



Report of
DIRECTORS



The Board is pleased to present the Report of Directors together with the audited financial statements of the Company and its subsidiaries for the year ended 31 December, 2002.

PRINCIPAL ACTIVITIES AND FINANCIAL RESULTS

The Company and its subsidiaries mainly engage in railway passenger and freight transportation between Guangzhou and Shenzhen and certain long-distance passenger transportation services, provision of railway facilities and technical services, and sales of food, beverages and merchandise in railway stations and on board.

The consolidated operating results of the Company and its subsidiaries for the year ended 31 December, 2002 and the financial positions of the Company and its subsidiaries as of 31 December, 2002 are set out in the consolidated income statement and consolidated balance sheets prepared in accordance with International Financial Reporting Standards (“IFRS”) as set out on page 47 and page 48 of this annual report, respectively.

PROPOSED PROFIT APPROPRIATION

For the year ended 31 December, 2002, the appropriations of profit as dividends and reserves as proposed by the Board are set out in Note 32 and Note 24 to the financial statements, respectively.

DIVIDENDS

The Company did not declare any interim dividend for the six months ended 30 June, 2002.

On 23 April, 2003, the Board proposed a distribution of a final dividend of RMB0.10 per share to the shareholders of the Company for the year ended 31 December, 2002.

Shareholders whose names appear on the Register of Members on 11 May, 2003 will qualify for entitlement to the final dividend for the year ended 31 December, 2002. The Register of Members for H shares will be closed from 11 May, 2003 to 10 June, 2003, both days inclusive.

Holders of H shares who wish to qualify for entitlement to the final dividend must lodge all transfer forms, together with the relevant share certificates, at the Company’s share registrars, Hong Kong Registrars Limited, at Rooms 1712-1716 on 17th Floor, Hopewell Centre, 183 Queen’s Road East, Wanchai, Hong Kong no later than 4:00 p.m. on 9 May, 2003, the last trading day before the Register of Members is closed.

Details concerning the final dividend payments to holders of H shares are to be announced after the approval by the shareholders at the 2002 annual general meeting, which is to be held on 10 June, 2003. The specific date and procedure for the payment of the final dividend will be announced separately.

In accordance with the articles of association of the Company (the “Articles of Association”), the dividend for domestic shares will be paid in Renminbi (“RMB”) while the dividend for H Shares will be calculated in RMB and paid in Hong Kong dollars. The exchange rate will be based on the average closing exchange rates for RMB to Hong Kong dollars as announced by the People’s Bank of China during the calendar week preceding the date on which the dividend is to be distributed.

OVERDUE TIME DEPOSITS

As of 31 December, 2002 the Company had approximately RMB31.365 million overdue time deposits placed with Zengcheng Urban Credit Cooperative ("Zengcheng"). Zengcheng failed to repay the Company the time deposits when they matured. The Company had obtained judgment in its favour regarding the unpaid time deposit. However, as the judgment debtor was under restructuring, the Court ordered a stay of execution of the judgment obtained by the Company. The said overdue time deposit accounts for approximately 0.3% of the Company's net assets and 1.2% of the Company's total current assets and has no material impact on the capital usage and operations of the Company. For prudence, the Company has reclassified such amount to other receivables and made a provision in its financial statements for such overdue deposit pursuant to management's estimates.

Except for such overdue time deposit, the Company has no other overdue time deposits which have not been repaid. The Company has not encountered any difficulty withdrawing deposits. The Company has placed its deposits with other commercial banks in the PRC and the MOR's Railway Deposit-taking Centre.

ENTRUSTED DEPOSITS

As of 31 December, 2002, the Company did not have any entrusted deposits placed with any financial institutions in the PRC.

BANK BORROWINGS

As of 31 December, 2002, the Company had no bank loans or borrowings.

CONTINGENCY

As of 31 December, 2002, the Company's investment in an associated company, Guangzhou Tiecheng Enterprise Company Limited ("Tiecheng"), amounted to approximately RMB140 million. In 1996, Tiecheng and a Hong Kong incorporated company jointly established Guangzhou Guantian Real Estate Company Limited ("Guangzhou Guantian"), a sino-foreign cooperative joint venture to carry on real estate business near a railway station operated by the Company.

