# Kunming Dianchi Water Treatment Co., Ltd.
# 昆明滇池水務股份有限公司

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

**(Stock Code: 3768)**

## RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2017

**FINANCIAL SUMMARY**

For the year ended 31 December 2017, the Group's:

- revenue amounted to approximately RMB1,224 million, representing an increase of 33.76% from 2016;
- profit before income tax amounted to approximately RMB372 million, representing an increase of 13.94% from 2016;
- profit attributable to equity holders of the Company amounted to approximately RMB313 million, representing an increase of 13.85% from 2016;
- earnings per share amounted to approximately RMB0.33, representing a decrease of 13.16% from 2016.

The Board recommends the distribution of a final cash dividend of RMB0.1527 per share (tax included) (2016: RMB0.1 per share (tax included)) (RMB157,145,249.70 in total (tax included)) to all shareholders, subject to the approval of shareholders at the annual general meeting for 2017 to be held on Friday, 22 June 2018. The expected dividend distribution date is Wednesday, 8 August 2018.

The board of directors (the "**Board**") of Kunming Dianchi Water Treatment Co., Ltd. (the "**Company**") announces the audited results of the Company and its subsidiaries (collectively, the "**Group**") for the year ended 31 December 2017 (the "**Reporting Period**"), together with the comparative figures for the year ended 31 December 2016, as following:

## I. FINANCIAL STATEMENTS AND NOTES THERETO

### CONSOLIDATED BALANCE SHEET

*As at 31 December 2017*

| | | As at 31 December | |
|---|---|---|---|
| | *Notes* | **2017** | 2016 |
| | | ***RMB'000*** | *RMB'000* |
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Land use rights | | **445,974** | 433,484 |
| Long term prepayments | | **450,000** | 450,000 |
| Property, plant and equipment | | **2,342,663** | 2,369,089 |
| Receivables under service concession arrangements | *11* | **529,997** | 341,944 |
| Amounts due from customers for construction contracts | *12* | **238,383** | 35,573 |
| Intangible assets | | **135,099** | 75,197 |
| Investments in associates | | **15,257** | 15,101 |
| Prepayments for acquisition of subsidiaries | | **43,356** | 79,950 |
| Deferred income tax assets | | **32,957** | 23,697 |
| | | **4,233,686** | 3,824,035 |
| **Current assets** | | | |
| Receivables under service concession arrangements | *11* | **13,747** | 9,679 |
| Inventories | | **7,515** | 10,336 |
| Amounts due from customers for construction contracts | *12* | **12,296** | 5,716 |
| Available-for-sale financial assets | | **80,000** | – |
| Trade and other receivables | *13* | **386,397** | 306,895 |
| Cash and cash equivalents | | **1,291,170** | 446,830 |
| | | **1,791,125** | 779,456 |
| **Total assets** | | **6,024,811** | 4,603,491 |

**CONSOLIDATED BALANCE SHEET (Continued)**

| | | As at 31 December | |
|---|---|---|---|
| | *Notes* | **2017** | 2016 |
| | | ***RMB'000*** | *RMB'000* |
| **Equity** | | | |
| **Capital and reserves attributable to equity holders of the Company** | | | |
| Share capital | | **1,029,111** | 720,000 |
| Other reserves | | **1,413,937** | 696,513 |
| Retained earnings | | **1,257,039** | 1,077,795 |
| | | **3,700,087** | 2,494,308 |
| **Non-controlling interests** | | **6,114** | 5,102 |
| **Total equity** | | **3,706,201** | 2,499,410 |
| **Liability** | | | |
| **Non-current liabilities** | | | |
| Deferred revenue | | **157,479** | 107,121 |
| Borrowings | | **1,091,625** | 741,995 |
| Deferred income tax liabilities | | **39,848** | 9,321 |
| | | **1,288,952** | 858,437 |
| **Current liabilities** | | | |
| Trade and other payables | *14* | **369,850** | 422,339 |
| Current income tax liabilities | | **60,238** | 44,568 |
| Borrowings | | **599,570** | 778,737 |
| | | **1,029,658** | 1,245,644 |
| **Total liabilities** | | **2,318,610** | 2,104,081 |
| **Total equity and liabilities** | | **6,024,811** | 4,603,491 |

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

*For the year ended 31 December 2017*

| | *Notes* | **For the year ended 31 December** **2017** ***RMB'000*** | 2016 *RMB'000* |
|---|---|---|---|
| **Revenue** | *3* | **1,223,825** | 914,925 |
| Cost of sales | *6* | **(723,335)** | (489,444) |
| **Gross profit** | *6* | **500,490** | 425,481 |
| Selling expenses | *6* | **(13,875)** | (10,605) |
| Administrative expenses | *6* | **(124,490)** | (97,604) |
| Research and development expenses | | **(7,282)** | (7,398) |
| Other income | *4* | **93,291** | 82,019 |
| Other losses – net | *5* | **(4,817)** | (1,272) |
| **Operating profit** | | **443,317** | 390,621 |
| Finance income | | **33,706** | 16,670 |
| Finance costs | | **(104,754)** | (80,299) |
| Finance costs – net | *7* | **(71,048)** | (63,629) |
| Share of results of associates | | **156** | (121) |
| **Profit before income tax** | | **372,425** | 326,871 |
| Income tax expense | *8* | **(58,336)** | (51,193) |
| **Profit for the year** | | **314,089** | 275,678 |
| **Profit attributable to:** | | | |
| – The equity holders of the Company | | **313,077** | 274,993 |
| – Non-controlling interests | | **1,012** | 685 |
| | | **314,089** | 275,678 |
| **Other comprehensive income** | | **(1,847)** | – |
| **Total comprehensive income for the year** | | **312,242** | 275,678 |

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Continued)**

| | | For the year ended 31 December | |
|---|---|---|---|
| | *Notes* | **2017** | 2016 |
| | | ***RMB'000*** | *RMB'000* |
| **Attributable to:** | | | |
| – The equity holders of the Company | | **311,230** | 274,993 |
| – Non-controlling interests | | **1,012** | 685 |
| | | **312,242** | 275,678 |
| **Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in RMB per share)** | | | |
| – Basic and diluted earnings per share | *9* | **0.33** | 0.38 |
| Dividends | *10* | **102,911** | – |

# NOTES TO THE FINANCIAL STATEMENTS

*For the year ended 31 December 2017*

## 1 CORPORATE INFORMATION

The Company was incorporated in Yunnan Province of the PRC on 23 December 2010 as a joint stock company with limited liabilities under the Company Law of the PRC. The registered office of the Company is located at Wastewater Treatment Plant No. 7, Kunming Dianchi Tourist Resort, Yunnan Province. The Company's shares were listed on the Main Board of The Stock Exchange of Hong Kong Limited on 6 April 2017.

The Group is principally engaged in the development, design, construction, operation and maintenance of water supply and wastewater treatment facilities in the PRC.

The consolidated financial statements are presented in Renminbi ("**RMB**"), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 26 March 2018.

The Group's financial position was specifically subject to the following events and transactions which occurred during the Reporting Period:

- The Company completed the initial public offering on 6 April 2017.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of the financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

***(a) Compliance with International Financial Reporting Standards and Hong Kong Company Ordinance***

The consolidated financial statement of the Company has been prepared in accordance with International Financial Reporting Standards ("**IFRSs**") and the disclosure requirements of the Hong Kong Company Ordinance Cap. 622.

***(b) Historical cost convention***

The financial statements have been prepared under the historical cost convention except for available-for-sale financial assets which were measured at fair value.

***(c) New standards and amendments to standards adopted by the Group***

In preparation of annual report from 1 January 2017, the Group initially adopts the following standards and amendments to standards

- Recognition of deferred tax assets for unrealised losses – amendments to International Accounting Standards ("**IAS**") 12, and
- Disclosure initiative – amendments to IAS 7

The adoption of such amendments does not affect the amounts recognised in past periods. Most amendments will not affect the current period or further periods.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.1 BASIS OF PREPARATION (Continued)

#### *(d) New standards and interpretations not yet adopted*

Up to the date of this report, International Accounting Standards Board ("**IASB**") has issued the following new standards, amendments to standards and interpretations which are relevant to the Group's operations but are not yet mandatory for annual periods beginning on 1 January 2017 and which have not been early adopted by the Group:

| | | **Effective for the annual periods beginning on or after** |
|---|---|---|
| IFRS 9 Financial instruments and associated amendments to various other standards | IFRS 9 replaces the multiple classification and measurement models in IAS 39 Financial instruments: Recognition and measurement with a single model that has initially only two classification categories: amortised cost and fair value. | 1 January 2018 |
| IFRS 15 Revenue from contracts with customers and associated amendments to various other standards | The IASB has issued a new standard for the recognition of revenue. This will replace IAS 18 which covers contracts for goods and services and IAS 11 which covers construction contracts. The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer – so the notion of control replaces the existing notion of risks and rewards. | 1 January 2018 |
| IFRS 16 "Leases" | IFRS 16 will affect primarily the accounting by lessees and will result in the recognition of almost all leases on balance sheet. The standard removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. An optional exemption exists for short-term and low-value leases. | 1 January 2019 Early adoption is permitted only if IFRS 15 is adopted at the same time |

The Group does not plan to early adopt any of these standards. For these new standards not yet effective, the Group had assessed the impact and does not expect any significant impact on the Group's operating results or financial position.

### 2.2 Subsidiaries

#### *2.2.1 Consolidation*

A subsidiary is an entity (including a structured entity) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

*(a) Business combinations not under common control*

The Group applies the acquisition method to account for business combinations not under common control. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis. Non-controlling interests in the acquiree that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation are measured at either fair value or the present ownership interests' proportionate share in the recognised amounts of the acquiree's identifiable net assets. All other components of non-controlling interests are measured at their acquisition date fair value, unless another measurement basis is required by IFRSs.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.2 Subsidiaries (Continued)

#### *2.2.1 Consolidation (Continued)*

*(a) Business combinations not under common control (Continued)*

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date; any gains or losses arising from such re-measurement are recognised in the consolidated statement of comprehensive income.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognised in the consolidated statement of comprehensive income. Contingent consideration that is classified as equity is not remeasured, and its subsequent settlement is accounted for within equity.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If the total of consideration transferred, non-controlling interest recognised and previously held interest measured is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the consolidated statement of comprehensive income.

Intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the transferred asset. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

Results and non-controlling interest in interest of subsidiaries are separately presented in consolidated statement of comprehensive income, statement of changes in equity, and balance sheet.

*(b) Business combination under common control*

The financial information incorporates the financial statements of the combining entities or businesses in which the common control combination occurs as if they had been combined from the date when the combining entities or businesses first came under the control of the controlling party.

The net assets of the combining entities or businesses are combined using the existing book values from the controlling parties' perspective. No amount is recognised in consideration for goodwill or excess of acquirers' interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost at the time of common control combination, to the extent of the continuation of the controlling party's interest.

The consolidated statement of comprehensive income include the results of each of the combining entities or businesses from the earliest date presented or since the date when the combining entities or businesses first came under the common control, where there is a shorter period, regardless of the date of the common control combination.

The comparative amounts in the consolidated financial statements are presented as if the entities or businesses had been combined at the previous balance sheet date or when they first came under common control, whichever is earlier.

A uniform set of accounting policies is adopted by those entities. All intra-group transactions, balances and unrealised gains on transactions between combining entities or businesses are eliminated on consolidation.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.2 Subsidiaries (Continued)

#### *2.2.1 Consolidation (Continued)*

*(c) Changes in ownership interests in subsidiaries without change of control*

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions – that is, as transactions with the owners of the subsidiary in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

*(d) Disposal of subsidiaries*

When the Group ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognised in the consolidated statement of comprehensive income. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to the consolidated statement of comprehensive income.

#### *2.2.2 Separate financial information*

Investments in subsidiaries are accounted for at cost less impairment. Cost also includes direct attributable costs of investment. The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

Impairment testing of the investments in subsidiaries is required upon receiving dividends from these investments if the dividend exceeds the total comprehensive income of the subsidiary in the period the dividend is declared or if the carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial statements of the investee's net assets including goodwill.

### 2.3 Associates

An associate is an entity over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting. Under the equity method, the investment is initially recognised at cost, and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. The Group's investments in associates include goodwill identified on acquisition. Upon the acquisition of the ownership interest in an associate, any difference between the cost of the associate and the Group's share of the net fair value of the associate's identifiable assets and liabilities is accounted for as goodwill.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income is reclassified to the consolidated statement of comprehensive income where appropriate.

