DEUTSCHE BANK AKTIENGESELLSCHAFT
Form 424B2
July 06, 2017

**Pricing Supplement**

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| *To underlying supplement No. 1 dated August 17, 2015,* | *Pricing Supplement No. 2861B* |
| *product supplement B dated July 31, 2015,* | *Registration Statement No. 333-206013* |
| *prospectus supplement dated July 31, 2015 and* | *Rule 424(b)(2)* |
| *prospectus dated April 27, 2016* | |

**The information in this preliminary pricing supplement is not complete and may be changed. This preliminary pricing supplement and the accompanying underlying supplement, product supplement, prospectus supplement and prospectus do not constitute an offer to sell nor do they seek an offer to buy the notes in any jurisdiction where the offer or sale is not permitted.**

Subject to Completion. Dated July 6, 2017

**Structured Investments** **Deutsche Bank AG**
**$ Capped Return Enhanced Notes Linked to the SPDR® S&P® Bank ETF due July 25, 2018**

**General**

- The notes are designed for investors who seek a return at maturity of two times the potential positive performance (if any) of the SPDR® S&P® Bank ETF (the "**Underlying**"), subject to a Maximum Return of 21.20%. However, if the Final Price is less than the Initial Price, for each $1,000 Face Amount of notes, investors will lose 1.00% of the Face Amount for every 1.00% by which the Final Price is less than the Initial Price. The notes do not pay any coupons or dividends and investors should be willing to lose some or all of their investment if the Final Price is less than the Initial Price. Any payment on the notes is subject to the credit of the Issuer.
- Senior unsecured obligations of Deutsche Bank AG due July 25, 2018
- Minimum purchase of $10,000. Minimum denominations of $1,000 (the "**Face Amount**") and integral multiples thereof.
- The notes are expected to price on or about July 7, 2017 (the "**Trade Date**") and are expected to settle on or about July 12, 2017 (the "**Settlement Date**").

**Key Terms**

| | |
|---|---|
| Issuer: | Deutsche Bank AG, London Branch |
| Underlying: | SPDR® S&P® Bank ETF (Ticker: KBE) |
| Issue Price: | 100% of the Face Amount |
| Upside Leverage Factor: | 2.00 |
| Maximum Return: | 21.20%. The actual Maximum Return on the notes will be determined on the Trade Date and will not be less than 21.20%. Accordingly, the maximum Payment at Maturity will not be less than $1,212.00 per $1,000 Face Amount of notes. |
| Payment at Maturity: | · **If the Final Price is greater than the Initial Price,** you will receive a cash payment at maturity per $1,000 Face Amount of notes calculated as follows:<br><br>$1,000 + ($1,000 x the *lesser of* (i) Underlying Return x Upside Leverage Factor and (ii) Maximum Return)<br><br>· **If the Final Price is equal to the Initial Price,** you will receive a cash payment at maturity equal to the Face Amount per $1,000 Face Amount of notes.<br><br>· **If the Final Price is less than the Initial Price,** you will receive a cash payment at maturity per $1,000 Face Amount of notes calculated as follows:<br><br>$1,000 + ($1,000 x Underlying Return)<br><br>*If the Final Price is less than the Initial Price, you will be fully exposed to the negative Underlying Return and, for each $1,000 Face Amount of notes, you will lose 1.00% of the Face Amount for every 1.00% by which the Final Price is less than the Initial Price. In this circumstance, you will lose some or all of your investment at maturity. Any payment at maturity is subject to the credit of the Issuer.* |
| Underlying Return: | The performance of the Underlying from the Initial Price to the Final Price, calculated as follows:<br><br>$\frac{\text{Final Price – Initial Price}}{\text{Initial Price}}$<br><br>*The Underlying Return may be positive, zero or negative.* |

*(Key Terms continued on next page)*

**Investing in the notes involves a number of risks. See "Risk Factors" beginning on page 7 of the accompanying product supplement, page PS-5 of the accompanying prospectus supplement and page 13 of the accompanying prospectus and "Selected Risk Considerations" beginning on page 7 of this pricing supplement.**

**The Issuer's estimated value of the notes on the Trade Date is approximately $962.00 to $982.00 per $1,000 Face Amount of notes, which is less than the Issue Price. Please see "Issuer's Estimated Value of the Notes" on page 2 of this pricing supplement for additional information.**

**By acquiring the notes, you will be bound by and deemed irrevocably to consent to the imposition of any Resolution Measure (as defined below) by the competent resolution authority, which may include the write down of all, or a portion, of any payment on the notes or the conversion of the notes into ordinary shares or other instruments of ownership. If any Resolution Measure becomes applicable to us, you may lose some or all of your investment in the notes. Please see "Resolution Measures and Deemed Agreement" on page 3 of this pricing supplement for more information.**

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the notes or passed upon the accuracy or the adequacy of this pricing supplement or the accompanying underlying supplement, product supplement, prospectus supplement or prospectus. Any representation to the contrary is a criminal offense.

| | Price to Public[1] | Fees[1][2] | Proceeds to Issuer |
|---|---|---|---|
| **Per Note** | $1,000.00 | $10.00 | $990.00 |
| **Total** | $ | $ | $ |

(1) JPMorgan Chase Bank, N.A. and J.P. Morgan Securities LLC, which we refer to as JPMS LLC, or one of its affiliates will act as placement agents for the notes. The placement agents will forgo fees for sales to fiduciary accounts. The total fees represent the amount that the placement agents receive from sales to accounts other than such fiduciary accounts. The placement agents will receive a fee from the Issuer that will not exceed $10.00 per $1,000 Face Amount of notes.

(2) Please see "Supplemental Plan of Distribution" in this pricing supplement for more information about fees.

*The notes are not deposits or savings accounts and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other U.S. or foreign governmental agency or instrumentality.*

**JPMorgan**

**Placement Agent**

July , 2017

*(Key Terms continued from previous page)*

| | |
|---|---|
| Initial Price: | The closing price of the Underlying on the Trade Date |
| Final Price: | The arithmetic average of the Closing Prices of the Underlying on each of the five Averaging Dates |
| Closing Price: | The closing price of one share of the Underlying on the relevant date of calculation *multiplied by* the then-current Share Adjustment Factor, as determined by the calculation agent. |
| Share Adjustment Factor: | Initially 1.0, subject to adjustment for certain actions affecting the Underlying. See "Description of the Securities — Anti-dilution Adjustments for Funds" in the accompanying product supplement. |
| Trade Date[2]: | July 7, 2017 |
| Settlement Date[2]: | July 12, 2017 |
| Averaging Dates[1, 2]: | July 16, 2018, July 17, 2018, July 18, 2018, July 19, 2018 and July 20, 2018 |
| Maturity Date[1, 2]: | July 25, 2018 |
| Listing: | The notes will not be listed on any securities exchange. |
| CUSIP / ISIN: | 25155MCF6 / US25155MCF68 |

[1] Subject to adjustment as described under "Description of Securities — Adjustments to Valuation Dates and Payment Dates" in the accompanying product supplement.

[2] In the event that we make any changes to the expected Trade Date or Settlement Date, the Averaging Dates and Maturity Date may be changed so that the stated term of the notes remains the same.

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**Issuer's Estimated Value of the Notes**

The Issuer's estimated value of the notes is equal to the sum of our valuations of the following two components of the notes: (i) a bond and (ii) an embedded derivative(s). The value of the bond component of the notes is calculated based on the present value of the stream of cash payments associated with a conventional bond with a principal amount equal to the Face Amount of notes, discounted at an internal funding rate, which is determined primarily based on our market-based yield curve, adjusted to account for our funding needs and objectives for the period matching the term of the notes. The internal funding rate is typically lower than the rate we would pay when we issue conventional debt securities on equivalent terms. This difference in funding rate, as well as the agent's commissions, if any, and the estimated cost of hedging our obligations under the notes, reduces the economic terms of the notes to you and is expected to adversely affect the price at which you may be able to sell the notes in any secondary market. The value of the embedded derivative(s) is calculated based on our internal pricing models using relevant parameter inputs such as expected interest and dividend rates and mid-market levels of price and volatility of the assets underlying the notes or any futures, options or swaps related to such underlying assets. Our internal pricing models are proprietary and rely in part on certain assumptions about future events, which may prove to be incorrect.

The Issuer's estimated value of the notes on the Trade Date (as disclosed on the cover of this pricing supplement) is less than the Issue Price of the notes. The difference between the Issue Price and the Issuer's estimated value of the notes on the Trade Date is due to the inclusion in the Issue Price of the agent's commissions, if any, and the cost of hedging our obligations under the notes through one or more of our affiliates. Such hedging cost includes our or our affiliates' expected cost of providing such hedge, as well as the profit we or our affiliates expect to realize in consideration for assuming the risks inherent in providing such hedge.

The Issuer's estimated value of the notes on the Trade Date does not represent the price at which we or any of our affiliates would be willing to purchase your notes in the secondary market at any time. Assuming no changes in market conditions or our creditworthiness and other relevant factors, the price, if any, at which we or our affiliates would be willing to purchase the notes from you in secondary market transactions, if at all, would generally be lower than both the Issue Price and the Issuer's estimated value of the notes on the Trade Date. Our purchase price, if any, in secondary market transactions will be based on the estimated value of the notes determined by reference to (i) the then-prevailing internal funding rate (adjusted by a spread) or another appropriate measure of our cost of funds and (ii) our pricing models at that time, less a bid spread determined after taking into account the size of the repurchase, the nature of the assets underlying the notes and then-prevailing market conditions. The price we report to financial reporting services and to distributors of our notes for use on customer account statements would generally be determined on the same basis. However, during the period of approximately six months beginning from the Trade Date, we or our affiliates may, in our sole discretion, increase the purchase price determined as described above by an amount equal to the declining differential between the Issue Price and the Issuer's estimated value of the notes on the Trade Date, prorated over such period on a straight-line basis, for transactions that are individually and in the aggregate of the expected size for ordinary secondary market repurchases.

