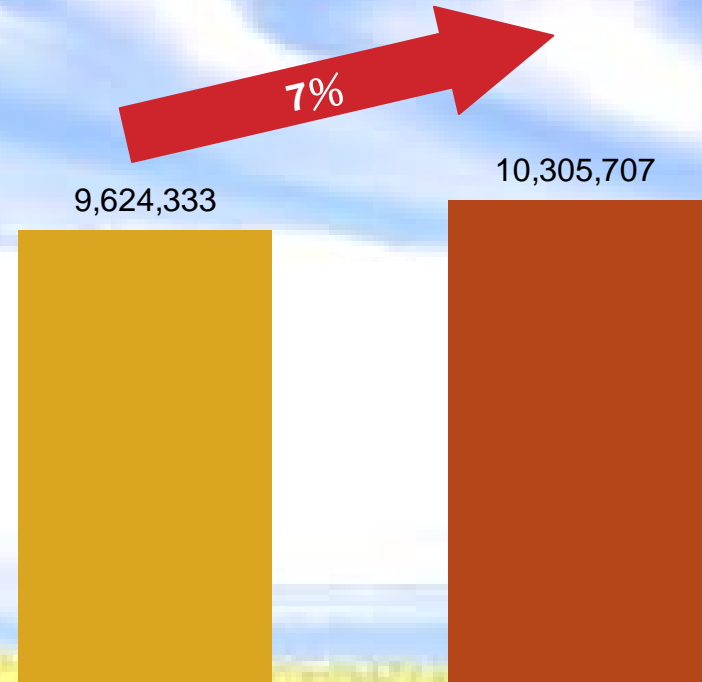
Note: (1) 2005 audited figure on a pro rata basis

# Steady Growth in Operation Scale

Sales volume (Kt)



Turnover (HKD '000)



