

REVIEW OF OPERATIONS



G=i x i

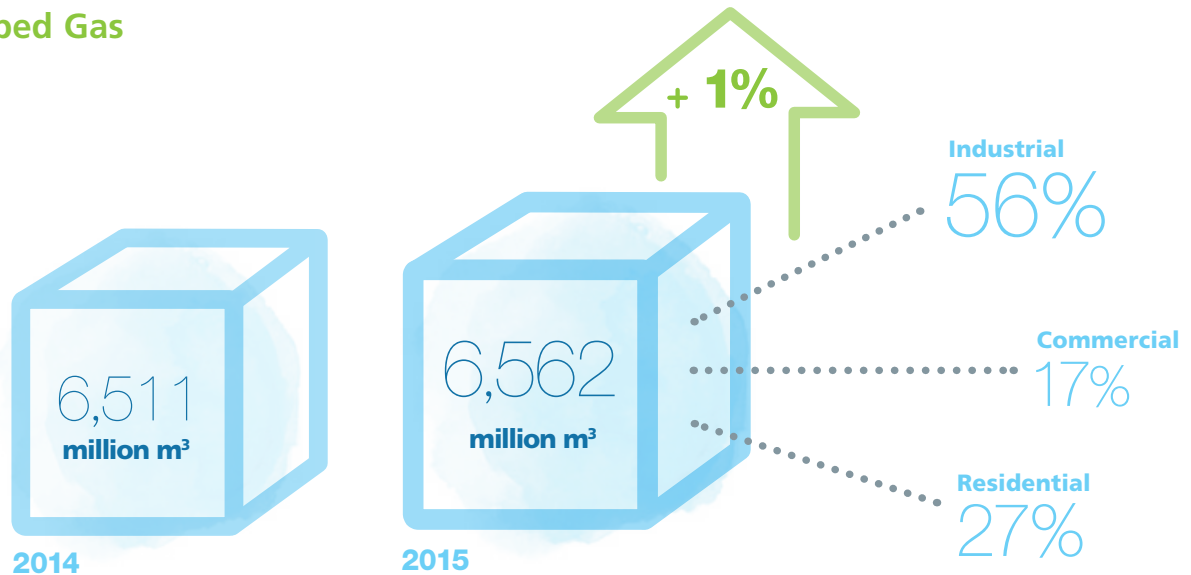
“ China’s GDP growth recorded a 25-year low of merely 6.9% in 2015. As the growth of the manufacturing sector in China continued to decelerate, coupled with the tumbling oil prices and other macroeconomic factors, as well as the lagging adjustment of piped natural gas prices, sales in the natural gas industry in China deteriorated.

Despite the sluggish economic environment, our businesses succeeded in achieving steady growth in 2015 due to the concerted efforts of the Group as a whole. In view of the Group’s forward-looking development strategies based on the prevailing circumstances, we not only continued to proactively expand our customer base, but also ventured into new business areas, thereby injecting additional growth momentum to the Group’s businesses. At the same time, we continued to leverage our inherent advantages leading to positive results in our different businesses. Among these, both the number of our customers and the sales of Bauhinia gas appliances grew steadily, while the total volume of city-gas sales remained stable. Our ability to achieve such results against the difficult backdrop of slowing economic growth was satisfactory indeed.

As always, we continued to pursue continuous innovation as well as Total Quality Management (TQM) in our daily operations. To enhance operational efficiencies, and ultimately drive business growth, every effort was also made to unleash the power of creativity and advancement while enhancing workflow. To this end, we promoted the importance of TQM among our regional offices and project companies across the country. As a result, staff implemented improvement initiatives throughout the Group leading to further enhancements in workflow in a number of aspects, ranging from engineering, and safety to services. Furthermore, the easy-to-understand formula ($G = i \times i$, Growth = innovation x implementation), which was specially designed to highlight the Group’s management direction, came to fruition last year in a number of wide-ranging categories. This substantially improved overall efficiencies and brought in an increasingly effective range of services to our customers.

