

BUSINESS REVIEW

Since listing, operations of GZI REIT have been in stable development, with rent collection proceeding smoothly, without any default situation.

Active Asset Acquisition Strategy

At the moment, the Pearl River Delta region of Guangdong Province, including the Guangzhou Municipality, is in robust development, and provides an ideal current operating environment as well as a good future expansion opportunity for GZI REIT.

In 2005, Guangzhou GDP reached the mark of RMB500 billion, representing an increase of approximately 13% as compared to 2004. Guangzhou's urban resident disposal income per capita was approximately RMB18,287, representing an increase of approximately 8.3% year on year. The tertiary industry, comprising mainly service industries, had contributed approximately 53% to the overall GDP growth of Guangzhou.

We will actively seek expansion opportunities, and acquire properties with sustainable profit growth potential, including, but not limited to, the acquisition of existing or newly completed projects from GZI through the exercise of the Right of First Refusal. These measures are aimed at reducing the reliance on a single project or major tenants, and to help maintain a stable property income.

Pro-active Leasing Policy

In terms of asset management, we adopt a strategy of active and aggressive management in order to achieve maximum asset value enhancement and improve return for all Unitholders. We will make reference to the market value and the Properties' endowment to raise rent and to control expenses. Together with the ongoing improvement of the tenant mix, we will continue to strive to raise occupancy rates.

With the strategy for rent rate and occupancy rate enhancement, we will continue to improve the lease expiry structure, in order to increase the resilience of GZI REIT's operations.

Looking into the future, we will emphasize acquisition, active asset management and refine capital structure, and rely on these strategies to enhance asset return for GZI REIT, realizing the objective of stable and growing return to Unitholders. In terms of specific operating strategy, we have completed the conversion of the 8th and 9th Floor of White Horse Building. We will also strive to increase the occupancy rate of Fortune Plaza, maintain the occupancy rate of City Development Plaza while improving the tenancy mix and the business mix of Victory Plaza with an aim to enhance its competitiveness.

Furthermore, through staff training we will strive to improve service quality, and will aim at achieving an international professional management standard, actively implementing retention programmes for quality tenants, refining management details in order to attract more tenants and increase asset value, thereby achieving better returns to all Unitholders.

FINANCIAL REVIEW

Intended Distribution Per Unit

The Properties performed well during the Relevant Period with intended distribution per Unit (“the DPU”) exceeding GZI REIT’s profit forecast for the Relevant Period (“the Profit Forecast”) as disclosed in the offering circular of GZI REIT dated 12 December, 2005 (“the Offering Circular”) by 25 times at HK\$0.0405. Based on the closing price of the Units as at 31 December, 2005 of HK\$3.450, the DPU calculated based on only the 11 days during the Relevant Period represented a yield of 1.18%, as compared to the yield of 0.046% as disclosed in the Profit Forecast. Using the IPO price of HK\$3.075, the DPU calculated based on only the 11 days during the Relevant Period represented a yield of 1.32%, as compared to the yield of 0.052% as disclosed in the Profit Forecast. The substantial increase in DPU is mainly due to the non-recurring interest income in the sum of HK\$41.128 million generated from funds received for units applications during the IPO of GZI REIT which had attracted enormous interest from investors in Hong Kong and overseas, with subscription rates of over 496 times for its Hong Kong public offering.

Unit Activity

Since the listing of GZI REIT on 21 December, 2005, investors have enjoyed Unit price appreciation from the IPO price of HK\$3.075 to year-end closing of HK\$3.450, representing an increase of 12%.

GZI REIT’s Unit price reached a high of HK\$3.775 and a low of HK\$3.450 during the Relevant Period. The volume transacted during the Relevant Period was 572.983 million Units, equivalent to an average of 95.497 million Units daily.

Asset Unit

The net asset value per Unit as at 31 December, 2005 was HK\$3.016, which represents an increase of 5.7% as compared to net asset value per Unit of HK\$2.853 as disclosed in the unaudited proforma balance sheets as at 7 December, 2005, the date of establishment of GZI REIT based on the maximum offer price of HK\$3.075 as disclosed in Appendix III of the Offering Circular. The net tangible asset value per Unit as at 31 December, 2005 was HK\$2.863, which represents an increase of 3.2% as compared to the net tangible asset per Unit of HK\$2.775 as disclosed in the unaudited proforma balance sheet of GZI REIT as at 7 December, 2005 based on maximum offer price of HK\$3.075 as disclosed in Appendix III of the Offering Circular.

