



浙江滬杭甬高速公路股份有限公司
ZHEJIANG EXPRESSWAY CO., LTD.

EVER DEVELOPING
EVER GROWING

Annual Report 1997

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Company Profile

Zhejiang Expressway Co., Ltd. (the "Company") is a joint stock limited company incorporated in the Peoples' Republic of China (the "PRC") with limited liability in 1997. The H shares ("H Shares") of the Company were listed on The Stock Exchange of Hong Kong Limited ("Hong Kong Stock Exchange") on 15 May 1997.

The Company and its subsidiaries (the "Group") are principally engaged in investing in, operating and developing high grade toll roads in Zhejiang Province, and the development and operation of certain ancillary services, such as automobile servicing and fuel facilities.

The Company is regarded by the Zhejiang Provincial Government as an main enterprise investing in, constructing and operating expressways and Class 1 roads in Zhejiang Province. The Company has been granted an exclusive concession right to construct and operate the Shanghai-Hangzhou-Ningbo Expressway and the Shangyu-Sanmen Road for a period of 30 years. A first right of refusal has also been granted to the Company under which the Company was given priority over other third parties to accept any concession right in respect of any specified road in Zhejiang Province offered by the Zhejiang Provincial Government or its authorised departments.

The Company's principal strategies are:

- to extract maximum value from existing expressways through the building of ancillary facilities and other improvements, and (if appropriate) by adding extra lanes; and
- to build or acquire new toll roads, generate increased traffic flow and revenues, and attract more traffic into the existing toll roads of the Company.

The Company will only select those projects which it considers to be the most economically viable. In the immediate future, the Company will concentrate on building or acquiring new roads which connect with the Shanghai-Hangzhou-Ningbo Expressway with a view to increasing traffic flow into the Company's existing network. In view of the prevailing policies and conditions of the PRC and Zhejiang Provincial government, the Company intends to review its strategies as it deems appropriate in order to expand its asset base, increase its profitability and maximize the shareholders' return.



CONSOLIDATED PROFIT AND LOSS ACCOUNT

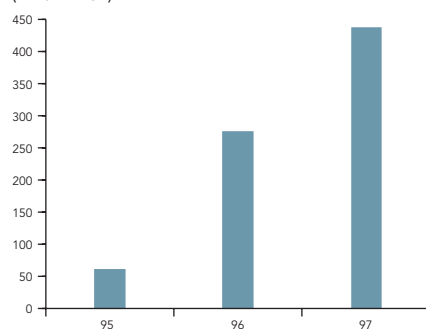
	For the 10 months ended 31 December 1997 Rmb'000	Pro forma For the year ended 31 December 1997 Rmb'000	1996 Rmb'000	Growth (%)
Turnover	376,785	439,789	273,843	60.6
Operating profit before exceptional item	329,044	346,871	159,964	116.8
Exceptional item	25,355	25,355	—	
Operating profit before taxation	354,399	372,226	159,964	132.7
Taxation	(53,085)	(58,639)	(60,296)	
Net profit before minority interests	301,314	313,587	99,668	214.6
Minority interests	(15,986)	(17,255)	186	
Net profit attributable to shareholders	285,328	296,332	99,854	196.8
Transferred to reserves	(45,253)			
Dividends	(69,490)			
Retained profits at the end of the period	170,585			
Earnings per share	7.15 cents	7.77 cents	3.43 cents	126.5

CONSOLIDATED BALANCE SHEET

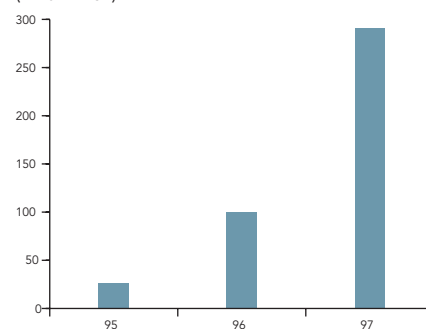
	As at 31 December 1997 Rmb'000	Pro forma 1996 Rmb'000	Change (%)
Total assets	11,466,377	6,222,082	84.3
Total liabilities	(3,266,309)	(3,448,751)	-5.3
Net book value	8,200,068	2,773,331	195.7

Financial Highlights

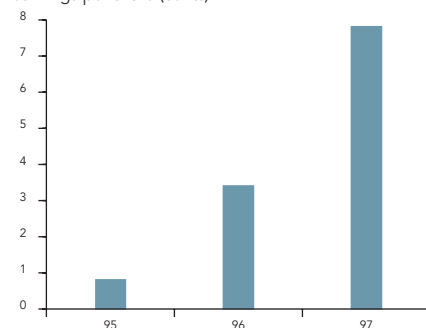
Pro forma
turnover
(Rmb million)



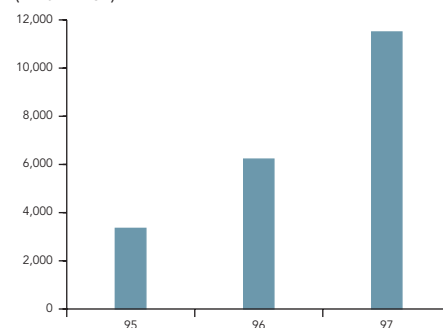
Pro forma
net profit attributable
to shareholders
(Rmb million)



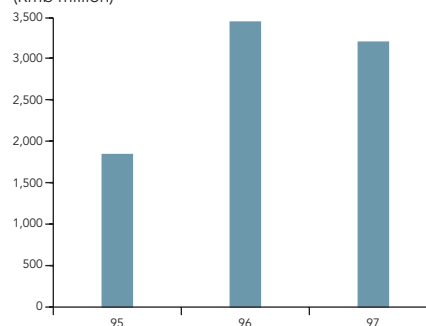
Pro forma
earnings per share (cents)



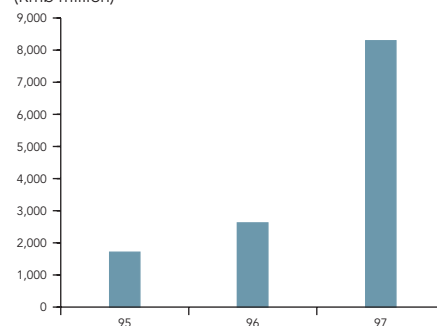
Pro forma
total assets
(Rmb million)



Pro forma
total liabilities
(Rmb million)



Pro forma
net book value
(Rmb million)



Chairman's Statement

Dear Shareholders,

The Company has achieved impressive results in a short period of time since the listing of its H Shares on the Hong Kong Stock Exchange in May 1997. The year of 1997 was a year of celebration when Hong Kong was returned to the PRC. However, the financial turmoil which had swept through Asia (excluding the PRC) during the year caught the world by surprise with a far reaching impact. Notwithstanding the adverse conditions, the H Shares were successfully listed before the handover and the business of the Company has achieved substantial development. Due to the increase in the mileage of roads in operation and appropriate use of capital, pro forma turnover of the Company was increased from Rmb273,843,000 in 1996 to Rmb439,789,000 in 1997 by 60.6 %, pro forma net profit attributable to shareholders was increased from Rmb99,854,000 in 1996 to Rmb296,332,000 in 1997 by 196.8% (exceeding the forecast set out in the prospectus for the offer of H Shares issued by the Company on 6 May 1997 ("Prospectus") by 48.2%) and pro forma earnings per share increased from Rmb0.034 in 1996 to Rmb0.077 in 1997 by 126.5%.

The Company aims to maximize shareholders' returns and to develop infrastructure in the PRC and in particular, in the Zhejiang Province. I believe that these two goals complement each other.

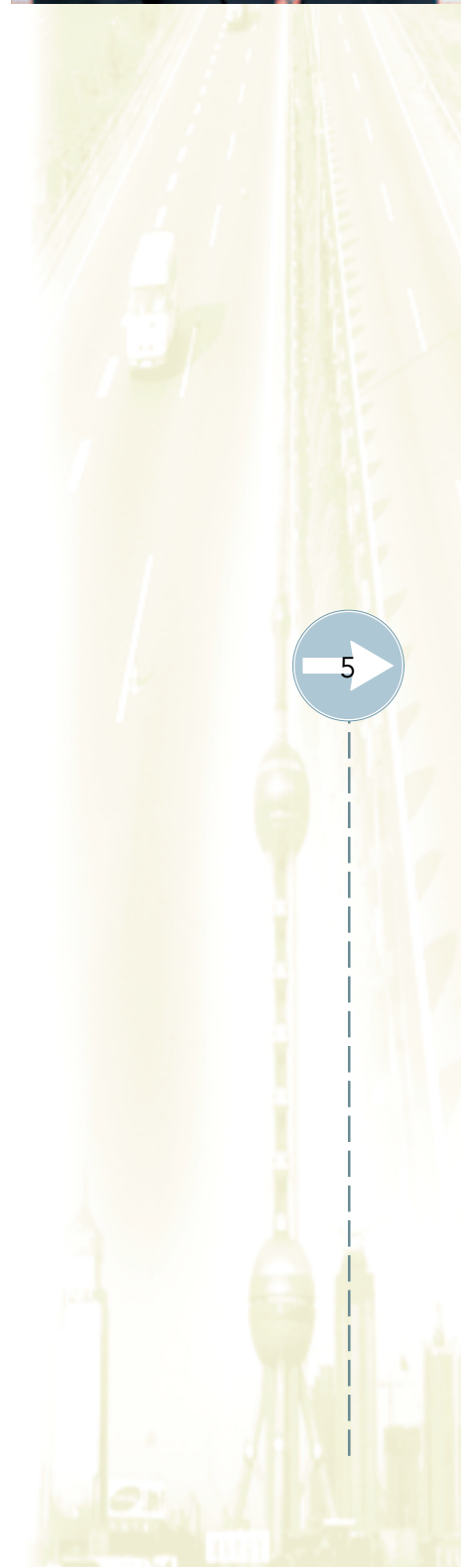
Three Objectives

The Company has striven to achieve the following three objectives since its listing:

- to achieve the forecast of consolidated profit after taxation and minority interests but before extraordinary items of the Group for the year ended 31 December 1997 in the sum of Rmb200 million;
- to proceed with various investment projects and to appropriately use the proceeds raised from the issue of H Shares; and
- to raise the standard of the Company to meet international standard, to improve the transparency of the Company and to improve its corporate image.

The first objective has been outperformed with the dedication of all of the staff of the Company.

The second objective is a mid-term target. The Company has applied 34.5% of the proceeds from the issue of H Shares for, inter alia, contribution to the capital of Zhejiang Jiaying Expressway Company Limited ("Jiaying Co") and the new Shangyu-Sanmen Road project. To maximize the returns of the unused proceeds, some of them were placed in short-term deposits and others were invested in government bonds and government bond repurchase agreements.





Chairman's Statement

Three Objectives *(continued)*

The last objective is a long-term goal. Raising the standard of the Company to meet international standard means refining the corporate philosophy, operating mechanism, management skill and mode of practice of the Company.

I stress that this is a gradual process and not an end. During this process, the Company and its staff continue to seek to improve their abilities and improve management efficiency. As such, the Company's asset and profit will be strongly enhanced and as a result, the shareholders will benefit from this.

Improving the transparency of the Company means strengthening the communication among its staff, shareholders, investors and the government to enable them to have a better understanding of the Company. Since the listing of H Shares, the Company has achieved effective communications by a number of ways, including holding promotion activities, arranging for research analysts and fund managers to visit the toll roads, and participating in presentations held by various organizations. These activities helped improve its corporate image and strengthen confidence of international investors in the Company's management.

Looking Ahead

I believe the longer the term of the objective, the more difficult it is to achieve. Long term objectives and the interests of the Company largely depend on its management, contributions from its staff and support of its shareholders and the government.

The Company is committed to enhancing the value of its shares through effective corporate management and strategic planning.

Corporate Management

Building on its own management experience and taking into consideration the management experiences of those outstanding local and overseas companies, the Company is to set up a management system that is both pragmatic and of international standards and requirements.

This system includes laying down the rules governing duties of the board of directors (the "Directors") with a view to developing a self-regulating mechanism. This helps ensure that the Directors always act in the best interests of the Company. Measures will also be introduced to improve the Company's communication channels. Different departments of the Company are required to follow certain objectives and behaviour codes. This helps the departments coordinate their operations, carry out their respective duties and accomplish the Company's overall objectives.

The Company will also adopt a flexible system of staff recruitment, assessment, motivation and training. The Company also aims to provide its staff with a pleasant working environment to enable them to attain job satisfaction so as to contribute to the Company. The Company will continue to recruit outstanding and experienced professionals and improve qualifications of staff.



Strategic Planning : Development

To enable the Group to take any favourable opportunities, the Company reviews its development strategies from time to time.

The Directors believe that economic reforms in the PRC will be further carried out and the government also encourages large enterprises which are financially sound and competitive to acquire and merge with other existing enterprises in order to improve their efficiency and productivity. In addition, the Directors believe that the PRC government also encourages investment in infrastructure projects.

Looking ahead, the Company also plans to invest in other road-related projects, with a view to broadening the Company's scope of business. In light of the PRC government's current policy which encourages the development and investment in infrastructure projects whilst continuing to engage in operation of toll roads, the Group also wishes to invest in other transportation-related infrastructure projects' gradually.

The memorable year of 1997 is over and the Company is facing a more challenging year ahead. The Company believes, that with the dedication of its staff, the continuous support of its shareholders as well as the government, the Company will be able to achieve a stable growth in the forthcoming year.