In 2015, in addition to investing in our manpower resources, the Group remained committed to enhancing our corporate social responsibilities as we worked towards building a sustainable community and environment, while also pursuing our ongoing business growth.

Piped Gas



In 2015, the Group sold a total of 6,562 million cubic metres of piped gas, representing an overall increase of 1%, with a total number of 10.04 million customers. Industrial gas sales is 3,679 million cubic metres, accounting for 56% of the total volume of gas sold by the Group, while commercial gas sales is 1,111 million cubic metres, accounting for 17% of the total volume of gas sold by the Group, and residential gas sales accounted for 27% of the total volume of gas sold by the Group.

As the growth of the manufacturing sector in China continued to slacken, some large enterprise customers cut their production volume, affecting the overall industrial gas consumption. The Group seized business opportunities swiftly on the back of its abundant gas supply in vigorously expanding into the commercial gas market, so as to ensure the continued future growth of the gas sales of the Group.

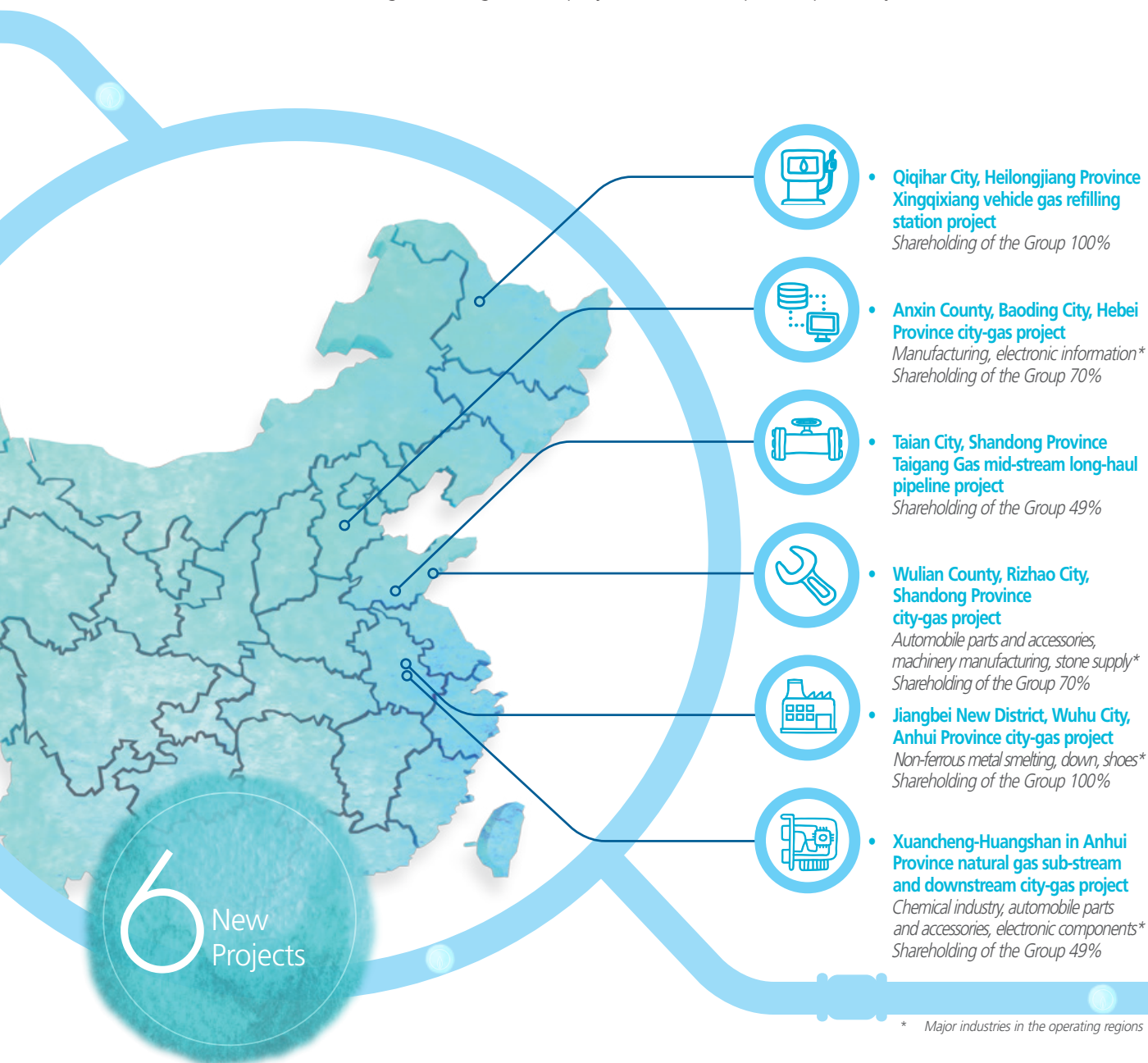
2015
Total Number of Customers **10.04** Million