**Resolution Measures and Deemed Agreement**

On May 15, 2014, the European Parliament and the Council of the European Union adopted a directive establishing a framework for the recovery and resolution of credit institutions and investment firms (commonly referred to as the "**Bank Recovery and Resolution Directive**"). The Bank Recovery and Resolution Directive required each member state of the European Union to adopt and publish by December 31, 2014 the laws, regulations and administrative provisions necessary to comply with the Bank Recovery and Resolution Directive. Germany adopted the Recovery and Resolution Act (*Sanierungs- und Abwicklungsgesetz*, or the "**Resolution Act**"), which became effective on January 1, 2015. The Bank Recovery and Resolution Directive and the Resolution Act provided national resolution authorities with a set of resolution powers to intervene in the event that a bank is failing or likely to fail and certain other conditions are met. From January 1, 2016, the power to initiate resolution measures applicable to significant banking groups (such as Deutsche Bank Group) in the European Banking Union has been transferred to the European Single Resolution Board which, based on the European Union regulation establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund (the "**SRM Regulation**"), works in close cooperation with the European Central Bank, the European Commission and the national resolution authorities. Pursuant to the SRM Regulation, the Resolution Act and other applicable rules and regulations, the notes may be subject to any Resolution Measure by the competent resolution authority if we become, or are deemed by the competent supervisory authority to have become, "non-viable" (as defined under the then applicable law) and are unable to continue our regulated banking activities without a Resolution Measure becoming applicable to us. By acquiring the notes, you will be bound by and deemed irrevocably to consent to the provisions set forth in the accompanying prospectus, which we have summarized below.

By acquiring the notes, you will be bound by and deemed irrevocably to consent to the imposition of any Resolution Measure by the competent resolution authority. Under the relevant resolution laws and regulations as applicable to us from time to time, the notes may be subject to the powers exercised by the competent resolution authority to: (i) write down, including to zero, any payment (or delivery obligations) on the notes; (ii) convert the notes into ordinary shares of (a) the Issuer, (b) any group entity or (c) any bridge bank or other instruments of ownership of such entities qualifying as common equity tier 1 capital; and/or (iii) apply any other resolution measure including, but not limited to, any transfer of the notes to another entity, the amendment, modification or variation of the terms and conditions of the notes or the cancellation of the notes. We refer to each of these measures as a "**Resolution Measure**." A "group entity" refers to an entity that is included in the corporate group subject to a Resolution Measure. A "bridge bank" refers to a newly chartered German bank that would receive some or all of our assets, liabilities and material contracts, including those attributable to our branches and subsidiaries, in a resolution proceeding.

Furthermore, by acquiring the notes, you:

- are deemed irrevocably to have agreed, and you will agree: (i) to be bound by, to acknowledge and to accept any Resolution Measure and any amendment, modification or variation of the terms and conditions of the notes to give effect to any Resolution Measure; (ii) that you will have no claim or other right against us arising out of any Resolution Measure; and (iii) that the imposition of any Resolution Measure will not constitute a default or an event of default under the notes, under the senior indenture dated November 22, 2006 among us, Law Debenture Trust Company of New York, as trustee, and Deutsche Bank Trust Company Americas, as issuing agent, paying agent, authenticating agent and registrar, as amended and supplemented from time to time (the "**Indenture**"), or for the purposes of, but only to the fullest extent permitted by, the Trust Indenture Act of 1939, as amended (the "**Trust Indenture Act**");

- waive, to the fullest extent permitted by the Trust Indenture Act and applicable law, any and all claims against the trustee and the paying agent, the issuing agent and the registrar (each, an "**indenture agent**") for, agree not to initiate a suit against the trustee or the indenture agents in respect of, and agree that the trustee and the indenture agents will not be liable for, any action that the trustee or the indenture agents take, or abstain from taking, in either case in accordance with the imposition of a Resolution Measure by the competent resolution authority with respect to the notes; and

- will be deemed irrevocably to have: (i) consented to the imposition of any Resolution Measure as it may be imposed without any prior notice by the competent resolution authority of its decision to exercise such power with respect to the notes; (ii) authorized, directed and requested The Depository Trust Company ("**DTC**") and any direct participant in DTC or other intermediary through which you hold such notes to take any and all necessary action, if required, to implement the imposition of any Resolution Measure with respect to the notes as it may be imposed, without any further action or direction on your part or on the part of the trustee or the indenture agents; and (iii) acknowledged and accepted that the Resolution Measure provisions described herein and in the "Resolution Measures" section of the accompanying prospectus are exhaustive on the matters described herein and therein to the exclusion of any other agreements, arrangements or understandings between you and the Issuer relating to the terms and conditions of the notes.

*This is only a summary, for more information please see the accompanying prospectus dated April 27, 2016, including the risk factors beginning on page 13 of such prospectus.*

**Additional Terms Specific to the Notes**

You should read this pricing supplement together with underlying supplement No. 1 dated August 17, 2015, product supplement B dated July 31, 2015, the prospectus supplement dated July 31, 2015 relating to our Series A global notes of which these notes are a part and the prospectus dated April 27, 2016. Delaware Trust Company, which acquired the corporate trust business of Law Debenture Trust Company of New York, is the successor trustee of the notes. When you read the accompanying underlying supplement, product supplement and prospectus supplement, please note that all references in such supplements to the prospectus dated July 31, 2015, or to any sections therein, should refer instead to the accompanying prospectus dated April 27, 2016 or to the corresponding sections of such prospectus, as applicable, unless otherwise specified or the context otherwise requires. You may access these documents on the website of the Securities and Exchange Commission (the "**SEC**") at.www.sec.gov as follows (or if such address has changed, by reviewing our filings for the relevant date on the SEC website):

- Underlying supplement No. 1 dated August 17, 2015:

http://www.sec.gov/Archives/edgar/data/1159508/000095010315006546/crt_dp58829-424b2.pdf

- Product supplement B dated July 31, 2015:

http://www.sec.gov/Archives/edgar/data/1159508/000095010315006059/crt_dp58181-424b2.pdf

- Prospectus supplement dated July 31, 2015:

http://www.sec.gov/Archives/edgar/data/1159508/000095010315006048/crt-dp58161_424b2.pdf

- Prospectus dated April 27, 2016:

https://www.sec.gov/Archives/edgar/data/1159508/000119312516559607/d181910d424b21.pdf

Our Central Index Key, or CIK, on the SEC website is 0001159508. As used in this pricing supplement, "**we**," "**us**" or "**our**" refers to Deutsche Bank AG, including, as the context requires, acting through one of its branches. This pricing supplement, together with the documents listed above, contains the terms of the notes and supersedes all other prior or contemporaneous oral statements as well as any other written materials including preliminary or indicative pricing terms, correspondence, trade ideas, structures for implementation, sample structures, brochures or other educational materials of ours. You should carefully consider, among other things, the matters set forth in this pricing supplement and in "Risk Factors" in the accompanying product supplement, prospectus supplement and prospectus, as the notes involve risks not associated with conventional debt securities. We urge you to consult your investment, legal, tax, accounting and other advisers before deciding to invest in the notes.

**You may revoke your offer to purchase the notes at any time prior to the time at which we accept such offer by notifying the applicable agent. We reserve the right to change the terms of, or reject any offer to purchase, the notes prior to their issuance. We will notify you in the event of any changes to the terms of the notes and you will be asked to accept such changes in connection with your purchase of any notes. You may also choose to reject such changes, in which case we may reject your offer to purchase the notes.**

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**Hypothetical Examples**

The following table illustrates a range of hypothetical payments at maturity on the notes. The table and the hypothetical examples below assume a Maximum Return on the notes of 21.20% and reflect the Upside Leverage Factor of 2.00. The actual Initial Price and Maximum Return will be determined on the Trade Date. The table and hypothetical examples set forth below are for illustrative purposes only. The actual return applicable to a purchaser of the notes will be based on the Underlying Return, determined using the Closing Prices of the Underlying on the specified Averaging Dates. The numbers appearing in the table and examples below may have been rounded for ease of analysis. You should consider carefully whether the notes are suitable to your investment goals.

| Hypothetical Underlying Return (%) | Hypothetical Return on the Notes (%) | Hypothetical Payment at Maturity ($) |
|---|---|---|
| 100.00% | 21.20% | $1,212.00 |
| 90.00% | 21.20% | $1,212.00 |
| 80.00% | 21.20% | $1,212.00 |
| 70.00% | 21.20% | $1,212.00 |
| 60.00% | 21.20% | $1,212.00 |
| 50.00% | 21.20% | $1,212.00 |
| 40.00% | 21.20% | $1,212.00 |
| 30.00% | 21.20% | $1,212.00 |
| 20.00% | 21.20% | $1,212.00 |
| **10.60%** | **21.20%** | **$1,212.00** |
| 10.00% | 20.00% | $1,200.00 |
| 5.00% | 10.00% | $1,100.00 |
| **0.00%** | **0.00%** | **$1,000.00** |
| -5.00% | -5.00% | $950.00 |
| -10.00% | -10.00% | $900.00 |
| -20.00% | -20.00% | $800.00 |
| -30.00% | -30.00% | $700.00 |
| -40.00% | -40.00% | $600.00 |
| -50.00% | -50.00% | $500.00 |
| -60.00% | -60.00% | $400.00 |
| -70.00% | -70.00% | $300.00 |
| -80.00% | -80.00% | $200.00 |
| -90.00% | -90.00% | $100.00 |
| -100.00% | -100.00% | $0.00 |

**Hypothetical Examples of Amounts Payable at Maturity**

The following hypothetical examples illustrate how the payments on the notes at maturity set forth in the table above are calculated.

**Example 1: The Final Price is greater than the Initial Price, resulting in an Underlying Return of 30.00%.** Because the Final Price is greater than the Initial Price and the product of the Underlying Return of 30.00% and the Upside Leverage Factor is greater than the Maximum Return, the investor receives the Maximum Return on the notes. Accordingly, the investor receives a Payment at Maturity of $1,212.00 per $1,000 Face Amount of notes, calculated as follows:

$1,000 + ($1,000 x the *lesser of* (i) Underlying Return x Upside Leverage Factor and (ii) Maximum Return)
$1,000 + ($1,000 x 21.20%) = $1,212.00

**Example 2: The Final Price is greater than the Initial Price, resulting in an Underlying Return of 5.00%.** Because the Final Price is greater than the Initial Price and the product of the Underlying Return of 5.00% and the Upside Leverage Factor is less than the Maximum Return, the investor receives a Payment at Maturity of $1,100.00 per $1,000 Face Amount of notes, calculated as follows:

$1,000 + ($1,000 x the *lesser of* (i) Underlying Return x Upside Leverage Factor and (ii) Maximum Return)
$1,000 + ($1,000 x 5.00% x 2.00) = $1,100.00

**Example 3: The Final Price is equal to the Initial Price, resulting in an Underlying Return of 0.00%.** Because the Final Price is equal to the Initial Price, the investor receives a Payment at Maturity of $1,000.00 per $1,000 Face Amount of notes.

