

# MANAGEMENT DISCUSSION AND ANALYSIS

## 1. Summary of the Results

### (1) Summary of income statement

The Group's profits

	2002	2001	2000	RMB'000	
				Pro forma	
				1999	1998
Turnover	451,620	667,435	612,640	432,368	416,079
Profit after taxation	93,193	191,778	289,520	224,041	226,499
Profit attributable to shareholders	92,791	190,616	287,900	222,047	224,619
Earnings per share (RMB)	0.09	0.19	0.28	0.36	0.37

### (2) Analysis of segment results

	RMB'000									
	2002		2001		2000		Pro forma			
	Amount	% on profit before taxation	Amount	% on profit before taxation	Amount	% on profit before taxation	Amount	% on profit before taxation	Amount	% on profit before taxation
Total segment profit before taxation of the Group	156,280	100	302,809	100	400,758	100	308,390	100	302,724	100
Main segment results included:										
Shenyang Water	158,816	82.69	267,167	88.20	357,319	89.20	264,717	85.80	250,368	82.70
Shenhai Co-generation	20,388	10.61	18,447	6.10	21,444	5.40	38,419	12.50	41,747	13.80
Real Estate Company	12,865	6.70	16,780	5.50	(403)	—	—	—	—	—

### (3) Analysis of segment turnover

	RMB'000									
	2002		2001		2000		Pro forma			
	Amount	% on total turnover	Amount	% on total turnover	Amount	% on total turnover	Amount	% on total turnover	Amount	% on total turnover
Total turnover	451,620	100	667,435	100	612,640	100	432,368	100	416,079	100
Of which:										
Shenyang Water	325,400	72.05	577,362	86.50	595,285	97.20	403,425	93.30	385,232	92.60
Real Estate Company	125,820	27.90	90,073	13.50	—	—	—	—	—	—
Other Operations	400	0.05	—	—	—	—	—	—	—	—

## 2. Analysis of Urban Water Supply Business

### Summary of operating results

Items	Jan-July 2002	Jan-July 2001	<i>RMB'000</i>
			Change (%)
Sales volume of water ('000 cu.m.)	<b>256,945</b>	No comparative figures	No comparative figures
Turnover	<b>325,400</b>	No comparative figures	No comparative figures
Profit before taxation	<b>158,816</b>	No comparative figures	No comparative figures

During the Year, there were significant changes in the external environment of purified water business and Shenyang Water was facing the following adverse conditions: (1) there was a substantial increase in the production costs of Shenyang Water resulting from the change in policies; (2) the actual water usage by end-users in Shenyang continued to decline; (3) the uncertainty relating to SWGC's ability to fully honour its obligations to Shenyang Water pursuant to the Purified Water Supply and Purchase Agreement and the supplementary agreement; and (4) the substantial decrease in the valuation on the business of Shenyang Water. Accordingly, in order to get away completely from the unfavourable conditions in operating the purified water businesses by the Group, the Company disposed of its entire 99.37% equity interest in Shenyang Water during the Year. The Disposal was approved at the extraordinary general meeting of the Company convened on 20th August 2002.

The Company dispatched a circular to shareholders of the Company on 5th July 2002 in respect of the above disposal. It was set out in the circular that the economic benefits relating to the 99.37% equity interest in Shenyang Water for the period from 1st January 2002 to 31st March 2002 would be attributable to the Company and from 1st April 2002, the corresponding 99.37% equity interest in Shenyang Water and the related assets (including but not limited to the outstanding receivable) and liabilities would be borne by Zheng Xing and all or part of the outstanding receivables of Shenyang Water recovered in the future would not be recognized in the accounts of the Group. The consideration of disposal of 99.37% equity interest in Shenyang Water was RMB 900,000,000, representing a profit of approximately RMB 37,700,000 over the net assets of Shenyang Water as at 31st March 2002 of approximately RMB867,800,000 (the unaudited net asset value prepared under the accounting principles generally accepted in Hong Kong ("HKGAAP")).