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New Projects

We continued to expand the geographic footprint of our business presence with the acquisition of a total of six new gas projects in Shandong Province, Hebei Province, Anhui Province and Heilongjiang Province, including city gas projects in Wulian County in Rizhao City, Shandong Province, Anxin County in Baoding City, Hebei Province, Jiangbei New District of Wuhu City, Anhui Province; Xuancheng-Huangshan natural gas sub-stream and downstream city-gas project, Anhui Province; Taigang Gas mid-stream long-haul pipeline project in Taian City, Shandong Province, and Xingqixiang vehicle gas refilling station project located in Qiqihar City, Heilongjiang Province, the second vehicle gas refilling station project of the Group in Qiqihar City.



* Major industries in the operating regions

Industrial and Commercial Markets

The growth of China's industrial production decelerated as a result of the weakening global economic situation in 2015. At the same time, aiming to regulate the lavish consumption visible in certain circles, the central government implemented its Eight-point Code to curb spending and reduce excessive lavishness. This dealt a blow to the high-end catering industry. As such, the already difficult business climate in the industrial and commercial market sector, which accounts for around 73% of the Group's overall gas usage, worsened even further.

The Group, however, implemented targeted strategies to address the situation. This helped to consolidate our foundations for the further development of our industrial and commercial business.

Industrial

Revamp of Boilers

Benefiting from the national environmental protection policy and air quality improvement measures with its target to prohibit new boilers from using coal and convert all small boilers to use clean fuels by the end of 2017, we were able to proactively persuade industrial customers to opt for new gas-for-coal substitutions.

As a result and in view of the scale and scope of the many revamped boiler projects made during the year, our sales of natural gas is expected to record considerable growth in the year to come.



Supporting the development of clean energy, the production plant of Mengniu Dairy is equipped with natural gas boilers.



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Energy-efficient Kilns

Despite the fact that natural gas has not enjoyed many price advantages over coal, as the price of the latter has declined steadily over the years, we were able to successfully attract a number of industrial customers to make the switch to natural gas to benefit from its environmental benefits. We have worked closely with kiln specialists and professional institutions to develop kilns which use innovative technologies to enhance efficiencies. These energy-efficient kilns have not only helped customers to cut fuel and operational costs, they are also recognised as eco-friendly businesses. Additionally, the National Development and Reform Commission lowered non-residential natural gas city-gate prices in late 2015, which will pave the way forward for further developments in the industry.

During the year, many large-scale kiln revamps were completed. In Songyang County, Zhejiang Province, a stainless steel pipe manufacturer switched to an energy-efficient natural gas kiln. This has improved product quality and enhanced efficiencies.

Commercial

In the commercial market, the Group made a concerted effort to tap into the small and medium scale restaurant market. To this end, we laid pipelines in advance at the initial stages of road construction projects in provincial areas. We also streamlined the installation process, lowering thresholds and shortening the timeframe for project construction. This has enabled customers to use natural gas as soon as possible while also saving on our investment costs. As a result, in 2015, the number of our new commercial customers increased by a positive 2.4% in comparison to 2014.



This food court in Jiangsu Province is one of our small and medium scale catering customers who made the successful transition to natural gas.

