

## MANAGEMENT DISCUSSION AND ANALYSIS

### OPERATION REVIEW

The Board of Directors of Shenzhen Expressway Company Limited (the “Company”) are pleased to announce the unaudited interim results of the Company and its subsidiaries (collectively the “Group”) for the six months ended 30 June, 2001 (the “Period”), prepared in accordance with the accounting principles in Hong Kong. During the Period, the Group has achieved a turnover of RMB219.7 million from toll road operations, with an increase of 5.33% as compared with the corresponding period of 2000. Profit attributable to shareholders amounted to RMB203.6 million, representing a growth of 17.61% over the same period of 2000. Earnings per share for the Period are RMB0.101, representing an increase of 17.58% over the same period of 2000.

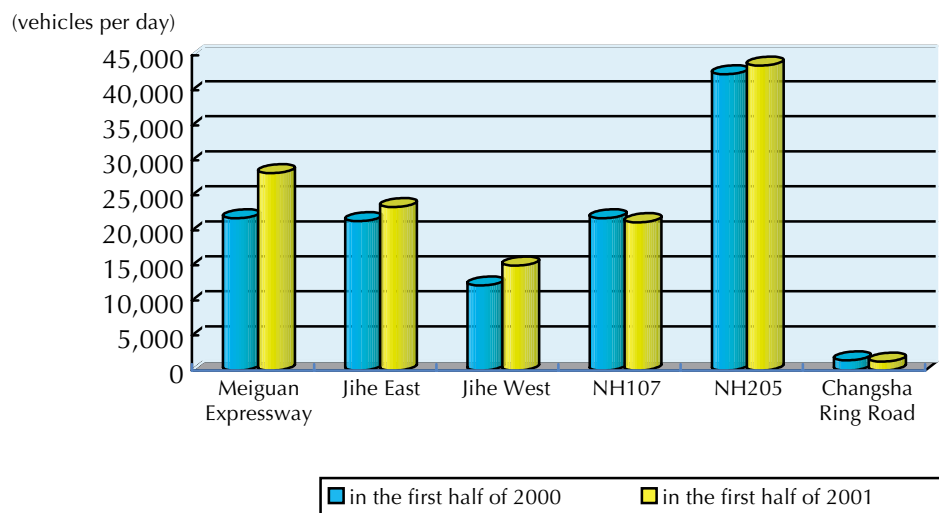
#### Business summary

The Company is mainly engaged in the development, operation and management of toll highways and expressways in the PRC. Currently, it owns five expressways and two national highways, namely Shenzhen Meiguan Expressway (“Meiguan Expressway”), Shenzhen Airport-Heao Expressway (Eastern Section) (“Jihe East”), Shenzhen Airport-Heao Expressway (“Western Section”) (“Jihe West”), Section A of Yanba Expressway (“Yanba A”), Changsha Ring Road (Northwestern Section) (“Changsha Ring Road”), National Highway 107 (Shenzhen Section) (“NH107”) and National Highway 205 (Shenzhen Section) (“NH205”). The operating results of the above toll roads during the Period are set out as follows:

| Toll roads         | Average daily mixed traffic volume |                        | Change (%) | Toll revenue RMB'000   |                        | Change (%) |
|--------------------|------------------------------------|------------------------|------------|------------------------|------------------------|------------|
|                    | The first half of 2001             | The first half of 2000 |            | The first half of 2001 | The first half of 2000 |            |
|                    | Meiguan Expressway                 | <b>28,177</b>          |            | 21,707                 | 29.81                  |            |
| Jihe East          | <b>23,331</b>                      | 21,296                 | 9.56       | <b>71,780</b>          | 64,540                 | 11.22      |
| Jihe West          | <b>14,975</b>                      | 12,128                 | 23.47      | <b>48,370</b>          | 40,260                 | 20.14      |
| Changsha Ring Road | <b>1,239</b>                       | 1,426                  | -13.11     | <b>3,060</b>           | 3,510                  | -12.82     |
| Yanba A            | <b>2,546</b>                       | —                      | N/A        | <b>2,650</b>           | —                      | N/A        |
| NH107              | <b>21,151</b>                      | 21,729                 | -2.66      | <b>37,670</b>          | 42,170                 | -10.67     |
| NH205              | <b>43,511</b>                      | 42,290                 | 2.89       | <b>70,790</b>          | 79,430                 | -10.88     |



### ***The traffic volume of each toll road for the six months ended 30 June (2001 VS 2000)***



Note: Yanba A commenced operation in April, 2001. The traffic volume of Yanba A is not included in the above chart.

