



Report of Directors



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 December 31, 2004.

PRINCIPAL ACTIVITIES AND FINANCIAL RESULTS

The Company and its subsidiaries are mainly engaged in railway passenger and freight transportation between Guangzhou and Shenzhen and certain long-distance passenger transportation services. They also operate the passenger transportation service of Hong Kong Through Trains together with KCR in Hong Kong. They are also engaged in other businesses such as provision of railway facilities and technical services and sales of food, beverages and merchandise in railway stations and on trains.

The consolidated operating results of the Company and its subsidiaries for the year ended December 31, 2004 and the financial positions of the Company and its subsidiaries as of December 31, 2004 are set out in the consolidated income statement and balance sheets prepared in accordance with International Financial Reporting Standards ("IFRS") as set out on page 66 and page 120 of this annual report, respectively.

PROPOSED PROFIT APPROPRIATION

For the year ended December 31, 2004, the appropriations of profit as dividends and reserves proposed by the Board are set out in Note 9 and Note 24 to the financial statements, respectively.

DIVIDENDS

The Company did not declare any interim dividend for the six months ended June 30, 2004.

On March 17, 2005, the Board proposed a distribution of final dividend of RMB0.11 per share to the shareholders of the Company for the year ended December 31, 2004.

Shareholders whose names appear on the Register of Members on April 12, 2005 will qualify for the final dividend for the year ended December 31, 2004. The Register of Members for H shares will be closed from April 12, 2005 to May 12, 2005, 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, with the Company's share registrars, Hong Kong Registrars Limited, at Rooms 1712-1716 on 17th Floor, Hopewell Center, 183 Queen's Road East, Wanchai, Hong Kong no later than 4:00 p.m. on April 11, 2005, 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 subject to the approval of the shareholders at the 2004 annual general meeting, which is to be held on May 12, 2005. The specific date and procedure for the payment of the final dividends will be announced separately.

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In accordance with the articles of association of the Company (the “Articles of Association”), the dividend for domestic shares will be paid in 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 of the 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.

ENTRUSTED DEPOSITS

As of December 31, 2004, the Company did not have any entrusted deposits placed with any financial institutions in the PRC.

BANK BORROWINGS

As of December 31, 2004, the Company had no bank loans or borrowings.

CHARGE ON ASSETS AND GUARANTEE

As of December 31, 2004, there were no outstanding charges against any of the Company’s assets and the Company did not have any guarantee outstanding.

INTEREST CAPITALIZED

There was no interest capitalized in the construction-in-progress or fixed assets of the Company and its subsidiaries during 2004.

FIXED ASSETS

Changes in fixed assets of the Company and its subsidiaries during 2004 are set out in Note 10 to the financial statements.

TAXATION

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 income tax rate of 33% applicable to PRC companies.

Details regarding taxation of the Company and its subsidiaries are set out in Note 6 to the financial statement.

RESERVES

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

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STATUTORY PUBLIC WELFARE FUND

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

SUBSIDIARIES

Details of the Company's principal subsidiaries as of December 31, 2004 are set out in Note 13 to the financial statements.

EQUIPMENT AND MAINTENANCE

The Company owned 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 Company leased eight high-speed electric passenger trains from 廣州中車鐵路機車車輛銷售租賃有限公司 Guangzhou China Railway Rolling Stocks Sales and Service Company Limited. 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 NYSE on May 13, 1996 (New York time) and 217,812,000 H shares were listed on the Hong Kong Exchange on May 14, 1996 (Beijing time). Upon the exercise of the over-allotment options by the underwriters, the Company issued 186,650,000 H shares in the form of ADSs on May 24, 1996. The aggregate number of issued H Shares was therefore increased to 1,431,300,000. Each share has a par value of RMB1.00.

	H Shares listed in Hong Kong <i>(HK\$/share)</i>	ADSs listed in New York <i>(US\$/ADS)</i>
Issue price	2.91	19.00
Highest trading price during 2004	3.35	20.74
Lowest trading price during 2004	1.76	11.50
Opening price on the first trading day of 2004	2.20	14.12
Closing price on the last trading day of 2004	3.18	20.47
Total number of turnover in 2004	1,503,000,000	10,280,000

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SHARE CAPITAL STRUCTURE

As of December 31, 2004, the share capital of the Company consisted of:

Type of share capital	Number of shares (<i>'000</i>)	Percentage of share (%)
State-owned legal person 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 share capital of the Company during the year.