The increase in the net asset value per unit was mainly attributable to the increase in the valuation of the Properties as at 31 December, 2005 by 1.2% to HK\$4,053.8 million as compared to a valuation of HK\$4,005.0 million as at 30 September, 2005 and the increase in profit after tax and before transactions with Unitholders of HK\$40,543,000. The subject valuation was prepared based on an average of the values derived using the income capitalisation approach and the discounted cash flow analysis. The slight increase in valuation indicates the stable environment in the investment property market in Guangzhou.

Financial Results

The Properties performed well during the Relevant Period. GZI REIT's consolidated net profit after tax during the Relevant Period amounted to HK\$40.543 million, representing an increase by 25 times as compared to the forecasted profit of HK\$1.594 million stated in the Profit Forecast for the Relevant Period as disclosed in the Offering Circular. The following is a summary of GZI REIT's financial results during the Relevant Period:

	Actual HK\$'000	The Profit Forecast HK\$'000 (Note 1)	% of change
Gross income	6,835	6,704	2.0%
Leasing agents' fee	(241)	(235)	2.6%
Property related taxes	(643)	(640)	0.5%
Other property expenses (Note 2)	(269)	(269)	—
Total property operating expenses	(1,153)	(1,144)	0.8%
Net property income	5,682	5,560	2.2%
Withholding tax	(649)	(637)	1.9%
Manager's fees	(574)	(538)	6.7%
Trustee's fees	(40)	(37)	8.1%
Other trust expenses (Note 3)	(3,565)	(1,212)	194.1%
Total non-property expenses	(4,828)	(2,424)	99.2%
Net profit before finance costs, interest income and tax	854	3,136	(72.8%)
Interest income (Note 4)	41,209	0	—
Finance costs	(1,520)	(1,542)	(1.4%)
Net profit before tax	40,543	1,594	2,443.5%
Income tax expense	—	—	—
Net profit after tax before transactions with Unitholders	40,543	1,594	2,443.5%
Transactions with Unitholders (Note 5)			
Distributions to Unitholders (Note 6)	(40,543)	—	—
Increase in fair value of Units (Note 7)	(463,348)	—	—
(Note 8)	(463,348)	—	—

Trust Review

- Note 1 Based on the Profit Forecast together with the accompanying assumptions as disclosed in the Offering Circular.
- Note 2 Other property expenses include valuation fee, insurance premium and depreciation.
- Note 3 Other trust expenses include audit fees, legal advisory fees, printing charges, Trustee's inception fee, company secretarial fees and listing fees.
- Note 4 This mainly represents non-recurring interest income generated from funds received for units applications during the IPO of GZI REIT.
- Note 5 The Trust Deed requires GZI REIT to distribute to Unitholders an amount not less than 90% of Total Distributable Income for each financial period/year subject to adjustments allowed under the Trust Deed. In accordance with Hong Kong Accounting Standard 32 ("HKAS 32"), amounts attributable to Unitholders are recorded as a financial (not legal) liabilities.
- Note 6 According to HKAS 32, distributions to Unitholders are regarded as finance costs for accounting purposes.
- Note 7 According to HKAS 32, the financial liabilities referred to in Note 5 would be recorded at fair value for accounting purposes.
- Note 8 Note 5, 6 and 7 represent only accounting treatments which have no impact on net assets attributable to Unitholders. They have no impact on Total Distributable Income to Unitholders. They are non-cash items representing accounting adjustments made in conformity with HKAS 32.

As indicated in the above schedule, gross income and net property income exceeded the projections in the Profit Forecast by approximately 2%, whilst all fees and expenses except for other trust expenses are in line with the Profit Forecast. The increase in other trust expenses of more than HK\$2.353 million is mainly attributable to the increase in professional fees for services rendered by legal advisers, auditors and company secretaries, an one-off inception fee payable to the Trustee and the increase in printing charges as a result of an under-estimation of number of investors.

Whilst finance costs incurred were in line with the Profit Forecast, the non-recurring interest income in the sum of HK\$41.128 million as referred to above resulted in a substantial increase in the net profit before tax and before transactions with Unitholders in the sum of HK\$40.543 million as compared to HK\$1.594 million as recorded in the Profit Forecast.

The transactions with Unitholders disclosed above relate to only non-cash accounting adjustments which have no impact on the net assets attributable to Unitholders and no impact on the Total Distributable Income to Unitholders. They also have no impact on calculations of financial ratios.

