



鄭州燃氣股份有限公司
Zhengzhou Gas Company Limited*

intensifying reforms

regularizing management

capturing opportunities

stepping up development pace

Interim Report 2004

* for identification purpose only

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This report, for which the directors (the “Directors”) of Zhengzhou Gas Company Limited collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on GEM of The Stock Exchange of Hong Kong Limited (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company. The Directors having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

FINANCIAL HIGHLIGHTS

- Unaudited consolidated turnover and profit attributable to shareholders of the Group for the six months ended 30 June 2004 amounted to approximately RMB214,796,000 and RMB37,080,000 respectively, representing respective increases of approximately 22.72% and 31.85% over the corresponding period of last year.
- Sales of piped natural gas for the Relevant Period amounted to approximately RMB130,497,000, representing an increase of approximately 36.76% over the corresponding period of last year, which was primarily attributed to the increase in the number of residential, industrial, commercial and vehicular users, coupled with a significant increase in gas consumption by industrial, commercial and vehicular users.
- Turnover derived from gas pipeline construction aggregated to approximately RMB68,598,000 for the Relevant Period, representing an increase of approximately 34.85% over the corresponding period of last year, which was primarily attributed to satisfactory growth in gas pipeline construction projects for residential users.
- Basic earnings per share for the Relevant Period was approximately RMB0.030, representing an increase of approximately RMB0.008 as compared with approximately RMB0.022 for the corresponding period of last year.
- The Directors do not recommend the payment of any interim dividend for the Relevant Period.

FINANCIAL STATEMENTS

The board of directors (the "Board") of Zhengzhou Gas Company Limited (the "Company") is pleased to present the unaudited financial statements of the Company and its subsidiaries (collectively the "Group") for the six months ended 30 June 2004 (the "Relevant Period") and comparative figures of the corresponding period of last year.

Consolidated Income Statement (Unaudited)

For the three months and six months ended 30 June 2004 and 2003

	Notes	Three months ended 30 June		Six months ended 30 June	
		2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Turnover	3	104,369	83,258	214,796	175,034
Cost of sales		(61,688)	(55,693)	(135,064)	(115,786)
Gross profit		42,681	27,565	79,732	59,248
Other revenue		248	282	421	404
Selling and distribution costs		(2,827)	(1,944)	(5,036)	(4,383)
Administrative costs		(7,934)	(7,829)	(15,282)	(14,959)
Other operating costs		(25)	(20)	(125)	(20)
Profit from operating activities		32,143	18,054	59,710	40,290
Finance costs		–	(47)	–	(57)
Profit before income tax		32,143	18,007	59,710	40,233
Income tax expenses	4	(12,885)	(4,137)	(20,325)	(10,539)
Profit before minority interests		19,258	13,870	39,385	29,694
Minority interests		(1,037)	(778)	(2,305)	(1,571)
Net profit attributable to shareholders		18,221	13,092	37,080	28,123
Basic earnings per share (RMB Yuan)	5	0.015	0.010	0.030	0.022

Condensed Consolidated Balance Sheet

	Notes	As at 30 June 2004 RMB'000 (Unaudited)	As at 31 December 2003 RMB'000 (Audited)
ASSETS			
Non-current assets			
Long term investment		200	200
Deferred income tax assets		–	1,266
Property, plant and equipment	7	238,749	203,954
Construction in progress		131,846	123,962
		<u>370,795</u>	<u>329,382</u>
Current assets			
Cash and cash equivalents		98,547	115,261
Trade receivables	8	33,554	39,816
Bills receivables		3,719	–
Inventories		7,898	1,234
Contracted construction work in progress		–	2,008
Prepayments, deposits and other receivables		8,449	14,698
		<u>152,167</u>	<u>173,017</u>
TOTAL ASSETS		<u>522,962</u>	<u>502,399</u>
EQUITY AND LIABILITIES			
Equity			
Share capital	9	125,150	125,150
Reserves	10	218,204	186,632
		<u>343,354</u>	<u>311,782</u>
Minority interests		<u>12,388</u>	<u>13,180</u>
Non-current liabilities			
Deferred income tax liabilities		1,718	–
Due to the Holding Company	11	12,433	12,433
		<u>14,151</u>	<u>12,433</u>
Current liabilities			
Dividend payables		62	–
Trade payables	12	26,911	18,568
Deferred income		89,956	88,958
Other payables and accrued amounts		12,342	23,712
Tax payable		12,565	11,697
Due to the Holding Company	11	10,447	21,509
Due to fellow subsidiaries	13	786	560
		<u>153,069</u>	<u>165,004</u>
TOTAL EQUITY AND LIABILITIES		<u>522,962</u>	<u>502,399</u>

Condensed Consolidated Cash Flow Statement (Unaudited)

	Six months ended 30 June	
	2004 <i>RMB'000</i>	2003 <i>RMB'000</i>
Net cash inflow/(outflow) from operating activities	41,125	41,343
Net cash inflow/(outflow) from investing activities	(49,298)	(42,971)
Net cash inflow/(outflow) from financing activities	(8,542)	(8,058)
Net increase/(decrease) in cash and cash equivalents	(16,715)	(9,686)
Balance of cash and cash equivalents, at the beginning of the period	115,261	166,969
Balance of cash and cash equivalents, at the end of the period	<u>98,547</u>	<u>157,283</u>

Condensed Consolidated Statement of Changes in Equity (Unaudited)

	Six months ended 30 June	
	2004 <i>RMB'000</i>	2003 <i>RMB'000</i>
Total equity, at the beginning of the period	311,782	277,029
Net profit for the period	37,080	28,123
Dividend	(5,507)	(18,184)
Total equity, at the end of the period	<u>343,355</u>	<u>286,967</u>

NOTES TO FINANCIAL STATEMENTS

1. BASIS OF PREPARATION AND ACCOUNTING POLICIES

The Company was incorporated as a joint stock limited company in the People's Republic of China (the "PRC") on 18 December 2000. The overseas listed shares with a nominal value of RMB0.10 each (the "H Shares") in the registered share capital of the Company were listed on GEM on 29 October 2002.

The condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements of Chapter 18 of the GEM Listing Rules, International Financial Reporting Standards ("IFRS") 34 "Interim Financial Reporting" promulgated by the International Accounting Standards Board and the Hong Kong Companies Ordinance.

The accounting policies and methods used in preparing the condensed consolidated financial statements are the same as those used in the financial statements of the Group for the financial year ended 31 December 2003.

2. SEGMENT INFORMATION

The principal activities of the Group are the sale of natural gas and relevant appliances to local consumers and the construction of gas pipelines network for local consumers. The products and services of the Group are subject to similar risks and returns and, therefore, the Group has only one business segment. The principal assets of the Group are located in Zhengzhou, Henan Province, the PRC. Accordingly, no segmental analyses by business and geographical segments are provided.

3. TURNOVER

An analysis of the Group's turnover for the three months and six months ended 30 June 2004 together with the comparative figures for the corresponding periods in 2003 is as follows:

	Three months ended 30 June		Six months ended 30 June	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Natural gas	56,460	48,385	130,497	95,423
LPG (Note)	–	–	–	11,051
Gas appliances	2,570	3,440	3,423	5,108
Gas pipeline				
– Gas pipeline construction	37,666	24,798	68,598	50,869
– Gas pipeline repairs and maintenance services	8,917	7,819	14,490	14,799
Others	35	75	59	378
	105,648	84,517	217,067	177,628
Less: Business tax and government surcharges	(1,279)	(1,258)	(2,271)	(2,593)
Turnover	104,369	83,258	214,796	175,034

Note: Pursuant to the resolution of the Board dated 18 March 2003, the Company has terminated the LPG sales business since 1 April 2003. The Directors of the Company are of the view that the termination of the LPG sales business will not have any significant impact on the Group's operating results.

4. TAX

No provision for Hong Kong tax has been made as none of the Group's income was arising in nor derived from Hong Kong during the Relevant Period. The PRC income tax of the Company has been provided at the applicable income tax rate of 33% on estimated assessable profit in accordance with the relevant tax laws and regulations.

	Three months ended 30 June		Six months ended 30 June	
	2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Provision for income tax in respect of profit for the period:				
– Current	12,669	2,943	15,169	6,864
– Deferred	216	1,194	5,156	3,675
Tax expenses for the period	<u>12,885</u>	<u>4,137</u>	<u>20,325</u>	<u>10,539</u>

5. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the net profit attributable to shareholders of approximately RMB37,080,000 (corresponding period in 2003: approximately RMB28,123,000) divided by the weighted average number of 1,251,500,000 shares of the Company in issue during the Relevant Period (corresponding period in 2003 was 1,251,500,000 shares).

Diluted earnings per share for the six months ended 30 June 2003 and 2004 have not been calculated as no diluting events existed during those periods.

6. INTERIM DIVIDEND

The Board does not recommend the payment of any interim dividend for the six months ended 30 June 2004.

7. DEPRECIATION

During the Relevant Period, depreciation charge in respect of the Group's property, plant and equipment was approximately RMB6,904,000 (the corresponding period of 2003: approximately RMB4,949,000).

8. TRADE RECEIVABLES

	As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
Outstanding balances by aging:		
Within 30 days	25,294	35,758
31 days to 90 days	7,375	3,917
91 days to 180 days	859	851
181 days to 365 days	901	244
Over 365 days	590	511
	<u>35,019</u>	<u>41,281</u>
Less: Provision for bad and doubtful debts	(1,465)	(1,465)
	<u>33,554</u>	<u>39,816</u>

9. SHARE CAPITAL

During the Relevant Period, there was no change in the share capital of the Company.

	As at 30 June 2004		As at 31 December 2003	
	Number of shares '000	Nominal value RMB'000	Number of shares '000	Nominal value RMB'000
Registered	<u>1,251,500</u>	<u>125,150</u>	<u>1,251,500</u>	<u>125,150</u>
Issued and fully paid share capital:				
Domestic Shares of RMB0.10 each	<u>700,840</u>	<u>70,084</u>	<u>700,840</u>	<u>70,084</u>
H Shares of RMB0.10 each	<u>550,660</u>	<u>55,066</u>	<u>550,660</u>	<u>55,066</u>
	<u>1,251,500</u>	<u>125,150</u>	<u>1,251,500</u>	<u>125,150</u>

10. RESERVES

	Share premium RMB'000	Statutory surplus reserve RMB'000	Statutory public welfare fund RMB'000	Discretionary surplus reserve RMB'000	Undistributed profit RMB'000	Total RMB'000
As at 1 January 2003	101,026	6,025	6,025	2,124	36,679	151,879
Dividend paid for 2002					(18,184)	(18,184)
Transferred from retained earnings				3,932	(3,932)	–
Profit for the period					15,031	15,031
As at 31 March 2003	<u>101,026</u>	<u>6,025</u>	<u>6,025</u>	<u>6,056</u>	<u>29,594</u>	<u>148,726</u>
Profit for the period					13,092	13,092
As at 30 June 2003	<u>101,026</u>	<u>6,025</u>	<u>6,025</u>	<u>6,056</u>	<u>42,686</u>	<u>161,817</u>
As at 1 January 2004	101,026	13,797	13,797	6,180	51,832	186,632
Dividend paid for 2003					(5,507)	(5,507)
Transferred from retained earnings				6,572	(6,572)	–
Profit for the period					18,859	18,859
As at 31 March 2004	<u>101,026</u>	<u>13,797</u>	<u>13,797</u>	<u>12,752</u>	<u>58,612</u>	<u>199,984</u>
Profit for the period					18,221	18,221
As at 30 June 2004	<u>101,026</u>	<u>13,797</u>	<u>13,797</u>	<u>12,752</u>	<u>76,833</u>	<u>218,204</u>

