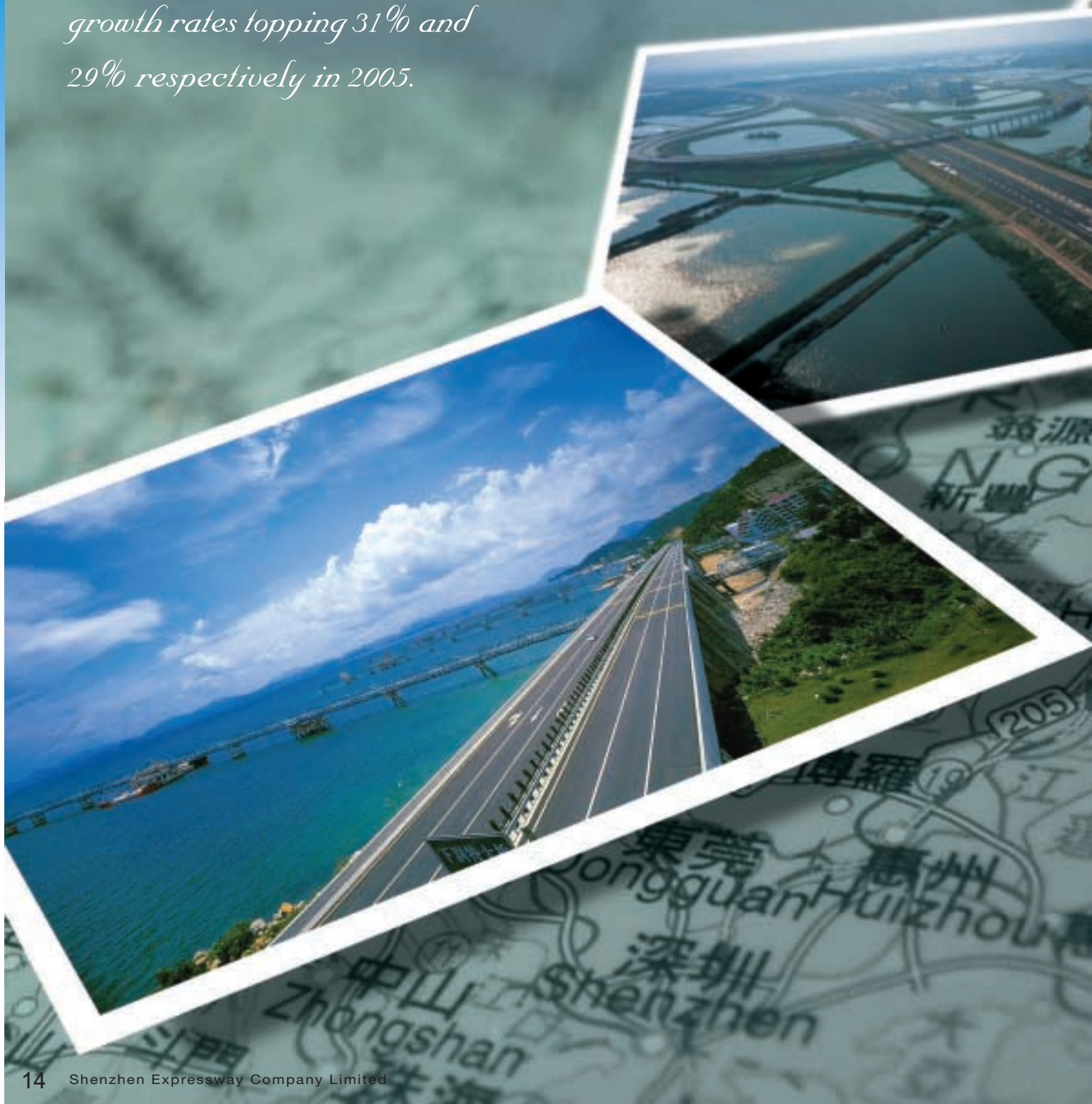


*The traffic flow and toll revenues of the toll highways operated and invested in by the Group recorded average growth rates topping 31% and 29% respectively in 2005.*





# Management Discussion and Analysis

China's economy has been growing speedily and steadily for many years. According to the preliminary statistics released by the National Bureau of Statistics, China's GDP increased by 9.9% in 2005 over the previous year, representing an approximately 10% growth for three consecutive years. Blessed by its favourable policy and geographical proximity to Hong Kong and Macau, the Pearl River Delta region has always been one of the most vibrant areas and is most characterised by a dynamic and export-oriented economy. In 2005, the GDP of Guangdong Province and Shenzhen increased by 12.5% and 15% respectively, higher than the national average, whilst their exports totalled US\$428 billion and US\$182.9 billion respectively, an increase of 19.8% and 24.2% respectively over the previous year. Economic prosperity is set to lead to frequent passenger and cargo flows, which in turn results in rising traffic demand.

Fuelled by internal demands from economic development and the move towards economic globalisation, regional economies are rapidly integrating, coupled with increasing trade exchanges and cooperation between regions. In particular, with the gradual implementation of CEPA and the Pan-Pearl River Economic Circle, the logistics transportation industry of the Pearl River Delta region - a gateway into Hong Kong, Macau and other provinces of China - is growing rapidly. Taking Shenzhen as an example, its port cargo throughput reached 153.51 million tons in 2005, an increase of 13.4% over the previous year; and its containers throughput reached 16.2 million TEUs, an increase of 18.6% over the previous year, enabling Shenzhen to retain the position as the world's fourth largest container port. Cargo and passenger turnovers handled by the whole city increased by more than 20% in 2005 over the previous year.

Economic growth will also drive the pace of urbanisation, resulting in an increase in the number and size of counties and towns as well as in personal income of local residents, all of which in turn push up the demand for public travels in terms of quantity and quality. The Pearl River Delta region had an early and speedy economic startup, leading the nation in terms of number of established counties and towns, population density, personal income level and so forth. According to the figures of GDSTATS.GOV.CN, the per capita disposable income of residents of counties and towns in Guangdong Province amounted to RMB14,770 in 2005, an increase of 8% over the previous year, while the per capita expenditure on the purchase of family cars increased by 95% over the previous year, representing a car ownership rate of 9.7 vehicles per 100 households, an increase of 47.7% over the previous year. Car-related expenditures also surged substantially, and spending on cars has become a major spending hotspot in 2005. In accordance with the White Paper on Composite Management Solutions to Traffic Conditions in Shenzhen City (深圳交通綜合治理工作白皮書) promulgated in March 2006, the total numbers of vehicles in Shenzhen registered in 2002 and 2005 were 461,000 and 813,000, respectively, representing a growth of approximately 75%. As at the end of 2005, the total number of motor vehicles in Shenzhen (including vehicles from other places) amounted to 970,000.

Toll revenue is a major source of the Group's income. Driven by the strong economic growth in China and in particular, the Pearl River Delta and its neighbouring areas, the Group recorded a continued increase in its business. The Board is pleased to announce that the Group achieved a revenue of RMB911,482,000 in 2005 (2004: RMB705,776,000) prepared in accordance with the HKFRS, representing an increase of 29.15% over the same period of the previous year. Profit attributable to equity holders of the Company amounted to RMB552,622,000 (2004: RMB414,888,000). Earnings per share was RMB0.25 (2004: RMB0.19), representing an increase of 33.20% over the same period of the previous year.

## BUSINESS REVIEW AND ANALYSIS

As at the end of the Reporting Period, the Group operated and invested in 18 toll road projects which were either in operation or under construction. General information about each road is set out in Information of Toll Highways attached to this annual report.

### Toll Road Operations

#### Shenzhen Area

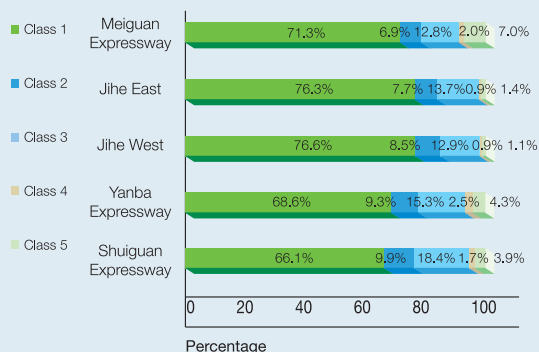
Having benefited from a number of factors such as the robust economic growth in Shenzhen and its neighbouring areas, regional integration and urbanisation during the Reporting Period, the Group continued to maintain a steady growth in traffic flow and toll revenue generated on its various toll roads located in the Shenzhen area.