### **Business Analysis**

In the first half of 2001, the Gross Domestic Product (“GDP”) of the PRC grew by 7.9%. Shenzhen’s economic development continues to outperform other cities in the PRC, with a GDP growth of 12.5%. Domestic demands were further expanded. Though affected by the slowed global economic growth and the slowdown of Guangdong’s imports and exports, the operation of toll roads of the Group has provided steadily increasing cash flow for the Group during the Period, which has laid a solid foundation for the fulfillment of the targets and future development of the Group.

### ***The traffic volume and toll revenue of expressways continue to grow***

The Group focuses on the development, construction and operation of expressways. During the Period, the expressways operated by the Group grew at a fast pace, which have become the main sources of the Group’s growth. Meiguan Expressway and Jihe Expressway have become the main drivers of the Company’s continuous profit growth, and they will continue to play important roles in the Company’s future development.

Since the completion of Guanshen Expressway in October 2000, which connects with Meiguan Expressway, the traffic volume and toll revenue of Meiguan Expressway has entered a new stage of growth. The opening of Huawei Toll Plaza in April, 2001 and the effective control of traffic distraction at Minle Interchange were attributable to the continuous growth of toll revenue of Meiguan Expressway in the first half of 2001. The collapse of a bridge within the nearby road network caused by typhoons and heavy rains in June this year has led much traffic to Meiguan Expressway, which contributed to the even higher toll revenue growth of Meiguan Expressway. Though the toll revenue growth of Jihe East had slowed after a high growth of 35% in 2000, it still recorded a growth of 11.2% in the first half of 2001. Jihe West witnessed remarkable growth in traffic volume, with its toll revenue increasing by 20.1%.

***The passage conditions of national highways improved, and toll revenue of national highways restored***

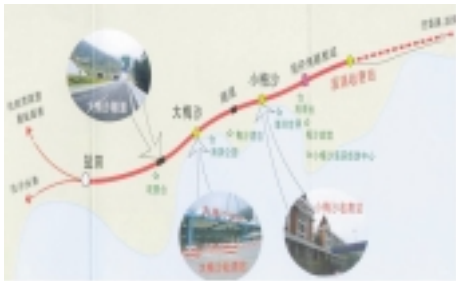
During the Period, the Company improved the passage conditions and reduced toll payment time through the installation of non-stop toll collection systems in two national highways. The toll revenue of the two national highways was maintained at steady level through strengthening the control of traffic distraction at certain sections of the highways. The decline of toll revenue of NH205 has slowed, and it is expected that there will be a slight decrease in the annual toll revenue of NH205 in 2001 as compared with 2000. The average daily toll revenue of NH107 has restored to the same level as that of the same period of 2000. NH107 is expected to record a slight increase in the annual toll revenue in 2001 as compared with that of 2000.



***Unsatisfactory performance of Changsha Ring Road and the newly opened Yanba Expressway (Section A)***

Owing to the non-completion of the surrounding road network and the unopening of two toll plazas, the traffic volume and toll revenue of Changsha Ring Road are still at a low level.

Section A of Yanba Expressway commenced toll collection on 16 April, 2001, and the whole section of Yanba A was opened on 1 June, 2001. Because it is the first operational section of Yanba Expressway, and that large vehicles constitute a minor proportion in the total traffic volume due to its short length and the non-completion of road network, the toll revenue of Section A of Yanba Expressway is at a low level. Average daily toll revenue for the first half of 2001 is RMB34,500, and the toll revenue for the Period amounted to RMB2,650,000. It is expected that average daily toll revenue of Section A of Yanba Expressway will increase in the second half of 2001.



**PLANNING AND PROSPECTS**

China's imminent accession to the World Trade Organization will further boost the economic development of China. Trade activities will become more and more active, and imports and exports will grow at an even higher rate. That will in turn pose a pressing demand for highway transportation. Since January 2001, Shenzhen's vehicles has increased by 15%, and its private cars has increased by thousands on monthly basis. Shenzhen has approximately 500,000 vehicles, out of which 350,000 vehicles, 150,000 vehicles and 30,000 vehicles are registered vehicles, non-local vehicles and cross-boarder vehicles, respectively. Shenzhen tops other cities in vehicle ownership in the PRC. The above has provided a steady demand for the toll road operation of the Company. The Company will further strengthen its management and consolidate its foundation for the future growth of its revenue.

