



## MANAGEMENT DISCUSSION AND ANALYSIS

### (1) Business Summary

In the first half of the year, the Company experienced the difficulties arising from the unexpected incident of SARS. However, in the unfavourable operating environment, the Company implemented various measures to strengthen management, enhance quality of services, reduce costs and complete the work cautiously so that the Company was able to achieve comparatively satisfactory operating results. The Group recorded a total turnover of Rmb454,208,000 for the Period, representing an increase of 21.26% over the same period of last year. During the Period, net profit attributable to shareholders was approximately Rmb99,159,000 and earnings per share amounted to Rmb0.0388, representing an increase of 12.14% over the same period of last year.

### (2) Business Review and Analysis

#### 1. Principal Activities - Toll Road Operations

The Group is principally engaged in the operation and management of toll roads and bridges including Sichuan Chengyu Expressway ("Chengyu Expressway"), Sichuan Chengya Expressway ("Chengya Expressway"), Chengdu Chengbei Exit Expressway ("Chengbei Exit Expressway"), Zigong Ring Roads and the two roads and one bridge in Luzhou.



## Operating conditions for the six months ended 30 June 2003

Toll roads and interests held by the Company	Average daily traffic flow (Number of vehicles)	Period		Period		Comment on performance
		growth / decline (+/- %)	Toll income (Rmb'000)	growth/ decline (+/- %)	Net profit/ (loss) (Rmb'000)	
Chengyu Expressway (100%)	10,266	+6.66%	267,179	+0.36%	119,871	Growth in toll income
Chengya Expressway (58.975%)	7,331	-6.61%	79,675	-3.05%	(35,404)	Decline in toll income
Chengbei Exit Expressway (60%)	22,249	+64.18%	27,818	+91.93%	11,777	Significant growth in toll income
Zigong Ring Roads and two roads and one bridge in Luzhou (59.94%)	N/A	N/A	32,532	+7.49%	6,946	Growth in toll income

### Chengyu Expressway

The 226 km Chengyu Expressway, the core asset wholly owned by the Company, is a closed dual two-lane highway in the middle of Sichuan Province. The expressway maintained steady growth over the years. It is the principal source of profit of the Group.

In the first half of the year, the rate of growth in toll income of Chengyu Expressway decreased. During the six months ended 30 June 2003, average daily traffic flow of Chengyu Expressway was approximately 10,266, representing an increase of 6.66% over the same period of last year, and it achieved toll income of approximately Rmb267,179,000, representing an increase of 0.36% over the corresponding period of the previous year. During the Period, there was a slight increase in repairs and maintenance expenses for Chengyu Expressway. However, due to the decrease in provision for bad debts by approximately Rmb10,839,000 as compared with the corresponding period of the previous year, net profit for the Period amounted to approximately Rmb119,871,000, representing an increase of 11.32% over the corresponding period of last year.



The major factors affecting the traffic flow and toll income of Chengyu Expressway were as follows:

- In the first half of the year, the PRC was adversely affected by SARS. As a result, the economic growth in areas along Chengyu Expressway experienced an obvious slow-down. A large number of commercial and official activities were cancelled or postponed. There was a sudden decrease in the volume of passenger and cargo transportation. When the conditions of SARS were the most serious in May, the average daily traffic flow of Chengyu Expressway decreased by 7.88% as compared with the corresponding period of last year and toll income decreased by 13.28% as compared with the same period of last year, which resulted in a decrease of toll income by more than Rmb7,000,000 during the whole second quarter of the year.
- To assist the development of private enterprises and speed up the economic development of Sichuan Province, the government of Sichuan Province drew a significant decision. From 17 May 2003, the “green passage” policy of exempting from payment of toll fee was implemented provisionally for trucks carrying livestocks and fresh agricultural products passing through expressways for a trial period of three years. Chengyu Expressway commenced to open the “green passage” on 1 June 2003. Up to 30 June 2003, there were 22,602 trucks carrying livestocks and fresh agriculture products passed through Chengyu Expressway, and the toll fee exempted amounted to Rmb836,000.