Toll road	Average daily mixed traffic volume (number of vehicles)			Average daily toll revenue (RMB)		
	2005	2004	Change	2005	2004	Change
Meiguan Expressway	76,343	64,199	18.92%	795,315	707,711	12.38%
Jihe East	56,468	44,446	27.05%	786,573	631,107	24.63%
Jihe West	46,462	35,257	31.78%	739,855	593,856	24.58%
Yanba A and B	11,572	9,427	22.75%	115,139	89,165	29.13%
Shuiguan Expressway	54,747	39,733	37.79%	504,054	382,291	31.85%
Shuiguan Extension*	31,739	N/A	N/A	229,452	N/A	N/A

\* Shuiguan Extension was completed and opened to traffic in July 2005, and tolled from October 2005.

Small vehicles accounted for the main share of traffic flow on Jihe Expressway. Traffic flow of the Class 1 vehicles running on Jihe East and Jihe West increased by 28% and 35% respectively in 2005, contributing significantly to the increase in traffic flow on Jihe Expressway. Traffic flow of Class 4 and 5 vehicles increased by approximately 40% and 60% respectively, remarkably higher than the increase in mixed traffic flow, reflecting the positive impact of the construction and development of industrial centres and logistics parks in the surrounding areas on the operating performance of Jihe Expressway. Yanpai Expressway, a Yantian Port feeder road of Jihe Expressway, is scheduled to be completed and opened to traffic by the middle of 2006 and is set to contribute further traffic growth on Jihe Expressway.

Share of vehicle categories in 2005



During the Reporting Period, Shuiguan Expressway recorded a rapid increase of 38% in its traffic flow over the same period of the previous year as a result of the speedy development of the Longgang Industrial Zone and its neighbouring counties and towns, coupled with the opening of Shuiguan Extension in July 2005. Traffic flow on Shuiguan Expressway only increased by 24% in the first half of 2005 over the same period of the previous year, which demonstrated a strong driving force to traffic flow upon the formation of a highway network. In addition, in the year of its opening, Shuiguan Extension already recorded a daily average mixed traffic flow exceeding 30,000 vehicles, thus suggesting a huge traffic demand from the neighbouring areas as well. Upon the full operation of Nanping Freeway which will connect Shuiguan Expressway and Shuiguan Extension, the improved highway network in the surrounding area is expected to stimulate further traffic growth for Shuiguan Expressway and Shuiguan Extension.

As mentioned in our previous periodic reports, Yanba Expressway's toll revenue under-performed in the short-term due to the absence of a holistic network coverage in the eastern part of Shenzhen. The Company sought to identify a large batch of potential customers through the launch of aggressive marketing activities and to lure traffic flow by providing quality and smooth travel services. Besides, members of the community have been upbeat about the traffic convenience brought about by the opening of Yanba A and B, as construction works in the surrounding areas of the expressway have been increased and vehicles related to construction works have brought additional traffic flow to Yanba Expressway. As a result, the rate of increase in toll revenue of Yanba Expressway in 2005 was higher than the average rate of increase of roads in the Shenzhen area. The construction of Shenhui Coastal Expressway in Huizhou has already commenced, and Yanba C is scheduled to be completed corresponding with Shenhui Coastal Expressway. With increased development in the eastern part of Shenzhen and Huizhou and an improving highway network forthcoming, Yanba Expressway is expected to continue to enjoy a growth in traffic flow and toll revenue.

In 2005, Meiguan Expressway was able to maintain a growth in traffic flow and toll revenue but the growth began to slow down, partly because the expressway was entering a mature phase of its operation. Furthermore, since the middle of the year, the reconstruction works of a municipal road connecting with Meiguan Expressway had affected the travel efficiency on the connected section, forcing large trucks to switch to other roads. The opening of Shuiguan Extension has also diverted some traffic to Shuiguan Expressway.

While Yanpai Expressway, Nanguang Expressway and Longda (Longhua - Dalingshan) Expressway have been completed and opened to traffic, and improvements are being made to the highway network in the Dongguan and Huizhou areas, traffic flows on the various toll roads in Shenzhen are expected to be redistributed. In light of the sound economic environment in Shenzhen and its neighbouring areas, the management remains optimistic about the overall growth in traffic flow on the toll roads in the region.

#### **Other Areas**

To increase its market share and to enhance its position and influence in the sector, the Company has capitalised on the opportunity arising from the disposal of equity interests in toll road projects by Guangdong Province and other provinces over the past two years and has been undertaking active participation in toll road project investments beyond Shenzhen.

Listed below are operational toll road projects invested in by the Company in Guangdong Province, together with their operating performance details:

<b>Toll road</b>	<b>Percentage of equity interest</b>	<b>Daily average mixed traffic volume (numbers of vehicles)</b>	<b>Daily average toll revenue (RMB)</b>	<b>Date of commencement of operation</b>
Yangmao Expressway	25%	10,362	546,907	November 2004
Guangwu Expressway	30%	6,120	164,830	December 2004
Jiangzhong Expressway	25%	6,563	200,847	November 2005
Qinglian Highway	56.28%	16,459	364,449	—

Yangmao Expressway, Guangwu Expressway and Jiangzhong Expressway, in which the Company does not have controlling interests, have not contributed substantially to the Company's revenues and profits at the moment since they are still at the initial stage of operation. Blessed by the sound macro-economic environment, these expressways showed a sign of growth in both traffic flow and toll revenue. Among the three, Yangmao Expressway outperformed and recorded increases of 27% and 39% in daily average traffic flow and toll revenue, respectively, in 2005 compared to the month when operation commenced. The commencement of operation of the Guangdong section of Yuzhan (Chongqing - Zhanjiang) Expressway at the end of 2005 will further enhance the operating performance of Yangmao Expressway in future. Guangwu Expressway recorded a slight growth in daily average toll revenue in 2005 against the period of initial stage of operation, which is within the Company's expectations. Upon completion of the Guangwu Phase II (under planning) connecting with its western end, Guangwu Expressway, which forms an integral part of an express passage linking the Pearl River Delta with Guangxi and southwestern provinces, is expected to have an improved performance. Jiangzhong Expressway, once operated, has shortened the traveling distance between the eastern and western parts of the Pearl River Delta (with Guangzhou as centre) by almost 80 km. Jiangzhong Expressway is expected to see steadily rising traffic flow and toll revenue.



Located in the northern part of Guangdong Province, Qinglian Class I Highway covers a total mileage of 215.85 km and serves as a major passage linking the Pearl River Delta with the central and northern parts of Guangdong Province, Hunan Province and other central regions, offering an advantageous strategic location. However, the highway fails to satisfy current and future traffic needs due to poor road surface conditions. Qinglian Highway recorded fair operating performance as a whole during the Reporting Period. The Company invested in this project mainly for the purpose of reconstructing it into an expressway to fully capitalise on its existing routing and its role as an essential corridor. Upon completion of the project, the reconstructed Qinglian Class I Highway will connect with the highway network in the Pearl River Delta via Guangqing (Guangzhou - Qingyuan) Expressway in the south, and with Jingzhu (Beijing - Zhuhai) Expressway in the north via the Lianzhou-Yizhang section. It will also interconnect with the latest-planned Erguang (Erliahaote - Guangzhou) Expressway, Jingzhu Expressway Dual Lane and Shankun (Shantou - Kunming) Highway, forming an essential route linking the northern and southern highway framework in Guangdong Province and enhancing the trading and economic activities from the Pearl River Delta region towards the central areas. The reconstruction project will generate promising investment returns for the Group and presents a major strategic significance to the Group's growth. Please refer to the section of "Project Construction and Management" on page 20 of this annual report for relevant details in the reconstruction progress of Qinglian Class 1 Highway.

The Group has invested in toll road projects in areas outside Guangdong Province, which include Wuhuang Expressway and Geputan Bridge in Hubei Province, Changsha Ring Road in Hunan Province and Nanjing Third Bridge in Jiangsu Province, in which the Group owns equity interests of 55%, 42%, 51% and 25% respectively.