***To further enhance corporate governance, and to establish the development strategy of the Company***

The Board of Directors have approved *The Regulation of the Board of Directors, The Regulation of the General Manager and Views on How to Promote the Competitiveness of the Company*. They are reviewing the Company's development strategy, in order to promptly establish the Company's medium and long-term development strategies and to ensure its continuous development in the long run.

***To promote operating capacity through active marketing, tight control of costs and promotion of non-stop toll collection systems***

The Company will continue to adhere to its strict cost control policy and adopt various marketing measures to attract traffic and control distraction, so as to increase its toll revenue. It will develop and install non-stop toll collection systems on expressways so to simplify toll collection procedures and to enhance their operating capacity .

***To expand operation of expressways in Shenzhen***

By capitalizing various opportunities and making full use of the first right of refusal to develop expressways in Shenzhen pursuant to the Concession Agreement entered into between the Company and Shenzhen Municipal Government and given Shenzhen's unique economic environment as a special economic zone and its adjacency to Hong Kong, the Company will further expand its core business of expressway operation in Shenzhen.

***To actively develop other business***

While perfecting and expanding its toll road operation, the Company will select one to two fields to invest at an appropriate time, so as to reduce risks and to broaden the profit base of the Company.

***To set up scientific evaluation and incentive systems at all levels***

After the Company appointed a foreign consulting firm to diagnose the Company's management, it appointed a professional consulting firm to conduct the position analysis with a view to establishing a set of strict and scientific evaluation systems and perfecting relevant incentive systems.

***To complete the issue and listing of A Shares in the PRC***

After having obtained the preliminary approval by China Securities Regulatory Commission, the Company is expected to complete the issue of a maximum 180,000,000 Renminbi-denominated ordinary shares (A Shares) and the listing of such A Shares on the Shanghai Stock Exchange in the second half of this year.



## MAJOR INVESTMENTS AND FINANCING

The major investment of the Company, Section A of Yanba Expressway commenced operation on 16 April, 2001. It is 9.65km long, running from Yantian to Xicong, with dual-three lanes and three toll plazas. The Company is settling the payments of the construction costs of the project. The total investment of the project is estimated to be approximately RMB800 million, RMB300 million out of which comes from the financial assistance of Shenzhen Municipal Government.

The major investment approved by the Board of Directors of the Company is the construction of Sections B and C of Yanba Expressway. Section B of Yanba Expressway will run from Xicong to Kuaicong, with a length of 9.19km. Section C of Yanba Expressway will start from Kuaicong to Bagang, with a length of 10.08km. Sections B and C of Yanba Expressway will be funded by the proceeds raised through the issue of Renminbi-denominated ordinary shares (A Shares) in the PRC. The Company is conducting the feasibility studies of Yantian—Paibang Expressway (“Yanpai Expressway”) and other planned expressways in Shenzhen. If the above projects are approved by relevant authorities, the Company will raise funds through bank loans, capital financing, issue of convertible bonds and financial assistance. The Company does not have any plans for capital financing or issue of convertible bonds within this year, apart from the proposed A Share issue in the PRC.



## FINANCIAL RESULTS AND FINANCIAL POSITION

### Operation results

During the Period, the financial position of the Group remained sound, and its business grew continuously and steadily.

|  | For the six months ended 30 June |                 | Change<br>(%) |
|--|----------------------------------|-----------------|---------------|
|  | 2001<br>RMB'000                  | 2000<br>RMB'000 |               |
| Turnover   | 219,700                          | 208,585         | 5.33          |
| Other revenue  | 38,838                           | 15,746          | 146.65        |
| Total operation costs  | 64,541                           | 59,065          | 9.27          |
| Operating profits  | 193,997                          | 165,266         | 17.38         |
| Share of results before taxation<br>of jointly controlled entities | 29,646                           | 29,503          | 0.48          |
| Finance costs  | 18,483                           | 20,512          | -9.89         |
| Profit attributable to shareholders                                | 203,596                          | 173,107         | 17.61         |

