



Chairman's Statement



Economic Landscape

The COVID-19 pandemic (the "Pandemic") had a crippling effect on the global economy in 2020. The Chinese economy also faced its most serious challenge since reforms first started and the country opened up, recording a 6.8% year-on-year drop in growth in the first quarter of the year, the lowest single quarter growth since the use of gross domestic product ("GDP") as a macro-economic indicator.

The central government took effective measures to curb the spread of the Pandemic across mainland China with effects seen by the end of the first quarter. In April, work and production gradually resumed and business activities recovered. The central government promptly rolled out fiscal and monetary policies to boost economic recovery, including drastically cutting taxes and fees by RMB2.5 trillion throughout the year. It also increased the issue of government bonds to raise the budgetary deficit ratio of the central government. During the year, the People's Bank of China took two Loan Prime Rate cuts, while local government and state-owned banks provided varying interest subsidies on corporate loans, driving interest rates down as a result. On the back of the concerted efforts of the government and the community, the country's economy has seen continuous recovery since the second quarter. By the end of the year, all key economic indicators except social consumption had returned to pre-Pandemic levels. Furthermore, China's GDP increased by 2.3% year-on-year, making China the only major economy in the world to achieve positive economic growth. As the Chinese economy recovered and the United States dollars ("USD") index declined, the exchange rate of Renminbi ("RMB") against the USD strengthened, rising by over 7% in aggregate during the year.



During the year, China entered into several strategic agreements, ranging from “Regional Comprehensive Economic Partnership” to “China-EU Comprehensive Agreement on Investment” with several Asia-Pacific countries and the European Union, to help ease external fluctuations in the economic environment arising from the Sino-US trade friction. Also, though the Pandemic risks in mainland China still exist to an extent, prevention and control measures have become normal practice. As such, the Chinese economy is expected to gradually emerge from the crisis and embark on a new course of top-quality development, as the country enters the opening year of its fourteenth five-year plan (“14th Five-Year Plan”).

Reforms in the Marketisation of Natural Gas

In 2020, the market economy reforms for natural gas continued to abide by the principle of “regulating the core and relaxing the ends” to further promote the operation of the market system. In May 2020, the State Council of China promulgated the “Opinions of the Central Committee of Communist Party of China (“CCCPC”) and the State Council on Accelerating the Improvement of the Socialist Market Economy System in the New Era” to steadfastly promote reforms in inherently monopolistic industries, accelerate market-driven competition, open up oil and gas pipeline networks to market players, and favourably relinquish control over the sources and sale prices of natural gas.



Chairman's Statement

In March 2020, the National Development and Reform Commission (the "NDRC") officially promoted the new "Central Pricing Catalogue", moving the city-gate natural gas price from the main body of the catalogue to the appendix. It also recommends that the city-gate natural gas prices in the provinces with competitive capabilities can be determined by the market. This marked the starting point of the marketisation of city-gate natural gas prices in mainland China's upstream market. As trading volumes of natural gas in Shanghai and Chongqing's trading exchanges gradually rise, the source price of natural gas has increasingly been driven by the market. Accelerating these developments even further, the "Opinions on Promoting the Reform of Mineral Resources Management (Trial)" officially took effect on 1 May 2020, marking the full opening of the oil and gas exploration and exploitation market in the country's private enterprises and foreign-owned businesses.

On 1 October 2020, China Oil & Gas Pipeline Network Corporation ("PipeChina") officially commenced operation and began to implement consigner access management to open PipeChina's existing liquefied natural gas ("LNG") receiving terminals and natural gas pipelines to third-party vendors. With the pipeline networks of PetroChina Company Limited, China Petroleum & Chemical Corporation and China National Offshore Oil Corporation, as well as provincial pipeline networks in Guangdong, Hainan, Hubei, and other provinces successively integrating into the national pipeline network in batches, the nation-wide "Single Network" began to take shape. PipeChina's official operations commencement is providing the relevant infrastructure for the diversification of gas sources in mainland China and the nationwide delivery of natural gas resources, alleviating the prevailing monopolistic landscape in the current upstream market.

With regard to reforms in the downstream market, on the one hand, the government continued to strictly control charges and prices in a bid to lower gas costs of customers. Given the impact of the Pandemic in 2020, the NDRC and governments at various levels required gas suppliers to reduce their sale prices to hit targets. These included lowering pipeline transmission charges and the early adoption of off-season prices, while also reiterating that local government should monitor the pricing and cost of transmission of natural gas on provincial pipeline networks as well as the supply price of urban fuel gas. These efforts will ensure that the permitted profit margin will not exceed 7% or lower (as appropriate). To further rectify and regulate urban gas supply charges, five ministries and commissions, including the NDRC, jointly promoted the "Opinions on Regulating the Standards of Charges of Urban Water, Power, Gas and Heat Supply Industries to Promote Quality Development" in December 2020, for official implementation on 1 March 2021. On the other hand, local governments intend to facilitate the direct trading of natural gas between upstream and downstream markets as well as direct supplies to large-scale users, which may undermine the competitiveness of urban fuel gas companies. Within the Group, we are actively addressing the impact of government regulations and market competition by improving our business presence, enhancing full-supply chain capabilities and boosting smart operational processes, as well as by taking measures such as lowering costs and enhancing efficiencies.