# MANAGEMENT DISCUSSION AND ANALYSIS

The operating result of Shenyang Water for the period from 1st January 2002 to 31st March 2002 was disclosed in the interim report of the Year. However, pursuant to “the Notification of Implementing ‘Corporation Accounting System’ and Explaining Relevant Accounting Principles” (CaiKuai [2002] No.18) dated 21st October 2002 issued by the Ministry of Finance of the PRC and in view of opinions of international auditors of the Company, the Group should have accounted for the result of Shenyang Water up to 31st July 2002 according to audit and accounting requirements. From 1st August 2002, all rights and interests relating to the 99.37% equity interest of Shenyang Water was no longer attributable to the Company. Such adjustment resulted in a loss on disposal of RMB 20,382,000, representing the difference between the consideration of disposal of 99.37% equity interest in Shenyang Water and the net assets value of RMB920,382,000 of Shenyang Water as at 31st July 2002 (based on the unaudited net asset value prepared under HKGAAP). On the other hand, the profit after taxation of Shenyang Water attributable to the Company for the four months from 1st April 2002 to 31st July 2002 was increased by approximately RMB 58,049,000. Consequently, the above adjustment only resulted in a change in structure of profit after taxation and gain from disposal of Shenyang Water included in the consolidated profit after taxation of the Group for the Year and had no material effect on the Group’s consolidated profit after taxation. As a result, the Company only sets out the operation data of Shenyang Water for the seven months ended on 31st July 2002 and it is not appropriate to compare the figures with those of the corresponding period of the Previous Year.

## 3. Analysis of Real Estate Company Business

### Summary of operating results

Items	RMB'000		
	Jan-Dec 2002	Jan-Dec 2001	Change (%)
Sales area ('000 sq.m.)	<b>41.02</b>	28.81	42.38
Turnover	<b>125,820</b>	90,073	39.69
Profit before taxation	<b>12,865</b>	16,973	(24.20)

During the Year, real estate market in Shenyang was continuously optimistic. The Company seized opportunities arising from such optimism and set the sale of residential project “Hongji Garden” and the construction of the phase one of the residential project “Water-Flowers City” as the main objectives and achieved satisfactory results in the Year. As at 31st December 2002, 95% of salable areas of “Hongji Garden” had been sold. Phase one of the residential project “Water-Flowers City” were roofed on schedule.

During the Year, the real estate operations of the Company recognised turnover amounting to RMB125,820,000 and profit before taxation amounting to RMB12,865,000, representing an increase of 39.69% and a decrease of 24.20% over those of the Previous Year respectively. The main reason for an increase in turnover is that sales area of the residential project “Hongji Garden” for the Year was larger than those of the Previous Year; the main reasons for a decrease in profit before taxation are that the residential project “Water-Flowers City” was not available for sale and no profits were generated during the Year, as well as the relevant expenses were charged to the income statement for the Year.

The residential project “Water-Flowers City” has gross floor area of 95,560 square metres, including gross floor area of 59,760 square metres for phase one. It is expected that residential units of phase one project will be available for sale in the spring of 2003. Phase two of “Water-Flowers City” has gross floor area of 35,800 square metres. It is expected that the main building in phase two project will be roofed by the end of 2003.

## 4. Analysis of Electricity and Heat Co-generation Business

### Summary of operating results

Items	2002	2001	RMB '000
			Change (%)
Turnover	<b>556,362</b>	520,159	6.96
Profit before taxation	<b>90,613</b>	81,988	10.52
The Group's share of profit before taxation (22.50%)	<b>20,388</b>	18,447	10.52
Profit after taxation	<b>72,755</b>	63,431	14.70
The Group's share of profit after taxation (22.50%)	<b>16,370</b>	14,272	14.70

During the Year, Shenhai Co-generation recognised turnover and profit before taxation amounting to RMB556,362,000 and RMB90,613,000 respectively, representing an increase of about 6.96% and 10.52% over those of the Previous Year respectively. During the Year, on-grid sales volume of electricity of Shenhai Co-generation was 2,088,100 MWh, representing an increase of 8.64% from that of the Previous Year. Total heat production was 4,631,991 GJ, representing a decrease of 7.58% over that of the Previous Year.

The main reasons for an increase in the on-grid sales volume of electricity are that (i) the market demand for electricity increased during the Year; and (ii) Shenhai Co-generation strengthened its internal production management, ensuring the smooth operations of its power generators.

The main reason for a decrease in the total heat production is that temperature was relatively high during the winter of 2002, leading to a decrease in market demand for heat energy.