11. DUE TO THE HOLDING COMPANY

	As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
Current (Note (1))	10,447	21,509
Long-term (Note (1))	12,433	12,433
	<u>22,879</u>	<u>33,942</u>

Note:

1. The amount due to Zhengzhou Gas Group Co., Ltd. (the "Holding Company") is unsecured and interest-free. Pursuant to the repayment agreement (the "Repayment Agreement") entered into between the Company and the Holding Company on 30 September 2002, the first installment of RMB10,000,000 of the loan of RMB32,433,000 which the Company borrowed from the Holding Company has fallen due on 1 March 2004. The Company has repaid the first installment pursuant to the Repayment Agreement. According to the Repayment Agreement, the repayments are subject to the following conditions: (i) the Group has positive cashflow and retained earnings and such positive cash flow is sufficient to fund the repayment of the amount due and all working capital needs of the Group for the financial year in which such repayment is required to be made; and (ii) each of the independent non-executive Directors confirms that such repayment of any of the outstanding amount will not adversely affect the Group's operations or the implementation of its business plans during the year ending 31 December 2004. After taking into account of the operation forecast, investment plans and cashflow prediction of 2004, the Board of the Company is of the view that the operating position in 2004 fulfils the requirements of the first condition set out above. At the same time, after taking into account of the operation forecast, investment plans and cashflow prediction of 2004, each of the independent non-executive directors believes that the repayment of the first installment will not adversely affect the Group's operations or the implementation of its business plans during the year ending 31 December 2004. Since the two conditions of the Repayment Agreement are satisfied, the Board decided to pay the first installment.

Pursuant to the Repayment Agreement, the outstanding balance of RMB22,433,000 due to the Holding Company will fall due as follows:

Repayable on	RMB'000
31 December 2004	10,000
31 December 2005	<u>12,433</u>
Portion classified as current liabilities	<u>(10,000)</u>
Non-current liabilities portion	<u>12,433</u>

Apart from the RMB22,433,000 payable to the Holding Company as stated above, the balance payable to the Holding Company is unsecured and non-interest bearing.

12. TRADE PAYABLES

	As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
Outstanding balances by aging:		
Within 30 days	13,887	11,821
Between 31 days to 90 days	8,613	2,402
Between 91 days to 180 days	700	2,890
Between 181 days to 365 days	2,912	591
Over 365 days	798	864
	26,911	18,568

13. DUE TO FELLOW SUBSIDIARIES

The amounts due to fellow subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

14. CONNECTED TRANSACTIONS

The Company entered into a sale and purchase agreement (the "Sale and Purchase Agreement") on 30 March 2004 for the acquisition of three assets (the "Acquisition"), including distant monitoring and signaling system, natural gas distribution pipelines and pipeline network cathode protection system (the "Assets") from the controlling shareholder of the Company, Zhengzhou Gas Group Co., Ltd. (鄭州燃氣集團有限公司) (the "Vendor") for an aggregate consideration (the "Consideration") of RMB19.7 million (equivalent to approximately HK\$ 18.5 million) which will be settled in cash.

As set out in the section headed "Business Objectives" in the prospectus of the Company dated 22 October 2002 (the "Prospectus"), the Company proposed to upgrade the overall management efficiency of the pipeline networks, which includes the pipeline network cathode protection system and the distant monitoring and signaling system. The Directors consider that the safety, stability and economy of gas transmission is crucial to the Group's business and the Acquisition provides a valuable opportunity for the Company to enhance its overall management efficiency which is in line with the business objectives set out in the Prospectus. Meanwhile, the Board believes that the acquisition of the new natural gas distribution pipelines in Zhengzhou under the Sale and Purchase Agreement serves to broaden the revenue base as well as the earning potential of the Company. In this regard, the Board believes that the Acquisition is in the interests of the Company and the shareholders of the Company as a whole.

The terms of the Sale and Purchase Agreement (including the Consideration) have been determined after arm's length negotiations between the Company and the Vendor, with reference to the preliminary valuation of the Assets of RMB19.8 million (equivalent to approximately HK\$18.6 million) as at 29 February 2004 as appraised by Vigers Appraisal & Consulting Limited, an independent valuer. The Directors (including the independent non-executive Directors) believe that the terms of the Sale and Purchase Agreement have been based on normal commercial terms and are fair and reasonable so far as the Shareholders are concerned.

As the Vendor is the controlling shareholder of the Company, the Acquisition constitutes a connected transaction of the Company under the GEM Listing Rules. As the Consideration for the Acquisition exceeds the higher of HK\$10,000,000 or 3% of the net tangible assets of the Company, the Acquisition accordingly is subject to the reporting, announcement and independent Shareholders' approval requirements as provided in Rules 20.15, 20.34 and 20.35 of the GEM Listing Rules in effect as at 30 March 2004.

The independent shareholders of the Company have approved the transactions contemplated under the Sale and Purchase Agreement at the EGM convened on 8 June 2004. The Vendor and its associates abstained from voting at the EGM. Meanwhile, the company is waiting for the approval of the PRC relevant authority to complete the transactions.

Details of the above connected transaction are set out in the announcement of the Company on the GEM website published on 31 March 2004.