Geng Xiaoping

Chairman and General Manager

Hangzhou, Zhejiang Province, the PRC

24 March 1998



Management Discussion and Analysis

General Situation of Zhejiang Province

Since the economic reform and implementation of the open door policy, Zhejiang Province has experienced rapid social and economic growth and has become economically strong. From 1992 to 1996, the average annual growth rate of the gross domestic production ("GDP") of Zhejiang Province was 32.5%. In 1997, Zhejiang Province maintained a stable economic growth. Its GDP for the year reached Rmb460 billion, increasing by 11% when compared with last year whilst its per capita GDP was Rmb10,374, increasing by 10% when compared with last year.

Market prices of goods have been rising at low rates. The retail price of commodities and the retail price of consumption goods for the whole year increased by 0.4% and 2.8% respectively over last year, representing a 5.4% and 5.1% drop respectively in increase rates when compared with last year.

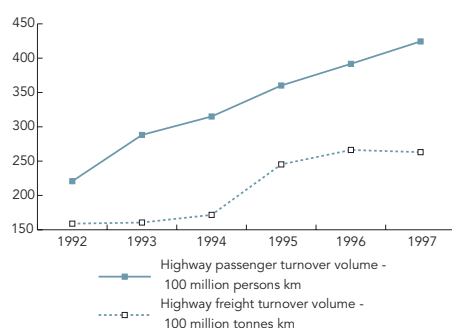
General Situation of Road Traffic

In the last five years, Zhejiang Province has witnessed the largest scale of investment and fastest development in its transportation infrastructure. The total investment for the past five years amounted to Rmb27 billion and the total length of roads built was 36,532 km, the total length of newly built roads in Zhejiang Province was 4,608 km, of which expressways accounted for 161 km, and Class 1 roads, 414 km. In 1997, an additional 10 km of expressways and 225 km of Class 1 roads were in operation.

In 1997, the freight traffic volume by various transport modes was 91.52 billion tonnes km with an increase of 1.6% from last year, of which 17.22 billion tonnes km was by railways (decreased by 3.7%), 26.3 billion tonnes km was by roads (decreased by 1.2%) and 48 billion tonnes km was by waterways (increased by 5.3%). The passenger traffic volume for the whole year was 53.6 billion persons km, representing an increase of 7.0% over last year,

General Situation of Road Traffic *(continued)*

a total of 10.12 billion persons km, 42.43 billion persons km and 1.08 billion persons km were attributed to railways, road and waterways respectively, representing an increase of 3.1% and 8.3% and a decrease of 3.7% respectively.



The cargo handling capacity of the important ports along the coastal line was 0.13 billion tonnes for the year, representing an increase of 23.5% when compared with last year.

However, transportation in Zhejiang Province still lags behind the economic and social developments of the PRC. The main indices of the traffic infrastructure of Zhejiang Province, such as class and length of roads, are only at the nation's medium level.

Zhejiang Province is planning to increase the length of high grade roads to approximately 1,000 km in the next five years, the target is to build "a road network which requires four hours of drive between the provincial capital and the towns" by the completion of the road network consisting of Zhejiang Section of the Shanghai-Hangzhou-Ningbo Expressway, Ningbo-Taizhou-Wenzhou Expressway, Hangzhou-Jinhua-Quzhou Expressway, Shangyu-Shanmen Class 1 Road, Zhejiang section of Hangzhou-Nanjin Expressway and Jinhua-Lishui-Wenzhou Class 1 Road.

Business Review

The revenue of the Company is mainly attributable to the toll income of the Shanghai-Hangzhou-Ningbo Expressway and its connecting road. In 1997, it amounted to Rmb465.27 million, representing an increase of 60.5% over 1996. The significant improvement was due to the increase of traffic mileage of the Shanghai-Hangzhou-Ningbo Expressway. Sections of the expressway which were opened to traffic in 1997 were 158.2 km. Prior to the Hangzhou-Ningbo Expressway becoming fully operational in December 1996, the total length of the sections opened to traffic was approximately 92.8 km. This is an increase by 65.4 km when compared with that in 1996.



Management Discussion and Analysis

Business Review (continued)

Due to the increase of traffic mileage, both the average distance travelled and the toll rate per motor vehicle have significant growth:

	1997	1996	Increase (%)
Annual average daily full trip traffic flows ^{(1) (2)} (number of vehicles)	9,500	9,489	0.1
Average distance travelled ⁽³⁾ (km)	46.19	28.98	59.4
Average toll rate per motor vehicle ⁽⁴⁾ (Rmb)	36.51	27.89	30.9

Notes:

- (1) annual average daily traffic flows = annual total vehicle mileage (traffic mileage *365). The above 1997 figure is smaller than the estimated figure stated in the Prospectus. It is mainly due to two interchanges constructed by Hangzhou Municipal Government between the end of June and December in 1997. The traffic flows were therefore temporarily affected. After completion of the construction, the traffic flows have been improved.
- (2) excluding the toll free vehicles allowed by law.
- (3) average distance travelled = annual total vehicle mileage/annual total number of vehicles which passed through.
- (4) toll rate per motor vehicle = annual total toll revenue/annual total number of vehicles which passed through.

HANGZHOU-NINGBO EXPRESSWAY

The overall length of the Hangzhou-Ningbo Expressway is 145 km. The Hangzhou-Ningbo Expressway starts at Pengbu in the eastern suburb of Hangzhou and passes in a south easterly direction through Xiaoshan, Shaoxing, Shangyu, Yuyao and Yinxian, ending at Dazhujia in the suburbs of Ningbo. The Hangzhou-Ningbo Expressway is wholly-owned by the Company and there are 12 toll stations.

The first section of Hangzhou-Ningbo Expressway, with a length of 7 km, runs from Pengbu of Hangzhou to Xiaoshan. It was opened to traffic in 1992. The section from Xiaoshan to Shangyu was first opened to traffic at the end of 1995, and was fully opened in December 1996. Three interchanges in Keqiao, Guali and Dayin were opened respectively in February, March and November of 1997. Sanjiang service station commenced operation in March in the same year.

Toll revenue of the Hangzhou-Ningbo Expressway in 1997 amounted to Rmb373.52 million, representing an increase of 31.6% from 1996.



Management Discussion and Analysis

SHANGHAI-HANGZHOU EXPRESSWAY

The overall length of the Shanghai-Hangzhou Expressway (in Zhejiang Province) is 102.6 km. The Shanghai-Hangzhou Expressway starts on the boundary between Zhejiang Province and Shanghai Municipality and ends at Pengbu in the eastern suburbs of Hangzhou where it connects with the Hangzhou-Ningbo Expressway. The Shanghai-Hangzhou Expressway has 7 toll stations and comprises the Hangzhou Section, Yuhang Section and Jiaxing Section.

Hangzhou Section

The Hangzhou Section, with an overall length of 3.4 km, connects the Shanghai-Hangzhou Expressway with the Hangzhou-Ningbo Expressway. The Hangzhou Section is wholly-owned by the Company and was opened to traffic at the end of December in 1995. Toll revenue for this section is calculated in proportion to the length of the section bears to the total length of the Shanghai-Hangzhou Expressway. In 1997, toll revenue from this section amounted to Rmb14.74 million, representing an increase of 42.1% over 1996.

Yuhang Section

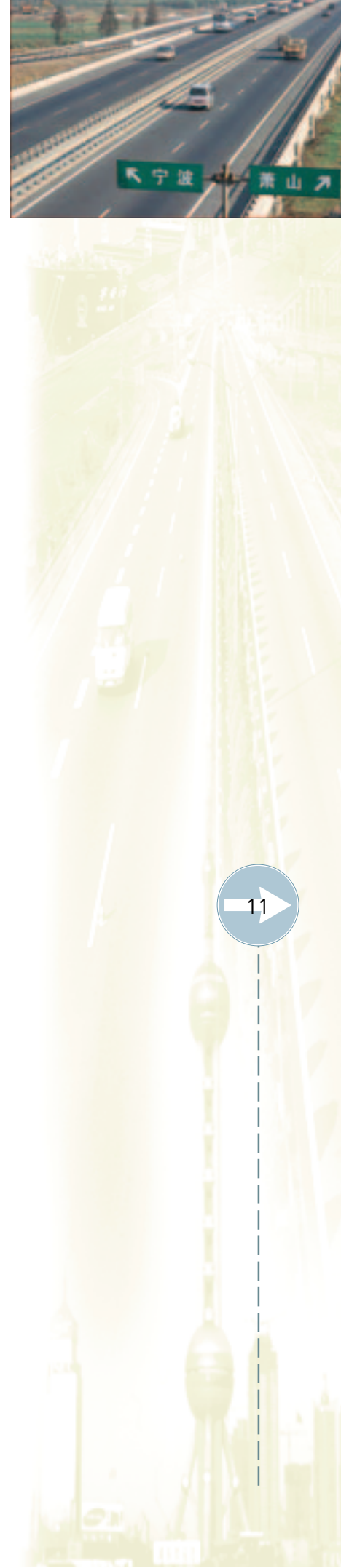
Yuhang Section falls within the boundary of Yuhang County. The total length of Yuhang Section is 11.1 km, of which 9.8 km was opened to traffic and started collecting tolls since the end of December in 1995. The remaining 1.3 km of the section is expected to be operational before the end of 1998, the same time the Jiaxing Section of the Shanghai-Hangzhou Expressway is expected to be operational. Yuhang Section has one toll station.

The Yuhang Section is owned by Zhejiang Yuhang Expressway Company Limited ("Yuhang Co") in which the Company has a 51% interest. Yuhang Co is responsible for the construction, maintenance and management of the Yuhang Section. It also has an interest in a road of 5.7 km connecting National Road 320 to the Yuhang Section ("East Connecting Road"). In 1997, toll revenues from the Yuhang Section and the East Connecting Road amounted to Rmb 77.01 million, representing an increase of 40.3% over 1996.

Jiaxing Section

The Jiaxing Section of the Shanghai-Hangzhou Expressway, with an overall length of 88.1 km, connects Yuhang Section through Haining southwesterly. It extends northeasterly to Shanghai, connecting expressways in Shanghai Municipality.

Jiaxing Section is owned by Jiaxing Co in which the Company originally had a 51% interest. Subsequently, the Company acquired an additional 2.44% interest in Jiaxing Co according to the restructuring arrangement after the Company's listing. The Company's interest in Jiaxing Co increased to 53.44%.





Management Discussion and Analysis

Jiaxing Section *(continued)*

A subscription agreement was signed by the Company, Jiaxing Co and, a shareholder of Jiaxing Co, Zhejiang Jiaxing Road and Bridge Construction and Development Company ("Road and Bridge Co") on 11 April 1997 in respect of the increase in the registered capital of Jiaxing Co by Rmb1 billion. Pursuant to that agreement the parties thereto agreed that the Company and Road and Bridge Co would subscribe for the additional capital of Jiaxing Co in the sum of approximately Rmb 534 million and Rmb 466 million respectively after the listing of the H Shares. On 28 October 1997, the said parties agreed to subscribe for the additional capital of Jiaxing Co according to the following schedule:

	The Company Rmb'000	Road and Bridge Co Rmb'000
October 1997	80,167.5	69,832.5
December 1997	80,167.5	69,832.5
January 1998	80,167.5	69,832.5
March 1998	80,167.5	69,832.5
May 1998	80,167.5	69,832.5
July 1998	80,167.5	69,832.5
September 1998	53,445.0	46,555.0
Total	534,450.0	465,550.0

By December 1997, the Company made a contribution to the registered capital of Jiaxing Co in the sum of approximately Rmb160 million as scheduled. The balance will be invested in 1998 by instalments.

In 1997, the construction works representing 25.73% of the total contract sum of Jiaxing Section were completed and the construction works representing an aggregate of 70.70% of the total contract sum was completed. Paving works, drainage works, protection works, construction of bridges and passageways, and road facilities of the foundation works representing 18.60%, 76.99%, 79.5%, 89.09% and 7.61% of the contract sums respectively were completed. Jiaxing Section is expected to be completed and opened to traffic by the end of 1998.

Shangyu-Sanmen Road

On 8 December 1997, the Company convened an extraordinary general meeting to approve the establishment of a limited liability joint venture company, Zhejiang Shangyu-Sanmen Highway Company Limited ("Shangsan Co"), with Zhejiang Provincial High Class Highway Investment Company Limited ("Provincial Investment Co."), Shangyu Municipal Transport Bureau ("Shangyu Transport"), Shengzhou Municipal Transport Bureau ("Shengzhou Transport"), Xinchang County Transport Development Company ("Xinchang Transport"), Tiantai County Transport Development Company ("Tiantai Transport") and Huajian Transportation Economic Development Centre ("Huajian"), a subsidiary of the Ministry of Communications of the PRC. Shangsan Co will engage in the investment, construction, development, operation and toll-collection of the Shangyu-Sanmen Road and the acquisition of the operational section of Shangyu-Sanmen Road.

The Shangyu-Sanmen Road is a Class I Road which, upon completion, will run from Guzhu Interchange on the Hangzhou-Ningbo Expressway to Wuao Interchange on the Ningbo-Taizhou-Wenzhou Expressway. The total investment of the Shangyu-Sanmen Road, with a total length of 143km, was estimated to be Rmb4,290 million. The construction of the project is divided into two phases. Phase 1, consisting of four short sections in Shangyu, Shenzhou, Xinchang and Tiantai, has a total length of 37.5km and has been operational since February 1997. The construction of the second phase commenced in February 1998 and is intended to be completed by the middle of 2001.