Looking forward, the Group will continue to not only identify projects with high potential but also form partnerships with business associates to research and incubate more innovative solutions that will deliver energy-saving benefits. As we improve efficiencies in natural gas applications for our customers, we will in turn attract more industrial and commercial customers to switch to, and adopt, this clean source of energy. This will further expand our customer base which will accelerate growth and increase momentum in our businesses. At the same time, we are keeping an eye on the emerging opportunities arising from new policies and technologies, the combined heat and power business for example. The Group's strategies to foster cooperation with both local and international institutions will also bring in technological innovations, which will help to further expand both our businesses as well as our geographical footprint.

Residential

In 2015, the number of our residential customers, who account for approximately a quarter of the Group's total gas sales, recorded a substantial increase of 800,000.

Hand-in-hand with this growth, we expanded our customer service network, adding a total of 6 customer centres during the year to meet the ever-growing service demand. We also introduced a brand new app, "Ganghua Pay", allowing customers to check their personal accounts, details of their bills and make payment anytime, anywhere. Users can log onto our website via this mobile app on their smartphones, making these service procedures both more user-friendly and efficient.

Adhering to our "Customer-oriented, Professional and Efficient" service principle, we set both comprehensive and stringent service targets. Our service pledge affirms these service targets, which cover gas safety and reliability, the speed and convenience of service appointments, service quality as well as customer response. Performance results against these service targets are published regularly to promote further enhancement to our service quality.

In addition, we rolled out the first cross-evaluation mechanism among our project companies across the country during the year. Independent institutions were also commissioned to carry out "mystery shopper" customer satisfaction surveys to provide an even more objective view of our performance.

We maintain an ongoing flow of communication with our customers through multi-channels. These range from customer focus groups and service hotlines to customer opinion handling committees. These activities help us to gain comprehensive evaluations of our service quality and a better understanding of our customer needs, enabling us to provide better services and products, while also ensuring that the Group's service quality is best in class in the country.

During the year, we also launched a number of programmes to enhance our "customer experience" – our "Dandelion Scheme", an elite customer service-training scheme and "Service with a Smile Ambassador Competition" for example. Taking our service quality to the next level, we also launched the Group's first "We Smile" campaign, looking for individual stories and anecdotes to be published on social media platforms, to promote our caring, sincere and professional services.



Our "Service with a Smile Ambassadors" are chosen from amongst the many contestants nominated by our different project companies. The champion of the competition in 2015 demonstrates her caring services at our Customer Centre in Taian City, Shandong Province.

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Branding and Extended Services

The Group is not only focused on expanding our core gas business and selling Bauhinia gas appliances, we are also committed to providing a range of value-added services to our customers. Our aim is to enhance customer lifestyles with the premise “Quality Kitchen, Contemporary Living.”

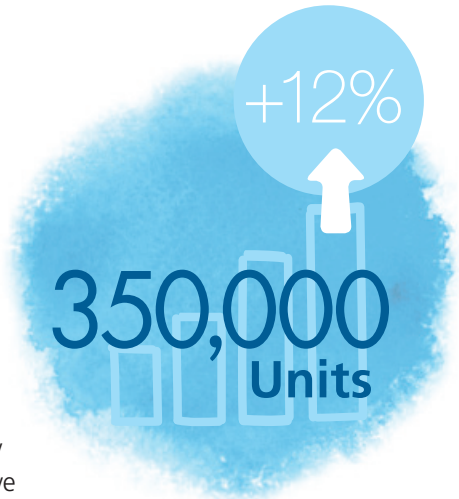
Branding

Bauhinia

Since its inception over a decade ago, Bauhinia has enjoyed tremendous popularity among our customers. This year, Bauhinia sales grew to approximately 350,000 units, a 12% increase over the same period last year.

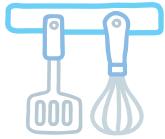
New generations of Bauhinia appliances are released regularly. This constant innovation enables us to stand out, well ahead of the competition. Bauhinia gas stoves with their national first-grade energy efficiency ratings in 2015, for example, provide customers with innovative products that promote a green lifestyle. The latest series of Bauhinia products also benefit from built-in microcomputers using cutting-edge technology to automatically adjust water, gas, air and temperature levels. These up-to-date facilities reduce carbon dioxide emissions while fully reflecting our green philosophy.