Wuhuang Expressway covers a total mileage of 70.3 km, which is a highway trunk connecting with Wuhan and Huangshi and exiting from eastern part of Hubei Province, and also forms an integral part of Hurong (Shanghai - Chengdu) National Highway and commands a superior and strategic location. Wuhuang Expressway recorded a daily average mixed traffic flow of 22,895 vehicles and a daily average toll revenue of RMB728,039 during 2005, up approximately 10% and 17% respectively over 2004. Wuhuang Expressway's satisfactory operating performance was attributable to the economic growth and improving highway networks in Hubei Province. Besides, certain toll rates for trucks have increased in actuality as a result of the government's measures against vehicle overloading, and so the rate of increase in Wuhuang Expressway's toll revenue was higher than that in traffic flow for the same period. Nanjing Third Bridge was opened to traffic in October 2005, about two years ahead of schedule. Its daily average mixed traffic flow and daily average toll revenue amounted to 8,276 vehicles and RMB324,889 respectively in the first three months since its opening. Changsha Ring Road and Geputan Bridge did not have satisfactory operating performance during the Reporting Period, recording daily average mixed traffic flow of 5,393 and 2,730 vehicles respectively. However, they did not have a major impact on the Group's overall operating performance, given that their revenues accounted for only approximately 1% of the Group's total revenue.

#### ***Toll Policy and Others***

Pursuant to the "Notice Concerning Adjustments of the Toll Rates of Vehicles on Expressways" jointly issued by Guangdong Provincial Price Index Bureau (廣東省物價局) and Guangdong Provincial Communications Department (廣東省交通廳), from 1 June 2005 the toll coefficient for Class 5 vehicles traveling on Meiguan Expressway and Jihe Expressway was amended from 6 to 5, representing an approximately 16.7% decrease; the toll coefficient for Class 5 vehicles traveling on Yanba Expressway, Shuiguan Expressway, Yangmao Expressway and Guangwu Expressway was amended from 4 to 3.5, representing an approximately 12.5% decrease; while the toll coefficients for Class 1 to 4 vehicles traveling on all expressways remain unchanged. Considering that toll revenues from Class 5 vehicles account for a small proportion of the Group's total revenues, and the decrease in toll rates will have positive effect on traffic flow, the aforesaid changes did not have a material impact on the Group's revenues or profits. A toll-by-weight pilot scheme for Guangdong Province is being tried out but not throughout the province yet.

In 2005, toll standards were already revised in Hubei Province, Hunan Province and Jiangsu Province pursuant to the instruction of the Ministry of Communications. The Company's toll standards applicable to its highway projects in these provinces are set out in the Information of Toll Highways attached to this annual report. The toll-by-weight system will be implemented in Hubei Province in April 2006, which is expected to be conducive for the operating performance of Wuhuang Expressway.

#### ***Operation and Management***

The Group has timely adjusted the focus of work on its toll road operation in the recent two years in response to the impact brought about by various changes: improved highway networks, implementation of inter-road network toll collection and the Company's expansion on external investments. On the one hand, the Group has worked to ensure that its toll revenue target would be achieved through stepping up the analysis of highway networks and the marketing activities aimed at specific vehicles. On the other hand, it has enhanced the management of the enterprises in which the Group invested to help achieve returns from the investments through strengthening the development and training of assigned management staff. Furthermore, in respect of the implementation of the inter-road network toll collection project, the Company has taken relevant measures such as continuously reviewing and improving the management system and operation rules, organising training for toll collection staff, and maintaining close liaison with relevant management authorities to ensure that toll revenues would be distributed timely and accounted for safely, so that the Company's operating objectives would be smoothly achieved.

### Project Construction and Management

The Company is currently carrying out the construction of Yanpai Expressway and Nanguang Expressway as well as preliminary preparation work on Yanba C. For Yanpai Expressway, as per the progress of the physical completion of the project, an accumulated amount of approximately RMB915 million had been utilised as construction costs as at the end of the Reporting Period, representing approximately 80% of the estimated investment. Foundation, bridge-culvert and tunnel works have basically been completed. As for Nanguang Expressway, land requisition, demolition and relocation are underway, while tenders have already been invited for the construction of some sub-contracted sections of the expressway. Constructions on the main roads of the two expressways are scheduled for completion by the middle of 2006 and by the end of 2007 respectively. For Yanba C, the preliminary design has been reviewed and the Municipal Environmental Protection Bureau has given a reply in respect of the environmental assessment report. With a construction plan being drawn up, the project is scheduled for completion concurrently with Shenhui Coastal Expressway, now under construction in Huizhou. Meanwhile, for GZ W2 Expressway, a project being constructed by an associated company, an accumulated amount of RMB1,434 million had been utilised as construction costs representing approximately 48% of the estimated investment. The whole project is scheduled for completion by the first half of 2007.



Six expressways have been planned for development by the Shenzhen Municipal Government in Shenzhen, with the proprietary development right of only Exterior Ring Expressway 6 being unconfirmed. A proprietary tendering scheme is being implemented across Guangdong Province pursuant to the requirements of the “Toll Road Management Regulations” and relevant legislations, under which the development rights to the toll highway projects should be determined by way of bidding in government tenders. The Shenzhen Municipal Government had granted the Company the first right of refusal to develop the planned expressways in Shenzhen in 1997. While pursuant to the requirements of the “Toll Road Management Regulations” and relevant legislations, a public tender announcement on the development right to Exterior Ring Highway has recently been published by the Shenzhen Municipal Government, and the Company is actively participating in the tenders to strive for the proprietary right to the project, in an attempt to further consolidate the Company’s share of the toll highway sector in Shenzhen and to earmark quality highway projects for the Company’s long-term, stable development.

The reconstruction of Qinglian Class I Highway into an expressway proceeded smoothly during 2005. Senior management members and key technical and management staff of the Company have been assigned to set up a construction management head office to actively push forward relevant work. Tenders have been invited for project designs and for the construction of the project management office. Land requisition, demolition and relocation is all underway as well. The reconstruction of an experimental section started in full wing in December 2005, marking the commencement of a special research on foundation works and laying a sound platform for achieving the objective of successfully completing Qinglian Expressway and opening it to traffic in 2008.

The reconstruction of Qinglian Class I Highway and the construction of Nanguang Expressway are the Company’s key construction management projects in the next three years. On the premises of accomplishing the objectives on quality, safety and environmental protection, to complete the projects on schedule is key to reducing project financial expenses and management costs and to assuring investment returns, which will lay a good foundation for the Group to achieve exponential growth in operating scale and operating results according to its established objectives. To such end, the management highly values the construction and management of these projects and will step up controls over phase-by-phase objectives and on-site management through assigning accountabilities to specific positions. Apart from full support in terms of funds and human resources that the Company has given to the project, two project competitions have also been organised and a special incentive scheme has been devised to specify rules for rewarding and penalising staff, with an aim to promote and ensure the achievement of the overall objectives of the projects by mobilising the enthusiasm and sense of responsibility of project managers.

## Project Acquisitions

In 2005, the Company acquired 30% equity interest in Guangwu Expressway, 56.28% equity interest in Qinglian Project and 55% equity interest in Wuhuang Expressway. The operations of these projects during the Reporting Period have been described in the preceding paragraphs. Details of the relevant transactions are set out in “Connected Transactions” of the Report of the Directors on page 63 of this annual report.

Since 2004, the Company’s management has been implementing the development strategies and objectives devised by the Board and actively proceeding with investment in and acquisition of quality toll highway projects. As such, the Group’s business has expanded from Shenzhen to Guangdong Province and other areas across the PRC, recording a breakthrough increase in total equity-based mileage of the Group’s toll highways at the end of 2005 as compared to the end of 2003.

To increase its control over the Qinglian Project and to enhance its management of the operation and project construction of Qinglian Company so that a smooth and efficient reconstruction of Qinglian Class I Highway will be facilitated, the Company entered into an agreement with the liquidation committee of Qingyuan Yueqing Highway Construction and Development Co., Ltd. on 8 February 2006 for a proposed further acquisition of 20.09% equity interest in Qinglian Company at a consideration of RMB484 million.

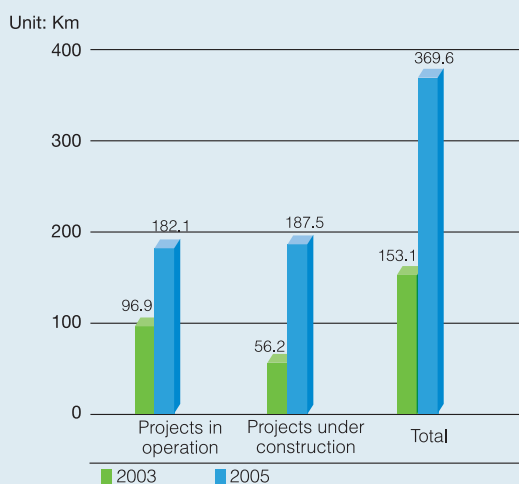
This transaction is subject to the approval of independent shareholders at a shareholders’ meeting pursuant to the Listing Rules of the HKEX. Should the acquisition be completed, the Group will own a total of 76.37% equity interest in Qinglian Company, and the Group will be entitled to appoint 12 out of 15 directors of Qinglian Company. From an accounting viewpoint, Qinglian Company will change from the status of an associate to a subsidiary of the Group, and its operating results will be consolidated into the Group’s financial statements. This will help the Group to further strengthen its operating scale and to expand its income base.