Shangsan Co has a registered capital of Rmb2,400 million, of which Rmb1,224 million was contributed by the Company. Accordingly, the Company owns a 51% interest in the Shangsan Co., while Huajian, Tiantai Transport, Provincial Investment Co., Shangyu Transport, Xinchang Transport and Shengzhou Transport own 18.4%, 7.0%, 6.6%, 6.0%, 6.0% and 5.0% of the interests in Shangsan Co, respectively.

Management Discussion and Analysis

Use of Proceeds

A total of Rmb3,524 million (approximately HK\$3,293 million) was raised by the issue of H Shares after deduction of listing expenses of Rmb155 million (approximately HK\$145 million).

The application of proceeds was in line with proposed application as disclosed in the Prospectus. The proceeds were mainly applied as follows:

		Rmb million
1.	Repayment of loans and interest	
	Repayment of the principal and interest of banking facilities (annual interest rate ranging from 10.98% to 13.14%)	253.5
	Repayment of the principal and interest of loans by the Ministry of Communications of the PRC (annual interest rate of 6.6%)	116.0
	Repayment of interest of loans by World Bank (annual interest rate of approximately 6.5%)	19.0
	Subtotal	388.5
2.	Investment in the Shangyu-Samen Road project	637.5
3.	Investment in Jiaxing Section of the Shanghai-Hangzhou Expressway	160.0
4.	Purchase of approximately 2.44% of the registered capital of Jiaxing Co	29.4
	Total	1,215.4

The Future Plan for the Unused Proceeds

		Rmb million
1.	Investment in the Shangyu-Sanmen Road project	586.5
2.	Investment in the Jiaxing Section of the Shanghai-Hangzhou Expressway	374.0
3.	Investment in the Huzhou Section of the Hangzhou-Nanjing Expressway and related National Road 104 (depending on the outcome of negotiations)	900.0
4.	Payment in respect of Contract No. 8 (to upgrade traffic operation systems)	146.0
	Total	2,006.5

The balance will be used mainly for working capital and repayment of loans and interest.

Management Discussion and Analysis

Financial Review

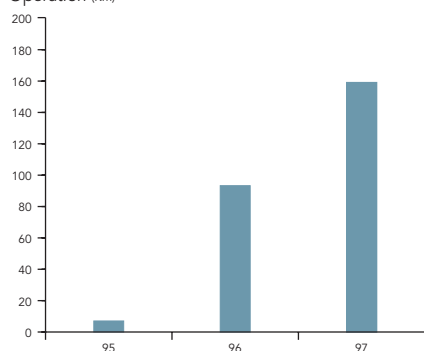
The following discussion and analysis are designed to enhance understanding of the financial performance and condition of the Group. The accounting period for the Company in 1997 was the ten month period from 1 March 1997 to 31 December 1997. The 1996 and 1997 pro forma results are used for comparative purposes. This section should be read in conjunction with the Company's and the Group's audited accounts and notes to the Accounts on pages 33 to 57 of this report.

Turnover

The Group's pro forma turnover increased to Rmb439,789,000 from Rmb273,843,000 in 1996, representing a 60.6% growth. As the toll rate in 1997 remains the same as in 1996, the increase in 1997 turnover was mainly due to the increase in the length of road in operation from 92.8 km in 1996 to 158.2 km in 1997, representing a 70.5% increase.

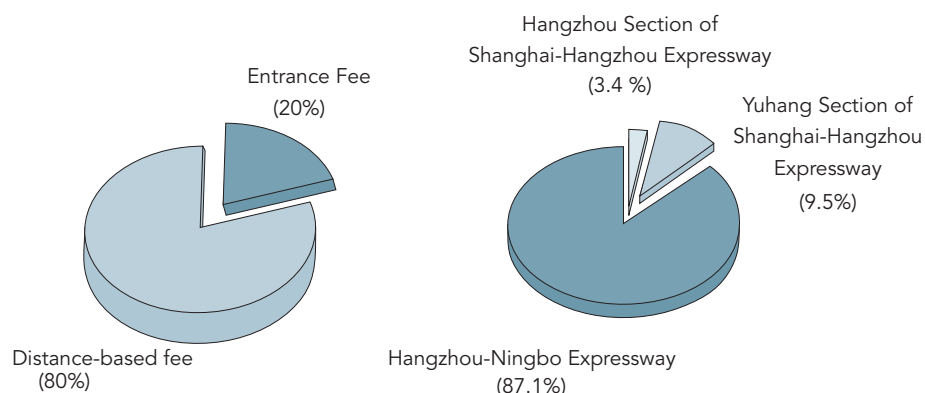
In accordance with the Concession Agreement signed between the Company and the Zhejiang Provincial Government, there will be a first toll rate increase of the Shanghai-Hangzhou-Ningbo Expressway in July 1999.

Length of Road in Operation (Km)



Management Discussion and Analysis

Turnover Contribution



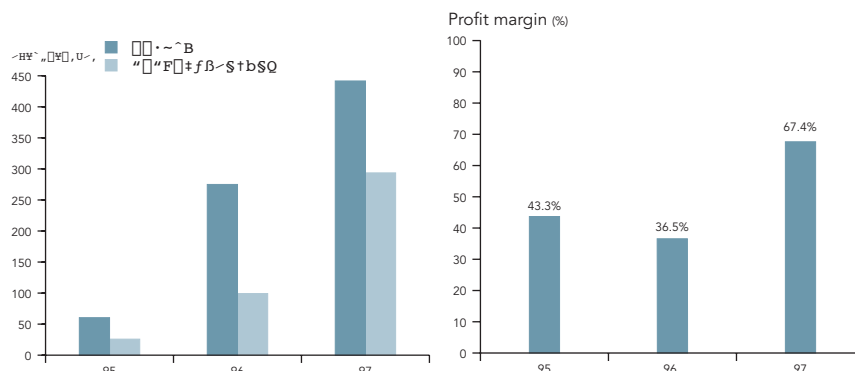
Toll structure of the Company combines both entrance fee and distance-based charge while tolls for most of the other toll roads in the PRC comprise only the distance-based charge. As the entrance fee contributed 20% to the turnover of the Company in 1997, it will be very important to the Company due to the additional roads in operation in the future.

In 1997, Hangzhou-Ningbo Expressway contributed most to the Company's turnover. In January 1998, Shangyu-Sanmen Road Phase 1 (37.5km) began its revenue contribution. Following the construction schedule, by the end of 1998, Shanghai Hangzhou Expressway (Yuhang Section and Jiaxing Section), an expressway connecting Shanghai and Hangzhou, will become fully operational.

The Company will continue to explore opportunities to expand its business to ancillary services such as road-side advertising, communication conduit rental, towing and gas servicing.

Net Profit Attributable to Shareholders

Pro forma net profit attributable to shareholders of the Company increased to Rmb296,332,000, 196.8% growth from 1996. Profit margin (pro forma net profit attributable to shareholders divided by pro forma turnover) reached 67.4% in 1997 from 36.5% in 1996 was mainly due to the increase in interest income (mainly the exceptional item as described in note 5 to the financial statements in page 42 of this report), improved efficiency and further cost control.



Management Discussion and Analysis

Net Profit Attributable to Shareholders *(continued)*

The pro forma net profit attributable to shareholders of the Group for the year ended 31 December 1997 exceeded the forecast net profit attributable to shareholders of the Group referred to in the Prospectus by 48.2% due to the following reasons:

- 1) the funds raised from the issue of H Shares exceeded the estimated amount referred to in the Prospectus and the earned interest has thus increased;
- 2) the high interest rate (10.98%-13.14% per annum) commercial loans have been repaid in advance of the due date and the interest expenditure for the year 1997 was thus decreased;
- 3) the investment to be made in the Huzhou Section of the Hangzhou-Nanjing Expressway has been postponed and the interest income for the year was thus increased; and
- 4) the actual revenue from the non-principal business, including communication conduit rental, roadside advertising, towing and gas servicing, exceeded the estimated revenue by approximately Rmb11 million.

Management Discussion and Analysis

The Year 2000 Problem

The main computer systems of the Company include the financial management system and the toll collection system.

The Company has adopted an advanced financial system. Accordingly, its computer programmes do not have the Year 2000 Problem.

The Company will adopt a new toll collection system for Hangzhou-Ningbo Expressway under Contract No.8 by the end of 1998 in place of the existing toll collection system. The Company also requires the relevant suppliers to ensure the programmes of the new system is free from the Year 2000 Problem.

In the event of adoption of any new computer systems in the future, the Company will take into account of such a problem, in order to avoid any material adverse impact on its sound operational management.

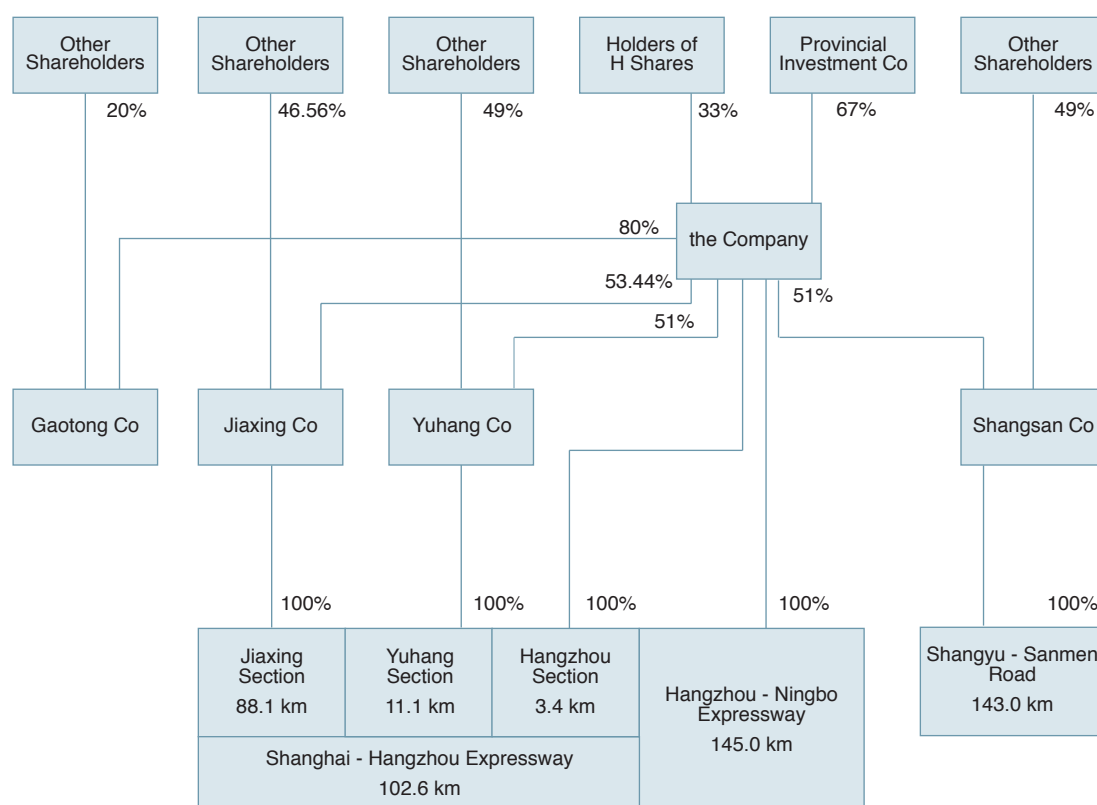
The Effect of Recent Economic Developments on the Company

Since 1997, the economy of Asia has changed greatly, particularly in the second half of 1997. Some regions in Asia, including Southeast Asia, Japan and Korea were in financial crisis. However, the revenue and profit of the Company were not affected.

All businesses of the Company are operated in the PRC. The revenue and profit of the Company would be affected mainly by two factors, namely traffic volume and toll rates with their adjustments. Traffic volume would be affected mainly by economic developments of the PRC and in particular, Zhejiang Province, which has not been materially affected by the recent economic developments in Asia. Toll rates may be adjusted with reference to the compound growth rate of the PRC Retail Price Index every three years.

The revenues of the Company are denominated in Reminbi. In case Reminbi devalues, the profitability of the Company will be adversely affected. Though the Asian financial turmoil puts devaluation pressure on Reminbi, officials of the PRC government have, in various occasions, claimed that in the near future, Reminbi will not devalue, given the satisfying macro economy, import/export trade and foreign reserve conditions in the PRC.

Corporate Structure



Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway with a total length of approximately 145 km and 3.4 km respectively are wholly owned by the Company. It also has a 51% interest in the Yuhang Section of the Shanghai-Hangzhou Expressway (which is approximately 11.1 km long) through Yuhang Co and a 53.44% interest in the Jiaxing Section of the Shanghai-Hangzhou Expressway (which is approximately 88.1 km long) through Jiaxing Co. Hangzhou-Ningbo Expressway together with Shanghai-Hangzhou Expressway are collectively referred to as the "Shanghai-Hangzhou-Ningbo Expressway" and has a total length of 247.6 km. Moreover, the Company has a 51% interest in the Shangyu-Sanmen Road with a total length of 143 km through Shangsan Co.