On 27 October, 2000, Guangzhou Guantian together with Guangzhou Guanhua Real Estate Company Limited ("Guangzhou Guanhua") and Guangzhou Guanyi Real Estate Company Limited ("Guangzhou Guanyi") agreed to act as joint guarantors (the "Guarantors") of certain payables owed by Guangdong Guancheng Real Estate Company Limited ("Guangdong Guancheng") to an independent third party. Guangzhou Guantian, Guangzhou Guanhua, Guangzhou Guanyi and Guangdong Guancheng were related companies with a common chairman. As Guangdong Guancheng failed to repay the debt, the independent third party sued Guangzhou Guantian, Guangzhou Guanhua and Guangzhou Guanyi for the debt owed to it by Guangdong Guancheng. According to a court verdict on 4 November, 2001, Guangzhou Guantian, Guangzhou Guanhua and Guangzhou Guanyi had to pay an amount of approximately RMB257 million plus interest.

As stated above, if Guangzhou Guantian is held responsible for the guarantee, the Company may need to make provision for the decrease in value of its investment in Tiecheng. Having consulted an independent lawyer, the directors are of the opinion that the guarantee is invalid according to the relevant PRC rules and regulations. Tiecheng is now in the process of applying to the court for discharging the obligation of Guangzhou Guantian under the guarantee. Accordingly, the directors consider that as of the date of this report, the chance of Guangzhou Guantian having to settle the above claim is remote and no provision for the decrease in value of the Company's investment in Tiecheng was made in the accounts.

CHARGE ON ASSETS AND GUARANTEE

As of 31 December, 2002, the Company had not charged any of its assets and had not provided any guarantees.

CAPITALIZED INTEREST

There was no interest capitalized in the construction-in-progress or fixed assets of the Company and its subsidiaries during 2002.

FIXED ASSETS

Changes in fixed assets of the Company and its subsidiaries during 2002 are set out in Note 10 to the financial statements.

INCOME TAX EXPENSE

As the Company was registered and established in the Shenzhen Special Economic Zone of the PRC, it is subject to income tax at a rate of 15%. The rate is 18% lower than that of the standard rate for PRC companies of 33%. Details regarding income tax expense of the Company and its subsidiaries are set out in Note 6 to the financial statements.

RESERVES

Changes in the reserves of the Company and its subsidiaries during the year are set out in Note 24 to the financial statements.

STATUTORY PUBLIC WELFARE FUND

Details of the Company's statutory public welfare fund are set out in Note 24 to the financial statements.

SUBSIDIARIES

Details of the Company's principal subsidiaries as of 31 December, 2002 are set out in Note 13 to the financial statements.





EQUIPMENT AND MAINTENANCE

The Company owns 12 diesel high-speed locomotives, 5 high-speed electric locomotives, 18 shunting locomotives, 1 high-speed electric passenger train, 84 quasi-high-speed passenger coaches, 41 regular-speed passenger coaches and 112 long-distance express train passenger coaches. The freight cars used by the Company are all leased from the MOR, to which the Company paid rental fees and depreciation based on the uniform rate set by the MOR.

INFORMATION RELATING TO THE ORIGINAL ISSUE AND LISTING

20,536,760 ADSs (each ADS represents 50 H Shares) of the Company were listed on the New York Stock Exchange on 13 May, 1996 (New York time) and 217,812,000 H Shares were listed on the Hong Kong Exchange on 14 May, 1996 (Beijing time). Pursuant to the over-allotment options exercised by the underwriters, the Company also issued 186,650,000 H Shares in the form of ADSs on 24 May, 1996. The aggregate number of issued H Shares was 1,431,300,000 (par value of RMB1.00 per share).

	H Shares listed in Hong Kong (HK\$/share)	ADSs listed in New York (US\$/ADS)
Issue price	2.91	19.00
Highest traded price during 2002	1.59	10.30
Lowest traded price during 2002	1.26	7.90
Opening price on the first trading day of 2002	1.26	8.40
Closing price on the last trading day of 2002	1.32	8.70
Total transaction volume for 2002	1,350,356,000 shares	1,235,900 ADSs

SHARE CAPITAL STRUCTURE

As of 31 December, 2002, the Company's share capital consisted of:

Type of share capital	Number of shares (‘000)	Percentage of share (%)
State-owned Domestic Shares	2,904,250	66.99
H Shares	1,431,300	33.01
Total	4,335,550	100.00

There was no change in the Company's share capital during the year.