The Group's share of post-acquisition profit or loss is recognised in the consolidated statement of comprehensive income, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income with a corresponding adjustment to the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount adjacent to "share of results of associates" in the consolidated statement of comprehensive income.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.3 Associates (Continued)

Profits and losses resulting from upstream and downstream transactions between the Group and its associates are recognised in the Group's consolidated financial statements only to the extent of unrelated investor's interests in the associates. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

## 3 SEGMENT INFORMATION

The chief operating decision-maker has been identified as executive directors of the Company. Management has determined the operating segments based on reports reviewed by the executive directors of the Company for the purpose of allocating resources and assessing performance.

The executive directors of the Company consider the business from product and service perspective.

The Group's reportable segments are as follows:

- Wastewater treatment;
- Water supply; and
- Others, including management service and transportation service.

The executive directors of the Company assess the performance of the operating segments based on the measurement of revenue and operating profit.

Unallocated assets consist of deferred income tax assets and investments in associates. Unallocated liabilities consist of deferred income tax liabilities and current income tax liabilities.

Capital expenditure comprises mainly additions to land use rights, property, plant and equipment and intangible assets.

### (a) Revenue from all services

The revenue of the Group for the year ended 31 December 2017 is set out as follows:

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Wastewater treatment | **1,037,163** | 765,906 |
| Operating services – under TOO model | **739,620** | 697,322 |
| Operating services – under TOT/BOT model | **37,029** | 28,122 |
| Construction services – under BT model | **158,800** | 3,761 |
| Construction services – under BOT model | **82,213** | 22,426 |
| Finance income | **19,501** | 14,275 |
| Reclaimed water supply and running water supply | **68,520** | 62,366 |
| Operating services of reclaimed water supply – under TOO model | **8,262** | 6,814 |
| Operating services of running water supply – under TOT/BOT model | **10,251** | 5,668 |
| Construction services – under BT model | **5,657** | 11,711 |
| Construction services – under BOT model | **42,491** | 36,261 |
| Finance income | **1,859** | 1,912 |
| Others | **118,142** | 86,653 |
| Management services | **100,098** | 75,941 |
| Transportation services | **3,025** | 2,914 |
| Others | **15,019** | 7,798 |
| | **1,223,825** | 914,925 |

## 3 SEGMENT INFORMATION (Continued)

### (b) Segment information

The segment information provided to senior executive management for the reportable segments for the year ended 31 December 2017 is as follows:

| Business segment | For the year ended 31 December 2017<br>Wastewater treatment<br>*RMB'000* | Water supply<br>*RMB'000* | Others<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|
| Revenue from external customers | **1,037,163** | **68,520** | **118,142** | **1,223,825** |
| Segment gross profit | **446,773** | **4,233** | **49,484** | **500,490** |
| Segment profit/(loss) | **403,171** | **(844)** | **40,990** | **443,317** |
| Finance income | | | | **33,706** |
| Finance costs | | | | **(104,754)** |
| Share of results of associates | | | | **156** |
| Profit before income tax | | | | **372,425** |
| **Other information** | | | | |
| Depreciation of property, plant and equipment | **153,654** | **9,035** | **3,262** | **165,951** |
| Amortisation of land use rights | **9,810** | **–** | **–** | **9,810** |
| Amortisation of intangible assets | **5,880** | **–** | **–** | **5,880** |
| Capital expenditure | **205,626** | **23,691** | **483** | **229,800** |

| Business segment | As at 31 December 2017<br>Wastewater treatment<br>*RMB'000* | Water supply<br>*RMB'000* | Others<br>*RMB'000* | Total<br>*RMB'000* |
|---|---|---|---|---|
| **Segment assets** | **5,605,826** | **352,835** | **17,936** | **5,976,597** |
| **Unallocated:** | | | | |
| Deferred income tax assets | | | | **32,957** |
| Investments in associates | | | | **15,257** |
| Total assets | | | | **6,024,811** |
| **Segment liabilities** | **2,199,632** | **13,608** | **5,284** | **2,218,524** |
| **Unallocated:** | | | | |
| Deferred income tax liabilities | | | | **39,848** |
| Current income tax liabilities | | | | **60,238** |
| **Total liabilities** | | | | **2,318,610** |

## 3 SEGMENT INFORMATION (Continued)

### (b) Segment information (Continued)

The segment information provided to senior executive management for the reportable segments for the year ended 31 December 2016 is as follows:

| | For the year ended 31 December 2016 | | | |
|---|---|---|---|---|
| Business segment | Wastewater treatment | Water supply | Others | Total |
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| Revenue from external customers | 765,906 | 62,366 | 86,653 | 914,925 |
| Segment gross profit | 386,938 | 3,292 | 35,251 | 425,481 |
| Segment profit/(loss) | 355,229 | (468) | 35,860 | 390,621 |
| Finance income | | | | 16,670 |
| Finance costs | | | | (80,299) |
| Share of results of associates | | | | (121) |
| Profit before income tax | | | | 326,871 |
| **OTHER INFORMATION** | | | | |
| Depreciation of property, plant and equipment | 157,011 | 4,642 | 709 | 162,362 |
| Amortisation of land use rights | 8,646 | – | – | 8,646 |
| Amortisation of intangible assets | 3,812 | – | – | 3,812 |
| Capital expenditure | 651,030 | 17,034 | 86 | 668,150 |

| | As at 31 December 2016 | | | |
|---|---|---|---|---|
| Business segment | Wastewater treatment | Water supply | Others | Total |
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| Segment assets | 4,220,160 | 331,504 | 13,029 | 4,564,693 |
| **Unallocated:** | | | | |
| Deferred income tax assets | | | | 23,697 |
| Investments in associates | | | | 15,101 |
| **Total assets** | | | | 4,603,491 |
| **Segment liabilities** | 2,036,766 | 9,494 | 3,932 | 2,050,192 |
| **Unallocated:** | | | | |
| Deferred income tax liabilities | | | | 9,321 |
| Current income tax liabilities | | | | 44,568 |
| **Total liabilities** | | | | 2,104,081 |

## 4 OTHER INCOME

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Government grants: | **80,029** | 75,312 |
| – relating to property plant and equipment | **11,671** | 5,461 |
| – relating to research and development activities | **11,764** | 6,291 |
| – relating to tax refund *(Note (a))* | **56,594** | 63,560 |
| Interest income from cash and cash equivalents | **3,307** | 3,329 |
| Interest income arising from structured deposit | **7,615** | – |
| Others | **2,340** | 3,378 |
| | **93,291** | 82,019 |

(a) Pursuant to Notice on Issuing the Catalogue of Preferential Value-added Tax Policies for Products Made through and Labour Services for Integrated Utilisation of Resources issued by the State Administration of Taxation, companies who sell self-produced products made with integrated utilised resources or provides labour services for integrated utilisation of resources can enjoy the policy of value-added tax ("**VAT**") refund upon collection from 1 July 2015. The wastewater treatment business and the reclaimed water supply business of the Group which fall into the catalogue are qualified to enjoy 70% and 50% tax refund proportions respectively.

## 5 OTHER LOSSES – NET

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Losses on disposal of property, plant and equipment – net | **85** | 3,219 |
| Gains on disposal of land use rights – net | **(964)** | (2,420) |
| Donation expenses | **3,763** | – |
| Others | **1,933** | 473 |
| | **4,817** | 1,272 |

## 6 EXPENSES BY NATURE

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Depreciation of property, plant and equipment | **165,951** | 162,362 |
| Utilities and electricity | **87,555** | 80,779 |
| Employee benefit expenses | **99,420** | 97,546 |
| Costs of wastewater and water distribution services | **49,120** | 54,100 |
| – Material costs | **37,063** | 42,710 |
| – Costs for sludge and water hyacinth treatment | **12,057** | 11,390 |
| Cost of construction services | **289,161** | 74,159 |
| Taxes and levies | **40,035** | 27,796 |
| Transportation costs | **9,001** | 11,326 |
| Repair and maintenance costs | **26,411** | 19,166 |
| Commission charge | **8,289** | 7,692 |
| Amortisation of land use rights | **9,810** | 8,646 |
| Office expenditures | **8,344** | 9,960 |
| Labour costs | **25,581** | 14,617 |
| Professional expenses | **13,548** | 13,337 |
| Materials used in research and development activities | **2,433** | 3,685 |
| Amortisation of intangible assets | **5,880** | 3,812 |
| Auditor's remuneration | **3,580** | 311 |
| Listing expenses | **13,255** | 2,507 |
| Miscellaneous | **11,608** | 13,250 |
| Total cost of sales, selling expenses, administrative expenses and research and development expenses | **868,982** | 605,051 |

## 7 FINANCE EXPENSES – NET

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Finance income:** | | |
| – Interest income charged to related parties | **26,314** | 14,693 |
| – Interest income arising from construction contracts | **7,392** | 1,923 |
| – Others | **–** | 54 |
| | **33,706** | 16,670 |
| **Finance costs:** | | |
| – Interest expenses on unsecured borrowings | **(47,397)** | (45,107) |
| – Interest expenses on corporate bonds | **(30,952)** | (31,360) |
| – Interest expenses on secured borrowings | **(3,811)** | (12,314) |
| – Total interest expenses on borrowings | **(82,160)** | (88,781) |
| – Less: borrowing costs capitalised in property, plant and equipment | **6,615** | 8,544 |
| – Interest expenses – net | **(75,545)** | (80,237) |
| – Exchange losses | **(29,130)** | – |
| – Others | **(79)** | (62) |
| | **(104,754)** | (80,299) |
| Finance costs – net | **(71,048)** | (63,629) |

## 8 INCOME TAX EXPENSE

The amounts of income tax expense charged to the consolidated statement of comprehensive income represent:

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Current income tax | **64,476** | 46,075 |
| Deferred income tax | **(6,140)** | 5,118 |
| Income tax expense | **58,336** | 51,193 |

The Group was not subject to Hong Kong profits tax for the year ended 31 December 2017 as there was no assessable income arising in or derived from Hong Kong (2016: Nil).

## 8 INCOME TAX EXPENSE (Continued)

Under the Law of the PRC on Corporate Income Tax (the "**CIT Law**") and implementation Regulations of the CIT Law, the tax rate of the PRC subsidiaries is 25% from 1 January 2008. The income tax rate of 25% is applicable to all of the Group's PRC subsidiaries for the year ended 31 December 2017, except for certain subsidiaries that enjoy tax exemption or a preferential income tax rate as approved by the tax authorities, which was discussed as follows:

(a) China's west region development policy (the "**West Region Development Policy**") is a preferential tax ruling issued by the State Administration of Taxation for companies whose business fall into the catalogue of encouraged industries and located in west region of China. For the year ended 31 December 2017, the Company and certain subsidiaries qualified for the West Region Development Policy were granted the preferential income tax rate of 15% from 1 January 2011 to 31 December 2020 (2016: 15%).

(b) In addition to the West Region Development Policy, the Company also qualifies as a high-tech enterprise and enjoys a 15% enterprise income tax rate for the year ended 31 December 2017 (2016: 15%).

(c) Certain newly upgraded wastewater treatment facilities meet the criteria provided in the catalogue for public basic infrastructure projects qualified for CIT preferential treatments, and are entitled to three years' exemption from CIT followed by three years of a 50% tax reduction on relevant taxable income derived from such new projects.

(d) Certain subsidiaries use the resources stipulated in the catalogue for comprehensive utilisation of resources project qualified for CIT preferential treatments as its major raw materials and enjoyed 10% deduction of CIT.

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Profit before income tax | **372,425** | 326,871 |
| Tax calculated at the domestic CIT rate applicable | **93,106** | 81,718 |
| Tax effect of: | | |
| Expenses not deductible for tax purpose *(Note (i))* | **870** | 261 |
| Preferential tax rate of the Company and certain subsidiaries *(Note (a) and (b))* | **(35,085)** | (30,653) |
| Income not subject to income tax *(Note (c))* | **(126)** | (156) |
| Share of results of associates | **(23)** | 18 |
| Others | **(406)** | 5 |
| Income tax expense | **58,336** | 51,193 |

(i) Expenses not deductible for tax purpose primarily include expenses without valid invoices, welfare and entertainment expenses exceeding the tax deduction limits under the CIT Law, write-off of inventories and receivables without tax authorities' approval.