1H 2005

1H 2006

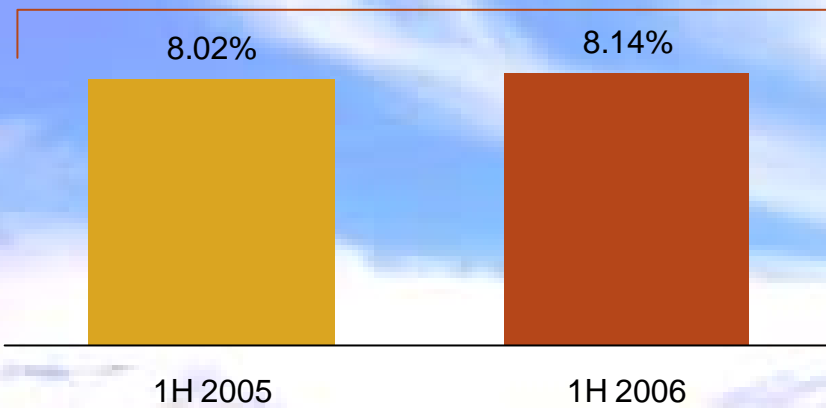
1H 2005

1H 2006

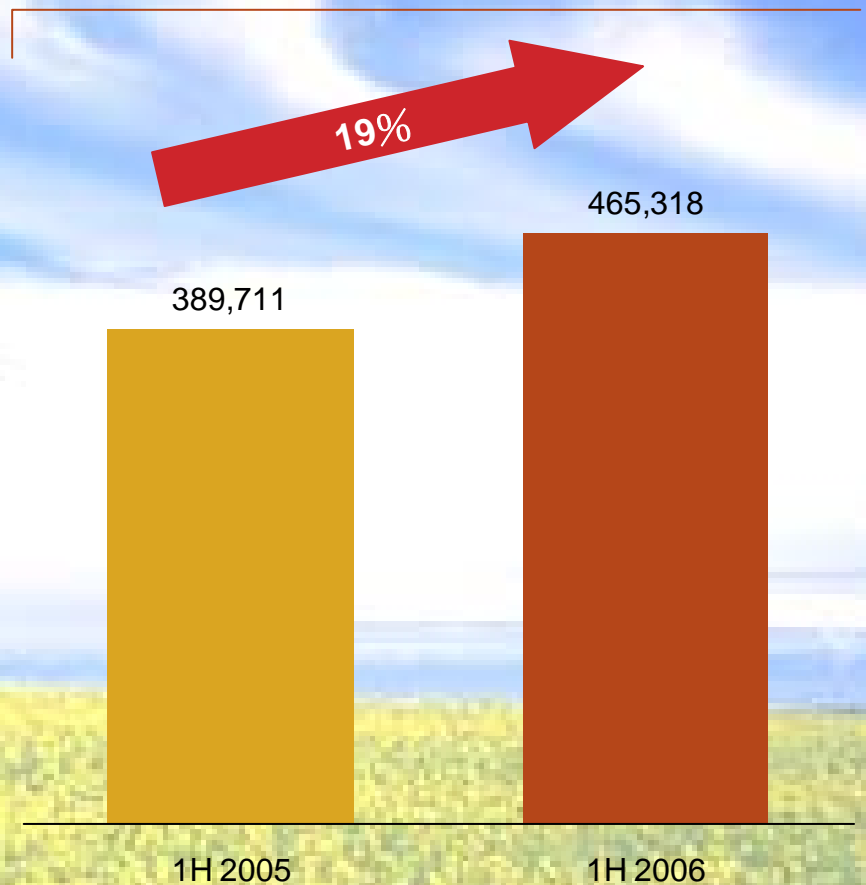


# Continuous Improvement in Profitability

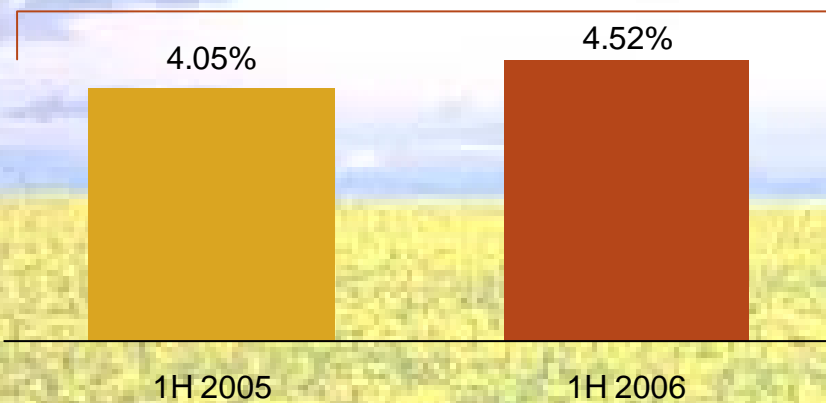
**Gross margin (%)**



**Net profit (HKD '000)**

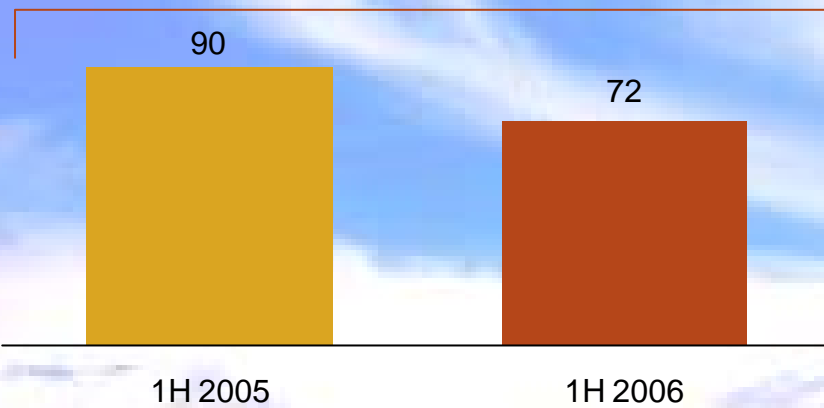