In the past year, we also won several customer service awards. This included being named as one of the “Top 10 After-sales Service in China” awardees, in recognition of our outstanding Bauhinia after-sales services.



On the occasion of its tenth anniversary, Bauhinia organised a “Cooking for Mom” competition to celebrate and promote flame-cooking while at the same time raising awareness of the safe use of gas.

Extended Services



Displaying its imported and beautifully designed kitchen cabinets, the Mia Cucina showcase in our customer centre in Taian City, Shandong Province, provides customer-oriented one-stop services.



In addition to our large base of 10 million customers and widespread customer service network, we expanded our services even further, venturing into new businesses to provide our customers with one-stop value-added services. Our new range of “Towngas Lifestyle” extended services and products were thus introduced. These include comprehensive gas insurance and quality home products as well as high-end kitchen cabinets, with more yet to come.

Gas Insurance

In line with our “Safety First” principle, we launched the Group’s first household gas insurance service in the second quarter of the year to offer our customers further value and “peace of mind”. Benefiting from our well-established and sophisticated bulk purchasing mechanisms, suppliers are selected under stringent screening criteria to provide comprehensive insurance coverage to ensure household safety. Since the successful introduction of this insurance initiative, more than 40,000 policy-holders have signed up for this service.

Quality Home Products

We have introduced an array of middle and high-end overseas kitchenware brands together with a number of fashion kitchenware products complying with the highest safety standards. In 2015, we set up a pilot showcase in our customer centre in the Eastern Region to sell quality household products that complement our “Quality Kitchen, Contemporary Living” philosophy. We also launched an online sales platform allowing customers to purchase fashionable, decorative yet useful home products and kitchenware anywhere and at anytime.

High-end Kitchen Cabinets

With the help of our parent company HKCG, we introduced the high-end kitchen cabinet brand Mia Cucina. Mia Cucina cabinets use first class materials imported from Europe, with an ergonomic, fashionable and minimalist design. Hand-in-hand with these cabinets, we provide professional services in design and installation, delivering tailored layouts to best suit the unique styles of individual customers. Currently, our Mia Cucina showroom in Taian City is helping our customers to create the perfect tailored workspace and quality standards of living to enjoy the many benefits of cooking.



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Safety

Safety underpins the sustainable development of any gas company. As an established leader in the city gas industry in China, we are famous for our stringent safety standards both in the sale and supply of gas as well as in our operations. In view of the tremendous importance that we attach to safety, a comprehensive safety and risk management regime has been specially designed to cover every aspect of our daily operations.

Following the strict occupational safety standards as set by our parent company, HKCG, we adopt an effective corporate safety and risk management scheme. We strictly enforce our "General Manager Safety Inspection System" and, adhering to the Group's guidelines, general managers are personally accountable for every aspect of safety and risk management in their project companies. They not only conduct monthly safety checks, they also supervise cross-checks among the different project companies twice a year. Led by the Chairman and Chief Executive Officer, members of the Safety Committee and management would pay visits and annual safety inspections to project companies in the different regions. During the year, the southwest region, Anhui, Jiangxi and the northeast regions were inspected. The Group also requires each project company to hold at least one joint drill with local police and fire service authorities every two years.

After years of commitment and hard work, all our remaining coke gas residential customers made the switch to natural gas in October 2015, laying the cornerstone for our full entry into the natural gas era.

We are committed to perfecting our safety management regime. As such, we are actively promoting our Engineering Supervisory Personnel Qualification System. Under this scheme, we provide training for engineering supervisors, helping them to obtain their safety supervisory training certificates. This move is enhancing standards in the industry even further.

The safe use of gas among our customers is one of our main priorities. Our customer service representatives therefore get in touch with customers, proactively scheduling safety checks once every 18 months. These checks, on the gas facilities and equipment at customers' premises, are carried out by our technicians as a precautionary measure. At the same time, we promote the safe use of gas to raise public awareness through animation clips. We

also implemented TQM (Total Quality Management) during the year to further enhance our safety and risk management systems.