**Example 4: The Final Price is less than the Initial Price, resulting in an Underlying Return of -40.00%.** Because the Final Price is less than the Initial Price, the Underlying Return is negative and the investor receives a Payment at Maturity of $600.00 per $1,000 Face Amount of notes, calculated as follows:

$1,000 + ($1,000 x Underlying Return)
$1,000 + ($1,000 x -40.00%) = $600.00

**Selected Purchase Considerations**

- **CAPPED APPRECIATION POTENTIAL** — The notes provide the opportunity to enhance returns by multiplying a positive Underlying Return by the Upside Leverage Factor of 2.00, subject to the Maximum Return on the notes of 21.20%, resulting in a maximum Payment at Maturity of $1,212.00 per $1,000 Face Amount of notes. The actual Maximum Return on the notes will be determined on the Trade Date and will not be less than 21.20%. **Any payment on the notes is subject to our ability to satisfy our obligations as they become due.**

- **FULL DOWNSIDE EXPOSURE** — If the Final Price is less than the Initial Price, for each $1,000 Face Amount of notes, you will lose 1.00% of the Face Amount for every 1.00% by which the Final Price is less than the Initial Price. In this circumstance, you will lose some or all of your investment in the notes.

- **RETURN LINKED TO THE PERFORMANCE OF THE SPDR® S&P® BANK ETF** — The return on the notes, which may be positive, zero or negative, is linked to the performance of the SPDR® S&P® Bank ETF as described herein. The SPDR® S&P® Bank ETF is an exchange-traded fund managed by SPDR® Series Trust, a registered investment company. The SPDR® Series Trust consists of numerous separate investment portfolios, including the SPDR® S&P® Bank ETF. SSgA Funds Management, Inc. is the investment adviser of the SPDR® S&P® Bank ETF. The SPDR® S&P® Bank ETF seeks to provide investment results that, before fees and expenses, correspond generally to the total return performance of the S&P® Banks Select Industry® Index, which represents the performance of the bank sub-industry portion of the S&P® Total Market Index. The SPDR® S&P® Bank ETF trades on the NYSE Arca under the ticker symbol "KBE." *This is only a summary of the SPDR® S&P® Bank ETF. For more information on the SPDR® S&P® Bank ETF, please see the section entitled "The SPDR® S&P® Bank ETF" in this pricing supplement.*

- **TAX CONSEQUENCES** — In the opinion of our special tax counsel, Davis Polk & Wardwell LLP, which is based on prevailing market conditions, it is more likely than not that the notes will be treated for U.S. federal income tax purposes as prepaid financial contracts that are not debt. Generally, if this treatment is respected, (i) you should not recognize taxable income or loss prior to the maturity or other taxable disposition of your notes and (ii) subject to the potential application of the "constructive ownership" regime discussed below, the gain or loss on your notes should be capital gain or loss and should be long-term capital gain or loss if you have held the notes for more than one year. The Internal Revenue Service (the "**IRS**") or a court might not agree with this treatment, however, in which case the timing and character of income or loss on your notes could be materially and adversely affected.

Even if the treatment of the notes as prepaid financial contracts is respected, purchasing a note could be treated as entering into a "constructive ownership transaction" within the meaning of Section 1260 of the Internal Revenue Code ("**Section 1260**"). In that case, all or a portion of any long-term capital gain you would otherwise recognize upon the taxable disposition of the note would be recharacterized as ordinary income to the extent such gain exceeded the "net underlying long-term capital gain" as defined in Section 1260. Any long-term capital gain recharacterized as ordinary income would be treated as accruing at a constant rate over the period you held the note, and you would be subject to a notional interest charge in respect of the deemed tax liability on the income treated as accruing in prior tax years. Due to the lack of direct legal authority, our special tax counsel is unable to opine as to whether or how Section 1260 applies to the notes.

In 2007, the U.S. Treasury Department and the IRS released a notice requesting comments on various issues regarding the U.S. federal income tax treatment of "prepaid forward contracts" and similar instruments. The notice focuses in particular on whether beneficial owners of these instruments should be required to accrue income over the term of their investment. It also asks for comments on a number of related topics, including the character of income or loss with respect to these instruments; the relevance of factors such as the nature of the underlying property to which the instruments are linked; the degree, if any, to which income (including any mandated accruals) realized by non-U.S. persons should be subject to withholding tax; and whether these instruments are or should be subject to the "constructive ownership" regime discussed above. While the notice requests comments on appropriate transition rules and effective dates, any Treasury regulations or other guidance promulgated after consideration of these issues could materially and adversely affect the tax consequences of an investment in the notes, possibly with retroactive effect.

Withholding under legislation commonly referred to as "FATCA" might (if the notes were recharacterized as debt instruments) apply to amounts treated as interest paid with respect to the notes. Notwithstanding anything to the contrary in the section of the accompanying product supplement entitled "U.S. Federal Income Tax Consequences," under a recent IRS notice, withholding under FATCA will not apply to payments of gross proceeds (other than any amount treated as interest) of a taxable disposition, including redemption at maturity, of the notes. You should consult your tax adviser regarding the potential application of FATCA to the notes.

Section 871(m) of the Code and Treasury regulations promulgated thereunder ("**Section 871(m)**") generally impose a 30% withholding tax (unless an income tax treaty applies) on dividend equivalents paid or deemed paid to non-U.S. holders with respect to certain financial instruments linked to U.S. equities or indices that include U.S. equities. Section 871(m) provides certain exceptions to this withholding regime, including for instruments linked to certain broad-based indices that meet requirements set forth in the applicable Treasury regulations (such an index, a "**Qualified Index**"). Additionally, the applicable regulations exclude from the scope of Section 871(m) instruments issued in 2017 that do not have a delta of one with respect to underlying securities that could pay U.S.-source dividends for U.S. federal income tax purposes (each an "**Underlying Security**"). Based on certain determinations made by us, we expect that Section 871(m) will not apply to the notes with regard to non-U.S. holders. Our determination is not binding on the IRS, and the IRS may disagree with this determination. Section 871(m) is complex and its application may depend on your particular circumstances, including whether you enter into other transactions with respect to an Underlying Security. If necessary, further information regarding the potential application of Section 871(m) will be provided in the pricing supplement for the notes. You should consult your tax adviser regarding the potential application of Section 871(m) to the notes.

You should review carefully the section of the accompanying product supplement entitled "U.S. Federal Income Tax Consequences." The preceding discussion, when read in combination with that section, constitutes the full opinion of our special tax counsel regarding the material U.S. federal income tax consequences of owning and disposing of the notes.

Under current law, the United Kingdom will not impose withholding tax on payments made with respect to the notes.

For a discussion of certain German tax considerations relating to the notes, you should refer to the section in the accompanying prospectus supplement entitled "Taxation by Germany of Non-Resident Holders."

**You should consult your tax adviser regarding the U.S. federal tax consequences of an investment in the notes (including possible alternative treatments, the potential application of the "constructive ownership" regime and the issues presented by the 2007 notice), as well as tax consequences arising under the laws of any state, local or**

**non-U.S. taxing jurisdiction.**

**Selected Risk Considerations**

An investment in the notes involves significant risks. Investing in the notes is not equivalent to investing directly in the shares of the Underlying or in any of the component securities held by the Underlying. In addition to these selected risk considerations, you should review the "Risk Factors" sections of the accompanying product supplement, prospectus supplement and prospectus.

- **YOUR INVESTMENT IN THE NOTES MAY RESULT IN A LOSS** — The notes do not guarantee any return of your investment. The return on the notes at maturity is linked to the performance of the Underlying and will depend on whether, and the extent to which, the Underlying Return is positive, zero or negative. If the Final Price is less than the Initial Price, for each $1,000 Face Amount of notes, you will lose 1.00% of the Face Amount for every 1.00% by which the Final Price is less than the Initial Price. In this circumstance, you will lose some or all of your investment in the notes. **Any payment on the notes is subject to our ability to satisfy our obligations as they become due.**

- **THE RETURN ON THE NOTES IS LIMITED** — If the Final Price is greater than the Initial Price, for each $1,000 Face Amount of notes, you will receive at maturity the Face Amount plus an additional amount that will not exceed the product of the Maximum Return of 21.20% and $1,000 Face Amount of notes. Consequently,

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assuming the Maximum Return is determined on the Trade Date to be 21.20%, the maximum Payment at Maturity will be $1,212.00 per $1,000 Face Amount of notes, regardless of any increase in the price of the Underlying, which may be significant.

- **THE NOTES DO NOT PAY ANY COUPONS** — Unlike ordinary debt securities, the notes do not pay any coupons and do not guarantee any return of your investment at maturity.

- **THE NOTES ARE SUBJECT TO THE CREDIT OF DEUTSCHE BANK AG** — The notes are senior unsecured obligations of Deutsche Bank AG and are not, either directly or indirectly, an obligation of any third party. Any payment(s) to be made on the notes depends on the ability of Deutsche Bank AG to satisfy its obligations as they become due. An actual or anticipated downgrade in Deutsche Bank AG's credit rating or increase in the credit spreads charged by the market for taking Deutsche Bank AG's credit risk will likely have an adverse effect on the value of the notes. As a result, the actual and perceived creditworthiness of Deutsche Bank AG will affect the value of the notes and, in the event Deutsche Bank AG were to default on its obligations or become subject to a Resolution Measure, you might not receive any amount(s) owed to you under the terms of the notes and you could lose your entire investment.

- **The Notes May Be Written Down**, **Be Converted Into Ordinary Shares or Other Instruments of Ownership or Become Subject to Other Resolution Measures**. **You May Lose Some or All of Your Investment If Any Such Measure Becomes Applicable to US** — Pursuant to the SRM Regulation, the Resolution Act and other applicable rules and regulations described above under "Resolution Measures and Deemed Agreement," the notes are subject to the powers exercised by the competent resolution authority to impose Resolution Measures on us, which may include: writing down, including to zero, any claim for payment on the notes; converting the notes into ordinary shares of (i) the Issuer, (ii) any group entity or (iii) any bridge bank or other instruments of ownership of such entities qualifying as common equity tier 1 capital; or applying any other resolution measure including, but not limited to, transferring the notes to another entity, amending, modifying or varying the terms and conditions of the notes or cancelling the notes. The competent resolution authority may apply Resolution Measures individually or in any combination.