## 9 EARNINGS PER SHARE

(a) Basic earnings per share are calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| Profit attributable to equity holders of the Company *(RMB'000)* | **313,077** | 274,993 |
| Weighted average number of ordinary shares in issue *(thousand)* | **947,760** | 720,000 |
| Basic earnings per share *(RMB)* | **0.33** | 0.38 |

(b) The diluted earnings per share are same as the basic earnings per share as there was no dilutive potential share during the year ended 31 December 2017 (2016: same).

## 10 DIVIDENDS

| | | As at 31 December | |
|---|---|---|---|
| | | **2017** | 2016 |
| | | ***RMB'000*** | *RMB'000* |
| (a) | 2016 final dividend of RMB0.1 (2015: Nil) per share *(Note i)* | **102,911** | – |
| (b) | Dividends not recognised at the end of the Reporting Period | | |
| | In addition to the above dividends, the Board have recommended the payment of 2017 final dividend of RMB0.1527 per share (2016 – RMB0.1). The aggregate amount of the above dividend expected to be paid in 2018 out of retained earnings at 31 December 2017 is *(Note 16)* | **157,145** | 102,911 |

(i) As approved by the Board on 25 April 2017, the Company declared a dividend of RMB102,911,100 in respect of the accumulated distributable profit as at 31 December 2016. The declaration of the dividend has been reflected as an appropriation of retained earnings during the year ended 31 December 2017. The dividends were paid out during the year ended 31 December 2017.

## 11 RECEIVABLES UNDER SERVICE CONCESSION ARRANGEMENTS

The Group has entered into certain arrangements with governmental authorities in the PRC under TOT or BOT models in respect of its wastewater treatment and water supply services (the "**Facilities**").These service concession arrangements generally involve the Group as an operator (i) paying a specific amount for those arrangements under TOT models; (ii) constructing the Facilities for those arrangements under BOT models; and (iii) operating and maintaining the Facilities at a specified level of serviceability on behalf of the relevant governmental authorities for the periods from 24.6 to 45.2 years (the "**Service Concession Periods**"), and the Group will be paid for its services over the service concession periods at prices stipulated through a pricing mechanism. The Group is generally entitled to use all the property, plant and equipment of the Facilities, however, the relevant governmental authorities as grantors will control and regulate the scope of service that the Group must provide with the Facilities, and retain the beneficial entitlement to any residual interest in the Facilities at the end of the term of the Service Concession Periods. Each of these service concession arrangements is governed by a contract and, where applicable, supplementary agreements entered into between the Group and the relevant governmental authority in the PRC that set out, inter alia, performance standards, mechanisms for adjusting prices for the services rendered by the Group, specific obligations levied on the Group to restore the Facilities to a specified level of serviceability at the end of the Service Concession Periods and arrangements for arbitrating disputes.

## 11 RECEIVABLES UNDER SERVICE CONCESSION ARRANGEMENTS (Continued)

The consideration paid by the Group for a service concession arrangement is accounted for as an intangible asset (operating concession) or a financial asset (receivable under a service concession arrangement) or a combination of both, as appropriate.

The effective interest rate fell within the range from 6.51% to 9.23%.

The following is the summarised information of the financial asset component (receivable under a service concession arrangement) with the respect to the Group and Company's service concession arrangements.

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Receivables under service concession arrangements** | | |
| Current portion: | **13,747** | 9,679 |
| Non-current portion: | **529,997** | 341,944 |
| | **543,744** | 351,623 |

In respect of the Group and Company's receivables under service concession arrangements, the various group companies have different credit policies, depending on the locations in which they operate. Collection of receivables under service concession arrangements are closely monitored in order to minimise any credit risk associated with the receivables.

The receivables under service arrangements were billable receivables. They were mainly due from governmental authorities in the PRC, as grantors in respect of the Group's service concession arrangements. Based on past experience, the directors of the Company are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances still considered fully recoverable.

The directors of the Company are of the view that, as at 31 December 2017, none of the receivables under service concession arrangements is past due and impaired (31 December 2016: Nil).

## 12 AMOUNTS DUE FROM CUSTOMERS FOR CONSTRUCTION CONTRACTS

Costs incurred to date plus recognised profits less recognised losses:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Current portion of costs incurred to date plus recognised profits less recognised losses:** | | |
| Current portion: | **12,296** | 5,716 |
| Non-current portion: | **238,383** | 35,573 |
| | **250,679** | 41,289 |

## 13 TRADE AND OTHER RECEIVABLES

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Trade receivables *(Note (a))*:** | | |
| – Third parties | **4,852** | 941 |
| – Related parties | **95,467** | 39,678 |
| – Local government | **146,232** | 85,381 |
| **Trade receivables – net** | **246,551** | 126,000 |
| **Other receivables:** | | |
| – Third parties | **5,176** | 6,539 |
| – Hongzetianying Water Treatment Co., Ltd. (洪澤天楹污水處理有限責任公司, "**Hongze Water**") *(Note b)* | **–** | 41,725 |
| – Haian Qutang Water Treatment Co., Ltd. (海安曲塘污水處理有限公司, "**Qutang Water**") *(Note b)* | **–** | 3,744 |
| – Haian Libao Water Treatment Co., Ltd. (海安李堡污水處理有限公司, "**Libao Water**") *(Note b)* | **–** | 2,279 |
| – Related parties | **68,857** | 39,472 |
| – Local government | **55,665** | 51,590 |
| **Other receivables – net** | **129,698** | 145,349 |
| **Prepayments:** | | |
| – Listing expenses | **–** | 28,946 |
| – Others | **10,148** | 6,600 |
| **Prepayments – net** | **10,148** | 35,546 |
| **Trade and other receivables – net** | **386,397** | 306,895 |

As at 31 December 2017, the fair value of the current portion of trade and other receivables of the Group due within one year, except for the prepayments which are not financial assets, approximated their carrying amounts.

As at 31 December 2017, the carrying amounts of trade and other receivables are denominated in RMB.

## 13 TRADE AND OTHER RECEIVABLES (Continued)

(a) Aging analysis of trade receivables at the respective balance sheet dates, based on the invoice dates, are as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| – Within one year | **243,528** | 125,542 |
| – Over one year and within two years | **3,023** | 458 |
| | **246,551** | 126,000 |

Based on the past experiences, the directors believe that no impairment allowance is necessary because the customers are mainly local government authorities in Kunming and related parties and there has not been a significant change in their credit quality. Accordingly, these long-aged balances are considered fully recoverable.

The Group does not hold any collateral as security over these debtors.

(b) RMB41,725,000, RMB3,744,000 and RMB2,279,000 was granted to Hongze Water, Qutang Water and Libao Water respectively and all of the three companies were acquired by the Group in January 2017.

## 14 TRADE AND OTHER PAYABLES

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Trade payables | **3,802** | 2,093 |
| Other payables due to: | **71,899** | 53,176 |
| – Related parties | **18,171** | 20,881 |
| – Local government | **4,416** | – |
| – Third parties | **49,312** | 32,295 |
| Outstanding consideration payable for acquisition of subsidiaries | **12,690** | 18,447 |
| Staff salaries and welfare payables | **28,667** | 28,661 |
| Advance from customers | **6,124** | 12,177 |
| – Related parties | **4,222** | 9,879 |
| – Local government | **101** | – |
| – Third parties | **1,801** | 2,298 |
| Payables on acquisition of property, plant and equipment due to: | **84,297** | 151,957 |
| – Related parties | **32,521** | 29,769 |
| – Third parties | **51,776** | 122,188 |
| Payables on acquisition of land use rights from related parties | **58,194** | 58,194 |
| Interest payables | **2,021** | 1,310 |
| Accrued taxes other than income tax | **102,156** | 96,324 |
| | **369,850** | 422,339 |

## 14 TRADE AND OTHER PAYABLES (Continued)

(a) As at 31 December 2017, all trade and other payables of the Group were non-interest bearing, and their fair values, except for the advance from customers, staff salaries and welfare payables and accrued taxes other than income tax which are not financial liabilities, approximated their carrying amounts due to their short maturities.

(b) For the year ended 31 December 2017, the Group's trade and other payables are denominated in RMB.

(c) Aging analysis of trade payables to third parties at the respective balance sheet dates is as follows:

| | **As at 31 December** | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| – Within one year | **3,471** | 2,093 |
| – Over one year and within two years | **331** | – |
| | **3,802** | 2,093 |

## 15 BUSINESS COMBINATIONS

For the year ended 31 December 2017, the Group acquired equity interests in certain subsidiaries from independent third parties. Details of the acquisitions are as follows:

(i) On 1 January 2017, the Group acquired 100% of the equity interests in Qutang Water at a consideration of RMB5,300,000. After the acquisition, Qutang Water became a directly owned subsidiary of the Company.

Qutang Water's principal activities are wastewater treatment, and were acquired as part of the Group's expansion in the industry. Details of the fair values of assets acquired and liabilities assumed from the acquisition are as follows:

| | **As at 1 January 2017** |
|---|---|
| | *RMB'000* |
| **Consideration:** | |
| Cash consideration | 5,300 |
| **Recognised amounts of identifiable assets acquired and liabilities assumed:** | |
| Cash and cash equivalents | 766 |
| Land use rights | 1,673 |
| Intangible assets | 3,812 |
| Property, plant and equipment | 5,252 |
| Trade and other receivables | 539 |
| Trade and other payables | (5,789) |
| Deferred tax liabilities | (953) |
| **Total identifiable net assets** | 5,300 |

An intangible asset of concession rights of RMB3,812,000 was recognised as at the acquisition date.

Of the revenue included in the consolidated statement of comprehensive income of the Group since the acquisition date to 31 December 2017, Qutang Water accounted for approximately RMB1,517,000. Qutang Water also contributed a net profit of RMB560,000 over the same period.

## 15 BUSINESS COMBINATIONS (Continued)

(ii) On 1 January 2017, the Group acquired 100% of the equity interests in Libao Water at a consideration of RMB6,750,000. After the acquisition, Libao Water became a directly owned subsidiary of the Company.

Libao Water's principal activities are wastewater treatment, and were acquired as part of the Group's expansion in the industry. Details of the fair values of assets acquired and liabilities assumed from the acquisition are as follows:

| | **As at 1 January 2017** *RMB'000* |
|---|---|
| **Consideration:** | |
| Cash consideration | 6,750 |
| **Recognised amounts of identifiable assets acquired and liabilities assumed:** | |
| Cash and cash equivalents | 841 |
| Land use rights | 1,579 |
| Intangible assets | 4,345 |
| Property, plant and equipment | 4,939 |
| Trade and other receivables | 623 |
| Trade and other payables | (4,491) |
| Deferred tax liabilities | (1,086) |
| **Total identifiable net assets** | 6,750 |

An intangible asset of concession rights of RMB4,345,000 was recognised as at the acquisition date.

The revenue included in the consolidated statement of comprehensive income of the Group since the acquisition date to 31 December 2017 contributed by Libao Water was approximately RMB1,505,000, with a net profit of approximately RMB360,000.

## 15 BUSINESS COMBINATIONS (Continued)

(iii) On 1 January 2017, the Group acquired 100% of the equity interests in Hongzetianying Water Treatment Co., Ltd. (洪澤天楹污水處理有限責任公司, "**Hongze Water**") at a consideration of RMB67,900,000. After the acquisition, Hongze Water became a directly owned subsidiary of the Company.

Hongze Water's principal activities are water treatment, and were acquired as part of the Group's expansion in the industry. Details of the fair values of assets acquired and liabilities assumed from the acquisition are as follows:

| | **As at 1 January 2017** *RMB'000* |
|---|---|
| **Consideration:** | |
| Cash consideration | 67,900 |
| **Recognised amounts of identifiable assets acquired and liabilities assumed:** | |
| Cash and cash equivalents | 1,023 |
| Receivables under service concession arrangements | 79,503 |
| Amounts due from customers for construction contracts | 53,428 |
| Land use rights | 3,555 |
| Property, plant and equipment | 163 |
| Trade and other receivables | 5,171 |
| Inventories | 11 |
| Trade and other payables | (63,173) |
| Deferred tax liabilities | (11,781) |
| **Total identifiable net assets** | 67,900 |

The revenue included in the consolidated statement of comprehensive income of the Group since the acquisition date to 31 December 2017 contributed by Hongze Water was approximately RMB14,111,000. Hongze Water also contributed a net profit of approximately RMB9,338,000 over the same period.

