

REPORT OF THE DIRECTORS

The Directors have pleasure in submitting to shareholders their Report and the Audited Accounts for the year ended 31st December 2005 which are to be presented at the Annual General Meeting to be held in the Four Seasons Grand Ballroom, Four Seasons Hotel, 8 Finance Street, Central, Hong Kong on Friday, 19th May 2006.

Principal Activities

The principal activities of the Company continue to be the production, distribution and marketing of gas and related activities. The particulars of the principal subsidiaries are shown on pages 118 to 120 of this Annual Report. Turnover and contribution to operating profit are derived from activities carried out in Hong Kong and the Mainland China.

Results and Appropriations

The results of the Group for the year ended 31st December 2005 are set out in the consolidated income statement on page 62 of this Annual Report.

An interim dividend of HK 12 cents per share was paid to shareholders on 24th October 2005 and the Directors recommend a final dividend of HK 23 cents per share payable on 22nd May 2006 to shareholders whose names are on the register of members on 12th May 2006.

Financial Summary

A summary of the results of the Group for the past nine financial years is set out on pages 48 and 49 of this Annual Report.

Reserves

Movements in reserves of the Group and the Company during the year are set out in Note 37 to the Accounts.

Property, Plant and Equipment

Movements in property, plant and equipment of the Group and the Company including the details of property under development are shown in Note 16 to the Accounts.

Share Capital

Movements in share capital of the Company are shown in Note 35 to the Accounts.

Borrowings

Particulars of the borrowings of the Group are provided in Note 32 to the Accounts.

Financial Assistance and Guarantees to Affiliated Companies

As at 31st December 2005, the Group has provided financial assistance and guarantees to certain of its associated companies and jointly controlled entities (collectively, the “affiliated companies”) totalling HK\$5,044 million, representing approximately 30 per cent of the Group’s net assets. Pursuant to rule 13.22 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”), a combined balance sheet of the affiliated companies and the Group’s attributable interests as at 31st December 2005 are set out below:

| | Combined Balance Sheet HK\$ Million | Group’s attributable interests HK\$ Million |
|-------------------------|---|--|
| Non-Current Assets | 30,836 | 6,181 |
| Current Assets | 9,472 | 4,062 |
| Current Liabilities | (19,664) | (4,748) |
| Non-Current Liabilities | (8,199) | (1,784) |
| Net Assets | 12,445 | 3,711 |
| Share Capital | 1,486 | 733 |
| Reserves | 10,555 | 2,917 |
| Minority Interests | 404 | 61 |
| Total Equity | 12,445 | 3,711 |

Particulars of the financial assistance, guarantees of banking facilities and committed capital injection for the affiliated companies are shown in Notes 20, 21, 38 and 39 to the Accounts.

Charitable Donations

Charitable donations made by the Group in 2005 amounted to HK\$4,452,000 (2004: HK\$1,098,000), of which HK\$3,351,000 was donated for the purpose of Southeast Asia tsunami relief in 2004.

Directors

At the Annual General Meeting held on 4th May 2005, Mr. Lee Ka Kit and Mr. Leung Hay Man were re-elected as Directors of the Company. Dr. Lee Shau Kee, Mr. Liu Lit Man, Mr. Colin Lam Ko Yin, Dr. The Hon. David Li Kwok Po, Mr. Ronald Chan Tat Hung, Mr. Alfred Chan Wing Kin, Mr. James Kwan Yuk Choi and Mr. Lee Ka Shing held office throughout the year.

According to the Company’s Articles of Association, one-third of the non-executive directors and one-third of the executive directors are subject to retirement by rotation at every annual general meeting. Pursuant to Article 97, Dr. Lee Shau Kee, Mr. Liu Lit Man and Dr. The Hon. David Li Kwok Po, non-executive directors, and Mr. Ronald Chan Tat Hung, an executive director, are due to retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for reappointment. Details of these directors proposed for re-election are set out in the circular sent together with this Annual Report.

Biographical Details of Directors

The biographical details of Directors and senior management who are also executive directors are set out on pages 11 and 12 of this Annual Report.