The German law on the mechanism for the resolution of banks of November 2, 2015 (*Abwicklungsmechanismusgesetz*, or the "**Resolution Mechanism Act**") provides that, in a German insolvency proceeding of the Issuer, certain specifically defined senior unsecured debt instruments would rank junior to, without constituting subordinated debt, all other outstanding unsecured unsubordinated obligations of the Issuer and be satisfied only if all such other senior unsecured obligations of the Issuer have been paid in full. This prioritization would also be given effect if Resolution Measures are imposed on the Issuer, so that obligations under debt instruments that rank junior in insolvency as described above would be written down or converted into common equity tier 1 instruments *before* any other senior unsecured obligations of the Issuer are written down or converted. A large portion of our liabilities consist of senior unsecured obligations that either fall outside the statutory definition of debt instruments that rank junior to other senior unsecured obligations according to the Resolution Mechanism Act or are expressly exempted from such definition.

Among those unsecured unsubordinated obligations that are expressly exempted are money market instruments and senior unsecured debt instruments whose terms provide that (i) the repayment or the amount of the repayment depends on the occurrence or non-occurrence of an event which is uncertain at the point in time when the senior unsecured debt instruments are issued or is settled in a way other than by monetary payment, or (ii) the payment of interest or the amount of the interest payments depends on the occurrence or non-occurrence of an event which is uncertain at the point in time when the senior unsecured debt instruments are issued unless the payment of interest or the amount of the interest payments solely depends on a fixed or floating reference interest rate and is settled by monetary payment. This order of priority introduced by the Resolution Mechanism Act would apply in German insolvency proceedings instituted, or when Resolution Measures are imposed, on or after January 1, 2017 with effect for debt instruments of the Issuer outstanding at that time. In a German insolvency proceeding or in the event of the imposition of Resolution Measures with respect to the Issuer, the competent regulatory authority or court would determine which of our senior debt securities issued under the prospectus have the terms described in clauses (i) or (ii) above, referred to herein as the “**Structured Debt Securities**,” and which do not, referred to herein as the “**Non-Structured Debt Securities**.” We expect the notes offered herein to be classified as Structured Debt Securities, but the competent regulatory authority or court may classify the notes differently. In a German insolvency proceeding or in the event of the imposition of Resolution Measures with respect to the Issuer, the Structured Debt Securities are expected to be among the unsecured unsubordinated obligations that would bear losses after the Non-Structured Debt Securities as described above.

**Nevertheless**, **you may lose some or all of your investment in the notes if a Resolution Measure becomes applicable to us**. Imposition of a Resolution Measure would likely occur if we become, or are deemed by the competent supervisory authority to have become, "non-viable" (as defined under the then applicable law) and are unable to continue our regulated banking activities without a Resolution Measure becoming applicable to us. The Bank Recovery and Resolution Directive and the Resolution Act are intended to eliminate the need for public support of troubled banks, and you should be aware that public support, if any, would only potentially be used by the competent supervisory authority as a last resort after having assessed and exploited, to the maximum extent practicable, the resolution tools, including the bail-in tool.

By acquiring the notes, you would have no claim or other right against us arising out of any Resolution Measure and we would have no obligation to make payments under the notes following the imposition of a Resolution Measure. In particular, the imposition of any Resolution Measure will not constitute a default or an event of default under the notes, under the Indenture or for the purposes of, but only to the fullest extent permitted by, the Trust Indenture Act. Furthermore, because the notes are subject to any Resolution Measure, secondary market trading in the notes may not follow the trading behavior associated with similar types of securities issued by other financial institutions which may be or have been subject to a Resolution Measure.

In addition, by your acquisition of the notes, you waive, to the fullest extent permitted by the Trust Indenture Act and applicable law, any and all claims against the trustee and the indenture agents for, agree not to initiate a suit against the trustee or the indenture agents in respect of, and agree that the trustee and the indenture agents will not be liable for, any action that the trustee or the indenture agents take, or abstain from taking, in either case in accordance with the imposition of a Resolution Measure by the competent resolution authority with respect to the notes. **Accordingly**, **you may have limited or circumscribed rights to challenge any decision of the competent resolution authority to impose any Resolution Measure**.

- **THE ISSUER'S ESTIMATED VALUE OF THE NOTES ON THE TRADE DATE WILL BE LESS THAN THE ISSUE PRICE OF THE NOTES** — The Issuer's estimated value of the notes on the Trade Date (as disclosed on the cover of this pricing supplement) is less than the Issue Price of the notes. The difference between the Issue Price and the Issuer's estimated value of the notes on the Trade Date is due to the inclusion in the Issue Price of the agent's commissions, if any, and the cost of hedging our obligations under the notes through one or more of our affiliates. Such hedging cost includes our or our affiliates' expected cost of providing such hedge, as well as the profit we or our affiliates expect to realize in consideration for assuming the risks inherent in providing such hedge. The Issuer's estimated value of the notes is determined by reference to an internal funding rate and our pricing models. The internal funding rate is typically lower than the rate we would pay when we issue conventional debt securities on equivalent terms. This difference in funding rate, as well as the agent's commissions, if any, and the estimated cost of hedging our obligations under the notes, reduces the economic terms of the notes to you and is expected to adversely affect the price at which you may be able to sell the notes in any secondary market. In addition, our internal pricing models are proprietary and rely in part on certain assumptions about future events, which may prove to be incorrect. If at any time a third party dealer were to quote a price to purchase your notes or otherwise value your notes, that price or value may differ materially from the estimated value of the notes determined by reference to our internal funding rate and pricing models. This difference is due to, among other things, any difference in funding rates, pricing models or assumptions used by any dealer who may purchase the notes in the secondary market.

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**INVESTING IN THE NOTES IS NOT THE SAME AS INVESTING IN THE SHARES OF THE UNDERLYING OR THE COMPONENT SECURITIES HELD BY THE UNDERLYING** — The return on the notes may not reflect the return you would have realized if you had directly invested in the shares of the Underlying or the component securities held by the Underlying. For instance, you will not have voting rights or rights to receive cash dividends or other distributions or other rights that holders of the shares of the Underlying or the component securities held by the Underlying would have. In addition, you will not receive more than the Maximum Return regardless of any potential increase in the price of the Underlying, which could be significant, even though you will be exposed to any decline in the price of the Underlying at maturity.

- **IF THE PRICE OF THE UNDERLYING CHANGES, THE VALUE OF YOUR NOTES MAY NOT CHANGE IN THE SAME MANNER** — Your notes may trade quite differently from the shares of the Underlying and the component securities held by the Underlying. Changes in the prices of the shares of the Underlying and the component securities held by the Underlying may not result in comparable changes in the value of your notes.

- **NO DIVIDEND PAYMENTS OR VOTING RIGHTS** — As a holder of the notes, you will not have any voting rights or rights to receive cash dividends or other distributions or other rights that holders of the shares of the Underlying or the component securities held by the Underlying would have.

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- **THE EQUITY SECURITIES HELD BY THE SPDR® S&P® BANK ETF ARE SUBJECT TO RISKS ASSOCIATED WITH THE BANKING SECTOR** — All or substantially all of the equity securities held by the SPDR® S&P® Bank ETF are issued by companies whose primary line of business is directly associated with the banking sector. The performance of companies in the banking sector may be affected by governmental regulation that may limit the amount and types of loans and other financial commitments that banks can make, the interest rates and fees they can charge and the amount of capital they must maintain. Profitability is largely dependent on the availability and cost of capital funds, and can fluctuate significantly when interest rates change. Credit losses resulting from financial difficulties of borrowers can negatively impact the banking sector. Banks may also be subject to severe price competition. The regional banking industry is highly competitive, and thus, failure to maintain or increase market share may adversely affect profitability. These factors or the absence of such factors could cause a downturn in the bank industries and could cause the value of some or all of the component securities held by the SPDR® S&P® Bank ETF and the price of the SPDR® S&P® Bank ETF to decline during the term of the notes.

- **THE POLICIES OF THE INVESTMENT ADVISOR OF THE UNDERLYING AND CHANGES THAT AFFECT THE UNDERLYING OR ITS TRACKED INDEX COULD ADVERSELY AFFECT THE VALUE OF THE NOTES —** The policies of the investment advisor of the Underlying (the "**Underlying Advisor**") concerning the calculation of the Underlying's net asset value ("**NAV**"), additions, deletions or substitutions of securities or other assets or financial measures held by the Underlying, substitution of the Tracked Index and the manner in which changes affecting how the Tracked Index is calculated are reflected in the Underlying could adversely affect the price of the shares of the Underlying and, therefore, the value of, and your return on, the notes. The value of, and your return on, the notes could also be adversely affected if the Underlying Advisor changes its policies, for example, by changing the manner in which the Underlying Advisor calculates the Underlying's NAV, or if the Underlying Advisor discontinues or suspends calculation or publication of the Underlying's NAV, in which case it may become difficult to determine the value of the notes. If events such as these occur or if the Closing Price of the Underlying is not available on an Averaging Date because of a market disruption event or for any other reason, the calculation agent, in certain circumstances, may determine the Closing Price of the Underlying and the Payment at Maturity in a manner it considers appropriate in its sole discretion.

- **The Performance of the Underlying**, **Particularly During Periods of Market Volatility**, **May Not Match the Performance of THE Tracked INDEX or its Net Asset Value per Share** — The performance of the Underlying may not match the performance of the Tracked Index due to a number of factors. For instance, the Underlying may not hold all or substantially all of the securities included in the Tracked Index and the Underlying Advisor may invest a portion of the Underlying's assets in securities not included in the Tracked Index. Therefore, the performance of the Underlying is generally linked, in part, to assets other than the securities included in the Tracked Index. Additionally, the performance of the Underlying will reflect transaction costs and fees that are not included in the calculation of the Tracked Index.

In addition, because the shares of the Underlying are traded on a securities exchange and are subject to supply and demand, the performance of one share of the Underlying may differ from the performance of the Tracked Index or the Underlying's NAV per share. Furthermore, during periods of market volatility, securities or other assets held by the Underlying may become unavailable in the secondary market due to reduced liquidity or suspensions of, or limitations on, trading, making it difficult for market participants to accurately calculate the NAV per share of the Underlying and/or create, redeem or hedge shares of the Underlying. In such circumstances, the prices at which market participants are willing to buy and sell shares of the Underlying may be significantly lower than the Underlying's NAV and the liquidity of the shares of the Underlying may be materially and adversely affected. Consequently, the performance of the Underlying may deviate significantly from the performance of the Tracked Index or the Underlying's NAV per share. These circumstances may or may not constitute market disruption events and, in either case, your return on the notes may be determined based on the price of the shares of the Underlying when it deviates significantly from the performance of the Tracked Index or the Underlying's NAV per share. If this occurs, the value of, and your return on, the notes may be materially and adversely affected.

