MANAGEMENT DISCUSSION AND ANALYSIS

The Group's turnover and operating profit are shown by business segment in note 3 to the condensed financial statements. The Group principally engages in the electricity generation and sale of electricity, the sales and distribution of Liquefied Petroleum Gas ("LP Gas") and piped gas, and gas pipelines construction businesses. Turnover for the period totaled HK$751.1 million, an increase of 106.0% over the same period last year, mainly due to an increase of sale of electricity by 61.6% to HK$589.1 million and the inclusion of the turnover of HK$162.0 million contributed from Panva Gas. Profit attributable to shareholders for the period increased substantially by 397.0% over the same period last year to HK$176.2 million.

The Group's operating expenses for the period increased by 181.6% to HK$41.4 million as compared to HK$14.7 million in the same period last year, mainly due to an increase of HK$13.4 million in the administrative and selling expenses as the result of the consolidation of the administrative and selling expenses of Panva Gas.

BUSINESS REVIEW

Overview on electricity generation business and outlook

For the six months ended 30 June 2005, the Group recorded an increase of 38.9% in segment profit to HK$87.6 million. This remarkable performance in this segment was the result of the increase in power generation due to increased capacity, the strong demand for electricity in the Guangdong Province and the management's effective cost control measures especially on the fuel supply.

During the period, the Group sold 1,022.3 million kwh of electricity, representing an increase of 61.4% as compared to 633.5 million kwh over the same period last year. The turnover for the six months period ended 30 June 2005 also increased by 61.5% from the previous period to HK$589.1 million. This increase was largely due to the completion of third and fourth combined cycle generating units which commenced commercial production in September 2004 and May 2005 respectively and the increased demand for electricity in the Guangdong Province. In June 2005, the Group was currently equipped with a total installed capacity of 665,000 kilowatts, an increase of 2.2 times over the installed capacity of last period.

The direct operating expenses for the six months period ended 30 June 2005 attributable to electricity supplies increased by 70% to HK$490.8 million due to the increase in electricity generation and higher fuel costs, which were the primary direct operating expense for electricity generation. Currently, the Group's power plant is mainly powered by heavy oil which is a refined product of crude oil. The staggering high world crude oil price has significantly affected the energy sector in the People's Republic of China ("PRC") and, to a lesser extent, the Group's fuel costs. This was mainly due to the price of heavy oil had increased relatively substantial lower than the price of crude oil during the period. In addition, the management had contributed a lot of efforts towards improving productivity and continued to strengthening of fuel procurement and inventory control, so as to minimize the impact of higher fuel costs to the Group. Therefore, the gross profit margin of sale of electricity for the period was moderately decreased by 3.2% over the same period last year.

Recent years the management has seen increased participation from hedge funds and institutional investors with investment or speculative perspective and some of them have more actively pursued short term speculation on the uncertainties encountered in the oil producing regions, which has exaggerated short term price swings and, to some extent, has distorted the equilibrium price of supply and demand. Nevertheless, the Group expects the current price level of crude oil will sustain for a period of time. Going forward, the management will continue to implement various remedial measures in order to minimize the fluctuation of fuel costs to the Group. The Group is also in discussion with Shenzhen Power Supply Bureau on various measures in order to compensate part or all of the increased fuel costs. In the immediate term, the Group is actively pursuing to convert using heavy oil to natural gas as the Group's primary source of fuel to generate electricity at the power plant as natural gas and is expecting to be significantly cheaper source of fuel with substantial less pollution. In view of the location of the power plant is in close proximity to the Guangdong Liquefied Natural Gas Terminal which is expecting to be completed in 2006, therefore the Group's power plant is in an advantageous position to change from heavy oil to natural gas.

Overview on gas business and outlook

On 2 June 2005, the Group completed the acquisition of 58.45% shareholding interest in Panva Gas for a consideration of HK$1,753.0 million payable in issuing new shares of Enerchina at HK$0.69 per share. Panva Gas is principally engaged in the sale and distribution of LP Gas and natural gas (together "Gas Fuel") in the PRC including the sale of LP Gas in bulk and in cylinders, the provision of piped LP Gas and natural gas, construction of gas pipelines, the operation of city gas pipeline network, the operation of Gas Fuel automobile refilling stations, and the sale of LP Gas and natural gas household appliances. The Board considers that Panva Gas will provide a long term and reliable income base for Enerchina.