SHAREHOLDERS

So far as the Directors are aware, as at December 31, 2004, the interests and short positions of the persons, other than directors or supervisors of the Company, in the shares and underlying shares of the Company as recorded in the register required to be kept under section 336 of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) were as follows:

Name of shareholder	Class of shares	Number of shares	Capacity	Type of interest	Percentage of class of shares (%)	Percentage of total share capital (%)
Guangzhou Railway (Group) Company	Domestic shares	2,904,250,000 (L)	Beneficial owner	Corporate	100.00	66.99
Sumitomo Life Insurance Company (<i>Note</i>)	H Shares	128,916,000 (L)	Interest of controlled corporation	Corporate	9.01	2.97
Sumitomo Mitsui Asset Management Company Limited	H Shares	128,916,000 (L)	Investment Manager	Corporate	9.01	2.97
Mondrian Investment Partners Ltd (formerly known as Delaware International Advisers Limited)	H Shares	71,818,500 (L)	Investment Manager	Corporate	5.02	1.66

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Note: As at December 31, 2004, Sumitomo Life Insurance Company was deemed to be interested in 128,916,000 H Shares (representing 9.01% of the total H Shares of the Company or 2.97% of the total share capital of the Company) held by Sumitomo Mitsui Asset Management Company, Limited, a controlled corporation of Sumitomo Life Insurance Company.

The letter "L" denotes a long position.

PUBLIC FLOAT

As at March 17, 2005, at least 25% of its total issued share capital was held by the public. The Company is therefore in compliance with the Listing Rules as regard to sufficiency of public float.

PURCHASE, SALE AND REDEMPTION OF SHARES

During the year ended December 31, 2004, there was no purchase, sale or redemption by the Company, or any of its subsidiaries, of the shares of the Company.

PRE-EMPTIVE RIGHTS

There is no provision regarding pre-emptive right 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 Listing Rules) entered into by the Company during 2004 were entered into in the ordinary and usual course of its business and conducted on normal commercial terms. Such transactions were conducted in accordance with the terms of the agreements governing them. The terms were fair and reasonable and in the interests of the shareholders of the Company as a whole.

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DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Information relating to the directors, supervisors and senior management of the Company as of March 17, 2005 is as follows:

Name	Age	Position	Nationality
Directors:			
Wu Junguang	56	Chairman of the Board	Chinese
Li Kelie	57	Director and General Manager	Chinese
Hu Lingling	41	Director	Chinese
Wu Houhui	56	Director	Chinese
Wen Weiming	42	Director	Chinese
Li Qingyun	41	Director and Deputy General Manager	Chinese
Li Peng	58	Director and Chairman of the Trade Union	Chinese
*Chang Loong Cheong	59	Director	Hong Kong, the PRC
*Deborah Kong	45	Director	Australian
*Wilton Chau	43	Director	Singaporean
Supervisors:			
Yao Muming	51	Chairman of the Supervisory Committee	Chinese
Tang Dinghong	55	Supervisor	Chinese
Zhao Genrong	59	Supervisor	Chinese
Chen Yongbao	53	Supervisor	Chinese
Chen Yunzhong	52	Supervisor	Chinese
Yang Rongjiu	57	Supervisor	Chinese
Other Senior Management:			
Wu Weimin	47	Deputy General Manager	Chinese
Han Dong	43	Deputy General Manager	Chinese
Yang Yuzheng	42	Deputy General Manager	Chinese
Yao Xiaocong	51	Chief Accountant	Chinese
Guo Xiangdong	39	Company Secretary	Chinese

* Independent non-executive directors who are also Hong Kong residents.