- The completion of the construction of the related road networks led to the pressure of diverting traffic flow from Chengyu Expressway. At present, the roads which have direct impact on the traffic flow of Chengyu Expressway mainly include two roads. The first one is Chengnan Expressway which commenced operation on 23 December 2002. This road has diverted the traffic flow from the northeastern region of Sichuan Province and the northern region of Chongqing through Chengyu Expressway to Chengdu. As the road is also a part of the key national artery for traffic from Shanghai to Chengdu, it has a relatively significant impact on diverting the traffic flow of cargo transportation along the route from Shanghai through Chongqing to Chengdu. The second is that as a result of the urban expansion, the section of old Chengyu Road from Chengdu to Longquan has been included in the scope of management of the municipal roads. The expansion of the section of the road has been completed and commenced operations in October 2002. The above two roads led to a decrease of average daily toll income by approximately Rmb140,000.



As a major traffic artery in Sichuan Province, the change in the operating conditions of Chengyu Expressway has drew great attention from the Company. To ensure that Chengyu Expressway can elaborate great social impact and continue to achieve good economic effectiveness, after a detailed research and study, the Company has taken and will implement the following measures to further strengthen the operation and management of Chengyu Expressway, enhance the service quality and strengthen the market competitiveness. Firstly, the Company applied modern and advanced technology to change the toll collection environment and methods for Chengyu Expressway. On 1 March 2003, the IC card toll collection system of Chengyu Expressway formally commenced operation. This represented the full implementation of the three major automatic systems in toll fee collection, communication and traffic surveillance. This will assist the Company in enhancing the traffic management standard and service quality in all aspects, effectively reducing management and operating costs and improving the good social image of Chengyu Expressway. Secondly, the Company relied on the tourist industry to stimulate the traffic flow. The government of Sichuan Province has placed great priority in the development of tourist industry as the key economic works of the province for the year. The development of the tourist facilities and the boom in tourist industry along Chengyu Expressway will effectively stimulate the increase in traffic flow. The Company will seize this opportunity to establish the interactive relationship between traffic and tourist activities by way of various measures such as placing more resources in advertisement for tourist industry and increasing the number of entrance in appropriate places of the expressway. Thirdly, the Company adopted new operation and sales concepts to increase toll income. The Company organised a specialised team and carried out a research and study on the potential customers of Chengyu Expressway. Based on the results of the research and study, the Company also completed the compilation of a handbook for traffic in expressways to enhance the level of knowledge for drivers relating to the traffic in expressways. At the same time, the Company strengthened the relationship with target customers to attract more vehicles of corporations in using Chengyu Expressway. Fourthly, the Company put more efforts in repairs and maintenance of Chengyu Expressway. As Chengyu Expressway has been in operation for a long time, its design was relatively lagged behind. It has been carrying out a very important traffic mission as a major traffic artery in Sichuan Province because of its physical location. As a result, the road conditions are currently deteriorating and have caused certain inconvenience to vehicles when traveling on it. In the second half of the year, the Company will increase its input on conducting maintenance works in respect of some of the roads, bridges and tunnels which were damaged in order to ensure high speed, safety, comfort and smooth traffic flow of Chengyu Expressway.



The gross domestic products of the whole province will increase by 11.1% or 0.9 percentage point over the corresponding period of last year to Rmb226.02 billion as a result of the faster growth in the economic development of Sichuan Province. There has been a gradual improvement in the control on SARS since June 2003. In addition, the Company has implemented a series of measures to increase toll income. The Company therefore expects that Chengyu Expressway will be able to achieve a recovery growth in toll income in the second half of the year.

### **Chengya Expressway**

Chengya Expressway, 144 km long, starts from Chengdu and ends at Duiyan, Ya'an City. It is a closed dual two-lane and partly three-lane expressway. The Company has 58.975% equity interests in Sichuan Chengya Expressway Company Limited.

During the six months ended 30 June 2003, toll income of Chengya Expressway amounted to approximately Rmb79,675,000, representing a decrease of about 3.05% as compared with the corresponding period of last year. Average traffic flow was approximately 7,331, representing a decrease of about 6.61% as compared with the same period of the previous year. Due to the decrease in toll income of Chengya Expressway, coupled with heavy burden of finance costs in view of higher gearing ratio, a loss of Rmb35,404,000 was recorded during the Period, representing an increase in loss by approximately 4.72% or approximately Rmb1,595,000 as compared with the same period of last year.

