*Potential investors should carefully consider all of the information set out in this prospectus and, in particular, should consider the following risks and special considerations associated with an investment in the Company before making any investment decision in relation to the Company.*

## RISKS RELATING TO THE GROUP AND ITS BUSINESS

### Substantial initial capital expenditure requirement

Due to the nature of the Group's business, the Group is required to make a substantial initial investment in the construction of gas pipeline infrastructure for each gas project. The initial investment must be financed by internal resources of the Group, bank loans or equity fund raising. There can be no assurance that external sources of financing will be available to fund the Group's capital expenditure programme. The failure to obtain such financing may hinder the Group's ability to continue its existing investments or make new investments.

### Dependence on economic development of an Operational Location

The business of the Group relies, in part, on the economic development of its Operational Locations. Although the Group carries out comprehensive financial and legal due diligence in respect of each project before it enters into a joint venture contract with the relevant local joint venture partner, there is no guarantee that an Operational Location will develop or prosper economically as projected by the relevant local government. Given the substantial capital investment at the early stages of each project, any unexpected adverse changes in the economic growth of an Operational Location may materially adversely affect the performance of the relevant project and hence, the performance of the Group.

### Price control

*(i) Connection fees*

Connection fees chargeable by the Group require the approval of the local state price bureau. There is no assurance that the Group will be able to obtain approvals from the relevant state price bureau for an increase in the connection fees, which may in turn materially adversely affect the profits of the Group.

*(ii) Gas usage charges*

Any increase in gas usage charges exceeding the original approved charge requires the approval of the local state price bureau. There is no assurance that any increases (except for an increase to offset the rise in the Group's purchase price of gas) will be approved.

### Dependence on property development of an Operational Location

The Group normally acts as the project manager for the laying of customers' pipeline in a property development project and the Group receives connection fees in stages based on the percentage-of-completion of pipeline construction work.

Property development projects may be materially adversely affected by a number of factors, including shortage of equipment or materials, price fluctuations, bad weather, natural disasters, accidents, downturns in the property market, economic conditions and other unforeseeable situations or matters. Should any of these risks occur, the completion of the whole or part of the property development project may be postponed and consequently the receipt of the progress payment of connection fees by the Group may be delayed. However, there will not be any compensation in the connection fees to be received as a result of such delay.

**Reliance on the suppliers of natural gas**

Natural gas, the primary raw material purchased by the Group, accounted for 34.4%, 35.5% and 25.9% of total purchases for each of the three financial years ended 31 December 2000, respectively. At present, the Group purchases natural gas primarily from three PRC national oil and gas exploration and production companies pursuant to gas purchase agreements with terms ranging from one to 15 years. There can be no assurance that the Group will be able to obtain natural gas from suppliers on terms similar to the current ones or without material interruption. If natural gas cannot be purchased by the Group on schedule or on terms acceptable to the Group, the Group's business and profitability may be materially adversely affected.

**Limited insurance coverage**

As natural gas is an inherently flammable and explosive substance, the Group has implemented strict safety measures for the operation and maintenance of its facilities. However, the Group cannot guarantee that industry-related accidents will not happen in the future. Significant operational hazards and natural disasters may cause interruptions in the Group's operations that could have a material adverse impact on the financial condition of the Group.

The Group has obtained insurance for certain fixed assets (including the pipelines owned by the Group) with net book value of RMB167,460,000 as at 28 February 2001 that the Group considers to be subject to significant operating risks. The maximum coverage is RMB102,800,000.

The Group has also taken out third party liability insurance policies covering (i) the loss of life or property of third parties arising out of any accident that may occur at processing stations of the Group (with maximum coverage being RMB10,000,000), and (ii) the loss of life of staff arising out of the business operations (with maximum coverage being RMB6,625,000). However, the Group has not taken out an insurance policy for any interruption in the business of the Group.

A successful claim made against the Group that is not covered by any of the Group's insurance policies or is in excess of its insurance coverage could have a material adverse effect on the Group's business and financial position.

**Environmental liability**

The Group is subject to the PRC environmental protection laws and regulations which impose fines for violations of laws, regulations or decrees and provide for the shutdown by the central, provisional or municipal governments of any facility not in compliance with governmental orders requiring the cessation or cure of certain activities causing environmental damage. Since natural gas is an environmentally friendly form of fuel, the Group has not adopted any special environmental protection measures other than the measures taken in the ordinary course of business by companies in the industry.

**Joint venture risks**

The Group has, and may have, interests in many joint ventures engaging in the piped gas business in the PRC. Such joint ventures may involve special risks, including the possibility that the joint venture partner may (i) have economic or business objectives that are inconsistent with those of the Group; (ii) experience financial difficulties; or (iii) be unable or unwilling to fulfil its obligations under the joint venture contracts. Although the Company has majority shareholdings in, and control over, the board of each of its existing joint ventures, certain important resolutions of these joint ventures, including (i) the amendment to articles of association; (ii) the termination and dissolution of the joint ventures; (iii) the transfer of any interests in the joint ventures; or (iv) the merger of the joint ventures with other economic entities, must be passed by unanimous approval of the joint venture partners.

Although the Acquisition Agreements and the Sino-foreign joint venture contracts have been entered into by the Group in respect of the Acquisition Companies and the New Project Companies, the completion of the acquisitions and the investments depends on obtaining approval from the relevant local foreign trade and economic co-operation departments. According to the Catalogue for the Guidance of Foreign Investment Industries (外商投資行業指導目錄) approved by the State Council on 29 December 1997 and promulgated on 31 December 1997, foreign investors are prohibited from ownership and management of complete gas supply networks for cities. As advised by the Company's PRC legal adviser, the business of the Group, being the provision of piped gas to selected locations within a city (such as economic development zones and independent residential districts and counties surrounding a city), does not contravene the relevant PRC laws and regulations. The Directors are of the view that the business of the Group is in line with national policy and that local governments are highly supportive of the business of the Group. This is evidenced by the fact that the establishment and the business of the Existing Project Companies have been approved by the relevant local foreign trade and economic co-operation departments. **In the event the relevant approvals in respect of the transfer of interests in the Acquisition Companies and the establishment of the New Project Companies are not granted, the Group's existing expansion plans and strategies may have to be revised and the operating results, prospects and financial condition of the Group may be materially adversely affected.**

**Holding company risks**

The Company's profits are derived from its Sino-foreign joint ventures, which have been established in the PRC. Profits available for distribution to the Shareholders are conditional upon profits being available for distribution to the Company by these joint ventures. Dividends to be declared will be based on the profits of these joint ventures determined pursuant to generally accepted accounting principles in the PRC or Hong Kong (whichever results in a lower profit calculation). In addition, pursuant to pertinent PRC laws and regulations on finance, profits available for distribution shall be determined after allocation to the statutory reserve funds. For further details, please refer to the paragraphs headed "Dividends" and "Distributable reserves" in the section headed "Financial information" in this prospectus. The ability of the joint ventures to make distributions to the Company will be subject to, among other things, the profit recorded in accordance with PRC generally accepted accounting principles, cashflow conditions and the expected future capital requirements of the joint venture.

As initial investment in a gas project is substantial, if the Directors decide to use retained profits to fund the Group's future development, the amount of profit available for distribution will be reduced. There is no guarantee that dividends will be declared by the Directors and there is no assurance that the current dividend payout ratio will continue in the future.

**Reliance on key management**

To a significant extent, the Group's success is built upon the technical expertise and in-depth knowledge of the piped gas supply industry possessed by the executive Directors and certain other key technical and management personnel as set out in the section headed "Directors, senior management and staff" in this prospectus. Each of the executive Directors has entered into a service contract with the Group for a fixed term of three years expiring on 29 February 2004 which service contract may be early terminated by the executive Director giving not less than six months' notice in writing, such notice not to be given at any time before 1 September 2003. Each of the key technical and management personnel (as referred to in the section headed "Directors, senior management and staff" in this prospectus) has entered into a service contract with the Group for a fixed term of at least two years which service contract may be early terminated by him or her giving not less than three months' notice in writing. Each of the executive Directors has also undertaken not to divulge or communicate confidential or other information or to engage in a competing business during the term of the service contract and for at least two years after expiration of the service contract. If any of the executive Directors or any of the key technical and management personnel ceases to be involved in the operation of the Group or if any of them fails to observe and perform their obligations under their service contracts, the implementation of the Group's business strategies may be affected and may lead to a material adverse impact on the operations of the Group.

Future growth and success of the Group will depend to a large extent on its ability to retain or recruit qualified individuals to strengthen its management, operational and research teams. With the growth in business, there may be a lack of sufficient management staff to oversee sales and operating, administrative and financial procedures and controls, which may in turn materially adversely affect the business of the Group.

**Concentration of ownership**

The Company will be beneficially owned by Easywin as to 70% of the issued capital of the Company following the completion of the Placing (assuming the Over-allotment Option is not exercised). As a result, Easywin will have the ability to reject all matters which are subject to approval of the Shareholders whether by way of ordinary resolution or special resolution (but excluding those from which Easywin must abstain from voting) and, therefore, Easywin has the ability to manage the Company's affairs. Such concentration of ownership may have the effect of delaying, deferring or preventing a change in control of the Company, impeding a merger, consolidation, takeover or other business combination involving the Company or discouraging a potential acquirer from making a general offer or otherwise attempting to obtain control of the Company, which in turn could have a material adverse effect on the market price of the Shares.

**Additional funding may be required**

The Directors are of the view that the net proceeds of the Placing are not sufficient to finance the implementation targets as described in the paragraph headed "Statement of business objectives and strategies – Implementation targets" in this prospectus in full. The Company will also use internally generated funds from operations and/or through other fund raising activities, including bank borrowings and equity financing. If the Group fails to obtain the necessary funding, the implementation targets may be readjusted or some of the implementation targets may not be achieved.

## RISKS RELATING TO THE INDUSTRY

### Substitute products

Coal gas, LPG and electricity are the main substitutes for natural gas. Ultimate consumers will consider factors such as cost, reliability, convenience and safety when choosing a fuel. Connection fees, gas usage charges and heat content are the major factors affecting customers' choice of fuel. Save for newly built residential apartments which are required to be equipped with gas supply for cooking stoves in most of the Operational Locations in which the Group has established a presence, there is no assurance that existing fuel users will shift to use piped natural gas.

## RISKS RELATING TO THE PRC

Since substantially all of the business of the Group is operated in the PRC, the profitability, financial position and prospects of the Group may be affected by the PRC's economic, political and regulatory regime.

### Political and economic considerations

The PRC economy is currently evolving from a planned economy into a market-oriented economy. Although the PRC has adopted an open door policy, changes in the policies of the PRC Government regarding the domestic economy (for example, changes affecting foreign exchange rates, inflation, taxation and trade) may have a material effect on the overall economy. The current reforms are unprecedented, produce effects that are unpredictable, and are subject to further refinement and improvement. New political, economic and social developments and considerations may lead the PRC Government to make adjustments to these reform measures. Such amendments and adjustments may not have a favorable effect on the Group's business. Any change, variation or adjustment to the reform measures taken by the PRC Government may have a material adverse effect on the business of the Group.

### Changes in laws, regulations and policies

The PRC legal system is a civil law system. Unlike the common law system, the civil law system is based on written statutes in which decided legal cases have little precedential value. In 1979, the PRC began to promulgate a comprehensive system of laws and has since introduced many laws and regulations to provide general guidance on economic and business practices in the PRC and to regulate foreign investment. Progress has been made in the promulgation of laws and regulations dealing with economic matters such as corporate organisation and governance, foreign investment, commerce, taxation and trade. The promulgation of new changes to existing laws and the abrogation of local regulations by national laws could have a negative impact on the business and prospects of the Group and its joint ventures. In addition, as these laws, regulations and legal requirements are relatively recent, their interpretation and enforcement involve significant uncertainty.

In the PRC, gas distribution companies invest in and operate the piped gas supply business in urban areas under the supervision of a number of government ministries and departments, including the Ministry of Foreign Trade and Economic Co-operation (對外經濟貿易合作部), the State Economic and Trade Commission (國家經濟貿易委員會), the Ministry of Construction (建設部), the Ministry of Labour and Social Security (勞動和社會保障部) and the

Ministry of Public Security (公安部). The Group must comply with the relevant requirements of certain regulations, including the City Fuel Gas Administration Regulations (《城市燃氣管理辦法》), the Tentative Regulations in relation to the Supervision and Administration of the Safety of Petroleum and Natural Gas Pipelines (《石油天然氣管道安全監督與管理暫行規定》) and the Regulations of the Safety of City Fuel Gas Administration (《城市燃氣安全管理規定》). In addition, the Group must comply with the relevant requirements and policies of local authorities where the Group's projects are situated.

Exclusive rights or rights of first refusal to provide piped gas are granted by local governments pursuant to policies of promoting environmental protection and encouraging the use of natural gas and the construction of natural gas supply facilities.

There can be no assurance that the above regulatory regime and policies (including the granting of exclusive rights or rights of first refusal to supply piped gas in Operational Locations) will not be changed. The Group's operations and profitability may be materially adversely affected if changes that occur are not favourable to the Group.

**Changes in favourable taxation treatment**

According to the rules and regulations of the PRC on taxation, a Sino-foreign joint venture which commences to be profitable may first recoup prior years' retained losses (such recoupment may not exceed five consecutive years), and thereafter such joint venture is exempt from income tax for the first two years after becoming profitable and is subject to a 50% reduction in the rate of profit tax for the following three years.

The Group holds interests in four Sino-foreign equity joint ventures, namely Langfang Xinao, Liaocheng Xinao, Beijing Xinao and Huludao Xinao which are all currently conducting operations. Langfang Xinao was established on 28 March 1993 and its first profit-making year was the financial year ended 31 December 1996. Accordingly, Langfang Xinao was exempted from PRC enterprise income tax for each of the financial years ended 31 December 1996 and 1997 and was then entitled to a 50% reduction in the rate of profit tax for each of the financial years ended 31 December 1998, 1999 and 2000. With effect from 1 January 2001, Langfang Xinao will pay income tax at the normal rate of 30%. As for the other three joint ventures, they became Sino-foreign equity joint ventures in August 2000, accordingly, they will be entitled to favourable taxation treatment from their respective first profit-making year.

Income tax refund amounted to approximately RMB5,180,000 for the two financial years ended 31 December 1999 was received by Langfang Xinao in January 2001. Such refund was granted pursuant to a favourable taxation policy adopted by the Finance Department of the Langfang Economic and Technical Development Zone in 1999. Based on such policy, part of the income tax paid for the two financial years ended 31 December 1999 was refunded. There can be no assurance that such tax concession will be granted to the Company again in the future. Pursuant to relevant tax regulations, Langfang Xinao may be refunded such amount of sales tax which exceeds the amount payable under the Commercial and Industrial Consolidated Tax abolished on 1 January 1994 upon obtaining approval from the tax authority. Sales tax refund amounting to approximately RMB2,656,000 was received in the financial year ended 31 December 1999. Such refund was one-off in nature and, accordingly, there can be no assurance that such refund will occur in the future.

There can be no assurance that the current taxation allowance (including sales tax refunds) will not be changed in the future. In the event of any change, the profitability of the Group may be materially adversely affected.

**Changes in foreign exchange regulations**

Since 1996, the PRC Government has promulgated various foreign exchange rules, regulations and notices (the "Policies") to raise the convertibility of Renminbi. According to the Policies, a foreign-invested enterprise ("FIE") must open a "current account" and a "capital account" at a bank authorised to trade foreign exchange. A FIE may convert Renminbi in the capital account into any foreign currency at any authorised bank with the prior approval of the State Administration for Foreign Exchange ("SAFE").

The income and expenditures of the Group are denominated in Renminbi. At present, Renminbi cannot be freely converted into other currencies. According to the Policies, upon producing the board resolution on the authorisation of the distribution of profits or dividends or the commercial documents evidencing foreign exchange transactions, the Group may purchase the foreign exchange required for the distribution from a designated authorised bank. The Group cannot guarantee that the Policies will not be withdrawn or amended.

The Group continues to have substantial requirements for foreign currency, including foreign currency denominated loans and purchases of imported equipment and materials. Repayment of the principal and interest of loans denominated in foreign currency shall be approved by SAFE in advance. Such approval requirement could affect the Group's ability to obtain foreign exchange through debt financing or to obtain foreign exchange for capital expenditure.

In addition, according to the current foreign exchange control system, there can be no assurance that sufficient foreign exchange can be obtained pursuant to a specific exchange rate in order to satisfy the Group's entire needs. A shortage in the foreign exchange may prevent the Company from obtaining sufficient currency to pay dividends or limit its ability to satisfy its needs for foreign exchange.

**Currency and exchange fluctuations**

The value of Renminbi is subject to changes in the PRC Government's policies and depends to a large extent on domestic and international economic and political developments, as well as supply and demand in the local market. Since 1994, the official exchange rate for the conversion of Renminbi to US dollars has generally been stable, and Renminbi has appreciated slightly against the US dollar. However, given the economic instability and currency fluctuations in Asia in recent years, the Directors cannot give any assurance that the value of Renminbi will continue to remain stable against the US dollar or any other foreign currency.

Any devaluation of Renminbi may adversely affect the value of, and dividends payable on, the Shares in foreign currency terms since the Group receives its revenues and expresses its profits in Renminbi. Results of operations and the financial condition of the Group may also be affected by changes in the value of certain currencies other than Renminbi in which the Group's obligations are denominated. In particular, a devaluation of the Renminbi is likely to increase the portion of the Group's cash flow required to satisfy its foreign currency-denominated obligations.

## RISKS RELATING TO THE PLACING

### Non-active trading market and potential share price volatility

Prior to the listing of Shares on GEM, the Shares will not be available in any open market. The Placing Price is determined by the Company and ICEA (on behalf of the Underwriters) upon considering a number of factors, including the current market conditions, the market value of companies which the Group and ICEA believe are comparable to the Group, the Group's development and financial position, the Group's piped gas supply business in the PRC and its prospects, the income and profit forecasts of the Group and other relevant factors. There can be no assurance that an active trading market will develop, that the market will be sustained upon the flotation of the Shares on the market and that the market price of the Shares will not drop below the Placing Price.

In addition to the above factors, the trading price of the Shares may fluctuate due to other factors, including:

- investors' views on the Group and investments in the PRC;
- the development of the gas industry;
- fluctuations in the business results of the Group;
- variations in the prices charged by the Group, its competitors or suppliers of fuel substitutes;
- shareholding distribution ratio and liquidity of Shares; and
- the overall economic situation or other factors.

The Shares held by the public Shareholders may be sold in the market immediately after listing. If the Shareholders sell the Shares in bulk within a short time frame, the Share price may fall substantially.

### Developments in other markets

Securities listed on GEM have been, to varying degrees, influenced by economic and market conditions in other emerging markets and other countries. Although economic conditions vary among countries, investors' reactions to developments in one country may affect the securities of issuers in other countries, including the PRC. Continued volatility in the Asian or the United States financial markets, may lead to increased volatility in other securities markets, including Hong Kong and the PRC securities markets, and may materially adversely affect the price of the Placing Shares.

In addition, Hong Kong and the PRC financial and securities markets are, to varying degrees, influenced by economic and market conditions in more industrialised countries, particularly the United States. Events that increase the opportunity cost of investing outside the United States may tend to reduce the attractiveness of the securities investments in other countries, such as the PRC.