- **ANTI-DILUTION PROTECTION IS LIMITED AND THE CALCULATION AGENT MAY MAKE ADJUSTMENTS IN ADDITION TO, OR THAT DIFFER FROM, THOSE SET FORTH IN THE ACCOMPANYING PRODUCT SUPPLEMENT** — The calculation agent will make adjustments to the Share Adjustment Factor, which will initially be set at 1.0, for certain events affecting the shares of the Underlying. The calculation agent is not required, however, to make such adjustments in response to all events that could affect the shares of the Underlying. If an event occurs that does not require the calculation agent to make an adjustment, the value of the notes may be materially and adversely affected. In addition, you should be aware that the calculation agent may, at its sole discretion, make adjustments to the Share Adjustment Factor or any other terms of the notes that are in addition to, or that differ from, those described in the accompanying product supplement to reflect changes occurring in relation to the Underlying in circumstances where the calculation agent determines that it is appropriate to reflect those changes to ensure an equitable result. Any alterations to the specified anti-dilution adjustments described in the accompanying product supplement may be materially adverse to investors in the notes. You should read "Description of Securities — Anti-Dilution Adjustments for Funds" in the accompanying product supplement in order to understand the adjustments that may be made to the notes.

- **THERE IS NO AFFILIATION BETWEEN THE UNDERLYING OR THE UNDERLYING STOCK ISSUERS AND US AND WE HAVE NOT PARTICIPATED IN THE PREPARATION OF, OR VERIFIED, ANY INFORMATION ABOUT THE UNDERLYING OR THE UNDERLYING STOCK ISSUERS** — We are not affiliated with the Underlying or the issuers of the component stocks held by the Underlying or included in the Tracked Index (such stocks, "**Underlying Stocks**," and the issuers of Underlying Stocks, "**Underlying Stock Issuers**"). However, we or our affiliates may currently, or from time to time in the future, engage in business with the Underlying Stock Issuers, including extending loans to, making equity investments in, acting as underwriter in connection with future offerings of the Underlying Stocks by, or providing advisory services (including merger and acquisition advisory services) to, such Underlying Stock Issuers. In the course of this business, we or our affiliates may acquire non-public information about the Underlying Stock Issuers and we will not disclose any such information to you. Nevertheless, neither we nor our affiliates have participated in the preparation of, or verified, any information about the Underlying Stocks or any of the Underlying Stock Issuers. You, as an investor in the notes, should make your own investigation into the Underlying Stocks and the Underlying Stock Issuers. Neither the Underlying nor any of the Underlying Stock Issuers is involved in this offering in any way and none of them has any obligation of any sort with respect to your notes. The Underlying has no obligation to take your interests into consideration for any reason, including when taking any actions that would require the calculation agent to adjust the Share Adjustment Factor, which may adversely affect the value of your notes.

- **PAST PERFORMANCE OF THE UNDERLYING IS NO GUIDE TO FUTURE PERFORMANCE** — The actual performance of the Underlying over the term of the notes may bear little relation to the historical closing prices of the Underlying and/or the hypothetical examples set forth elsewhere in this pricing supplement. We cannot predict the future performance of the Underlying or whether the performance of the Underlying will result in the return of any of your investment.

- **ASSUMING NO CHANGES IN MARKET CONDITIONS AND OTHER RELEVANT FACTORS, THE PRICE YOU MAY RECEIVE FOR YOUR NOTES IN SECONDARY MARKET TRANSACTIONS WOULD GENERALLY BE LOWER THAN BOTH THE ISSUE PRICE AND THE ISSUER'S ESTIMATED VALUE OF THE NOTES ON THE TRADE DATE** — While the payment(s) on the notes described in this pricing supplement is based on the full Face Amount of notes, the Issuer's estimated value of the notes on the Trade Date (as disclosed on the cover of this pricing supplement) is less than the Issue Price of the notes. The Issuer's estimated value of the notes on the Trade Date does not represent the price at which we or any of our affiliates would be willing to purchase your notes in the secondary market at any time. Assuming no changes in market conditions or our creditworthiness and other relevant factors, the price, if any, at which we or our affiliates would be willing to purchase the notes from you in secondary market transactions, if at all, would generally be lower than both the Issue Price and the Issuer's estimated value of the notes on the Trade Date. Our purchase price, if any, in secondary market transactions would be based on the estimated value of the notes determined by reference to (i) the then-prevailing internal funding rate (adjusted by a spread) or another appropriate measure of our cost of funds and (ii) our pricing models at that time, less a bid spread determined after taking into account the size of the repurchase, the nature of the assets underlying the notes and then-prevailing market conditions. The price we report to financial reporting services and to distributors of our notes for use on customer account statements would generally be determined on the same basis. However, during the period of approximately six months beginning from the Trade Date, we or our affiliates may, in our sole discretion, increase the purchase price determined as described above by an amount equal to the declining differential between the Issue Price and the Issuer's estimated value of the notes on the Trade Date, prorated over such period on a straight-line basis, for transactions that are individually and in the aggregate of the expected size for ordinary secondary market repurchases.

In addition to the factors discussed above, the value of the notes and our purchase price in secondary market transactions after the Trade Date, if any, will vary based on many economic and market factors, including our creditworthiness, and cannot be predicted with accuracy. These changes may adversely affect the value of your notes, including the price you may receive in any secondary market transactions. Any sale prior to the Maturity Date could result in a substantial loss to you. The notes are not designed to be short-term trading instruments. Accordingly, you should be able and willing to hold your notes to maturity.

- **THE NOTES WILL NOT BE LISTED AND THERE WILL LIKELY BE LIMITED LIQUIDITY** — The notes will not be listed on any securities exchange. There may be little or no secondary market for the notes. We or our affiliates intend to act as market makers for the notes but are not required to do so and may cease such market making activities at any time. Even if there is a secondary market, it may not provide enough liquidity to allow you to sell the notes when you wish to do so or at a price advantageous to you. Because we do not expect other dealers to make a secondary market for the notes, the price at which you may be able to sell your notes is likely to depend on the price, if any, at which we or our affiliates are willing to buy the notes. If, at any time, we or our affiliates do not act as market makers, it is likely that there would be little or no secondary market in the notes. If you have to sell your notes prior to maturity, you may not be able to do so or you may have to sell them at a substantial loss, even in cases where the price of the Underlying has increased since the Trade Date.

- **MANY ECONOMIC AND MARKET FACTORS WILL AFFECT THE VALUE OF THE NOTES** — While we expect that, generally, the price of the Underlying will affect the value of the notes more than any other single factor, the value of the notes prior to maturity will also be affected by a number of other factors that may either offset or magnify each other, including:

- the expected volatility of the Underlying;

- the time remaining to the maturity of the notes;

- the market prices and dividend rates of the shares of the Underlying and the component securities held by the Underlying;

- the composition of the Underlying;

- the occurrence of certain events affecting the Underlying that may or may not require an anti-dilution adjustment;

- interest rates and yields in the markets generally;

- geopolitical conditions and economic, financial, political, regulatory or judicial events that affect the Underlying, the Tracked Index or the markets generally;

- supply and demand for the notes; and

- our creditworthiness, including actual or anticipated downgrades in our credit ratings.

During the term of the notes, it is possible that their value may decline significantly due to the factors described above even if the price of the Underlying remains unchanged from the Initial Price, and any sale prior to the Maturity Date could result in a substantial loss to you. You must hold the notes to maturity to receive the stated payout from the Issuer.

**TRADING AND OTHER TRANSACTIONS BY US, JPMORGAN CHASE & CO. OR OUR OR ITS AFFILIATES IN THE EQUITY AND EQUITY DERIVATIVE MARKETS MAY IMPAIR THE VALUE OF THE NOTES** — We or our affiliates expect to hedge our exposure from the notes by entering into equity and equity derivative transactions, such as over-the-counter options, futures or exchange-traded instruments. We, JPMorgan Chase & Co. or our or its affiliates may also engage in trading in instruments linked or related to the Underlying on a regular basis as part of our or their general broker-dealer and other businesses, for proprietary accounts, for other accounts under management or to facilitate transactions for customers, including block transactions. Such trading and hedging activities may adversely affect the price of the Underlying and, therefore, make it less likely that you will receive a positive return on your investment in the notes. It is possible that we, JPMorgan Chase & Co. or our or its affiliates could receive substantial returns from these hedging and trading activities while the value of the notes declines. We, JPMorgan Chase & Co. or our or its affiliates may also issue or underwrite other securities or financial or derivative instruments with returns linked or related to the Underlying. To the extent that we, JPMorgan Chase & Co. or our or its affiliates serve as issuer, agent or underwriter for such securities or financial or derivative instruments, our, JPMorgan Chase & Co.'s or our or its affiliates' interests with respect to such products may be adverse to those of the holders of the notes. Introducing competing products into the marketplace in this manner could adversely affect the price of the Underlying and the value of the notes. Any of the foregoing activities described in this paragraph may reflect trading strategies that differ from, or are in direct opposition to, investors' trading and investment strategies related to the notes.

- **WE, JPMORGAN CHASE & CO. OR OUR OR ITS AFFILIATES MAY PUBLISH RESEARCH, EXPRESS OPINIONS OR PROVIDE RECOMMENDATIONS THAT ARE INCONSISTENT WITH INVESTING IN OR HOLDING THE NOTES. ANY SUCH RESEARCH, OPINIONS OR RECOMMENDATIONS COULD ADVERSELY AFFECT THE PRICE OF THE UNDERLYING AND THE VALUE OF THE NOTES** — We, JPMorgan Chase & Co. or our or its affiliates may publish research from time to time on financial markets and other matters that could adversely affect the price of the Underlying and the value of the notes, or express opinions or provide recommendations that are inconsistent with purchasing or holding the notes. Any research, opinions or recommendations expressed by us, JPMorgan Chase & Co. or our or its affiliates may not be consistent with each other and may be modified from time to time without notice. You should make your own independent investigation of the merits of investing in the notes and the Underlying.

