

# BUSINESS REVIEW

## MAINLAND CHINA

China's future energy needs are enormous and the country is the largest single area for new gas markets and projects in the world. Prospects are immense given the Central Government's intention to double natural gas consumption to around 6 per cent of the primary energy requirement by 2010. Towngas' strategy is to focus on expanding our foothold in city piped gas businesses so as to be ready to exploit opportunities for growth when natural gas starts to flow in earnest to downstream markets by 2005.

## Strategic Joint Ventures

At the end of 2003, Towngas had a portfolio of 24 joint ventures (JVs) made up of 21 established city piped gas distribution JVs and three more similar deals successfully concluded during the year but still in the process of being established. Total project investments for the 24 JVs will amount to approximately HK\$6 billion. We are also currently in discussion with more than ten further cities for possible JV or equity investment in 2004, as part of our measured but dynamic strategy to maximise our position for future advancement. Our aim in stepping up our mainland drive is to multiply overall Company profit contributions from our JV businesses within the next three to five years as projects reach maturity.

A key imperative in our mainland policy is the impending and strategic value of blossoming consumer gas markets. Towngas' world-class management, technological know-how, expertise,



*High quality installation and after-sales service are nurturing customer confidence and boosting the reputation of the Towngas brand name.*



*Extensive media publicity, particularly praising our customer services, highlights the Company's growing presence in the mainland.*

reputation, and not least, symbiotic resource allocation amongst our JVs are attractive assets for China gas companies seeking to leverage their standing in a highly capital intensive but potentially very lucrative energy supply chain. In addition, as we develop even more applications for natural gas in the coming year, utilisation of gas is expected to rise in parallel with a significant growth in residential, commercial and industrial customer numbers.

**“China's burgeoning gas industry is driven by environmental concerns and the need to secure future energy supplies.”**

Our focus to date has been on the coastal and central regions of China. These include the Pearl River Delta; the Yangtze River Delta, especially Jiangsu and Zhejiang Provinces and Shanghai; up

and coming Shangdong Province; and Anhui and Hubei Provinces. All are economically flourishing areas in the mainland, well-known for their trading, manufacturing and tourism industries which attract both foreign and domestic investment. Furthermore, all these regions will be supplied with natural gas links between 2004 and 2006.

During 2003, we established ten further JV local distribution companies throughout these areas and the provincial capital cities of Nanjing, Wuhan and Jinan. Three other projects are also being finalised, including one in Hong Kong's immediate hinterland, the Shenzhen Special Economic Zone, where we have been looking to form a city gas partnership for many years. This we achieved in July when we signed a framework agreement to hold a 30 per cent interest in Shenzhen Gas Corporation (SGC), which has an existing customer base of 400,000 and an adjusted net asset value of approximately HK\$850 million. SGC also has a 10 per cent stake in the Guangdong Liquefied Natural Gas (LNG) Terminal, in which the Company also





**Suzhou Customer Centre** showcases an extensive and tempting range of modern gas appliances and offers professional, high-class quality service in a friendly and comfortable setting.



## Towngas' City Piped Gas Joint Ventures in Mainland China



|                           | Year of Establishment | Project Investment Rmb Mn | Registered Capital Rmb Mn | Equity Share |
|---------------------------|-----------------------|---------------------------|---------------------------|--------------|
| <b>GUANGDONG PROVINCE</b> |                       |                           |                           |              |
| 1 Panyu                   | 1994                  | 260                       | 105                       | 80%          |
| 2 Zhongshan               | 1995                  | 240                       | 96                        | 70%          |
| 3 Dongyong                | 1998                  | 132                       | 53                        | 80%          |
| 4 Jianke                  | 2002                  | 45                        | 23                        | 70%          |
| 5 Shenzhen                | —*                    | 905                       | —*                        | 30%          |
| <b>CENTRAL CHINA</b>      |                       |                           |                           |              |
| 6 Wuhan                   | 2003                  | 1,200                     | 400                       | 50%          |
| <b>EASTERN CHINA</b>      |                       |                           |                           |              |
| 7 Suzhou Industrial Park  | 2001                  | 88                        | 44                        | 45%          |
| 8 Yixing                  | 2001                  | 246                       | 124                       | 80%          |
| 9 Taizhou                 | 2002                  | 200                       | 83                        | 65%          |
| 10 Changzhou              | 2003                  | 248                       | 166                       | 50%          |
| 11 Zhangjiagang           | 2003                  | 150                       | 60                        | 51%          |
| 12 Nanjing                | 2003                  | 1,283                     | 642                       | 50%          |
| 13 Wujiang                | 2003                  | 150                       | 60                        | 80%          |
| 14 Xuzhou                 | —*                    | 245                       | —*                        | 80%          |
| 15 Tongxiang              | 2003                  | 83                        | 58                        | 76%          |
| 16 Maanshan               | 2003                  | 248                       | 108                       | 50%          |
| <b>SHANDONG PROVINCE</b>  |                       |                           |                           |              |
| 17 Jimo                   | 2001                  | 37                        | 19                        | 90%          |
| 18 Laoshan                | 2002                  | 60                        | 30                        | 60%          |
| 19 Zibo                   | 2002                  | 240                       | 106                       | 50%          |
| 20 Longkou                | 2002                  | 84                        | 42                        | 70%          |
| 21 Weifang                | 2003                  | 241                       | 140                       | 50%          |
| 22 Jinan                  | 2003                  | 245                       | 100                       | 60%          |
| 23 Weihai                 | 2003                  | 245                       | 99                        | 50%          |
| 24 Taian                  | —*                    | 200                       | —*                        | 50%          |

\* JV company to be established



holds a 3 per cent interest. By late 2006, both Hong Kong and Shenzhen will start to receive natural gas from the Guangdong LNG Terminal.

### **Hong Kong and China Gas Investment Limited**

The asset management arm of the Company's mainland ventures, Hong Kong and China Gas Investment Limited (HCIL), established in 2002, is crucial in promoting the Company's vision and mission to mainland JVs. In spearheading best practices, safety standards, better allocation and joint purchasing of resources, an ethics policy and other Company strategies during 2003, HCIL played a significant part in guiding our JV operations towards developing a reputation for service and safety over and above their competitors. This not only boosted publicity for the Towngas corporate brand within China over the year, but also nurtured extensive media coverage of our JVs, customer service initiatives and safety precautionary measures, and inspired many written compliments from the public.

**“Our hallmark reputation for safety and services is beginning to attract attention locally from public and press, TV and radio.”**

HCIL also oversaw the smooth transfer of knowledge and human resources from Hong Kong to the mainland in 2003, and brokered a large number of training programmes to enhance management skills, ethical procedures, service attitudes, technical proficiency and safety techniques amongst all levels of JV personnel. As a result of our emphasis on transferring know-how to local JV businesses, in which through HCIL the Company has strong management involvement, and our obvious commitment to developing the natural gas market, our reputation with municipal governments is growing.

### **Future Prospects**

China's improving quality of living and determination to reduce environmental pollution are progressively driving the pace of natural gas exploitation and utilisation. Towngas' carefully formulated geographical strategy for our mainland China business development rides on our judicious investment in potentially prosperous city piped gas projects serving rapidly urbanising and expanding industrial regions. Our good relationship with municipal governments, our growing status within the community, and our attention to local markets underpin our successful ability to reach agreements with other industry players and capitalise on our strengths and expertise.

We have also identified a large pent-up demand for residential water heaters and space heating and commercial gas cooling systems that favours