



## Management Discussion and Analysis

### 1. Business Summary

In the first half of the year, the Company adheres to its business strategy of sticking to core business. With its attention focused on economic benefits, the Company actively embarked on a variety of projects and achieved more satisfactory operating results. The Group recorded a total turnover of RMB372,508,000 for the Period, representing an increase of 17% over the same period of last year. During the Period, net profit attributable to shareholders was approximately RMB88,422,000 and earnings per share was RMB0.0346, representing an increase of 2.26% over the same period of last year.

The composition and percentage of revenue of the Group are as follows:

Item	For the six months ended 30 June 2002 (RMB'000)	Percentage of total income	Compared with the same of the previous year (%)
Toll income from Sichuan Chengyu Expressway	266,231	64.84%	16.28%
Toll income from Sichuan Chengya Expressway	82,183	20.02%	31.11%
Toll income from Chengdu Chengbei Exit Expressway	14,494	3.53%	3.6%
Toll income from Class II roads in Zigong and Luzhou and the toll bridge	30,265	7.37%	-0.43%
Income from other operations	17,423	4.24%	5.65%
<b>Total</b>	<b>410,596</b>	<b>100%</b>	<b>16.48%</b>

The growth in the Group's net profit attributable to shareholders during the Period was mainly due to the following factors: (1) Revenue from the Group's principal activities was surging significantly, with the apparent growth in toll income generated from Sichuan Chengyu Expressway, the core asset of the Group, and Sichuan Chengya Expressway, a major investment project of the Group, representing increase of 16.28% and 31.11%, respectively, over the same period of last year; (2) the efforts on reducing expenses and lowering consumption have further tightened the Group's internal cost control and management which resulted in a decrease of 10.15% in general and administrative expenses compared with the corresponding period of last year.



## 2. Business Review and Analysis

### (1) Principal Activities – Toll Road Operations

#### **Sichuan Chengyu Expressway (“Chengyu Expressway”)**

The 226km Chengyu Expressway, the core asset wholly owned by the Company, maintained steady growth over the year. It is the principal source of profit of the Group.

During the first half of the year, toll income of Chengyu Expressway grew further. As at 30 June 2002, Chengyu Expressway achieved toll income of RMB266,231,000, representing an increase of 16.28% over the same period of last year; average daily traffic flow was 9,625, an approximately 7.87% increase over the corresponding period of the previous year. Nevertheless, due to such factors as a net increase of RMB25,840,000 for repair and maintenance expenses in respect of Chengyu Expressway during the Period, net profit decreased to approximately RMB107,679,000, a 5.06% decline from the corresponding period of last year.

Increases in traffic flow and toll income of Chengyu Expressway were mainly attributable to the followings:

- The economy of the PRC maintained sustainable and steady growth during the first half of the year. As triggered by the grand development strategy of the western region, the economic growth rate of Sichuan Province outperformed the national average. The gross national product of Sichuan Province amounted to RMB202,716 billion, edged up by 10.2% over the same period of last year. The positive economic development has laid a solid foundation for drastic increase in traffic flow of Chengyu Expressway.
- The opening for traffic of both Southwest Road leading to Beihai Harbour and Chengdu Ring Expressway have further extended the coverage of Chengyu Expressway, resulting in substantial increase of its use by vehicles from other provinces for freight transportation.
- The accession of the PRC to the WTO and reduction of tariff for automobile stimulated rapid growth in domestic automobile consumption, particularly private cars. The private car ownership of Chengdu was in leading position amongst the cities in the PRC.



Following the escalation of traffic flow of Chengyu Expressway from year to year, it is necessary to expedite the process for automation of toll collection, telecommunication and supervision systems. The testing and inspection in the trial operation and on-the-job training for operators and technicians of the Q1 Electrical and Mechanical Contract Project, which was organised and undertaken by the Company through international tender, were basically completed during the first half of the year. Trial operation of the system was implemented on the whole expressway section on 25 June 2002. The Company will devote every effort on testing of the various functions of such systems during six-month trial operation so as to find out new problems which may occur and solutions therefor during the Period in an attempt to assure that the whole project will meet the requirements with regard to functions and utilisation as stipulated in the Technical Standards. The Company will strive to undertake acceptance inspection of the Q1 Mechanical and Electrical Contract Project by the end of the year.