#### 1. Turnover

|                                  | For the six months ended 30 June |                 | Change<br>(%) |
|----------------------------------|----------------------------------|-----------------|---------------|
|                                  | 2001<br>RMB'000                  | 2000<br>RMB'000 |               |
| Income from toll roads           | 231,754                          | 215,147         | 7.72          |
| Less: business tax and surcharge | 12,054                           | 6,562           | 83.69         |
| Turnover                         | 219,700                          | 208,585         | 5.33          |

Turnover comprises turnover from wholly-owned toll roads, namely National Highway 107 (Shenzhen Section), National Highway 205 (Shenzhen Section), Jihe Expressway (Western Section), Yanba Expressway (Section A) and the 95% directly held Meiguan Expressway.

The Group recorded relatively great change in turnover as compared with the same period of 2000, mainly because RMB4,630,000 of business tax for the fourth quarter of 1999 was refunded in the first half of 2000, though business tax refund treatment was terminated with effective from 2000. Turnover for the Period grew by 10.16% after excluding incompatible factors such as the business tax refund and the unified charge fee (統繳費) for two national highways were collected in the first quarter of 2000.

## 2. Other revenue

| Items  | For the six months ended 30 June |                 | Change<br>(%) |
|--|----------------------------------|-----------------|---------------|
|  | 2001<br>RMB'000                  | 2000<br>RMB'000 |               |
| Gains from project management                | 13,500                           | —               | N/A           |
| Gains from investments on bonds              | 10,624                           | 1,948           | 445.38        |
| Net interest income from<br>a long-term loan | 9,607                            | 9,660           | 0.55          |
| Other income                                 | 5,107                            | 4,138           | 23.42         |
| Total  | 38,838                           | 15,746          | 146.65        |

The Company manages the linkage project from Yantian Ports Section along Shenzhen Eastern Highway to Yanba Expressway, which is developed and owned by Shenzhen Municipal Government. Phase I of the project was completed, and Phase II is expected to be completed in September, 2001. Realised gains from management of the project amounted to RMB13.50 million (excluding related business taxes), which increases the Company's profit for the Period.

Gains from investments on government bonds and other bonds for the Period totaled RMB10,624,000, with an increase of RMB8,676,000 over the same period of 2000. During the Period, RMB3,489,000 from the gains from bonds investment was realised, while the remaining RMB7,135,000 was unrealised.

Net interest income from a long-term loan represents the interest charged at a yearly rate of 6.21% by the Company on the long-term loan of RMB306,000,000 advanced to Changsha Ring Road Construction and Development Co., Ltd., the joint venture partner of Changsha Shenchang Expressway Company Limited ("Shenchang"). The interest receivable has been fully received, which makes up for the relatively low return from the early operation of Shenchang. The loan will be treated as advance made by the Company to Shenchang when due in 2007.

## 3. Finance costs

During the Period, finance costs was down by 9.89% as compared to the corresponding period of 2000, mainly due to the reduction of loan interest rates. Most of the Company's loans were granted with the preferential loan interest rates which are 10% lower than the respective prime rates.

## Financial Position

### 1. Liquidity

|  | At 30 June, 2001 | At 31 December, 2000 |
|--|------------------|----------------------|
| Proportion of cash and cash equivalents to current assets      | 97.45%           | 94.30%               |
| Proportion of cash and cash equivalents to current liabilities | 1.14             | 2.15                 |
| Current ratio  | 1.17             | 2.28                 |
| Quick ratio  | 1.16             | 2.26                 |

Current assets mainly comprise cash and cash equivalents, with good liquidity. The current ratio and the quick ratio comfortably stand at 1.17 and 1.16 respectively. The repayment ability of the Company remains strong.

### 2. Financial resources

Financial resources of the Group include bank loans, share capital, retained earnings and government assistance.

As at 30 June, 2001, the Group's borrowings amounted to RMB890 million. A short-term loan of RMB150 million was repaid when due, and an aggregate of RMB50 million long-term loan was repaid before due. During the Period, the Group's short-term loans and long-term loans were increased by RMB240 million and RMB100 million, respectively. The Group's borrowings are mainly used to finance project constructions.

As at 30 June, 2001, the Group was granted with an aggregate of RMB2.15 billion banking facilities, of which RMB1.9 billion is secured while the rest RMB250 million is unsecured. The Group has utilized altogether RMB890 million banking facilities, with the remaining RMB1.26 billion banking facilities for standby purpose.

