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TOWNGAS PEOPLE

We know our strength lies in our people. Therefore, training continues and remains our dominant focus underpinned by two main objectives – ensuring absolute safety of our industry by continually upskilling our technical and engineering employees, and providing the best possible customer service through quality performance programmes for our front-line staff.

One measure of our success is that with a 2.1 per cent reduction in the headcount during 2001 owing to natural attrition, together with a growth of 5.9 per cent in number of customers served, productivity effectively increased by a pleasing 8.3 per cent. As we move towards a more knowledge- and technology-based operation, the drive to enhance employee capabilities, cultivate multi-skilling, improve competencies and develop a culture of lifelong learning has become a pivotal tenet of our human resources policies.

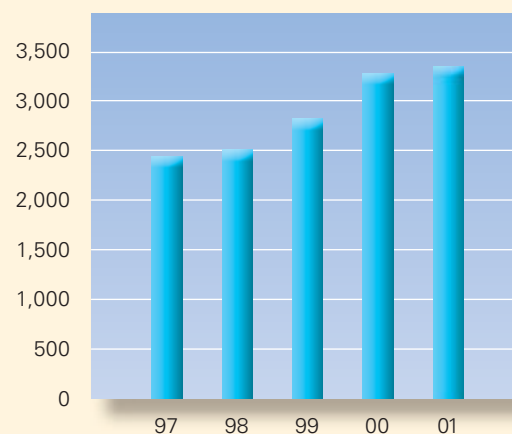
Creativity is the most important building block for sustained prosperity. In 2001, we set out to encourage Towngas people to take a fresh perspective on our tried-and-true resources.

We have been delighted with the results. In particular our Superior Quality Service theme – “Creativity Enhancing Values” – inspired 36 per cent of our employees to realise quality improvements and cost savings totalling in excess of HK\$21 million.

However, good business practices also go hand in hand with good safety performance. To this end, in 2001, we replaced our old gas utilisation