Zhejiang Gaotong Stone Developing Co., Ltd. ("Gaotong Co") was established on 3 November 1997 in the PRC as a limited liability company, with a registered capital of Rmb5, 000,000. The Company owns 80% of its interests. The other shareholder is an independent third party not connected with the Company. Gaotong Co, by developing a stone market (which is situated beneath the flyover near the Hangzhou toll station of Shanghai-Hangzhou-Ningbo Expressway), is engaged in processing and selling stones, selling stone craftwork, pottery, construction decoration materials and stone processing machinery and moulds, and designing stone decoration works and stone decorations, so as to fully utilize the geographical advantages enjoyed by the expressway.

Directors, Supervisors and Senior Management

Executive Directors and Senior Management

Mr Geng Xiaoping, age 49, is the Chairman of the Board of Directors and General Manager of the Company. He is responsible for the overall management of the Company's business. Mr Geng graduated from the East China College of Political Science and Law in Shanghai and obtained a bachelor's degree in law in 1984. From 1979 until 1991 he worked in various positions at the People's Procuratorate of Zhejiang Province including Division Chief and Deputy Procurator. In 1991, he was appointed the Deputy Director of Zhejiang Provincial Expressway Executive Commission, and responsible for the business operation and administration of the expressway system in Zhejiang. Mr. Geng has entered into a service contract with the Company and works full time for the Company.

Mr Ying Shudeng, age 60, is a senior engineer. He is a Director, the Chief Financial Officer and a Deputy General Manager of the Company and is responsible for administration and finance. Mr Ying obtained a degree from Hangzhou Technical College (which is now Zhejiang University) in 1960 in mechanical engineering specialising in road construction design. Between 1960 and 1962, he completed a masters degree in advanced mathematics from Zhejiang University. In December 1962, he began his career in the transport industry with the Works Bureau of the Zhejiang Provincial Communications Office. His responsibilities included road construction. From 1964 until 1971, he held a number of positions ranging from engineer to Division Chief in the Provincial Communication Office. His responsibilities included transport planning, financial administration, auditing and transport enterprise management. Since 1996 and prior to joining the Company, he was a Deputy Head of the preparatory unit which was responsible for establishing the Company and co-ordinating the reorganization of the Group for the purposes of listing and listing of the Company on the Hong Kong Stock Exchange. Mr Ying has entered into a service contract with the Company and works full time for the Company.

Mr Fang Yunti, age 48, is a Director and Deputy General Manager of the Company. He is responsible for overall operations of the Shanghai-Hangzhou-Ningbo Expressway which includes responsibility for technical equipment used by the Company in its operations. Mr Fang graduated from Qing Hua University with a degree in automotive engineering in 1976. From 1976 to 1988, he was the Deputy Engineer and General Manager of Zhejiang Province Automobile Transport Company. From 1988 to 1990, he was the Chief Engineer at the Provincial Road Transport Company. In 1990, he was appointed as the Head of the Operating Administrative and Technical Equipment Divisions of the Executive Commission where his responsibilities included supervision of the operations and construction of the Shanghai-Hangzhou-Ningbo Expressway. He remained in that position until joining the Company upon its formation. He has entered into a service contract with the Company and works on a full time basis.

Directors, Supervisors and Senior Management

Executive Directors and Senior Management *(continued)*

Mr Xu Yikuang, age 62, is a senior engineer, a Director and the Chief Engineer of the Company and is responsible for planning and development of the Company's operations. Mr Xu graduated from Tong Ji University in 1958 and obtained a degree in engineering, majoring in the construction and design of bridges and tunnels. Since 1958, Mr Xu has held several positions including as the Chief Engineer of the Hunan Province Transport Planning Design Institute, and Chief of the Engineering Administrative Division of the Executive Commission. From 1988 to 1990 he was in charge of the design of the Hangzhou-Ningbo Expressway. From 1990 until 1996, Mr Xu was actively involved in the preparation, assessment, negotiation and implementation of the World Bank loans project in connection with the construction of the Shanghai-Hangzhou-Ningbo Expressway. Mr Xu has more than 40 years of experience in the design, construction and administration of roads and bridges. Since 1996 and prior to joining the Company, Mr Xu was a Deputy Head in the preparatory unit which was responsible for establishing the Company, co-ordinating the reorganization of the Group for the purposes of listing and listing the Company on the Hong Kong Stock Exchange. Mr Xu has entered into a service contract with the Company and works full time for the Company.

Mr Xuan Daoguang, age 53, is a senior engineer, a Director and Manager of the Company. Mr Xuan graduated from the Tong Ji University in 1960 with a degree in engineering, majoring in the construction and design of bridges and tunnels. Mr Xuan has 37 years of experience in engineering maintenance with the Road Administration Division including being the Section Head and, later, the Head of the Road Administrative Division of Jinhua City. Since 1996 and prior to joining the Company, he worked for the Executive Commission and was responsible for the administration of engineering works within Zhejiang Province, including repair and maintenance on the completed sections of the Shanghai-Hangzhou-Ningbo Expressway. Mr Xuan has entered into a service contract with the Company and works full time for the Company.

Mr Zhang Jingzhong, age 34, is a lawyer and is a Director and Company Secretary of the Board of Directors and is responsible for all secretarial and legal matters. He graduated from Hangzhou University in July 1984 obtaining a bachelor's degree in law. In 1984, he joined the Zhejiang Provincial Political Science and Law Policy Research Unit. From 1988 to 1994, he was the Associate Director of Hangzhou Municipal Foreign Economic Law Firm where he obtained considerable experience in company and commercial law. In January 1994, Mr Zhang became the Senior Partner at the T&C Law Firm in Hangzhou. He retired as the Senior Partner to join the Company on 2 April 1997. Mr Zhang has entered into a service contract with the Company and works on a full time basis for the Company.

Directors, Supervisors and Senior Management

Executive Directors and Senior Management *(continued)*

Ms Zhang Chunming, age 33, is a lawyer and is a Director and Manager of the Company and is responsible for legal and securities related issues. She graduated from the East China College of Political Science and Law in Shanghai obtaining a bachelor's degree in law in 1986. From 1987 to 1994, she practised as a lawyer with the Zhejiang Provincial Economics Law Firm in Hangzhou and her practice included financial, securities and property matters. Ms Zhang has also obtained the qualifications required by the regulatory authorities in China to practise law involving securities and, in 1994, she spent six months undergoing training in Hong Kong. Since 1994 she has been a partner of the Shield Law Office in Hangzhou. She has entered into a service contract with the Company under which she has agreed to devote 60% of her time to the Company's business.

Independent non-executive Directors

Dr Hu Hung Lick, Henry O.B.E. PhD, JP., age 78, has been practising as a barrister for over 42 years and is currently the President of Shue Yan College, and a member of the Standing Committee of the Chinese People's Political Consultative Congress and the China International Economic and Trade Arbitration Commission. Dr Hu is also an adviser to the China Research Committee of Juvenile Delinquency.

Mr Tung Chee Chen, age 55, is the Chairman of Orient Overseas (International) Limited. Mr Tung was educated at the University of Liverpool, England, where he received his Bachelor of Science degree. He later acquired a masters degree in Mechanical Engineering at the Massachusetts Institute of Technology in the United States. He is a registered Professional Engineer in the State of California.

Supervisors

Mr Xia Linzhang, age 54, is an engineer, having graduated from Jiao Zou Mining College. Prior to commencing with the Company, he was the Head of Suichang Gold Mine, Deputy Head and Head of Suichang County, Zhejiang Province and Deputy General Secretary of Lishui District. In 1994, he was appointed the Chief of the Planning and Finance Division of the Executive Commission. Mr Xia has extensive experience in project planning, finance and administrative management.

Ms Ge Ailian, age 54, having graduated from Shanghai Maritime College with a major in water transport economics. She has held positions as an accountant, Deputy Chief of the Finance Section, Deputy Manager, and Deputy Chief of the Auditing Division of the Transport Department of Zhejiang Provincial (Communications Office). In 1990, she was appointed Chief of the Planning and Finance Division of the Executive Commission. At present, she serves as Chief of the Supervisory Auditing Division of the Executive Commission. Ms Ge's area of expertise is financial planning and auditing.

Directors, Supervisors and Senior Management

Supervisors *(continued)*

Mr Jiang Wen Yao, age 33, obtained a masters degree in engineering from Zhejiang University with a major in industrial automation and manufacturing mechanics. In 1991, he became involved in the Executive Commission in the areas of engineering administration, financial planning, and advising on technical equipment. In 1996, he was involved in the establishment of the Company. At present, he is a Deputy Manager of the Company. Mr Jiang is experienced in project management, equipment purchase and management, advertising and public relations.

Report of the Directors

The Directors herein present their report and the results of the Group for the period from 1 March 1997 (date of the Company's establishment) to 31 December 1997 (the "Period").

Group Reorganization

The Company was established as a joint stock limited company in the PRC on 1 March 1997. On the same date, the Company issued 2,909,260,000 fully paid domestic shares of Rmb1 each to Provincial Investment Co in consideration of the following:

- (i) acquisition of assets that comprised the exclusive operating rights relating to the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway at a valuation of Rmb208,000,000;
- (ii) 51% equity interests in Yuhang Co and Jiaxing Co; and
- (iii) certain assets and liabilities of Provincial Investment Co, which include all the fixed assets and other long-term assets, together with the current assets and liabilities relating to the daily operations of the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway together with all bank loans and other loans as at 30 November 1996.

Further details of the Company's establishment and the reorganization of the Group in anticipation of its issue of H Shares are set out in the Prospectus and notes 1, 25 and 27 to the financial statements.

Principal Activities

The Group's principal activities consist of investment in the construction, operation and management, of high grade roads as well as the development and operation of certain ancillary services such as automobile servicing and fuel facilities.

Segmented Information

During the Period, the entire turnover and contribution to the operating profit of the Group was derived from toll income earned from expressway operations in Zhejiang Province, the PRC. Accordingly, a further analysis of the turnover and contribution to operating profit by principal activity and geographical area is not presented.

Results and Dividends

The operating results of the Group for the Period and the state of affairs of the Company and the Group as at 31 December 1997 are set out in the financial statements on pages 33 to 57.

The Directors recommend the payment of a dividend of Rmb0.016 (approximately HK\$0.015) per share in respect of the Period to shareholders on the register of members at the close of business on 24 April 1998. This recommendation has been incorporated in the financial statements.

Summary of Financial Information

The only published Group consolidated profit and loss account and balance sheet are as set out on pages 33 and 34 of the financial statements.

The following is a summary of the pro forma consolidated results of the Group prepared on the basis set out in the notes below:

	Year ended 31 December				
	1997	1996	1995	1994	1993
	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000
Results					
Turnover	439,789	273,843	59,105	49,331	40,914
Operating profit before exceptional item	346,871	159,964	41,965	36,351	27,040
Exceptional item	25,355	—	—	—	—
Operating profit before taxation	372,226	159,964	41,965	36,351	27,040
Taxation	(58,639)	(60,296)	(16,378)	(13,915)	(11,025)
Profit before minority interests	313,587	99,668	25,587	22,436	16,015
Minority interests	(17,255)	186	—	—	—
Net profit attributable to shareholders	296,332	99,854	25,587	22,436	16,015
Earnings per share	7.77 cents	3.43 cents	—	—	—

Notes:

1. The pro forma consolidated results of the Group for the four years ended 31 December 1996 have been extracted from the Company's annual report dated 26 July 1997, while those of the year ended 31 December 1997 were prepared based on the profit and loss account as set out on page 33 of the audited financial statements for the 10 months ended 31 December 1997 and the profit and loss account for the two months ended 28 February 1997, which were prepared based on the management accounts of the Relevant Investments of the Old Group as defined in note 1 to the financial statements, after making appropriate adjustments in all material respects to comply with the accounting principles generally accepted in Hong Kong. The summary of the consolidated pro forma results of the Group includes the results of the Company and its subsidiaries as if the current structure of the Group, as outlined in the Group reorganization above and as set out in note 1 to the financial statements, had been in existence throughout the five years ended 31 December 1997.
2. The pro forma earnings per share of 1997 is based on the pro forma net profit attributable to shareholders for the year ended 31 December 1997 of Rmb296,332,000 and 3,812,785,000 shares, being the weighted average of 2,909,260,000 domestic shares, as if they were issued on 1 January 1997, and the 1,433,854,500 H Shares issued on 15 May 1997. The pro forma earnings per share of 1996 is based on the pro forma net profit attributable to shareholders for the year ended 31 December 1996 of Rmb99,854,000 and 2,909,260,000 domestic shares as if they were issued on 1 January 1996.

Major Customers and Suppliers

The five largest customers and suppliers contributed to less than 30% of total toll revenue and purchases, respectively, of the Group during the Period. Accordingly, a corresponding analysis of major customers and suppliers is not presented.

Report of the Directors

Connected Transactions

A summary of the significant connected transactions of the Group is set out in note 32 to the financial statements. In the opinion of the executive Directors and the non-executive Directors, these transactions were:

- (i) entered into in the usual and ordinary course of business of the Group;
- (ii) entered into in accordance with the terms of the respective agreements governing such transactions; and
- (iii) entered into on normal commercial terms and were fair and reasonable so far as the shareholders of the Company are concerned.

Fixed Assets

Details of the movements in fixed assets of the Company and the Group during the Period are set out in note 10 to the financial statements.

Capital Commitments

Details of capital commitments of the Company and the Group as at 31 December 1997 are set out in note 28 to the financial statements.

Subsidiaries

Particulars of the Company's subsidiaries, are set out in note 14 to the financial statements.