- **POTENTIAL CONFLICTS OF INTEREST** — We and our affiliates play a variety of roles in connection with the issuance of the notes, including acting as calculation agent, hedging our obligations under the notes and determining the Issuer's estimated value of the notes on the Trade Date and the price, if any, at which we or our affiliates would be willing to purchase the notes from you in secondary market transactions. In performing these roles, our economic interests and those of our affiliates are potentially adverse to your interests as an investor in the notes. The calculation agent will determine, among other things, all values, prices and levels required to be determined for the purposes of the notes on any relevant date or time. The calculation agent also has some discretion about certain adjustments to the Share Adjustment Factor and will be responsible for determining whether a market disruption event has occurred. Any determination by the calculation agent could adversely affect the return on the notes.

- **THE U.S. FEDERAL INCOME TAX CONSEQUENCES OF AN INVESTMENT IN THE NOTES ARE UNCERTAIN** — There is no direct legal authority regarding the proper U.S. federal income tax treatment of the notes, and we do not plan to request a ruling from the IRS. Consequently, significant aspects of the tax treatment of the notes are uncertain, and the IRS or a court might not agree with the treatment of the notes as prepaid financial contracts that are not debt. If the IRS were successful in asserting an alternative treatment for the notes, the tax consequences of ownership and disposition of the notes could be materially and adversely affected.

Even if the treatment of the notes as prepaid financial contracts is respected, purchasing a note could be treated as entering into a "constructive ownership transaction." In that case, all or a portion of any long-term capital gain you would otherwise recognize on the taxable disposition of the note would be recharacterized as ordinary income to the extent such gain exceeded the "net underlying long-term capital gain," and a notional interest charge would apply with respect to the deemed tax liability that would have been incurred if such income had accrued at a constant rate over the period you held the note.

As described above under "Tax Consequences," in 2007 the U.S. Treasury Department and the IRS released a notice requesting comments on various issues regarding the U.S. federal income tax treatment of "prepaid forward contracts" and similar instruments. Any Treasury regulations or other guidance promulgated after consideration of these issues could materially and adversely affect the tax consequences of an investment in the notes, possibly with retroactive effect. You should review carefully the section of the accompanying product supplement entitled "U.S. Federal Income Tax Consequences," and consult your tax adviser regarding the U.S. federal tax consequences of an investment in the notes (including possible alternative treatments, the potential applie to a decrease in the bonuses we pay based on our operating results. The decrease in such bonuses also led to a decrease in the overall costs of our welfare benefits. - Materials and supplies. Our materials and supplies expenses consist mainly of fuel, water and electricity expenses. In 2003, our material and supplies expenses amounted to RMB217.0 million, representing an increase of 13.0% from RMB192.1 million in 2002. This increase was mainly due to an increase in the prices of diesel oil and other fuels used by locomotives, which was caused by a rise in the prices of petroleum products. Our consumption of water and electricity also increased significantly because of the additional ventilation systems and disinfection equipments we installed in our stations and on board our trains and an increase in the frequency of the cleaning and disinfecting of public areas during the SARS period. In addition, the operation of the additional Hong Kong through- 34 trains and the high-speed passenger trains between Guangzhou and Shenzhen also increased our consumption of materials, water and electricity. - Depreciation. In 2003, depreciation expenses relating to our fixed assets were RMB290.0 million, representing a decrease of 13.6% from RMB335.5 million in 2002. This decrease was mainly due to an extension of the estimated useful life of a portion of our fixed assets. We re-estimated the useful life and the depreciation rate of part of its fixed assets in 2003 based on the experience and maintenance program established by our management and engineering personnel, which decreased depreciation expenses relating to our fixed assets in 2003. See note 13 to our audited financial statements included elsewhere in this annual report. - Repair. In 2003, our repair expenses were RMB89.6 million, representing a decrease of 12.5% from RMB102.4 million in 2002. This decrease was mainly due to a decrease in the repair expenses relating to our buildings in 2003. We also undertook the repair work of some locomotives and vehicles formerly outsourced to other factories. Completion of the improvement work at passenger stations along the Guangzhou Shenzhen route in 2002 also contributed to a decrease in our related expenses in 2003. - Equipment leases and services. Our expenses on equipment leases and services mainly consist of railway line usage fees, train hauling fees and train leasing fees paid to other railway administrations. In 2003, our expenses on equipment leases and services were RMB437.7 million, representing an increase of 0.9% from RMB433.9 million in 2002. This increase was mainly due to the operation of additional Hong Kong through-trains and the high-speed passenger trains between Guangzhou and Shenzhen in 2003. We also leased more trucks from the MOR in 2003, resulting in an increase in the leasing fees we paid to the MOR. - Social services. These fees relate to services provided to our employees, including health care and education and to services relating to passenger safety and security. In 2003, our fees for social services were RMB62.6 million, representing an increase of 9.0% from RMB57.4 million in 2002. This increase was mainly due to the additional medical and sterilization services we implemented during the SARS epidemic. - General and administrative. Our general and administrative expenses were RMB134.7 million in 2003, representing an increase of 8.8% from RMB123.8 million in 2002. This increase was mainly due to a growth in payment for pensions. The pensions were calculated based on the aggregate amount of our employees' salaries for the previous year. As the aggregate amount of our employees' salaries in 2002 was higher than those in 2001, our expenses for pensions in 2003 increased. - Other expenses. In 2003, our other expenses amounted to RMB113.4 million, representing an increase of 11.9% from RMB101.3 million in 2002. PROFIT FROM OPERATIONS Our profit from operations decreased by 9.6% from RMB622.5 million in 2002 to 35 RMB562.7 million in 2003 due to a decrease in our total revenues. TAXATION As we are registered and established in the Shenzhen Special Economic Zone, our railroad businesses are subject to income tax at a rate of 15%. According to relevant tax regulations, our other businesses and our subsidiaries are subject to income tax at the rate of either 15% or 33%, depending on the location of incorporation. In addition, a member of our subsidiaries engaged in other businesses are Sino-foreign joint ventures which are entitled to full exemption from the PRC income tax for two years and a 50% reduction in the next three years starting from the first profit-making year, after offsetting available tax losses carried forward from prior years. Our income tax expense was RMB93.4 million in 2003, representing an effective tax rate of 15.4% and a decrease of RMB11.0 million compared to RMB104.4 million in 2002. NET PROFIT Our consolidated net profit decreased by 8.1% from RMB557.1 million in 2002 to RMB511.8 million in 2003. YEAR ENDED DECEMBER 31, 2002 COMPARED WITH YEAR ENDED DECEMBER 31, 2001 REVENUES In 2002, our total revenues were RMB2,517.5 million, representing an increase of 16.9% from RMB2,153.6 million in 2001. Revenues from passenger transportation service, freight transportation service and other businesses accounted for 73.4%, 20.4% and 6.2% of our 2002 total revenues respectively. Revenues from passenger transportation service and freight transportation service accounted for 78.2% and 21.8% of our 2002 revenues from railway businesses, respectively. Passenger transportation service. In 2002, passenger transportation experienced significant growth. The revenues from the passenger transportation business were RMB1,846.6 million in 2002, representing an increase of 29.5% from RMB1,426.0 million in 2001. The sharp increase in revenues from passenger transportation was due primarily to the full-year operation of our Shenzhen-Yueyang and Shenzhen-Beijing long-distance passenger trains (as compared to 2001, when these trains operated for less than half the year) and the completion of our "As-Frequent-As-Buses" Train Project between Guangzhou and Shenzhen in 2002. Since January