In view of the rapidly expanding investment size and the substantial proportion of projects-in-progress within the Company’s existing investment portfolio, the Company will be even more prudent than before in decision making as regards project investment and acquisition. The management has recently focused on the integration of existing resources and will conduct a thorough assessment of the impact of new projects on the development of the Company as a whole, as well as the impact on the compatibility of these projects with the Company’s strategic objectives and on the security of the Company’s financial resources. Such assessment work aims to further rationalise the Company’s investment portfolio to enhance the overall returns of the projects.

## Entrusted Construction Management – Business of “Entrusted Construction System”

Entrusted Construction Management refers to the government’s selection and appointment of private companies specialising in project management to organise, implement and manage the construction of government-invested projects. Under the entrusted construction management system, the entrusted administrator provides construction management services to the government for a management fee. Generally, the management fee is charged on a balance-of-cost basis, and the administrator is responsible for any breach of contract in respect of construction costs, construction schedules and quality within the scope of entrustment as agreed in the contract.

Over the past decade, the Group has built extensive experience in highway construction and management, and has earned a reputation for assuring reliable quality and for its professional capabilities in controlling budgets and work schedules, which are the Group’s advantages and assets for competing in the Entrusted Construction Management sector.





The Company has been appointed by the government as administrators for Nanping Project and Hengping Project in 2004. As at the end of the Reporting Period, as per the progress of the physical completion, an accumulated amount of approximately RMB1,908 million had been utilised as construction costs in Nanping Project. The western section was opened to traffic on 3 December 2005 while the whole project is scheduled for completion by the first half of 2006. During the Reporting Period, Nanping Project contributed a profit of approximately RMB59,968,000 to the Company, which is within the Company's expectations. Based on the management's reasonable and prudent expectations, the project will still generate management income in phases for the Company in the next two years. Hengping Project is lagging behind schedule due to land requisition, demolition and relocation works, and the whole project is scheduled for completion by 2007. As at the end of the Reporting Period, as per the progress of the physical completion, an accumulated amount of approximately RMB137 million had been utilised as construction costs in Hengping Project, representing approximately 30% of estimated investment. As the Company is not required by the agreement to be responsible for land requisition, demolition or relocation, the Company's performance in accordance with the construction schedules as stipulated in the agreement will not be affected.

In 2006, new progress was made in the Company's entrusted construction management business. Pursuant to the contract entered into with the Shenzhen Communications Bureau (representing the Shenzhen Municipal Government), the Company has been appointed as project administrator for the Wutong Mountain Avenue (Supplementary Road) and Jihe Expressway Yantian Subsidiary Road Checkpoint Station Project in Shenzhen. This project is an auxiliary project of Yanpai Expressway, with a construction budget of approximately RMB254 million, subject to finalisation by the Shenzhen Municipal Audit Bureau. Pursuant to the contract terms, the Company's management income is to be determined by the project costs savings: if the final savings of project costs or any deficit was to fall within 2.5% of the estimated construction budget, then the savings or the deficit amount would be credited to or borne by the Company. If the savings or the deficit was greater than 2.5% of the estimated construction budget, the portion of savings or deficit that exceeded 2.5% would be equally shared or borne by the Company and the Shenzhen Communications Bureau.

The Entrusted Construction System is now being widely promoted and applied to the management of government-invested projects, and is becoming more transparent and market-oriented, offering a favourable opportunity for the Group to develop entrusted construction management business through the utilisation of its engineering management expertise and experience, which will become a new income base for the Group in the next few years.

### Other Businesses and Matters

The Company invests in an advertising company which is engaged in the businesses of billboard leasing, advertising agency, design production and related services, utilising land-use rights alongside the Company's toll highways and toll stations. During the Reporting Period, the Advertising Company recorded a revenue of RMB10,914,000 and a profit of RMB2,705,000.

The Company has established Consulting Company together with certain engineering and technical personnel as primary shareholders to develop businesses such as project management consultancy, information technology consultancy, engineering consultancy, and construction costs consultancy and tendering agency. Preliminary progress has been made by Consulting Company in its current efforts to expand the markets in Shenzhen and the Pearl River Delta. In 2005, Consulting Company recorded a revenue of RMB12,010,000 and a net profit of RMB656,000.

The Wutongling Ropeway project remains suspended. In line with the spirit of the relevant meetings of the Shenzhen Municipal Government, the government has decided to cancel the project and offered suitable compensations to investors based on the audit findings of the Shenzhen Municipal Audit Bureau. Part of the impairment provisions made for the project in previous periods was hereby written back during the Reporting Period. Please refer to note 9(b) to the financial statements.

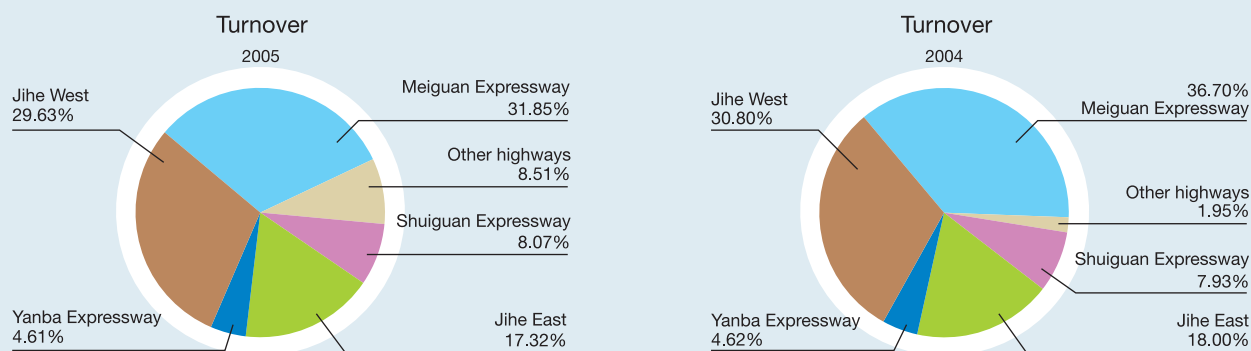
## ANALYSIS OF OPERATING RESULTS

Principal financial indicator (RMB'000)	2005	2004 (restated)	Change
Turnover	911,482	705,776	29.15%
Operating expenses	298,135	259,588	14.85%
Operating profit	766,916	523,483	46.50%
Share of profit/(loss) of associates	(24,015)	(706)	N/A
Finance costs	100,621	24,052	318.34%
Profit attributable to the equity holders of the Company	552,622	414,888	33.20%

### Turnover

During 2005, the Group recorded turnover of RMB911,482,000, representing an increase of 29.15% as compared to 2004. Among such increase, Meiguan Expressway, Jihe East, Jihe West, Yanba Expressway, Shuiguan Expressway and Changsha Ring Road recorded increases of 12.07%, 24.29%, 24.24%, 28.78%, 31.49% and 5.38% respectively. Wuhuang Expressway was consolidated with the Group's financial statements since August 2005. Excluding this new project, the Group recorded an increase of 20.12% in turnover as compared to the previous year.

### Composition of Turnover



During the Reporting Period, benefited from the continuous growth of the PRC economy and the increase in the number of vehicles, the source of growth in the Group's turnover was mainly from the increase of traffic flow on the Group's major toll highways. The composite traffic flow of the Group's toll highways recorded an overall increase of 30.95% as compared to the previous year. Without taking into account the effect brought by Wuhuang Expressway, the composite traffic flow of the Group's toll highways increased by 26.15% as compared to the previous year. Due to the slight increase in the proportion of small vehicles in the Group's toll vehicle composition as compared to the corresponding period of the previous year, and the moderate decrease in the toll coefficient for Class 5 vehicles since 1 June 2005 (Please refer to "Business Review and Analysis" on page 19 of this annual report for details), and without taking into account the effect brought by the newly acquired Wuhuang Expressway, the average toll revenue per vehicle for the Group's toll highways dropped slightly by 3.83% as compared to the previous year. As a result, the growth rate of toll revenue was slightly lower than that of traffic flow for the Reporting Period.