## 5. Analysis of Investment in the Technology Business

Tsinghua Unisplendour Hi-Tech Venture Capital Inc. (THCI) is a venture capital company principally engaged in investment of high-tech projects. THCI was formally established in May 2000 by nine shareholders, including the Company. As at 31st December 2002, the registered capital of THCI was RMB250,000,000. It is owned by twelve shareholders. The Company contributed RMB20,000,000 to THCI, representing 8.00% of the total share capital of THCI.

During the Year, being adversely affected by the capital market and macroeconomic factors relevant to venture investment, loss of THCI amounted to RMB1,849,000. Since THCI recorded loss for the Year, no profits were distributed.

## 6. Analysis of Education Investment Business

Investment in education was a new business focus of the Company for the Year. It was in the initial phase of investment and construction, and therefore, education investment business did not generate any operating results for the Year.

During the Year, the Company acquired the land use right of a parcel of land with an area of 790,000 square meters located in the Zone for a consideration of RMB150 per square meter. Such land is intended to be used for the construction of Shenyang Development Beida Education Science Park and medium and top grade residential properties. In September 2002, the Company and Real Estate Company jointly invested RMB50,000,000 to establish Shenyang Education in the Zone. The Company directly holds 30% equity interest in it. Real Estate Company holds the remaining 70% equity interest in it.

During the Year, the Board approved the Company to acquire relevant equity interest in three education companies from connected parties respectively. The extraordinary general meeting of the Company held on 10th February 2003 approved the resolution to acquire 70% equity interest in Zhuhai Education and to jointly acquire 100% equity interest in Shanghai Education with Real Estate Company for the considerations of RMB166,600,000 and RMB194,400,000 respectively. Works relating to the change of equity holding are currently in progress (please refer to announcements of the Company dated 28th November 2002, 10th February 2003, 13th March 2003 and Section "Report of the Directors – Significant Event (5)" for details).

For the purpose of the collection of rents for the leasing properties of Zhuhai Education and Shanghai Education, the Company and the relevant parties entered into the master lease agreements.

## 7. Analysis of the Group's Assets and the Financial Position

### (1) Financial statistics of the Group

Items	Basis of calculation	As at 31st December 2002	As at 31st December 2001
Gearing ratio	Total liabilities/total assets x 100%	<b>10.83%</b>	10.20%
Current ratio	Current assets/current liabilities	<b>5.79</b>	5.30
Quick ratio	(Current assets – inventories – properties under development – properties held for sale)/current liabilities	<b>5.24</b>	4.00
Earnings/net assets ratio	Net profit/net assets x 100%	<b>5.02%</b>	10.90%
Sales profit margin	Net profit/sales x 100%	<b>20.55%</b>	28.60%
Debt equity ratio	Total liabilities/shareholders' equity x 100%	<b>12.20%</b>	11.40%

### (2) Overall position of the Group's assets

During the Year, there was an increase in the total assets of the Group when compared with that of the Previous Year. The total assets of the Group increased to approximately RMB2,072,427,000 in 2002 from approximately RMB1,955,354,000 in the Previous Year, representing an increase of approximately RMB117,073,000 or 5.99%.

Items	As at 31st December 2002	As at 31st December 2001	<i>RMB'000</i> Change in in amounts
Total assets	<b>2,072,427</b>	1,955,354	117,073
Of which :			
Property, plant and equipment	<b>10,478</b>	734,239	(723,761)
Properties under development	<b>279,732</b>	171,000	108,732
Interest in a jointly controlled entity	<b>100,265</b>	140,638	(40,373)
Deposits paid for acquisitions of subsidiaries	<b>360,994</b>	—	360,994
Investment securities	<b>20,000</b>	20,000	—
Current assets	<b>1,300,958</b>	889,477	411,481

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## (3) Current assets of the Group

During the Year, the current assets of the Group increased by RMB411,481,000 to RMB1,300,958,000 as compared with RMB889,477,000 of the Previous Year, representing an increase of approximately 46.26%.

