Management Discussion and Analysis

Dear Shareholders,

OPERATING REVIEW

Operating Results

The Group's total turnover decreased by 7.2% to HK$732.4 million (2001: HK$789.3 million) which primarily comprised tariff revenue of HK$638.4 million (2001: HK$768.2 million) and additional fuel cost surcharges of HK$94.0 million (2001: HK$21.1 million). The Group's cost of sales decreased by 17.4% to HK$542.3 million (2001: HK$656.2 million), mainly attributable to decrease in electricity sales volume and lower fuel oil cost for the year. As a result, gross profit increased significantly by 42.9% to HK$190.2 million (2001: HK$133.1 million) and gross profit margin improved from 16.9% to 26.0%. Although administrative expenses surged by 57.9% to HK$28.9 million (2001: HK$18.3 million), profit from operations grew markedly by 54.9% to HK$133.5 million (2001: HK$86.2 million) while operating profit margin also improved from 10.9% to 18.2%. Finance cost continued to fall, by 26.5% to HK$34.6 million (2001: HK$47.1 million) and the Group's profit attributable to shareholders improved by 284.5% to HK$49.6 million (2001: HK$12.9 million). Earnings per share was 5.98 Hong Kong cents (2001: 1.55 Hong Kong cents).

Electric Power market

Guangdong Province continued to experience electricity shortage primarily due to its robust economic activities during the year. The Province's electric power industry reform has almost approached its final stages. As one of the key objectives of the electric power industry reform programs currently implemented by the provincial government has been to reduce general tariff levels in order to attract foreign investment and stimulate the overall economic environment, retail tariffs have been reduced on a provincial-wide scale in the past years. Although power producers in Guangdong have also been under potential threat of tariff cut, there has not been full-scale drastic cut on producer prices in the province. Producer tariffs of many power plants have continuously been maintained at relatively high levels and a diversity of tariff structures for power plants of different fuel types continued to prevail. Such phenomenon primarily reflected the persistent electricity shortage of Guangdong Province. The situation was particularly severe in high growth areas such as the Pearl River Delta Area where Foshan City is situated.

Management Discussion and Analysis

Electricity Sales

Shakou JV's electricity sales decreased by 16.9% to 1.33 billion kilowatt-hours ("kwh") (2001: 1.60 billion kwh), primarily reflecting the absence of (2001: 219.2 million kwh) electricity purchases from other power plant. During the year, Shakou JV has been discouraged to acquire electricity from other power plant for resale principally because the electricity shortage and high fuel oil prices have increased the cost of electricity acquisition and would eliminate substantially Shakou JV's overall profit margin. All electricity sold comprised only Shakou JV's self-generation (2001: 1.38 billion kwh). The average plant utilization rate of Shakou Power Plant was at approximately 50.6% (2001: 52.5%). Under the prevailing electricity consumption pattern with demand growth mainly concentrated on the peak load demand periods, Shakou JV's electricity sales remained almost stagnant as its power generating facilities have already been operated almost at its maximum available capacity during the periods. Under the power purchase agreement entered into between Shakou JV and 佛山市區電力工業局 (Foshan City District Electric Power Industry Bureau) on 29 December 1997 (the "1997 PPA"), which rights and obligations of Foshan District Power Bureau were subsequently novated to 佛山電力工業局 (Foshan Municipal Electric Power Industry Bureau) ("Foshan Municipal Power Bureau") on 25 September 1998, all the electricity was sold to 佛山電力工業總公司 (Foshan City Electric Power Industrial Corporation) during the year until April 2003. Since then, all the electricity were sold to 廣東省廣電集團有限公司佛山供電分公司 (Guangdong Guan-Dian Electric Power Grid Group Co. Ltd.) ("Guang-Dian Power Group Foshan"). The per-unit tariff for all electricity sold was Renminbi 0.51384 (exclusive of value-added tax) for most of the year until November-end. Effective from 1 December 2002, the per-unit tariff has been adjusted downward by approximately 1.7% to Renminbi 0.5051 (exclusive of value-added tax).

Major Overhaul

Pursuant to an overhaul agreement entered into between Shakou JV and a European equipment supplier dated 30 September 2001 (the "Overhaul Agreement"), Shakou Power Plant has undertaken a routine large-scale inspection and overhaul, and an upgrade of its power generating facilities since January 2003. As at the date of this report, all the necessary work in respect of the major overhaul has been completed and production has also resumed ahead of schedule.