## 15 BUSINESS COMBINATIONS (Continued)

(iv) On 1 October 2017, the Group acquired 100% of the equity interests in Liuyang Hongyu Water Treatment Co., Ltd. (瀏陽市宏宇水務有限公司, "**Hongyu Water**") at a consideration of RMB126,900,000. After the acquisition, Hongyu Water became a directly owned subsidiary of the Company.

Hongyu Water's principal activities are wastewater treatment, and were acquired as part of the Group's expansion in the industry. Details of the fair values of assets acquired and liabilities assumed from the acquisition are as follows:

| | **As at 1 October 2017** *RMB'000* |
|---|---|
| **Consideration:** | |
| Cash consideration | 126,900 |
| **Recognised amounts of identifiable assets acquired and liabilities assumed:** | |
| Cash and cash equivalents | 4,451 |
| Land use rights | 17,239 |
| Intangible assets | 54,651 |
| Property, plant and equipment | 62,837 |
| Inventories | 264 |
| Deferred income tax assets | 76 |
| Trade and other receivables | 1,734 |
| Trade and other payables | (689) |
| Deferred tax liabilities | (13,663) |
| **Total identifiable net assets** | 126,900 |

An intangible asset of concession rights of RMB54,651,000 was recognised as at the acquisition date.

The revenue included in the consolidated statement of comprehensive income of the Group since the acquisition date to 31 December 2017 contributed by Hongyu Water was approximately RMB1,785,000, with a net loss of approximately RMB307,000.

Had Hongyu Water been consolidated from 1 January 2017, the annualized consolidated revenue of the Group would be increased by approximately RMB5,179,000 and the net profit of the Group would be decreased by RMB228,000.

(v) The following table summarised the cash flows and relevant costs from the acquisitions for the year ended 31 December 2017:

| | **As at 31 December 2017** *RMB'000* |
|---|---|
| Total cash consideration | 206,850 |
| Less: Change in consideration payable for purchase of subsidiaries | 5,757 |
| Cash and cash equivalents in the subsidiaries acquired | (7,081) |
| Change in prepayment (a) | (36,594) |
| **Cash outflows from the acquisitions of subsidiaries** | 168,932 |

## 16 EVENTS AFTER THE BALANCE SHEET DATE

### (a) Acquisition of subsidiaries

The quality testing of the wastewater treatment facilities of Kunming No. 10 Water Purification Plant was completed in January 2018 and the final consideration was RMB572,323,000. All the relevant facilities were transferred to the Company in January 2018.

Pursuant to the Board resolution of the Company dated 20 September 2017, the Group plans to acquire sewage treatment businesses including 100% equity interest in Leshan Debeiao Water Limited (樂山德貝奧水務有限公司, "**Debeiao Water**") directly or indirectly owned by Zou Hanping, Sichuan Debeiao Environmental Technology Industrial Co., Ltd. (四川德貝奧環保科技實業有限公司), and Sichuan Weilai Luzhou Municipal Public Engineering Co., Ltd. (四川未來綠洲市政公用工程有限公司). The acquisition was completed in January 2018 with a consideration of RMB80,230,000.

Pursuant to the Board resolution of the Company dated 19 December 2017, the Group plans to purchase sewage treatment businesses including 100% equity interest in Zhuji Dongda Ciwu Sewage Treatment Co., Ltd. (諸暨市東大次塢污水處理有限公司, "**Dongda Ciwu Sewage Treatment**") directly owned by Dongda Water Industry Group Co., Ltd. (東大水業集團有限公司) and Zhuji City Urban Public Transport Co., Ltd. (諸暨市長運城鄉公交有限公司). The acquisition was completed in January 2018 with a consideration of RMB85,326,000.

### (b) Dividend

As approved by the Board on 26 March 2018, the Group intends to distribute to all shareholders annual cash dividend of RMB0.1527 per share, amounting to RMB157,145,000 in total. The proposal is subject to the Annual General Meeting for approval.

### (c) Providing entrusted loan to Kunming Industrial Development and Construction Co., Ltd. 昆明產業開發投資有限責任公司, ("KIDC")

On 16 March 2018, the Company entered into a entrusted loan agreement with KIDC and Bank of Communications under which the Company entrusted Bank of Communications to provide a 9-month entrusted loan of RMB300 million to KIDC with annual interest of 7%.

## II. MANAGEMENT DISCUSSION AND ANALYSIS

## A. INDUSTRY OVERVIEW

The industry chain of China's municipal water industry primarily consists of three key components: production and supply of running water from qualified raw water sources, treatment of municipal wastewater collected through municipal pipelines and further treatment of wastewater for reuse. Our core business segments include municipal wastewater treatment, reclaimed water supply and running water supply.

### *1. Overview of Wastewater Treatment Industry*

The PRC government introduced the "13th Five-Year" National Urban Wastewater Treatment and Recycling Facilities Construction Plan (《「十三五」全國城鎮污水處理及再生水利用設施建設規劃》) which deemed wastewater treatment as an important part for the improvement of urban water ecology and environment and required that urban wastewater treatment facilities achieve full coverage by the end of 2020 with a possible capacity of 66.3 billion cubic metres, and wastewater treatment capacity expected to increase from 168.4 million $m^3$ per day to 218.0 million $m^3$ per day. In 2017, the Chinese government issued the Instructions for the Promotion of Public-Private Partnership ("**PPP**") in Water Pollution Prevention Field (《關於推進水污染防治領域政府和社會資本合作的實施意見》), requiring wastewater treatment projects in which the government participates to fully implement the PPP model. In 2017, the Communist Party of China (CPC) held the 19th National Congress of the Communist Party of China, the report of which put forward that ecological culture construction is a strategy that affects the Chinese people for a millennium to come and that we must uphold and practise the philosophy of "Lucid waters and lush mountains are invaluable assets", and for the first time included "Being beautiful" in the objectives to build a strong country. With the Chinese government's various investments and policies, the comprehensive wastewater treatment business will obtain continuous benefits, and will gradually shift its focus to comprehensive treatment of water environment and the improvement of usage rate of reclaimed water, drawing from the important favorable policy for the long-term growth of the environmental protection industry.

The prospect of the macro-economy in Yunnan Province poses potential threat to the demand for wastewater treatment because the overall economy in Yunnan Province directly impacts on the level of business activities and thus further impacts on the volume of wastewater discharge. Changes in government policies and their level of implementation are of equal importance to the prospects of the industry, as a supportive governmental policy is a key driver of the increase in wastewater treatment business in Yunnan Province.

### *2. Overview of Reclaimed Water Industry*

Looking forward, the capacity of reclaimed water is expected to grow at a CAGR of 10.4% between 2015 and 2020. By 2020, the total production capacity of reclaimed water in China is estimated to reach 41.6 million $m^3$ per day. Due to strong supports from the government of Yunnan Province for the development of the reclaimed water industry, the total production capacity of reclaimed water in Yunnan Province, the PRC is expected to reach 272,000 $m^3$ per day in 2020, representing a substantial increase.

### *3. Overview of Municipal Water Supply Industry*

Due to continuous urbanization and construction of water supply facilities in county-level regions, the national municipal running water supply capacity is expected to keep growing at a rate of 1.3% in the five coming years, reaching 368.0 million $m^3$ per day by 2020. In Yunnan Province, the PRC, the municipal running water supply capacity grows continuously. The relocation of manufacturing industry to China's western provinces and the accelerated urbanization in these regions are expected to boost the growth of urban population and Gross Domestic Product (GDP), which in turn will increase the demand for municipal running water supply. The government highly values the development of running water supply in western China.

Driven by the state policies, the water treatment services industry is expected to see huge market opportunities and potential in the future. Wastewater treatment, reclaimed water and water supply industry will benefit from the rapidly accelerating urbanization in China and the Chinese government's policy supporting the environmental protection industry. The Board expects that the level of development, scale and growth of such industries will be further promoted and investors in capital markets will also gradually pay more attention to the environmental protection industry.

### *4. Comprehensive Treatment of Water Environment Will Obtain Continuous Benefits*

The PRC government introduced the "13th Five-Year" National Urban Wastewater Treatment and Recycling Facilities Construction Plan (《「十三五」全國城鎮污水處理及再生水利用設施建設規劃》) which deemed wastewater treatment as an important part for the improvement of urban water ecology and environment and required that urban wastewater treatment facilities achieve full coverage by the end of 2020, with cities at prefecture-city level and above achieving comprehensive sewage collection and processing; county seats no less than 85% whereas those in the east aimed for 90%; and established towns achieving 70% whereas those in central and western regions of China aimed for 50%, the wastewater treatment capacity for urban areas shall increase to 268 million $m^3$ per day. During the 13th Five-year Plan period, it is to further coordinate the planning and reasonable layout, and to make greater contribution, for purposes of changing the mode of the construction of urban wastewater treatment facilities from "scaled growth" to "quality and efficiency enhancement" and from "water-primary and sludge-secondary" to "focusing on both sludge and water treatment", and from "water treatment" to "water reclaiming and recycling". As a result thereof, the safeguarding capability and service level of the PRC urban wastewater treatment facilities will be enhanced and upgraded completely. Further, with the issuance of a series of plans during the "13th Five Year" period relating to water treatment, the wastewater treatment industry, processing-only, is gradually shifting towards comprehensive treatment of water environment and enhancement of usage rate of reclaimed water.

### 5. *PPP Model Becomes a Mainstream*

PPP model refers to a model under which private capitals undertake the designing, construction, operation and maintenance of infrastructure projects in pursuit of reasonable investment returns, and the government departments are responsible for pricing and quality regulation in respect of infrastructures and public services with the aim of maximizing public interests. According to Chinese government's Notice on Effectively Implementing Works Relating to the Public-Private Partnership in Traditional Infrastructure Field (《關於切實做好傳統基礎設施領域政府和社會資本合作有關工作的通知》), wastewater and waste treatment was identified as a major municipal construction area in traditional infrastructure field, and as key project in promotion of PPP model. In October 2016, the Notice on Promoting Public-Private Partnership (PPP) in Public Services Field (《關於在公共服務領域深入推進政府和社會資本合作的通知》) required that PPP model shall be adopted compulsorily in newly-constructed projects in waste treatment, wastewater treatment and other public services areas. In July 2017, the Instructions for the Promotion of Public-Private Partnership ("**PPP**") in Water Pollution Prevention Field required that PPP model shall be fully implemented in wastewater and treatment projects with government participation. Guided by the above policies, PPP model is gradually becoming a major cooperation model highly advocated in the environmental protection market.

## B. DEVELOPMENT STRATEGY AND PROSPECTS

As indicated by the Chinese government's identification of the pollution prevention and treatment as one of the three critical battles for China, the Chinese economy shifted to a stage of quality-oriented development from a stage of rapid growth, which presents great opportunities for the environmental protection industry. Supported by such favorable policies, the environmental protection industry is expected to become increasingly important to China's economic development under the "New Normal".

We are a leading municipal wastewater treatment and reclaimed water supply services provider in Yunnan Province, the PRC. We are the largest municipal wastewater treatment company in Yunnan Province, the PRC, and one of the major enterprises implementing the PRC's strategic goal to treat pollutants at Dianchi Lake. We enjoy exclusive rights to provide wastewater treatment services in Kunming and certain other areas of China. Our concessions help us maintain and consolidate our advantages and competitive positions in Yunnan Province, and lay a favourable foundation for our consolidation of water treatment resources near Yunnan Province, and exploration into neighboring regions to achieve cross-region operation.

During the Reporting Period, we expanded into the upstream and downstream sectors of the water treatment industry, seized industrial opportunities and endeavoured to expand market to acquire equities in multiple urban wastewater treatment plants and industrial wastewater treatment plants in Sichuan Province, Hunan Province and other places. In the wake of these acquisitions, our business activities spanned Yunnan, Guizhou, Sichuan, Jiangsu, Zhejiang, Anhui and Hunan. We proactively entered into cooperation framework agreements or other agreements with the Tourist Resort (度假區), Xishan District (西山區), Yiliang County (宜良縣), Shilin County (石林縣) and Xundian County (尋甸縣) of Kunming, to vigorously promote the comprehensive treatment of water environment, ecological environmental construction and development of environmental protection industry, and expand our share in the environmental protection market. On the back of the cumulative advantages of Yunnan and Hong Kong's resources relating to the "One Belt One Road" scheme, we actively explored cooperation with state and local governments in South Asia and Southeast Asia, and continuously sought new profit growth opportunities.