### **Sichuan Chengya Expressway (“Chengya Expressway”)**

Chengya Expressway is 144km long. Its main section (129km) was opened to traffic and put into trial operation on 28 December 1999. Chengya Expressway was fully completed and commenced operation on 28 December 2000. The Company holds 58.975% interest in Sichuan Chengya Expressway Company Limited.

Since opening for traffic of Chengya Expressway, its traffic flow and toll income have demonstrated a remarkable upward trend. During the Period, the average daily traffic flow of Chengya Expressway reached approximately 7,850. Toll income of approximately RMB82,183,000 was recorded, edged up by 31.11% over that of the same period of the previous year. Notwithstanding significant improvement in the operating performance of Chengya Expressway, the economic conditions and social development along the expressway have to undergo a progressive process before they can be improved, traffic flow and revenue of Chengya Expressway were still at relatively low levels. Furthermore, depreciation of fixed assets were comparatively high and interest expenses were heavy, a loss of RMB33,809,000 for the Period was recorded, which nevertheless represented an improvement of approximately 36.71% when compared with the corresponding period of the previous year.



The increases in traffic flow and toll income of Chengya Expressway were mainly attributable to the followings:

- 2002 is the third year of which Chengya Expressway was opened to traffic. Its traffic flow is in the stage of growth;
- the avoidance of traffic flow diversion from Chengya Expressway due to the closure of the section from Chengdu to Xinjin along Dajian Road, which is parallel to Chengya Expressway, for repair works during the first five months of 2002;
- the improvement in the tourism industry of the western part of Sichuan and economic development of the region led to growth in traffic flow of Chengya Expressway.

### **Chengdu Chengbei Exit Expressway (“Chengbei Exit Expressway”)**

The 10.42km Chengbei Exit Expressway was opened to traffic in December 1998. The Company has a 60% interest in Chengdu Chengbei Exit Expressway Company Limited (“Chengbei Company”)

Chengbei Exit Expressway experienced difficult operating conditions during the first half of 2002. Chengdu Ring Expressway was opened to traffic in January 2002 and the section of Sima Bridge section along Dajian Road, which is parallel to Chengbei Exit Expressway, has implemented dual travel directions together with the closure for maintenance of Fuqing Road in Chengdu, which is adjacent to Chengbei Exit Expressway, during the first half of the year causing serious traffic diversion from the Chengbei Exit Expressway. As at 30 June 2002, the daily average traffic flow of Chengbei Exit Expressway was approximately 13,552, representing a drop of 13.13% from the same period of last year. However, Chengbei Exit Expressway implemented a new toll rate commencing from 20 June 2001 that the basic toll rate has been adjusted upward from RMB4.00/tonne vehicle to RMB5.00/tonne vehicle, resulting in toll income edged up slightly to approximately RMB14,494,000, slightly increased by 3.6%. However, Chengbei Exit Expressway has opened for traffic for over three years, maintenance expenses increased by RMB557,000, depreciation and amortisation expenses grew by RMB942,400 at normal rate. As a result, net loss of approximately RMB245,000 was recorded, representing a decline in profit of 141.46% from the corresponding period of the previous year. Following the opening for traffic of the whole route of the Third Ring Road in Chengdu on 1 October 2002, further traffic diversion is expected during the second half of the year. Chengbei Exit Expressway will confront with a further deteriorated operating conditions thereafter.



In order to tackle the serious problem of traffic diversion to the roads paralleled to Chengbei Exit Expressway and improve the operating conditions for Chengbei Company, its board of directors approved the investment proposals in relation to the acquisition and renovation of Dajian Road Northern Section, which is parallel to Chengbei Exit Expressway, as well as the acquisition of Qinglongchang Bridge at the beginning of the year. At present, the construction proposal, toll rate proposal and the feasibility study report of Dajian Road Northern Section have been completed, and the design and tender works are in the pipeline. Construction works are expected to commence during mid or by the end of September. Traffic flow of Chengbei Exit Expressway will be improved during the construction period. The acquisition of Qinglongchang Bridge is almost completed. It is expected that application to the relevant provincial authorities for approval will be completed in September. Commercial operation is expected to commence in October. It is hoped that toll income of Chengbei Company will be improved significantly at that time.