2002, we have been operating 54 pairs of high speed trains and 4 pairs of regular speed trains, with high speed trains accounting for more than 93% of the total. The per passenger ticket price of long distance trains is two to four times the price of the Guangzhou Shenzhen high speed trains, and the ticket price of the Guangzhou Shezhen high-speed trains is double the price of regular speed trains. As a result of the increase in the number of high-speed trains and long-distance trains operating in 2002 compared to 2001, our revenue per passenger increased by 26.4% from RMB36.7 in 2001 to RMB46.4 in 2002. 36 In 2002, we operated an average of 99 pairs of passenger trains per day on the Guangzhou Shenzhen route, of which seven pairs were the Hong Kong through trains between Guangzhou and Kowloon, 54 pairs were high-speed trains between Guangzhou and Shenzhen, four pairs were regular speed trains between Guangzhou and Schenzhen and 34 pairs were long-distance trains. The total number of passengers increased by 2.4% from approximately 38.8 million in 2001 to approximately 39.8 million in 2002. Freight transportation. In 2002, our freight transportation revenues were RMB514.0 million, representing a decline of 9.4% from RMB567.3 million in 2001. The decline was primarily due to the intense competition from other modes of transportation. Total freight tonnage was approximately 27.6 million tons, representing a 4.9% decrease from approximately 29.0 million tons in 2001. - Our outbound freight revenue increased by 2.4% from RMB92.1 million in 2001 to RMB94.26 million in 2002. The increase in outbound freight transportation revenue was mainly due to higher transportation volume generated by freight price discounts. These decreased prices helped us to maintain our existing customers and attract some new freight customers. Furthermore, we enhanced our relationships with ports, mines and factories, and strengthened our efforts in directing certain freight from ocean shipments to our railway, which also contributed to the increase in transportation volume. Outbound freight tonnage increased by 7.2% from approximately 6.8 million tons in 2001 to approximately 7.3 million tons in 2002. - Our inbound and pass through freight revenue decreased by 8.5% from RMB271.2 million in 2001 to RMB 248.1 million in 2002. The decline was mainly caused by the construction of the second track on the Beijing Jiujiang line and the national railway re-routing that decreased the volume of inbound and pass through freight transportation. Furthermore, there was a decline in the amount of goods being shipped to Shenzhen from other parts of China due to an increase of imported goods from overseas. In 2002, our inbound and pass through freight transportation volume was approximately 20.3 million tons, representing a decline of 8.6% from approximately 22.2 million tons in 2001. - Our revenue from storage, loading, unloading and other miscellaneous items of freight services decreased by 15.8% from RMB204.0 million in 2001 to RMB171.7 million in 2002. The decrease was mainly due to the drop in freight price discounts and the reduction of storage and loading charges. The following table sets forth the revenues from freight transportation and the volumes of commodities shipped for the three years ended December 31, 2002: YEAR ENDED DECEMBER 31, ------------------------------ CHANGE FROM 2000 2001 2002 2001 ---- ---- ---- ---- Revenue from freight transportation (RMB thousands)........................................................ 549,694 567,276 514,036 (9.4%) Total freight tons (thousands of tons)........................................ 28,733 29,012 27,583 (4.9%) 37 YEAR ENDED DECEMBER 31, ----------------------------- CHANGE FROM 2000 2001 2002 2001 ---- ---- ---- ---- Revenue per ton (RMB).......................................................... 19.13 19.55 18.64 (4.7%) Total ton-kilometers (millions)................................................ 2,071.6 2,082.5 1,926.0 (7.5%) Revenue per ton-kilometer (RMB)................................................ 0.27 0.27 0.27 - Other Businesses. Revenues from our other businesses decreased by 2.1% from RMB160.3 million in 2001 to RMB156.9 million in 2002. The decline was due primarily to increased train frequency and higher train speeds that reduced passengers' consumption of food and beverages both on-board and in railway stations. In addition, the subway construction outside Shenzhen Station also affected the number of customers dining at our station restaurants. The table below sets forth a breakdown of the revenues from different categories of our other businesses for the three years ended December 31, 2002: YEAR ENDED DECEMBER 31, ---------------------------------------- 2000 2001 2002 ---- ---- ---- (RMB THOUSANDS) On-board and station sales........................................................ 58,030 51,627 40,977 Station services.................................................................. 65,934 41,287 43,913 Tourism, advertising and others................................................... 69,451 67,392 72,003 ------- ------- ------- Total......................................................................... 193,415 160,306 156,893 ======= ======= ======= Operating Expenses. In 2002, our total operating expenses were RMB1,895.0 million, representing an increase of 18.5% from RMB1,599.5 million in 2001. This was due mainly to an increase in railway operating expenses. Railway Operating Expenses. Our total railway operating expenses increased by 18.8% from RMB1,460.6 million in 2001 to RMB1,735.3 million in 2002. Details are as follows: - Labor and benefits. In 2002, our labor and benefits expenses amounted to RMB373.8 million, representing an increase of 16.6% from RMB320.6 million in 2001. The rise in labor and benefits expenses was mainly due to the increase in the number of employees resulting from the operation of two additional long-distance trains and the more frequent train service along the Guangzhou-Shenzhen route, as well as an increase in the average salaries of our employees. The number of our employees increased to 9,258 as of December 31, 2002 from 9,132 as of December 31, 2001. Moreover, our efforts to link compensation with our employees' performance also increased the overall salary and welfare expenses in 2002. - Materials and supplies. Materials and supplies consisted of fuel, water and electricity. In 2002, our materials and supplies expenses amounted to RMB192.1 million, representing an increase of 32.8% from RMB144.7 million in 2001. The higher expenses were mainly caused by the increase in materials consumption resulting from the full year operation of the eight newly operated "Blue Arrow" electric trains that were part of our "As-Frequent-As-Buses" Train Project that we leased in the second half of 2001 and the two additional long-distance passenger trains that operated throughout 2002. The higher frequency of train service on the 38 Guangzhou-Shenzhen route, the increased number of pairs of electric trains and the shift to electricity power on some freight trains also added to the materials and supplies expenses. - Depreciation. In 2002, depreciation expenses of fixed assets were RMB335.5 million, representing a 2.0% decrease from RMB342.5 million in 2001. The decrease in depreciation expenses was mainly due to our contribution of RMB120.6 million of telecommunication assets and certain related construction-in-progress to China Railcom. The depreciation associated with these assets of approximately RMB11.1 million was no longer reflected in our audited consolidated financial statements, thus reducing our depreciation expenses in 2002. - Repair expenses. In 2002, repair expenses amounted to RMB102.4 million, representing an 8.3% increase from RMB94.6 million in 2001. The increase was mainly due to the full year operation of two new long-distance trains that commenced operation in the second half of 2001 and the full year operation of the "As-Frequent-As-Buses" Train Project on the Guangzhou-Shenzhen route. In addition, efforts to improve both passenger and freight transportation facilities along the Guangzhou-Shenzhen route also increased repair expenses. - Equipment leases and services. In 2002, expenses on equipment leases and services amounted to RMB433.9 million, representing a 65.4% increase from RMB262.3 million in 2001. The substantial increase of such expenses in 2002 was mainly due to the full year operation of two new long-distance trains (Shenzhen-Yueyang and Shenzhen-Beijing) which significantly increased the expenditures paid to other railway companies for railway line usage and train hauling expenses. Furthermore, the full year operation of the eight high-speed electric trains leased from Guangzhou Zhong Che Rolling Stock Sales and Leasing Company also increased leasing expenses significantly. - Fees for social services. Fees for social services are paid for services provided to our employees, including health care and education and for services relating to passenger safety and security. In 2002, fees for social services were RMB57.39 million, representing an increase of 0.4% from RMB57.16 million in 2001. The increase was due primarily to the fees paid for passenger safety and security on our two new long-distance passenger trains. - General and administrative expenses. General and administrative expenses in 2002 were RMB123.8 million, representing a decrease of 17.6% from RMB150.2 million in 2001. The decrease was due primarily to the significant drop in the provision for bad debts in 2002, and to the decrease in losses from bad debts from RMB29.6 million in 2001 to RMB4.6 million in 2002. In 2002, we improved our receivables collection by managing and clearing outstanding accounts receivable. As a result, our accounts receivable dropped significantly. - Other expenses. In 2002, other expenses amounted to RMB101.3 million, representing an increase of 38.2% from RMB73.2 million in 2001. The increase in 39 other expenses was due to the addition of two long-distance trains and the full year operation of the "As-Frequent-As-Buses" Train Project on the Guangzhou-Shenzhen route, which increased various direct costs. Since we contributed our telecommunication assets into China Railcom, we started to pay for telecommunication services provided by China Railcom, which increased our expenses for telecommunication services. PROFIT FROM OPERATIONS Our profit from operations increased by 12.3% from RMB554.1 million in 2001 to RMB622.5 million in 2002, principally driven by the increase in operating profit from railroad businesses from RMB532.7 million in 2001 to RMB625.3 million in 2002, which was offset slightly by a decrease in operating profit of our other businesses from RMB21.5 million in 2001 to an operating loss of RMB2.8 million in 2002. TAXATION As we are registered and established in the Shenzhen Special Economic Zone, our railroad businesses are subject to income tax at a rate of 15%. According to relevant tax regulations, our other businesses and our subsidiaries are subject to income tax at the rate of either 15% or 33%, depending on the location of incorporation. Taxes payable by us and our subsidiaries were RMB104.4 million in 2002, implying an actual tax rate of 15.7%. Income tax expense of RMB104.4 million in 2002 increased by RMB5.0 million over RMB99.4 million in 2001, which was due to the growth of profits before tax. NET PROFIT Our consolidated net profit increased from RMB533.5 million in 2001 to RMB557.1 million in 2002, representing an increase of 4.4%. CRITICAL ACCOUNTING POLICIES AND ESTIMATES Our audited consolidated financial statements have been prepared in accordance with IFRS. Our principal accounting policies are set out in Note 2 to our audited consolidated financial statements. IFRS requires that we adopt the accounting policies and estimation techniques that are most appropriate in the circumstances for the purpose of giving a true and fair view of our results and financial condition. We based our estimates and judgments on historical experience and on various other assumptions we deem reasonable under relevant circumstances. However, different policies, estimation techniques and assumptions in critical areas could lead to materially different results, in particular, with respect to fixed assets, receivables, provision and impairments discussed in the following paragraphs. FIXED ASSETS The railway industry is capital intensive. Under IFRS, fixed assets are initially recorded at cost less accumulated depreciation and impairment loss. Cost represents the purchase price of the asset and other costs incurred to bring the asset into existing use and subsequent to the initial recognition, fixed assets are stated at cost or valuation less accumulated depreciation and impairment losses. Independent valuations, on a market value basis or depreciated replacement 40 cost basis when there is no evidence of market value for such an item, are performed at least every five years or sooner if considered necessary by the directors. In the intervening years, the directors review the carrying values of the fixed assets and an adjustment is made where there has been a material change. Repairs and maintenance are charged to our income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Group. Major renovations are depreciated over the remaining useful life of the related asset. Estimation of the useful lives of assets that are long-lived as well as their salvage values requires significant management judgment. Depreciation is calculated using the straight-line method to write off the cost or revalued amount, after taking into account the estimated residual value of 4% to 10% of cost, of each asset over its estimated useful life. Our management reassessed the estimated useful lives and depreciation rates of fixed assets periodically. The assessment was based on the experience and maintenance program established by the management and the engineering personnel, current operations and potential changes in technology, personnel, estimated salvage value of assets, and industry regulations. Effective from 1 January, 2003, we changed the estimated useful lives of our track, bridges and service roads from 44 years to a range from 55 years to 100 years and changed the useful lives of our locomotives and rolling stock from 16 years to 20 years. The effect of such change of accounting estimates to our consolidated income statement for the year ended 31 December 2003 is set out in Note 13 to our audited financial statements includes elsewhere in this annual report. The estimated useful lives of our fixed assets are as follows: Buildings 25 to 40 years Leasehold improvements over the lease terms Track, bridges and service roads 55 to 100 years Locomotives and rolling stock 20 years Communications and signaling systems 8 to 20 years Other machinery and equipment 7 to 25 years Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Due to the capital intensive nature of our business and the large base of depreciable assets, variances to those estimates could have a material effect on our Consolidated Financial Statements. If the estimated useful