Accounting treatment: distributions to Unitholders as finance costs

Pursuant to Rule 7.12 of REIT Code and the terms of the Trust Deed, GZI REIT is required to distribute to Unitholders not less than 90% of its audited annual net income after tax subject to certain adjustments as defined in the Trust Deed. In accordance with the HKAS 32, such distributions to be paid to Unitholders represent finance costs and are therefore presented as expenses in the income statement. Consequently, GZI REIT has, for accounting purpose, recognised distributions as finance costs in their income statement.

Accounting treatment: Units recorded as financial liabilities carried at fair value through profit and loss

On the basis of the accounting standard stated above, GZI REIT has, for accounting purpose, designated its Units as financial (not legal) liabilities carrying at fair value through profit and loss and has recorded such amounts at fair value as at 31 December, 2005. The number of Units in issue and the market price per Unit as at 31 December, 2005 are 1,000 million Units and HK\$3.45 respectively resulting in market capitalization of HK\$3,450 million. The increase in value in the sum of HK\$463.348 million arising from fluctuation of market capitalization during the Relevant Period has therefore been presented as a deduction from profit after tax before transactions with Unitholders.

Accounting treatment: Relevant Period as different from financial period recorded in audited financial statements

The financial review referred to above relates to only the 11 days during the Relevant Period. The audited consolidated financial statements of GZI REIT include the period from 7 December, 2005, the date of establishment of GZI REIT, to 31 December, 2005. According to the reorganisation deed dated 7 December, 2005 entered into between the Manager, the Trustee, GZI REIT (Holding) 2005 Company Limited ("Holdco") and GZI as the guarantor ("the Reorganisation Deed"), any change in the net asset value of the special purpose vehicles holding the Properties ("the SPVs") from 7 December, 2005 to 20 December, 2005, the date preceding the Listing Date should be for the account of the vendor. Accordingly, GZI REIT consolidated its results from 21 December, 2005 to 31 December, 2005 in its audited consolidated financial statements.

PORTFOLIO OVERVIEW

The Properties include Whitehorse Units, Fortune Plaza Units, City Development Units and Victory Plaza Units all of which performed well in the last quarter of 2005, showing improvement in occupancy rates as compared to the historical performance in the first three quarters of the year 2005 as disclosed in the Offering Circular.

The following table shows the rental income generated by each of the Properties during the Relevant Period and the comparison between occupancy rates as at 31 December, 2005 and the historical rates as at 30 September, 2005 as disclosed in the Offering Circular.

	Occupancy rate			Rental income generated during Relevant Period	
	Actual as at 31 December, 2005	Historical as at 30 September, 2005	% of increase	HK\$'000	% of total rental
Whitehorse Units	100.0%	100.0%	0	3,269	47.8%
Fortune Plaza Units	90.2%	76.9%	13.3%	1,229	18.0%
City Development Units	92.6%	91.0%	1.6%	1,165	17.0%
Victory Plaza Units	100.0%	100.0%	0	1,172	17.2%
Total property portfolio	95.5%	91.7%	3.8%	6,835	100.0%

The occupancy rate of the overall portfolio increased from 91.7% as at 30 September, 2005 to 95.5% as at 31 December, 2005, representing an increase of 3.8%. Whilst Whitehorse Units and Victory Plaza Units maintained a full occupancy rate of 100%, occupancy rates of Fortune Plaza Units increased from 76.9% to 90.2% whilst City Development Units increased from 91.0% to 92.6%.

During the Relevant Period, Whitehorse Units contributed 47.8% of the total rental income of the Properties whilst the remaining three Properties provided an average contribution of 17.4%.

There were no bad debts recorded during the Relevant Period.