### **Chengdu Airport Expressway (“Airport Expressway”)**

The 11.92 km Airport Expressway has commenced operation since July 1999. The Company has a 25% interest in Chengdu Airport Expressway Company Limited.

Due to surges in passenger throughput and the number of flights of Chengdu Shuangliu Airport, the opening for traffic of the whole route of Airport Expressway at the end of last year and the completion and commencement for use of the new departure premises brought about remarkable results for Airport Expressway for the first half of 2002. As at 30 June 2002, the daily average traffic flow of Airport Expressway was approximately RMB20,505, a growth of 14.89% over the same period of last year. Total toll income was approximately RMB23,720,000, increased by 17% over the same period of last year. Profit for the Period was approximately RMB1,269,000, surged by 78.10% over the same period of the previous year. In view of the Airport Expressway's potential of achieving traffic volume well over that of the first half year during the latter half of the year, toll income of Airport Expressway is expected to keep growing in the latter half of the year.

### **Toll roads and bridge in Zigong and Luzhou**

The Company holds, through its subsidiary - Chengdu Shuhai Investment Management Company Limited, 59.94% of the operation rights and related interests in each of Zigong Ring Roads in Zigong and Lulong Road, Luhe Road and Tuojiang Er Bridge in Luzhou.



Toll income from Zigong Ring Roads and the two roads and one bridge in Luzhou for the period amounted to approximately RMB30,265,000, a 0.43% decline from the same period of last year. Toll income from Zigong Ring Roads grew by 18.57% over the same period of the previous year. As affected by the diversion of Longna Expressway and change to single travel direction of Tuojiang Er Bridge, toll income from the two roads and one bridge in Luzhou dropped by 9.87%. Net profit for the Period was approximately RMB6,762,000, a 2.74% decline from the same period of last year. The decline in profit was mainly attributable to the following factors: (1) the decrease in toll income from the two roads and one bridge in Luzhou; (2) the increase in maintenance expenses for Zigong Ring Roads and Lulong Road which in turn resulted in a surge in operating costs by 5.96% to approximately RMB2,000,000 when compared with the same period of last year.

## **Renovation of Dajian Road Southern Section Project**

As Dajian Road plays a critical role in road transportation of Sichuan with a relatively strong public welfare nature and its toll period has expired, it is no longer appropriate to be operated as a toll road. The Sichuan Provincial Department of Communications had reviewed and decided to resume the renovation and administration capacities of Sichuan Dajian Management Division over Dajian Road Southern Section and to implement administrative fee system in respect of Dajian Road after completion of its renovation. According to the decisions of the Sichuan Provincial Department of Communications, the Company intends to cancel the registration of Sichuan Shutong Road Industrial Company Limited ("Shutong Company"), which had originally undertaken the renovation project with respect to Dajian Road Southern Section. The cancellation formalities of Shutong Company are in progress. The registered capital of Shutong Company in the sum of RMB19,500,000 was fully repaid by the Department of Communications in June 2002.



## (2) Other Business

The Group's non-core businesses are principally developed by the following three subsidiaries:

### 1. **Chengdu Shuhai Investment Management Company Limited ("Shuhai Company")**

Shuhai Company is an investment management company principally engaged in investment in road infrastructure projects and other industrial projects, investment consulting service (excluding financial and security business), high-tech products and technological development. The Company holds 99.9% interests therein. Currently, Shuhai Company's income mainly derives from road infrastructure investment (in the toll roads and bridge in Zigong and Luzhou, details of which were disclosed above).

### 2. **Sichuan Shusha Enterprise Company Limited ("Shusha Company")**

Shusha Company is mainly engaged in gas station operation, advertisement leasing, vehicle maintenance and mobile emergency repair services along Chengyu Expressway and also develops multiple operations beyond the road. The Company holds 99.5% interest in Shusha Company.