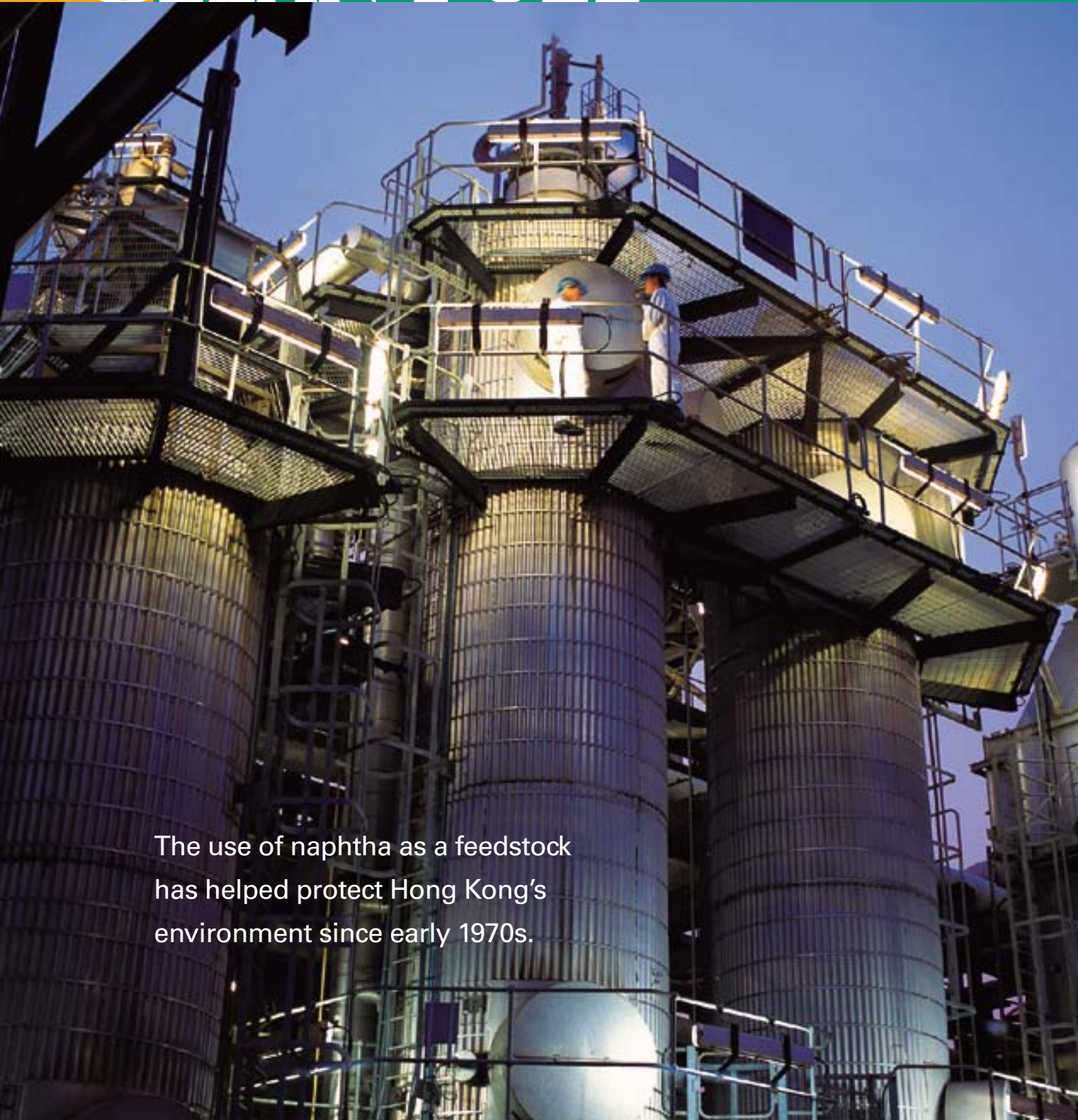
Turnover per Employee

Company (HK\$ thousand)





CLEAN FUEL



The use of naphtha as a feedstock has helped protect Hong Kong's environment since early 1970s.

CAPTURING OPPORTUNITIES IN CHINA



Our technicians are trained with a wide range of skills to deal with different appliances.

apprenticeship training scheme with a new programme that not only meets the increasing demand for more Regular Safety Inspection services, but will eventually also boost the pool of trained Registered Gas Installers available to better serve this vital sector of the gas industry.

A further advantage of having a well-trained workforce is that we can make this a cornerstone for developing business initiatives in the mainland. This means not only can we rely on our employees being sufficiently skilled to apply the necessary technology and management expertise required for expanding our business base in China, but we can also depend on them to pass on their skills to our joint venture personnel as well. In support of these initiatives, and to ensure our very stringent standards are met in our China business operations, we have developed a three-pronged programme – on-site training at specific joint venture companies, in-house programmes at our Training School in Guangzhou, Guangdong Province, and intensive immersion training in Hong Kong.

The Group's prescient search for suitable projects in the mainland in the last two years has in 2001, for the first time, extended our frontier beyond Guangdong into East China and resulted in good future prospects for city infrastructure developments, especially in the Pearl River Delta and Yangtze River Delta regions.

In the year under review, we expanded our strategic foothold in Jiangsu Province by acquiring a 45 per cent equity stake from Shell (China) Limited for an existing gas supply project in Suzhou Industrial Park (SIP), and by forming a city gas joint venture in the world-famous ceramic city of Yixing. We have also established a similar joint venture at Jimo, Shandong Province. The Group manages and holds major equity shareholding in all these

The Suzhou Industrial Park joint venture represents our first strategic foothold in downstream market in East China.



With its reputation as one of Asia's most established **quality** gas service providers, Towngas is set to repeat the **SUCCESS** it has had in Hong Kong and South China, as **potential markets** continue to widen in the mainland.

enterprises. The anticipated arrival of natural gas at these cities in three years' time will further foster the development of the piped gas business in these projects. The Group is optimistic about prospects for these investments.

Our strategic investments in midstream natural gas projects also reached a major turning point in 2001. The consortium led by Royal Dutch Shell, in which the Group participates together with OAO Gazprom and OAO Stroytransgaz, signed an interim agreement with PetroChina

Locally-trained staff assist customers at our new Zhongshan Customer Centre.

to become a 45 per cent foreign equity partner in the mega West-to-East gas transmission pipeline project. With a length of 4,200 km, the pipeline will cost about RMB 46 billion, and on completion in 2005, will bring natural gas from the Tarim Basin in Xinjiang Province to markets in East China.

In South China, where piped natural gas availability is limited, the Group is in equity partnership with, among others, China National Offshore Oil Corporation and BP to build the Guangdong Liquefied Natural Gas (LNG) terminal and an associated trunkline, the first such development in China. Once operational in 2005, this RMB 5 billion project will supply natural gas to the Pearl River Delta region, including cities where

Our modern Suzhou Towngas Customer Centre epitomises the slogan – "Living the Towngas Way".



we already have gas supply joint ventures. As tendering for the LNG supply is already underway, the Group is planning to build a pair of high-pressure submarine pipelines connecting the receiving terminal located in Shenzhen to the gas production plant in Hong Kong. This project will also realise both cost benefits and price stability by facilitating replacement of naphtha with LNG as the feedstock.

Gas consumption in the joint ventures in Zhongshan, Panyu and the Guangzhou Economic and Technological Development District grew by 54 per cent, with the Group's contribution increasing by 140 per cent in 2001. We expect this high level of growth in consumption to continue for the next few years with recovery in the property market and expansion in economic activity, boosted by the trend for improving environmental protection. Once LNG is available in the region in 2005, gas will be more competitive and consumption is expected to increase substantially.