**Net Margin (%)**

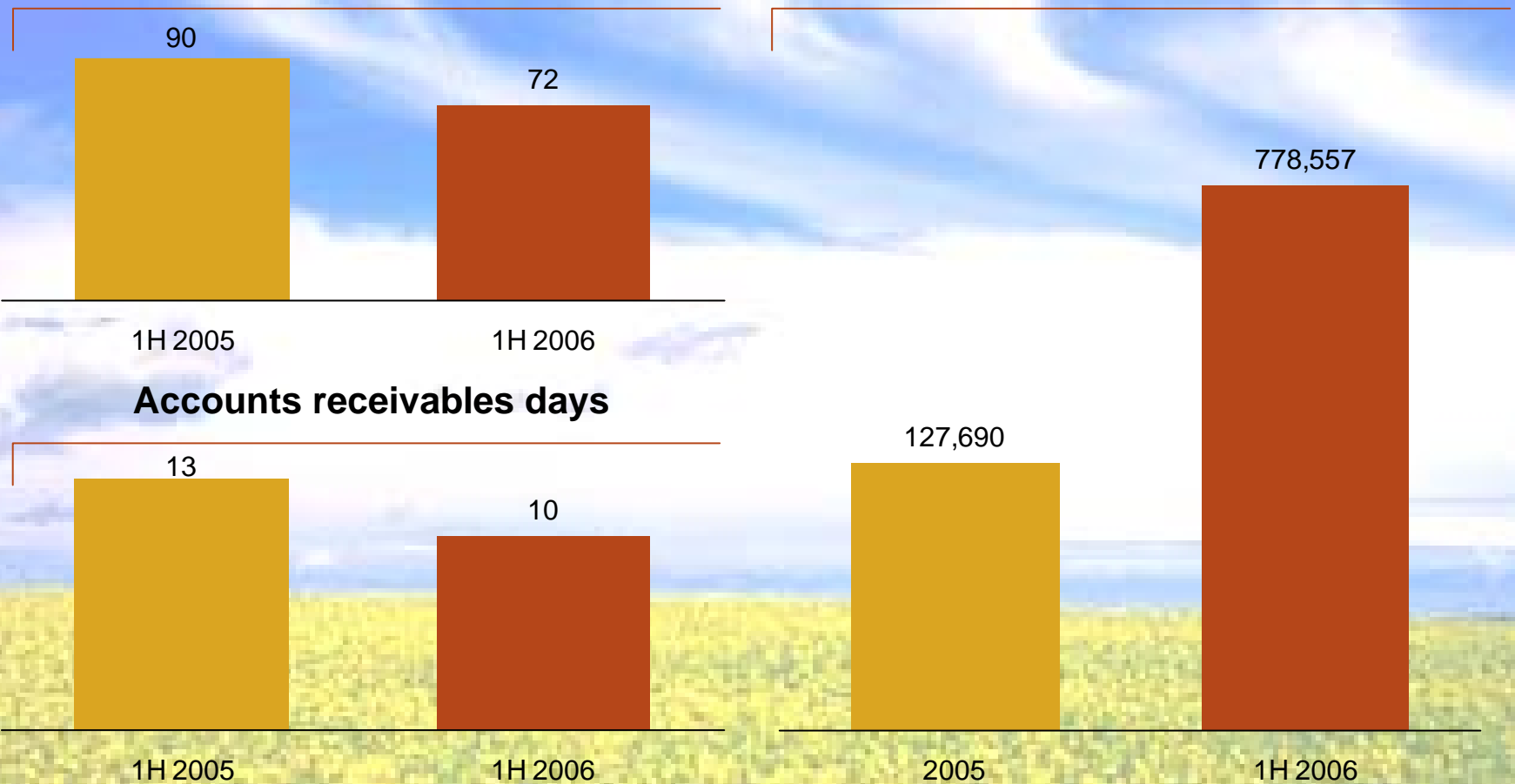


# Improved Operational Efficiency and Cash Flow

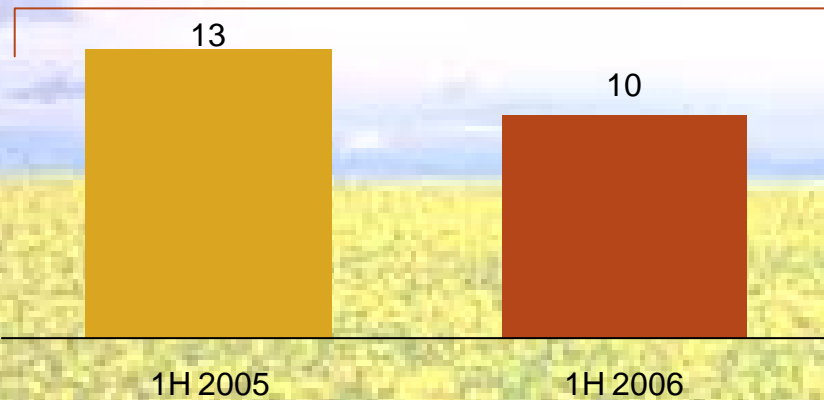
## Inventory days



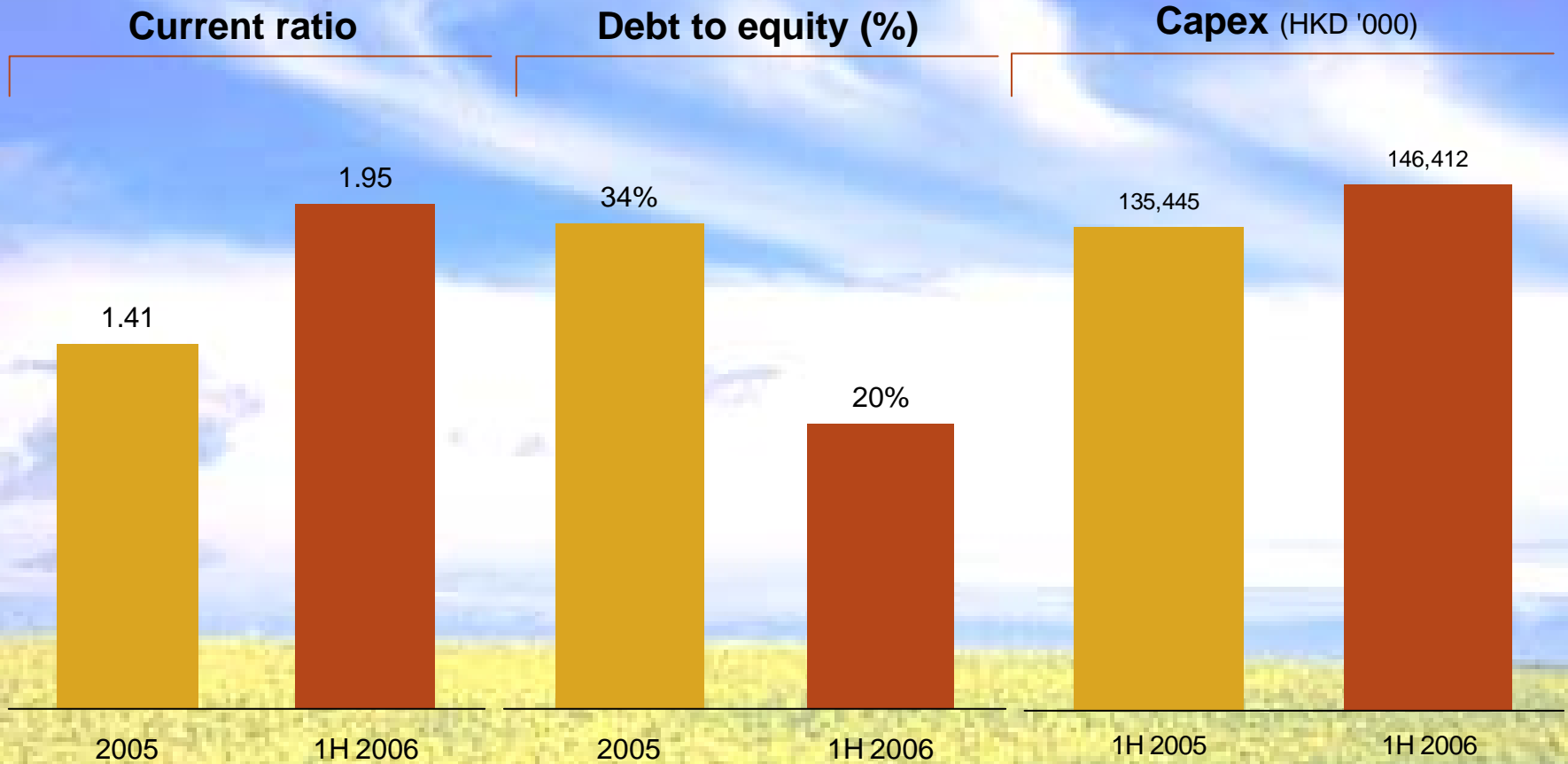
## Operating Cashflow (HKD '000)



## Accounts receivables days



# Solvency and Capital Expenditure





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# Proven Business Strategy: Focusing on Distribution and Integrating Production, Supply and Sales for Synergic Development