As at 30 June 2002, major operating revenue of Shusha Company was approximately RMB2,084,000, representing a decrease of 10.29% from the same period of last year; a loss of RMB31,000 was recorded. The loss was mainly attributable to the followings: The profitability of existing assets of Shusha Company was weak and its major investment project, namely, Zigong Shuping Petrol Depot is still under construction and did not have any investment return. It is expected that after completion and commencement of operation Shuping Petrol Depot in September 2002, the asset structure of Shusha Company will be improved and thereby enhance its profitability.



### 3. Sichuan Shugong Expressway Engineering Company Limited ("Shugong Company")

Shugong Company is a mechanical engineering company mainly engaged in the construction and maintenance of infrastructures like road, bridge and tunnel and the sale of mechanical machinery and materials. The Company holds 95% interest therein.

The Company undertook renovation in its maintenance system during the second half of 2001 and shifted the road construction and maintenance business originally undertaken by Shugong Company to one of the maintenance centres. Therefore, revenue from principal operation of Shugong Company for the Period was entirely derived from leasing of mechanical machinery, totalling RMB1,744,000. A loss of RMB134,000 was recorded.

### 3. Financial Review

Summary of the Group's results

	For the six months ended 30 June	
	2002	2001
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Turnover	372,508	318,373
Profit before taxation	92,209	84,083
Net profit attributable to shareholders	88,422	86,472
Earnings per share (RMB)	0.0346	0.0338

Summary of the Group's assets

	30 June	31 December
	2002	2001
	RMB'000	RMB'000
	(Unaudited)	
Total assets	7,894,807	7,907,440
Total liabilities	2,970,383	2,980,246
Minority interests	440,056	454,506
Net assets	4,484,368	4,472,688
Net asset per share (RMB)	1.753	1.748





## Financial Analysis

The Group adopted positive and prudent financial policy. With the aim of continuous development, the Group endeavoured to reduce operating costs, strictly control investment risk so as to maximize returns to the Company and its shareholders.

As at the end of June 2002, the Company has a stable financial position. The major investment project, Chengya Expressway, achieved significant increase in toll income and the loss further improved dramatically. However, the Group has placed emphasis on road surface maintenance and provision for bad debts. The growth of the Group's results was not satisfactory. Turnover of the Group amounted to RMB372,508,000 for the Period, representing a 17% increase over the same period of last year; net profit attributable to shareholders amounted to RMB88,422,000, up by 2.26% over the same period last year.

Principal factors affecting net profit attributable to shareholders of the Company during the first half of 2002: The traffic flow of Chengya Expressway was still unsatisfactory. Its toll income amounted to RMB82,183,000. Finance costs reached RMB58,138,000 and operating loss amounted to RMB33,809,000; 2. Chengyu Expressway has opened to traffic for over nine years, some of its sections required major overhaul. Among the operating costs, road maintenance costs of Chengyu Expressway for the first half of the year has already increased by over RMB25,840,000 over the same period of the year. Costs for major and medium overhauls of the Group surged by RMB29,885,000 when compared with the same period of the last year, which has become a major factor affecting net profit attributable to shareholders; 3. Provision for the deposit of RMB11,170,000 placed with Guanghua Office under Sichuan Trust and Investment Company, which has underwent liquidation procedures; 4. The salary reward policy of the Company is pegged to toll income, and toll income during the Period had increased significantly and the payment of the one-off additional pension contribution resulted in a surge in staff costs by approximately RMB9,080,000 over the same period of last year; 5. Depreciation and amortisation grew by RMB6,300,000 at normal rate.



Nevertheless, the Company has strengthened its control on toll income. Thus, toll income of Chengyu Expressway, Chengya Expressway and Chengbei Expressway increased by 16.28%, 31.11% and 3.6%, respectively, over the same period of the previous year. On the other hand, the Group also enhanced its internal cost control and management, which resulted in a decline in general and administrative expenses by approximately RMB3,120,000 from the same period of the previous year. Moreover, the Group has made reasonable adjustments to its debt and loan repayment arrangements, resulting in a drop in financial cost by approximately RMB9,462,000 and an increase in net profit attributable to shareholders over the same period of last year.