In addition, we proactively engaged in waste treatment, sludge recycling and other solid waste treatment businesses. We also expanded into clean energy business and cooperated with other parties in scientific researches and project incubation. These moves are aimed to enhance the Group's abilities to make profits sustainably.

We adhered to the strategy of "Focusing on one business and diversifying into other businesses". On the one hand, we consistently improved the Group's operation, technologies and project management capabilities, so as to further improve operational efficiency and realize sustainable development. On the other hand, we actively explored global markets to become a knowledge-intensive and technology-intensive high-tech environmental protection company.

The Group aims to become a leading integrated water and environmental protection services provider in the PRC. Thus, we intend to seize the development opportunities that will arise from the "One Belt One Road" scheme to build a more ecological Yunnan and China, strengthen our core business of wastewater treatment and running water and reclaimed water supply, expand our geographic coverage and extend our services.

2017 was the first year that the H Shares of the Company were listed on The Stock Exchange of Hong Kong Limited. The successful listing of H Shares not only strengthened the shareholder base of the Group, but also further enhanced the Group's financing capability and increased its brand awareness and reputation. During the Reporting Period, the Group continued to steadily develop its various business segments. With the support of relevant favorable environmental policies and growing market demands in the PRC and Southeast Asia, the Group continued to expand its geographical coverage of services, in addition to consolidating and expanding the achievements gained in its existing water business.

## C. BUSINESS REVIEW

The Group principally adopts the TOO, TOT and BOT project models, with a focus on the TOO model. For the year ended 31 December 2017, our TOO projects contributed 61.1% of our total revenue. Our TOT projects contributed 3.8% of our total revenue and our BOT projects contributed 10.2% of our total revenue. We also adopt the BT project model for some of our projects.

For the TOO and TOT models, we acquire concessions to operate existing facilities at agreed prices from the relevant local governments. For the BOT model, we finance, construct and operate our own facilities. After the expiration of the relevant concessions, we either obtained new concessions from or transferred the relevant facilities back to the relevant local governments, depending on project types. As of 31 December 2017, we had a total of 42 plants (35 wastewater treatment plants, 6 running water plants and 1 industrial water supply plant) under concession agreements, of which 37 plants were in operation, 4 plants were under construction and 1 plant was under development. Among the 37 plants in operation, 14 were TOO projects, 19 were TOT projects, 2 were BOT projects and 2 were BOO projects.

During the Reporting Period, the utilization rate of our facilities was above the industry average and the volume of wastewater treated was maintained at a high level. For the year ended 31 December 2017, the total volume of wastewater treated was 550.9 million $m^3$ with an average facility utilization rate of 93.9%, representing a growth of approximately 1.2% from 92.8% for the year ended 31 December 2016.

***Wastewater Treatment Projects***

As of 31 December 2017, we had a total of 32 wastewater treatment plants in operation (including 14 in Kunming and 18 in other areas of China), with a total wastewater treatment capacity of 1.8 million $m^3$ per day. We also had 3 wastewater treatment plants under construction in Yunnan Province, the PRC and in Laos, respectively. Additionally, our management services facilities had total designed wastewater treatment capacity of 0.4 million $m^3$ per day. With our technologically advanced facilities, independently developed patents and strong management skills, we were able to maintain low costs while providing high quality wastewater treatment services. As of 31 December 2017, 92.54% of our designed wastewater treatment capacity reached the National Class I Category A discharge standard.

***Reclaimed Water Business***

For our reclaimed water business, as of 31 December 2017, we had 7 of our wastewater treatment plants producing reclaimed water, with a total designed daily production capacity of 52,000 $m^3$, representing a growth of approximately 18.2% compared with that as of 31 December 2016. Customers of our reclaimed water include commercial and industrial establishments, enterprises and public institutions in Kunming. The production of our reclaimed water supply business has increased year by year from 2015 to 2017. During the Reporting Period, our reclaimed water supply increased 17.7% year on year to 6,882,777 $m^3$. We expect this growth momentum to continue as we expand our reclaimed water business.

***Running Water Business***

For our running water business, as of 31 December 2017, we had 4 running water plants in operation in Yunnan Province, the PRC, and 2 running water plants under construction, with 1 in Yunnan Province, the PRC and 1 in Laos.

Our project in Laos marks our first step expanding into the Southeast Asian market. As a leading company in water and environmental protection industry, we will make full use of our rich experiences in water resources development and water environment quality, so as to participate in the Chinese government's "One Belt One Road" scheme, and build advantages in overseas expansion based on Yunnan Province' geographical advantage arising from its being the intersection for "One Belt One Road".

## D. FINANCIAL REVIEW

### *1. Consolidated Results of Operations*

Our revenue increased by RMB308.9 million, or 33.8%, to RMB1,223.8 million for the year ended 31 December 2017, from RMB914.9 million for the year ended 31 December 2016. Our gross profits were RMB425.5 million and RMB500.5 million for 2016 and 2017, respectively. For 2016 and 2017, the revenue from the service of wastewater treatment respectively accounted for 83.7% and 84.7% of the total revenue; the revenue from reclaimed water, running water supply and management services accounted for most of other revenue for the same period.

The following discussion addresses the principal trends that have affected our results of operations during the Reporting Period. The following table sets out our consolidated results of operations for the periods indicated:

| | For the year ended 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Revenue** | **1,223,825** | 914,925 |
| Cost of sales | **(723,335)** | (489,444) |
| **Gross profit** | **500,490** | 425,481 |
| Selling expenses | **(13,875)** | (10,605) |
| Administrative expenses | **(124,490)** | (97,604) |
| Research and development expenses | **(7,282)** | (7,398) |
| Other income | **93,291** | 82,019 |
| Other losses – net | **(4,817)** | (1,272) |
| **Operating profit** | **443,317** | 390,621 |
| Finance income | **33,706** | 16,670 |
| Finance costs | **(104,754)** | (80,299) |
| Finance costs – net | **(71,048)** | (63,629) |
| Share of results of associates | **156** | (121) |
| **Profit before income tax** | **372,425** | 326,871 |
| Income tax expense | **(58,336)** | (51,193) |
| **Net profit** | **314,089** | 275,678 |
| Other comprehensive income | **(1,847)** | – |
| **Total comprehensive income** | **312,242** | 275,678 |

*a. Revenue*

Our revenue increased by RMB308.9 million, or 33.8%, to RMB1,223.8 million for the year ended 31 December 2017 from RMB914.9 million for the year ended 31 December 2016, primarily due to:

- revenue from our wastewater treatment segment increased by RMB271.3 million, or 35.4%, to RMB1,037.2 million for the year ended 31 December 2017 from RMB765.9 million for the year ended 31 December 2016, primarily due to BT construction revenue of RMB158.8 million recognized for the period based on percentage-of-completion of the newly signed BT project in Haitou Village, Qingshuihai, Xundian County (尋甸縣清水海海頭村), BOT construction revenue of RMB30.1 million recognized for the period based on percentage-of-completion of the newly signed BOT project of wastewater treatment plant and auxiliary projects in Yiliang Industrial Park (宜良工業園區), an increase of RMB16.2 million in BOT construction revenue attributable to the consolidation of Shuangjiang Dianchi Water Treatment Co., Ltd. into the Group from October 2016, an increase of RMB25.8 million in BOT construction revenue during the year attributable to the consolidation of Dian Chi Water Treatment (LAOS) Sole Co., Ltd into the Group from August 2016, as well as an increase of approximately RMB20.0 million in our water plant factory revenue attributable to growth in water treatment volume.

- The revenue from our other water-related services segment increased by RMB6.1 million, or 9.9%, to RMB68.5 million for the year ended 31 December 2017, from RMB62.4 million for the year ended 31 December 2016, primarily due to the higher water supply volume in running water plants.

- The revenue from our other segments increased by RMB31.4 million, or 36.3%, to RMB118.1 million for the year ended 31 December 2017, from RMB86.7 million for the year ended 31 December 2016, primarily due to an increase of RMB7.6 million in entrusted management services fees attributable to the management of Haikou Water Purification Plant, Baiyukou Water Purification Plant, Baiyuhe Water Purification Plant and Luolonghe Water Purification Plant on behalf of our controlling shareholder since 1 August 2016, revenue contribution of RMB13.0 million from entrusted management services fees for management of wastewater treatment facilities in the towns and villages in Dianchi Watershed and Niulanjiang Water Replenishment District (Kunming Section) on behalf of Kunming Municipal Dianchi Administration Bureau from 1 January 2017, and an increase of RMB3.5 million in revenue from providing pipeline construction service to Yunnan Reclaimed Water Engineering Co., Ltd in 2017.

*b.* *Cost of sales*

Our cost of sales increased by RMB233.9 million, or 47.8%, to RMB723.3 million for the year ended 31 December 2017, from RMB489.4 million for the year ended 31 December 2016, primarily due to higher construction costs in wastewater treatment segment during the year. Details are as follows:

- Our cost of sales for the wastewater treatment segment increased by RMB211.4 million, or 55.8%, to RMB590.4 million for the year ended 31 December 2017, from RMB379.0 million for the year ended 31 December 2016, primarily due to RMB158.8 million BT construction costs arising from the newly signed project in Haitou Village, Qingshuihai, Xundian County based on construction progress, and RMB30.1 million BOT construction costs arising from the newly signed BOT project of wastewater treatment plant and auxiliary projects in Yiliang Industrial Park based on construction progress.

- Our cost of sales for other water-related services segment increased by RMB5.2 million, or 8.8%, to RMB64.3 million for the year ended 31 December 2017, from RMB59.0 million for the year ended 31 December 2016, primarily due to increase in materials, labor and other costs relating to our running water supply business.

- Our cost of sales for other segments increased by RMB17.3 million, or 33.6%, to RMB68.7 million for the year ended 31 December 2017, from RMB51.4 million for the year ended 31 December 2016, primarily due to more entrusted management services and expanding scope of services provided by us, with relevant materials and labor costs increasing by around RMB6.6 million, and an increase of RMB4.7 million in consolidated costs for 2017 attributable to consolidation of Kunming He'ertai Environmental Industry and Trade Co., Ltd. into the Group from May 2016.

*c.* *Gross margin*

Our gross profit increased by RMB75.0 million, or 17.6%, to RMB500.5 million for the year ended 31 December 2017, from RMB425.5 million for the year ended 31 December 2016, primarily due to an increase of RMB59.8 million in profit from our wastewater treatment segment, an increase of RMB1.0 million in profit from our other water-related service segment, and an increase of RMB14.2 million in profit from our other segments.

- Our gross profit margin decreased by 5.6% to 40.9% for the year ended 31 December 2017 from 46.5% for the year ended 31 December 2016, primarily due to the decrease in gross profit margin of wastewater treatment affected by the gross profit margin of construction, partially offset by an increase in gross profit margin of other water-related service segment and other segments.

- Our gross profit for the wastewater treatment segment increased by RMB59.9 million, or 15.5%, to RMB446.8 million for the year ended 31 December 2017, from RMB386.9 million for the year ended 31 December 2016. Our segment gross margin decreased by 7.6% to 43.1% for the year ended 31 December 2017 from 50.7% for the year ended 31 December 2016, primarily due to impacts from the newly-signed domestic wastewater treatment project in Qingshuihai Water Conservation District in Xundian County and project of wastewater treatment plant and auxiliary projects in Yiliang Industrial Park, which are still under construction and have incurred relatively high costs and generated low gross profit amid the construction process.

- Our gross profit for other water-related services segment increased by RMB1.0 million, or 28.6%, to RMB4.3 million for the year ended 31 December 2017, from RMB3.3 million for the year ended 31 December 2016. Our segment gross margin increased by 0.9% to 6.2% for the year ended 31 December 2017 from 5.3% for the year ended 31 December 2016, primarily due to higher revenue from the running water supply and lower proportion of the construction revenue that yielded relatively low gross profit.