- **Upstream strategy: leverage resources advantage (potash and phosphate) to expand production capacity and reach a capacity of around 8 mn tonnes by 2008**

- Capacity expansion of existing invested companies
- Fertilizer assets acquisition from parent company
- Strategic investment in production enterprises with resource advantage

- **Downstream strategy: expand distribution network with the support of agrichemical services, and increase number of outlets to 2000 by 2008**

- Optimization of existing outlets and setting up new outlets
- New market expansion, setting up at least one outlet in each of the 1,800 agricultural counties nationwide

- **Trade and distribution strategy: average growth rate of operation and profit at 20%, increase market share in China fertilizer sector from 12% in 2005 to 20-25% in 2008**

- Solidify import fertilizers supplier network to maintain leading position in both import potash and compound fertilizer
- Improve supply system for domestic fertilizers and expand operation scale of nitrogen fertilizers
- Promote product portfolio sales with segmented marketing strategy to improve product profitability and increase market share



# 1H 2006 Strategic Development – Increased Production Capacity in Resource Advantage

■ **Upstream strategy** : leverage resources advantage (potash and phosphate) to expand production capacity and reach a capacity of around 8 mn tonnes by 2008

**Downstream strategy**

**Trade and distribution strategy**

The potash reserve in Qinghai accounts for over 97% of total national reserves

Shanxi is the coal-based Nitrogen fertilizer production center of China

Yunnan and Guizhou account for 70% of national rich phosphorite reserve

★ compound    ▲ Nitrogen  
● Phosphate    ■ potash

## Increased production capacity in resource advantage

- MAP productivity of Sinochem Fuling increased by 0.3 mt
- Gross capacity reached 3.03mt, a growth of 11% over 2005, including capacity of phosphate fertilizers 2.36 mt and compound fertilizers 0.67 mt

## Planned acquisition of Salt Lake Potash

- Salt Lake Potash acquisition currently pending approval from domestic authorities

## Comprehensive product offerings

- The only domestic producer/provider of full-line product offerings

# 1H 2006 Strategic Development – Expanded Distribution Network and Provided Agrichemical Services

## Upstream strategy

- **Downstream strategy** : expand distribution network with the support of agrichemical services, and increase number of outlets to 2000 by 2008

## Trade and distribution strategy

## Further expansion of distribution network

- 2 branches set up in 1H2006 and net increase of 80 outlets (133 new outlets opened and 53 existing outlets merged their operations). On June 30th, the company has 16 branches and 1,143 outlets
- Covering 21 agricultural provinces and 75% of farmland in China
- Network distribution sales accounted for 65%

## Agrichemical services offering

- Sponsors of “Agrochem Plaza” program with China National Radio to educate farmers about scientific application of fertilizers
- National toll free hotline
- Joint promotion of specialized formula fertilizer projects with universities
- Provided integrated services



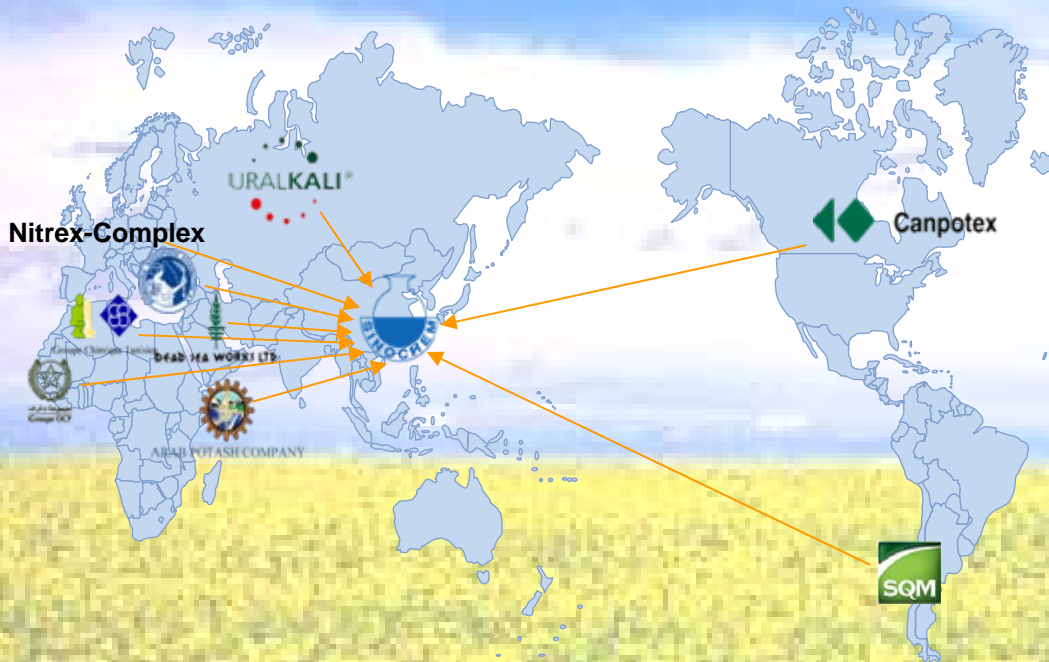
# 1H 2006 Strategic Development – Solidified and Enhanced Domestic and International Supply Chain