The main reasons for the decrease in traffic flow and toll income of Chengya Expressway were as follows:

- During the second quarter of this year, the pace of economic growth of the western region of Sichuan Province slowed down and the tourist industry was cooled down as a result of SARS. This led to sudden decrease in traffic flow and toll income of Chengya Expressway. During the period of public holidays around 1 May 2003, toll income decreased by approximately Rmb1,600,000 as compared with the corresponding period of last year.



- From 1 June 2003, Chengya Expressway commenced to open the “green passage”. This made an impact on toll income of Chengya Expressway.
- During the first five months of the previous year, the renovation project of the southern section of Dajian Road, which is parallel to Chengya Expressway, had not been completed so that there had been no diversion of traffic flow from Chengya Expressway. After the southern section of Dajian Road recommenced operation in May 2002, there had been an impact on diverting the traffic flow from Chengya Expressway.

### **Chengbei Exit Expressway**

Chengbei Exit Expressway, 10.42 km long, starts from Qinglongchang and ends at Baihelin. It is a closed dual three-lane system which connects Chengdu and Chengmian Expressway. The Company has 60% equity interests in Chengdu Chengbei Exit Expressway Company Limited (“Chengbei Company”).

According to the relevant approvals from Sichuan Provincial Government and Sichuan Provincial Department of Communications, Chengbei Company was approved to acquire the operating rights of Chengbei Exit Dajian Road and Qinglongchang Bridge, which runs in parallel and is connected to Chengbei Exit Expressway, respectively, from Chengdu Municipal Department of Communications, and be engaged to carry out the renovation works of Chengbei Exit Dajian Road as appointed by Chengdu Municipal Department of Communications before obtaining such operating rights. In this connection, the renovation project along the whole section of Chengbei Exit Dajian Road, which is 8.6 km long, has commenced and traffic arrangement plan for Chengbei Exit Dajian Road was implemented in 2003 by Chengbei Company. As a result, the traffic flow of Dajian Road was restricted. This led to a significant increase in traffic flow of Chengbei Exit Expressway. During the six months ended 30 June 2003, average daily traffic flow of Chengbei Exit Expressway was approximately 22,249, representing a significant increase of 64.18% over the same period of last year. Toll income reached the level of Rmb27,818,000, representing an increase of 91.93% over the corresponding period of the previous year. Net profit for the Period amounted to approximately Rmb11,777,000, which achieved the operation target of turnaround from loss making to registering profit.



## Chengdu Airport Expressway

Chengdu Airport Expressway ("Airport Expressway"), 11.92 km long, is an affiliated project of Chengdu Shuangliu International Airport ("Shuangliu Airport"). It is a closed dual three-lane expressway connecting Chengdu and Shuangliu Airport. The Company has 25% equity interests in Chengdu Airport Expressway Company Limited.

During the first half of the year, the spread of SARS over the whole country had a significant impact on the domestic air travel industry. It directly led to a sudden decrease in the number of flight for Shuangliu Airport and a significant decrease in the volume of passenger and cargo transportation. As the number of passengers and flights of Shuangliu Airport directly affects the traffic flow and toll income of Airport Expressway, toll income of Airport Expressway in April, May and June 2003 decreased by 17.04%, 61.54% and 27.2% respectively as compared with the same period of last year, representing a significant loss for Airport Expressway. In addition, the opening of "green passage" also affected the level of toll income to a certain extent. Accordingly, toll income of Airport Expressway for the six months ended 30 June 2003 was approximately Rmb20,498,000, representing a decrease of 13.59% as compared with the same period of last year. Daily traffic flow was 18,721, representing a decrease of 8.7% as compared with the corresponding period of last year. Profit for the Period was approximately Rmb127,000, representing a decrease of 85.06% as compared with the same period of last year. As the conditions of SARS has gradually been put under control in June 2003 and the traffic flow of Airport Expressway in the second half of each year is usually significantly higher than the first half of each year, it is expected that toll income of Airport Expressway will have a recovery growth.

## Zigong Ring Roads and Two Roads and One Bridge in Luzhou

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





During the six months ended 30 June 2003, toll income of Zigong Ring Roads and the two roads and one bridge in Luzhou amounted to approximately Rmb32,532,000, representing an increase of 7.49% over the corresponding period of last year. Toll income of Zigong Ring Roads amounted to approximately Rmb11,757,000, representing a decrease of 1.68% as compared with the same period of last year. Toll income of the two roads and one bridge in Luzhou amounted to approximately Rmb20,775,000, representing an increase of 13.48% over the corresponding period of the previous year. During the Period, net profit of approximately Rmb6,946,000 was recorded, representing an increase of 2.72% over the same period of last year. The increase in profit was mainly attributable to the change to single direction traffic flow in view of the renovation project of the access of Tuojiang Er Bridge in Luzhou during the same period of last year which had a significant impact on toll income.