Long term forecasts for China are upbeat regarding restructuring and overhauling the market economy. This is good news for the gas industry as continuing growth in GDP will be accompanied by increasing need for energy capacity expansion. In addition, China's current reliance on pollution-inducing coal as its primary energy source, coupled with the impending implementation of the Kyoto Protocol, is boosting mainland efforts to step up its clean air campaign. Most recently, entry into the WTO and Beijing's success in winning the right to host the Olympic Games in 2008 are also expected to significantly impact the gas industry with an accelerated demand for natural gas supply.

The Group foresees two main areas for growth potential as the rising demand for gas consumption and intensifying pressure for infrastructure development take hold. Downstream, we are actively looking for gas projects in cities that are going to have natural gas availability, high living standards and good economic growth prospects in the near future, so as to both tap into the rapidly expanding utility needs of developing city populations and service industrial infrastructure growth. Midstream, upward integration will enable us to turn downstream potential into reality by establishing a strong strategic link to a secured natural gas supply.

With its reputation as one of Asia's most established quality gas service providers, Towngas is in an enviable position, set to repeat the success it has had in Hong Kong and South China, as potential markets continue to widen in the mainland.



LPG FILLING STATIONS

By leveraging our existing strengths in gas expertise, Towngas has been able to develop a new line of business focusing on the green economy. Our ECO Stations are a major cornerstone of Towngas' green business initiatives, significantly contributing to improving the air quality of urban Hong Kong, whilst providing new outlets for increased revenue for the Group. Business

at our four dedicated LPG filling stations has grown more than 300 per cent throughout the year. So we are delighted to have also been awarded a fifth station centrally located to serve the busy districts of Hong Kong Island, and scheduled to open for business in the summer of 2002.

Of a total of 18,000 originally diesel-powered taxis in Hong Kong, 14,000 have switched to LPG by the end of the year under review, not only making the urban air cleaner but suggesting good prospects for the growth of LPG as a motor vehicle fuel. The drive to improve air quality is also now stimulating the light bus sector, comprising 6,400 vehicles, to convert its fleet to environmentally-friendly fuel.



Our LPG filling stations provide taxis with an environmentally-friendly source of fuel.

U-TECH

U-Tech Engineering Company Limited (U-Tech) initially subcontracted pipelaying from Towngas, and was instrumental in the construction of our ECO Stations. The Company has now expanded into working on Water Supplies Department tenders, as well as engaging in engineering work for the LPG industry. In the year under review, major projects have included replacement of water pipes for the Government and for the first time, installation of water, electricity, provision of gas, drainage and sewerage facilities for one of Hong Kong's major housing projects, creating added value in terms of cost and efficiency of site supervision for main contractors.

With the success of this latter project, U-Tech has moved into a new phase, providing a one-stop-shop utility service in which Towngas is perfectly positioned to take a leading role as the refurbishment and replacement of Hong Kong's outdated infrastructure gains pace. With its



Our ECO Stations (marked orange) are within easy reach of our customers throughout the territory.

investment in automation and advanced tooling, and the backing of Towngas' expertise, U-Tech can offer the latest technology and innovative techniques in laying pipes, cables and ductings, resulting in minimal open road excavation.



iCARE

Business has grown steadily as more services were introduced this year, such as e-brokering and the iCare Digital Mall which focuses on digital, electronic and personal computer products. The iCare shopping site was ranked one of the top three Hong Kong shopping websites for the second consecutive year. iCare Hotspot, a retail outlet and showroom for iCare products, is gaining in popularity and has recorded impressive growth. iCare's fee-based Internet Service Provider service, launched early in 2001, has also received high overall customer satisfaction rates in public surveys. Subscriptions are continuing to rise as a result of effective promotional initiatives organised in conjunction with strategic partners.

In December 2001, iCare also introduced an IDD service (iCare 1608) offering a quality international dialling option for residential and



commercial consumers at competitive prices. Capitalising on iCare's and Towngas' established name for service quality, this new service is fully expected to benefit from the ever-increasing telecommunications traffic between Hong Kong and the mainland – an excellent platform from which to grow the business.



TOWNGAS BRAND NAME

Also positioned as a value-added product to provide convenience, enhance customer service and improve customer relations, the Towngas Card is equally proving to be a viable business in itself. Always aware that our customers lead busy lives, want more choice and expect increasingly better services, we are therefore gratified that our innovative Towngas Card has now attracted more than 116,000 users despite keen competition in the credit card industry.

By linking the Towngas name with iCare, credit card and other services such as home insurance packages, we are capitalising on the good name of our Company in the minds of our consumers. In the long term, we recognise that brand extension has real possibilities for effective marketing as we move more towards other niche business opportunities.