Disclosure of Interests

A. Directors

As at 31st December 2005, the interests and short positions of each Director of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (“SFO”)) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the “Exchange”) pursuant to the Model Code for Securities Transactions by Directors of Listed Companies were as follows:

Shares (Long Positions)

| Name of Company | Director | Personal Interests | Family Interests | Corporate Interests | Other | Total | %** |
|---|-------------------------------|--------------------|------------------|---------------------------|---------------------------|---------------|-------|
| The Hong Kong and China Gas Company Limited | Dr. Lee Shau Kee | 3,226,174 | | 2,157,017,776 (Note 5) | | 2,160,243,950 | 39.21 |
| | Mr. Liu Lit Man | 1,778,681 | | | | 1,778,681 | 0.03 |
| | Dr. The Hon. David Li Kwok Po | 14,000,000 | | | | 14,000,000 | 0.25 |
| | Mr. Ronald Chan Tat Hung | 1,940 | | | | 1,940 | 0.00 |
| | Mr. Lee Ka Kit | | | | 2,157,017,776 (Note 4) | 2,157,017,776 | 39.16 |
| | Mr. Chan Wing Kin | 102,825* | | | | 102,825* | 0.00 |
| | Mr. James Kwan Yuk Choi | 36,300 | 41,129 | | | 77,429 | 0.00 |
| | Mr. Lee Ka Shing | | | | 2,157,017,776 (Note 4) | 2,157,017,776 | 39.16 |
| Lane Success Development Limited | Dr. Lee Shau Kee | | | 9,500 (Note 6) | | 9,500 | 95 |
| | Mr. Lee Ka Kit | | | | 9,500 (Note 6) | 9,500 | 95 |
| | Mr. Lee Ka Shing | | | | 9,500 (Note 6) | 9,500 | 95 |
| Primeland Investment Limited | Dr. Lee Shau Kee | | | 95 (Note 7) | | 95 | 100 |
| | Mr. Lee Ka Kit | | | | 95 (Note 7) | 95 | 100 |
| | Mr. Lee Ka Shing | | | | 95 (Note 7) | 95 | 100 |
| Yieldway International Limited | Dr. Lee Shau Kee | | | 2 (Note 8) | | 2 | 100 |
| | Mr. Lee Ka Kit | | | | 2 (Note 8) | 2 | 100 |
| | Mr. Lee Ka Shing | | | | 2 (Note 8) | 2 | 100 |

* These shares were jointly held by Mr. Chan Wing Kin and his spouse.

** Percentage which the aggregate long position in the shares represents to the issued share capital of the Company or any of its associated corporations.

Disclosure of Interests (continued)

A. Directors (continued)

Save as mentioned above, as at 31st December 2005, there were no other interests or short positions of the Directors in any shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) recorded in the register maintained by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

B. Substantial Shareholders and Others (Long Positions)

As at 31st December 2005, the interests and short positions of every person, other than Directors of the Company, in the shares and underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO were as follows:

| | Name of Company | No. of Shares in which interested | %** |
|---|---|--------------------------------------|-------|
| Substantial Shareholders (a person who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting) | Disralei Investment Limited (Note 1) | 1,159,024,597 | 21.04 |
| | Timpani Investments Limited (Note 1) | 1,643,249,599 | 29.83 |
| | Henderson Investment Limited (Note 1) | 2,072,571,545 | 37.62 |
| | Kingslee S.A. (Note 1) | 2,072,571,545 | 37.62 |
| | Henderson Land Development Company Limited (Note 1) | 2,072,571,545 | 37.62 |
| | Henderson Development Limited (Note 2) | 2,076,538,017 | 37.70 |
| | Hopkins (Cayman) Limited (Note 3) | 2,157,017,776 | 39.16 |
| | Riddick (Cayman) Limited (Note 4) | 2,157,017,776 | 39.16 |
| | Rimmer (Cayman) Limited (Note 4) | 2,157,017,776 | 39.16 |
| Persons other than Substantial Shareholders | Macrostar Investment Limited (Note 1) | 429,321,946 | 7.79 |
| | Medley Investment Limited (Note 1) | 484,225,002 | 8.79 |

** Percentage which the aggregate long position in the shares represents to the issued share capital of the Company.

Save as mentioned above, as at 31st December 2005, the register maintained by the Company pursuant to section 336 of the SFO recorded no other interests or short positions in shares and underlying shares of the Company.