## Liquidity of Capital and Financial Sources

During the period, the capital expenditure of the Group amounted to RMB70,517,000 which was mainly derived from operations and bank loans. As at 30 June 2002, the Group had loans aggregating to RMB2,117,200,000 with an average interest rate of approximately 5.7% per annum; and, unutilised banking facilities amounted to RMB1,071,000,000 which are all five-year long term banking facilities. The outstanding banking facilities is standby and will be utilised when appropriate. The gearing ratio of the Group was 37.62% as at 30 June 2002. Details of capital structure and comparative figures of 31 December 2001 are set out below:

	As at 30 June 2002		For the six months ended 31 December 2001	
	Total amount RMB'000 (Unaudited)	Percentage %	Total amount RMB'000	Percentage %
Shareholders' equity	4,484,368	56.80	4,472,688	56.56
Debt of floating interest rate	2,117,220	26.82	2,108,877	26.67
Interest-free debt	853,163	10.81	871,369	11.02
Minority interests	440,056	5.57	454,506	5.75
<b>Total</b>	<b>7,894,807</b>	<b>100</b>	<b>7,907,440</b>	<b>100</b>
Debt-equity swap ratio	66.24%		66.63%	



## Financial Policy

The Group has stringent cash management and risk control measures. The Group usually places its cash as short term deposit in Renminbi. Among the Group's debts of floating interest rate, there is a loan of US\$14,331,000 from the World Bank in favour of Sichuan Highway Development Holding Company, the parent company. The Company makes payment of the principal and related interest through purchase of foreign exchange from its parent company with Renminbi at floating exchange rate. Other loans are denominated in Renminbi and repaid from Renminbi income. In addition, the Group purchases foreign exchange to make dividend distribution to holders of H shares. The Group evaluates exchange risk as follows: There is a slowdown in the development of the global economy and, in particular, the burst out of a number of accounting rumours about certain giant companies in the US during the first half of the year further imposed uncertainties on the recovery of the weakened US economy. The decreasing trend of US dollars is expected to persist in the latter half of the year. In the first half of 2002, the import of the PRC maintained a better growth. On the other hand, foreign investors are optimistic about the PRC economy that foreign investment increased drastically. This has consolidated the stability of the exchange rate of Renminbi. There are even experts who are of the opinion that the exchange rate of Renminbi will remain pegged to the US dollars for quite a long time. Accordingly, the present exchange risk faced by the Company in respect of its assets and liabilities in US dollars is very low.

The interest expenses of the Company for part of its US dollar float rate loans have decreased as a result of US dollar interest rate cuts.

## Capital Commitment

Details of the capital commitment of the Group are set out in Note 11 to the account.



## 4. Business Development Plan for the Second Half of 2002

In the second half of the year, the Company will focus on the following work:

- (1) To set up modern enterprise systems in accordance with the requirements of the Company Law and to establish and refine the organization and systems of the Company in an effort to make decision scientifically, conduct business specifically, achieve services standardization and to undertake inspection systematically and improve the overall management of the Company;
- (2) The core asset of the Company, Chengyu Expressway, is a major traffic artery in Sichuan Province. Following the gradual implementation of the grand development strategy of the western region and as the starting of Xinan Chuhai Passage, the role played by Chengyu Expressway in road transportation will be more important. As Chengyu Expressway has been in operation for a long time, its maintenance and repairs should be more emphasized. The Company will adopt further effective measures based on real situation, so as to guarantee its speed, safety, comfort and smooth traffic flow, and ensure a sustainable and steady growth in its toll income:
  - (i) To carry out renovation works in a scientific manner and guarantee road engineering technology standard and quality, so as to minimize the inconvenience caused by renovation works to traffic;
  - (ii) To adopt effective measures to reinforce the management of toll collection business units and toll collection staff, implement standardized services and upgrade the quality of toll collection service, and attract as many vehicles as possible to use Chengyu Expressway.
- (3) To further strengthen the inspection and guidance of operations and management of the subsidiaries of the Company, reinforce the supervision of their financial operations and encourage further enhancement in management and operating results in an effort to improve the overall profitability of the Group;



- (4) To focus on the operation of its principal activities, review its investment and operations of other businesses in order to conclude and learn from past experience, rationalize business strategies and fully explore the potential profitability of existing resources, actively and duly select projects in an effort to create new foundation of profit growth.