Discussion and Analysis of the Group's Performance

OVERVIEW ON ELECTRICITY GENERATION BUSINESS

During the year, the Group's on-grid electricity generation amounted to 1,946 million kwh, representing a decrease of 12.9% as compared to 2,233 million kwh over 2005. As a result, the turnover of on-grid electricity decreased by 10.1% to HK$1,161.3 million. This decrease was mainly due to the technical malfunction of one of our power generating units, which was shut down for repairs from July through to December 2006. The manufacturer of this generating unit has completed the repairs and all the power generating units are functioning normally in the first quarter of 2007. We have commenced the claims procedures with both our insurance provider and the manufacturer to recover the losses incurred as a result of the breakdown. As the final claims have not been finalised and received yet, we have not included the claims amount for the year ended 31 December 2006.

Direct operating expenses attributable to electricity supplies decreased by 11.8% to HK$1,006.5 million due to the decrease in electricity generation. However, the fuel cost per tonne increased by 15.4% due to the escalating fuel cost especially in the first half of 2006. During the year, the Group incurred a total fuel cost of HK$873.4 million.

The staggeringly high world crude oil price had significantly affected the price of heavy oil which put the Group's power generation business under enormous pressure. Through management's efforts in improving productivity, strengthening fuel procurement and inventory control, the gross profit margin of the power generation business for the year increased slightly by 2.1% as compared to 2005.

The Group was granted an amount of HK$262.8 million, in compensation for the high fuel cost, by the Shenzhen Government for the period from September 2005 to October 2006.

Currently, the Group's power plants are undergoing conversion from using heavy oil to natural gas, a more economical and environmentally friendly fuel source. Management plans to modify the two 180 MW power generator units so that these can use natural gas as an additional energy source, making them unique with dual-fuel firing capabilities by the first half of 2007. When completed, this will provide greater flexibility for the Group to select the most economical source of fuel. The proximity of the Group's power plant to the Guangdong Liquefied Natural Gas Terminal, which was completed in June 2006, ensures that the Group is well positioned for the change from heavy oil to natural gas.

OVERVIEW ON GAS BUSINESS

For the year ended 31 December 2006, Panva Gas recorded a turnover of HK$2,642.9 million, an increase of 13.7% over 2005. The gas fuel business was further divided into the sale of piped gas, gas pipeline construction and sale of LP gas. Turnover contribution from each of these activities amounted to HK$374.3 million, HK$331.2 million, and HK$1,900.8 million, accounting for 14.2%, 12.5%, and 71.9%, respectively, of Panva Gas's turnover. The rapid growth of the piped gas business underlines Panva Gas's shift towards a utility business model with the sale of piped gas becoming a significant source of income.

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Its gross profit decreased by 41.3% to HK$404.7 million and the loss attributable to shareholders amounted to HK$256.3 million. The net loss was due to the loss in fair value on the two interest rate swaps of approximately HK$124.2 million, the increase in interest expenses of approximately HK$4.4 million, the increase in the distribution and administrative expenses of approximately HK$172.5 million and a fewer number of new piped gas user connections recorded during the year when compared to 2005.

On 4 December 2006, the Company, Panva Gas and HKCG announced that the Panva Gas has agreed to acquire the entire issued share capital of each of the eight companies held by HKCG (collectively the "Target Companies"), which hold equity interests in ten PRC companies that are engaged in piped gas fuel businesses. Panva Gas also agreed that it will take assignment of the outstanding loans due from the Target Companies to HKCG or its associates, being approximately HK$568.1 million, together with all interest accrued thereon, if any. In consideration of the acquisition (which includes taking assignment of the shareholder loans), Panva Gas agreed to issue approximately 773 million new shares to HKCG, which represented 43.97% of the enlarged issued share capital of Panva Gas. The resolutions related to the agreement were approved at the extraordinary general meeting of both Panva Gas and Enerchina and the completion of the agreement took place on 1 March 2007, upon which HKCG became the single largest shareholder of Panva Gas and Enerchina's shareholding in Panva Gas was reduced from 57.94% to 32.47%.

In order to maintain the public float of Panva Gas at the minimum level of 25%, on the same date, Enerchina placed down 33,918,400 shares in Panva Gas at the placing price of HK$3.77, raising approximately HK$126.1 million for the Group. The placement further reduced our shareholding in Panva Gas to 30.54%.

FINANCIAL POSITION

The Group's total borrowings decreased from HK$3,285.0 million as at 31 December 2005 to HK$3,103.1 million as at 31 December 2006.

The total borrowings were mainly comprised of bank and other loans amounting to HK$1,146.9 million, and convertible bonds and notes amounting to HK$1,956.2 million. The bank borrowings were mainly used to finance the expansion of the power plant in Shenzhen and the convertible bonds and notes were used for the expansion of the gas business in the PRC. The Group's total net debt to equity as at 31 December 2006 was 57.63%.