Outlook for the Natural Gas Market

The Pandemic in 2020 severely hampered short-term demand for natural gas consumption in mainland China, with the impact being especially marked in the first half of the year, gradually easing in the second half of the year. Natural gas consumption in the year reached 324 billion cubic metres, representing a 5.6% year-on-year increase, though growth overall was 2% lower than that in 2019.



The Group believes that as the impact of the Pandemic diminishes and as the country's economy gradually recovers, normal demand growth in the natural gas market will resume. "The CCCPC's Proposals for Formulating the 14th Five-Year Plan for National Economic and Social Development and the Long-Range Objectives Through the Year 2035" (the "14th Five-Year Plan Proposals") suggested that the fully-fledged green transformation in the economic and social development plan should be facilitated to expedite the promotion of green and low-carbon development. It has thus formulated an action plan for carbon emissions to peak by 2030. Although natural gas is a fossil fuel, it is also a clean energy, which will play a principal role in the transformation of energy development in China. According to plans, it is targeted to hold a 15% share in primary energy consumption by 2030, continuing to increase from this basis into the future. Furthermore, the "Administrative Measures for Carbon Emissions Trading (Trial)" has been implemented nation-wide on 1 February 2021 to increase the willingness of large industrial and energy-consuming enterprises to switch to clean energy. This move will boost the demand for natural gas in industrial and power generation environment.

With regard to the infrastructure, conditions for the development of natural gas in mainland China have steadily improved. The interconnected supply system, featuring the "West-to-East Gas Pipeline, North-to-South Gas Pipeline, Offshore Gas Pipeline to Coastal Areas and Nearby Gas Source" projects, have taken shape, better balancing supply and demand. The degree of interconnection of nation-wide pipeline networks, the receiving capacity with the expansion of LNG receiving stations, as well as the operational gas volume of underground gas storage facilities have all increased. Natural gas production in mainland China reached 188.8 billion cubic metres in 2020 while the daily piped gas supply capacity of the China-Russia East-Route Natural Gas Pipeline transporting gas to the Beijing-Tianjin-Hebei region via northeastern China increased by 27 million cubic metres. With the reliance on external natural gas being stabilised, the average price of imported gas sources fell steadily. These factors are extremely conducive to the long-term stable development of the natural gas market in mainland China.

The reforms of the natural gas market in the country as well as the transformation of energy development strategies will result in further changes to the natural gas market. These will include the new trend to diversify gas sources in the upstream market, the further regulation and consolidation of the city gas market, as well as integrated, efficient and smart applications of natural gas in the downstream market. To align ourselves with this new market landscape, we will further strengthen our presence in the natural gas industry chain, closely monitor the progress of regional market consolidation and fully promote smart applications of natural gas. This will allow us to better respond to industry challenges and seize our market opportunities.

Environmental, Social and Governance (ESG)

In recent years, there has been an increasing emphasis on environmental, social and governance issues and performance around the world. Upholding our corporate vision and mission, we make every effort to set an example and act as a role model in our business operations. We thus seek to protect the health and safety of our stakeholders, care for our environment and serve the community.

The Group's Board of Directors promotes a proactive ESG agenda, regularly reviews important ESG issues, and has set up an ESG Committee composed of our chief executive officer and several senior executives. This committee is responsible for integrating ESG into our business and operations, promoting related plans, and regularly reporting the progress of relevant projects and related matters to the Board.

In 2020, Towngas China was selected as a constituent stock of the Hang Seng Corporate Sustainability Benchmark Index Series for the tenth year, demonstrating the extensive recognition of the Group's ESG performance by the community.



Chairman's Statement

In addition, we won numerous awards during the year, including the "Listed Company with the Best Investment Potential" from Hong Kong Ta Kung Wen Wei Media Group, The Hong Kong Institute of Chartered Secretaries and the Hong Kong Chinese Enterprises Association. We also received the "Cutting Edge Enterprise in Energy Innovation" award from Energy magazine, in recognition of our financial performance and the foresight of our business development strategies.

We attach great importance to integrity, strictly abiding by, and implementing, ethical principles in our business operations, as a core corporate value. With these clear objectives, our aim is to create long-term value for all our stakeholders, from investors and partners to suppliers, employees and the community.

Our Business Outlook

Amid the 2020 Pandemic, our Group took proactive measures, uniting our staff at all levels to exercise sound disease prevention and control procedures, while remaining committed to our work. We worked hard to ensure a safe gas supply, actively helped customers to solve their concerns and problems, made every effort to render assistance to residents and the community, whilst at the same time, uniting to fight the virus, underpinned by our corporate values of "courtesy", "craftsmanship" and "integrity". During the year, our business faced great challenges, but we were able to maintain stable overall development, with both ongoing progress as well as several breakthroughs on a number of fronts.