- Our gross profit for other segments increased by RMB14.2 million, or 40.4%, to RMB49.5 million for the year ended 31 December 2017, from RMB35.3 million for the year ended 31 December 2016. Our segment gross margin increased by 1.2% to 41.9% for the year ended 31 December 2017 from 40.7% for the year ended 31 December 2016. The gross profit margin remained substantially the same.

d. *Selling expenses*

Our selling expenses increased by RMB3.3 million, or 30.8%, to RMB13.9 million for the year ended 31 December 2017, from RMB10.6 million for the year ended 31 December 2016, primarily as a result of an increase of RMB0.5 million in wages of sales staff due to the increase in employees' average wages and bonuses for 2017, and RMB1.2 million of one-off payment made to running water suppliers (collecting wastewater treatment tariffs from end users for us) for system upgrading (for upgrading suppliers' tariff collection system and supporting its tariff collection services).

e. *Administrative expenses*

Our administrative expenses increased by RMB26.9 million, or 27.5%, to RMB124.5 million for the year ended 31 December 2017, from RMB97.6 million for the year ended 31 December 2016, primarily due to an increase of RMB10.8 million in listing expense, an increase of RMB12.2 million in land use tax, property tax and other taxes attributable to the consolidation of Qutang Water, Libao Water, Hongze Water and Hongyu Water and other companies into the Group, an increase of RMB3.2 million in audit fee and increases in professional service expenses, employee benefit expenses and office expenditures associated with our acquisition activities.

*f.* *Research and development expenses*

Our research and development expenses decreased by RMB0.1 million, or 1.6%, to RMB7.3 million for the year ended 31 December 2017, from RMB7.4 million for the year ended 31 December 2016. The research and development expenses remained substantially the same for both years.

*g.* *Other income*

Our other income increased by RMB11.3 million, or 13.7%, to RMB93.3 million for the year ended 31 December 2017, from RMB82.0 million for the year ended 31 December 2016, primarily due to an investment income of RMB7.6 million from the structured deposits acquired this year and an increase of RMB5.5 million in government grants we received relating to our R&D activities.

*h.* *Other losses*

Our other losses increased by RMB3.5 million, or 279.0%, to RMB4.8 million for the year ended 31 December 2017, from RMB1.3 million for the year ended 31 December 2016, primarily due to a donation of RMB3.8 million made this year.

*i.* *Operating profit*

As a result of the foregoing factors, our operating profit increased by RMB52.7 million, or 13.5%, to RMB443.3 million for the year ended 31 December 2017, from RMB390.6 million for the year ended 31 December 2016. Our operating margins for the year ended 31 December 2017 and 2016 were 36.2% and 42.7%, respectively.

*j.* *Finance income*

Our finance income increased by RMB17.0 million, or 102.2%, to RMB33.7 million for the year ended 31 December 2017, from RMB16.7 million for the year ended 31 December 2016, primarily due to an increase of RMB14.0 million in occupation fee for provision funds.

*k.* *Finance costs*

Our finance costs increased by RMB24.5 million, or 30.5%, to RMB104.8 million for the year ended 31 December 2017, from RMB80.3 million for the year ended 31 December 2016, primarily due to a foreign exchange loss of RMB29.1 million on HKD bank deposits of the proceeds from the listing of our shares.

*l.* *Profit before income tax*

As a result of the foregoing factors, our profit before income tax increased by RMB45.5 million, or 13.9%, to RMB372.4 million for the year ended 31 December 2017 from RMB326.9 million for the year ended 31 December 2016.

*m.* *Income tax*

We incurred income tax expenses of RMB58.3 million for the year ended 31 December 2017 and RMB51.2 million for the year ended 31 December 2016 respectively at effective tax rates of 15.7% and 15.7%, respectively. Our effective tax rates remained substantially the same as last year. Our effective tax rates were slightly higher than 15% due to the expiration of preferential tax treatments of some of our wastewater treatment facilities and our acquisition of subsidiaries which did not qualify for the 15%-preferential enterprise income tax rate of the "Developing Western China Policy" and were subject to the full enterprise income tax rate of 25%.

*n.* *Total comprehensive income*

As a result of the foregoing factors, our total comprehensive income increased by RMB36.5 million, or 13.3%, to RMB312.2 million for the year ended 31 December 2017 from RMB275.7 million for the year ended 31 December 2016.

## ***2. Liquidity and Capital Resources***

Our primary uses of cash are for investing in, constructing, operating and maintaining our wastewater treatment and water supply facilities. To date, we have funded our investments and operations principally with bank loans, cash generated from our operations, equity contributions and issuance of debt instruments.

The following table sets out our cash flows for the periods indicated:

| | **For the year ended 31 December** | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Net cash generated from operating activities | **104,651** | 56,649 |
| Net cash used in investing activities | **(307,700)** | (238,304) |
| Net cash generate form/(used in) financing activities | **1,078,366** | (459,048) |
| Net increase/(decrease) in cash and cash equivalents | **875,317** | (640,703) |
| Effect of foreign exchange rates | **(30,977)** | – |
| Cash and cash equivalents at beginning of the year | **446,830** | 1,087,533 |
| Cash and cash equivalents at end of the year | **1,291,170** | 446,830 |

*a. Net cash generated from operating activities*

Our net cash generated from operating activities primarily consists of cash received from our clients for services provided by us. We also use cash in our operations for the purchase of raw materials and other inventories, payments to suppliers and subcontractors, payments of expenses such as salaries and benefits, and payments of interest and income tax.

For the year ended 31 December 2017, our net cash generated from operating activities was RMB104.7 million and was more than our net cash generated from operating activities for the year ended 31 December 2016 of RMB56.6 million, primarily comprising cash generated from operations amounting to RMB220.7 million, partially offset by the income tax paid amounting to RMB48.8 million and interest paid amounting to RMB67.2 million. The increase is primarily attributable to the increase of RMB38.4 million in net profit.

*b. Net cash used in investing activities*

Our net cash used in investing activities has principally been used to purchase property, plant and equipment and equity interests in subsidiaries and associates.

Our net cash used in investing activities increased to RMB307.7 million for the year ended 31 December 2017 from RMB238.3 million for the year ended 31 December 2016, primarily comprising the purchase of property, plant and equipment amounting to RMB134.4 million and the acquisition of subsidiaries amounting to RMB168.9 million. The net cash used in investing activities during the year increased by RMB69.4 million compared with the previous year, primarily due to an increase of RMB69.3 million in net cash paid for acquisition of subsidiaries compared with the previous year. The cash paid for acquisition of subsidiaries during the year included RMB114.2 million paid for acquiring Hongyu Water, RMB32.0 million prepayment made for acquiring Debeiao Water, and RMB11.3 million repayment made for acquiring Dongda Ciwu Sewage Treatment.

*c. Net cash used in/generated from financing activities*

Our net cash generated from financing activities primarily represents proceeds raised through listing and borrowings.

For the year ended 31 December 2016, our net cash generated from financing activities was RMB459.0 million (net outflow) and was changed to RMB1,078.4 million (net inflow) for the year ended 31 December 2017, primarily comprising the cash proceeds from the listing of RMB1,072.3 million and the proceeds from borrowings of RMB1,050 million, partially offset by repayments of borrowings amounting to RMB887.7 million. The difference between net cash generated from financing activities for this year and previous year was primarily attributable to the increase of RMB670.0 million in borrowings and cash inflow of RMB1,072.3 million from the listing of shares this year.

### *3. Working Capital*

The table below presents our current assets and current liabilities as at the dates indicated:

| | As of 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Current assets** | | |
| Receivables under service concession arrangements | **13,747** | 9,679 |
| Inventories | **7,515** | 10,336 |
| Amount due from customers for construction contracts | **12,296** | 5,716 |
| Available-for-sale financial assets | **80,000** | – |
| Trade and other receivables | **386,397** | 306,895 |
| Cash and cash equivalents | **1,291,170** | 446,830 |
| **Total current assets** | **1,791,125** | 779,456 |
| **Current liabilities** | | |
| Trade and other payables | **369,850** | 422,339 |
| Current income tax liabilities | **60,238** | 44,568 |
| Borrowings | **599,570** | 778,737 |
| **Total current liabilities** | **1,029,658** | 1,245,644 |
| **Net current assets/(liabilities)** | **761,467** | (466,188) |

We recorded net current assets of RMB761.5 million as of 31 December 2017 and net current liabilities of RMB466.2 million as of 31 December 2016, respectively. The increase in our net current assets was mainly attributable to the proceeds from the listing of shares in 2017.

*a. Receivables under service concession arrangements*

We accrue receivables under service concession arrangements throughout a concession period. Our receivables under service concession arrangements refer to the outstanding receivables arising from our construction services (for BOT projects) or acquisition considerations (for TOT projects), adjusted by operation services and finance income after deducting payments accrued throughout a concession period. Under our BOT and TOT agreements, the amount of receivables under service concession arrangements will be settled by tariff payments to be received during the operation phases of our BOT and TOT projects. The portion of the receivables under service concession arrangements due within twelve months from a particular balance sheet date are classified as current assets as at that balance sheet date and the remainder is classified as non-current assets.

Our receivables under service concession arrangements that were classified as current assets amounted to RMB13.7 million as of 31 December 2017. This represented a year-on-year increase of 42.0% between 2016 and 2017, primarily due to an increase in the number of service concession projects we undertook.

Our receivables under service concession arrangements that were classified as non-current assets amounted to RMB530.0 million as of 31 December 2017. This represented a year-on-year increase of 55.0% from 2016 to 2017, primarily due to receivables of RMB79.5 million recognized under concession agreement acquired from the consolidation of Hongze Water into our financial results on 1 January 2017, as well as receivables of RMB30.1 million recognized based on percentage-of-completion of the newly-signed BOT project of wastewater treatment plant and auxiliary projects in Yiliang Industrial Park. Trade receivables of RMB14.0 million were recognized based on percentage-of-completion of the newly-signed domestic wastewater treatment project in Qingshuihai Water Conservation District. Receivables of RMB16.2 million were recognized based on percentage-of-completion due to the consolidation of Shuangjiang Dianchi Water Treatment Co., Ltd. into our financial results from October 2016. Receivables of RMB25.8 million for BOT construction revenue were recognized based on percentage-of-completion due to the consolidation of Dian Chi Water Treatment (LAOS) Sole Co., Ltd. into our financial results from August 2016.

*b.* *Inventories*

Our total inventory balance decreased by RMB2.8 million, or 27.3%, to RMB7.5 million as of 31 December 2017 from RMB10.3 million as of 31 December 2016. Such a decrease reflected a decrease in materials for wastewater treatment and water supply services by RMB1.9 million, or 44.5%, to RMB2.4 million as of 31 December 2017 from RMB4.2 million as of 31 December 2016 and a decrease in spare parts by RMB0.9 million, or 15.3%, to RMB5.2 million as of 31 December 2017 from RMB6.1 million as of 31 December 2016.

For the years ended 31 December 2016 and 2017, our inventory turnover days were 6.3 days and 4.5 days respectively (calculated as the average inventories for the relevant period divided by the cost of sales recognized as cost of sales for the relevant period, multiplied by 365 days. The arithmetic mean of the opening and closing balances of inventories is used for the years ended 31 December 2016 and 2017). The inventory turnover days for 2017 remained stable.

*c.* *Amounts due from customers for construction contracts*

The portion of amounts due from customers for construction contracts due within twelve months from a particular balance sheet date are classified as current assets as at that balance sheet date and the remainder is classified as non-current assets. Our total amounts due from customers for construction contracts increased by RMB209.4 million, or 507.1%, to RMB250.7 million as of 31 December 2017 from RMB41.3 million as of 31 December 2016, primarily due to the amount due from customers of RMB160.0 million recognized based on percentage-of-completion of the newly signed project in Haitou Estate, Qingshuihai, Xundian County, and the amount due from customers for construction contracts of RMB53.4 million acquired from the consolidation of Hongze Water into our financial results on 1 January 2017.

*d. Trade and other receivables*

Our trade and other receivables primarily consist of (i) trade receivables from third parties, related parties and local governments; (ii) other receivables from third parties, related parties and local governments; and (iii) prepayments. Our trade receivables are amounts due from customers for services provided in the ordinary course of business, including services performed for TOO and TOT projects and performed during the operation period of BOT projects. Our other receivables primarily consist of loans granted to and interest receivable from related parties, and VAT refund yet to be received. Our prepayments primarily consist of prepaid electricity and listing expenses related to the global offering of shares.