Fuel Oil Prices

Oil prices continued to hover at high levels due to movements in international oil prices. However, the weighted average cost of heavy fuel consumed by Shakou JV decreased by 4.2% to Rmb 1,560 per tonne (2001: Rmb 1,628 per tonne). The unit fuel cost of electricity produced by Shakou JV decreased by 2.8% to Rmb 0.35 (2001: Rmb 0.36) per kwh. This was mainly due to the bulk-purchasing strategy of Shakou JV to purchase most of the heavy oil consumed for the year in early 2002 when fuel oil prices were at comparatively lower levels. As the aggregate amount of additional fuel cost surcharges received by Shakou JV increased markedly mainly because of the persistent high fuel oil prices prevailing during the year, Shakou JV's gross profit margin significantly improved.

New Fuel Supply Agreement

On 30 November 2002, Shakou JV entered into a new fuel supply agreement with 佛山市區電力燃料公司 (Foshan City District Electricity Fuel Supply Company) (the "Fuel Company") (the "New Fuel Supply Agreement") whereby the Fuel Company agreed to sell and deliver to Shakou JV the quantity of fuel requested by Shakou JV according to an annual schedule agreed between the parties for a term of three years commencing from 1 January 2003. The conclusion of the New Fuel Supply Agreement was essential: (1) as the existing fuel supply agreement entered into between Shakou JV and the Fuel Company on 29 December 1997 would expire by the end of December 2002; and (2) as to secure for uninterrupted supply of the necessary fuel oil as required by Shakou JV for its normal production and operation in the coming years. Details of the New Fuel Supply Agreement have been disclosed in the Company's circular dated 14 December 2002 and approved by the Company's shareholders on 31 December 2002.

Power Purchase Agreement

Shakou JV entered into a new power purchase agreement (the "New PPA") on 4 December 2002 with Guang-Dian Power Group Foshan whereby Shakou JV agreed to generate and supply electricity to Guang-Dian Power Group Foshan at a price determinable by Shakou JV and Guang-Dian Power Group Foshan subject to approval by 廣東省物價局 (Guangdong Provincial Price Bureau). The New PPA has the effect of replacing the 1997 PPA. The entering into of the New PPA was necessitated by a change in governmental policies in Guangdong Province which relieved Foshan Municipal Power Bureau the authority of setting purchase price and quantity for electricity generated by power plants and has the effect of rendering the 1997 PPA redundant. The major difference between the New PPA and the 1997 PPA are that there will no longer be a guaranteed minimum quantity for the electricity generated by Shakou JV. Details of the New PPA have been disclosed in the Company's announcement dated 4 December 2002.

Employees and Remuneration Policies

As at year end, the Group employed a total of approximately 220 staff (2001: 205 staff). Remuneration packages principally comprised salary and performance bonuses based on individual merits. The Group's total remuneration for the year was approximately HK$25.2 million (2001: HK$16.7 million).

FINANCIAL REVIEW

Liquidity and Financial Resources

The Group continued to fund its operation principally by internal cash inflow generated from operating activities. Compared with the previous year, net cash inflow from operating activities increased by 48.7% to HK$245.2 million (2001: HK$164.9 million). Accounts receivable turnover (turnover as a percentage of accounts receivable) improved from the previous 4.9 to 6.0 and the average collection period shortened from the previous 75 days to 61 days. Average credit periods from suppliers were also slightly shortened. As at 31 December 2002, the Group's total current assets decreased by 2.5% to HK$307.8 million (2001: HK$315.6 million) which primarily comprised cash & cash equivalents of HK$167.9 million (2001: HK$140.8 million) and trade and other receivables of HK$128.2 million (2001: HK$163.8 million). Total current liabilities increased by 8.8% to HK$356.7 million (2001: HK$327.9 million) which comprised mainly the current portions of long-term loans of an aggregate amount of HK$113.6 million (2001: HK$136.6 million), trade & other payables of HK$115.8 million (2001: HK$163.3 million) and short-term bank loans of HK$84.2 million (2001: Nil). As at 31 December 2002, the Group's short-term liquidity position deteriorated with net working capital deficit of HK$49.0 million (2001: HK$12.3 million). Current ratio worsened from the previous 0.96 to 0.86. Cash expenditure on tangible fixed assets for the year was HK$5.2 million (2001: HK$3.2 million).