Upstream strategy

Downstream strategy

■ Trade and Distribution strategy : average growth rate of operation and profit at 20%, increase market share in China fertilizer sector from 12% in 2005 to 20-25% in 2008

- Signed exclusive contracts with 9 global fertilizer suppliers to ensure competitive position in imported fertilizer business
- Improved supply system of domestic fertilizer, implemented supply chain management and enhanced procurement of domestic fertilizers
  - Improved stability and sustainability of domestic supply via strategic investments in large producers (e.g. cooperation with Luxi Chemicals)
  - Enhanced regional procurement from medium and small producers leveraging regional distribution network
- Signed import contracts with Canpotex, DSW, APC and other major international potash suppliers for 2006 after conclusion of price negotiations





# 1H 2006 Strategic Development – Provide One-stop Shopping Solution

Upstream strategy

Downstream strategy

■ Trade and Distribution strategy : average growth rate of operation and profit at 20%, increase market share in China fertilizer sector from 12% in 2005 to 20-25% in 2008

- Shifting from "potash being No. 1" to implement the strategy of "co-development of diversified fertilizers", with top priority given to expanding nitrogen business. During first half 2006 the pattern of "co-development of diversified fertilizers" basically took shape.

Product	Percentage
potash	55%
nitrogen	16%
compound	15%
phosphate	14%

Product mix (1H 2005 Turnover)

Product	Percentage
potash	40%
nitrogen	26%
compound	20%
phosphate	14%

Product mix (1H 2006 Turnover)

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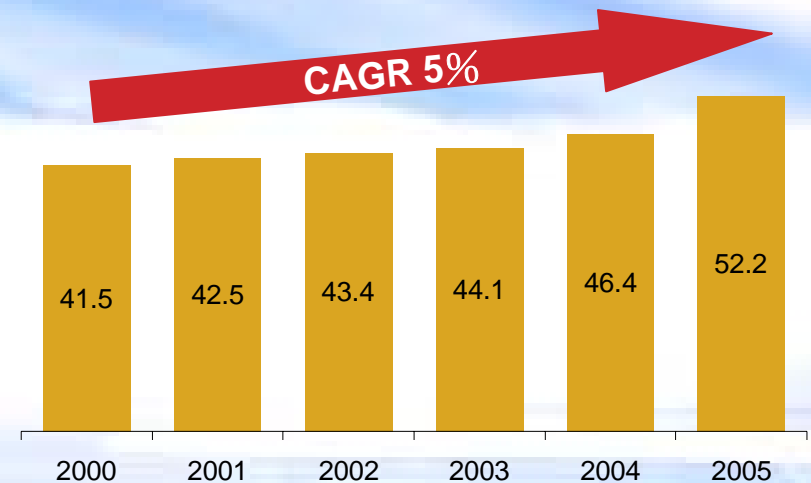
# 2H2006 Outlook – Favorable Macro Environment

## ■ Supportive agricultural policies

- Agricultural tax abolished nationwide and tax burden of farmers reduced by RMB 125 bn
- “Sannong” (agriculture, rural areas and farmers ) expenditure reached RMB 339.7 bn in 2006, up by RMB 42.2 bn over last year, an increase of 14.2%
- Implement strict policy to protect agricultural land
- Minimum purchase price applied to grains
- Direct subsidy to grain farmers total RMB 26.7 bn, an increase of 102%
- Aim to raise farmers’ average annual income by over 5% during the “11<sup>th</sup> 5 year plan” period