Technician carries out regular checks on gas pipelines and other facilities to ensure safe gas supplies.

Engineering

As the major city gas supplier in China, the Group has designed and upholds stringent standards in every area, from production and engineering design to construction and technology application. As such, we have achieved considerable success in improving the overall level of service quality.

In the field of engineering technology and design, the Group formulated a series of guidelines to establish workflow standards in construction, installation and monitoring. During the year, the Group prepared and amended numerous guidelines, completing more than 20 new and revamped projects in accordance with these guidelines.

Streamlining on-site work procedures, Zhuojia Public Engineering (Maanshan) Company Limited was established to assemble precast units in full compliance with specified standards and requirements. This prefabrication process, which not only improves precision levels in pipeline installation but also the speed of installation, will enhance overall project efficiencies and lower the cost of installation and management works.

We pioneered to implement a production standardisation plan in the industry. Also, the Group continued to be invited to participate in the drafting of national, city and town-level industrial standards, making additional contributions to the development of the natural gas industry. During the year, the Group proposed amendments to nine national standards, which involved the codes and specifications of engineering technology, construction, acceptance, regular inspections, and the monitoring and protection of natural gas pipelines, such as the "Technical Specification for Trenchless Rehabilitation and Replacement Engineering of City Gas Pipelines". All our proposals were adopted by the authorities, both boosting and consolidating our industry leadership position. We were also invited to participate in the preparation of design codes and technical specifications on a number of city and town-level engineering projects – the "Code for Design of town gas distribution engineering" being a prime example.

Enhancing our daily operations, we actively pushed forward our gas pipeline network plan, to leverage regional synergies and improve peak shaving capabilities in gas storage. The plan not only improves the safety and reliability of gas supply, it also lowers our investment costs in engineering for the Group. Further integrating our engineering processes, the Group continued to employ intelligent information technology solutions in many aspects among our various project companies. This advanced technology, which includes an on-site inspection system together with other mobile applications among others, enhances the efficiency of on-site construction management.



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Human Resources

As at 31 December 2015, the Group employed a total of 21,548 staff.

We greatly value the importance of employee training and development and are fully committed to assisting staff to seize every opportunity to advance their careers. To this end, we have set up our own training institute and organised joint training courses with prestigious institutions to provide our employees across the entire Group spectrum with diversified training schemes, helping them to build their careers.

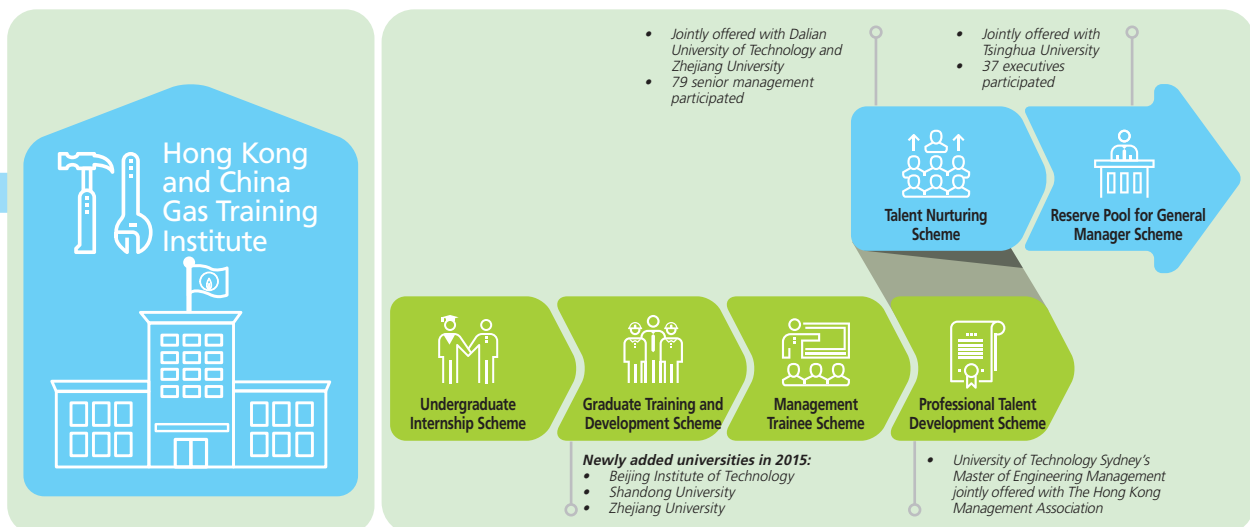


Hong Kong and China Gas Training Institute (Training Base for Eastern China Region) provides a wide-range of training in professional skills to nurture professional talent for the Group.