Capitalization of Interest

During the Period, interest capitalized to construction in progress amounted to approximately Rmb55,614,000.

Share Capital

Details of movements in the share capital of the Company during the Period, together with the reasons thereof, are set out in note 25 to the financial statements.

Reserves

Details of movements in the reserves of the Company and the Group during the Period are set out in note 26 to the financial statements.

Substantial Shareholders

As at 31 December 1997, the following are interests of 10% or more in the share capital of the Company which were recorded in the register of interests in shares required to be kept by the Company pursuant to Section 16 (1) of the Securities (Disclosure of Interest) Ordinance ("SDI Ordinance"):

	Number of shares	Percentage
Provincial Investment Co	2,909,260,000	67%
	(domestic shares)	
HKSCC Nominees Limited	1,417,477,500	32.64%
	(H Shares)	

Save as disclosed above, no person had registered an interest in the share capital of the Company that was required to be recorded under Section 16(1) of the SDI Ordinance.

Purchases, Sales or Redemption of the Company's Listed Securities

Other than in connection with the Company's initial public offering, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the Period.

Bank Loans and Other Loans

Particulars of the bank loans and other loans of the Group and the Company are set out in notes 20 and 21 to the financial statements.

Use of Proceeds of the Issue of H Shares

A total of Rmb3,524 million (approximately HK\$3,293 million) was raised by the issue of H Shares during the Period after the deduction of listing expenses of Rmb155 million (approximately HK\$145 million), which was used for the following purposes:

- (1) approximately Rmb388.5 million was used to repay the Company's outstanding bank loans and related interest expenses;
- (2) approximately Rmb637.5 million was injected into the Shangyu-Sanmen Road project. Details of the Shangyu-Sanmen Road project are set out in note 29 to the financial statements;
- (3) approximately Rmb160 million was invested in completing the Jiaxing Section of the Shanghai-Hangzhou Expressway;

Report of the Directors

Use of Proceeds of the Issue of H Shares *(continued)*

- (4) approximately Rmb29.4 million was used to purchase approximately 2.44% of the registered capital of Jiaxing Co. (Further details of the transaction are set out in note 32 to the financial statements); and
- (5) the remaining balance was placed as fixed or term deposits or otherwise invested in short term investments.

Directors

The Directors during the Period were:

Executive Directors

Mr. Geng Xiaoping
Mr. Ying Shudeng
Mr. Fang Yunti
Mr. Xu Yikuang
Mr. Xuan Daoguang
Mr. Zhang Jingzhong
Ms. Zhang Chunming

Independent Non-executive Directors

Dr. Hu Hung Lick, Henry
Mr. Tung Chee Chen

All the Directors were appointed on 1 March 1997. In accordance with the Company's articles of association, all Directors continue to be in office.

Directors' and Supervisors' Service Contracts

Each of the Directors and supervisors of the Company ("Supervisors") has entered into a service agreement with the Company with effect from the date of the Company's establishment for an initial term of three years.

Save as disclosed above, none of the Directors and Supervisors 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 of Directors and Supervisors in contracts

None of the Directors and Supervisors and chief executive of the Company had a beneficial interest in any material contract to which the Company or any of its subsidiaries, its fellow subsidiaries or its holding company was a party, at the end of the Period or at any time during the Period.

Directors' and Supervisors' Interests in Shares

As at 31 December 1997, none of the Directors, Supervisors, chief executive of the Company or their associates had any personal, family, corporate or other interests in any equity or debt securities of the Company or any associated corporation, as defined in the SDI Ordinance as recorded in the register required to be kept under section 29 of the SDI Ordinance or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transaction by Directors of Listed Companies.

Directors' and Supervisors' Rights to Subscribe for Shares or Debentures

At no time during the Period was the Company or any of its subsidiaries, its fellow subsidiaries or its holding company a party to any arrangement to enable any Directors, Supervisors or chief executive of the Company to acquire benefits by means of the acquisition of shares in, or debentures of the Company or any other body corporate. No rights to subscribe for shares in, or debentures of, the Company have been granted by the Company to, nor have any such rights been exercised by, any person during the Period and up to the date of this report.

Directors' and Supervisors' Remuneration

	Rmb'000
Fees	—
Basic salaries, housing, other allowance and benefits in kind	971
Pension scheme contributions	—
Bonuses paid and payable	—
	971

None of the Directors and Supervisors received remuneration in excess of HK\$1 million.

The amount disclosed above included remuneration of HK\$80,000 paid to each of the independent non-executive Directors. There was no arrangement under which any of the Directors or Supervisors had waived or agreed to waive any remuneration.

Highest Paid Individuals

The five highest paid individuals of the Company were all Directors. The aggregate amount paid to them for the Period was approximately Rmb643,000. None of them received remuneration in excess of HK\$1 million.

Retirement Scheme

As stipulated by the State regulations of the PRC, the Company participates in a defined contribution retirement scheme. All employees are entitled to an annual pension equal to a fixed proportion of the average basic salary amount within the geographical area of their last employment at their retirement date. The Company is required to make contributions

Report of the Directors

Retirement Scheme *(continued)*

to registered insurance companies at a rate of 23% of the average basic salaries of the previous year within the geographical area where the employees are under employment with the Company. The Company has no obligation for the payment of pension benefits beyond such annual contributions to the registered insurance companies.

Pre-emptive Rights

There is no provision for pre-emptive rights in the Company's articles of association or the laws of the PRC which would oblige the Company to offer new shares on a pro rata basis to existing shareholders.

Accommodation Benefits for Employees

According to relevant rules and regulations in the PRC, the Group and its employees are required to contribute to an accommodation fund, being a certain percentage of the salaries and wages of the employees. There are no further obligations beyond the contribution to the accommodation fund.

Disposal of Staff Quarters

The Company does not own any staff quarters and has not disposed of any staff quarters during the Period.

Recent Economic Developments

The Directors are of the view that the recent economic developments in Asia do not have any adverse impact on the Company's operations.

Compliance with the Code of Best Practice

In the opinion of the Directors, the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules") since the listing of the H Shares on 15 May 1997, except for full board meetings (within the meaning of the Appendix 14 of Listing Rules) held during the Period due to personal commitments of the non-executive Directors.

Auditors

Ernst & Young will retire, and a resolution for their reappointment, as international auditors of the Company will be proposed at the forthcoming annual general meeting.

On behalf of the Board

Geng Xiaoping

Chairman and General Manager

Hangzhou, Zhejiang Province, the PRC
24 March 1998



Report of the Supervisory Committee

Dear Shareholders,

The Supervisory Committee, which comprises three supervisors, was established upon the incorporation of the Company in accordance with the PRC Company Law and the articles of association of the Company. The major tasks of the Supervisory Committee are to carry out the supervisory duties according to law and protect the lawful rights and interests of the shareholders and the Company. The scope of its task includes :

1. supervising the Directors, general manager and senior management staff. The Supervisory Committee supervises the acts of the Directors, general manager and other senior management staff in business operations and daily affairs mainly by attending board meetings and participating in major events of the Company; and
2. examining the operation and financial conditions of the Company.

The Supervisory Committee is of the opinion that the Directors, general manager and other senior management staff of the Company have implemented all the resolutions passed in general meetings in good faith, and they have been fully committed to their jobs and conduct the business according to applicable laws. The Supervisory Committee has not noticed any act of the Company and members of the board which violates any law, regulation and provisions of the articles of association.

The Company was not engaged in any major litigation and there were no disputes between any representative of the Supervisory Committee and any of the Directors and no litigation has been instituted against any of the Directors.

The Supervisory Committee has examined the financial reports for the year 1997 prepared by domestic and international accountants which the Directors intend to deliver to the shareholders. In our opinion, these reports have been prepared in compliance with the relevant laws, regulations and provisions of the articles of association and give a true and fair view of the operating results and asset position of the Company.

On behalf of the Supervisory Committee

Xia Linzhang

Chairman of the Supervisory Committee

Hangzhou, Zhejiang Province, the PRC

24 March 1998

Report of the International Auditors



To the shareholders

Zhejiang Expressway Co., Ltd.

(Established in the People's Republic of China with limited liability)

We have audited the financial statements on pages 33 to 57 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes an examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view, in all material respects, of the state of affairs of the Company and the Group as at 31 December 1997 and of the profit and cash flows of the Group for the period from 1 March 1997 (date of the Company's establishment) to 31 December 1997 and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Ernst & Young

Certified Public Accountants

Hong Kong

24 March 1998

Consolidation Profit and Loss Account

Period from 1 March 1997 (date of establishment) to 31 December 1997

	Notes	Rmb'000
TURNOVER	3	376,785
OPERATING PROFIT BEFORE EXCEPTIONAL ITEM	4	329,044
Exceptional item	5	25,355
OPERATING PROFIT BEFORE TAXATION		354,399
Taxation	6	(53,085)
PROFIT BEFORE MINORITY INTERESTS		301,314
Minority interests		(15,986)
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS	7	285,328
Transferred to reserves	26	(45,253)
Dividends	8	(69,490)
RETAINED PROFITS AT THE END OF THE PERIOD		170,585
EARNINGS PER SHARE	9	7.15 cents

The notes on pages 37 to 57 form an integral part of these financial statements.

Consolidated Balance Sheet
31 December 1997

	Notes	Rmb'000
FIXED ASSETS	10	5,571,783
CONSTRUCTION IN PROGRESS	11	1,643,231
DEFERRED COSTS		3,181
OPERATING RIGHTS	12	256,378
LONG TERM INVESTMENTS	13	11,149
		7,485,722
CURRENT ASSETS	15	3,980,655
CURRENT LIABILITIES	16	900,218
NET CURRENT ASSETS		3,080,437
TOTAL ASSETS LESS CURRENT LIABILITIES		10,566,159
LONG TERM BANK LOANS	20	125,000
OTHER LONG TERM LOANS	21	1,570,335
DEFERRED TAXATION	24	3,042
MINORITY INTERESTS		667,714
		8,200,068
SHARE CAPITAL	25	4,343,115
RESERVES	26	3,856,953
		8,200,068

Geng Xiaoping
Director

Ying Shudeng
Director

The notes on pages 37 to 57 form an integral part of these financial statements.

Consolidated Cash Flow Statement

Period from 1 March 1997 (date of establishment) to 31 December 1997

	Notes	Rmb'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	27(a)	423,159
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		
Interest received		144,761
Interest paid		(105,455)
Dividends paid to minority interests	27(b)	(6,145)
Net cash inflow from returns on investments and servicing of finance		33,161
TAXATION		
Taxes paid		(35,746)
INVESTING ACTIVITIES		
Purchases of fixed assets		(8,390)
Increase in time deposits		(2,049,865)
Additions to construction in progress		(624,348)
Prepayment for the Shangsang Agreement	19	(637,500)
Increase in long term investments		(4,849)
Acquisition of additional interest in a subsidiary	32	(29,362)
Net cash outflow from investing activities		(3,354,314)
NET CASH OUTFLOW BEFORE FINANCING ACTIVITIES		(2,933,740)
FINANCING ACTIVITIES	27(b)	
Issue of share capital		3,655,382
Share issue expenses		(154,893)
New long term loans		486,222
New short term loans		174,679
Repayment of loans		(621,015)
Minority interests		135,069
Net cash inflow from financing activities		3,675,444
INCREASE IN CASH AND CASH EQUIVALENTS		741,704
Cash and cash equivalents at beginning of the Period		105,042
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD		846,746
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS		
Cash and bank balances		840,746
Time deposits		6,000
		846,746

The notes on pages 37 to 57 form an integral part of these financial statements.

Balance Sheet
31 December 1997

	Notes	Rmb'000
FIXED ASSETS	10	5,075,424
CONSTRUCTION IN PROGRESS	11	10,633
OPERATING RIGHTS	12	203,378
INTERESTS IN SUBSIDIARIES	14	777,299
		6,066,734
CURRENT ASSETS	15	3,627,944
CURRENT LIABILITIES	16	530,220
NET CURRENT ASSETS		3,097,724
TOTAL ASSETS LESS CURRENT LIABILITIES		9,164,458
LONG TERM BANK LOANS	20	125,000
OTHER LONG TERM LOANS	21	842,635
DEFERRED TAXATION	24	3,042
		8,193,781
SHARE CAPITAL	25	4,343,115
RESERVES	26	3,850,666
		8,193,781

Geng Xiaoping
Director

Ying Shudeng
Director

The notes on pages 37 to 57 form an integral part of these financial statements.

1. COMPANY REORGANIZATION AND PRINCIPAL ACTIVITIES

Zhejiang Expressway Co., Ltd. (the "Company") was established as a joint stock limited company in the People's Republic of China (the "PRC") on 1 March 1997. The principal activities of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") are the investment in, the construction, operation and management of high grade roads. In addition, the Company has the rights to develop and operate certain ancillary services such as automobile servicing and fuel facilities.

Before the establishment of the Company and the corporate reorganization described below was effected, Zhejiang Provincial High Class Highway Investment Company Limited ("Provincial Investment Co"), owned the assets and liabilities of the Company's investments in the Hangzhou-Ningbo Expressway, the Hangzhou Section of the Shanghai-Hangzhou Expressway, a 51% equity interest in Zhejiang Yuhang Expressway Company Limited ("Yuhang Co"), which owned the Yuhang Section of the Shanghai-Hangzhou Expressway, and a 51% equity interest in Zhejiang Jiaxing Expressway Company Limited ("Jiaxing Co"), which owned the Jiaxing Section of the Shanghai-Hangzhou Expressway (hereinafter collectively referred to as the "Relevant Investments of the Old Group").