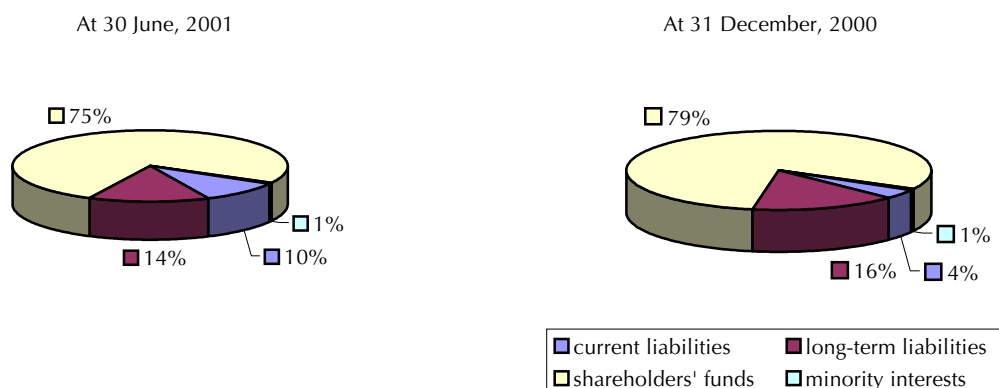
To ensure a reasonable return for the Company's investment in Yanba Expressway, Shenzhen Municipal Government has agreed to provide financial assistance of RMB300 million to the Company for the construction of Section A of Yanba Expressway, of which RMB290 million has been received by the Company and the other RMB10 million will be available in the second half of 2001. Shenzhen Municipal Government has also agreed to provide financial assistance of RMB150 million for the construction of Section B of Yanba Expressway which is expected to commence construction in the second half of 2001.

The Company had a total capital commitment of RMB1.139 billion for the construction of Yanba Expressway, which will be funded through the proceeds of RMB900 from the proposed A Share issue and the financial assistance of RMB150 million from Shenzhen Municipal Government as mentioned above.



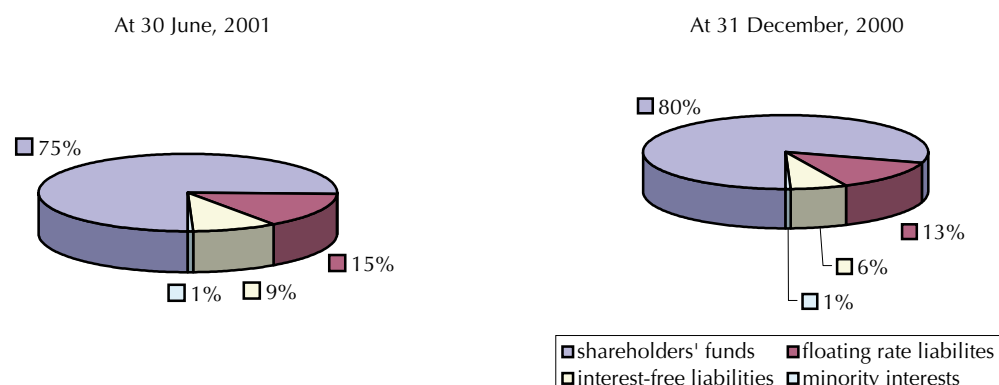
### 3. Capital structure

The capital structure of the Group classified in respect of liquidity is set out below:



The Company's solid capital structure is in conformity with the specific feature of toll road sector, i.e., substantial amount of investments with a long period of recovery.

The capital structure classified in respect of capital costs is set out as follows:



|                           | At 30 June, 2001  |                   | At 31 December, 2000 |                   |
|---------------------------|-------------------|-------------------|----------------------|-------------------|
|                           | Amount<br>RMB'000 | Percentage<br>(%) | Amount<br>RMB'000    | Percentage<br>(%) |
| Shareholders' funds       | 4,541,524         | 75.42             | 4,539,498            | 79.81             |
| Floating rate liabilities | 890,000           | 14.78             | 750,000              | 13.19             |
| Interest-free liabilities | 555,110           | 9.22              | 363,123              | 6.38              |
| Minority interests        | 34,799            | 0.58              | 35,202               | 0.62              |
| <b>Total</b>              | <b>6,021,433</b>  | <b>100</b>        | <b>5,687,823</b>     | <b>100</b>        |

Floating rate liabilities are all bank loans denominated in Renminbi, with the current yearly interest rate of 5.022%~6.03% which may be adjusted as per the adjustment of the loan interest rate by the People's Bank of China. Interest-free liabilities are mainly advances from the PRC government and other repayables. The short term interest-free liabilities of the Group are mainly funds for road maintenance and project construction, which will be repaid in due.