On January 6, 2004, resolutions were passed at the seventh meeting of the third session of the Board of the Company to terminate the engagement of Mr. Yan Ping as Deputy General Manager and the engagement of Mr. Yao Xiaocong as Chief Accountant and Company Secretary. Resolutions were also passed at the same meeting to appoint each of Mr. Shao Huaping and Mr. Wu Weimin as Deputy General Manager, Ms. Li Ruizhi as Chief Accountant and Mr. Guo Xiangdong as Company Secretary.

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On June 10, 2004, the Company convened the annual general meeting of the Company. Resolutions were passed at the annual general meeting to appoint Mr. Wilton Chau Chi Wai as an independent non-executive director, terminate the engagement of Mr. Gu Hongxi as a supervisor of the third session of the Supervisory Committee of the Company and appoint Mr. Tang Dinghong, a representative of shareholders, as a supervisor of the third session of the Supervisory Committee.

On June 10, 2004, resolution was passed at the sixth meeting of the third session of the Supervisory Committee to appoint Mr. Yao Muming as chairman of the Supervisory Committee.

On August 12, 2004, resolutions were passed at the ninth meeting of the third session of the Board of the Company to terminate the engagement of Mr. Shao Huaping as Deputy General Manager and Ms. Li Ruizhi as Chief Accountant, to appoint Mr. Han Dong and Mr. Yang Yuzheng as Deputy General Manager and to appoint Mr. Yao Xiacong as Chief Accountant of the Company.

On October 4, 2004, resolutions were passed at the tenth meeting of the third session of the Board of the Company to terminate the engagement of Mr. Feng Qifu and appoint Mr. Li Kelie as the General Manager of the Company.

On December 30, 2004, resolutions were passed at the extraordinary general meeting to terminate the engagement of Mr. Feng Qifu and appoint Mr. Li Kelie as a director of the Company.

On March 17, 2005, resolution was passed at the fourteenth meeting of the third session of the Board of the Company to terminate the engagement of Mr. Luo Qingming as the Deputy General Manager and Chief Engineer of the Company.

PROFILE OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Directors

Wu Junguang, age 56, joined the Company in June 2003 and is the Chairman of the Board of the Company. Mr. Wu graduated from South China Normal University (華南師範大學). Since 1964, he has served in various managerial positions in various railway departments. He had served as the Stationmaster of Guangzhou Station, the General Manager of Yangcheng Railway Company and in other positions. He is currently the Chairman of the board of directors and the General Manager of Guangzhou Railway (Group) Company, the parent company of the Company.

Li Kelie, age 57, joined the Company in October 2004. He is a Director and the General Manager of the Company. Mr. Li is a member of Chinese Writers' Association and a vice chairman of Guangzhou Writers' Association (廣州市作家協會). Mr. Li has participated in the operation and management of railway transportation for years and has extensive industry experience. Since 1994, Mr. Li has held various senior positions within Guangzhou Railway (Group) Company and its subsidiaries. He is currently a member of the senior management of Guangzhou Railway (Group) Limited. Before he joined the Company, he was the Chairman and the General Manager of Sanmao Railway Company Limited (三茂鐵路股份有限公司).

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Hu Lingling, age 41, joined the Company in June 2003 and is a Director of the Company. He graduated from Changsha Railway Institute (長沙鐵道學院) and is an engineer. Since 1985, Mr. Hu has served in various technical and managerial positions in various railway departments. He had served as the Deputy General Manager of Yangcheng Railway Company and the Director of Transportation Department of Guangzhou Railway (Group) Company. Mr. Hu is currently the Deputy General Manager of Guangzhou Railway (Group) Company.

Wu Houhui, age 56, joined the Company in March 1999 and is a Director of the Company. He graduated from Dalian Railway College (大連鐵道學院) and is a senior economist. Mr. Wu served in various managerial positions in Guangzhou Railway (Group) Company from 1984 to 2003. He is currently the Chief Economist of Guangzhou Railway (Group) Company.

Wen Weiming, age 42, joined the Company in June 2003 and is a Director of the Company. Mr. Wen graduated from Workers University of Guangzhou Railway Bureau (廣州鐵路局職工大學) and Party School of the CPC (中央黨校) and is a senior accountant. He has many years of experience in the financial field. He had served as the Director of the Finance Sub-section of Yangcheng Railway Company and the Director of Finance Department of Guangzhou Railway (Group) Company. Mr. Wen is currently the Deputy Chief Accountant of Guangzhou Railway (Group) Company.