Toll highway	Average toll revenue per vehicle (RMB)		
	2005	2004	Change
Meiguan Expressway	10.42	11.02	-5.50%
Jihe East	13.93	14.20	-1.90%
Jihe West	15.92	16.84	-5.46%
Yanba Expressway	9.95	9.46	5.20%
Shuiguan Expressway	9.21	9.62	-4.31%
Changsha Ring Road	10.81	11.93	-9.41%
Geputan Bridge	7.27	7.97	-8.77%
<b>Subtotal</b>	<b>11.90</b>	<b>12.37</b>	<b>-3.83%</b>
Wuhuang Expressway *	31.80	27.86	14.15%
<b>Total</b>	<b>12.67</b>	<b>12.37</b>	<b>2.38%</b>

\* Presented in terms of year-on-year figures

## Taxes on Turnover

In accordance with the “Notice Concerning Policies Regarding Business Tax on Toll Fee Income of Highway Operation Enterprises by the Ministry of Finance and the State Administration of Taxation” jointly promulgated by the Ministry of Finance and the State Administration of Taxation, starting from 1 June 2005, the business tax on the Group’s toll revenue derived from expressways has been reduced to 3% (before adjustment: 5%). Hence during the Reporting Period, the rate of increase in business tax and surcharges was lower than the rate of increase in turnover.

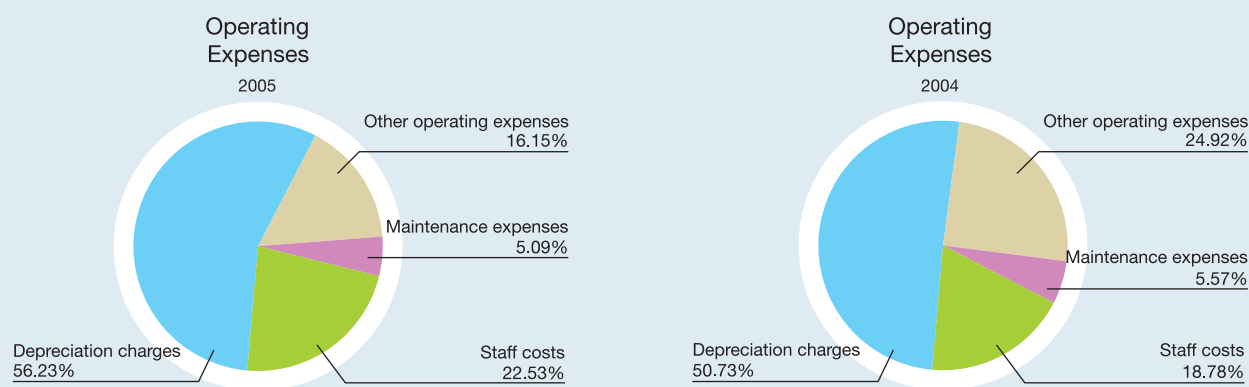
## Operating Expenses

Due to the growth in traffic flow on the Group’s major toll highways and the increase of operating expenses in relation to new projects during the Reporting Period, operating expenses of the Group during the Reporting Period amounted to RMB298,135,000, representing an increase of 14.85% as compared to the previous year, among which:

- as a result of traffic growth, depreciation charges increased by 27.30% as compared to the corresponding period of the previous year to RMB167,634,000.
- employee benefit expenses increased by 37.78% as compared to the previous year to RMB67,163,000, mainly due to the increases in toll stations and toll collection staff as a result of traffic growth, rise of wage standards on toll collection staff and the provision of incentive cash bonus under the share appreciation rights scheme of RMB4,412,000 during the Reporting Period.
- road maintenance expenses increased by 5.05% as compared to the corresponding period of the previous year to RMB15,181,000 due to the growth of traffic flow and aging of roads, which led to more resources put on maintenance to ensure good road conditions and traffic environment. However, maintenance expenses in general accounted only for a small percentage of toll revenue. Currently, various toll highways of the Group are in good conditions and no major overhaul is scheduled in the coming two years.

- Other operating expenses decreased by 25.57% as compared to the previous year to RMB48,157,000. During the Reporting Period, there were new expenses of settlement service charges incurred for the new inter-road network toll collection system of Guangdong Province, and business expenses on new projects also increased as compared to the previous year, but other operating expenses decreased as compared to the previous year mainly due to the write-back of impairment provision of RMB40 million for the ropeway project made in previous years.

### Structure of Operating Expenses



### Other Revenues

During the Reporting Period, the Group's other revenues increased by 67.10% as compared to the previous year to RMB191,930,000, mainly represented by:

- A bank deposit interest income of RMB9,798,000, representing a decrease of 21.26% as compared to the previous year.
- Interest income of RMB13,054,000 in respect of long-term receivables discounted in connection with the disposal of two Class 1 highways being recognised in this period (2004: RMB35,779,000), representing a decrease of 63.51% over the previous year.
- A discounted interest income of RMB6,315,000 derived from advances made to Qinglong Company.
- An income of RMB34,955,000 recognised in respect of the recognition of the excess of fair value of share of the acquired net assets of jointly controlled entity, JEL Company, over the cost of acquisition.
- An income of RMB27,356,000 (2004: RMB35,708,000) recognised during the Year in respect of government subsidies for Yanba Expressway, representing a decrease of RMB8,352,000 over the previous year.
- During the Year, the Company received subsidies of RMB10,309,000 granted by the Shenzhen Municipal Government in relation of the cancellation of certain preferential policies on the income tax of the Group.
- During the Reporting Period, an income of RMB72,830,000 was recognised according to the completion progress in respect of the entrusted construction management service, representing an increase of RMB54,962,000 over the previous year. Among such income, an income of RMB67,323,000 was recognised for the entrusted construction management service provided to Nanping Project, while an income of RMB5,507,000 was recognised for the entrusted construction management service provided to Hengping Project. The profit recognised during the Reporting Period for the entrusted service provided to Nanping Project amounted to RMB59,968,000. As the outcome of Hengping Project could not be estimated reliably, and the Directors believe that future reimbursements of administration expenses incurred relating to this project were probable, the Company recognised income and expenses for the project on the basis of actual administration expenses of RMB 5,507,000 incurred during the Reporting Period. No profit was accounted for during the Reporting Period.

# Management Discussion and Analysis

## Operating Profit

As a result of growth in toll revenues and other revenues, the Group recorded an operating profit of RMB766,916,000 during the Reporting Period, representing an increase of 46.50% as compared to the previous year. During the Reporting Period, operating profit margin of toll highway (excluding government allowance) was 68.57%, representing an increase of 2.21 percentage points over the previous year, which was mainly attributable to the decrease in business tax rate in the Reporting Period.

## Share of Profit of Associates

During the Reporting Period, the Group's share of results of associates amounted to RMB-24,015,000, including the share of profits or losses after tax of Yangmao Company, Guangyun Company, Jiangzhong Company, Huayu Company, Nanjing Third Bridge Company, Consulting Company and Qinglian Company. The information on associates is set out in Note 11 to the financial statements.

## Earnings before Interest and Tax ("EBIT")

During the Reporting Period, contributions by the Group's principal activities to EBIT were as follows:

Principal activities	(Unit: RMB'000)			
	2005	2004	Change (amount)	Change (%)
Meiguan Expressway	213,360	184,105	29,255	15.89%
Jihe East	117,535	94,907	22,628	23.84%
Jihe West	211,339	166,480	44,859	26.95%
Yanba Expressway	25,193	31,948	(6,755)	-21.14%
Shuiguan Expressway	42,913	33,580	9,333	27.79%
Other highways (Note 1)	5,992	2,645	3,347	126.54%
Highway-related business (Note 2)	157,889	67,076	90,813	135.39%
<b>Subtotal</b>	<b>774,221</b>	<b>580,741</b>	<b>193,480</b>	<b>33.32%</b>
Unallocated expenses of the Group	(31,320)	(57,964)	26,644	-45.97%
<b>Total</b>	<b>742,901</b>	<b>522,777</b>	<b>220,124</b>	<b>42.11%</b>

Note 1: Other highways included Wuhuang Expressway, Changsha Ring Road, Geputan Bridge and the highways operated by associates.

Note 2: Income from highway-related businesses consisted of income on project management fees from government-entrusted construction management services, income from Advertising Company, income generated from the acquisition of a jointly controlled entity, discounted interest income from installment payment collections, bank deposit interest income and subsidies from government, etc.

## Finance Costs

During the Reporting Period, the Group's finance costs amounted to RMB100,621,000, representing an increase of 318.34% as compared to the previous year. Such increase was mainly attributable to the increased scale of borrowings as compared to the previous year.