## **2. Other Businesses**

The Company'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 limited company and its major scope of businesses includes investment in road infrastructure projects and other industrial projects, investment consulting services (excluding financial and securities business), high-tech products and technological development. The Company holds 99.9% equity interests in Shuhai Company. Currently, Shuhai Company's income is mainly derived from road infrastructure investments (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 principally engaged in gas station operation, advertisement billboard leasing, vehicle maintenance and mobile emergency repair services along Chengyu Expressway and multiple operations beyond the road. The Company holds 99.5% equity interests in Shusha Company.

During the six months ended 30 June 2003, principal operating income of Shusha Company amounted to approximately Rmb3,082,000, representing an increase of 47.89% as compared with the corresponding period of last year. Net profit amounted to Rmb914,000. However, as Sichuan Expressway Energy Development Company Limited, the subsidiary of Shusha Company, was adversely affected by the sharp fall in price of petroleum products and the weak market conditions arisen from SARS in the second quarter of the year, the war in Iraq and the adjustment of the State policy, although principal operating income amounted to approximately Rmb68,227,000, representing an increase of 3,119.18% over the corresponding period of last year, an operating loss of Rmb1,586,000 was still recorded due to the small margin between the selling and purchase prices of petroleum products. As a result, Shusha Company had a consolidated loss of approximately Rmb838,000.

(3) Sichuan Shugong Expressway Engineering Company Limited (“Shugong Company”)

Shugong Company is principally engaged in the construction and maintenance of infrastructures such as roads, bridge and tunnel and the sale of mechanical machinery and materials. The Company holds 95% equity interests in Shugong Company. At present, Shugong Company is mainly engaged in the business of road maintenance of Chengyu Expressway. Following the entering into an overhaul stage of Chengyu Expressway, the business of Shugong Company will surge as it will undertake large volume of maintenance works.



### 3. Financial Analysis

#### Summary of the Group's Results

	For the six months ended 30 June	
	2003	2002
	Rmb'000	Rmb'000
	(Unaudited)	(Unaudited)
Turnover	454,208	374,576
Profit before tax	109,282	92,209
Profit attributable to shareholders	99,159	88,422
Earnings per share (Rmb)	0.0388	0.0346

#### Summary of the Group's Assets

	At 30 June	At 31 December
	2003	2002
	Rmb'000	Rmb'000
	(Unaudited)	
Total assets	8,116,130	8,053,518
Total liabilities	3,037,040	3,019,618
Minority interests	450,422	427,649
Total net assets	4,628,668	4,606,251
Net assets per share (Rmb)	1.809	1.801

#### Financial Analysis

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



As at 30 June 2003, the Group had a relatively stable financial position. During the period from January to June 2003, the turnover of the Group amounted to Rmb454,208,000, representing an increase of 21.26% over the corresponding period of last year. The increase was mainly attributable to the increase in sales of petroleum products by Rmb66,159,000 and increase in revenue from toll roads by 3.57%. Profit attributable to shareholders was Rmb99,159,000, representing an increase of 12.14% over the same period of last year.

Major factors affected profit attributable to shareholders of the Group for the period from January to June 2003 were as follows: (1) As affected by various factors such as SARS, the increase in toll income of Chengyu Expressway was not satisfactory. (2) Toll income of Chengyu Expressway was Rmb79,675,000, representing a decrease of 3.05% as compared with the corresponding period of last year. Finance costs reached the level of Rmb53,237,000 and operating loss amounted to Rmb35,404,000, representing an increase in loss of Rmb1,595,000 as compared with the corresponding period of the previous year. (3) There was a normal increase in depreciation and amortisation charges amounted to Rmb11,140,000. On the other hand, the significant increase in traffic flow of Chengbei Exit Expressway led to an increase of toll income by Rmb13,324,000 over the corresponding period of last year. At the same time, finance costs were reduced by Rmb8,031,000 as compared with the same period of last year as a result of the Company's efforts in strengthening internal cost control and management, adjusting the structure of debts on a timely reasonable basis as well as arranging for the repayment of debts. Thus, there was an increase in the profit attributable to shareholders as compared with the corresponding period of the previous year.