Li Qingyun, age 41, joined the Company in September 1999. He is a Director and Deputy General Manager of the Company. Mr. Li graduated from North Jiaotong University (北方交通大學), majored in railway transportation and organization in 1989. He holds a master degree. He served in managerial positions in technical and transportation departments of Guangzhou Railway (Group) Company from 1989 to August 1999.

Li Peng, age 58, joined the Company in December 1997. He is a Director and the Chairman of the Trade Union of the Company. Mr. Li graduated from the East China Civil Engineering Institute (華東工程學院). He had served in various executive and labour administration positions in Yangcheng Railway Company since 1977. He was the Deputy General Manager of the predecessor of the Company, Guangshen Railway Company, and Guangshen Railway Enterprise Development Company from 1992 to 1997.

Chang Loong Cheong, age 59, joined the Company in March 1996 and is an independent non-executive Director of the Company. Mr. Chang holds a management certificate from the Hong Kong Management Association. He is also a director of Shanghai Xinhua Iron & Steel Company Limited and Orient International (Shanghai) Limited. Mr. Chang had been a manager of Cathay Restaurant in Lagos, Nigeria, a member of the senior management of Island Navigation Corporation International Limited in West Africa and Orient Overseas Container Line Limited, and the General Manager and a director of Noble Ascent Company Limited.

Deborah Kong, age 45, joined the Company in March 1996 and is an independent non-executive Director of the Company. Ms. Kong is currently an executive director of Centennial Resources Company Limited. Ms. Kong holds a Bachelor of Arts degree from Sydney University and has obtained a Master Diploma in Finance from Macquarie University in Australia. She is a member of the People's Political Consultative Standing Committee of Shandong Province in the PRC.

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Wilton Chau Chi Wai, age 43, joined the Company in June 2004 and is an independent non-executive Director of the Company. Mr. Chau holds a bachelor degree in applied mathematics from the University of Hong Kong, a Bachelor of Laws degree from University of Wolverhampton and a Master of Business Administration from the University of Wales. Mr. Chau is a fellow member of the Association of Chartered Certified Accountants, a member of Singapore Institute of Arbitrators and Council member of Hong Kong Biotechnology Association. Since 1987, Mr. Chau has served in senior positions in various financial institutes overseeing investment and development in railway, road and airport infrastructure projects. Mr. Chau is currently the chairman of Qleap Venture Limited.

The appointment of each non-executive Director of the Company was for a period from his/her date of appointment until new Directors of the Company are being elected at the general meeting of the Company to be held in 2005.

Supervisors

Yao Muming, age 51, joined the Company in April 1997 and is the Chairman of the Supervisory Committee of the Company. Mr. Yao graduated from South China Normal University (華南師範大學) and had served as the Deputy Director of the Guangzhou and Zhuhai Animal and Plant Quarantine Bureaus. From 1997 to 2003, he was a member of the senior management of the Company. Since July 2003, Mr. Yao has been a member of the senior management of Guangzhou Railway (Group) Company.

Tang Dinghong, age 55, joined the Company in July 2003 and is a Supervisor of the Company. Mr. Tang graduated from Zhongshan University (中山大學). He joined the railway departments in 1969 and had served in various senior managerial positions of Guangzhou Railway (Group) Company.

Zhao Genrong, age 59, joined the Company in January 1996 and is a Supervisor of the Company. Mr. Zhao graduated from Northern Jiaotong University (北方交通大學). He served in finance position in Hengyang Railway Sub-administration from 1968. Since 1983, Mr. Zhao had served as the Deputy Director and the Director of the Finance Department of Guangzhou Railway (Group) Company. Since August 1999, Mr. Zhao has been the Director of the Auditing Department of Guangzhou Railway (Group) Company. He was a Director of the Company from January 1996 to June 2000.