As the acquisition was completed on 2 June 2005, these interim accounts have consolidated the results of Panva Gas from 2 June 2005 up to 30 June 2005.

For the period from the date of acquisition to 30 June 2005, Panva Gas recorded a turnover of HK$162.0 million with a gross profit margin of 28.8%.

Subsequent to the acquisition, the Group had through various on-market purchased an aggregate of 19,935,000 shares of Panva Gas for a total consideration of HK$62,310,431, equivalent to an average of HK$3.126 per share, representing approximately 2.1% of the issued share capital of Panva Gas. As the results of the acquisition and the various on-market purchases, the Group is currently holding approximately 60.6% shareholding interest in Panva Gas.

Exceptional gain

In the first half of 2005, the Group had completed a disposal of its 41.0% equity interest in Xin Hua Control for a consideration of US$23.5 million, which was equivalent to approximately HK$182.8 million. The Group recorded a gain of HK$95.9 million from the disposal. Xin Hua Control is principally engaged in the business of manufacture and sale of control systems for power plants and large scale manufacturing plants. The Directors are of the view that the disposal is the sale of non-core business and it is in the interest of the Group.

FINANCIAL POSITION

The Group's total borrowings increased from HK$1,305.7 million as at 31 December 2004 to HK$3,205.7 million as at 30 June 2005. The increase of the total borrowings was mainly due to the consolidation of the total borrowings of Panva Gas after the acquisition.

The total borrowings were mainly comprised of bank and other loans amounted to HK$1,226.0 million, and convertible bonds and notes amounted to HK$1,979.7 million. The bank borrowings are mainly used to finance the expansion of the power plant in Shenzhen and the convertible bonds and notes are used for the expansion of gas business in the PRC. The Group's total debt to total capital as at 30 June 2005 was 84.9%.

Total assets pledged in securing these loans have a net book value of HK$218.8 million as at 30 June 2005. All the bank borrowings of the Group are at floating rates and denominated in both Renminbi and United States dollars. The Group operation is mainly carried out in the PRC, substantial receipts and payments in relation to the operations are denominated in Renminbi. No financial instruments were used for hedging purpose other than the interest rate swaps entered into by Panva Gas to hedge the senior notes. However, the Board will continue to evaluate and monitor the potential impact of the appreciation of Renminbi to the Group and manage the risks of using different financial instruments.

The Group's cash and cash equivalents amounted to HK$2,350.1 million as at 30 June 2005 and mostly denominated in Renminbi, Hong Kong dollars and United States dollars.

Contingent Liabilities

A supplier filed an arbitration in August 2003 against Shenzhen Fuhuade Electric Power Co., Limited claiming for additional contract price in the amount of HK$28.0 million. The arbitration is still in progress and the outcome of such cannot be ascertained. No provision for the amount claimed has been made by the Group as at 30 June 2005. Save as the outstanding arbitration, the Group had no material contingent liabilities as at 30 June 2005.

Capital Commitments

As at 30 June 2005, the Group has capital commitments in respect of the acquisition of property, plant and equipment and interest in subsidiaries not provided in the financial statements amounted to HK$96.9 million and HK$35.0 million respectively.

PROSPECTS

As the Group's fourth generating unit with an installed capacity of 180,000 kilowatts was completed and commenced in May 2005, which has brought the Group's total installed capacity to 665,000 kilowatts. The Group expects with the increased in installed capacity, the power plant will further increase the power output in the second half of 2005. The Group will continue to strengthen its remedial policies to mitigate the effect of the rising fuel costs. In addition, the Group will endeavour to reduce operating costs and enhance overall efficiency.

Looking ahead, the Group sees the power sector in the PRC as a challenge. Despite the fact that the demand for electricity in the Guangdong Province as well as the PRC would continue to be strong, the future heavy oil price is still a major determinant of the Group's power sector profitability and the Group considers that the heavy oil price may further increase if the price of crude oil continues to rise. Therefore, the Group has planned to convert the fuel consumption of the power plant from heavy oil to natural gas, a significantly cheaper and cleaner source of fuel. In addition, a significant expansion plan has been put in place to increase the power generation capacity from the Group's exiting total installed capacity of 665,000 kilowatts to 1,450,000 kilowatts.