Notes:

- These 2,072,571,545 shares were beneficially owned by Macrostar Investment Limited ("Macrostar"), Medley Investment Limited ("Medley") and Disralei Investment Limited ("Disralei"). Macrostar was a wholly-owned subsidiary of Henderson Investment Limited ("HI"). Medley and Disralei were wholly-owned subsidiaries of Timpani Investments Limited, which was in turn, a wholly-owned subsidiary of HI. Kingslee S.A., a wholly-owned subsidiary of Henderson Land Development Company Limited ("HLD"), owned 73.48 per cent of the total issued shares in HI.
- Henderson Development Limited ("HD") beneficially owned 61.87 per cent of the total issued shares of HLD. Of these 2,076,538,017 shares, 2,072,571,545 shares represented the shares described in Note 1 and the other shares were beneficially owned by a wholly-owned subsidiary of HD.
- Of these 2,157,017,776 shares, 2,076,538,017 shares represented the shares described in Notes 1 and 2 and 80,479,759 shares were beneficially owned by Fu Sang Company Limited ("Fu Sang"). Hopkins (Cayman) Limited ("Hopkins") owned all the issued ordinary shares which carry the voting rights in the share capital of HD and Fu Sang as trustee of a unit trust ("Unit Trust").
- These 2,157,017,776 shares are duplicated in the interests described in Note 3. Rimmer (Cayman) Limited ("Rimmer") and Riddick (Cayman) Limited ("Riddick"), as trustees of respective discretionary trusts, held units in the Unit Trust. Mr. Lee Ka Kit and Mr. Lee Ka Shing, as discretionary beneficiaries of the discretionary trusts, were taken to have duties of disclosure in relation to these shares by virtue of Part XV of the SFO.

Disclosure of Interests (continued)**B. Substantial Shareholders and Others (Long Positions)** (continued)

Notes: (continued)

5. These 2,157,017,776 shares included the shares described in Notes 1 to 4. Dr. Lee Shau Kee beneficially owned all the issued shares in Rimmer, Riddick and Hopkins and was taken to be interested in these shares by virtue of Part XV of the SFO.
6. These 9,500 shares in Lane Success Development Limited were beneficially owned by a wholly-owned subsidiary of the Company (as to 4,500 shares) and a wholly-owned subsidiary of HLD (as to 5,000 shares). Dr. Lee Shau Kee, Mr. Lee Ka Kit and Mr. Lee Ka Shing were taken to be interested in HLD and the Company as set out in Notes 1 to 5 by virtue of Part XV of the SFO.
7. These 95 shares in Primeland Investment Limited were beneficially owned by a wholly-owned subsidiary of the Company (as to 30 shares) and a wholly-owned subsidiary of HLD (as to 65 shares). Dr. Lee Shau Kee, Mr. Lee Ka Kit and Mr. Lee Ka Shing were taken to be interested in HLD and the Company as set out in Notes 1 to 5 by virtue of Part XV of the SFO.
8. These 2 shares in Yieldway International Limited were beneficially owned by a wholly-owned subsidiary of the Company (as to 1 share) and a wholly-owned subsidiary of HLD (as to 1 share). Dr. Lee Shau Kee, Mr. Lee Ka Kit and Mr. Lee Ka Shing were taken to be interested in HLD and the Company as set out in Notes 1 to 5 by virtue of Part XV of the SFO.

Service Contracts

No Director proposed for re-election at the forthcoming Annual General Meeting has entered into any service contract with the Company which is not determinable by the Company within one year without payment of compensation other than statutory compensation.

Interests in Contracts and Connected Transactions

The Group had 18.05 per cent equity interest in Henderson Cyber Limited ("HCL"). HCL had been listed on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited ("GEM") since July 2000. The Company, Henderson Land Development Company Limited ("HLD"), Henderson Investment Limited ("HI") and HCL issued a joint announcement on 16th August 2005 (the "Announcement") regarding a proposed privatisation of HCL by HI and the Company by way of a scheme of arrangement under Section 86 of the Companies Law of the Cayman Islands (the "Scheme") involving the cancellation and extinguishment of shares held by shareholders of HCL (other than those indirectly held by HI and the Group) (the "Scheme Shares") at the cancellation price of HK\$0.42 (the "Cancellation Price") per share.