Chen Yongbao, age 53, joined the Company in June 2002 and is a Supervisor of the Company. Mr. Chen graduated from Zhuzhou Railway Mechanical Secondary Technical School (株洲鐵路機械學校). Since 1975, he had served in various managerial positions in Guangzhou Railway Sub-administration and Yangcheng Railway Company. From 1997 to 2001, Mr. Chen served in the administration supervisory position of Guangzhou Railway (Group) Company. Since May 2001, Mr. Chen has been the chief of the Supervision Department of Guangzhou Railway (Group) Company.

Chen Yunzhong, age 52, joined the Company in May 2000 and is a Supervisor of the Company. Mr. Chen graduated from Guangzhou Railway Driver's School (廣州鐵路司機學校), Guangdong Jinan University (廣東暨南大學) and Party School of the CPC (中央黨校). He was a member of the senior management of Hainan Railway Company.

Yang Rongjiu, age 57, is a Supervisor of the Company. Mr. Yang graduated from Cadres Refresh Class (幹部進修班) in Guangzhou Zhongshan University (廣州中山大學). He joined the Company in September 1964 and was the Stationmaster of Shenzhen Railway Station, which belongs to the Company. Since May 2001, Mr. Yang has been the Deputy Chairman of the Trade Union of the Company.

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Other Senior Management

Wu Weimin, age 47, joined the Company in January 2004 and is a Deputy General Manager of the Company. Mr. Wu graduated from Guangdong Radio & TV University (廣東廣播電視大學) and is an engineer. Since 1984, he had served in various managerial positions in the Material and Equipment Department, the Planning and Statistic Department and the Labour and Wage Department of Yangcheng Railway Company. He also had served as an engineer in the Material and Equipment Section, the Director of the Planning and Statistic Sub-department of Yangcheng Railway Company. Mr. Wu was the Director of Labour and Wage Sub-department and Director of Social Insurance Centre of Yangcheng Railway Company before joining the Company as a Deputy General Manager in January 2004.

Han Dong, age 43, joined the Company in May 2000 and is a Deputy General Manager of the Company. Mr. Han graduated from Party School of the CPC (中央黨校), majored in economics and management, and is an engineer. Mr. Han joined the Company in August 1985 and had served in various managerial positions in the Material and Equipment Department, the Planning and Statistic Department, Passenger and Freight Transportation Marketing Department. Mr. Han was director of each of the Passenger and Freight Management Department and Equipment and Property Department of the Company.

Yang Yuzheng, age 42, is a Deputy General Manager of the Company. Mr. Yang graduated from Changsha Railway Institute (長沙鐵道學院) and is an engineer. Since 1985, Mr. Yang had served in Transportation Scheduling Department in railway departments and was a Deputy Director of the Scheduling Department and Chief Scheduler of the Company.

Yao Xiacong, age 51, is the Chief Accountant of the Company. Mr. Yao graduated from Party School of the CPC (中央黨校), majored in economics and management. Since 1975, Mr. Yao has served in the Financial Accounting Department in railway departments and has acquired nearly 30-year experience in financial accounting. Mr. Yao was a member of the senior management of the Company from June 1997 to January 2004. Mr Yao was the Director of the Accounting Department of Guangzhou Railway (Group) Company before he was appointed as the Chief Accountant of the Company in August 2004.

Guo Xiangdong, age 39, is the Company Secretary and the Director of Secretariat of the Board of Directors. Mr. Guo graduated from the Central China Normal University (華中師範大學) with a Bachelor of Laws degree and is an economist. He joined the Company in 1991, and had served as the Deputy Section Chief, Deputy Director and the Director of Secretariat of the Board of Directors of the Company. Mr. Guo has been the Company Secretary since January 2004.

INTERESTS OF DIRECTORS, SUPERVISORS AND OTHER SENIOR MANAGEMENT IN THE SHARE CAPITAL OF THE COMPANY

As of December 31, 2004, there was no record of interests and short positions (including the interests and short positions which were taken or deemed to have under the provisions of the Securities and Futures Ordinance) of the directors or supervisors of the Company in the shares, underlying shares and debentures of the Company or any associated corporation (within the meaning of the Securities and Futures Ordinance) in the register required to be kept under section 352 of the Securities and Futures Ordinance. The Company had not received notification of such interests and short positions from each director or supervisor of the Company as required to be made to the Company and the Hong Kong Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in Appendix 10 to the Listing Rules. 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.

