Business Review, Discussion and Analysis, Prospects and Other Information

RESULTS

The Board of directors (the "Board") is pleased to report a remarkable growth in the Group's results for the first half of 2006. The Group's consolidated net profit attributable to shareholders amounted to HK$830 million (2005: HK$682 million), representing an increase of 21.8% as compared to the same period last year. The basic earnings per share were 13.80 HK cents (2005: 12.07 HK cents), representing an increase of 14.3% over the same period last year.

INTERIM DIVIDEND

The Board has resolved to declare the payment of an interim dividend of 5.0 HK cents per ordinary share for the six months ended 30 June 2006 (2005: 4.0 HK cents).

FINANCIAL REVIEW

The consolidated revenue of the Group for the first half of 2006 was HK$3,082 million (2005: HK$2,660 million), an increase of 15.9% as compared to the same period last year. All the Group's six business sectors, namely water distribution, electric power generation, toll roads and bridges, property investment, department stores, and hotel operations and management, achieved satisfactory growth.

The consolidated net profit attributable to shareholders amounted to HK$830 million (2005: HK$682 million), an increase of 21.8% as compared to the same period last year. The water distribution business remains the major source of our profit. Indeed, notwithstanding that our sales volume during the period was affected by the unusual heavy rainfall, this was more than made up by the arrangements under the Hong Kong Water Supply Agreement and the further increase in the water tariffs for the Shenzhen and Dongguan areas, and our water distribution business has therefore continued to provide stable profit contribution to the Group. The increase in profit was also mainly attributable to increases in the revenue from the electric power generation business of HK$259 million (an increase of 145.2%), the hotel operations and management business of HK$24 million (an increase of 21.6%) and the department stores business of HK$112 million (an increase of 21.6%). As far as finance costs are concerned, even though interest rates are currently in an upward trend, interest rate swap arrangements have already been made for a major portion of the Company's floating rate loans. Accordingly, the impact of the rising interest rates on the Group's financials is only minor. Benefitting from not only the interest margin reduction arrangements made in November 2005, but also the continuing repayment of outstanding borrowings, the Group's finance costs for the period under review decreased by HK$51 million.

The earnings before interest, tax, depreciation and amortisation ("EBITDA") for the first half of 2006 increased by 11.2% to HK$1,930 million (2005: HK$1,736 million).

The basic earnings per share were 13.80 HK cents (2005: 12.07 HK cents), representing an increase of 14.3% over the same period of 2005.

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BUSINESS OVERVIEW

A summary of the performance of the Group's major businesses during the period under review is as follows:

Water Distribution

Profit contribution from the Dongshen Water Supply Project remained significant to the Group. The Group's effective interest in the Dongshen Water Supply Project has increased by 1.03% to 87.37% during the six months ended 30 June 2006. The planned annual capacity of water supply is 2.423 billion cubic meters.

The total water sales to Hong Kong, Shenzhen and Dongguan during the six months ended 30 June 2006 amounted to 957 million cubic meters, a decrease of 9.0% over the same period last year, in terms of volume and HK$1.69 billion, an increase of 0.9%, in terms of revenue.

In April 2006, the Government of Hong Kong Special Administrative Region and the Guangdong Provincial Government concluded the Hong Kong Water Supply Agreement for 2006 to 2008. According to the new agreement, the total annual fixed amount for the water sales to Hong Kong is HK$2.49 billion. As compared with the total annual revenue for the Hong Kong water sales for 2004 and 2005, there will be a slight annual decrease of HK$34.9 million. The Guangdong Provincial Government has already undertaken that the revenue to the Group from its Hong Kong water sales will not fall below the 2004 level as a result of any adverse impact of the new agreement. The Guangdong Provincial Government will therefore provide financial subsidies to the Group and the annual amount of such subsidies will definitely be no less than the annual shortfall as aforesaid. The Company is still in the course of actively following up with the Guangdong Provincial Government on the implementation of the subsidy arrangements.

Under the new Hong Kong Water Supply Agreement, the total revenue for each year is fixed and is payable by 11 equal monthly installments. That being the case, the water sales to Hong Kong for the six months ended 30 June 2006 was HK$1.36 billion in terms of revenue (a slight increase of 0.7% as compared to the same period last year) notwithstanding that it was only 371 million cubic meters in terms of volume (a decrease of 15.1%).

The water sales volume to Shenzhen and Dongguan decreased by 4.7% to 586 million cubic meters during the six months ended 30 June 2006 (2005: 615 million cubic meters). This is partly because as a result of the unusual heavy rainfall during the period, there has been a lesser reliance on the supply by the Dongshen Water Supply Project for the water supply for the region. It is also in part due to the fact that during the period, two of our customers had to use more water from their own reservoirs to make way for maintenance works to be carried out. But given the further increase in water tariffs for Shenzhen and Dongguan since January 2006 and also the appreciation of Renminbi, the water sales revenue to these two regions during the six months ended 30 June 2006 slightly increased by 1.8% to HK$335 million (2005: HK$329 million).

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BUSINESS OVERVIEW (continued)

Water Distribution (continued)

The profit contribution to the Group from the water distribution business for the period under review (excluding the unrealised gain of HK$4,385,000 (2005: HK$78,606,000) on interest rate swap agreements ("Non-qualified IRS") that did not qualify as hedging transactions for accounting purposes) was HK$489,716,000 (2005: HK$463,457,000), 5.7% higher than the same period last year. Excluding the related costs arising from the Non-qualified IRS and the exchange differences, the EBITDA of the water distribution business during the period amounted to HK$1,445,412,000 (2005: HK$1,429,317,000), an increase of 1.1%.

In November 2005, the Group contracted with Industrial and Commercial Bank of China (Asia) Limited ("ICBC(Asia)") and Industrial and Commercial Bank of China Limited, Shenzhen Branch ("ICBC(SZ)") as the facility agents to reduce the interest margin of the existing syndicated bank loans of the Group totalling HK$10.7 billion at that time. The interest margin for the then outstanding loan due to ICBC (Asia) syndicate was reduced from HIBOR+1.339% to HIBOR+0.6% and the interest margin for the then outstanding loan due to the ICBC (SZ) went down from HIBOR + 1% to HIBOR + 0.6%. As a result of the interest margin reduction, the amount of interest savings during the six months ended 30 June 2006 amounted to approximately HK$36 million.

Electric Power Generation

Shaoguan Power Plant D ("Shaoguan PPD")

The Group's effective interest in Shaoguan PPD is 45.9% (a 51% owned subsidiary of the Company holding a 90% interest in the project joint venture company). Shaoguan PPD has 1 power unit with installed capacity of 200 MW. The management's efforts to increase electricity sales have borne fruit. Also there has been no major repair that requires the shut down of the power unit during the period. Thus, the sales of electricity in the first six months of 2006 rose to 735 million kwh (2005: 523 million kwh), an increase of 40.5%. The sales revenue for the period amounted to HK$294,960,000 (2005: HK$178,341,000), an increase of 65.4%, which increase was mainly due to the increase in both the electricity sales and the tariff. The profit before tax for the period was HK$54,746,000 (2005: loss before tax HK$29,043,000). The Group's share of the profit before tax was HK$25,128,000 (2005: loss before tax HK$13,331,000).

廣東省韶關粵江發電有限責任公司 (Guangdong Shaoguan Yue Jiang Power Supply Limited) ("Yue Jiang Power Plant")

Yue Jiang Power Plant is a 25% associate held by Shaoguan PPD. Yue Jiang Power Plant currently has 2 power units with a total installed capacity of 600 MW. In the first six months of 2006, sales of electricity reached 1,683 million kwh (2005: 760 million kwh), an increase of 121.4%. Sales revenue for the period reached HK$632,751,000 (2005: HK$285,453,000), an increase of 121.7%. The increase in revenue was mainly due to a new power unit with installed capacity of 300 MW coming into operation in July 2005. The Group's share of the profit before tax from this associate was HK$3,841,000 (2005: loss before tax HK$341,000).

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BUSINESS OVERVIEW (continued)

Electric Power Generation (continued)

Meixian Power Plant

The Group's effective interest in Meixian Power Plant is 12.25% (a 49% associate of the Company, Guangdong Power Investment Limited ("GD Power Investment"), holding a 25% interest in the project joint venture company).

Meixian Power Plant has 3 power units with a total installed capacity of 385 MW. In the first six months of 2006, sale of electricity amounted to 1,387 million kwh (2005: 1,275 million kwh), an increase of 8.8%. Sales revenue for the period reached HK$501,017,000 (2005: HK$441,233,000), an increase of 13.5%. However, because of the increase in finance costs, the profit before tax was only HK$54,994,000 (2005: HK$63,669,000), a decrease of 13.6%. During the period, GD Power Investment received dividend income of HK$3,863,000 (2005: HK$16,508,000) from this investment.

There is yet another new power unit with installed capacity of 135 MW that has been commissioned. Construction has already been completed. However, full commercial operation will only be able to commence when all the new approval requirements that have since come into force are also met.

Zhongshan Power Plant

In 1993, the Group through its 95% owned subsidiary, Zhongshan Power (Hong Kong) Limited, participated in a contractual joint venture, 中山火力發電廠 ("Zhongshan Power Plant"), with a tenure of 20 years. Agreement was reached with the joint venture partner to completely overhaul the terms of the joint venture agreement and the supplemental joint venture agreement was formally signed in January 2006. Zhongshan Power Plant has since become a subsidiary of the Company.

Zhongshan Power Plant has 2 power units with a total installed capacity of 110 MW. In the first six months of 2006, the electricity sales amounted to 332 million kwh (2005: 218 million kwh), an increase of 52.3%. There has also been an increase in the tariff. As a result, the sales revenue for the period rose to HK$142,306,000 (2005: HK$88,551,000), an increase of 60.7%. The profit before tax for the period was HK$32,749,000 (2005: HK$725,000). The Group's share of the profit before tax was HK$19,600,000 (2005: Nil).

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BUSINESS OVERVIEW (continued)

Toll Roads and Bridges

"1 Road and 2 Bridges"

In the first six months of 2006, the profit before tax generated by the Group's 51% jointly-controlled entity (the "JCE") which holds interests in the "1 Road and 2 Bridges" project amounted to HK$93,655,000 in aggregate (2005: HK$79,252,000). However, while the Humen Bridge and Shantou Haiwan Bridge recorded growth in traffic flow and performed well during the period, the Guangzhou-Shantou Highway (Huizhou section) suffered a drop in traffic flow.

(i) *Humen Bridge*

The JCE holds a 30% interest in this project. The Humen Bridge recorded a growth of 16.1% in traffic flow. The average daily traffic for the period increased to 48,200 vehicle trips (2005: 41,531 vehicle trips). Revenue for the period reached HK$371,268,000 (2005: HK$302,028,000), an increase of 22.9%. With private cars becoming a popular means of transport in the developing city of Humen, the traffic flow of light vehicles has increased. Also, during the period, it has become no longer necessary to continue offering tariff concession to medium size vehicles. With the repayment of shareholders' loans, finance costs decreased by HK$11,678,000 as compared with the same period last year. Accordingly, the profit before tax for the period increased by 40.5% to HK$233,730,000 (2005: HK$166,306,000).

(ii) *Shantou Haiwan Bridge*

The JCE holds a 30% interest in this project. The Shantou Haiwan Bridge recorded a 7.4% increase in traffic flow. The average daily traffic for the period was 11,079 vehicle trips (2005: 10,311 vehicle trips). The revenue for the period was HK$66,285,000 (2005: HK$58,743,000), an increase of 12.8% as compared with that of the last period. This is mainly because the road repair and maintenance works carried out to the nearby Shenzhen-Shantou Expressway (Eastern Section) during the period have made it necessary for more vehicles to use the bridge. The profit before tax for the period was HK$45,648,000 (2005: HK$41,545,000), an increase of 9.9%.

(iii) *Guangzhou-Shantou Highway (Huizhou Section)*

The JCE holds a 51% interest in this project. Mainly as a result of the competition from the nearby Guangzhou-Huizhou Expressway, the Guangzhou-Shantou Highway (Huizhou Section) suffered 6.6% drop in traffic flow in 2006. The average daily traffic for the period was 17,054 vehicle trips (2005: 18,255 vehicle trips). Revenue for the period was HK$30,183,000 (2005: HK$33,543,000), a decrease of 10.0%. Two new highways, namely 粵贛高速公路 and 河梅高速公路 came into operation in the vicinity and have diverted part of the traffic flow of the No. 205 Expressway which fed to the Guangzhou-Shantou Highway (Huizhou Section). The profit before tax for the period was HK$4,885,000 (2005: HK$7,315,000), a decrease of 33.2%.

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BUSINESS OVERVIEW (continued)

Toll Roads and Bridges (continued)

Yingkeng Highway

The Group's effective interest in this project is 70%. The average daily traffic flow for the period of the Yingkeng Highway was 5,194 vehicle trips (2005: 4,414 vehicle trips), a 17.7% increase in traffic flow as compared with that of the same period last year. As there are now more heavy vehicles that pay a higher tariff using the road, revenue increased markedly by 31.5% to HK$7,137,000 (2005: HK$5,427,000). The profit before tax for the period was HK$2,002,000 (2005: HK$1,308,000), an increase of 53.1%.

Panyu Bridge

The Panyu Bridge is a 20% associate of the Group. The Panyu Bridge recorded a growth of 9.4% in traffic flow in the current period. The average daily traffic during the period was 68,233 vehicle trips (2005: 62,362 vehicle trips). Revenue for the period has increased by 8.3% to HK$77,483,000 (2005: HK$71,560,000). The profit before tax for the period was HK$29,282,000 (2005: HK$26,700,000), an increase of 9.7%.

Two Pak Kong Bridges

The Group's effective interest in this project used to be 24.5%. Such interest was sold to 清遠市交通建設開發公司 for a total consideration of RMB59,980,000. The disposal was completed during the period, resulting in a gain of HK$39,619,000.

Property Investment

Mainland China

Teemall

Teemall, one of the most popular shopping malls in the premier area of Guangzhou, has a total gross floor area and lettable area of approximately 160,000 square meters and 96,543 square meters respectively. The plaza continued to enjoy high average occupancy rate of approximately 99% during the period (2005: 98%). Revenue of the plaza during the period reached HK$162,633,000 (2005: HK$150,123,000), an increase of 8.3%. The profit before tax for the period increased by HK$10,321,000 to HK$153,377,000 (2005: HK$143,056,000). The ability of the plaza to attract brand-name tenants and the success of the new shopping sections remained the key reasons for such increases.

Building upon the success of the shopping mall operations, the Group is proceeding with the development of two new tower blocks on the site.

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BUSINESS OVERVIEW (continued)

Property Investment (continued)

Mainland China (continued)

Teemall (continued)

The East Tower, which is expected to be completed in late 2006, will be a 45-storey A-class office tower, with a total gross floor area and lettable area of approximately 113,380 square meters and 91,000 square meters respectively. Colliers International, a prestigious international property agent, has been engaged to market and promote the leasing of all the East Tower units. The estimated total cost of the East Tower development (inclusive of also the historic land and infrastructure costs now attributed to the East Tower) is about HK$840 million of which approximately HK$532 million has been invested as at the balance sheet date.

The West Tower, which is expected to be completed in 2008, will be a 5-star hotel with approximately 450 hotel rooms. In February 2006, Sheraton Overseas Management Corporation, a renowned international hotel management company, has been engaged to operate, manage and promote the hotel under the name of Sheraton Guangzhou Hotel (粵海喜來登酒店) for an initial 10 year term. The estimated total cost of the West Tower development (inclusive of also the historic land and infrastructure costs now attributed to the West Tower) is about HK$780 million of which approximately HK$142 million has been invested as at the balance sheet date.

At the balance sheet date, the Group holds an effective equity interest of 75.55% in the development made up of the shopping mall and the two tower blocks.

Hong Kong

Guangdong Investment Tower

The average occupancy rate of the Guangdong Investment Tower for the first six months of 2006 was 88.7% (2005: 93.2%), 4.5% lower than the same period last year. The total rental income for the period was HK$7,680,000 (2005: HK$9,417,000), a decrease of 18.4%. This is mainly because of the renovation and improvement works that have been carried out during the period to prepare the ground floor shop units for lease to a major bank.

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BUSINESS OVERVIEW (continued)

Department Stores

At the balance sheet date, the Group holds an effective equity interest of 84.84% in 廣東天河城百貨有限公司 (Guangdong Teemall Department Stores Ltd.) ("GDTDS") for the operation of department stores.

GDTDS operates with a total leased area of approximately 33,827 square meters (2005: 34,509 square meters) selling a wide range of products and is ranked, in terms of sales, as one of the major department stores in Guangzhou. During the period, GDTDS continued to enjoy record high revenue of HK$630,190,000 (2005: HK$518,411,000), an increase of 21.6%. The increase in revenue arose from the holding of different trade fairs and promotion activities throughout the period, and also the success of the jewellery and gold corners. The profit before tax for the period was HK$45,396,000 (2005: HK$36,396,000), an increase of 24.7%.

As at 30 June 2006, the Group's effective interest in 廣東吉之島天貿百貨有限公司 (Guangdong Jusco Teem Stores Co., Ltd.) ("JUSCO Teem") is 26.44%, which is a 35% associate of the Group's 75.55%-owned subsidiary 廣東天河城(集團)股份有限公司 (Guangdong Teem (Holdings) Limited). JUSCO Teem has been jointly managed by Guangdong Teem (Holdings) Limited and JUSCO Japan. It has achieved satisfactory growth in its business since its establishment in 1996.

Hotel Operations and Management

As at 30 June 2006, our hotel management team managed a total of 21 hotels (as at 31 December 2005: 19 hotels), of which 2 were in Hong Kong, 1 in Macau and 18 in Mainland China (located in Shenzhen, Zhuhai, Changzhou, Dongguan, Guangzhou, Qingdao, Jilin, Dalian, Shanghai and Beijing). Out of the above hotels, 8 were owned by the Group (2 in Hong Kong, 4 in Shenzhen, 1 in Zhuhai and 1 in Changzhou).

The average occupancy rate of our 4 hotels in Hong Kong, Zhuhai and Shenzhen has decreased by 1.8% to 83.1% (2005: 84.9%). However, as a result of the success of the effort of management and the marketing team in attracting a more upmarket clientele, the average room rate has increased by 15.6% to HK$526 (2005: HK$455). The turnover for our hotel business (excluding the limited service hotels as more particularly set out below which only went into operation in the second half of the last year) for the period increased by 11.7% to HK$126,213,000 (2005: HK$112,980,000). The profit before tax increased by 10.5% to HK$32,043,000 (2005: HK$29,001,000).

To meet the strong demands of a growing number of budget conscious travellers in the Mainland China, the Group is in the course of setting up a chain of limited service hotels under the "粵海之星商務快捷連鎖酒店" brand name to provide a basic, but quality, bed-and-breakfast type service. The first three of such hotels has already commenced operation in Shenzhen in the second half of the last year. The number of rooms in each of such hotels ranges from 57 to 220 and the total capital expenditure required for each of them is in the range of RMB5–14 million. Their aggregate turnover for the current period was HK$11,188,000.

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LIQUIDITY, GEARING AND FINANCIAL RESOURCES

As at 30 June 2006, the cash and bank balances of the Group decreased by HK$224 million to HK$1,916 million (31 December 2005: HK$2,140 million), of which 20% in Hong Kong dollars, 60% in Renminbi and 20% in US dollars.

As at 30 June 2006, the level of the Group's financial borrowing decreased by HK$769 million as compared to that as at 31 December 2005. The decrease was mainly due to the repayment of certain interest-bearing debts during the period.

As at 30 June 2006, the Group had financial borrowings amounting to HK$14,397 million (31 December 2005: HK$15,166 million), including non-interest bearing Hong Kong government loan of HK$2,009 million. Of the Group's total financial borrowings, HK$181 million was repayable within one year while the remaining balance of HK$3,808 million and HK$10,408 million are repayable within two to five years and beyond five years from the balance sheet date, respectively.

Save for the bank debts mainly incurred in our water distribution business, the Group maintained credit facilities of RMB50 million as at 30 June 2006 (31 December 2005: RMB50 million).

The gearing for the Group as at 30 June 2006 was 1.05 times (31 December 2005: 1.17 times). The improvement mostly reflected the reduction in the level of the Group's financial borrowings, together with an increase in net asset value of the Group. The healthy debt servicing position of the Group continues to improve and the EBITDA/finance cost is now 6.11 times (31 December 2005: 4.55 times).

The existing cash resources and available credit facilities of the Group, together with steady cash flows generated from the Group's operations, are sufficient to meet the Group's payment obligation and business requirements.

PLEDGE OF ASSETS

As at 30 June 2006, certain of the Group's prepaid land lease payments, buildings, plant and machinery with a total net book values of approximately HK$153,534,000 were pledged to secure general banking facilities granted to the Group (31 December 2005: Nil).

CAPITAL EXPENDITURE

The Group's capital expenditure in 2006 amounted to HK$148 million principally related to the construction in progress of the East Tower at Teemall.

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EXPOSURE TO FLUCTUATIONS IN EXCHANGE AND INTEREST RATES AND RELATED HEDGES

As at 30 June 2006, total Renminbi borrowings amounted to HK$1,263 million (31 December 2005: HK$1,360 million).

As at 30 June 2006, the Group's total floating rate borrowings amounted to HK$11,157 million (31 December 2005: HK$11,925 million). For the purpose of interest rate risk management, the Group entered into certain fixed or re-indexing interest rate swap agreements, the net position of all outstanding contracts amounted to HK$7,400 million (31 December 2005: HK$9,900 million), with an average remaining life ranging from 1.5–6.5 years.

EMPLOYEE AND REMUNERATION POLICY

As at 30 June 2006, the Group had a total of 4,052 employees. Among the employees, 3,808 were employed by subsidiaries in Mainland China and 244 were employed by the head office and subsidiaries in Hong Kong. Out of the total number, 721 were managerial employees at the head office and subsidiaries' level. Total remuneration paid for the period was approximately HK$123,775,000.

The human resources of an enterprise are the foundation of its development. The Group places great emphasis on building up and strengthening of its human resources. Adhering to the "Credibility, Integrity and Profitability" core values of our corporate culture, we conduct all our staff selection processes in a fair, just and open manner. We have in place also the mechanism for the periodic performance appraisal of our management to ensure their integrity and high performance. Our remuneration and incentive packages for our staff are driven mainly by the operating results of their respective companies. In order to most effectively motivate our staff to actively create added value in their work, the incentive bonuses we pay to our management, key staff in their respective fields and other staff with outstanding performance are determined not only by reference to the operating net cashflow and profits after tax of their respective companies, but also by applying a progressive scale depending on the extent by which the operating results of their companies have exceeded expectation and further taking into account of the individual performance of the staff him or herself. Moreover the Group has adopted a staff option scheme to attract, retain and motivate outstanding staff to contribute to the continuing success of the Group in the long run. In terms of staff training and development, the Group encourages its staff to actively participate in relevant professional development programmes. The Group has also achieved very good results in enhancing the quality of its staff through all the functional skill-based or general corporate culture internal training that it continues to offer on an on-going basis.

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PROSPECTS

Looking ahead, the overall performance and cashflow of the Group's businesses as a whole is expected to continue their healthy growth. Given our strength in terms of both market shares and human resources and expertise, water distribution business will continue to be the business in which the Group has distinct competitive advantages. It will also provide the Group with solid and stable profit and cashflow contribution as well as bring about new investment opportunities. Because of the success of our management and their efforts in keeping down cost, reducing production down time and improving overall operating efficiency, our electric power generation businesses are likely to continue to maintain their marked growth. Likewise, the growth in the businesses of our toll roads and bridges, property investments and department stores is expected to continue. Moreover, with the interest margin reduction and also more of the Group's existing debts being paid down and/or refinanced, the Group is likely to be able to continue to achieve interest cost savings.

In line with its business strategy, the Group will continue to focus on its existing core businesses with particular emphasis on utilities and infrastructure. When opportunities arise, the Group will either spin-off or dispose of its hotel business. The management is also actively exploring investment opportunities in water resources and toll road projects with the aim of creating even higher values of shareholders.