The Group has entered into the following transactions and arrangements as described below with persons who are "connected" for the purposes of the Listing Rules:

- (i) The shares of HCL in which HLD, Dr. Lee Shau Kee and Fu Sang Company Limited ("Fu Sang") were interested as at 16th August 2005, the date of the Announcement, had an aggregate value of approximately HK\$3.89 million based on the Cancellation Price. As HLD, Dr. Lee Shau Kee and Fu Sang are connected persons of the Company, the payment by the Company of 21.31 per cent of the Cancellation Price of approximately HK\$0.83 million to them in consideration for the cancellation of their interests in HCL constituted a connected transaction for the Company under the Listing Rules.
- (ii) The entering into an arrangement between HI and the Company for payment by HI and the Company of 78.69 per cent and 21.31 per cent respectively of the total consideration payable for the Scheme Shares also constituted a connected transaction for the Company as HI is a connected person of the Company.
- (iii) The acquisition by the Company of the Scheme Shares from non-connected persons under the Scheme constituted a connected transaction for the Company as it acquired interests in HCL, where a substantial shareholder of HCL, being HI, is a controller of the Company.

Interests in Contracts and Connected Transactions (continued)

The Scheme was approved by the shareholders of HCL at the Court Meeting and Extraordinary General Meeting both held on 31st October 2005. Following the effective date of the Scheme on 8th December 2005 and the withdrawal of listing of the Shares of HCL on GEM on 12th December 2005, the Group's equity interest in HCL increased to approximately 21.31 per cent.

Save as the above, no contracts of significance in relation to the Group's business to which any controlling shareholder of the Company or any of its subsidiaries was a party, and in which a Director of the Company had a material interest, whether directly or indirectly, subsisted at the year-end or at any time during the year.

Management Contracts

No contract concerning the management and administration of the whole or any substantial part of the business of the Company was entered into or existed during the year.

Purchase, Sale or Redemption of Own Shares

During the year, the Company repurchased 106,010,000 shares on The Stock Exchange of Hong Kong Limited at an aggregate consideration of HK\$1,677,034,850 before expenses. The repurchased shares were subsequently cancelled. The nominal value of the cancelled shares was transferred to the capital redemption reserve and the aggregate consideration was charged to unappropriated profits. The repurchases were effected by the Directors for the enhancement of shareholder value in the long term. Details of the shares repurchased are as follows:

| Month of Repurchase | Number of Shares Repurchased | Price per Share | | Aggregate Consideration Paid |
|---------------------|------------------------------|-----------------|--------|------------------------------|
| | | Highest | Lowest | |
| | | HK\$ | HK\$ | HK\$ |
| January 2005 | 16,713,000 | 15.80 | 15.25 | 259,470,550 |
| February 2005 | 200,000 | 15.65 | 15.65 | 3,130,000 |
| March 2005 | 6,575,000 | 15.65 | 15.20 | 101,652,900 |
| April 2005 | 12,415,000 | 15.70 | 15.00 | 191,624,150 |
| September 2005 | 6,067,000 | 16.15 | 15.90 | 97,369,150 |
| October 2005 | 62,300,000 | 16.20 | 15.80 | 995,738,850 |
| November 2005 | 1,740,000 | 16.15 | 16.10 | 28,049,250 |
| Total | 106,010,000 | | | 1,677,034,850 |

Save as mentioned above, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of its own shares during the year.

Major Customers and Suppliers

The percentages of the purchases attributable to the Group's largest supplier and the five largest suppliers were 20.6 per cent and 53.8 per cent respectively during the year. None of the Directors, their associates, or any shareholder (who to the knowledge of the Directors owned more than 5 per cent of the Company's share capital) had any interest in the Group's five largest suppliers. The percentage of the turnover attributable to the Group's five largest customers is less than 30 per cent during the year.

Corporate Governance

The Company's corporate governance principles and practices are set out in the Corporate Governance Report on pages 57 to 60 of this Annual Report.

Public Float

As at the date of this report, being also the latest practicable date prior to the issue of this Annual Report, the Company has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Company and within the knowledge of the Directors.

Auditors

The Accounts have been audited by PricewaterhouseCoopers who will retire at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-appointment at a fee to be agreed by the Board.

Lee Shau Kee

Chairman

Hong Kong, 20th March 2006