FINAL CONSIDERATION FOR ACQUISITION OF 100% OF ISSUED SHARE CAPITAL OF THE SPVs HOLDING THE PROPERTIES FROM SUBSIDIARIES OF GZI

Initial Consideration

Pursuant to the Reorganisation Deed entered into between the Manager, the Trustee, Holdco and GZI as guarantor, the Initial Consideration (as defined therein) payable by REIT Holdco for acquisition of 100% share capital of the SPVs was HK\$4,014,180,000, which was calculated based on the sum of the following:

	HK\$
a. combined net asset value of the SPVs Companies as at 30 October, 2005	2,972,767,000
b. amounts due to the fellow subsidiaries as at 30 October, 2005	994,267,000
c. amount to be injected by GZI as the guarantor into the SPVs before the closing of the global offering	47,146,000
	<u>4,014,180,000</u>

Adjustments

According to the terms of the Reorganisation Deed, the Final Consideration (as defined therein) to be payable by REIT Holdco for the issued share capital was to be adjusted as follows, after taking into consideration the Final Accounts referred to below:

- Initial Consideration
- plus/minus: Initial Adjustment (as defined therein)
- plus/minus: Combined Net Assets Adjustment (as defined therein)

Final Accounts

According to the terms of the Reorganisation Deed, the Combined Net Assets Adjustment shall be the increase or reduction in the Combined Net Assets in the interval from date of the Reorganisation Deed, 7 December, 2005 until 20 December, 2005 as calculated based on the Initial Accounts and the Final Accounts (as defined therein) after certain defined excluded items. The Initial Accounts were included as an appendix to the Reorganisation Deed.

The Final Accounts representing the audited combined accounts of the SPVs as at 20 December, 2005, which was the date immediately preceding the Listing Date, were completed on 20 March, 2006.

Final Consideration

The calculation of Final Consideration may be summarized as follows:

	HK\$	HK\$
Initial Consideration		4,014,180,000
Initial Adjustment	60,137,537	
Combined Net Asset Adjustment	<u>23,941,000</u>	
Total Adjustment		<u>84,078,537</u>
Final Consideration		<u><u>4,098,258,537</u></u>

The Combined Net Asset Adjustment representing the remaining balance of the Final Consideration has been settled on or about 21 April, 2006.

FINAL CONSIDERATION AS DIFFERENT FROM PURCHASE CONSIDERATION

Please note that Final Consideration referred to above is different from the purchase consideration as disclosed in the audited consolidated accounts of GZI REIT, of which the former relates to consideration for cash settlement purpose between Holdco and the Vendor whilst the later is for determining the goodwill of GZI REIT in the acquisition of the SPVs.

CAPITAL STRUCTURE

The capital management policy of GZI REIT is to achieve optimal debt profile. GZI REIT, through its special purpose vehicles, entered into a facility agreement with a syndicate of banks for an US\$165 million three-year term loan facility. Total borrowings (which exclude capitalisation of debt-related expenses) as a percentage of gross assets is 29% whilst total liabilities excluding capitalisation debt-related expenses as a percentage of gross assets is 33%. The bank borrowings are secured and the security package includes, among others, a registered mortgage over each of the Properties, assignment of rental income and all other proceeds arising from each of the Properties and of all tenancy agreements relating to each of the Properties and a legal mortgage over the shares of the SPVs including Partat Investment Limited ("Partat"), Moon King Limited ("Moon King"), Full Estates Investment Limited ("Full Estates") and Keen Ocean Limited ("Keen Ocean").

REVIEW OF FINANCIAL RESULTS

The final results of GZI REIT for the Relevant Period have been reviewed by the Disclosures Committee and Audit Committee of the Manager.

NEW UNITS ISSUED

There were no new Units issued during the Relevant Period.

REPURCHASE, SALE OR REDEMPTION OF UNITS

Pursuant to the Trust Deed, the Manager shall not repurchase any Units on behalf of GZI REIT until permitted to do so by the relevant codes and guidelines issued by SFC from time to time.

During the Relevant Period, there was no repurchase, sale or redemption of Units by GZI REIT or subsidiaries of GZI REIT.

SUMMARY OF ALL REAL ESTATE SALES AND PURCHASES

GZI REIT did not enter into any real estate sales and purchases during the Relevant Period.

TOP 5 REAL ESTATE AGENTS AND CONTRACTORS ENGAGED BY GZI REIT

During the Relevant Period, GZI REIT has engaged Yicheng Property Management Co., Ltd. (“Yicheng”) and White Horse Property Management Company Ltd. (“White Horse Property Management Company”) (collectively “the Leasing Agents”) to provide dedicated leasing, marketing, tenancy management and property management services to the Properties. Other than the Leasing Agents referred to above, GZI REIT did not engage any other real estate agents and contractors during the Relevant Period.

INTEREST COVERAGE

Interest coverage was 27 times for the Relevant Period measured based on the operating profit after adjustment for non-cash items.

EMPLOYEES

GZI REIT is managed by the Manager. GZI REIT does not employ any staff.