In addition to the above connected transactions, the Group entered into the following transactions with related parties:

Name of related parties	Nature of transactions	Period ended 30 June 2004 RMB'000	Period ended 30 June 2003 RMB'000
Zhengzhou Gas Group Co., Ltd. (Note (1))	Operating lease of equipment and land and buildings from the related company	1,804	1,270
Zhengzhou Zhengran Gas Equipment Co., Ltd. (Note (2))	Purchase of construction materials from the related company	–	268
Zhengzhou Zhengran Property Management Co., Ltd. (Note (2))	Payment of comprehensive service fee to related company	395	–
Zhengzhou Zhengran Gas Appliances Co., Ltd. (Note (2))	Purchase of construction materials from the related company	297	467
Zhengran Design Development Co., Ltd. (Note (2))	Payment of design fee to related company	428	–
Zhengzhou Gas Group LPG Co., Ltd. (Note (3))	Receiving equipment rentals from related company	140	–

- Zhengzhou Gas Group Co., Ltd. is the holding company of the Company.
- Zhengzhou Zhengran Gas Equipment Co., Ltd., Zhengzhou Zhengran Property Management Co., Ltd., Zhengzhou Zhengran Gas Appliances Co., Ltd., and Zhengran Design Development Co., Ltd. are fellow subsidiaries of the Company.
- Zhengzhou Gas Group LPG Co., Ltd. is an associated company of the Holding Company.

The Directors of the Company, including the independent non-executive Directors, are of the view that the above transactions were conducted based on normal commercial terms and at market prices.

15. COMMITMENTS

	As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
Capital commitments		
Capital commitments in respect of property, plant and equipment:		
– authorised, but not contracted for	19,257	66,761
– contracted, but not provided for	38,152	1,202
	<u>57,409</u>	<u>67,963</u>
Capital commitment in respect of equity investment:		
– authorised but not contracted for	–	10,000
	<u>57,409</u>	<u>77,963</u>

15. COMMITMENTS (continued)

Operating lease commitments

As lessee

At the balance sheet date, the Group had future minimum lease payments under non-cancellable operating leases in respect of equipment and land and buildings falling due as follows:

- Within one year
- In the second to fifth years, inclusive
- Over five years

As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
4,686	5,005
13,766	13,766
32,354	34,697
50,806	53,468

As lessor

At the balance sheet date, the Group had future minimum lease receivables under non-cancellable operating leases in respect of plant and equipment falling due as follows:

- Within one year

As at 30 June 2004 RMB'000	As at 31 December 2003 RMB'000
140	280

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

General

During the 6 months ended 30 June 2004, the Group recorded a total turnover of approximately RMB214,796,000, a gross profit of approximately RMB79,732,000, representing an increase in turnover of approximately 22.72% over the corresponding period of last year, which was primarily attributed to the increase in the number of natural gas users, coupled with the substantial increase in gas consumption by industrial, commercial and vehicular users.

Gross profit margin of the Group for the Relevant Period was 37.12%, which was higher than 33.85% of the corresponding period of last year. It was mainly due to the fact that the proportions of income from gas pipelines construction and gas sales to industrial, commercial and vehicular users, which had higher profit margins, in the total turnover were increased.

During the Relevant Period, administrative expenses amounted to RMB15,282,000, representing a slight increase of 2.16% as compared to RMB14,959,000 for the corresponding period of last year. The Group has implemented stringent cost control since the beginning of 2004 in order to keep administrative expenses at the same level to those at the corresponding period of the previous year. As a result, the increase in the administrative expenses was insignificant.

Income tax expenses of the Group for the Relevant Period were approximately RMB20,325,000. The income tax rate of 33% was in accordance with the relevant tax laws and regulations.

Net profit attributable to shareholders of the Company for the Relevant Period was approximately RMB37,080,000, representing an increase of approximately 31.85% from RMB28,123,000 of the corresponding period of last year.

Sale of piped natural gas

The turnover of piped natural gas for the Relevant Period amounted to approximately RMB130,497,000, representing an increase of approximately 36.76% from RMB95,423,000 over the corresponding period of last year.

During the Relevant Period, total gas consumption by natural gas users of the Group was approximately 88,475,000 m³, representing an increase of approximately 64.57% as compared with approximately 53,762,000 m³ for the corresponding period of last year.

	2004		2003		increase %
	Gas consumption	As a percentage of total gas consumption	Gas consumption	As a percentage of total gas consumption	
Natural Gas					
total gas consumption (approximately '000 m ³)	88,475		53,762		64.57%
including:					
residential users	37,589	42.49%	34,108	63.44%	10.21%
commercial users	21,294	24.07%	15,266	28.40%	39.49%
industrial users	20,312	22.96%	2,038	3.79%	896.66%
vehicular users	9,280	10.49%	2,350	4.37%	294.89%

According to the table above, gas consumption by residential users during the Relevant Period sustained a stable growth with 37,589,000 m³, representing an increase of 10.21% as compared with the corresponding period of last year. Consumption by industrial users maintained its high growth momentum with 20,312,000 m³, representing an increase of 896.66% as compared with the corresponding period of last year. Consumption by commercial users amounted to 21,294,000 m³, representing an increase of 39.49% as compared with the corresponding period of last year. As at 30 June 2004, the Group has 474,578 residential users, representing an increase of 16,907 users as compared with 457,671 users as at 31 December 2003; 842 commercial users representing an increase of 83 users as compared with 759 users as at 31 December 2003, and 23 industrial users representing an increase of 5 users as compared with 18 users as at 31 December 2003.