SUBSTANTIAL SHAREHOLDERS

As at 31 December, 2002, holders of over 10% or more of the Company's shares were as follows:

Name of shareholder	Number of shares (‘000)	Percentage of share (%)
Guangzhou Railway (Group) Company (the "Parent Company")	2,904,250	66.99
HKSCC Nominees Limited	1,386,362	31.98

As at 31 December, 2002, holders of H Shares holding over 10% of the Company's issued share capital as recorded in the Central Clearing System of HKSCC Nominees Limited were as follows:

Name of shareholder	Number of shares (‘000)	Percentage of H Shares (%)
Hongkong and Shanghai Banking Corporation (Nominees) Limited	721,823	50.43

Other than the information stated above, no other person or corporation had any interest in the share capital of the Company as recorded in the register required to be kept pursuant to Section 16(1) of the SDI Ordinance as having an interest of 10% or more of the issued share capital of the Company as at 31 December, 2002.

PURCHASE, SALE AND REDEMPTION OF SHARES

During the year ending 31 December, 2002, there was no purchase, sale or redemption by the Company, or any of its subsidiaries, of the Company's shares.

PRE-EMPTIVE RIGHTS

There is no provision regarding pre-emptive rights under the Articles of Association and the laws of the PRC.

CONFIRMATION BY INDEPENDENT NON-EXECUTIVE DIRECTORS OF CONNECTED TRANSACTIONS

The independent non-executive directors of the Company confirmed that the connected transactions (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules")) that were entered into by the Company during 2002 were entered into in the ordinary and usual course of its business on normal commercial terms or on terms that were fair and reasonable so far as the shareholders were concerned, or in accordance with the terms of an agreement governing such transactions or, where there was no such agreement, on terms no less favourable than those offered to (or from) independent third parties.

DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Information relating to the Company's directors, supervisors and senior management as of 23 April, 2003 is as follows:

Name	Age	Position	Nationality
<i>Directors:</i>			
Jiang Linyang	59	Chairman of the Board	Chinese
Li Daihua	60	Director	Chinese
Wu Yiquan	58	Director and General Manager	Chinese
Li Qingyun	39	Director and Deputy General Manager	Chinese
Wu Houhui	54	Director	Chinese
Shen Jun	53	Director	Chinese
Li Peng	56	Director and Chairman of the Trade Union	Chinese
Chang Loong Cheong*	57	Director	Hong Kong, the PRC
Deborah Kong*	43	Director	Australian
Name	Age	Position	Nationality

Supervisors:

Gu Hongxi	56	Chairman of the Supervisory Committee	Chinese
Zhao Genrong	57	Supervisor	Chinese
Chen Yongbao	51	Supervisor	Chinese
Chen Yunzhong	50	Supervisor	Chinese
Yao Muming	49	Supervisor	Chinese
Yang Rongjiu	55	Supervisor	Chinese

Other Senior Management:

Yan Ping	43	Deputy General Manager	Chinese
Luo Qingming	46	Deputy General Manager & Chief Engineer	Chinese
Ma Kaiming	32	Deputy General Manager	Chinese
Yao Xiaocong	50	Chief Accountant and Company Secretary	Chinese

* Independent directors who are also Hong Kong residents.

On 28 June, 2002, the Company convened the Annual General Meeting of the Company. Resolutions were passed at the Annual General Meeting to appoint Mr. Jiang Linyang, Mr. Li Daihua, Mr. Wu Yiquan, Mr. Li Qingyun, Mr. Wu Houhui, Mr. Shen Jun, Mr. Li Peng, Mr. Chang Loong Cheong, and Ms. Deborah Kong as directors of the third session of the Board of the Company. Resolutions were also passed at the same meeting to elect Mr. Gu Hongxi, Mr. Zhao Genrong, Mr. Chen Yongbao, Mr. Chen Yunzhong and Mr. Yao Muming as supervisors of the third session of the Supervisory Committee to represent the Company's shareholders, and to elect Mr. Yang Rongjiu as supervisor to represent the staff of the Company in accordance with a democratic election by the Company's staff.