FINANCIAL RESOURCES REVIEW

■ *Liquidity and Capital Resources*

As at 31st December 2001, the Group had a healthy net cash position of HK\$499 million (31st December 2000: HK\$4,740 million).

During the year, the Company repurchased 447.6 million shares. The total consideration paid to the shareholders and the related expenses amounted to HK\$4,362 million in cash.

The operating and capital expenditure of the Group is funded by cash flow from operations, internal liquidity and bank loans. The Group has adequate sources of fund and unutilised banking facilities to meet its future capital expenditure.

■ *Borrowing Structure*

As at 31st December 2001, the Group's bank borrowings amounted to HK\$1,349 million (31st December 2000: HK\$1,255 million). All the Group's borrowings are unsecured and has a floating interest rate with maturity within one year on revolving credit or term loan facility.

The Group's borrowings are primarily denominated in Hong Kong dollars and the Group has no significant exposure to foreign exchange fluctuations. Also, there is no net gearing for the Group as it was in net cash positions throughout the years 2000 to 2001.

■ *Contingent Liabilities*

As at 31st December 2001, the Group provided guarantees totalling HK\$2,283 million (31st December 2000: HK\$1,050 million) in respect of bank borrowing facilities made available to the associated companies and the jointly controlled entity.

■ *Currency Profile*

The Group's operations and activities are predominantly based in Hong Kong. As such, both its cash and cash equivalents and borrowings are denominated in either Hong Kong dollars or United States dollars. Borrowings for our Group's subsidiaries and joint ventures in the mainland China are however predominantly in the local currency, Renminbi.

■ *Group's Investments in Securities*

Under the Group's Treasury Committee's guidance, investments have been made in equity and debt securities. As at 31st December 2001, the investments in securities amounted to HK\$2,287 million (31st December 2000: HK\$1,302 million). During the year, the Group increased investment in trading and investment securities by HK\$123 million and HK\$862 million respectively, with the majority in debt securities based on the outlook of a favourable environment for investment in debt securities. The performance of the Group's investments in securities was satisfactory.

COMMUNITY INVOLVEMENT

Although Hong Kong has not suffered as much from the Asian economic turmoil and recent global events as some other countries in the region, the community is not immune to challenges facing its social service support system. Towngas is ever mindful that it has a responsibility, as a major corporate presence within Hong Kong, to help deliver community services in partnership with the Government. This year our commitment was focused on expanding our charity programmes and developing a range of new services for the disadvantaged generally and the elderly in particular.

As the elderly enter the twilight of their years, we owe them a quality of life that is both

secure and respectful of their contribution to society. At Towngas, we also recognise that there are many people in our society who are disadvantaged, be it in their family circumstances, personally or at work. We therefore seek to have the widest influence in our community service efforts, and believe that our fund raising for the Community Chest, an independent, non-profit making and non-government organisation is especially worthy of our support.

This year our enthusiastic team of Towngas volunteers helped make and distribute over 30,000 rice dumplings during the Dragon Boat Festival and raised funds for the Community Chest. We were so motivated by the success of this programme that we also made special



| Towngas' community contribution includes giving away long-boiled soup to needy seniors.



The Towngas team gave it their all at the Dragon Boat Race in Tai Po, where they ranked first in the Industrial Category.



A highlight of the inauguration ceremony of Rice Dumplings for the Community was a dragon boat made up of 3,000 rice dumplings. Pictured from left: Peter Shiu Lo Sin, Assistant Director of Broadcasting (Radio), Lam Woon Kwong, JP, Secretary for Home Affairs, Alfred Chan Wing Kin, Towngas Managing Director and William Li of The Community Chest.

mooncakes, a traditional Chinese good luck delicacy, to donate to numerous elderly residential homes during the Mid Autumn Festival.

We believe however, that community involvement is not merely a way for Towngas to support charity events and enhance its own profile, but also a way we can say “thank you” to a society that supports us with their business and loyalty. In 2001, we organised over 20 free service programmes for the elderly such as hair-cutting, and delivery of warm soup and food packs. In October, we also launched a two-year appliance donation programme for elderly people who qualify for assisted accommodation on public housing estates. Our long years of donating to the Tung Wah Group of Hospitals also continued, as did our sponsorship of numerous cultural activities,

including “Music and Wellness” organised by the Hong Kong Philharmonic Society.

Towngas was very pleased therefore, that the efforts of its employees were well recognised when we were awarded third in the Top Ten Fund Raising Organisations for the Community Chest and received the President’s Award for the seventh consecutive year. This year, we were also honoured with the Top Highest Donation and Highest Participation Awards in the Community Assistance Raised by Employees (CARE) programme of the Corporate and Employee Contribution Programme.