Provincial Investment Co and its subsidiaries are hereinafter collectively referred to as the "Old Group".

As of the Company's date of establishment, the Company issued 2,909,260,000 fully paid domestic shares of Rmb1 each to Provincial Investment Co as consideration for the acquisition of the exclusive operating rights relating to the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway, together with the following assets and liabilities (hereinafter collectively referred to as the "Selected Assets and Liabilities"):

- (1) certain assets and liabilities of Provincial Investment Co, which included all the fixed assets and other long term assets, together with the current assets and liabilities relating to the daily operation of the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway and all bank loans and other loans as at 30 November 1996;
- (2) a 51% interest in Yuhang Co; and
- (3) a 51% interest in Jiaxing Co.

The Selected Assets and Liabilities together with the operating rights were revalued to Rmb4,475,785,000 by Zhejiang Assets Evaluation Company and Zhejiang Provincial Land Evaluation & Advisory Centre on 30 November 1996 in accordance with the guidelines set out by the PRC Ministry of Finance.

The Company was listed on The Stock Exchange of Hong Kong Limited on 15 May 1997, by placing a public offer of 1,433,854,500 overseas listed foreign shares ("H Shares") and of which, 187,024,500 H Shares were issued as a result of the oversubscription of the initial offering.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting

The financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice ("HKSSAP"), accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. The pro forma consolidated profit and loss account, which is presented for information purposes only, shows the results of the Group for the two years ended 31 December 1997 as if the Group structure has been in existence since 1 January 1996.

Basis of consolidation

The consolidated financial statements include the audited financial statements of the Company and its subsidiaries for the ten months ended 31 December 1997 (the "Period"). The results of subsidiaries acquired or disposed of during the Period are consolidated from their effective dates of acquisition or disposal. All significant inter-company transactions and balances are eliminated on consolidation.

Goodwill

Goodwill arising on consolidation of subsidiaries and on acquisition of associated companies represents the excess purchase consideration paid for subsidiaries/associates over the fair values ascribed to the net underlying assets acquired and is eliminated against reserves in the year of acquisition.

Subsidiaries

Interests in subsidiaries are stated at cost unless, in the opinion of the directors, there have been permanent diminutions in value, when they are written down to values determined by the directors.

Related parties

A related party is a company or a government body in which one or more of the beneficial shareholders of the Company or its subsidiaries have a beneficial interest therein or are in a position to exercise significant influence.

Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation. The cost of an asset comprises its purchase price, cost transferred from construction in progress and any directly attributable cost of bringing the asset to its present working condition and location for its intended use. Expenditures incurred after the tangible fixed assets have been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to the profit and loss account in the period in which they are incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in future economic benefits expected to be obtained from the use of the tangible fixed assets, the expenditure is capitalized as an additional cost of the tangible fixed assets.

Depreciation of expressways and bridges is provided by using the sinking fund method whereby the aggregate annual depreciation amounts, compounded at an average rate of 7% per annum, up to the expiry of the underlying 30 year expressway concession period will equal the total cost of the expressways and bridges.

Amortization of land is provided for on a straight-line basis to write off the valuation of the land use rights over the underlying 30 year expressway concession period.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fixed assets and depreciation (continued)

Depreciation of fixed assets other than expressways, bridges and land is provided for on a straight-line basis to write off the cost of the assets, less their estimated residual values, being 3% of the cost, over their estimated useful lives. The principal annual rates used for this purpose are as follows:

	Estimated useful life	Annual depreciation rate
Toll stations and ancillary facilities	30 years	3.2%
Communication and signalling equipment	10 years	9.7%
Motor vehicles	8 years	12%
Machinery and equipment	5-8 years	12-19.4%

Construction in progress

Construction in progress represents costs incurred in the construction of expressways and bridges. Cost comprises direct costs of construction as well as interest charges and certain exchange differences related to funds borrowed during the periods of construction, installation and testing. No provision for depreciation is made on construction in progress until such time as the relevant assets are completed and put into use.

Operating rights

Operating rights represent the rights to operate the expressways and are stated at valuation less accumulated amortization.

Amortization is provided on a straight-line basis over the periods of operating rights granted to the Company and its subsidiaries.

Revenue

Revenue is recognized when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

- toll revenue, net of any applicable revenue taxes, when received; and
- interest, on a time proportion basis.

Taxation

PRC income tax is provided at rates applicable to enterprises in the PRC on income for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes, based on existing PRC income tax legislation, practice and interpretations thereof.

Deferred taxation is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallize in the foreseeable future. A deferred tax asset is not recognized until its realization is assured beyond reasonable doubt.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Foreign currency transactions

The financial records of the Company and its subsidiaries are maintained and the financial statements are stated in Renminbi ("Rmb").

Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable rates of exchange ruling at that date. Exchange differences are dealt with in the profit and loss account unless such exchange differences relate to funds borrowed specifically for the financing of construction of expressways and bridges in which case they are capitalized to the extent that they can be regarded as an adjustment to interest costs.

Capitalization of borrowing costs

Borrowing costs that are directly attributable to the construction of expressways, tunnels and bridges are capitalized as part of the cost of such assets when it is probable that they will result in future economic benefits to the Group and the costs can be measured reliably. Other borrowing costs are recognized as an expense in the period in which they are incurred.

The amount of borrowing costs capitalized is determined by reference to the actual borrowing costs incurred on funds borrowed specifically for the construction of expressways, tunnels and bridges during the period less any investment income arising from the temporary investment of those borrowings.

Capitalization of borrowing costs on funds borrowed specifically for the construction of completed expressway sections ceases when the construction of such expressway sections is completed and the section completed is capable of commencing toll operations.

Leased assets

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Rentals applicable to such operating leases are charged to the profit and loss account on a straight-line basis over the lease terms.

Investments

Investments held on a long term basis are stated at cost less provisions for any permanent diminutions in values on an individual investment basis.

Short term investments are stated at the lower of cost and market value.

Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined on the weighted average basis. Net realizable value is based on estimated selling prices less any further costs expected to be incurred to completion and disposal.

Deferred costs

Deferred costs include deferred pre-operating expenses and are amortized over 5 years starting from the date of commencement of operations. They are stated at cost less accumulated amortization.

3. TURNOVER

Turnover represents toll income from operation of expressways, net of relevant revenue taxes.

	Rmb'000
Toll income	398,468
Less: Revenue taxes	(21,683)
	376,785

The Company and its subsidiaries are subject to the following types of revenue taxes:

- Business tax ("BT"), levied at 5% of toll income;
- City Development Tax, levied at 1% - 7% of BT; and
- Education Supplementary Tax, levied at 3.5% - 4% of BT.

4. OPERATING PROFIT BEFORE EXCEPTIONAL ITEM

The Group's operating profit before exceptional item is arrived at after charging/(crediting):

	Rmb'000
Depreciation charges	58,549
Operating lease rentals	
— land and buildings	1,746
Interest expense on:	
— bank loans	29,325
— other loans	130,184
Less: Amount capitalized in construction in progress and fixed assets	(69,237)
	90,272
Interest income	(119,406)
Less: Amount capitalized in construction in progress and fixed assets	13,623
	(105,783)
Interest expense/(income), net	(15,511)
Amortization of deferred costs	745
Amortization of operating rights	4,622
Profit on disposal of short term investments	(52,347)
Directors' remuneration:	
Fees	—
Other emoluments	951
Auditors' remuneration	1,006
Pension cost	988
Exchange differences incurred, net	(2,620)
Less: Amount capitalized in construction in progress and fixed assets	3,021
Exchange differences, net	401

5. EXCEPTIONAL ITEM

The exceptional item represents interest earned on the oversubscription monies of the Company's H Shares.

6. TAXATION

No Hong Kong profits tax has been provided as the Group had no taxable profit in Hong Kong during the Period.

The Group was subject to Enterprise Income Tax ("EIT") levied at a rate of 33% of taxable income based on income for financial reporting purposes prepared in accordance with the laws and regulations in the PRC.

Pursuant to directives numbered 1997 (27) dated 20 February 1997 and 1997(53) dated 11 August 1997 issued by the Zhejiang Provincial People's Government, the Company is entitled to a refund from the Zhejiang Finance Bureau of an amount equal to 18% of the Company's taxable income in respect of EIT paid to the Zhejiang Taxation Bureau with effect from 1 March 1997, being the date of establishment of the Company. Such a tax refund is also applicable to Yuhang Co and Jiaying Co, with effect from 15 May 1997, being the date of listing of the Company's shares on The Stock Exchange of Hong Kong Limited, pursuant to directives numbered 1997 (68) dated 2 April 1997 and 1997(67) dated 2 April 1997, issued by the Yuhang Municipal Government and the Jiaying Municipal Government, respectively. However, there is no assurance that the Company, Yuhang Co and Jiaying Co will continue to enjoy such preferential tax treatment in the future.

	Group Rmb'000
Taxation charged	110,095
Taxation refundable	(60,052)
PRC taxation	50,043
Deferred (note 24)	3,042
	53,085

7. NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS

Net profit attributable to shareholders dealt with in the financial statements of the Company is Rmb275,074,000.

8. DIVIDENDS

	Company Rmb'000
Proposed final dividend Rmb0.016 (approximately HK\$0.015) per share	69,490

9. EARNINGS PER SHARE

The calculation of earnings per share is based on the net profit attributable to shareholders for the Period of Rmb285,328,000 and the weighted average of 3,986,994,000 shares in issue during the Period.

10. FIXED ASSETS

Group

	Land	Expressways and bridges	Toll stations and ancillary facilities	Communi- cation and signalling equipment	Motor vehicles	Machinery and equipment	Total
	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000
Cost:							
At 1 March 1997	527,628	4,908,585	69,949	2,109	12,377	60,595	5,581,243
Additions	—	40,700	415	195	4,642	3,137	49,089
At 31 December 1997	527,628	4,949,285	70,364	2,304	17,019	63,732	5,630,332
Accumulated depreciation:							
At 1 March 1997	—	—	—	—	—	—	—
Provided during the Period	6,326	43,406	1,833	181	1,500	5,303	58,549
At 31 December 1997	6,326	43,406	1,833	181	1,500	5,303	58,549
Net book value:							
At 31 December 1997	521,302	4,905,879	68,531	2,123	15,519	58,429	5,571,783

Company

	Land	Expressways and bridges	Toll stations and ancillary facilities	Communi- cation and signalling equipment	Motor vehicles	Machinery and equipment	Total
	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000	Rmb'000
Cost:							
At 1 March 1997	350,384	4,592,253	65,269	2,109	11,919	60,440	5,082,374
Additions	—	40,700	287	195	4,642	2,847	48,671
At 31 December 1997	350,384	4,632,953	65,556	2,304	16,561	63,287	5,131,045
Accumulated depreciation:							
At 1 March 1997	—	—	—	—	—	—	—
Provided during the Period	6,326	40,660	1,759	181	1,500	5,195	55,621
At 31 December 1997	6,326	40,660	1,759	181	1,500	5,195	55,621
Net book value:							
At 31 December 1997	344,058	4,592,293	63,797	2,123	15,061	58,092	5,075,424

All fixed assets are situated in the PRC.

Notes to Financial Statements

31 December 1997

11. CONSTRUCTION IN PROGRESS

Movements of construction in progress during the Period are as set out below:

	Group Rmb'000	Company Rmb'000
At 1 March 1997	1,079,270	—
Additions, net	563,961	10,633
At 31 December 1997	1,643,231	10,633

12. OPERATING RIGHTS

	Group Rmb'000	Company Rmb'000
Cost:		
At 1 March and 31 December 1997	261,000	208,000
Amortization:		
At 1 March 1997	—	—
Provided during the Period	4,622	4,622
At 31 December 1997	4,622	4,622
Net book value:		
At 31 December 1997	256,378	203,378

13. LONG TERM INVESTMENTS

	Group Rmb'000	Company Rmb'000
Unlisted investments, at cost	11,149	—
Provision for diminution in value	—	—
	11,149	—

14. INTERESTS IN SUBSIDIARIES

	Company Rmb'000
Unlisted shares, at cost	758,943
Due from subsidiaries	18,356
	777,299

14. INTERESTS IN SUBSIDIARIES *(continued)*

Particulars of the Company's subsidiaries, all of which are directly held, are as follows:

Name of subsidiaries	Date and place of registration	Issued & fully paid registered capital	Percentage of equity attributable to the Company	Principal activities
Zhejiang Yuhang Expressway Company Limited ("Yuhang Co")	Note 1	75,222,997	51%	Construction and management of the Yuhang Section of the Shanghai-Hangzhou Expressway
Zhejiang Jiaxing Expressway Company Limited ("Jiaxing Co")	Note 2	1,159,200,000	53.44%	Construction and management of the Jiaxing Section of the Shanghai-Hangzhou Expressway
Zhejiang Gaotong Stone Developing Company Limited ("Gaotong")	Note 3	5,000,000	80%	Processing, designing and selling of stone and quarry materials

Note 1. Yuhang Co was established on 7 June 1994 in the PRC as a joint stock limited company and was subsequently restructured into a limited liability company under its current name on 28 November 1996.

Note 2. Jiaxing Co was established on 30 June 1994 in the PRC as a joint stock limited company and was subsequently restructured into a limited liability company under its current name on 29 November 1996.