## ■ Growing fertilizer demand

- Thanks to the agricultural products maintaining high and stable price level and continued support from the State, demand for fertilizers will keep rising, providing bright prospects for the fertilizer industry



**Favorable State agricultural policies and ever growing fertilizer demand provide supportive environment for long-term growth**

## 2H2006 Outlook – Major Policy Changes Expected

- According to its WTO commitments, China will fully open its fertilizer wholesale & retail markets to foreign companies by 11 December, 2006
- The Chinese government plans to abolish price controls on fertilizers. The reform principle is “remove price controls, abolish preferential policies, and directly subsidize the farmers”

Remove price controls – fully remove controls on (including imported fertilizers) factory prices, wholesale and retail prices. Prices will be determined by the market and regulated by the government through strategic reserves and import & export balancing

Abolish preferential policies – gradually abolish favorable power prices, gas prices, railway tariffs, etc. for fertilizer producers over two to three years

Direct subsidies to farmers – will directly subsidize farmers instead of subsidizing fertilizer industry

**Free competition in China’s fertilizer market will allow the Company to capitalize on its competitive strength and further sharpen its cutting edge in the fertilizer industry**

## 2H2006 Outlook – Expand Business Scale and Improve Profitability and Shareholder Return

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- **Upstream: continue to improve the Company’s ability to acquire production of natural resources advantage and build a solid basis for the Company’s sustainable development**
  - execute Salt Lake Potash acquisition
  - explore industry policy changes and M&A opportunities focused on resources advantages
- **Downstream: push forward distribution network expansion and use agrichemical services to improve network quality and core competitiveness**
  - complete nation-wide distribution network with opening of outlets in 1,800 agricultural counties nationwide
  - Improve the five major functions of the distribution network – “product sales, customer relation maintenance, brand promotion, agrichemical services, and fighting against counterfeiting to protect the Group’s interest”



## 2H2006 Outlook – Expand Business Scale and Improve Profitability and Shareholder Return

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### ■ Trade & Distribution: maintain and expand international and domestic supply chain systems and enhance Company's position as an organizer of global fertilizer trade and distribution

- solidify international alliances based on “exclusive agent and long-term contract” to source global high-quality fertilizer resources
- strengthen product segmentation policy

Potash fertilizers: after the completion of price negotiations, move forward to further consolidate and improve the Company's leading position in Chinese market

Nitrogen fertilizers: apply capital market principles and focus on liquidity rather than asset investment to improve efficiency, sustainability and stability of resource sourcing

Phosphate and compound fertilizers: leverage on the advantage of production-sales integration, gradually improve competitiveness of both products

### ■ Ongoing refinement of the Company's strategic plan for the next three years (2007-2009)

- fertilizer business: continue to implement the strategy of “focusing on distribution and integrating production, supply and sales for synergic development”
- other opportunities: explore entry into related markets such as pesticides and seeds





**Q & A**



# Appendices

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- **Appendix I: Major shareholders with solid strength**
- **Appendix II: Sea-borne potash import negotiations**
- **Appendix III: Issue HK\$ 1.3bn zero-coupon convertible bond**
- **Appendix IV: Strategic investment in Luxi Chemical**
- **Appendix V: Glossary**

# Appendix I: Major Shareholders with Definite Strengths

- Listed on HKSE through reverse takeover in July 2005



## Sinochem Corporation

- Fortune 500 company for 16 years, ranked 304th in 2006.
- 2005 turnover US\$ 21.4bn, total assets US\$ 7.8bn
- Major businesses include fertilizers, petroleum, chemicals and financial services
- Fertilizer assets ownership
  - Salt Lake Potash: Shenzhen listed company, potassium chloride capacity 1.7m TPA. 18.49% interest
  - Tianji Sinochem: Urea capacity 600,000 TPA. 40% interest
  - Shandong Fertilizers: compound fertilizer capacity 600,000 TPA. 60% interest

## PotashCorp

- Listed on Toronto Stock Exchange and NYSE
- 2005 total production exceeded 13m tonnes
- World's largest potash producer, accounting for 22% of global potash production