Our parent company, HKCG, established Hong Kong and China Gas Training Institute in the early years, setting up a total of five training bases in Shandong and other regions dedicated to providing Group employees with professional skills training. Examinations are also organised to help staff to obtain their professional qualifications. Regular experience sharing activities and in-house trainer programmes are also arranged amongst our project companies. During the year, over 3,200 staff participated in the Group's training schemes. The Hong Kong and China Gas Training Institute has also been invited to provide technical professionals to sit on judging panels at national and provincial-level industry competitions, consolidating our reputation as leading professionals in the industry.

The Group spares no effort to nurture talent, providing a wide range of joint training courses with well-known and highly distinguished domestic and overseas academic institutions. We also provide employees across the board with on-the-job training to help prepare them for their future careers. These programmes include the Undergraduate Internship Scheme, Graduate Training and Development Scheme, Management Trainee Scheme, Professional Talent Development Scheme, as well as the Talent Nurturing Scheme and Reserve Pool for General Manager Scheme.

We encourage our employees to maintain a positive work-life balance, while at the same time setting up an online learning platform for employees to pursue further studies during their leisure time. Our aim is to help them grow hand-in-hand with the development of the Group.



Corporate Social Responsibilities

While pursuing our business development, we also keep our corporate social responsibilities in mind. As such, we have integrated the principles of sustainable development into our daily operations and make every effort to balance environmental, social and economic factors in our corporate development strategies and in our day-to-day operations. Our goal is to make a contribution to the communities where we operate, and we are also committed to promoting the sustainable development of both the community and the environment.

Community Support

The Group has organised the Gentle Breeze Movement for charitable causes every year since its inception in 2013. We donate uniforms, sporting equipment, computers and other materials to schools located in remote mountainous areas, and help these schools refurbish their school buildings and build Towngas China Charity Libraries. Following the year's visits to impoverished villages in Guizhou, and with donations of over RMB1.35 million, a total of 18 schools benefitted from the Movement since its launch.

Our Towngas Rice Dumplings for the Community initiative is another flagship charitable programme. Every year we distribute rice dumplings to the elderly and people in need to celebrate the Dragon Boat Festival and promote a caring spirit within our neighbourhoods. Last year, 918 volunteers dedicated more than 3,400 hours to hand out over 27,000 rice dumplings and charity gifts, valued at more than RMB135,000, to community and welfare institutions, community care families and cleaning and construction workers. More than 8,600 people benefitted from this scheme.



Celebrating the Dragon Boat Festival, Mr. Wong Wai Yee, Peter, Executive Director and Chief Executive Officer, making dumplings with the elderly.



This year, volunteers of the Gentle Breeze Movement not only visited villages in Guizhou Province, they also built a Towngas Library at one of the local primary schools.

During the year, we continued to support the Firefly Programme run by the Shanghai Soong Ching Ling Foundation – BEA Charity Fund. The Fund helps rural schools with limited resources build multi-media classrooms and equip them with computers, internet connection facilities, books as well as desks and chairs. In 2015, we again donated over RMB200,000, in addition to hosting the opening ceremony for the fourth Firefly Centre in Longkou City, Shandong Province. We have been sponsoring this initiative since 2009.

We are highly concerned with regard to the education of the next generation, particularly the “left-behind children in rural China” whose parents work in the cities. As such we allocate resources from our daily operations to allow volunteers to support the China Guangcai Program Foundation and Beijing Global Village Environmental Education Centre. During the year, we sent three batches, consisting of a total of nine volunteers. Each batch spent six months in Yangqiao Village and Daping Village in Wuxi County, Chongqing City to provide tuition and care for these children who remain in their rural hometowns.

