

Chairman's Statement

On behalf of the Board of Directors ("Board") of China City Natural Gas Holdings Limited ("Company"), I present to our shareholders the report and the annual results of the Company and its subsidiaries (collectively "Group") for the year ended 31 July 2002.

The financial year of 2002 was a new chapter to us where Hikari Tsushin, Inc of Japan ("Hikari") has sold off its entire interests in the Company and ceased to be our controlling shareholder starting from December 2001. In April 2002, we have successfully entered into the energy industry in China through the acquisition of 50% interests in China City Natural Gas Co., Ltd. (CCNGCL), a Sino-foreign joint venture formed with China Petroleum Pipeline Bureau ("Bureau"), which is a wholly-owned subsidiary of China National Petroleum Corporation. In order to reflect Hikari's departure and our entrance into the natural gas sector in China, the Company was re-named as "China City Natural Gas Holdings Limited" in June 2002.

RESULTS

The Group's turnover for the year ended 31 July 2002 amounted to HK\$410,191,000, compared with the turnover of HK\$766,117,000 for the sixteen-month period ended 31 July 2001.

Carried forward a HK\$190,326,000 loss from the interim, the Group's loss attributable to shareholders was finished at HK\$451,836,000 for the year (2001: loss of HK\$155,976,000). The loss per share for the year under review was HK 8.1 cents (for the sixteen-month period ended 31 July 2001: loss of HK3.3 cents). The loss incurred for the year under review was mainly attributable to the discontinuance of our businesses in manufacture and trading of electronic finished products and trading of electronic parts and components ("Electronic Business") amounting to approximately HK\$97 million and the losses suffered by our Investment Business amounting to approximately HK\$349 million.

In light of the Group's performance, the Board does not recommend the payment of dividends for the year under review.

BUSINESS REVIEW

The Group consists of three main business divisions, namely, Investment Business, Manufacturing Business and Natural Gas Business and their performance is discussed below.

Investment Business

Inherited from last year an investment portfolio of approximately HK\$202 million and a negative investments revaluation reserve of approximately HK\$118 million, the performance of this Business is disappointing due to the less than encouraging worldwide economic conditions and our previous emphasis on the Internet and Internet-related businesses. Only a few of those long-term investments could implement their original business plans. Many of the invested companies changed their business models in order to cope with the changing market conditions. Some of the invested companies were even forced to undergo liquidation owing to the lack of further funding from the capital market.

Given all these external constraints, we have adopted a more cautious approach in both operating and reporting the Investment Business. We have utilised approximately HK\$112 million in acquisition of long-term investments this year (2001: approximately HK\$470 million). The Group cashed in four long-term investments at an aggregate consideration of approximately HK\$31 million. Upon review of the fundamentals and the latest operating situations of the invested companies in a prudent manner, the Group reduced its negative reserve from approximately HK\$118 million to approximately HK\$15 million and approximately HK\$243 million of impairment loss was charged to profit and loss account.

The Group also invested net cashflow of approximately HK\$133 million in marketable securities in Hong Kong for the year ended 31 July 2002. Due to the negative business sentiment and the disappointing performance of the global securities markets, the Group recorded realised and unrealised losses on short-term investments of approximately HK\$8 million and approximately HK\$41 million respectively for the year under review. However, in light of the low interest rate environment, the Group is still optimistic about the outlook of global securities markets.

Manufacturing Business

Suffered an operating loss of approximately HK\$90 million and approximately HK\$26 million in 2000 and 2001 respectively, our Electronic Business was hardly turning around in 2002 and continued to make a loss of approximately HK\$55 million. In view of the above, our management had then made a hard decision to discontinue the Electronic Business and disposed of it in March 2002 and consequently suffered a further book loss of approximately HK\$41 million.

Despite facing a severe market competition and sales decline for our Battery Business and Silicone Rubber Products Business in 2002, the performance of these businesses was still satisfactory. During the year under review, the loss of the Battery Business was substantially reduced by 67% to approximately HK\$1.9 million whereas the Silicone Rubber Products Business recorded a profit of approximately HK\$3.1 million.

Natural Gas Business

In April 2002, the Group invested approximately HK\$89 million to acquire 50% interests in CCNGCL of which the Bureau is our partner. The Bureau is specialised in the design and construction of oil and gas pipelines in China. Being supported by the advanced technology of the Bureau and the capital access advantage of the Group, CCNGCL targets to be one of the largest piped-city natural gas operators in China. CCNGCL has already achieved significant results in the past few months by securing the proprietary operation rights in seven cities/areas in China, namely Xining, Tianjin (Binhai District), Liling, Reian, Huimin, Qingyun and Binzhou.

Prospects

The Group is positive about the economic development of China though ambiguity is still hanging over the global economy. Fuelled by strong internal demand and successful access into the WTO, China's economy is expected to maintain a rapid growth. Demand for energy will increase and natural gas is expected to enjoy a privileged position because of the support from the Chinese Government and its emphasis on environmental protection, accompanying with the growing public recognition. Compared to international level of 26%, the total energy consumption of natural gas in China was only 3%, indicating enormous rooms for the expansion of the Natural Gas Business. The confirmed "West-East Gas Pipeline" would further increase the coverage of natural gas in China and the Group will seek to increase our presence in the cities surrounding "West-East Gas Pipeline".

The Group would continue to adopt a cautious and selective strategy in Investment Business. As the Internet and Internet-related industries showed little sign of recovery, the Group would consider realising some of the non-performing investments in our portfolio; whilst seeking new opportunities with the objective of achieving a better return for its shareholders.

For the Manufacturing Business, with the outstanding quality of the Group's battery products and silicone rubber products, we shall aim at attracting more worldwide reputable customers which in turn should translate into better margin. We will be selective rather than aggressive in customers' orders taking and shall initiate further cost reduction programs to maintain our competitiveness.

APPRECIATION

On behalf of the Board, I would like to take this opportunity to express my sincere appreciation for the valuable efforts of our fellow Directors, management and employees for their contributions to the Group. I also thank our business associates, investors and bankers for their continued support over the years.

Wong King Shiu, Daniel
Chairman

Hong Kong, 19 November 2002