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SERVICE CONTRACTS OF DIRECTORS AND SUPERVISORS

Each of the directors of the Company has entered into a service agreement with the Company. Save as disclosed, no other service contract has been entered into between the Company or any of its subsidiaries and any of the directors or supervisors that is not determinable 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 of the Company has any direct or indirect material interests in any contract of significance subsisting during or at the end of the year to which the Company or any of its subsidiaries was a party.

REMUNERATION OF THE DIRECTORS AND SUPERVISORS

The level of remuneration of the directors and supervisors of the Company was determined pursuant to the level of remuneration in Shenzhen, where the Company is located, and the job nature of each director and supervisor of the Company. The remuneration standard of each session of directors and supervisors is determined by the shareholder's general meeting of the Company.

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

IMPACT OF THE RECENT ECONOMIC DEVELOPMENTS ON THE COMPANY

The Company believes that no factor caused adverse effect to the Company's business and financial position in 2004.

ADJUSTMENT OF PRICE

In 2004, the Company made the following adjustments to the price for its passenger and freight transportation: (1) during the Spring Festival, the Company made different adjustments to passenger fares of different classes of long-distance domestic trains; (2) with the approval of the MOR, the Company made certain adjustments to the price for part of its freight and the overall price of freight transportation increased 3.6% in 2004 when compared with that of 2003; (3) during the New Year holidays, the Spring Festival, the Labour Day holidays and the National Day holidays, the Company increased the fare of the high-speed passenger trains and the regular-speed passenger trains between Guangzhou and Shenzhen by RMB5 per trip.

MATERIAL LITIGATION

The Company and its subsidiaries were not involved in any material litigation or dispute in 2004.

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AUDITORS

On June 10, 2004, resolutions were passed at the annual general meeting of the Company to appoint PricewaterhouseCoopers (certified public accountants in Hong Kong) as the international auditors of the Company for 2004 and to appoint Pan-China (Schinda) Certified Public Accountants as its PRC auditor for 2004. Resolutions to re-appoint these two firms as the international and PRC auditors of the Company for 2005 will be proposed at the annual general meeting of the Company to be held on May 12, 2005.

PricewaterhouseCoopers was the international auditors of the Company for 2003 and 2002.

ACCOUNTING TREATMENT REGARDING THE DIFFERENCES BETWEEN THE SELLING PRICES AND COSTS OF EMPLOYEES' HOUSING

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 and the proceeds from the sales of staff quarters to the employees was not more than RMB226.4 million as of December 31, 2004. 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 January 1, 2001, or in 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 of the Board. Such treatment conforms with the accounting principles and regulations applicable to the Company and its subsidiaries in the PRC.

In the financial statements of the Company for the year ended December 31, 2004 prepared in accordance with IFRS, the Company accounted for the losses arising from housing scheme as follows: losses from the sale of completed staff quarters to employees, or from the sale of premises under construction of 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 employees of 15 years from the time of such sales. During the year ended December 31, 2004, the amortization charged to the deferred labour costs of the consolidated income statement was RMB15.09 million and the accumulated amortization amounted to RMB75.46 million.

As of December 31, 2004, the unamortized deferred losses, which were recorded as deferred staff costs in the balance sheet of the Company and its subsidiaries, were RMB150.9 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 or obtained in the market. The Company may also purchase some of its equipment from overseas or domestic suppliers. The five largest customers of the Company accounted for less than 30% of the revenue of the Company and the five largest suppliers of the Company accounted for less than 30% of the purchases of the Company.