Management Discussion and Analysis

Commited Banking Facilities

In September and October 2002, Shakou JV obtained short-term banking facilities from three banks in the PRC for an aggregate amount of Renminbi 116.0 million for its working capital requirement. As at the balance sheet date, the aggregate outstanding balance of bank borrowings under these banking facilities was Renminbi 90.0 million (equivalent to approximately HK$84.2 million). These bank loans bear interest at annual rate of 4.536%. Save as disclosed herein, the Group had no other bank borrowings or committed banking facilities.

Commitment for Capital Expenditure

As at 31 December 2002, the Group's total amount of capital expenditure commitment was HK$5.9 million (2001: HK$108.0 million). Apart from such, the Group has no other significant capital expenditure commitment.

Charge on Group Assets

As at 31 December 2002, the Group's power generating facilities of an aggregate amount of HK$1.1 billion (2001: Nil) were charged to three banks in the PRC to secure the respective short-term banking facilities for Shakou JV's working capital requirement. Apart from such, no other part of the Group's assets had been charged to banks, financial institutions or other enterprises.

Contingent Liabilities

As at 31 December 2002, the Group has contingent liabilities of approximately HK$43 million (2001: HK$43 million), details of which has been disclosed in the section headed "Contingent Liabilities" under "Notes on the Accounts" in this report.

Capital Sturcture and Gearing Ratio

The Group financed its non-current assets principally by a mix of long-term debts and shareholders' equity. The Group's long-term debts (including their short-term portions) decreased by 20.9% to HK$448.2 million (2001: HK$566.8 million). Total long-term debts mainly comprised the aggregate outstanding balance of the unsecured Renminbi loans due to Shakou JV's PRC joint-venture partner and its associates. The long-term debts were primarily employed to re-finance Shakou JV's investment in its fixed assets, principally power generating facilities, and were repayable within 10 years commencing in 1997 and 1998 at fixed loan rates of 10.08% per annum. The applicable loan rates for the year were 5.76% (2001: 8.08%) per annum. During the year, the Group made partial payment by internal cash flow generated from its operating activities. Gearing ratio, being the total aggregate amount of long-term debts (including their current portions) as a percentage of shareholders' fund, decreased from the previous 38.9% to 30.0%.

Net Assets

The Group's net assets amounted to HK$1.49 billion (2001: HK$1.46 billion). The net book value of goodwill arising from acquisition of subsidiaries was HK$641.6 million (2001: HK$673.2 million). Net assets per share improved from the previous HK$1.76 to HK$1.80 while net tangible assets per share also improved from the previous HK$0.94 to HK$1.03.

Exchange Risk

The Group's revenue was substantially denominated in Renminbi while its operating costs, finance costs, debt servicing and capital expenditure were substantially denominated in Renminbi. Pursuant to the Overhaul Agreement, a total aggregate amount of US$12.5 million (equivalent to HK$97.2 million) has been settled during the year and an outstanding amount of US$2.7 million (equivalent to HK$21.1 million), representing the remaining balance of the total consideration needed to be settled in US dollars as at the balance sheet date. Currently the exchange rates of Renminbi against Hong Kong dollars and US dollars have been stable. The Group has strategically maintained certain portions of its cash and bank balances in Hong Kong dollars and US dollars to minimize the risk of potential loss arising from foreign exchange fluctuations. No financial instrument has been used for the purpose of hedging exchange rate risk during the year.

Prospects

Foshan City's electricity demand growth is expected to persist as a result of the robust economic activities of the Pearl River Delta Area and Guangdong Province. As a result, the prevailing electricity shortage of Guangdong Province is expected to continue and could benefit the Group's power generating business. The prevailing high fuel oil prices are expected to retreat to lower levels over the long term. While overall electricity supply to the Guangdong Province may increase mainly as a result of increasing supplies from the West-to-East Transmission, Guangdong's power demand is expected to remain very strong and to provide similar appetite for such electricity supplies. Shakou JV's output has been accounting for a significant portion of the annual total consumption of Foshan City District and such dominating market position is expected to continue. Electricity from Shakou JV is essential to ensure uninterrupted supply to economic and social activities. It was also reported that Guangdong is having Foshan City to undergo territorial adjustment, making it the third largest city in the province after Guangzhou and Shenzhen. It is expected economic growth of Foshan City will have beneficial effect on the Group's existing business. The Group will continue its effort to improve its cost effectiveness and enhance its operational efficiency to strive for sustained growth in the future.

HE Haochang
Managing Director

Hong Kong, 15 April 2003