In respect of the gas powered vehicles business, given the persistently high oil price, vehicle operators were more eager to convert their vehicles into natural gas powered vehicles. Our target to secure additional 1,200 vehicular users in 2004 was overfulfilled in the first half of the year. During the Relevant Period, the Group's natural gas powered vehicular users has been increased by 1,555, and the total number of natural gas powered vehicles converted has reached 3,083 as at 30 June 2004. The gas sale to vehicular users reached 9,280,000 m³, representing an increase of 294.89% as compared with 2,350,000 m³ for the corresponding period of last year. Apparently, the gas powered vehicles business has become the new momentum of the Group's profit growth.

During the Relevant Period, the Group purchased approximately 66,309,300 m³ of natural gas from the "Project of Transmitting Natural Gas through the West to the East Pipelines", at an aggregate cost of RMB69,563,100 based on the after tax cost of RMB1.04907/m³, representing 66.63% of the total volume of natural gas purchased .

To expand its market into Dengfeng City, the Group established a subsidiary, Dengfeng Zhengran Gas Limited (登封鄭燃燃氣有限公司) ("Dengfeng Zhengran"), on 17 February 2004. Its registered capital was RMB10,000,000, and 65% of its registered capital was owned by the Company directly and 35% by the Zhengzhou Gas Engineering and Construction Company Limited, a non-wholly owned subsidiary of the Company. The Group believes that the establishment of Dengfeng Zhengran would have a positive impact on its market development in Dengfeng City and by fostering its experience on market development outside Zhengzhou, the Group's momentum of growth could be remarkable. During the Relevant Period, Dengfeng Zhengran has completed part of the pipeline construction works, but has not yet commenced gas supply to users in Dengfeng City.

Natural gas pipeline construction services

For the Relevant Period, the Group's turnover in natural gas pipeline construction services amounted to approximately RMB68,598,000, representing a growth of 34.85% as compared with RMB50,869,000 for the corresponding period of last year and this was mainly attributable to the satisfactory growth in the natural gas pipeline construction projects for residential users.

In addition, the Group also collects fees from users for providing repair and maintenance services to gas pipelines. During the Relevant Period, such fees were approximately RMB14,490,000, representing a drop of 2.09% as compared with RMB14,799,000 for the corresponding period of last year. The drop was mainly due to a decrease in pipeline replacement projects, which resulted in a reduction in such fees received from users.

Net profit and shareholders' return

Net profit margin of the Group for the Relevant Period was 17.26%, representing an increase from 16.07% of the corresponding period of last year. Such increase in net profit margin was primarily attributed to the increase in gross profit margin and effective control over administrative costs.

In addition, average returns to shareholders for the Relevant Period, based on the profit attributable to shareholders divided by the average of shareholders' equity at the beginning and at the end of the period, was 11.32% ,which was higher than that of 9.97% of the corresponding period of last year. Its main reason was that the profit growth rate and net profit margin were higher than those of the corresponding period of last year.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

Borrowings and banking facilities

The Group relies on cash generated from its internal operation, net proceeds from the placing of H Shares and bank balances or cash in hand to meet its requirements of capital expenditure and operations. The Directors are of the view that, in the long run, the Group will generate liquidity from its business operation and may consider making use of further equity finances or bank loans when necessary.

As at 30 June 2004, the Group had no outstanding interest-bearing bank borrowings.

As at 30 June 2004, the Group had outstanding loans of RMB22,433,000 due to the Holding Company, details of which are set out in note 11 to financial statements.

Net current liabilities

As at 30 June 2004, the Group had net current liabilities of approximately RMB902,000 (31 December 2003: net current assets of approximately RMB8,013,000). Although the Group recorded a net current liability, there was a deferred income of approximately RMB89,956,000 in the current liabilities, which was an unrecognized income from pipeline network project, not an amount payable as a liability in nature. The Group had net current assets of approximately RMB89,054,000 after deducting such deferred income.

Working capital

As at 30 June 2004, the Group had no outstanding bank borrowings and had cash and bank balances of approximately RMB98,547,000. The Directors are of the view that the Group has sufficient working capital to meet its present requirements.

Capital to liabilities ratio

As at 30 June 2004, capital to liabilities ratio (being share capital over total liabilities and expressed in percentage) of the Group was approximately 205.33% which was higher than that of approximately 183.14% as at 31 December 2003. The reason for a higher capital to liabilities ratio is that the repayment of RMB10,000,000 to the holding company of the Company further reduced the liabilities of the Company. The current liabilities level of the Group indicated that, with over half of the assets being financed by its shareholders, the Group had ample room for external borrowings.

Contingent liability and pledged assets

As at 30 June 2004, the Group had no significant contingent liability or any asset under pledge.

Employees and remuneration policy

There is no significant change in the Group's employees and remuneration policy compared to that disclosed in the annual report for the year ended 31 December 2003.

Foreign currency risk

All of the Group's businesses are operated in the PRC and all its transactions are settled in Renminbi. Therefore the Group's exposure to foreign currency risk is minimal.

Future Prospects

(i) Business

In 2004, the Group will, on the basis of developing the market of residential users, further explore the market with a focus on industrial and commercial users. With a stronger emphasis on environmental protection in Zhengzhou, coal furnace under 10 tons will be prohibited by 2006 and the coal combustion-free zone will be further expanded. Both measures provide a golden opportunity to the Group for further exploring the market of commercial users. In addition, to maintain a mutual prosperous development of commercial and industrial activities in Zhengzhou, the local government of Zhengzhou promulgated certain preferential policies to encourage industrial investments and it is believed that such policies shall further propel the Group's development in the market of industrial users. Meanwhile, both the setting up of Zhengzhou new city and the enlargement of the scale of urbanization shall act as a catalyst for the Group's development of residential market and the Group expected the growth in the number of residential users can reach 30,000 by the year of 2004.