# Appendix II: Sea-borne potash import negotiations

## ■ Origin

- During the 2005 TFI meeting in Canada, Belarusian Potash Company (BPC) mentioned that imported sea-borne potash prices in the Chinese market were lower than in neighboring markets and formally announced it would increase prices to China by US\$ 40 per tonne in 2006
- Chinese importers reacted by holding price negotiations during 2006 under the leadership of the China Chamber of Commerce for Metals, Minerals & Chemicals Importers & Exporters

## ■ Negotiation progress

- The first round of negotiations started on 10 February, 2006 and negotiations ended on 21 July, 2006.
- After multiple rounds of negotiations at various price levels, the parties settled on an increase of \$ 25 per tonne, substantially lower than the original \$40.
- During this period, China did not import a single tonne of sea-borne potash under new contract

## ■ Agreement was reached on 21 July, 2006

- China's imported potash price in 2006 increases by \$ 25 per tonne from the 2005 contract price with BPC
- Other international potash suppliers will similarly adjust their export price of potash to China in 2006
- China's contract import quantity of potash in Aug-Dec 2006 is expected to remain the same as in 2005 on pro rata basis



## Appendix III: Issuance of HK\$ 1.3bn Zero-coupon Convertible Bond

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### Key terms

Pricing date:	20 July, 2006
Base size:	HK\$ 1.0bn
Option to increase:	HK\$ 300m
Maturity:	5 years (7 Aug, 2011)
Investor put:	3 years (7 Aug, 2009)
Issue price:	100.00%
Redemption price:	115.55%/127.23%
Coupon:	0.00%
Yield to maturity:	annual 4.875%, calculated semi-annually
Conversion premium:	30%
Issuer's call feature:	Callable after 3 years subject to a 130% accreted trigger
Dividend protection:	full dividend protection

## Appendix IV: Strategic Investment in Luxi Chemical



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- China's largest fertilizer distributor
- Covering 21 provinces and 75% of farmland area



山东鲁西化工股份有限公司  
Shandong Luxi Chemical Co., Ltd

- China's largest coal-based urea producer
- Ranking No. 1 in terms of fertilizer production in 2003-2005

### Investment

- Sinochem Hong Kong bought 50m shares of Luxi Chemical at RMB 2.6 each
- Total investment of RMB130 mn, representing 4.78% of Luxi's total capitalization

### Strategic alliance:

- Exclusive nitrogen fertilizer sales rights in Heilongjiang, Jilin, Liaoning and Jiangsu
- Annual supply of 150,000, 300,000 and 500,000 tonnes from 2006 to 2008 respectively
- Sinochem Hong Kong will provide 70% of Luxi Chemical's total potash requirement

**Win-win Solution**



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## Appendix V: Glossary

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### **Fertilizer**

Organic or inorganic material containing one or more of the nutrients—mainly nitrogen, phosphorus, and Potash, and other essential elements required for plant growth. Added to the soil or other medium, fertilizers provide plant nutrients that are naturally lacking or that have been removed by harvesting or grazing, or by physical processes such as leaching or erosion

### **Potash fertilizer**

Potash fertilizer is the commonly used term for the soil fertilizer forms of Potash (element K). Potash fertilizers should generally be applied at sowing time. The  $K^+$  ions are adsorbed in the soil and thus remain available, yet largely protected against leaching. Potash fertilizer involves in production, transportation and accumulation of sugar in plants. It maintains electrical balance in plant cell and assists hardiness of plants and their resistance to water stress, pests and diseases

### **Phosphate fertilizer**

Phosphate fertilizer is the commonly used term for the soil fertilizer forms of Phosphate (element P). Phosphate fertilizer encourages rooting, blooming and fruit production

# Glossary (continued)

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## **Nitrogen fertilizer**

Nitrogen fertilizer is the commonly used term for the soil fertilizer forms of nitrogen (element N). It is an important component of proteins and chlorophyll and is most responsible for yield increase

## **Compound fertilizer**

Compound fertilizer provides a mix of nutrients that can be tailored to a specific plant's nutritional needs, taking into account soil and climatic conditions. Compound fertilizers contain at least two of the three main plant nutrients: nitrogen (N), phosphate (P) and Potash (K), which together is often referred to as NPK fertilizer

## **Mt nutrient**

Million tonnes of nutrient, quantity of consumption and production of fertilizers are expressed in weight containing 100% effective nutrient