The following table shows the breakdown of our consolidated trade and other receivables as of the dates indicated:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Trade receivables** | | |
| – Third parties | **4,852** | 941 |
| – Related parties | **95,467** | 39,678 |
| – Local government | **146,232** | 85,381 |
| **Trade receivables – net** | **246,551** | 126,000 |
| **Other receivables:** | | |
| – Third parties | **5,176** | 6,539 |
| – Related parties | **68,857** | 39,472 |
| – Hongze Water | **–** | 41,725 |
| – Qutang Water | **–** | 3,744 |
| – Libao Water | **–** | 2,279 |
| – Local government | **55,665** | 51,590 |
| **Other receivables – net** | **129,698** | 145,349 |
| **Prepayments:** | | |
| – Listing expenses | **–** | 28,946 |
| – Others | **10,148** | 6,600 |
| **Prepayments – net** | **10,148** | 35,546 |
| **Trade and other receivables – net** | **386,397** | 306,895 |

Our net trade and other receivables increased by RMB79.5 million, or 25.9%, to RMB386.4 million as of 31 December 2017 from RMB306.9 million as of 31 December 2016. The increase reflected (i) an increase in trade receivables due from local government by RMB60.8 million, or 71.3%, to RMB146.2 million as of 31 December 2017 from RMB85.4 million as of 31 December 2016, primarily due to wastewater treatment fees charged for the forth quarter of 2017, which had been recognized but not yet paid by the relevant government authorities; (ii) an increase in amounts due from related parties by RMB55.8 million, or 140.6%, to RMB95.5 million as of 31 December 2017 from RMB39.7 million as of 31 December 2016, primarily due to service fees for entrusted operation which had been recognized but not yet paid; and (iii) a decrease in the prepayment of listing expenses, to Nil from RMB28.9 million as of 31 December 2016.

The aging analysis of trade receivables of our Group is shown as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| – Within one year | **243,528** | 125,542 |
| – Over one year and within two years | **3,023** | 458 |
| | **246,551** | 126,000 |

Based on the past experience, the Directors believe that no impairment allowance of trade receivables is necessary because the customers are mainly local government authorities and there has not been a significant change in their credit quality. Accordingly, these balances are considered fully recoverable.

The following table sets out our receivable turnover days for the periods indicated:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***Days*** | *Days* |
| Trade receivable turnover days (1) | **55.6** | 44.6 |
| Trade and other receivable turnover days (2) | **103.4** | 99.1 |

*Notes:*

(1) Calculated as the average net trade receivables for the relevant period divided by the revenue for the relevant period, and multiplied by 365 days. The arithmetic mean of the opening and closing balances of trade receivables is used for the years ended 31 December, 2016 and 2017.

(2) Calculated as the average net trade and other receivables for the relevant period divided by the revenue for the relevant period, and multiplied by 365 days. The arithmetic mean of the opening and closing balances of trade and other receivables is used for the years ended 31 December, 2016 and 2017.

*e.* *Trade and other payables*

Our trade and other payables primarily consists of trade payables, other payables, staff salaries and welfare payables, advance from customers, payables on acquisition of property, plant and equipment, payables on acquisition of land use rights from related parties, interest payables, and accrued taxes other than income tax.

The following table shows the breakdown of our trade and other payables as of the dates indicated:

| | **As at 31 December** | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Trade payables | **3,802** | 2,093 |
| Other payables | **71,899** | 53,176 |
| Consideration payable for acquisition of subsidiaries | **12,690** | 18,447 |
| Staff salaries and welfare payables | **28,667** | 28,661 |
| Advance from customers | **6,124** | 12,177 |
| Payables on acquisition of property, plant and equipment | **84,297** | 151,957 |
| Payables on acquisition of land use rights from related parties | **58,194** | 58,194 |
| Interest payables | **2,021** | 1,310 |
| Accrued taxes other than income tax | **102,156** | 96,324 |
| | **369,850** | 422,339 |

Our trade and other payables decreased by RMB52.5 million, or 12.4%, to RMB369.9 million as of 31 December 2017 from RMB422.3 million as of 31 December 2016. The decrease was mainly because the amount payable for the purchase of property, plant and equipment decreased by RMB67.7 million, or 44.4%, to RMB84.3 million as of 31 December 2017 from RMB152.0 million as of 31 December 2016. The above decrease was partially offset by the increase in other payables by RMB18.7 million, or 35.2%, to RMB71.9 million as of 31 December 2017 from RMB53.2 million as of 31 December 2016, primarily due to the increase in project service fees payable.

The aging analysis of trade and other payables of our Group is as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| – Within one year | **3,471** | 2,093 |
| – Over one year and within two years | **331** | – |
| | **3,802** | 2,093 |

As at 31 December 2016 and 2017, all trade and other payables of the Group were non-interest bearing, and their fair values, except for the advance from customers which are not financial liabilities, approximated their carrying amounts due to their short maturities.

The following table sets out our payable turnover days for the periods indicated:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***Days*** | *Days* |
| Trade and other payables turnover days (1) | **199.9** | 362.6 |
| Trade payables turnover days (2) | **37.4** | 19.4 |

*Notes:*

(1) Calculated as the average trade and other payables for the relevant period divided by cost of sales for the relevant period, and multiplied by 365 days. The arithmetic mean of the opening and closing balances of trade and other payables is used for the years ended 31 December, 2016 and 2017.

(2) Calculated as the balance of trade payables at the end of the relevant period divided by total purchase of materials for such period and multiplied by 365 days for the years ended 31 December 2016 and 2017.

Our trade payables turnover days increased by 18 days in 2017 as compared with 2016, mainly due to the increase of RMB1.7 million in the balance of trade payables at the end of the Reporting Period.

Directors confirm that up to 31 December 2017, there was no material default in payment of trade payables.

## *4. Indebtedness*

*a. Borrowings*

All of our borrowings are denominated in RMB and some are secured by our property, plant and equipment. The following table shows our borrowings as of the dates indicated:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Non-current:** | | |
| Unsecured long-term borrowings | **397,000** | – |
| Secured long-term borrowings | **–** | 48,356 |
| Corporate bonds | **694,625** | 693,639 |
| **Total non-current borrowings** | **1,091,625** | 741,995 |
| **Current:** | | |
| Unsecured short-term borrowings | **552,000** | 660,000 |
| Secured short-term borrowings | **47,570** | 118,737 |
| **Total current borrowings** | **599,570** | 778,737 |
| **Total borrowings** | **1,691,195** | 1,520,732 |

The weighted average effective interest rates at each balance sheet date are as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Average effective interest rates | **4.58%** | 4.78% |

Our total borrowings amounted to RMB1,520.7 million and RMB1,691.2 million as of 31 December 2016 and 2017, respectively. This represented an year-on-year increase of 11.2% between 2016 and 2017. Among our indebtedness, borrowings amounting to RMB167.1 million and RMB47.6 million as of 31 December 2016 and 2017 were secured by our property, plant and equipment. As at 31 December 2017, we have obtained a total of RMB2,250 million of bank credit facilities from multiple banks and financial leasing institutions in the PRC, of which line of credit used amounted to RMB949 million. In addition to bank borrowings, our total borrowings also include corporate bonds of approximately RMB700.0 million we issued on 25 December 2015 in the PRC for a term of seven years with an annual interest rate at 4.35%. At the end of the fifth year, the Company may adjust the interest rates for the remaining two years. In the event that investors disagree with the adjustment made to the interest rates, they may choose to demand an early redemption of corporate bonds outstanding.

As of 31 December 2017, there was no delay or default in the repayment of our borrowings, and no bank had withdrawn any of the banking facilities previously extended to us or had demanded any early repayment.

As of 31 December 2017, we were not in breach of any covenants in our loan agreements. Given our ability to access new bank borrowings and our strong credit profile, we believe we will not be subject to any risk of potential withdrawal of banking facilities or early repayment of outstanding loans. As of 31 December 2017, we had not received any requests for early repayment of the principal or interests under any of our loan agreements, and we did not have any plan for material external debt financing.

The table below sets out the maturity profiles of our borrowings as of the dates indicated:

| | **As at 31 December** | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| On demand or within 1 year | **599,570** | 778,737 |
| Between 1 and 2 years | **317,000** | 48,356 |
| Between 2 and 5 years | **80,000** | – |
| Later than 5 years | **694,625** | 693,639 |
| | **1,691,195** | 1,520,732 |

As of 31 December 2016 and 2017, our net gearing ratios were 30.1% and 7.95%, respectively. Our net gearing ratios as at 31 December 2017 dropped as compared with 31 December 2016 primarily due to the capital raised by public offering of H shares in April 2017 which substantially increased net assets.

Except as disclosed above, as of the 31 December 2017, we did not have any loan capital issued and outstanding or agreed to be issued, bank overdrafts, loans or other similar indebtedness, liabilities under acceptances or acceptable credits, debentures, mortgages, charges, hire purchases commitments, guarantees or other material contingent liabilities.

*b.* *Commitments*

Our capital commitments contracted for at each balance sheet date, but not yet incurred are as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Property, plant and equipment | **101,957** | 458,123 |
| Land use rights and intangible assets | **–** | 16,978 |
| Acquisition of interests in subsidiaries: | **122,200** | – |
| | **224,157** | 475,101 |

*c.* *Capital expenditure*

Our capital expenditure mainly comprises purchases of land use rights, property, plant and equipment and intangible assets. Our capital expenses were RMB668.2 million and RMB229.8 million for the years ended 31 December 2016 and 2017, respectively. We expect to fund our contractual commitments and capital expenditures principally though cash generated from our operating activities, proceeds from borrowings and the net proceeds we receive from the global offering of H Shares.

Our capital expenditure for each of our segments as at the dates indicated below is as follows:

| | As at 31 December | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Wastewater treatment | **205,626** | 651,031 |
| Other water-related services | **23,691** | 17,034 |
| Others | **483** | 86 |
| | **229,800** | 668,151 |

Based on our current business plan, we expect to incur capital expenditure amounting to RMB727.1 million for the year ending 31 December 2018. Our anticipated capital expenditure is subject to change from time to time based on the reassessment of our business plan, prevailing market conditions, regulatory environment and outlook of our future operational results.

***5. Off-balance sheet arrangements***

Other than as disclosed in this announcement and as of 31 December 2017, we did not have any outstanding off-balance sheet guarantees, interest rate swap transactions, foreign currency and commodity forward contracts or other off-balance sheet arrangements. We do not engage in trading activities involving non-exchange traded contracts. In the course of our business operations, we do not enter into transactions involving, or otherwise form relationships with, unconsolidated entities or financial partnerships that are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposed.

***6. Initial public offering and use of proceeds from initial public offering***

The H Shares of the Company were listed on the Hong Kong Stock Exchange on 6 April 2017 and the Company issued 339,430,000 H Shares of par value of RMB1.00 per share with the Offer Price of HK$3.91 per H Share. The total issuance size (before deducting the expenses) amounted to approximately HK$1,327,171,300. Following the listing of H shares of the Company, a total of 593,000 shares of H shares were over-allocated. After deducting (i) the net proceeds from the sale of Sale Shares by the Selling Shareholders in the Global Offering; and (ii) the underwriting commissions and other estimated expenses relating to the Global Offering, the Company would receive net proceeds of approximately HK$1,097.2 million from the Global Offering.

As of 31 December 2017, approximately RMB306.8 million, accounting for 28.61% of the RMB1,072.3 million net cash proceeds from the Global Offering, has been used pursuant to Use of Proceeds as follows: RMB2.7 million was used for investments in BOT/BOO wastewater treatment and running water supply projects; a total of RMB96.5 million was used for payments for acquisition of TOT/TOO wastewater treatment and running water supply projects, including Hongyu Water and prepayments for subsequent acquisitions; RMB207.6 million was used to repay existing bank borrowings.

***7. Foreign exchange risk and management***

The Group maintained some of the capital denominated in foreign currency, mainly the Hong Kong dollar. Fluctuations in exchange rate would influence our reserve in foreign currencies to a certain extent and the Company is exploring and discussing measures to respond to foreign exchange risk.

***8. Employees and remuneration policies***

As of 31 December 2017, we had 894 full-time employees, all of whom were in China and most of whom were based in Yunnan. The following table sets forth the breakdown of our employees by function as of 31 December 2017:

| **Function** | **Number** |
|---|---|
| Management and Administration | 107 |
| Finance | 18 |
| R&D | 40 |
| Quality Monitoring | 135 |
| Marketing | 15 |
| Operations | 553 |
| Construction and Maintenance | 26 |
| Total | 894 |

We recruit our employees on the open market. Compensation for our employees includes basic wages, variable wages, bonuses and other staff benefits. For the years ended 31 December 2016 and 2017, our employee benefits and labor expenses amounted to approximately RMB112.2 million and RMB125.0 million, respectively.

We believe our employees are the most valuable resources to achieve our success. To ensure the quality of our employees at all levels, we have in-house training programs to train our staff. New employees at our production facility receive trainings pertinent to their job duties. We also own the Kunming Dianchi Water Treatment Vocational Training School, which provides continuing training for our employees.

Our labor union communicates closely with the management regarding labor matters and represents our employees' interests. During the Reporting Period, we had not experienced any interruptions to our operations caused by major labor disputes and there were no complaints or claims from our employees which had a material adverse effect on our business. Our Directors believe that we have a good relationship with our employees. During the Reporting Period, the Group had no major labor disputes which might produce significant impact of the normal business and operation of the Group.

***9. Contingent liabilities***

As at 31 December 2017, the Group did not have any significant contingent liabilities.

***10. Material charges on assets***

There were no material charges on the Group's assets during the Reporting Period.

***11. Major investment and acquisition***

We entered into a framework agreement on 1 June 2016 to acquire 100.0% equity interests in three wastewater treatment companies in Jiangsu Province, namely Qutang Water, Libao Water and Hongze Water. The three companies had an aggregate designed wastewater treatment capacity of 50,000 $m^3$ per day. On 30 October 2016, we entered into three share transfer agreements thereby to acquire such three foregoing wastewater treatment companies for a total consideration of RMB79.95 million. These transactions were completed in January 2017 and such three companies have been consolidated into the Group thereafter. These acquisitions and development would not produce any significant financial impact on the Group individually or in an aggregate.

On 18 September 2017, the Company, Liuyang Hongyu Thermal Power Co., Ltd. (瀏陽市宏宇熱電有限公司), Hongyu Water, Zhuji Jujiyu Environmental Protection Equipment Co. Ltd. (諸暨巨集宇環保設備有限公司), and Huang Weifei entered into a Share Transfer Agreement, pursuant to which the Company has conditionally agreed to acquire, and Hongyu Thermal Power has conditionally agreed to sell the 100% equity interest in Hongyu Water for the estimated Consideration of RMB156.9 million. The acquisition was completed on 1 October 2017, and the amount of Consideration actually paid by the Company was RMB126.9 million because Hongyu Water needed to undergo project technology renovation to meet the effluent standard, which required RMB30 million to be paid by the Company after the acquisition. Hongyu Water became a wholly-owned subsidiary of the Company and its financial results, assets and liabilities were incorporated into the Group. For details, please refer to the Company's announcement dated 18 September 2017 and further announcements dated 11 October 2017 and 17 October 2017. Save the foregoing disclosures, the Company had no plans of major investments or capital and asset acquisition as of 31 December 2017.

### *12. Subsequent events*

*(a) Acquisition of subsidiaries*

The quality testing of the wastewater treatment facilities of Kunming No. 10 Water Purification Plant was completed and the final consideration was determined as RMB572,323,000. All the relevant facilities were transferred to the Company in January 2018.

Pursuant to the Board resolution of the Company dated 20 September 2017, the Group plans to acquire sewage treatment businesses including 100% equity interest in Debeiao Water directly or indirectly owned by Zou Hanping, Sichuan Debeiao Environmental Technology Industrial Co., Ltd. (四川德貝奧環保科技實業有限公司), and Sichuan Weilai Luzhou Municipal Public Engineering Co., Ltd. (四川未來綠洲市政公用工程有限公司). The acquisition was completed in January 2018 with a consideration of RMB80,230,000.

Pursuant to the Board resolution of the Company dated 19 December 2017, the Group plans to purchase sewage treatment businesses including 100% equity interest in Dongda Ciwu Sewage Treatment directly owned by Dongda Water Industry Group Co., Ltd. (東大水業集團有限公司) and Zhuji City Urban Public Transport Co., Ltd. (諸暨市長運城鄉公交有限公司). The acquisition was completed in January 2018 with a consideration of RMB85,326,000.

*(b) Dividend*

As approved by the Board on 26 March 2018, the Group intends to distribute to all shareholders annual cash dividend of RMB0.1527 per share, amounting to RMB157,145,249.70 in total. The proposal is subject to the Annual General Meeting for approval.

*(c) Providing entrusted loan to Kunming Industrial Development and Construction Co., Ltd. 昆明產業開發投資有限責任公司, ("**KIDC**")*

On 16 March 2018, the Company entered into a entrusted loan agreement with KIDC and Bank of Communications under which the Company entrusted Bank of Communications to provide a 9-month entrusted loan of RMB300 million to KIDC, with annual interest of 7%.

## III. COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE

The Company focuses on maintaining a high standard of corporate governance for purposes of enhancing the value of the shareholders and protecting their interests. The Company has adopted the code provisions of the Corporate Governance Code (the "**CG Code**") and Corporate Governance Report as contained in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "**Listing Rules**") and as its own corporate governance code. The Company has established and enhanced the corporate governance structure in accordance with the Listing Rules and the CG Code and has set up a series of corporate governance policies. The Directors believe that during the Reporting Period, the Company has been observing all mandatory code provisions as stipulated in the CG Code except for provision A.2.1.

Ms. Guo Yumei has been appointed as the Chairperson and President of the Company. In accordance with provision A.2.1 of the CG Code, the roles of chairperson and chief executive should be separated and should not be held by the same person. The Board of Directors has noticed that there was some deviation from Rule A.2.1 of the provisions of the Corporate Governance Code. However, given the development of the Group and the rich experience of Ms. Guo has in the industry and her many years of services at the Group, the Board of Directors believes, that Ms. Guo concurrently acting as the Chairperson and President will help implement the Group's business strategies and enhance the operating efficiency. In addition, the Board comprises 3 independent non-executive Directors and 2 non-executive Directors, enabling the interest of the Company's shareholders to be represented sufficiently and fairly under the supervision by the Board.

The Board will examine and review, from time to time, the Company's corporate governance practices and operation in order to comply with the relevant provisions under the Listing Rules and to protect shareholders' interests.

## IV. COMPLIANCE WITH THE MODEL CODE FOR SECURITIES DEALINGS BY THE DIRECTORS, SUPERVISORS AND RELEVANT EMPLOYEES

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 to the Listing Rules (the "**Model Code**") as its own code of conduct for its Directors, Supervisors and relevant employees (has the same meaning ascribed to it under the CG Code) in respect of their dealings in the Company's securities. After making specific enquiries to all of the Directors and Supervisors of the Company, the Directors and Supervisors of the Company confirmed that they had strictly complied with the required standards as set out in the Model Code during the Reporting Period.

## V. PURCHASE, SALE OR REDEMPTION OF THE COMPANY9S LISTED SECURITIES

Neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities during the Reporting Period.

## VI. AUDIT COMMITTEE

The Audit Committee is mainly responsible for reviewing and supervising the procedures for financial reporting and internal control of the Company. The Audit Committee of the Company has reviewed the audited annual results for the year ended 31 December 2017 and considered that the Group has adopted applicable accounting policies and made adequate disclosures in relation to preparation of relevant results.

## VII. FINAL DIVIDEND

The Board recommends the distribution of a final dividend ("**2017 Final Dividend**") of RMB0.1572 per share (tax included) (2016: RMB0.1 per share (tax inclusive) (RMB157,145,249.70 in total (tax included)) (2016: RMB102,911,100 (tax inclusive)) for the year ended 31 December 2017 to all shareholders, details of which are set out in Note 10 to the Financial Statements. The dividend of Domestic Shareholders shall be declared to be distributed and paid in RMB while the dividend of H Share Shareholders shall be declared to be distributed in RMB but paid in Hong Kong Dollars, as the exchange rate being subject to the average exchange published by the People's Bank of China within one week prior to the Annual General Meeting intended to be held by the Company on June 22, 2018. The expected dividend distribution date is Wednesday, 8 August 2018.

The proposal regarding the distribution of 2017 Final Dividend shall be confirmed subject to the approval of the general meeting for 2017 (the "**2017 Annual General Meeting**") to be held on 22 June 2018.

According to the provisions of the "Circular on Questions Concerning Withholding and Remitting Enterprise Income Tax for Dividends Received by Overseas H-share Holders (Non-resident Enterprise Shareholders) from Chinese Resident Enterprises (《關於中國居民企業向境外H股非居民企業股東派發股息代扣代繳企業所得稅有關問題的通知》) (Guo Shui Han [2008] No.897) issued by the State Administration of Taxation, an enterprise income tax at the rate of 10% shall be levied on dividends paid in or after 2008 by Chinese resident enterprises to overseas H-share shareholders that are non-resident enterprises.

Any shares registered in the name of the non-individual registered shareholders, including HKSCC Nominees Limited, other nominees, trustees or other groups and organizations, will be treated as being held by nonresident enterprise shareholders and therefore will be subject to the withholding of the enterprise income tax. If H shareholders intend to change its shareholder status, please enquire about the relevant procedures with your agents or transferee agent. The Company will strictly comply with the law or the requirements of the relevant government authority to withhold and pay enterprise income tax and individual income tax on behalf of the relevant shareholders based on the register of members for H shares of the Company as at the Dividend Registration Date. The Company assumes no responsibility and will not entertain any claims arising from any failure to timely determine, or inaccurate determination of, the status of the shareholders or any dispute over the arrangement of withholding and paying enterprise tax and individual income tax on behalf of such shareholders. Shareholders should consult their tax advisers regarding the PRC, Hong Kong and other tax implications of owning and disposing of the H shares of the Company.

If the individual H shareholders who are Hong Kong or Macau residents or residents of the countries which had an agreed tax rate of 10% for dividend with China under the relevant tax treaties, the Company should withhold and pay individual income tax on behalf of the relevant H shareholders at a rate of 10%. Should the individual H shareholders are residents of the countries which had an agreed tax rate of less than 10% with China under the relevant tax treaties, the Company shall withhold and pay individual income tax on behalf of the relevant H shareholders at a rate of 10%. If the relevant individual H shareholders wish to apply for a refund of the additional amount of tax withheld and paid, the Company can assist the relevant H shareholders to handle the application for the underlying preferential tax benefits pursuant to tax treaties. If the individual H shareholders who are residents of the countries which had an agreed tax rate of higher than 10% but lower than 20% for dividend with China under the relevant tax treaties, the Company should withhold and pay individual income tax on behalf of the relevant H shareholders at the actual rate specified under relevant tax treaties. In the case that the individual holders of H shares are residents of the countries which had an agreed tax rate of 20% with China under the tax treaties, or which has not entered into any tax treaties with China, or otherwise, the Company shall withhold and pay the individual income tax on behalf of the relevant H shareholders at a rate of 20%.

## VIII. CLOSURE OF REGISTER OF MEMBERS

For the purpose of determining H share shareholders' entitlement to attend the 2017 Annual General Meeting, the H share register of members of the Company will be closed from Tuesday, 22 May 2018 to Friday, 22 June 2018 (both days inclusive), during which no transfer of shares will be registered. In order to attend the 2017 Annual General Meeting, H share shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's H share registrar, Tricor Investor Services Limited, Level 22, Hopewell Centre, 183 Queen's Road East, Hong Kong, not later than 4:30 p.m. on Monday, 21 May 2018.

In order to determine the shareholders who are entitled to receive the above-mentioned final dividend, the register of members of the Company will be closed from Thursday, 28 June 2018 to Tuesday, 3 July 2018 (both days inclusive). To be eligible to receive the final dividend for the year ended 31 December 2017 (subject to the approval of the Company's shareholders), unregistered holders of H shares of the Company shall lodge relevant share transfer documents with the Company's H share registrar, Tricor Investor Services Limited, Level 22, Hopewell Centre, 183 Queen's Road East, Hong Kong for registration not later than 4:30 p.m. on Wednesday, 27 June 2018.

## IX. PUBLICATION OF ANNUAL REPORT

The annual report for the year ended 31 December 2017 of the Company will be dispatched to the holders of H shares of the Company in due course pursuant to the requirements of the Listing Rules and available for public viewing and downloading on the websites of Hong Kong Exchanges and Clearing Limited (http://www.hkexnews.hk) and the Company (http://www.kmdcwt.com).

By order of the Board
**Kunming Dianchi Water Treatment Co., Ltd.**
**Guo Yumei**
*Chairperson*

Kunming, the PRC, 26 March 2018

*As at the date of this announcement, the Board comprises Ms. Guo Yumei and Mr. Luo Yun, as executive Directors; Mr. Zeng Feng and Ms. Song Hong, as non-executive Directors; and Mr. Wong Man Chung Francis, Mr. Yin Xiaobing and Mr. He Xifeng, as independent non-executive Directors.*