Items	As at	As at	RMB'000
	31st December 2002	31st December 2001	Change in in amounts
Current assets	<b>1,300,958</b>	889,477	411,481
Of which:			
Cash and bank deposits	<b>486,308</b>	506,664	(20,356)
Accounts receivable	<b>2,845</b>	145,890	(143,045)
Prepayments, deposits and other receiv ables	<b>229,262</b>	111,278	117,984
Advance to a building contractor	<b>360,000</b>	—	360,000
Properties under development	<b>115,996</b>	—	115,996
Properties held for sale	<b>8,149</b>	98,079	(89,930)
Deposit paid for an investment	<b>94,380</b>	—	94,380
Amount due from a jointly controlled entity	<b>2,733</b>	23,855	(21,122)
Amount due from a fellow subsidiary	—	2,815	(2,815)
Tax recoverable	<b>1,285</b>	—	1,285
Inventories	—	896	(896)

## (4) Pledge of foreign currency deposits of the Group

As at 31st December 2002, the bank deposits amounting to HK\$60,000,000 pledged to banks for the bank loans totalling RMB60,000,000 granted to the Group in the year 2001 was released during the Year.

## (5) Currency risks

According to the “Quotations of the Exchange Rates for Converting Renminbi to Foreign Currencies by the Head Office of Designated Banks” periodically promulgated by the State Administration of Foreign Exchange of the PRC in 2002, the exchange rates of Renminbi to US dollar and to Hong Kong dollar were stable as a whole, and the exchange rate of the Hong Kong dollar to Renminbi experienced slight fluctuations during the Year. Accordingly, the risks of the Company’s deposits in Hong Kong were relatively low.

## (6) Land reserves

During the Year, the Group has two parcels of land reserves with a total area of 951,000 square meters as follows:

1. Portion No. 31, Wenhua East Road, Dongling District, Shenyang with an area of approximately 161,000 square meters and with cost of RMB171,000,000 already paid.
2. Portion 10th Road in the Zone with an area of 790,000 square meters and with cost of RMB100,000,000 already paid. The relevant land use right certificate is being applied for.

The Group intends to use the aforementioned land reserves for real estate development and education industry investment in the future, and its planning and design are being in progress.

## (7) Contingent liabilities

During the Year, the Group did not have any contingent liabilities.



## (8) Analysis of equity and reserves

	As at 31st December 2002	As at 31st December 2001	<i>RMB'000</i> Change in in amounts
Share capital	1,020,400	1,020,400	—
Share premium	323,258	323,258	—
Surplus from asset valuation	—	36,829	(36,829)
Statutory surplus reserve	66,332	109,487	(43,155)
Statutory public welfare reserve	33,167	54,741	(21,574)
Accumulated profits	396,590	202,241	194,349

## 8. Use of Proceeds Arising from the Issue of H Shares

The issue of 420,400,000 H Shares of the Company in December 1999 raised net proceeds of RMB684,256,000. No proceeds were raised by means of issuing new shares thereafter. The proceeds were applied basically in accordance with the intended use as disclosed in the prospectus of the Company dated 7th December 1999 (the "Prospectus"). The extraordinary general meeting of the Company convened on 20th August 2002 approved the resolution to change the intended use of the proceeds amounting to RMB200,000,000 which was the remaining unused net proceeds of the total amount of RMB489,000,000 originally intended to be used for Shenyang Water. Up to 31st December 2002, the Company had made investments totalling approximately RMB 593,230,000 (2001: RMB493,230,000), of which:

- (1) RMB231,951,000 had been applied to invest in the acquisition of No. 8 Water Plant (as defined in the Prospectus);
- (2) RMB56,787,000 had been applied for the acquisition and construction of the Shifosi Water Source expansion project (as defined in the Prospectus);
- (3) RMB9,041,000 had been applied to renovate the system of production facilities of Shenyang Water;
- (4) RMB1,000,000 had been applied to purchase new vehicles for Jingwei Transportation (as defined in the Prospectus);
- (5) RMB100,000,000 had been applied to acquire the land use right of a parcel of land in the Zone with an area of 790,000 square meters; and
- (6) the balance was used as working capital.

### 9. Number of Employees and Their Education Levels

As at 31st December 2002, the Group had 52 employees, of which 23 worked in the Company and 29 worked in Real Estate Company.

46 employees of the Group had received university or higher education, and 31 technicians were of intermediate rank or above.

During the Year, the aggregate salaries paid to the employees amounted to RMB22,269,000, including the salaries of January to July of 2002 paid to the employees of Shenyang Water and the salaries paid to the former employees in 2002 (2001: RMB44,419,000). The Group has not established any share option scheme for any of its senior management or employees.