In addition, on 14 June 2004, Henan Province Development and Reform Committee promulgated a new policy to compel the use of natural gas in areas now using coal gas ("the Conversion"). This policy will help the Company to extend its customer base of natural gas and lead to an eventual increase in the sales of the Group's natural gas. According to the estimation of the Board based on the information provided by the only state-owned supplier of coal gas in Zhengzhou, approximately 6,400 residential users and 30 industrial and commercial users of coal gas, will become users of natural gas of the Company (monopolized supplier of natural gas in Zhengzhou authorized by Zhengzhou Municipal Government). The Conversion process including the conversion of gas appliances and equipment is expected to be completed by the end of 2004. It is not sure whether the Company will incur capital expenditure as a result of the Conversion. If necessary, the Company will make further announcement in relation to the required capital expenditure according to the GEM Listing Rules.

In respect of the vehicular gas business, the Group planned to build another two natural gas refueling station to further improve the vehicular gas supply network. In addition, the Group will increase the price of vehicular gas from RMB1.9/m³ to RMB2.1/m³ from 1 July 2004. The vehicular gas business is expected to generate a higher return for the Group after such price increase.

In addition to the abovementioned markets, the Group is currently undertaking studies to expand the application of natural gas to air-conditioning, heating and power generation in order to further expand the development potential of the Group.

(ii) Introduction of strategic investors

On 1 June 2004, Zhengzhou Gas Group Co., Ltd. (the Group's holding company) entered into the framework agreement with China Resources Petrochems (Group) Company Limited ("China Resources Petrochems") (a subsidiary of China Resources Enterprise, Limited), pursuant to which, Zhengzhou Gas Group Co., Ltd., in principle, agreed to sell 250,300,000 Domestic Shares of the Company, representing 20% of the Company's total issued share capital to China Resources Petrochems. Up to 30 June 2004, the parties concerned were negotiating the specific terms, including the amount and payment method of the consideration, and no concrete terms have been concluded. In the opinion of the Board, should the equity investment by China Resources Petrochems be finalized, it would bring substantial benefits to the Group in many aspects, such as introduction of advanced management system, improvement of operation efficiency and expansion of development scopes.

COMPARISONS OF BUSINESS OBJECTIVES WITH ACTUAL BUSINESS PROGRESS

	Business objectives for the period from 1 January 2004 to 30 June 2004	Actual progress
Piped natural gas (in '0,000 m³)		
– Residential users	3,100	3,759
– Commercial/industrial users	4,100	4,160
Number of meters installed (units)		
– Residential users	15,000	17,433
– Commercial/industrial users	120	88
New vehicular gas users (cars)	1,250	1,555
LPG (tonnes) (Note 1)		
– Retail	4,300	0
– Wholesale	20,000	0
Urban pipelines network constructed (km)		
– Main pipelines	15	6.2
– Branch pipelines	20	19
Geographical distribution of sales of natural gas pipelines	Zhengzhou City	Zhengzhou City
Operation facilities		
Newly built vehicular refueling stations (number)	3	Land requisition contracts have been entered into in respect of two refueling stations (being Dongming Road Station and Daxue South Road Station) Currently, the relevant construction approval procedures is being processed with Government Authorities and it is expected that construction works will commence in the second half of this year. Furthermore, in the first half of this year, expansion works of different extent have been made to all existing refueling stations.
Invest HK\$12,000,000 in the natural gas pipelines network cathode protection project, the distant testing and signal project and the natural gas pipelines network geographical information system in order to upgrade the management standard of the pipelines networks (Note 2)	RMB6,360,000	RMB530,000

Notes:

- In the second quarter of 2003, the Company has by stages closed down the LPG operations.
- In the first half of 2004, RMB6,360,000 was planned for investment in the cathode protection system, distant monitoring and signaling system and geographical information system, of which only RMB530,000 was used in the development of geographical information system. In March 2004, the Company entered into a sale and purchase contract with Zhengzhou Gas Group Co., Ltd to purchase the cathode protection system and distant monitoring and signaling system. However, the transaction is still pending for approval by the relevant PRC government authority. The fund planned for such investment remains unused.

USE OF PROCEEDS FROM THE INITIAL PUBLIC OFFERING

New shares issued by the Company were listed on GEM on 29 October 2002 (the "Listing Date"). Net proceeds from the sale of 50,060,000 Sale H Shares after deducting relevant issue expenses amounted to approximately RMB118,897,000.

During the six months ended 30 June 2004, net proceeds from the public listing were used in accordance with application plans set out in the prospectus dated 22 October 2002 (the "Prospectus") as follows:

	Six months ended 30 June 2004	
	Application of proceeds as planned in the Prospectus RMB million	Actual application of proceeds RMB million
Ancillary works for the "West to East Pipelines" project (Note 1)	5.30*	0
Construction and renovation of urban pipeline networks (Note 2)	4.24	4.24
Expansion of sales network and sales and marketing team (Note 3)	0.53	0
Upgrading of management efficiency of pipeline networks (Note 4)	6.36	0.53
Development of vehicular gas business (Note 5)	4.77	3.41
Total	<u>21.20</u>	<u>8.18</u>

Notes:

1. Proceeds from the public listing of approximately RMB5,300,000 planned to be used in the first half of 2004 in ancillary works for the "West to East Pipelines" project is to be used in the construction of high-pressure transmission pipelines in Fourth Ring Road (四環路). Since the project is delayed, so the fund planned for such investment remains unused. It is expected that the project may commence in July 2004. The Group has no intention to change the usage of such funds.
2. Proceeds from the public listing planned to be used in the first half of 2004 for the construction and renovation of urban pipeline networks are to be used mainly in the construction of pipelines of Huancheng Road (環城路). Accumulated investment in the pipelines Huancheng Road amounts to approximately RMB6,620,000, of which, approximately RMB4,240,000 is funded by the proceeds from initial public offering, the balance of approximately RMB2,380,000 is financed by the funds generated from operations.
3. Proceeds from the public listing to be used for the expansion of the sales network and sales and marketing team are used mainly in the construction of sales centre at Mianfang East Road (棉紡東路). The total investment in this centre was approximately RMB4,311,900, of which approximately RMB2,120,000 was funded by the proceeds from the public listing and the balance was financed by internal funds. Since the completion of the sales centre was ahead of schedule, the proceeds from the public listing planned to be used in 2004 for the expansion of the sales network and sales and marketing team was fully utilized in 2003.
4. Proceeds from the public listing planned to be used in the first half of 2004 for upgrading the efficiency of pipeline networks are to be used in the purchase of the cathode protection system, the distant monitoring and signaling system and development of geographical information system. In March 2004, the Company entered into sale and purchase contracts with Zhengzhou Gas Group Co., Ltd to purchase the cathode protection system and the distant monitoring and signaling system. And completion of the transaction is subject to the approval by the relevant PRC government authorities. As such, out of the proceeds from the public listing planned to be used in the first half of 2004 in upgrading of the efficiency of pipeline networks, only RMB530,000 was used in the development of the geographical information system.
5. Proceeds from the public listing planned to be used for in the first half of 2004 for the development of vehicular gas business are mainly used for the expansion of existing refueling stations.

Proceeds not yet utilized, amounting to approximately RMB25,970,000, were placed with commercial banks in the PRC, and will be applied in the future in accordance with the Group's business objectives described in the Prospectus.

* The exchange rate used throughout this section is fixed at RMB1.06 = HK\$1.00.

FURTHER INFORMATION

Directors', Chief Executives' and Supervisors' Interests in Shares

As at 30 June 2004, the interests and short positions of the Directors, chief executives and supervisors of the Company in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which are required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) pursuant to the "Model Code for Securities Transactions by Directors of Listed Companies" to be notified to the Company and the Stock Exchange were as follows:

Long positions in shares of the Company

Director/ Supervisor	Capacity/ Nature of interests	Number of Domestic Shares held	Approximate % of beneficial interests in Domestic Shares	Approximate % in total registered share capital of the Company
Gao Mingshun	Corporate (Note 1)	15,400,000	2.20%	1.23%
Li Keqing	Corporate (Note 2)	115,500,000	16.48%	9.23%

Notes:

- As at 30 June 2004, Gao Mingshun was interested in 15,400,000 Domestic Shares as a result of him being interested in 95.71% of the registered capital of Zhengzhou Sifang Construction and Decoration Co., Ltd. which holds approximately 1.23% (out of the total registered share capital) and 2.20% (out of Domestic Shares) of the registered share capital of the Company.
- As at 30 June 2004, Li Keqing was interested in 115,500,000 Domestic Shares as a result of him and his spouse, Guo Wenjun, being in aggregate interested in 40% of the registered capital of Zhengzhou Qiyuan Investment Consultancy Company Limited, which holds approximately 9.23% (out of the total registered share capital) and 16.48% (out of Domestic Shares) of the registered share capital of the Company.

Save as disclosed in this paragraph, as at 30 June 2004, none of the Directors, chief executives or supervisors of the Company or their respective associates had interest and short positions in any securities of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which are required (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) pursuant to the "Model Code for Securities Transactions by Directors of Listed Companies" relating to securities transactions by directors to be notified to the Company and the Stock Exchange.

Disclosures under the SFO and Substantial Shareholders

So far as was known to any Director or supervisor of the Company, as at 30 June 2004, the persons or companies (not being a Director, chief executive or supervisor of the Company) who had equity interests or short positions in the shares or underlying shares of the Company which would be required to be disclosed under Divisions 2 and 3 of Part XV of the SFO, or who were directly or indirectly deemed to be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group (other than the Company) were as follows:

Long positions in shares of the Company

Name	Number of H Shares held	Approximate % of beneficial interests in H Shares	Number of Domestic Shares held	Approximate % of beneficial interests in Domestic Shares	Approximate % in total registered capital share of the Company
Zhengzhou Gas Group Co., Ltd			540,415,098	77.11%	43.18%
Zhengzhou Qiyuan Investment Consultancy Company Limited (Note 1)			115,500,000	16.48%	9.23%
Guo Wenjun (Note 2)			115,500,000	16.48%	9.23%
Partners Capital International Limited (Note 3)	29,400,000	5.34%			2.35%

Name of subsidiary of the Company	Name of shareholder	Amount of registered capital of the subsidiary	Approximate percentage of shareholding of the subsidiary
Zhengzhou Gas Engineering and Construction Company Limited (鄭州燃氣工程建設有限公司)	Zhengzhou Gas Group Labour Union Committee (鄭州燃氣集團工會委員會)	RMB6,600,000	16.50%
Dengfeng Zhengran Gas Limited (登封鄭燃燃氣有限公司)	Zhengzhou Gas Engineering and Construction Company Limited (鄭州燃氣工程建設有限公司)	RMB3,500,000	35.00%

Notes:

- Zhengzhou Qiyuan Investment Consultancy Company Limited ("Zhengzhou Qiyuan") holds 115,500,000 Domestic Shares of the Company, representing approximately 16.48% of the beneficial interests in Domestic Shares. However, pursuant to the GEM Listing Rules, Zhengzhou Qiyuan was not a substantial shareholder of the Company because the Domestic Shares held by Zhengzhou Qiyuan represented only 9.23% of the total registered share capital of the Company.
- As at 30 June 2004, Guo Wenjun was interested in 115,500,000 Domestic Shares of the Company as Guo Wenjun and her spouse, Li Keqing were in aggregate interested in 40% of the registered capital of Zhengzhou Qiyuan, which was interested in 115,500,000 Domestic Shares or approximately 16.48% of the beneficial interests in the Domestic Shares of the Company. However, pursuant to the GEM Listing Rules, Guo Wenjun was not a substantial shareholder of the Company because the Domestic Shares held by Guo Wenjun represented only 9.23% of the total registered share capital of the Company.
- Partners Capital International Limited ("Partners Capital") was a financial adviser to the Company. Pursuant to the GEM Listing Rules, Partners Capital was not a substantial shareholder of the Company because the H Shares held by Partners Capital represented only 2.35% of the total registered share capital of the Company.

Save as disclosed above, as at 30 June 2004, the Directors were not aware of any other person who had an interest or short position in the Shares or underlying Shares which would be required to be disclosed under Divisions 2 and 3 of Part XV of the SFO, or who was interested in 10% or more of the nominal value of any class of share capital, or options or debenture in respect of such capital, carrying right to vote in all circumstances at general meetings of any member of the Company.

Directors', Chief Executives' and Supervisors' Interests in the Underlying Shares pursuant to Equity Derivatives

Save as disclosed above, during the six months ended 30 June 2004, none of the Directors, chief executives or supervisors of the Company was granted options to subscribe for H shares of the Company. As at 30 June 2004, none of the Directors, chief executives or supervisors of the Company nor their spouses or children under the age of 18 had any right to acquire H shares in the Company or had exercised any such right during the period.

Sponsor's Interests

As at 30 June 2004, neither South China Capital Limited (the "Sponsor"), nor any of its directors or employees or associates, had any interests in the securities of the Company or any member of the Group or any rights to subscribe for or to nominate persons to subscribe for the securities of the Company or any members to the Group.

Pursuant to the sponsor agreement dated 21 October 2002 (the "Sponsor Agreement") entered into between the Company and the Sponsor, the Sponsor has agreed to act as a sponsor to the Company for the purpose of the GEM Listing Rules for a fee from the date on which dealings in the H Shares on GEM commenced (i.e., 29 October 2002) to 31 December 2004 or until the Sponsor Agreement is terminated upon the terms and conditions set out therein.

Purchase, Sale or Redemption of Securities

Neither the Company, nor its subsidiaries purchased, sold or redeemed any of the Company's listed securities during the period from 29 October 2002 (i.e. the date on which the H Shares were listed on GEM) to 30 June 2004.

Audit Committee

The Company established an audit committee on 31 March 2002 with terms of reference in compliance with Rules 5.23 and 5.24 of the GEM Listing Rules. The primary functions of the audit committee are to review the financial reporting process and the internal control systems of the Group. The audit committee comprises three members, namely Ms. Yu Shulian and Mr. Zhang Yichun, both being independent non-executive directors of the Company, and Mr. Zhang Chaoyi, a non-executive director. Ms. Yu Shulian is the chairperson of the audit committee.

During the Relevant Period, the audit committee held two meetings and reviewed this interim report.

Code of Conduct regarding Securities Transactions by Directors

During the six months ended 30 June 2004, the Company had adopted a code of conduct regarding securities transactions by directors on terms no less exacting than the required standard of dealings set out in the GEM Listing Rules. The Company, having made specific enquiry of all Directors, is not aware of any non-compliance by any of the Directors with the required standard of dealings and the Company's code of conduct regarding securities transactions by the Directors.

Competing Interests

Zhengzhou Gas Group Co., Ltd., being the controlling shareholder and initial management shareholder of the Company, through its interest of 48% of the registered capital in Zhengzhou Gas Group LPG Co., Ltd. ("Zhengzhou LPG"), is engaged in the sales of bottled LPG in Zhengzhou. As both of the business of Zhengzhou LPG of selling bottled LPG in Zhengzhou and the Company's business of selling pipeline natural gas involve the provision of fuel to customers, such businesses therefore constitute competing interests.

Save as disclosed above, none of the Directors, the initial management shareholders of the Company or their respective associates (as defined in the GEM Listing Rules) had any interests in a business which competes or is likely to compete, either directly or indirectly, with the business of the Group.

Board Practices and Procedures

In the opinion of the Directors, the Company has complied with the requirements of board practices and procedures of Rules 5.34 to 5.45 of the GEM Listing Rules throughout the accounting period covered by this interim report.

Directors and Supervisors

The members of the Board include (i) the executive Directors, Mr. Yan Guoqi (閔國起) (Chairman), Mr. Song Jinhui (宋金會) and Ms. Niu Minghua (牛鳴華); (ii) the non-executive Directors, Mr. Chang Zongxian (常宗賢), Mr. Wang Yuheng (王玉珩), Mr. Zhang Wushan (張武山), Mr. Li Keqing (李克清), Mr. Zhang Chaoyi (張超義), and Mr. Li Zhenguo (李振國); and (iii) the independent non-executive Directors, Mr. Zhang Yichun (張亦春), Mr. Liu Jianwen (劉劍文), and Ms. Yu Shulian (余恕蓮). The supervisors of the Company are Ms. Yang Qing (楊清), Mr. Ding Ping (丁平), Ms. Zhou Weihua (周衛華), Mr. Gao Mingshun (高明順), and Ms. Wang Xiaoxing (王小興).

By Order of the Board
Zhengzhou Gas Company Limited*
Yan Guoqi
Chairman

11 August 2004

Zhengzhou, the PRC

* For identification purpose only