On 28 June, 2002, resolutions were passed at the first meeting of the third session of the Board of the Company to appoint Mr. Jiang Linyang as chairman of the Board of the Company.

From 1 January to 28 June, 2002, Mr. Zhang Zhengqing was the chairman of the second session of the Board of the Company.

On 23 April, 2003, resolutions were passed at the third meeting of the third session of the Board of the Company to terminate the engagement of each of Mr. Ye Yongming and Mr. Chen Jianfu as the Deputy General Manager of the Company and to appoint Mr. Ma Kaiming as the Deputy General Manager of the Company.

INTERESTS OF DIRECTORS AND SUPERVISORS IN THE SHARE CAPITAL OF THE COMPANY

None of the directors or supervisors had, as at 31 December, 2002, any interest in any shares or debentures of the Company or any associated corporation (within the meaning of the SDI Ordinance) as recorded in the register as required to be kept under Section 29 of the SDI Ordinance, or as otherwise notified to the Company and the Hong Kong Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (for the purpose of this paragraph, the aforesaid are also applicable to the Supervisors of the Company). The Company has not granted to any of the Company's directors or supervisors or their spouses or children under the age of 18 any right to subscribe for any shares or debentures of the Company.

SERVICE CONTRACTS OF DIRECTORS AND SUPERVISORS

Each of the directors of the third session of the Board has entered into a service agreement with the Company for an initial term of three years commencing on 28 June, 2002. Except for the above, no other service contract has been entered into between the Company or any of its subsidiaries and any of the directors or supervisors. Apart from the above, the Company has not entered into any service contract with any director or supervisor that is not terminable by the Company within one year without payment of compensation (other than statutory compensation).



CONTRACTS ENTERED INTO BY THE DIRECTORS AND SUPERVISORS

No director or supervisor has any direct or indirect material interest in any contract of significance during the year to which the Company or any of its subsidiaries was a party.

REMUNERATION OF THE DIRECTORS AND SUPERVISORS

The remuneration of the directors and supervisors and senior management staff of the Company are set out in Note 5 to the financial statements of this annual report.

IMPACT OF THE RECENT ECONOMIC DEVELOPMENTS

The Company believes that there are no factors that will have a material negative effect on the Company's businesses and financial position in 2002.

ADJUSTMENT OF PRICING

In 2002, the Company has made the following adjustments to its passenger and freight transportation prices: (1) during the Spring Festival in 2002, the Company made different small scale upward adjustments to passenger fares based on different classes of fares of long-distance domestic trains; (2) with the approval of the MOR or the Parent Company, the Company continued to offer reduced prices for certain goods in order to improve its competitiveness in the freight transportation services; (3) during the New Year's holidays, the Spring Festival, the Tomb-sweeping Day holidays, the Labour Day holidays and the National Day holidays, the Company increased the fare on the high-speed passenger trains between Guangzhou and Shenzhen by RMB5 per trip.

EXCHANGE RISK

The Company has a certain amount of deposits denominated in Hong Kong dollars and in US dollars. It also receives income in Hong Kong dollars from the provision of its transportation services. If there are significant fluctuations in the exchange rates of Hong Kong dollars or US dollars to RMB, the financial condition of the Company will be affected.

MATERIAL LITIGATION

The Company and its subsidiaries were not involved in any material litigation or dispute in 2002.

AUDITORS

PricewaterhouseCoopers (certified public accountants in Hong Kong) and Pan-China (Schinda) (certified public accountants in the PRC) were the Company's international and domestic auditors respectively in 2002. Resolutions to continue to appoint these two firms as the Company's international and domestic auditors of the Company for 2003 will be proposed at the annual general meeting of the Company to be held on 10 June, 2003.

On 28 June, 2002, resolutions were passed at the annual general meeting of the Company to appoint PricewaterhouseCoopers as the Company's international auditors for the year 2002. The Company's international auditors were Arthur Andersen for 2000 and 2001.