The Group will continue to explore the opportunities to expand into the coal gasification business and the clean energy sector of the PRC. With the extensive gas distribution network of Panva Gas in the PRC, the management strongly believes it will provide synergies and logistic support for the development of Enerchina's possible future coal gasification business in the PRC.

MAJOR EVENTS

On 24 June 2005, Goodunited Holdings Limited, an indirect wholly owned subsidiary of Enerchina, seized the opportunity to maximize the benefit from the Group's electricity operations by entering into an agreement with Shenzhen Huishen Electric Power Company Limited ("Shenzhen Huishen") to purchase 30% registered capital of Shenzhen Fuhuade Electric Power Co., Limited, an indirect wholly owned subsidiary of Enerchina from Shenzhen Huishen for a total consideration of Renminbi 250.0 million, which was equivalent to approximately HK$233.9 million. The acquisition was completed on 29 July 2005.

INTERIM DIVIDEND AND SPECIAL INTERIM DIVIDEND

The Board has resolved to declare an interim dividend of HK$0.01 (2004: nil) per share and a special interim dividend of HK$0.01 (2004: nil) per share in respect of six months ended 30 June 2005. The interim dividend and the special interim dividend are payable on or before 14 October 2005 to shareholders whose names appear on the register of members of the Company on 7 October 2005.

CLOSURE OF REGISTER OF MEMBERS

The register of members will be closed from Tuesday, 4 October, 2005 to Friday, 7 October, 2005, both days inclusive, during which period no transfer of shares will be registered. In order to qualify for the interim dividend and the special interim dividend, all completed transfer forms together with relevant share certificates must be lodged with the Company's branch transfer office in Hong Kong, Computershare Hong Kong Investor Services Limited, Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:00 p.m. on Monday, 3 October 2005.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SHARES

There was no purchase, sale or redemption of the Company's listed shares by the Company or any of its subsidiaries during the six months ended 30 June 2005.

EMPLOYEES AND REMUNERATION POLICIES

As at 30 June 2005, the Group employed approximately 3,872 full time employees. The Group recognizes the importance of high caliber and competent staff and continues to provide remuneration packages to employees with reference to prevailing market practices and individual performance. In addition, share options may be granted to certain eligible directors and employees of the Group in accordance with the terms of the approved share option scheme adopted by the Group.

AUDIT COMMITTEE

The Group has established an audit committee comprising Messrs. Xin Luo Lin, Lu Yungang and Davin A. Mackenzie being independent non-executive directors of Enerchina.

The audit committee has reviewed the unaudited interim report for the period, and discussed with management the accounting principles and practices and internal controls of the Group.

The interim results of the Group for the six months ended 30 June 2005 had not been audited, but had been reviewed by Enerchina's auditors, Deloitte Touche Tohmatsu and the Audit Committee.

CORPORATE GOVERNANCE

On 1 January 2005, the Code of Best Practices was replaced by the Code on Corporate Governance Practices ("Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). The Company adopted all the code provisions in the Code as its own code on corporate governance practices.

During the period, the Company has complied with the code provisions as set out in the Code with the exception of the following code provision and the considered reason is as follows:–

Code Provision A.4.2 (last sentence)

The code provision A.4.2 of the Code (the last sentence) provides that, every director (including directors with specific terms) should be subject to retirement by rotation at least once every three years.

The Chairman of the Board of the Company was not subject to retirement by rotation at the annual general meeting held on 26 April 2005 in accordance with the provisions of bye-laws before amendment.

To comply with the code provision A.4.2 of the Code, the Company at the annual general meeting of the Company held on 26 April 2005 passed a special resolution to amend its bye-laws so that all directors are now subject to retirement by rotation at least once every three years.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code set out in Appendix 10 to the Listing Rules as the code of conduct regarding securities transactions by the directors. Having made specific enquiry of all directors, the Company confirmed that in respect of the six months ended 30 June 2005, all directors have complied with the required standard set out in the Model Code.

OTHER INFORMATION

Directors' and Chief Executives' interests or short positions in Shares and in Share Options

At 30 June 2005, the interests and short positions of the directors and the chief executive of the Company in the shares of the Company (the "Share") and debentures of the Company or the shares and debentures of any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register maintained by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange of Hong Kong Limited pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers , were as follows: