



With the high cost of crude oil, the world's attention is beginning to turn to the cleaner and more competitively-priced fossil fuel of natural gas. In Hong Kong, Towngas, with great foresight, is now in the final stage of preparing to accept natural gas as partial feedstock for territory-wide town gas supply.



Gas production and supply is our core business; it always has been and it always will be. We entered 2005 with cautious optimism. A rebound in the economy looked on the horizon, tourism was set to pick up with the opening of the much-anticipated theme park on Lantau Island, and our large natural gas infrastructure investment seemed not merely prudent but also prescient given surging crude oil prices in the last two years.

Residential and Commercial Activities

Despite new housing supply remaining relatively low, active residential accounts grew to 1.58 million, with an increase of about 34,000 customers throughout the year under review. Although higher naphtha prices dampened our competitiveness, we still nevertheless saw a modest rise in total gas sale figures for 2005, up 0.5 per cent as compared to 2004.

To off-set a drop in industrial gas use, we concentrated on cost improvements and seeking new consumption potential, especially in the commercial sector. These tactics

paid off. Marketing's hard work to encourage more restaurants and hotels to use gas for hot water supply was well-rewarded in 2005. In addition, continuous promotion of our highly efficient and environmentally-friendly condensing boiler generated gratifying results.

The hotel trade in general is looking good with several establishments opening throughout the year, or due to open in 2006. Given a year-on-year uplift in tourism ever since the end of SARS in 2003, we are optimistic gas sales will grow in 2006, especially if visitors stay longer and are also tempted, alongside local residents, into fashionable new eateries and up-market, contemporary hotel dining rooms.

Our new-look Towngas Cooking Centre is in the vanguard for promoting the pleasure of good, healthy food as much as for training the art of gourmet cuisine.



With a pleasing drop in unemployment and the feel-good factor coming back due to a turn around in economic prosperity, appliance sales in the retail market rose significantly in 2005. Our carefully-planned strategy, introduced in 2004, to renovate customer centres and move these to busier locations, also had a positive impact. Matched with innovative marketing practices and more sophisticated products, we were able to increase the penetration and reputation for choice, reliability and quality of Towngas signature brands, such as TGC and SIMPA. Towngas clothes dryers, together with a number of stylish built-in hobs launched during the year with revolutionary new safety features and improved flame control – important for Chinese wok stir-frying, were sold extremely well in 2005.

In celebration of our efforts to make our customers' lives safer and more comfortable, TGC won the Best Kitchen Equipment section in the eLife Awards organised by ESDLife in 2005, whilst our high quality and innovative Super Flame gas burner gained the Consumer Product Design award in the 2005 Hong Kong Awards for Industries. In October one of our managers was also honoured with an individual prize in the 2005 HKMA/TVB Awards for Marketing Excellence.



Innovative, sleek and highly-efficient, our Super Flame gas burner won the Consumer Product Design Award in the 2005 Hong Kong Awards for Industries.

Service Initiatives

We feel it is important to connect with our customers at a personal level by putting them at the heart of our business. Our hotlines link callers directly to knowledgeable staff rather than just recorded voices, whilst our customer centres provide a full range of sophisticated services, constantly up-dated to ensure one-stop quality shopping is integral to the total customer experience.

Additionally, allied to our high standard of retail products, we also offer a check-up service for home appliances for a reasonable monthly maintenance charge. During 2005, we made over 1.7 million residential visits, including both regular safety inspection calls scheduled on a rolling 18-month cycle and on-demand maintenance appointments initiated through our 24-hour 7 days-a-week hotline. By

such means, we ensure the safety of our customers and retain their trust in the enjoyment of using gas as a dependable energy source.

Cooking for pleasure is steadily becoming more popular in Hong Kong as people seek a relaxing antidote to their busy lives. Capitalising on its position at the heart of Hong Kong's culinary education, Towngas Cooking Centre (TCC) turned a new page in its history in 2005, by relaunching itself with a fresh perspective. In melding professional tuition with the concept of cooking as a leisure pursuit, TCC successfully created a resurgence of interest in its cookery classes and corporate team-building workshops during the year. A series of TV advertisements, begun in July, is underpinning this new-found momentum to promote the delights and inspiration of flame cooking. In the same month, we also expanded

Results of Towngas Service Pledge 2005		
		Results
Reliability	Uninterrupted gas supply (over 99.99%)	99.994%
	In case of supply interruption on account of maintenance or engineering work (3 days prior notification)	100%
	Restoration of gas supply within 12 hours	99.998%
Safety	Emergency Team arrived on site within 30 minutes (at 90% of the times) ¹	93.01%
Appointments	Availability of maintenance and installation services within 2 working days	Average 1.1 days
Speed and Convenience	Customer Service Hotline (calls answered within 4 rings)	95.63%
	Connect or disconnect gas supply within 1 working day	100% (upon customer's request)
	Deposit refunded at Customer Centres (2 hours after disconnection of gas supply)	100% (upon customer's request)
Service Quality	Efficiency ²	8.68
	Courteous and friendly attitude ²	8.73
Handling Suggestions	Reply within 3 working days	100%
	Resolution, or a statement of when the matter will be resolved, within 2 weeks	100%

1.

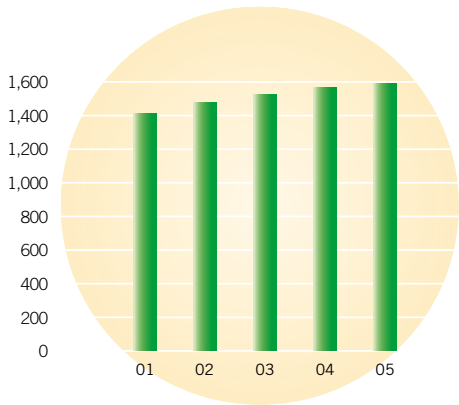
Average 19.77 minutes, taking into account all incidents which require Towngas personnel to arrive at the scene immediately, whether the incidents are gas related or not.

2.

The result was based on monthly surveys conducted from January to December 2005 by an independent research company. Our target is to exceed a score of eight out of ten.

Number of Customers

Company (Thousand)



our Towngas Cooking Ambassador Programme by partnering with the very popular Girl Guide movement in Hong Kong. Our hope is that members will develop an appreciation of good nutrition and extend their community service through charity cooking activities.

Towngas’ heritage of respect for traditional values sits happily with our aspirations to enhance society’s standard of living through better products and services. Our official commitment to maintaining

satisfaction of our customers is enshrined in the Towngas Service Pledge. In 2005, we continued to exceed our service targets and deliver a high level of service excellence.

We know however, that the kernel of our successful reputation lies with our dedicated and enthusiastic frontline staff whose professionalism ensured we retained the government’s coveted Q-Mark certification for the second year running in 2005. Employees, such



The luxurious Four Seasons Hotel, in which Towngas holds a property investment interest.

Property Developments

Towngas' investments in several residential and commercial properties appreciably boosted company earnings in 2005, following revaluations and excellent unit sales in the wake of a strengthening economy. We expect this strong contribution from properties to continue in the coming year.

A six-star hotel and a serviced suite hotel complex at International Finance Centre (IFC) and a residential development, Grand Promenade, came on stream in 2005; a third project, Grand Waterfront, at the redesignated Ma Tau Kok south plant site, is scheduled for completion by the end of 2006.

The Group has approximately a 15.8 per cent interest in IFC, which has become an iconic landmark in Hong Kong setting new standards of excellence for business, retail, hotel and serviced accommodation that helped underpin a revaluation surplus in 2005. Occupancy ratios are close to 100 per cent for offices and the shopping mall. The hotel has commercial gas appliances installed by the Company, such as dehumidifiers and boilers.

Property sales were strong at Grand Promenade with about 70 per cent of units sold by the end of 2005, yielding good returns. The Group

as Towngas technicians offering a free emergency-link check-up service to senior citizens during regular safety inspections, or colleagues winning the Hong Kong Retail Management Association's 2005 Service and Courtesy (Furniture and Home Accessories) award and being recognised by the Hong Kong Management Association's Distinguished Salesperson Programme for outstanding performance play a very large part in helping Towngas retain its quality image within the community.

As part of our Towngas Cooking Ambassador Programme, Girl Guides enhance their cooking knowledge and skills and take part in community service events.



has a 50 per cent interest in this high-end residential project where apartments are fitted with quality Towngas water heating and cooking appliances and Towngas Telecom home automation technology facilities, such as tone dial control for air-conditioners and lighting, a child surveillance system and internet connections to

management services and for personal computers. Luxury features will likewise be an integral part of the 1,800-unit development at Grand Waterfront which, with its prime location facing Hong Kong Island, is already generating good pre-sale interest. Transactions at another project at King's Park Hill also benefited from the rising property market in 2005.

Total net earnings from property sales and revaluations in 2005 had a significant positive impact on the Company's overall profit margins for the year under review. We anticipate property sales will continue to be a key driver of profit growth for our Hong Kong business during 2006.

Gas Supply

It took us 140 years to produce and supply the first 450,000 million MJ of gas. We are set to achieve the next 450,000 million milestone in 14 years! Town gas is a way of life for Hong Kong households, industrial and commercial businesses. So we are eagerly looking forward to the introduction of more economical and cleaner natural gas into the territory in 2006 which will bring even greater benefits to consumers and the Company alike.

Submarine pipes are being laid in preparation for the delivery of natural gas from Guangdong LNG terminal.



Guangdong LNG terminal should be supplying our main Tai Po gas production plant by the end of 2006 through a pair of 34 km, 450 mm-diameter submarine pipelines. By partially replacing naphtha with natural gas, we anticipate fuel cost savings and better feedstock price stability. These should enable us to reduce our tariff from its current level and at the same time keep future variations within a narrower range as we will be less exposed to fluctuations in crude oil prices.

In anticipation of this new intake source, work continued throughout 2005 to modify Tai Po plant for dual fuel gas production with six reformer units now ready and the final two nearing completion. We plan to take 0.33 million tonnes of natural gas per annum, equivalent to about 60 per cent of feedstock on a 25-year supply contract term. A landing station to receive the piped natural gas is due for completion in April 2006.

An international theme park officially opened in September 2005 by which time a 15 km town gas pipeline extension and an offtake station were complete. The popularity of the park is contributing to a growth in momentum of visitor arrivals to the territory that started

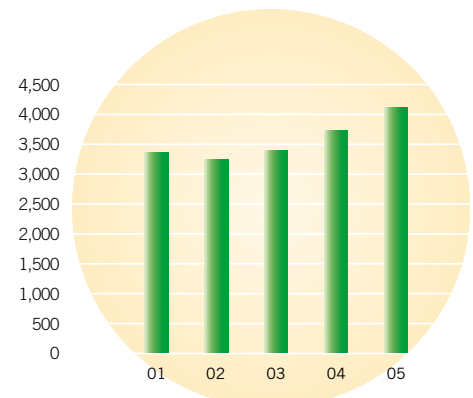
early in the year and which is expected to continue into 2006. This will have a knock-on effect in terms of lifting gas consumption through new hotel start-ups, an increase in occupancy rates and overnight stays, and a rise in the restaurant trade business.

Our 24 km Eastern Transmission Pipeline (ETP) is making good progress with an anticipated completion date in 2007. The ETP will reinforce supply and enhance system integrity, placing us in an excellent position to meet any rise in gas demand due to urban growth and renewal in the eastern New Territories and Kowloon generally. By enlarging our peak gas supply capacity through the ETP, we will successfully augment network configuration and boost supply security for many years to come.

We were very encouraged during 2005 by the support of the government and utility trades for our suggestion to seal cable ducts leading into manholes to mitigate seepage accumulation, and thus potential combustion, of gas. Our strenuous efforts to get all parties concerned to review the potential hazards and strive for a practical solution demonstrates Towngas'

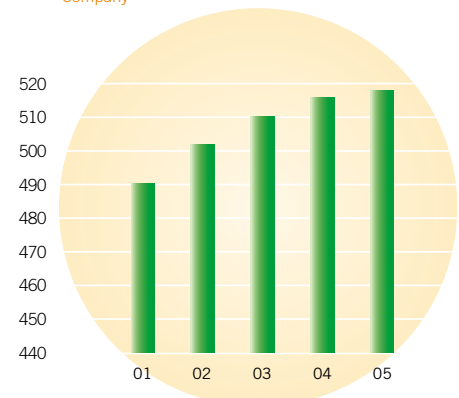
Turnover per Employee

Company (HK\$ thousand)



Number of Customers per km of Mains

Company



Towngas Network in Hong Kong



commitment to ensuring public safety. As such, the relevant government authorities have now prescribed requirements for sealing of ducts entering buildings into their codes of practice, and the Highways Department has recommended utility operators consider similar measures for manholes in the streets. The Highways Department has also commissioned a detailed study of the issue.

Employees and Managing Change

Thriving businesses seek to excel at everything they do and be the best in their field. This last year, Towngas people showed a spirit to win, a will to succeed, a drive to learn, and the courage to stir beyond their comfort zone and face new challenges. Their creativity and motivation are two key success factors for development of our corporate environment.

Our Superior Quality Service programme, which promotes better work efficiency and service quality, saw 800 SQS team members complete 65 projects in 2005, generating HK\$23 million in tangible benefits for both our core and diversified businesses. One SQS team also won the My Favourite Quality Circle award in the Quality Improvement and Experience Sharing Convention 2005, and an award at the 11th Hong Kong Quality Management and First Six

Sigma Convention, both superb achievements given they were competing against several other renowned local organisations for these coveted prizes.

Towngas' Technical Training Centre (TTC) and Learning and Development (L&D) section also play a vital role in enhancing knowledge and ensuring staff keep pace with the demands of a growing and transforming organisation. Relocated, redesigned and re-equipped in 2005, TTC is now at the cutting-edge for delivery of technical competency whilst L&D's encouraging efforts during the year to upgrade performance of our frontline sales and service staff underlined their position in helping employees develop their potential.

Our 2005 graduate trainee intake was the first to benefit from a new comprehensive scheme aimed at providing a strong, across-the-board foundation covering all aspects of the gas industry. The scheme additionally has the big advantage of enabling pick-and-mix components to be used for recent recruits and for technical staff refresher training. TTC is also now preparing a series of complementary e-learning

modules so material is easily accessible by joint venture colleagues.

Indeed, we expect out-reach initiatives generally to become an increasingly important aspect of our home-based training strategy so as to better facilitate transfer of Hong Kong best practices and consistency of engineering quality across the Group. TTC will have a pivotal function in the coming year in helping to develop staff to meet expansion of our new diversified water business. L&D's training input for JV colleagues, up by 71 per cent in 2005 compared to the previous year, is equally expected to intensify in 2006, particularly as we increase exposure of our mainland staff to modern management practices and related skills.

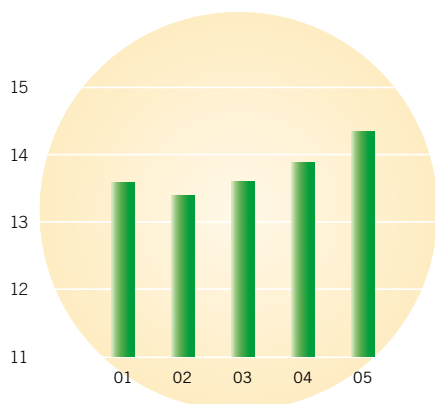
Towngas' service-pro campaign, which has brought a high standard of consistency to all our Hong Kong customer centres in the last few years, gained the bronze prize in 2005, under the Hong Kong Management Association's Award for Excellence in Training. We were also very pleased that two of our apprentices were amongst the ten winners chosen by the Vocational Training Council for their 2005 Outstanding Apprentice/Trainee Awards.

Our newly-renovated, state-of-the-art Technical Training Centre is the lynchpin for developing the Company's gas installation and maintenance engineers.



Town Gas Sales per Employee

Company (million MJ)



In addition, four of our graduate trainees successfully represented Towngas in the prestigious Hong Kong Management Game in 2005, coming in a second runner-up against strong competition. In-house, our Outstanding Employee roll of honour list was extended to our diversified businesses in recognition of their growing role within the Company. We also stepped up support for middle management colleagues during 2005 to encourage them to widen their professional and personal experience and sense of adventure by working in the mainland.

Corporate Social Responsibility

Here at Towngas, we take our corporate social responsibility (CSR) commitments very seriously; we always have. The Company has an enviable tradition of giving back to a community that has consistently given us their utmost support and loyalty down the years.

Our principles are based on our strong belief that CSR should be rooted in partnership where we work with others not for them. The success of this focus was underlined in February 2005 when we received the Outstanding Partnership Project award of the Caring Company Scheme for teaming up with the Senior Citizen Home Safety Association to check emergency links for the elderly during routine gas inspections.

Shareholders' fact-finding and experience-sharing tours of Tai Po gas production plant are very popular.



The framework on which our philosophy hangs is the time our employees give to arranging and taking part in community events. As Hong Kong is one of the best culinary cities in the world, it is no surprise then that many of our CSR programmes revolve around food! So from preparing traditional turnip cakes at Chinese New Year with popular local celebrities and wrapping rice dumplings with school children and district councillors during the Dragon Boat Festival in May and June, to making mooncakes for the delightful mid-autumn festival, our enthusiastic volunteers shared their spirit of generosity with others from the community throughout 2005 to bring warmth and harmony to our senior citizens during Hong Kong's many traditional celebrations.

We also like to take part in events where we feel the Company as a whole can make a lasting contribution to initiatives or programmes that really do make a difference to people's well-being. The Community Chest of Hong Kong is a much-loved, much-respected independent organisation whose concern for the welfare of the needy is very close to Towngas. Donations through a series of special day events – Skip Lunch, Dress Casual, etc – are always well-supported by employees and earned us the Community Chest President's



Celebrating founding of Towngas' first customer volunteer team at mooncake delivery event in September.

Award for the 11th year running in 2005. We were also pleased to be able to extend our reach beyond Hong Kong this last year by sponsoring Oxfam China Development Fund's Rice Sale, a project to help poverty alleviation and emergency relief in the mainland.

As we are one of the main energy suppliers in the market, we are always looking for ways to increase our value to our customers. In this respect, our Customer Focus and District Council Focus teams continued to do a great job during the year at channelling customer suggestions, as well as concerns, to relevant departments. The teams helped us to become better at conducting our business and at the same time gave us a chance to explain our plans and strategies directly to community representatives.

There is worth and merit in sharing our particular employees' skills and the Company's operations with the general public and interested specialists. This creates greater accountability and transparency and opens up a world that is often a closed book to many people. To give but a few examples for 2005: we organised a number of well-attended tours of our main Tai Po gas plant to enhance shareholders' understanding of gas production and its complexity; we took on interns from secondary schools and universities to provide them with some business exposure before entering the workplace; and we arranged one-year, on-the-job management training for executives from mainland China in partnership with the Business and Professionals Federation of Hong Kong.