### Change of Accounting Policies

During the Year, the Group has changed certain accounting policies in accordance with the new and revised HKFRS that are effective for accounting period commencing on or after 1 January 2005. The major impact of the changes to the accounting policies of the Group and the adoption of such new policies are as follows:

- The proportionate consolidation approach under HKAS 31 “Interests in Joint Ventures” is adopted to account for the interests in jointly controlled entities. In the previous years, the interests in jointly controlled entities of the Group were accounted for using the equity method of accounting. After the adoption of the new policy, the Group has restated the 2004 comparative figures. However, earnings per share and retained earnings remained unaffected.
- Adoption of HKAS 39 “Financial Instruments: Recognition and Measurement”: The accounting policies in respect of loans and receivables and long-term liabilities have been changed such that these instruments are initially stated at fair values and subsequently measured at amortised costs using the effective interest method. According to the standard, the recognition, derecognition and measurement of financial assets and liabilities are not applied retrospectively. But the amount of resulting adjustments should be recognised as an adjustment of retained earnings at the beginning of the Reporting Period. Adoption of such policy led to a decrease of RMB11,342,000 of retained earnings at the beginning of the Year. During the Reporting Period, an other income of RMB6,315,000 recognised using the effective interest method in respect of loan to a jointly controlled entity. As to the impact on long-term liabilities, the Directors consider that such amount does not have material impact on the financial statements, so no relevant adjustment was made.
- Adoption of HKFRS 3 “Business Combination”: The amortisation of goodwill was ceased from 1 January 2005, and from the year ended 31 December 2005 onwards, goodwill is tested annually for impairment as well as there is indication of impairment. In the previous years, goodwill was amortised on a straight-line basis over its estimated useful life or 20 years, whichever is shorter, and assessed for an indications of impairment at each balance sheet date. The change of this accounting policy is applied prospectively. The retained earnings at 1 January 2004 remain unaffected.
- Adoption of HKAS 17 “Leases”: The land use rights are reclassified as operating leases and are amortised over their useful lives using the straight-line method. In the previous years, the land use rights were classified as property, plant and equipment and were amortised using the units-of-usage method. According to the requirement of the standard, such change in accounting policy is required to be applied retrospectively and the retained earnings at 31 December 2004 was reduced by RMB59,541,000 as a result.



Details about the impact of adopting the new or revised HKFRS on the Group are set out in Note 2.1 to the financial statements on page 88 to page 93 of this annual report.

## ANALYSIS OF FINANCIAL POSITION

### Non-current Assets

The Group is principally engaged in the operation of toll highways and its non-current assets comprise mainly fixed assets investment, equity investment and debt investment in high-grade toll highways. As at 31 December 2005, the Group's non-current assets amounted to RMB8,993,846,000 (2004: RMB5,813,760,000), representing an increase of 54.70% as compared to the beginning of the Year. Such increase was mainly attributable to the increase in investment expenditures on Qinglian Project, Wuhuang Expressway, Yanpai Expressway, Guangwu Expressway, Jiangzhong Expressway, GZ W2 Expressway, etc. during the Reporting Period, which included increase in construction in progress of RMB406,859,000, interests in associates of RMB2,096,205,000 and intangible assets of RMB817,770,000. New investments made during the Reporting Period will become new sources of profit growth for the Group in the future. Details of the new investments made during the Reporting Period are set out in the "Business Review and Analysis" on pages 16 to 22 of this annual report.

### Current Assets and Liabilities

As at 31 December 2005, the Group's current assets amounted to RMB1,085,469,000 (2004: RMB1,714,003,000), including cash and cash equivalents of RMB892,485,000, restricted cash of RMB31,615,000 and accounts and other receivables of RMB157,829,000. During the Reporting Period, the Company received the balance of consideration of RMB386 million for the transfer of ownerships in two Class 1 highways in previous years. As such, the accounts receivable arising from the transfer of the two Class 1 highways had been fully received.

The cash of the Group is generally placed in commercial banks as current or short term fixed deposits. No deposit is placed with financial institutions other than banks or used for securities investment.

As at 31 December 2005, the Group's current liabilities amounted to RMB956,536,000 (2004: RMB883,556,000), including RMB253,900,000 as short-term borrowings, RMB16,208,000 as long-term liabilities due within one year, RMB141,760,000 as construction costs payable and deposits, RMB27,901,000 as performance bonds and RMB384,062,000 as balances outstanding for the acquisition of equity interests in Qinglian Company and JEL Company under the agreements. On the basis of the Group's existing liquidity position and the Group's arrangements and plans on future cash flow, the Group expects to have adequate funds for satisfying the relevant payments.

### Equity

As at 31 December 2005, total equity for the Group amounted to RMB6,372,759,000 (2004: RMB6,068,765,000), representing an increase of RMB303,994,000 as compared to the beginning of the Year. Such increase was mainly attributable to the increase of RMB552,622,000 as the profit attributable to the Company during the Year and the deduction of RMB239,877,000 as the distribution of dividend of 2004.

### Non-current Liabilities

As at 31 December 2005, non-current liabilities of the Group amounted to RMB2,750,020,000, which included the following:

- Long-term borrowings amounted to RMB2,230,602,000, including bank borrowings of RMB2,195,795,000, the Spanish government loans of RMB25,243,000 (excluding the portion due within one year) and minority shareholders' advance of RMB9,564,000.
- Deferred tax liabilities amounted to RMB155,030,000. The Group's net deferred tax liabilities amounted to RMB148,266,000, comprising deferred tax credits of RMB86,049,000 and RMB88,751,000 respectively arising from the temporary differences between the carrying amount of toll roads and toll road operating right and their tax bases and deferred tax debits of RMB26,534,000 in respect of the provision for impairment losses for investments in the Wutongling Ropeway Project and Shenchang Company.
- The balance of government subsidies amounted to RMB364,388,000, which included the subsidies of RMB291,408,000 paid by the relevant government bodies to subsidise the insufficient traffic flows on Yanba Expressway owing to its early completion in accordance with the overall township planning requirements of the Shenzhen Government (The subsidies are recognised annually in the income statement pursuant to the accounting policy of the Group within the duration of the operation franchise to Yanba Expressway), and a fund provided to Yanba Expressway by the Ministry of Communications amounting to RMB54,000,000 that is non-interest bearing with no fixed repayment terms, and a special financial allocations of RMB18,980,000 granted by the Ministry of Finance for the construction of Yanpai Expressway.

### Contingent Liabilities

According to the construction management contracts of Nanping Project and Hengping Project, the Company shall bear the management responsibility for overrun costs. For Hengping Project, the Company shall be liable for all the costs exceeding the budgeted costs of the project. For Nanping Project, if the actual construction cost exceeds the budgeted construction costs by 2.5% or less, the Company shall bear all the cost exceeding such budgeted cost of the project. If the overrun costs are more than 2.5%, the Company together with the relevant government department shall bear the portion that exceeds the 2.5% threshold. In addition, pursuant to the requirements of the contracts, the Company has provided to the Longgang Highway Bureau and the Shenzhen Communications Bureau with irrevocable letters of bank guarantee in the amount of RMB30 million and RMB100 million respectively. A deposit of RMB15 million has been paid to the Longgang Highway Bureau to guarantee the achievement of agreed progress of construction, quality and safety management of Hengping Project.

### Cash Flow of the Group

As at 31 December 2005, the Group's cash and cash equivalents amounted to RMB892,485,000 (2004: RMB1,241,838,000), representing a decrease of RMB349,353,000 as compared to the beginning of the Reporting Period.

During 2005, the Group's net operating cash inflows amounted to RMB564,752,000 (2004: RMB470,487,000), representing an increase of 20.04%. Such increase was mainly attributable to the continuous growth in toll revenue from the major toll highways operated by the Group during the Reporting Period. During the Reporting Period, the net increase of borrowings of the Group was RMB1,691,113,000, and the remaining balance of RMB386,000,000 from the disposal of two Class 1 highways and a special financial allocation to Yanpai Expressway from the government amounting to RMB18,980,000 were received.

During the Reporting Period, the Group's main cash outflows comprised capital expenditure of RMB2,793,516,000 on Yanpai Expressway, Nanguang Expressway, Qinglian Project, Jiangzhong Expressway, GZ W2 Expressway, Guangwu Expressway, Wuhuang Expressway, etc.(excluding interests capitalised) as well as the payment of dividend and interest of RMB328,869,000 in total.