EMPLOYEES, SALARY DISTRIBUTION POLICY AND TRAINING PLANS

As of 31 December, 2002, the Company had in total 9,258 employees.

The Company implemented a salary distribution policy which links remuneration closely with operating results, labour efficiency and individual contribution. Employees' salaries distribution is subject to macro-control and is based on their posted scores and performance reviews. The Company paid approximately RMB373.8 million in total for salary and benefits in 2002.

Pursuant to applicable state policies and regulations, the Company's employees enjoy the following benefits: (1) retirement pension — the Company is required to set aside a sum equivalent to 18% of the aggregate amount of salaries of all of its employees for the year and 5% of the aggregate amount of salaries of all of its employees for the year as employees' retirement pension and supplemental retirement pension, respectively; (2) welfare fund — the Company is required to set aside 14% of the aggregate amount of salaries of all of its employees as employees' welfare fund contributions and medical service fees; and (3) housing fund — both the Company and its employees are required to deposit 7% (for residents in Guangzhou area or along the Guangzhou — Shenzhen route), or 13% (for Shenzhen residents) of the employee's monthly salary into the employee's personal housing fund account. Save as disclosed, the Company has not participated in any other employees' basic medical insurance scheme.

During 2002, the Company has trained 556 employees on modern management techniques and 5,552 employees on adaptability. The training programmes included: knowledge about the World Trade Organization, office automation, human resources management, maintenance of the homemade high-speed electric trains, foreign-related services and safety regulations. The training courses were mainly organized by the Company's Employee Training Centre. The Company also employed certain external experts for these purposes. The total direct cost for the training programmes in 2002 was approximately RMB2.395 million.

EMPLOYEES' RESIDENTIAL PROPERTIES AND ACCOUNTING TREATMENT REGARDING THE DIFFERENCE BETWEEN THE SELLING PRICES AND COSTS OF EMPLOYEES' RESIDENTIAL PROPERTIES

The Company constructed and purchased new residential properties for its employees to improve their living conditions. Under a housing benefit scheme, the Company sold these residential properties to its employees at a price approved by the government. The losses arising from the difference between the net book value of the staff quarters and the proceeds collected from the sales of such quarters to the employees was not more than RMB226.4 million as of 31 December, 2002. Pursuant to the prevailing policies of the Ministry of Finance, the aforesaid losses should be credited to retained earnings in the statutory accounts as of 1 January, 2001, or in the case of a debit balance, to offset against statutory public welfare fund, statutory surplus reserve, discretionary surplus reserve and capital surplus reserve upon the approval by the Board. Such treatment conforms with the accounting rules and regulations applicable to the Company and its subsidiaries in the PRC.

In the financial statements of the Company as of 31 December, 2002 prepared in accordance with IFRS, the Company accounted for the housing losses as follows: losses arising from the sales of completed staff quarters to employees, or from the sales of premises under construction which could be reasonably estimated for future services was approximately RMB226.4 million. Such losses were amortized on a straight line basis over the estimated remaining average service period of 15 years from the time of such sales. During the year ended 31 December, 2002, the housing losses charged to the deferred staff costs in the consolidated income statement was approximately RMB15.09 million and the accumulated amortized amount was RMB45.27 million. As of 31 December, 2002, the unamortized deferred losses, which were recorded as deferred staff costs in the balance sheet of the Company and its subsidiaries, were RMB181.1 million.

MAJOR SUPPLIERS AND CUSTOMERS

Most of the locomotives, passenger coaches and major railway supplies and equipment of the Company are supplied directly or indirectly by the MOR. The Company may also purchase some of its equipment from foreign vendors and other domestic suppliers. The Company's five largest customers accounted for less than 30% of the Company's revenue and the Company's five largest suppliers accounted for less than 30% of the Company's purchases.

COMPLIANCE WITH THE CODE OF BEST PRACTICE

The Company and its directors hereby state that, to the best of their knowledge, the Company has, throughout the financial year ended 31 December, 2002, complied with the Code of Best Practice set out in Appendix 14 of the Listing Rules.

By Order of the Board

Jiang Linyang

Chairman

Shenzhen, the PRC

23 April, 2003