Note 3. Gaotong was established on 3 November 1997 in the PRC as a limited liability company.

15. CURRENT ASSETS

	Notes	Group Rmb'000	Company Rmb'000
Cash and bank balances		840,746	813,367
Time deposits		2,055,865	2,042,865
Short term investments	17	21,991	21,991
Accounts receivable	18	9,629	9,629
Profits tax refundable		17,172	9,496
Inventories		400	262
Prepayments, deposits and other receivables	19	1,025,733	730,334
Due from related parties	22	9,119	—
		3,980,655	3,627,944

16. CURRENT LIABILITIES

	Notes	Group Rmb'000	Company Rmb'000
Bank loans	20	284,679	279,679
Other loans	21	244,022	84,702
Accounts payable		31,030	1,657
Other payables and accrued liabilities		166,068	50,719
Due to related parties	22	25,338	3,722
Due to holding company	23	19,779	13,287
Profits tax payable		42,447	17,409
Other taxes payable		17,365	9,555
Proposed final dividends	8	69,490	69,490
		900,218	530,220

17. SHORT TERM INVESTMENTS

	Group Rmb'000	Company Rmb'000
Investments in government debentures, at cost	21,991	21,991
Provision for diminution in value	—	—
	21,991	21,991
Market value of investments	21,991	21,991

18. ACCOUNTS RECEIVABLE

	Group	Company
	Rmb'000	Rmb'000
Accounts receivable	9,629	9,629
Provision for doubtful debts	—	—
Accounts receivable, net	9,629	9,629

19. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Note	Group	Company
		Rmb'000	Rmb'000
Prepayments for the Shangsan Agreement (Note 29)		637,500	637,500
Prepayment to contractors in relation to construction of expressways		370,888	79,662
Others		17,345	13,172
		1,025,733	730,334

20. BANK LOANS

	Note	Group	Company
		Rmb'000	Rmb'000
Balances due:			
Within one year		284,679	279,679
In the second year		105,000	105,000
In the third to fifth years, inclusive		20,000	20,000
		409,679	404,679
Portion classified as current liabilities	16	(284,679)	(279,679)
Portion classified as long term liabilities		125,000	125,000

Included in the total bank loans of Rmb409,679,000, Rmb120,000,000 is secured by time deposits of Rmb111,000,000, US\$6,000,000 is secured by time deposits of HK\$46,497,000 and Rmb5,000,000 is guaranteed by related parties. The remaining balance is unsecured.

The bank loans bear interest at rates ranging from 6.6% to 13.14% per annum.

21. OTHER LOANS

	Note	Group Rmb'000	Company Rmb'000
Balances due:			
Within one year		244,022	84,702
In the second year		158,234	62,098
In the third to fifth years, inclusive		307,562	139,266
Thereafter		1,104,539	641,271
		1,814,357	927,337
Portion classified as current liabilities	16	(244,022)	(84,702)
Portion classified as long term liabilities		1,570,335	842,635

Other loans are unsecured and bear interest at rates ranging from 3% to 14.5% per annum.

22. BALANCES WITH RELATED PARTIES

The amounts due from related parties are unsecured, bear interest at 7.2% per annum and are repayable within 1 year.

The amounts due to related parties are unsecured, interest-free and have no fixed terms of repayment.

23. DUE TO HOLDING COMPANY

The amount due to holding company is unsecured, interest-free and has no fixed term of repayment.

24. DEFERRED TAXATION

	Group Rmb'000	Company Rmb'000
At 1 March 1997	—	—
Charge for the Period (note 6)	3,042	3,042
At 31 December 1997	3,042	3,042

The deferred taxation of the Company and the Group is made in respect of the difference in income recognition for accounting and taxation purposes of interest income arising from the oversubscription monies of the H Shares proceeds.

25. SHARE CAPITAL

	Number of shares	Rmb'000
Registered, issued and fully paid:		
Domestic shares of Rmb1.00 each	2,909,260,000	2,909,260
H Shares of Rmb1.00 each	1,433,854,500	1,433,855
	4,343,114,500	4,343,115

The domestic shares are not currently listed on any stock exchange.

The H Shares have been listed on The Stock Exchange of Hong Kong Limited since 15 May 1997.

All the domestic shares and H Shares rank pari passu with each other as to dividends and voting rights.

During the Period, the following changes in the Company's share capital took place:

- (a) On the date of establishment, 1 March 1997, the registered share capital of the Company was Rmb2,909,260,000 consisting of 2,909,260,000 domestic shares of Rmb1.00 each, all of which were issued and credited as fully paid in consideration for the acquisition of the Selected Assets and Liabilities together with the operating rights relating to the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway transferred from Provincial Investment Co at valuation of Rmb4,475,785,000.
- (b) On 15 May 1997, 1,433,854,500 H Shares of Rmb1.00 each were issued to public investors outside the PRC at HK\$2.38 each, for a total cash consideration of approximately Rmb3,524,000,000 (approximately HK\$3,293,458,000), net of share issue expenses.

26. RESERVES

	Share premium account Rmb'000	Capital/ (Goodwill) reserve Rmb'000	Statutory surplus reserve Rmb'000	Public welfare fund Rmb'000	Retained profits Rmb'000	Total Rmb'000
Group						
At 1 March 1997	1,578,448	2,850	—	—	—	1,581,298
Arising on issue of H Shares	2,221,527	—	—	—	—	2,221,527
Share issue expenses	(154,893)	—	—	—	—	(154,893)
Goodwill arising on acquisition of further interests in a subsidiary	—	(6,817)	—	—	—	(6,817)
Net profit for the Period	—	—	—	—	285,328	285,328
Transfer from/(to) reserves	—	—	30,169	15,084	(45,253)	—
Dividends (note 8)	—	—	—	—	(69,490)	(69,490)
At 31 December 1997	3,645,082	(3,967)	30,169	15,084	170,585	3,856,953
Company						
At 1 March 1997	1,578,448	—	—	—	—	1,578,448
Arising on issue of H Shares	2,221,527	—	—	—	—	2,221,527
Share issue expenses	(154,893)	—	—	—	—	(154,893)
Net profit for the Period	—	—	—	—	275,074	275,074
Transfer from/(to) reserves	—	—	26,722	13,361	(40,083)	—
Dividends (note 8)	—	—	—	—	(69,490)	(69,490)
At 31 December 1997	3,645,082	—	26,722	13,361	165,501	3,850,666

In accordance with the Company Law of the PRC and the Company's articles of association, the Company is required to allocate 10% of its profit after taxation, as determined in accordance with the PRC accounting standards and regulations applicable to the Company, to the statutory surplus reserve (the "SSR") until such reserve reached 50% of the registered capital of the Company. Subject to certain restrictions set out in the Company Law of the PRC and the Company's articles of association, part of the SSR may be converted to increase share capital.

In accordance with the Company Law of the PRC, the Company is required to transfer 5% to 10% of its profit after taxation to its statutory public welfare fund (the "PWF") which is a non-distributable reserve other than in the event of the liquidation of the Company. PWF must be used for capital expenditure on staff welfare facilities and these facilities remain as property of the Company.

The directors of the Company have proposed to transfer Rmb26,722,000 and Rmb13,361,000 to the SSR and the PWF, respectively. This represents 15% of the Company's profit after taxation of Rmb267,218,000 determined in accordance with PRC accounting standards. The transfer to the PWF is subject to shareholders' approval at the forthcoming annual general meeting.

26. RESERVES *(continued)*

According to the relevant regulations in the PRC, the amount of profit available for distribution is the lower of the amount determined under the PRC accounting standards and the amount determined under HKSSAP.

As at 31 December 1997, the Company had reserves of approximately Rmb157,645,000 available for distribution by way of cash or in kind.

As at 31 December 1997, in accordance with the Company Law of the PRC, the amount of approximately Rmb3,645,082,000 standing to the credit of the Company's share premium account was available for distribution by way of capitalization issues.

27. NOTES TO THE CASH FLOW STATEMENT

(a) Reconciliation of operating profit to net cash inflow from operating activities:

	Rmb'000
Operating profit before taxation and minority interests	354,399
Depreciation charges	58,549
Decrease in deferred costs	5,963
Amortization of operating rights	4,622
Interest income	(131,138)
Interest expense	90,272
Decrease in prepayments, deposits and other receivables	66,655
Increase in due to holding company	9,840
Increase in due to related parties, net	18,422
Increase in other taxes payable	13,862
Decrease in other payables and accrued liabilities	(36,267)
Increase in inventories	(400)
Increase in accounts receivable	(9,629)
Increase in short term investments	(21,991)
Net cash inflow from operating activities	423,159

27. NOTES TO THE CASH FLOW STATEMENT *(continued)*

(b) Analysis of changes in financing during the Period:

	Share capital (including premium) Rmb'000	Loans Rmb'000	Minority interests Rmb'000
At 1 March 1997	4,487,708	2,184,150	545,349
Cash inflows from financing	3,500,489	39,886	135,069
Arising from dilution of minority interests	—	—	(22,545)
Dividends paid to minority interests	—	—	(6,145)
Profit attributable to minority shareholders	—	—	15,986
At 31 December 1997	7,988,197	2,224,036	667,714

27. NOTES TO THE CASH FLOW STATEMENT *(continued)*

(c) Major non-cash transaction

As more fully described in note 1 above, the Company received the Selected Assets and Liabilities together with the exclusive operating rights of the Hangzhou-Ningbo Expressway and the Hangzhou Section of the Shanghai-Hangzhou Expressway thereof from Provincial Investment Co by issuing 2,909,260,000 fully paid domestic shares of Rmb 1.00 each. Details of the Selected Assets and Liabilities as at 1 March 1997 are set out below:

	Rmb'000
Net assets acquired:	
Fixed assets	5,581,243
Construction in progress	1,079,270
Long term investments	6,300
Deferred costs	9,145
Operating rights	261,000
Cash and bank balances	105,042
Prepayments, deposits and other receivables	425,713
Due from related parties	2,203
Bank loans	(607,224)
Other loans	(1,576,926)
Accounts payable	(71,720)
Other payables and accrued liabilities	(153,718)
Other tax payables	(3,503)
Income tax payable	(10,978)
Due to holding company	(9,940)
Minority interests	(545,349)
	4,490,558
Capital reserve on consolidation	(2,850)
Satisfied by:	
2,909,260,000 domestic shares issued	4,487,708

The net inflow of cash and cash equivalents in respect of the take over of assets and liabilities from Provincial Investment Co was approximately Rmb 105,042,000.

(d) The exceptional item had the following attributable cash inflows to the operating activities:

	Rmb'000
Interest earned on the oversubscription monies of the H Shares offering	25,355

28. COMMITMENTS

	Group Rmb'000	Company Rmb'000
Contracted, but not provided for		
— Construction of expressways	586,741	142,378
— Proposed investments in the Jiaxing section of the Shanghai- Hangzhou Expressway and the Shangyu-Sanmen Road	586,500	960,165
Authorized, but not contracted for		
— Construction of expressways	726,554	—
— Proposed investment in the Hangzhou-Nanjing Expressway	900,000	900,000
	2,799,795	2,002,543

29. POST BALANCE SHEET EVENTS

As of 18 December 1997, an agreement in respect of the proposed investment in the Shangyu-Sanmen Road (the "Shangsan Agreement") was entered into between Provincial Investment Co, Shangyu Municipal Transport Bureau, Shengzhou Municipal Transport Bureau, Xinchang County Transport Development Company, Tiantai County Transport Development Company and Huajian Transportation Economic Development Center, a subsidiaries of the Ministry of Communications of the PRC, (hereinafter collectively referred to as the "Other Parties") and the Company to set up a limited liability company, Zhejiang Shangyu-Sanmen Class 1 Highway Company Limited (the "Shangsan Co"). Shangsan Co was established on 1 January 1998. According to the Shangsan Agreement, the Company will contribute Rmb1,224 million in cash for a 51% interest in the Shangsan Co. Other Parties will contribute a total of Rmb1,176 million for an aggregate of 49% interest in the Shangsan Co.

Pursuant to the Shangsan Agreement and a supplemental agreement, Shangsan Co will be principally engaged in the development, operation, management and toll-collection of the Shangyu-Sanmen Road and the development of other related businesses.

The Shangyu-Sanmen Road is a Class 1 Road which, upon completion, will run from Guzhu Interchange on the Hangzhou-Ningbo Expressway to Wuao Interchange on the Ningbo-Taizhou-Wenzhou Expressway. The total length of the Shangyu-Sanmen Road will be approximately 143km. The construction of the project is divided into two phases. Phase 1, consisting of four short sections Shangyu, Shengzhou, Xinchang and Tiantai, has a total length of 37.5km and has been operational since February 1997. The construction of the second phase commenced in February 1998 and will be completed in four years. Upon completion the Shangyu-Sanmen Road will connect with the Hangzhou-Ningbo Expressway and the Ningbo-Taizhou-Wenzhou Expressway.

Pursuant to the Shangsan Agreement and a supplemental agreement, the total investment of the Shangyu-Sanmen Road is budgeted at approximately Rmb4,290 million.

30. DIFFERENCE IN FINANCIAL STATEMENTS PREPARED UNDER PRC AND HONG KONG ACCOUNTING STANDARDS

Other than the difference in recognizing the interest income arising from oversubscription monies received on listing of the Company's H Shares as described below, there are no material differences between the Company's consolidated financial statements for the Period ended 31 December 1997 prepared in accordance with PRC and Hong Kong accounting standards.