Total assets pledged in securing these loans have a net book value of HK$750.6 million as at 31 December 2006. All the bank borrowings of the Group are at floating rates and denominated in both Renminbi and United States dollars. The Group's operation is mainly carried out in the PRC and 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. These interest rate swaps were subsequently terminated in September 2006. The Board will continue to evaluate and monitor the potential impact of the appreciation of Renminbi to the Group's business and manage the risks of using different financial instruments.

The Group's cash and cash equivalents and pledged deposits amounted to HK$957.4 million and HK$20.0 million, respectively, as at 31 December 2006 and are mostly denominated in Renminbi, Hong Kong dollars and United States dollars.

OUTLOOK

The Group expects the growth in power consumption in the Guangdong province to continue in 2007. However, the Group's power generation business will find 2007 a challenging year ahead as the price of heavy oil is still a major determinant of the Group's power sector profitability and the Group considers that heavy oil price may not come down significantly in the near future even though it had receded slightly in the second half of 2006. Under the current electricity supply regime of the PRC, the Group cannot transfer the additional fuel costs to its customers and can only rely on partial compensation from the government for such rising fuel costs.

In view of this, in the first half of 2007, we will continue our efforts in improving productivity and closely monitor the conversion of our power plants from using oil fuel to natural gas. The Group will also continue our discussions in securing the supply of natural gas to coincide with the completion of the conversion of the power plants. The expansion plans to increase the power generation capacity, from the Group's existing total installed capacity of 665,000 kilowatts to 1,450,000 kilowatts would also be expedited once discussions on the supply of natural gas have reached final stages.

Looking ahead, Panva Gas will accelerate its integration with HKCG and focus on improving the management and cost efficiency of its existing projects by capitalising on its operational synergies with HKCG, focusing on the development of piped gas projects with an emphasis in operational and safety management for long-term results and consolidating its existing LP Gas operation while allocating resources to the development of new LP Gas projects on a selective basis.

With the integration of Panva Gas with HKCG from 1 March 2007 onwards, the Group will remain as a major strategic investor in Panva Gas. We are confident and optimistic about its prospects and if the opportunities arise, will capitalize on its valuation and enhance returns to our shareholders.

CAPITAL COMMITMENTS

As at 31 December 2006, the Group had capital commitments in respect of the acquisition of property, plant and equipment not provided in the financial statements amounting to HK$44.5 million.

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CONTINGENT LIABILITIES

(i) In August 2003, a supplier filed an application of arbitration against Shenzhen Fuhuade Electric Power Co., Ltd. ("Shenzhen Fuhuade"), a subsidiary of the Company in respect of a claim for extra contract sum due to the additional work involved during the installation of the new generating units. The extra contract sum claimed, together with interest thereon, amounts to approximately HK$28 million (2005: HK$28 million). Shenzhen Fuhuade has instructed a firm of lawyers to act on its behalf in respect of the arbitration. Although the arbitration was terminated by the court during the year, the supplier filed an appeal against it. Shenzhen Fuhuade was strongly resisting this claim and, accordingly, no provision for the amount claimed has been made by the Group as at 31 December 2005 and 2006.

(ii) During the year ended 31 December 2005, the Company disposed of its 41% equity interest in Xin Hua Control Engineering Company Limited ("Xin Hua") to a third party ("the Buyer"). A portion of the consideration in respect of such disposal of approximately HK$24.5 million was paid into the accounts of an escrow agent ("Escrow Agent") and shall be released to the Company on 31 March 2007, unless the Escrow Agent shall before such date receive a certificate from the Buyer of its objection to release such amount and request such amount to be released back to the Buyer.

The Company and the Escrow Agent have received such certificate dated 7 March 2007 from the Buyer and a claim against the sellers (including the Company) of US$12.2 million. Under the equity transfer agreement, the maximum liability of the Company shall not exceed 37.3% of the relevant damage or its portion of escrow money of US$3.2 million (equivalent to approximately HK$24.5 million), whichever is lower.

The Company has sent to the Escrow Agent a certificate objecting the transfer of the escrow money to the Buyer, and has sent to the Buyer a notice that the Company is disputing the Buyer's claim. The Company was in the process of gathering further details of the Buyer's claim. The Company did not see any grounds for withholding its portion of escrow money on the maturity date and, accordingly, the management takes the view that no contingency arises for which a provision is required to be made nor no allowance is required to be made to the amount receivable included in the consolidated financial statements as at 31 December 2006.

Save for the outstanding arbitration as stated above, the Group had no material contingent liabilities as at 31 December 2006.

FINAL DIVIDEND

In order to retain resources for the Group's business development, the Board does not recommend the payment of a final dividend for the year ended 31 December 2006 (2005: HK$0.01 per Share).

APPRECIATION

On behalf of the Board, I would like to take this opportunity to express my appreciation to the staff and management team of the Group for their contribution during the year and also to give my sincere gratitude to all our shareholders for their continual support all these years.

By order of the Board

Ou Yaping
Chairman

Hong Kong, 19 April 2007