## Capital Structure

As at 31 December 2005, the Group's debt-to-asset ratio (total liabilities/total assets) was 36.77% (2004: 19.38%), net borrowings-to-equity ratio ((total borrowings-cash and cash equivalents)/equity) was 25.24% (2004: not applicable, net borrowings amounted to RMB-515,845,000), gross liabilities-to-equity ratio (total liabilities/total equity) was 58.16% (2004: 20.04%); the Group's debt-to-equity ratio (total debts/total equity) was 58.16% (2004: 24.04%); interest coverage (profits before interest and taxation/interest expenses) during the Reporting Period was 7.74 times (2004: 21.99 times). At the end of the Reporting Period, the proportion of liabilities of the Group increased significantly as compared to the beginning of the period but still maintained at a secure level.

## Capital Expenditures and Financing Capability

As at 31 December 2005, the Group's capital expenditure plans comprised mainly construction expenditures for Yanpai Expressway, Nanguang Expressway and Yanba C and investment amounts in acquiring the interests of Qinglian Project, GZ W2 Expressway and Jiangzhong Expressway. Total capital expenditures to be incurred for the next five years are estimated to amount to RMB5,046 million. The Company plans to fund the capital expenditures of the Group for the next five years by both internal resources and borrowings. At present, according to the assessment of the Directors, the Group is able to meet various expected capital expenditures given the Group's financial resources and financing capabilities.

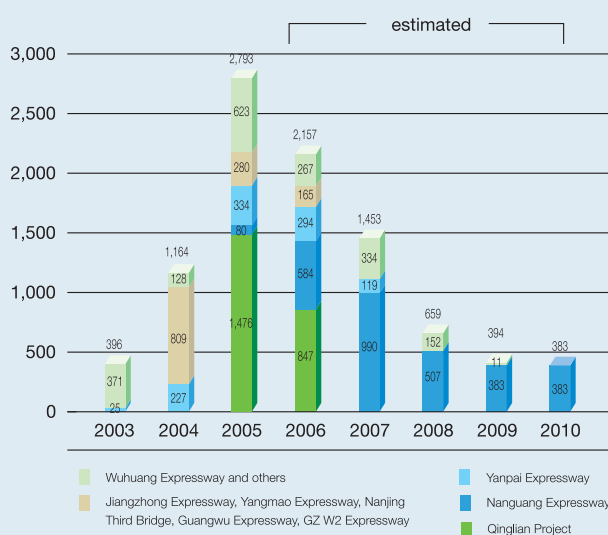
Apart from the aforesaid capital expenditure of the Company, funds for the reconstruction of Qinglian Class I Highway into an expressway amounting to RMB4.2 billion (including interests) is expected to be satisfied by external borrowings by Qinglian Company.

## Financing Activities

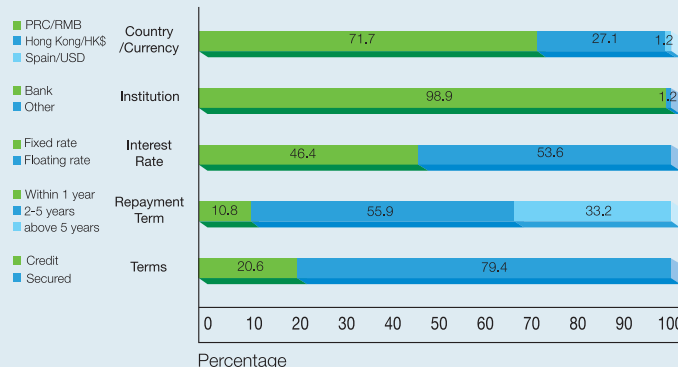
With the backing of steady growth in cash flow, a sound credit record and an excellent industry reputation, the Group has been granted an AAA credit rating for three consecutive years up to 2005 by a recognised institution of the People's Bank of China. A good credit rating is beneficial for the Company's financing activities and allows the Company to continue to enjoy prime rates under the interest rate policy of the People's Republic of China.

During the Reporting Period, with the increase in the scale of borrowings, adjustments have been made in the borrowing structure such that there was an increased proportion of long-term borrowings and fixed-interest borrowings for the purpose of reducing various financial risks. The average borrowing rate during the Year was 5.42%, higher than 4.78% of the previous year.

Capital Expenditure Plans (RMB'million)



Borrowing Structure (at 31 December 2005)



During the Reporting Period, the Group capitalised on both the favorable internal and external conditions to negotiate new financing facilities and agreements with banks. As at 31 December 2005, total credit facilities obtained by the Group amounted to RMB10 billion, of which utilised and unutilised credit facilities amounted to RMB3.18 billion and RMB6.82 billion respectively as at the end of the Reporting Period. The credit facilities available to the Group will meet the need of capital requirements for the Company's future development.

On 10 October 2005, the shareholders of the Company considered and approved the resolution for the issue of short-term commercial papers. Pursuant to the approval of the People's Bank of China, the Company is allowed to issue the short-term commercial papers up to RMB2 billion, which is valid until the end of November of 2006. The Company already issued the first batch of short-term commercial papers in the total amount of RMB1 billion in January 2006 with a term of nine months at 3.07% per annum. The issue of short-term commercial papers expanded the financial channels of the Company, improved the borrowing structure and lowered the overall financing costs of the Company.

#### **Use of Proceeds**

The Company raised RMB604 million from the issue of A shares in 2001. During the Reporting Period, the Company applied such proceeds in the construction of Yanba B in strict compliance with representations made in the Prospectus. The construction of Yanba B started in June 2001 and the section was opened to traffic for toll collection in June 2003.

An amount of RMB25,987,000 was applied during the Reporting Period and the cumulative amount of proceeds applied was RMB439,987,000. As at 31 December 2005, proceeds in the amount of RMB164,013,000 remained unutilised and were mainly held as short-term fixed deposits with banks in PRC to be used for the settlement of remaining project payments for Yanba B. After the commissioning of Yanba B, traffic flow and toll revenue of Yanba Expressway have been significantly enhanced with the formation of a local traffic network with Yanba A, details of which are set out in the section headed "Business Review and Analysis" on page 16 of this annual report.

## **RISK MANAGEMENT**

Faced with strategic opportunities for sustained rapid growth, the management also attaches great importance to various risks currently confronting the Group. Such risks are constantly subject to stringent reviews and appropriate preventive measures are undertaken, so as to achieve the strategic development goals of the Group.

#### **Political and Market Risks**

##### ***An Open Market with Intensified Competition***

Since the promulgation of the "Regulations on Administration of Toll Roads"(收费公路管理條例) in 2004 and the launch of other relevant incentive policies, the toll road sector has seen increasingly active participation from non-specialised companies and privately-owned companies, leading to intensified market competition. While presenting the Group with opportunities in developing entrusted construction management business, the continuous opening and marketisation of management services for government-funded projects have also attracted competition.

After a decade of development, the Company has accumulated considerable experience and expertise in the investment, construction, operational management and innovation of road projects. Besides, in order to further foster its core competitiveness, the Company has relentlessly pursued investment opportunities in the sector that matched its growth strategies in the past few years. Remarkable headway has been made. As such, the Company was able to enhance its competitive edge in the sector through cost control in construction and operations. On the other hand, it also enjoyed "non-price" competitive advantages from its good reputation, public image and government connections.

## **Toll Rate Adjustments**

As mentioned on page 19 in this annual report, toll rates in Guangdong Province for Class 5 vehicles were adjusted downwards in 2005. While such adjustments did not have a significant impact on the Company's revenue and profit during the Reported Period, the trends of toll rate adjustments, as well as whether toll rates will go up in accordance with sustained inflation or increase in interest rate, are still subject to the State's relevant policies and the approval of provincial government authorities.

In view of the uncertainty arising from toll rate adjustments, the Company has adopted prudent assumptions for price adjustments when analysing project investments, so as to equip new projects with stronger risk resilience. In addition, the Company will continue its cost reduction measures to enhance operating margins and to control project construction costs, so as to achieve a higher return for shareholders even when toll rates remain at the same level. Furthermore, the Company will maintain active communication and close cooperation relations with various government authorities and industry peers, in a bid to promote proper understanding and knowledge of the sector by the government and the public, so as to facilitate our pursuit for more reasonable toll rates.



## **Variations in Traffic Flow**

The continued economic growth of the PRC and the increase in vehicle ownership ensure the growth of traffic on toll roads. However, the operating performance of toll roads is subject to a variety of factors. Since all road projects are subject to limited terms of operation, if the traffic flows on the Company's projects fail to reach the projected levels during the terms of operation as a result of, inter alia, sluggish economic growth or changes in highway network deployment, the profit of the Company may be adversely affected.