#### 4. *Funding and treasury policies*

The Company adopts conservative treasury policies to provide funding for the current operation and future growth of the Company. The Company has introduced strict risk management over standby cash funding. It increases gains and lowers finance costs by way of investing the idle capital in low-risk government bonds and other bonds.

##### **Cash inflow and outflow (RMB'000)**

|  |           |
|--|-----------|
| Net cash inflow from operating activities  | 320,441   |
| Net cash inflow from dividends received from jointly controlled entities and other income received | 20,742    |
| New bank loans borrowed  | 140,000   |
| Government assistance for Yanba Expressway   | (40,000)  |
| Dividends paid   | (201,570) |
| Purchase of fixed assets and payment for construction  | (143,122) |
| Increase in cash and cash equivalents for the six months ended 30 June, 2001                       | 176,491   |

Net cash inflow from operating activities increased by RMB157 million, as compared with the corresponding period in 2000. The increase was primarily attributable to the steadily increasing cash inflow from toll road operation and the interest-free advances of RMB112 million from the PRC government for the construction of the linkage project managed by the Company.

During the Period, the Group has cash and cash equivalents of RMB668 million, among them: deposits denominated in Hong Kong dollars amounted to HK\$113 million, of which HK\$105 million is kept in fixed deposits, with the interest rates varying according to their deposit terms between 3.533% to 4.125%. The capitalisation of short-term investments in bonds amounted to RMB407 million, of which RMB240 million are invested in government bonds and other bonds managed through creditable and qualified brokerages in the PRC, so as to make full use of their professional advantages and to reduce risks of investments in bonds. Once the capital is needed, it can be drawn and realised completely when due. The main purpose of investments in bonds is to provide necessary capital fundings for the Group's future investments and to maximize the return on the idle capital. The remainings are Renminbi bank deposits.

#### 5. *Gearing ratio*

|               | <b>At 30 June, 2001</b> | At 31 December, 2000 |
|---------------|-------------------------|----------------------|
| Gearing ratio | <b>32.59%</b>           | 25.30%               |

Gearing ratio of the Company is calculated by the following formula: total liabilities for the Period/ shareholders' funds for the Period. With its strong capital base, relatively low debt ratio, steady gearing ratio and relatively low financial risks, the Group has ample capability for further fund raising. This will be further enhanced upon the completion of the issue of A shares which will raise RMB900 million. As the Company's investments expand, the banking borrowings will also increase accordingly. The Group will make full use of financial leverages after taking into consideration the returns on investment, financial flexibility, and financial risks, so as to achieve maximum returns for its shareholders.

## **FOREIGN EXCHANGE RATE RISK MANAGEMENT**

The Group's foreign currency are mainly Hong Kong dollars ("HK\$"). As at 30 June, 2001, the Group has an aggregate of HK\$113 million kept in bank deposits, mainly from toll revenue from toll roads. The Hong Kong dollars are utilized to pay dividends of its H Shares. In the first half of 2001, the exchange rate for converting HK\$ to RMB remains relatively stable, ranging from 1:1.0606 to 1:1.0638. This does not have any significant impact on the Group's interim results.

## **PROJECT MANAGEMENT**

The Company is responsible for the development, construction and maintenance of toll roads. The Company selects contractors through tendering system, so as to ensure the effective control of project costs. Currently, the Company is settling the construction costs for Section A of Yanba Expressway and the tendering of Section B of Yanba Expressway to select suitable contractors for the construction of Yanba Expressway.

The Company has accumulated extensive experience in project management, with favorable track records of project quality management, tight cost control and good reputation in toll road sector. The Company is considering the possibility of establishing a project management consultant company with a view to expanding into this area, so as to capitalise the Group's expertise in project management. It is expected that the project management business, if materialises, will become a new source of the Company's profit.