## Liquidity of Capital and Sources of Finance

For the six months ended 30 June 2003, capital expenditure of the Group reached Rmb64,698,000 which was mainly financed by funds derived from operations and bank loans. As at 30 June 2003, the Group's bank loans amounted to Rmb2,126,784,000 with an average interest rate of approximately 5.28% per annum. As at 30 June 2003, unutilised banking facilities of the Group amounted to approximately Rmb1,011,000,000, which are all five-year long-term loans. They are standby loans and will be utilised when appropriate. The gearing ratio of the Group was 37.42% as at 30 June 2003. Details of capital structure together with comparative figures as at 31 December 2002 are set out as follows:

	As at 30 June 2003		As at 31 December 2002	
	Amount	Percentage	Amount	Percentage
	Rmb'000	%	Rmb'000	%
	<i>(Unaudited)</i>			
Shareholders' equity	4,628,668	57.03	4,606,251	57.20
Debt with floating interest rate	2,126,784	26.20	2,149,220	26.68
Interest-free debt	910,256	11.22	870,398	10.81
Minority interests	450,422	5.55	427,649	5.31
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Total	8,116,130	100	8,053,518	100
Debt to equity ratio	45.95%		46.66%	



## **Financial Policy**

The Group has stringent cash management and risk control measures. The Group usually places its cash as short-term deposits in Renminbi. Among the Group's debts with floating interest rate, there is a loan of US\$11,145,000 lent by the World Bank which was on-lent through Sichuan Highway Development Holding Company, the parent company. The Company makes the payment of principal and related interest through the 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: The world economy will experience a gradual growth in the fourth quarter of this year and various developed countries will continue to maintain a relaxed monetary policy. The factors including the rapid growth of the PRC economy in the past and foreseeable future, stronger position of Renminbi in the Asian region, increase in the rate of investment and average purchasing power do not support the devaluation of Renminbi. On the other hand, the expectation of a rise in exchange rate of Renminbi becomes stronger. To ensure the continuous influx of foreign capital, stable increase in export and support of the fixed exchange rate mechanism of Hong Kong dollar, the central bank of the PRC needs to keep a proper balance between interest rate level and economic development and maintain a basically stable exchange rate of Renminbi. Accordingly, the present exchange risk faced by the Company in respect of its assets and loans denominated in US dollars is very low.

As a result of the decrease in US dollar interest rates, interest expenses for certain loans of the Company denominated in US dollar and with floating interest rate were reduced.

## **Capital Commitments**

Details of the Group's capital commitments are set out in note 10 to condensed financial statements.



#### **(4) Business Development Plan for the Second Half of 2003**

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

1. The Company will set up modern enterprise systems based on active and prudent principles, speed up the transformation of the Company's operation mechanism, adopt new management system and management concepts which can adapt to the mechanism of market competition and further strengthen the reform in the corporate personnel, segregation and recruitment systems to stimulate the morale of employees and enhance the effectiveness of various works of the Company so that the Company can speed up the pace of its development.
2. The Company will strengthen the operation management, enhance the service quality and strengthen the market competitiveness of Chengyu Expressway. At the same time, the Company will further step up the works of repairs and maintenance for Chengyu Expressway to improve its traffic conditions, ensure the safe and smooth traffic through the expressway and maintain and enhance its profitability.
3. The Company will strengthen the financial management and establish a financial system by adopting budget management as the core concept, cost control as the detailed plan and accounting supervision as the procedures to maintain and further enhance the stable financial positions, maintain the credit rating and capability of the Company in raising funds in the capital market and provide a support for the Company's future business development.
4. The Company will continue to strengthen the supervision and guidance of operation and management of the subsidiaries of the Company and encourage them to establish an internal operation mechanism with clear duty segregation, scientific management practice and system combined with incentive and restriction. At the same time, the Company will strengthen the review and control over the financial operation conditions of its subsidiaries to enhance the operating results and improve the Group's profitability as a whole.



5. The Company will strive to encourage the establishment of corporate culture in terms of “respect the work and job position, eager to learn, take into account the performance of the corporation as a whole and take an active approach for further development” so that the overall quality of the staff team can be improved continuously, the staff can be stimulated to work harder and have the morale to make more achievements and the corporation can be more cohesive and competitive.