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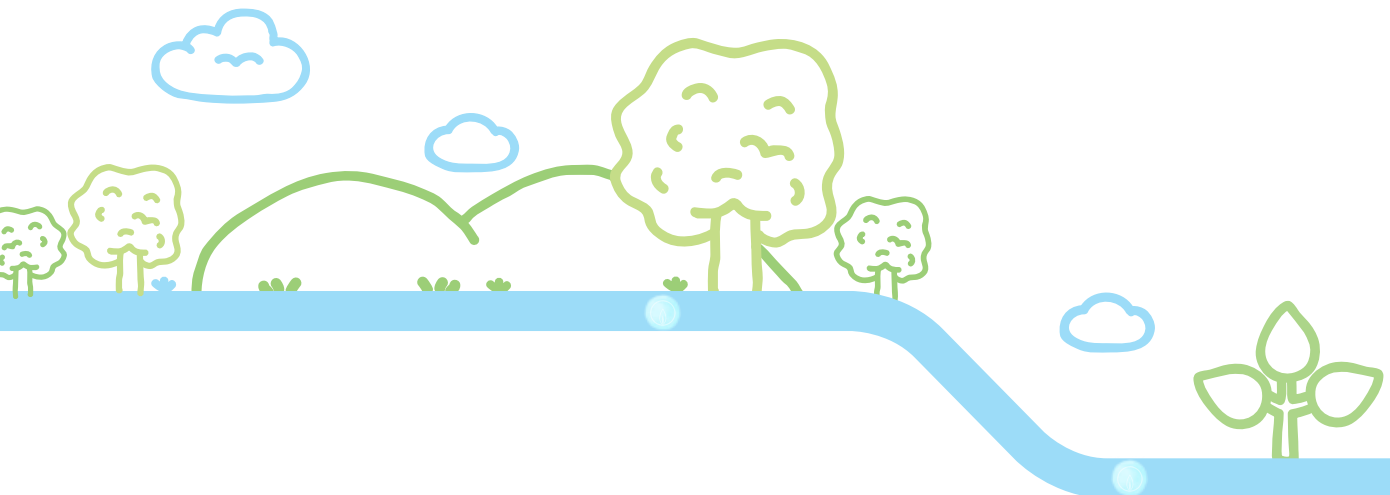
Environmental Protection



Towngas China Volunteer Teams participated in "A Date with Towngas China Forest" tree-planting campaign to create a greener environment.

As a clean energy supplier and with our social responsibilities in mind, we are not only committed to improving the energy efficiencies of our daily operations together with our products and services, we also participate in a number of environmental protection activities such as tree planting programmes.

Apart from these environmental protection activities, we also encourage our partners and customers to lead a green lifestyle. During the year for example, we launched our "A Date with Towngas China Forest" campaign, successfully inviting 11 partner institutions to work together with us towards a greener community. As a result, nearly 4,000 trees were planted, forming a green zone of some 8,000 square metres.



Long-term Development Strategy

The Group's mission is to provide our customers with a safe, reliable supply of gas and the caring, competent and efficient service they expect, while working to preserve, protect and improve our environment.

Moving forward, we will continue to focus on gas-related investment, exploration, sales and operation management. We continue to uphold our principle of prudent financial management, while at the same time grasping every business opportunity to boost reasonable returns for our shareholders.

According to China's Thirteenth Five-Year Plan, the country's clean energy policies will continue to foster city-gas development in China. It will also play an important role in the government's response to climate change. Looking to the future, in view of the Group's inherent business advantages – our reputable gas brand and professional and reliable customer services, the Group will be able to seize market opportunities and further expand our business initiatives to sustain our well-established industry leading position.

Meanwhile, the Group will continue to lead our project companies in our expansion into new arenas and the setting of new milestones. We will continue to fulfil our corporate social responsibilities, uphold our charity spirit and protect our environment, to spur our ongoing growth and sustainable business development.