Following the Group's entry into a capital increase agreement with Shanghai Gas Co., Ltd. ("Shanghai Gas") and Shenergy (Group) Company Limited ("Shenergy Group") in October 2020, all parties to the agreement have started to communicate on a number of business fronts. The progress of the collaboration is thus well on schedule. With a population of over 24 million, Shanghai is a huge gas market. Shanghai Gas has a customer base of 6.3 million and an annual natural gas sales volume of more than 9 billion cubic metres. Through the cooperation, we will not only extend our business footprint to Shanghai, the most economically developed city in China, but also create substantial synergies for our business presence in eastern China and the entire Yangtze River Delta. Furthermore, we will also benefit from the expansion of our scale of business and the enhancement of our quality of development. Yet another benefit is our ability to access and use the facilities of Yangshan Port LNG receiving terminal which is operated by Shanghai Gas. This will also help to expand our channels for the direct purchase of natural gas from abroad.

We also consolidated our capacities across the natural gas industry chain during the year. Jintan Gas Storage, owned by our parent company The Hong Kong and China Gas Company Limited ("HKCG"), saw its successful interconnection with the "West-to-East Gas Pipeline" and "Sichuan-to-East Gas Pipeline" networks. Gas from gas storage facilities to cater for peak requirements can thus be transmitted through these national pipeline networks, supplying over 140 million cubic metres of gas in 2020 to gas enterprises in the vicinity. Riding on the back of Tangshan Haohua Trading Co., Ltd., newly established by HKCG, as well as the joint investment initiative between HKCG and Caofeidian Suntien Liquefied Natural Gas Co., Ltd., we will be able to access gas storage services at the Tangshan LNG terminal and gas sources for imported LNG, to boost the capacity of our gas enterprises in China's northern and northeastern regions, ensuring that gas storage will cater for peak requirements. A new Group company, Towngas Sichuan United Energy Co., Ltd., was established in September 2020 to explore the use of shale gas in the upstream market, liquefaction exports and other trade related business. This new establishment will strengthen the capacity of our gas businesses in the southwestern regions, providing better gas storage to cater for peak requirements while also gaining greater access to stable and quality gas sources.



Aligning our business to the 14th Five-Year Plan, we will continue the development of distributed energy projects, aiming to provide users with affordable and highly efficient heating energy. In the meantime, we will continue to expand our commercial hot water sales, as well as our heating, cooling and heat supply businesses to boost the volume of gas sales.

Grasping the opportunities presented by the need for disease prevention and control, we strongly promoted the digital transformation of our offline business under the Towngas Lifestyle brand, enhancing the functionalities of our online service centre. An integrated Internet platform has been initially established, covering the gas cloud, smart Internet of Things, e-commerce and household services right on doorsteps. This innovative business model will facilitate the advancement of our extended business initiatives to achieve economies of scale. Towngas Lifestyle will consolidate our offline resources, focusing on our primary aim to provide the community with services for a healthy and comfortable lifestyle, coordinating with digital channels to create a new community business platform. In December 2020, the first Towngas China Home Lifestyle Centre under HKCG, “Moment+”, officially opened in Hudong community in the Suzhou Industrial Park, Jiangsu province. Going forward, more shops will be opened in a number of regions to provide the public with premium lifestyle services. In addition, Towngas Lifestyle consolidated our gas insurance promotion resources during the year, to buck the trend and achieve significant growth in gas insurance sales. Our “Cosy Home” brand, providing residents with smart kitchen, heating and water purification products and services, was officially launched, while our safe gas appliances under the Bauhinia brand recorded stable sales. Sales of our Mia Cucina signature cabinets also achieved notable growth, with its business promotion initiatives, which extended to a number of cities and provinces including Shanghai, Guangdong, Anhui and Shandong.

Our engineering arm, U-Tech (Guang Dong) Engineering Construction Co., Ltd acquired Jiangsu Jinzhuo Construction Engineering Co., Ltd. in September 2020 to become its controlling shareholder. The acquisition has resulted in enhanced engineering service qualification, an expanded talent pool and rational business planning to coordinate the improvement of engineering service processes throughout the country. The move also expands the variety of our engineering services and reduces the impact of lower engineering installation fees and any slowdown of the market economy.

2021 sees the kick-off of China’s 14th Five-Year Plan as well as our embarkation on a new stage in the Group’s business development. The Group has put forth “Smart Innovation Year” as the development theme of 2021 and proactively laid out our business development blueprint under the 14th Five-Year Plan, leveraging the opportunities arising from China’s development and industry transformation. As we drive our business towards a new stage of quality development, we continue to uphold our vision to be Asia’s leading clean energy supplier and quality service provider, with a focus on innovation and environmental friendliness.

Alfred Chan Wing-kin

Chairman

Hong Kong, 18 March 2021