To mitigate the impact of such risks, the Company has adopted a more prudent approach in project investment, such as avoiding new construction projects in unfamiliar and underdeveloped regions. Conservative assumptions were used when evaluating the growth of traffic flow to ensure a strengthened risk resilience of new projects. As for operation of projects, the Company has been devoted to attracting traffic flow and enhancing competitiveness of its expressways through various initiatives, including providing quality road services and facilities and reinforcing promotion and marketing of new expressways. Building on this basis, the Company also continues to maintain good communication and cooperative relations with various government authorities and industry peers to seek a rationalised layout of road networks and connections in the region.

## **Financial Risks**

### **Interest Rate Risks**

In recent years, as a result of increase in acquisitions and construction projects, the Group's capital expenditure has gone up quite substantially, and borrowings as a percentage of capital expenditure has also shown a rising trend. Consequently, the Group is becoming more susceptible to fluctuations in interest rates, especially in medium to long-term interest rates.

The Group employs an optimised portfolio comprising fixed and floating interest rates and short and long term borrowings to contain the risks arising from interest rate fluctuations within an acceptable range. The Group's good credit rating and reputation in the sector also presented an advantage in securing more preferential borrowing rates. Furthermore, the Company is actively exploring other financing channels. During the Reporting Period, a resolution regarding issue of short-term commercial papers was approved by shareholders of the Company. In January 2006, the first batch of RMB1 billion short-term commercial papers were issued and the financing cost was lower than the then prevailing bank borrowing rate, which reduced the consolidated financing costs of the Company. During the Reporting Period, the Company did not use any interest rate swap option contracts.

### **Cash Flow Risks**

The toll road business is characterised by its capital-intensive nature and a long period for investment return. At the present stage, the Company is required to commit increasing capital expenditure. Therefore, it is particularly important for the Company to contain cash flow risks.

Over the years, the Company has established a rigorous model of financial forecasts and estimates for evaluating its investment in new projects and its financial resources. All new projects are evaluated and prioritised strictly against criteria such as preset levels of return, cash flow of the Company and cost of capital. Necessary sensitivity analyses were conducted in respect of all important assumptions and parameters. The Company reviews the principal assumptions of the abovementioned model on a regular basis to ensure their compatibility with the latest situations. In addition, the Company maintains a balanced mix of debt portfolio and bank facilities to ensure its cash liquidity by taking into account such factors as repayment terms, interest rates and exchange rate risks with reference to the specific conditions of the industry, the domestic loan market and the Company.

### **Exchange Rate Risks**

All major operations of the Group are located in the PRC and the majority of transactions are settled in RMB. The Group did not have significant exposure to foreign exchange risk in the PRC, except for certain cash at bank balances of RMB58,200,000 and bank borrowings of RMB676 million which were denominated in HK\$ and other borrowings of RMB30,051,000 which were denominated in United States dollars, respectively.

### **Operation Risks**

#### **Construction Management**

In recent years, the Group has been engaged in large expressway construction projects. As a result of factors such as price fluctuations in construction materials, increasing difficulties in land requisitioning and resettlement of residents, changes in construction plans and promulgation of new policies and technical regulations by the government, the construction projects are exposed to the risks of increasing costs, delay and impaired work quality.



As the core competitive strengths of the Group, the Company's extensive expertise and experience in toll road construction management have formed the basis for managing the above risks. The Company has formulated and implemented a series of management systems and measures to effectively control risks and to eventually ensure completion of the projects in accordance with the required quality, construction costs, completion dates and safety standards. Moreover, the Company has also effectively transferred such risks as appropriate by entering into relevant insurance contracts, construction outsourcing agreements and centralised procurement contracts for major materials.

#### **Repairs and Maintenance of Highways**

At present, the highways of the Group are kept in good conditions. Maintenance costs as a percentage of operating costs stood at a relatively low level during the Reporting Period. As the useful life of the highways elapses and traffic flows and wear-and-tear increase, the scale of repair work and the related costs may also increase. Besides, road conditions may also be impaired to different extents by traffic accidents and other factors.

During the Reporting Period, the Company continued to step up reforms in the operational management model for the projects invested in by the Group in the Shenzhen area. Various road sections, previously rather independently managed, have now been centralised to enhance management efficiency and work quality and to reduce management costs. Moreover, the Company reinforced road inspections to effect prompt investigation and evidence collection for road facility damage and road accidents, thereby achieving a higher compensation rate for road asset losses. The Company will also strive to maintain smooth traffic flows on its highways as a whole by rationalising works arrangements, such as arranging works on a section-by-section or lane-by-lane basis, as well as arranging night-time works to minimise the impact upon peak-hours traffic.

## OUTLOOK

### Objectives and Plans

The Company's general development plan for the next five years is defined in its Development Strategies 2005-2009. These strategies principally aim to: (1) focus on the principal operations of toll road investment, construction, operation and management and expand from Shenzhen as the base to the Pearl River Delta and other economically-developed regions to increase market share on an on-going basis; (2) make a head start in establishing a presence in the highway construction and management sector by outputting engineering and management technology and experience; (3) raise management standards and quality of human resources in all aspects in line with business development and risk control; and (4) eventually achieve sustained profit growth for yielding above-average returns for our shareholders.

In 2006, the management will concentrate on enhancing the management of projects under construction and the operation and management of projects in operation and external investment projects, and make sure that the Company's growing needs will be sufficiently met by financial and human resources. The operating performance and results of various businesses in 2006 will serve as an essential base for the Group to achieve its development objectives in the next five years.

Based on its reasonable expectation that there will be no drastic changes in major aspects of the business environment while taking into account the performance of new projects, the management expects a double-digit increase in traffic flow on its toll roads on average, with total toll revenue of no less than RMB1.2 billion set as target for 2006. With respect to project construction, Yanpai Expressway and Nanping projects will be operational by the middle of 2006, construction of Qinglian Project and Nanguang Expressway will commence in full wing within the year, Construction investments of approximately RMB2 billion will be made for the whole year, and all of the investment for the construction projects will be kept within budget. With respect to project investment, the management will carry out a post-investment assessment of existing projects, focus on the proposed rational integration of existing resources, and assess and decide on future new projects in a more prudent manner.

In 2006, capital expenditure plans will be financed mainly by the Group's internal funds, issuance of short-term commercial papers and increased bank loans. Other types of borrowings other than bank loans will also be considered cautiously. Average lending rates will be kept at an appropriate level by proper debt or capital restructuring arrangements. The Group's financial costs are expected to surge substantially, given the increase in total capital expenditures. Besides, with the increased number of operating projects and an expanded operating scale, there will be a rise in the Group's operating expenses mainly comprising increased depreciation expenses and staff costs. The Group also plans to moderately increase its investment in highway maintenance in order to maintain good highway and traveling conditions. The management will strive to keep costs under control through strengthening routine management, optimising financing structure and other measures, so that the Company's profits can be maintained at a relatively stable level which will form a base for the Company's rapid growth in the years ahead.

## Outlook

Against the background of a growing Chinese economy, Guangdong Province and Shenzhen have been able to record an economic growth higher than the national average for many years and have gradually developed into a major industrial hub of China. In future, there will be huge demands and investments in highways in China to meet the needs of economic development. According to planning, the total mileage of expressways will increase by approximately 3,000 km annually throughout China until 2010, involving an annual average investment of RMB140 billion. The Guangdong Provincial Government has also proposed to build highways covering a total mileage of 4,000 km across the province by 2008. To raise funding from various sources, the major composition of investments in highways will become more diversified in future while the operation of highways will become more commercialised. The promulgation of the “Regulations for the Management of Toll Roads” and increasing regularisation of the toll road and construction management sectors will help safeguard the interests of investors, road users and the general public and help promote a long-term and healthy development of the sectors.



Increase in the transparency, commercialisation and regularisation of the toll road and construction management sectors has provided the Group with unprecedented opportunities for development on the one hand and has attracted more market entrants, intensified competition and accelerated pace on the other hand. Exposed to an external environment full of opportunities and challenges, the Group will remain committed to its principal operations and development directions, fully capitalise on its existing competitive advantages, consistently enhance management standards and staff quality, and foster and reinforce its core competitive strengths. The management is fully aware of the risks confronting the Group in the financial, marketing, operational and other aspects. On-going assessments and reviews will be conducted in a prudent manner and relevant preventive measures will be accordingly adopted, and resistance enhanced, for achieving a rapid and healthy growth.