Under the PRC accounting standards, the interest income arising from H Shares oversubscription monies is treated as deferred income and is amortised on a straight-line basis over 5 years. Under Hong Kong accounting standards, the entire interest income net of related taxation is accounted for in the current period profit and loss account.

31. ULTIMATE HOLDING COMPANY

In the opinion of the directors, the ultimate holding company of the Company is Zhejiang Provincial High Class Highway Investment Company Limited, a state-owned enterprise established in the PRC.

32. CONNECTED TRANSACTIONS

The following is a summary of significant transactions carried out in the ordinary course of business between the Company, its subsidiaries and certain government bodies in the Period:

Under the reorganization agreement, the Provincial Investment Co gave a number of undertakings to the Company including a non-competition undertaking, a tax indemnity, an indemnity against losses incurred which were not expressly transferred to the Company pursuant to the reorganisation and general indemnity provisions against any breach of representation warranty and undertakings contained in the agreement.

The World Bank provided financing for the construction of the Shanghai-Hangzhou Expressway and the Hangzhou-Ningbo Expressway through the Ministry of Finance and the Zhejiang Provincial Expressway Executive Commission (the "Executive Commission") which was responsible for the control of the construction and the management of the Hangzhou-Ningbo Expressway and the Zhejiang Section of the Shanghai-Hangzhou Expressway. The repayment responsibility for the financing provided for the Hangzhou-Ningbo Expressway which amounted to US\$112,000,000 as at 31 December 1997 was assumed by the Company. The loan repayment responsibility for the Shanghai-Hangzhou Expressway which amounted to US\$58,313,158 as at 31 December 1997 was assumed by Yuhang Co and Jiaxing Co.

Pursuant to a supplemental agreement dated 18 April 1997, the Company, Provincial Investment Co, Jiaxing Co, Yuhang Co, the Executive Commission, the Yuhang Executive Commission and the Jiaxing Executive Commission have agreed that the Company will take over the repayment responsibilities under the reorganization agreement and in respect of the World Bank financing as separately agreed. Jiaxing Co and Yuhang Co shall take over the repayment obligations with regard to World Bank financing for their respective sections. Appropriate agreements were entered into between the Company and its subsidiaries and the executive commissions, pursuant to which the Company and its subsidiaries will be charged the same rate of interest as that charged to the executive commissions.

32. CONNECTED TRANSACTIONS *(continued)*

The Zhejiang Provincial Government provided a number of loans for the construction of the Shanghai-Hangzhou Expressway. These loans were made available through the Yuhang Executive Commission and the Jiaxing Executive Commission to Yuhang Co and Jiaxing Co, respectively in the amount of Rmb169 million and Rmb718 million. As at 31 December 1997, each of Yuhang Co and Jiaxing Co has agreed to repay the loans. All of these loans are unsecured. The terms of the loans to the executive commissions are the same as those from the respective executive commissions to the companies.

A management agreement in relation to the Yuhang Section of the Shanghai-Hangzhou-Ningbo Expressway was entered into between the Company and Yuhang Co. The purpose of this agreement is to enable the Company to ensure that the Yuhang Section, together with all other sections of the Shanghai-Hangzhou-Ningbo Expressway, are operated and managed in a uniform manner, and to allocate the revenue, expenses and maintenance obligations of the Yuhang Section on an agreed basis between the Company and Yuhang Co.

The Company purchased an additional 2.44% of the issued capital of Jiaxing Co for a cash consideration of Rmb29.4 million from Provincial Investment Co.

A contract between the Company and the Executive Commission was reached whereby the Executive Commission will enter into a number of contracts relating to Contract No. 8 on behalf of the Company for the purpose of upgrading the Operating Systems (as defined in the section "Operation of the Expressway" of the prospectus) of the Shanghai-Hangzhou-Ningbo Expressway. The Company will take the benefit of these contracts when entered into and will assume the repayment obligations for any drawdowns on World Bank funding in respect of Contract No. 8.

33. PRO FORMA CONSOLIDATED PROFIT AND LOSS ACCOUNT

The following pro forma consolidated profit and loss account, which is presented for information purposes only, has been prepared on the basis as if the current Group structure had been in existence since 1 January 1996.

	Two months ended 28 February 1997	Ten months ended 31 December	Year ended 31 December	
	pro forma Rmb'000	1997 Rmb'000	pro forma 1997 Rmb'000	pro forma 1996 Rmb'000
Turnover	63,004	376,785	439,789	273,843
Operating profit before exceptional item	17,827	329,044	346,871	159,964
Exceptional item	—	25,355	25,355	—
Operating profit before taxation	17,827	354,399	372,226	159,964
Taxation	(5,554)	(53,085)	(58,639)	(60,296)
Profit before minority interests	12,273	301,314	313,587	99,668
Minority interests	(1,269)	(15,986)	(17,255)	186
Net profit attributable to shareholders	11,004	285,328	296,332	99,854
Earnings per share			7.77 cents	3.43 cents

The pro forma earnings per share of 1997 is based on the pro forma net profit attributable to shareholders for the year ended 31 December 1997 of Rmb296,332,000 and 3,812,785,000 shares, being the weighted average of 2,909,260,000 domestic shares, as if they were issued on 1 January 1997, and the 1,433,854,500 H Shares issued on 15 May 1997.

The pro forma earnings per share of 1996 is based on the pro forma net profit attributable to shareholders for the year ended 31 December 1996 of Rmb99,854,000 and 2,909,260,000 domestic shares as if they were issued on 1 January 1996.

34. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved by the board of directors on 24 March 1998.

Corporate Information

Executive Directors

Geng Xiaoping
Ying Shudeng
Xu Yikuang
Fang Yunti
Zhang Jingzhong
Zhang Chunming
Xuan Daoguang

Independent Non-executive Directors

Hu Hung Lick, Henry
Tung Chee Chen

Supervisors

Xia Linzhang
Ge Ailian
Jiang Wen Yao

Legal Advisers

As to Hong Kong law:
Herbert Smith
23rd Floor, Gloucester Tower
11 Pedder Street, Central
Hong Kong

As to PRC Law:
T & C Law Firm
18/F, Block A
100 Moqianshan Road,
Yaojian International Building,
Hangzhou, Zhejiang
PRC

Auditors and Reporting Accountants

Ernst & Young
Certified Public Accountants
15th Floor
Hutchison House
10 Harcourt Road, Central
Hong Kong

Sponsor

Kleinwort Benson Limited
33rd Floor, Jardine House
1 Connaught Place
Central
Hong Kong

Company Secretary

Mr. Zhang Jingzhong

Authorised Representatives

Mr. Geng Xiaoping
Mr. Zhang Jingzhong

Statutory Address

78 Beishan Road
Hangzhou, Zhejiang
PRC
Tel: 86-571-7964605
Fax: 86-571-7963205
E-mail: zjewltd@public.hz.zj.cn

Place of Business in Hong Kong

c/o Ernst & Young
11th Floor, Tower 2
The Gateway
25-27 Canton Road
Kowloon
Hong Kong

H Share Registrar and Transfer Office

HKSCC Registrars Limited
2nd Floor, Vicwood Plaza
199 Des Voeux Road, Central
Hong Kong

Principal Bankers

Bank of China, Hong Kong Branch
China Investment Bank, Zhejiang Branch
Industrial & Commercial Bank of China,
Zhejiang Branch
Construction Bank of China, Zhejiang
Branch

Listing Information

H Shares
The Stock Exchange of Hong Kong
Limited
Code: 0576



浙江滬杭甬高速公路股份有限公司
ZHEJIANG EXPRESSWAY CO., LTD.

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

Notice of Annual General Meeting

NOTICE IS HEREBY GIVEN that the 1997 Annual General Meeting of Zhejiang Expressway Co., Ltd. (the "Company") will be held at 10:00 a.m. on Monday, 25 May 1998 at 78 Beishan Road, Hangzhou 310007, the PRC for the conduct of the following business:

A. As ordinary resolutions:—

1. To consider and approve the report of the Directors for the year 1997;
2. To consider and approve the report of the Supervisory Committee for the year 1997;
3. To consider and approve the audited financial statements for the year 1997;
4. To consider and approve the budget plan for the year 1998;
5. To consider and approve the proposed distribution of profits for the year 1997;
6. To consider and approve the re-appointment of Ernst & Young (Hong Kong Certified Public Accountants) and Zhejiang Certified Public Accountants as the international auditors and the PRC auditors of the Company respectively and to authorise the Board of Directors to fix their remunerations;

B. As special resolutions:—

1. To approve the Company's allotting, issuing or otherwise dealing with, either separately or concurrently not more than 20% of each of the existing issued domestic invested shares and overseas listed foreign invested shares during the Relevant Period (as defined below) and to authorise the Board of Directors to deal with all necessary matters relating to such allotment and issue.

For the purpose of this resolution, "Relevant Period" means the period from the date upon which this resolution is passed until whichever is the earliest of:—

- (a) the last day of the twelve-month period from the date this resolution is passed; and
- (b) the revocation or variation of the authority given under this resolution by a special resolution of the shareholders of the Company in general meeting.

2. Subject to the passing of the resolution set out in paragraph 1 of this part B, to consider and approve the following amendments to the Articles of Association of the Company and to authorise the Board of Directors to file the amended Articles of Association with the relevant approval authority of the PRC:—

Article 18 be replaced in its entirety as follows:—

“ Article 18 As approved by the examination and approval authority authorised by the State Council, the Company has issued a total of 4,343,114,500 ordinary shares. Upon the establishment of the Company, 2,909,260,000 domestic invested shares were issued to the promoter, Zhejiang Provincial High Class Highway Investment Company Limited (浙江省高等級公路投資有限公司), representing approximately 67% of the total ordinary shares issued by the Company.”

Article 19 be replaced in its entirety as follows:—

“Article 19 After the establishment of the Company, 4,343,114,500 ordinary shares were issued of which 1,433,854,500 were issued as overseas listed foreign invested shares representing approximately 33% of the total number of ordinary shares issued by the Company. The shareholding structure of the Company comprises 4,343,114,500 ordinary shares of which 2,909,260,000 domestic invested shares are held by the promoter, Zhejiang Provincial High Class Highway Investment Company Limited (浙江省高等級公路投資有限公司) and 1,433,854,500 overseas listed foreign invested shares are held by holders of overseas listed foreign invested shares.

If the Company concurrently issues all of the domestic invested shares and overseas listed foreign invested shares being 20% of each of the existing issued domestic invested shares and overseas listed foreign invested shares pursuant to Article 89(1), the shareholding structure of the Company shall comprise 5,211,737,400 ordinary shares of which 3,491,112,000 shall be issued as domestic invested shares to Zhejiang Provincial High Class Highway Investment Company Limited (浙江省高等級公路投資有限公司) and 1,720,625,400 shares shall be issued as overseas listed foreign invested shares to holders of overseas listed foreign invested shares.”

By Order of the Board
Zhang Jingzhong
Company Secretary

Hangzhou, Zhejiang Province, the PRC

24 March 1998

Notes:

1. Eligibility for attending the Annual General Meeting

Holders of H Shares who intend to attend the Annual General Meeting must give all transfer instruments and the relevant shares certificates to the share registrars for H Shares of the Company, HKSCC Registrars Limited, at or before 4:00 p.m. on Friday, 24 April 1998.

2. Registration procedures for attending the Annual General Meeting

- (i) A shareholder or his proxy should produce proof of identity when attending the meeting. If a holder of domestic invested share(s) appoints its legal representative to attend the meeting, such legal representative shall produce proof of identity and a copy of the resolution of the board of directors or other governing body of such shareholder appointing such legal representative to attend the meeting.
- (ii) Holders of H Shares and domestic invested shares intending to attend the Annual General Meeting should return the reply slip for attending the Annual General Meeting to the Company on or before 5 May 1998.
- (iii) Shareholders may send the above registration documents to the Company in person, by post or by fax.

3. Proxy

- (i) A member eligible to attend the Annual General Meeting is entitled to appoint, in written form, one or more proxies to attend and vote on behalf of him. A proxy need not be a member.
- (ii) A proxy should be appointed by a written instrument signed by the appointor or its attorney. If the form of proxy is signed by the attorney of the appointor, the power of attorney or other authorisation document(s) of such attorney should be notarised.
- (iii) To be valid, the power of attorney or other authorisation document(s) which have been notarised together with the completed form of proxy must be delivered, in the case of holders of domestic invested shares, to the Company and, in the case of holders of H Shares, to HKSCC Registrars Limited, not less than 24 hours before the time designated for holding of the Annual General Meeting.
- (iv) A proxy may exercise the right to vote by a show of hands or by poll. However, if more than one proxy is appointed by a shareholder, such proxies shall only exercise the right to vote on a poll.

4. Closure of Register of Members

The register of members holding H Shares of the Company will be closed from 25 April 1998 to 25 May 1998 (both days inclusive).

5. Miscellaneous

(i) The Annual General Meeting will not last for more than one day. Shareholders who attend shall bear their own travelling and accommodation expenses.

(ii) Share Registrars for H Shares of the Company, HKSCC Registrars Limited is at:

2/F, Vicwood Plaza
199 Des Voeux Road Central
Hong Kong

(iii) The registered address of the Company is at:

No. 2 Villa, 78 Beishan Road
Hangzhou 310007,
The PRC

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