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PROPOSED ISSUE OF A SHARES, VERY SUBSTANTIAL ACQUISITION AND CONTINUING CONNECTED TRANSACTIONS

The Company and Guangzhou Railway Group Yangcheng Railway Company ("Yangcheng Railway Company") entered into an agreement for the acquisition by the Company of the railway transportation business between Guangzhou and Pingshi currently operated by Yangcheng Railway Company and the assets and liabilities relating to such business (the "Acquisition") on November 15, 2004 (the "Acquisition Agreement"). The consideration of the Acquisition was RMB10,264,120,700 (the amount as assessed in a valuation). The Company had applied to the relevant authorities for the issue and allotment of not more than 2.75 billion A shares (the "A Share Issue") and intended to use the proceeds from the A Share Issue to finance the Acquisition. Pursuant to the Listing Rules, the Acquisition constitutes a very substantial acquisition of the Company. As Yangcheng Railway Company is a wholly-owned subsidiary of Guangzhou Railway (Group) Company, the controlling shareholder of the Company, the Acquisition also constituted a connected transaction of the Company. In anticipation of the A Share Issue and the Acquisition, the Company had entered into various agreements with each of the vendor and its parent company in respect of certain continuing connected transactions. Such agreements shall take effect upon the completion of the Acquisition and shall replace all existing connected transaction agreements relating to the same categories of transactions.

The Company had made an announcement in respect of the above matters on November 15, 2004 and had also sent a circular to its shareholders on December 5, 2004. The circular contained details relating to the A Share Issue, the proposed amendments to the Articles of Association, the Acquisition and the continuing connected transactions, a letter from the independent board committee of the Company to the independent shareholders of the Company containing their recommendation and a letter from the independent financial adviser to the independent board committee and the independent shareholders containing its advice, etc. The Company held its domestic shareholders' class meeting, H shares shareholders' class meeting and extraordinary general meeting on December 30, 2004 to approve related matters. The Company submitted its application proposal relating to the A Share Issue to the China Securities Regulatory Commission (the "CSRC") on December 31, 2004.

The Acquisition Agreement is conditional upon the fulfilment of, among other things, the following conditions:

- (1) the formal approval of the relevant authorities or bodies in relation to the A Share Issue being obtained;
- (2) the A Share Issue having completed and raised an amount of not less than 65% of the consideration;
- (3) the approval of the relevant government bodies responsible for the supervision and management of state-owned assets in relation to the vendor's proposal on disposal of state-owned assets being obtained; and
- (4) the approval of the National Development and Reform Committee in relation to the price determination for passenger and freight railway transportation services between Guangzhou and Pingshi being obtained.

Save for condition (2) which can be waived by the Company, none of the above conditions can be waived. If the above conditions are not fulfilled within 2 years from the date of signing of the Acquisition Agreement, November 15, 2004, the Acquisition Agreement shall lapse and no party shall have any liability thereunder. In the event that any party rescinds the Acquisition Agreement for whatever reason after the A Share Issue has been completed, it is expected that the Company will retain the proceeds from the A Share Issue as general working capital.

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It is expected that the A Share Issue will be completed by the end of the second quarter of 2005, subject to the market conditions and policies of the CSRC.

CONNECTED TRANSACTIONS

The connected transactions of the Company were carried out on usual terms in 2004 in accordance with the conditions and waiver granted by the Hong Kong Exchange and the contracts entered into by the contracting parties. Save for the above conditional Acquisition Agreement and ongoing connected transactions agreements, which take effect upon the completion of the Acquisition, there has been no new connected transaction.

INDEPENDENCE OF INDEPENDENT DIRECTORS

The Company had received an annual confirmation of independence from each of Mr. Chang Loong Cheong, Ms. Deborah Kong and Mr. Wilton Chau Chi Wai, the independent non-executive directors of the Company, pursuant to Rule 3.13 of the Listing Rules. The Company confirms independent non-executive director of the Company to be independent.

AUDIT COMMITTEE

The Audit Committee consists of three independent non-executive directors of the Company. Its main duties include review and supervision of the financial reporting process and internal controls of the Company. The audited annual financial statements for the year ended December 31, 2004 have been reviewed by the Audit Committee.

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 December 31, 2004, complied with the Code of Best Practice set out in Appendix 14 of the Listing Rules.

Note: Appendix 14 of Listing Rules — Code of Best Practice was replaced by the new Appendix 14 — Code on Corporate Governance Practices on January 1, 2005.

By Order of the Board
Wu Junguang
Chairman

Shenzhen, the PRC
March 17, 2005