Chairman's Statement

"Fully capitalising on our technological strengths, extensive experiences, resources and application scenarios, we are committed to achieving our carbon reduction targets."

Dr. Lee Ka-kit
Chairman

Looking back on the past year, we were pleased to witness the conclusion of the global pandemic. The resurgence of the global economy, however, has been sluggish, creating a challenging road to recovery. The international political landscape has continued to be volatile, with various regions plagued by wars and conflicts, further exacerbating the energy crisis. During the year, life on the Chinese mainland returned to normal, albeit amidst a dampened global economy. This has led to fluctuations in the country's post-pandemic recovery whilst posing challenges to the business environment.

Despite the uncertain economic prospects, the Group put an emphasis on prudence, innovation and resilience. On the one hand, we reinforced our foothold in the gas business, leveraging the untapped potential of our existing business while maintaining rigorous discipline over capital expenditure. On the other hand, we continue to develop our renewable energy business based on an asset-light model, aiming to minimise financial leverage and provide our shareholders with stable returns.

In addition, the country has been actively committed to green development over the years. As such, it has drawn up a clear emission reduction plan to achieve the "30-60" dual carbon goals. A primary focus of this plan is to explore new green energy sources to replace fossil fuels. Relevant national policies have pointed out a clear direction for our future development, and we are well aware that this is not only an undeniable responsibility but also a precious opportunity.

Since the 1990s, we have been deeply rooted on the Chinese mainland, establishing a large industrial and commercial customer base there. Starting out as a city-gas business operator, we have built an impeccable reputation for safety and service quality. Coupled with the pressing demand from industrial and commercial customers to reduce energy costs and carbon emission, this gives us a unique advantage in developing comprehensive energy management services. In the face of the new race track and other new opportunities, we are pursuing a two-pronged approach with the business development of both the natural gas and renewable energy businesses. Leveraging our professional energy management technologies and platforms, we aim to provide our customers with a full range of energy management solutions.

All our staff members will also rise to these challenges with the utmost professionalism, entrepreneurial spirit and resilience, working together for the robust development of the Group's businesses.

Annual Results

At the end of 2023, the Group had 536 city-gas and renewable energy projects in 25 provinces, autonomous regions and municipalities, representing an increase of 173 projects as compared to last year. The gas sales volume for the year increased by 8% compared to last year. The total number of Group customers reached 16.77 million during the year, representing an increase of 840,000 customers. The renewable energy business also developed further, with 44 zero-carbon smart industrial parks developed during the year, bringing the cumulative number of projects to 124. Turnover increased by 4.2% to RMB17,915 million, but due to the exchange rate impact, turnover in Hong Kong dollars decreased slightly by 1.2% to HK$19,842 million. Profit attributable to shareholders of the Company increased significantly by 63.2% to HK$1,575 million. Core profit rose by 16.3% to HK$1,190 million (increased by 22.6% in Renminbi).

Chairman's Statement

Towngas Smart Energy announced its exit from its 25% equity interest in Shanghai Gas Co., Ltd. ("Shanghai Gas") after amicable negotiations with Shenergy (Group) Company Limited ("Shenergy Group") and Shanghai Gas, with a recovery of the fund of RMB4,663 million during the year. Both parties have established a deep and strong strategic relationship in the area of natural gas resources and supply chain, the renewable energy business, extended services, energy technology and low-carbon technology.

Final Dividend

The Board recommend a final dividend of 16 HK cents per share payable to shareholders whose names are on the Register of Members of the Company as at 6 June 2024, increased by 6.7% compared to last year. The Board also proposed to offer a scrip dividend option to allow shareholders to elect to receive the final dividend wholly or partly in the form of new and fully paid shares in lieu of cash.

Utility Business

Given the lacklustre growth of the global economy, the Chinese mainland continued to experience weak product demand in 2023. As such, its economic recovery slowed down in the second half of the year. Under the national policy of continuing to promote the use of natural gas, national consumption has seen an overall return to positive growth. The national natural gas consumption reached approximately 394.5 billion cubic metres, representing an increase of 7.6% compared to last year. With the improvement in the supply-demand structure of the natural gas industry, rational pricing has also returned.

Benefiting from these favourable policies and the improvement in the market environment, the Group's city-gas business recorded relatively satisfactory growth. During the year, we recorded an overall gas sales volume of 16,458 million cubic metres, representing an increase of 8%. Industrial gas sales rose by 6.1%, while commercial gas sales increased by 9%. The number of customers reached 16.77 million, representing an increase of 840,000 customers during the year. As for city-gas projects, 4 new projects were added during the year, totalling 187 projects (inclusive of corporate reinvestment projects).

Industrial gas consumption remains a key growth area for our city-gas business. For many years, the Group focused on attracting large-scale industrial users, providing customers with integrated energy solutions through "Gas+" services to help them optimise their energy consumption structure and efficiency. This initiative has promoted the development of low-carbon and smart industrial energy solutions, further consolidating and enhancing our gas business and increasing its contribution to gross profit.

Furthermore, with the country's encouragement and support for public institutions to adopt energy cost trusteeship services in recent years, our "Gas+" business has seen favourable progress. Through the provision of our energy-saving, carbon reduction, safe gas usage and integrated energy cost trusteeship services to government agencies, schools, hospitals and other major institutions, as well as our agreements with a number of government agencies and public institutions in the provision of services such as cooling, heating, hot water, steam, and electricity, we are contributing to the country's carbon peak and carbon neutrality goals.

In respect of residential city-gas, in June 2023, the National Development and Reform Commission issued the "Guiding Opinions on Establishing and Improving the Upstream and Downstream Natural Gas Price Linkage Mechanism" to all provinces. This initiative introduced an automatic transmission mechanism while establishing an adjustment mechanism for city-gas prices for residential users in various regions. These mechanisms can increase or decrease prices, moving flexibly to reflect changes in supply and demand. This, in turn, has allowed us to achieve significant progress in cost pass-through.

Renewable Energy Business

With the implementation of the "dual carbon" strategy, the country's renewable energy development grew rapidly in 2023. During the year, the national and local governments introduced several favourable policies, including encouraging and supporting energy transition. This positive move has helped to establish order as well as good industry norms, in addition to promoting innovation in technological products and fostering a focus on the most suitable operational approach. This excellent policy environment is driving the top-quality development of the industry.

During the year, our renewable energy business achieved profitability. As at the end of 2023, the Group developed 124 zero-carbon smart industrial parks, and laid out more than 1,000 renewable energy projects in 23 provinces, autonomous regions and municipalities. The business scope in these projects spans various aspects, such as photovoltaics, energy storage, battery charging and swapping stations, and integrated energy services for industrial and commercial customers.

The first virtual power plant built by the Group for a public institution in Shenzhen was officially put into operation during the year. This project integrates photovoltaic power generation, energy storage, charging piles, distributed power supplies, and loads. During peak power consumption periods, the virtual power plant outputs excess power to the grid to ensure smooth operation. We are excited to see more similar near-zero-carbon energy projects among other regions in the future, allowing for the expansion of our business portfolio.

With the ongoing deepening and refinement of electricity market reform, market-based green electricity trading is gradually becoming a standardised and scalable mechanism. Under our renewable energy electricity trading framework in Guangdong province, we have served a number of high-energy-consuming and export trading enterprises through renewable energy electricity trading. In 2023, the total amount of electricity sold by the Group was 1 billion kWh in Guangdong. The total amount of electricity sold by the Group on the Chinese mainland is expected to reach 10 billion kWh by 2025.

Environmental, Social and Governance

Towngas Smart Energy remains committed to integrating environmental, social and governance ("ESG") initiatives into our corporate governance and business operations. This unswerving policy allows us to respond to China's "30-60" dual carbon goals as well as the ESG concerns of stakeholders and capital markets on the highest levels. Towngas Smart Energy has received favourable evaluations from six major international ESG ratings and indices, including:

- CDP
- FTSE Russell
- Hang Seng Corporate Sustainability Index
- MSCI
- S&P Global
- Sustainalytics

In June 2023, Towngas Smart Energy, together with our parent company, The Hong Kong and China Gas Company Limited ("HKCG"), were ranked among the "Top 1%" of Chinese enterprises in ESG rating, and were also included in the first-ever S&P Global "Sustainability Yearbook (China Edition)". Just as impressively, Towngas Smart Energy was recognised as an "Industry Mover". Subsequently, in September, we were upgraded to an AA rating in the Hang Seng Corporate Sustainability Index Series, reflecting the ongoing recognition of our quality ESG performance.

Chairman's Statement

Business Outlook

Looking ahead to 2024, we do not expect to see any significant improvement in the many factors affecting the external environment. However, with a series of favourable national policies and measures to stabilise the economy, boost consumption, promote energy conservation and emission reduction, as well as to increase urbanisation rates, we anticipate a steady growth in residential gas demand and maintain an optimistic outlook on its development prospects.

The government is focusing on rectifying the safety hazards of liquefied petroleum gas bottled gas in catering establishments, and the related "bottle-to-pipe" business is expected to drive the continuous increase in natural gas sales volume. With the rapid development of the new energy industry on the Chinese mainland and the increase in demand for gas from new energy automobiles, photovoltaic glass, lithium batteries, and other industrial customers, we believe the Group will enjoy a considerable increase in gas sales volume.

The government intends to revise the "Policies on the Utilisation of Natural Gas", "Regulations on the Administration of Urban Gas" and "Measures for the Administration of Concession for Infrastructure and Public Utilities" to not only encourage investments in the public utility sector and ensure that reasonable returns can be obtained, but also to guide the quality development of the natural gas industry. It is anticipated that the relevant policies will have a positive impact on the development of the Group.

The outlook for the renewable energy business is promising. The country has proposed the multiplication of both wind and solar power generation during the "14th Five-Year Plan" period, with a total installed capacity of more than 1.2 billion kilowatts. As the installed capacity of wind power and photovoltaics continues to grow, energy storage will play an increasingly important role as a balancing resource. In 2023, the newly installed photovoltaic capacity exceeded 216GW on the Chinese mainland. As the upstream manufacturing capacity of the photovoltaic industry continues to grow, the price of photovoltaic components is dropping significantly. In turn, the investment cost of industrial and commercial distributed photovoltaic power station systems is being reduced, and returns on investment have increased. This situation is proving to be extremely beneficial to the growth of our photovoltaic business.

Additionally, the widening price differentials between peak and off-peak industrial electricity consumption on the Chinese mainland, coupled with the overcapacity in the battery manufacturing market, are creating enhanced arbitrage opportunities for commercial and industrial energy storage. The price of battery cells has dropped by almost 30% from previous highs. Coupled with the improvements in battery technology, where the number of battery cycles and efficiency have increased, the cost of power generation has been reduced. We therefore expect considerable growth in installed capacity for the industrial and commercial sectors.

Taking this positive environment further forward, the Central Commission for Comprehensively Deepening Reform has reviewed and approved multiple policies that emphasise the improvement in the total amount and intensity of energy consumption regulations, as well as the gradual shift to dual control of the total amount and intensity of carbon emissions. These policies will be conducive to enhancing the proportion of green power usage, increasing the demand for downstream green certification, accelerating voluntary emission reductions on the Chinese mainland, and stimulating the potential carbon asset value of clean energy. Guided by these policies, distributed photovoltaics, as one of the main green power sources and one of the main green energy sources covered by green certificates, will benefit significantly and is expected to create considerable additional revenue.

The country is vigorously developing the hydrogen energy economy. As a new energy source, hydrogen energy is an important element with unlimited growth potential. We are actively preparing for our pilot project, which blends hydrogen in our natural gas pipelines. In April 2023, the "Key Technology Research and Scale Application of Piped Hydrogen in the Field of Comprehensive Energy Supply in Towns" proposed by Weifang Hong Kong and China Gas Limited was approved by the Ministry of Science and Technology, and has now entered its research stage. The goal is to achieve a 10% hydrogen blending ratio covering 100,000 residential users. Furthermore, Foran Energy Group Co., Ltd., a company in which the Group has a stake, is actively advancing hydrogen energy services. It is constructing hydrogen production and refuelling stations in Foshan, Guangdong province, to support the development of public hydrogen-powered transportation. Foran Energy Group Co., Ltd. is also involved in the research and development of fuel cells and the manufacturing of hydrogen energy equipment.

In general, facing the uncertain operating environment, we believe the Group is well prepared. We continue to carefully review the operation of each business segment to improve our overall efficiency. We will also continue to capitalise on our own advantages and innovative insights to enhance our integrated energy services for industrial and commercial customers, as well as residential users, promoting our journey towards sustainable development.

On behalf of the Group's Board of Directors, I would like to express our tremendous gratitude to our customers, shareholders, investors, and members of the community who have long followed and supported the Group's development. Our many thanks, too, to all our dedicated colleagues who have consistently demonstrated resilience and innovation in their roles.

Lee Ka-kit
Chairman

Hong Kong, 19 March 2024