lives of all depreciable assets were increased by one year, annual depreciation expense would decrease by RMB16.3 million. If the estimated useful lives of all assets to be depreciated were decreased by one year, annual depreciation expense would increase by RMB19.9 million. RECEIVABLES Receivables are carried at original invoice amount less the provision made for impairment of these receivables. A provision for impairment of receivables is established when there is an objective evidence that we will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying 41 amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for similar borrowers. Other receivables are also assessed for incollectibility when the circumstances indicate that we might not be able to collect all amounts due according to the original terms of receivables. IMPAIRMENTS If circumstances indicate that the net book value of an asset or investment may not be recoverable, this asset may be considered "impaired", and an impairment loss may be recognized in accordance with IFRS 36 "Impairment of Assets". We review the carrying amounts of long-lived assets periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. We test these assets for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to the estimated recoverable amount. The amount of impairment loss is the difference between the carrying amount of the asset before the reduction and the estimated recoverable amount. The recoverable amount is the greater of the estimated net selling price and the value in use. It is difficult to precisely estimate selling prices because quoted market prices for our assets are often not readily available. In determining the value in use, we discount cash flows that we expect the asset to generate to their present value. Determining cash flows that we expect an asset to generate requires significant judgment relating to the expected level of sales volume, selling prices and the amount of operating costs. CONTINGENCY An accrual for a loss contingency is established if information available prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred or an asset has been impaired. Judgment is necessary in assessing the likelihood that a pending claim will succeed or a liability will arise. The estimates of whether an accrual is necessary have been developed in consultation with our outside counsel based upon an analysis of potential results. ITEM 5B. LIQUIDITY AND CAPITAL RESOURCES Our principal source of capital has been cash flow from operations, and principal uses of capital are to fund capital expenditures, investment and payment of taxes and dividends. We generated approximately RMB798.4 million of net cash flow from operating activities in 2003. Substantially all of our revenues were received in cash, with accounts receivable arising primarily from long-distance passenger and pass-through freight transactions originating from other railway companies whose lines connect to our railroad. Similarly, some accounts payable arise from payments for railroad transportation services that we collect on behalf of other railroad companies. Accounts receivable and payable were generally settled either quarterly or monthly between us and the other railroad companies. Most of our revenues 42 generated from other businesses were received in cash. We also have accounts payable associated with the purchase of materials and supplies in our other businesses. In 2003, other than operating expenses, our cash outflow mainly related to the following: - capital expenditures of approximately RMB306.0 million, representing a decrease of 2.8% from RMB535.0 million in 2002 (see "Item 4D. Property, Plant and Equipment" for a description of these capital expenditures); and - payment of dividends of approximately RMB433.6 million. Funds not required for immediate use are kept in short and medium-term investments and bank deposits. We had temporary cash investments of approximately RMB627.4 million as of December 31, 2003 and cash and cash equivalents of RMB1,402.4 million. As of 31 December, 2003, we had a fixed deposit of approximately RMB31.4 million in Zeng Cheng City Li Cheng Credit Cooperative, or "Li Cheng." We were unable to recover the principal from Li Cheng upon the expiry of the fixed deposit term. In March 1999, we instituted legal proceedings against Li Cheng to recover the deposit and the related interest. According to a court verdict dated 12 October, 1999, Li Cheng was required to repay the deposit principal and the related interest to us. Li Cheng failed to comply with the court ruling, and we further applied to the court for compulsory enforcement of the court order. In July 2000, Li Cheng filed a court petition for winding up. On 9 November, 2000, the court ordered the suspension of execution of the court ruling dated 12 October, 1999 during the winding-up of Li Cheng. On 23 November, 2000, we applied to the Guangdong Provincial Government for an allocation of funds by the government to Li Cheng for the repayment of our deposit principal. The provincial government accepted our petition and requested the municipal government to follow up on our case. As of December 31, 2003, we have not collected our fixed deposit. Accordingly, this amount is classified as other receivables and accounted for as part of our provision for doubtful accounts according to management's estimates. As of December 31, 2003, we did not have any bank loans or guarantees outstanding nor any trust deposits placed with any financial institutions in the PRC. CASH FLOW Our cash and cash equivalents in 2003 decreased by approximately RMB10.7 million over 2002 primarily due to the negative impact of SARS on sales. The table below sets forth the major items in the consolidated cash flow statements for 2002 and 2003 and the percentage change from 2002 to 2003. 43 YEAR ENDED DECEMBER 31, -------------------------------- CHANGE 2002 2003 FROM 2002 ---- ---- --------- (RMB THOUSANDS) Net cash generated from operating activities............................................................... 1,157,177 798,449 (31%) Net cash from/(used in) investing activities.................................. 251,003 (375,469) (250%) Net cash (used in) financing activities....................................... (360,643) (433,666) (20%) --------- -------- Net increase/(decrease) of cash and cash equivalents......................................................... 1,047,537 (10,686) (101%) ========= ======== ==== Our net cash generated from operating activities in 2003 was approximately RMB798.4 million, representing a decrease of RMB358.8 million from RMB1,157.2 million in 2002. The decrease resulted primarily from a decrease in cash flow generated from our passenger transportation business. Our working capital increased from RMB1,631.4 million in 2002 to RMB1,898.7 in 2003. The decrease was mainly due to the accrued expense decrease resulted from the house reform project completed. Our net cash used in investing activities was approximately RMB375.5 million in 2003, as compared to net cash provided by investing activities of RMB251.0 million in 2002. Cash used in investing activities in 2003 mainly included the purchase of fixed assets and payments for construction-in-progress. The net cash provided by investing activities in 2002 was mainly due to the company reduced the temporary cash investment by RMB777.09 million, while the temporary cash investment was increased by RMB60.1 million in 2003. Net cash used in financing activities in 2003 was approximately RMB433.7 million, representing an increase of RMB73.0 million from RMB360.6 million in 2002. It consisted of a dividend payment of RMB433.6 million to shareholders of the Company and distribution to minority shareholders of approximately RMB0.1 million. ITEM 5C. RESEARCH AND DEVELOPMENT, PATENTS AND LICENCES, ETC. We do not generally conduct our own research and development with respect to major capital projects. In the past, in connection with the high-speed project and electrification, our Parent Company has contracted for the engineering and technical services of research and design institutes under the Ministry of Railways. Since our inception, our Parent Company has not borne any research and development expenses on our behalf. We conduct limited research and development in designing and implementing automation in ticket sales, including the development of related computer software. We do not anticipate a significant need for research and development services in the foreseeable future, and do not expect to require any such services in connection with our other businesses. To the extent that these services are needed, we expect to contract outside service providers to satisfy this need. In connection with major engineering and construction projects, as well as major equipment acquisitions, we intend to conduct technical research and feasibility studies with relevant engineering service organizations, so as to ensure the cost-effectiveness of 44 our capital expenditures. ITEM 5D. TREND INFORMATION The Pearl River Delta has been one of China's fastest growing economic regions. We expect the PRC government's current economic, import and export, foreign investment and infrastructure policies to generate additional demand for transportation services generally. These policies and measures may have both positive and negative effects on our business development. They are expected to promote economic growth and create new demand for our transportation services. At the same time, however, with the improvement of highway and waterway transportation facilities, we anticipate additional competition. Due to the SARS epidemic, we experienced a significant decrease in passenger traffic in the first half of 2003. A similar outbreak of SARS or other epidemic in the future is likely to have a material adverse effect on our operating results and financial condition. We believe that while the PRC government is in the progress of lessening restrictions on foreign investment following China's entry into the WTO, the opening up of domestic railway transportation will be gradual and we expect due to competition from foreign and domestic railway to be limited in the short term. China's entry into the WTO may increase other Chinese coastal cities' significance in trading. As a result, part of the freight currently transferred through ports in Hong Kong and Shenzhen may be divested to other ports in the PRC, which will adversely affect our railway freight business. In addition, as the PRC government lifts control over foreign investments, including allowing foreign participation in railway construction, our railway monopoly position in our service region may be challenged by foreign strategic investment. We believe that we are prepared for the challenges as well as the opportunities that have arised or will arise with China's accession to the WTO. With increasing economic cooperation in regional economies of the "Great Pearl River Delta" and the "Extensive Pearl River Delta", and the implementation of the Mainland and Hong Kong Closer Economic Partnership Arrangement, or "CEPA", we expect our service territory to experience a rapid and sustained economic growth. In addition, we also expect domestic policies and developments, such as the "Fifth Great Speed Up in Chinese Railways," the "Relaxed Individual Travel to Hong Kong and Macao Special Administrative Region," the commencement of operation of the Shenzhen Subway and improvement in the Guangzhou Subway to have a positive impact on our passenger and freight transportation businesses in 2004. ITEM 5E. OFF-BALANCE SHEET ARRANGEMENTS There are no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors. ITEM 5F. TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS The following table sets forth our contractual obligations, capital commitments and operating lease commitments as of December 31, 2003 for the periods indicated. 45 CONTRACTUAL OBLIGATIONS PAYMENTS DUE BY PERIOD PAYMENT DUE BY PERIOD (RMB in thousands) 2009 AND CONTRACTUAL OBLIGATIONS TOTAL 2004 2005 2006 2007 2008 THEREAFTER Long-Term Debt Obligations - - - - - - - Capital (Finance) Lease Obligations - - - - - - - Operating Lease Obligations 291,375 108,000 108,000 75,375 - - - Purchase Obligations - - - - - - - Other Long-Term Liabilities Reflected - - - - - - - on the Company's Balance Sheet under IFRS Total 291,375 108,000 108,000 75,375 - - - We plan to implement the following development projects in 2004: - We plan to increase our overall transportation capacity, including the construction of a fourth line between Guangzhou and Shenzhen, a technical support and maintenance depot for passenger vehicles at Northern Shenzhen Station, an auxiliary station in Buji for long-distance passenger trains and a connecting track for passenger trains from Pinghu to Shenzhen. - In our passenger transportation business, we plan to: (i) further improve our "As-Frequent-As-Buses" Train Project of the Guangzhou-Shenzhen high-speed passenger trains by increasing the frequency of our high-speed train services and appropriately adjusting the stops at intermediary stations based on passenger demand; (ii) conduct feasibility studies on the introduction of advanced electric passenger trains and the IC Card Ticketing System; (iii) continue the integrated refurbishment of our stations and improve our passenger service facilities and enhance our service quality; and (vi) continue the expansion of our through-train business between Guangdong Province and Hong Kong. We commenced the operations of two pairs of Hong Kong through-trains on April 18, 2004. - In our freight transportation business, we plan to: (i) increase our marketing efforts and enhance our cooperation with key ports, mines, factories and corporate entities; (ii) continue to improve our service quality and efficiency; (iii) commence the operation of "5 fixed" (fixed location, fixed line, fixed time, fixed price and fixed schedule) freight train services in southwest China. - We also plan to maintain a tight control over our working capital and to achieve low-cost expansion through equity investments, mergers and acquisitions when appropriate opportunities arise. We may be unable to obtain sufficient financing to fund our substantial capital requirements, which could limit its growth potential. We estimate that we will require approximately RMB1,550.0 million for capital expenditures in 2004, mainly including the construction of our fourth track between Guangzhou and Shenzhen, the construction of a technical support and maintenance depot in northern Shenzhen, the purchase of additional 46 locomotives and trains. Our actual capital requirements may be greater. We may not be able to obtain sufficient funds on commercially acceptable terms. If adequate capital is not available, our planned capital expenditure and business prospects could be adversely affected. ITEM 5G. ADDITIONAL INFORMATION PRINCIPAL DIFFERENCES BETWEEN IFRS AND US GAAP Our audited consolidated financial statements conform to IFRS, which differ in certain respects from those prepared under US GAAP. A major difference between IFRS and US GAAP, which has a significant effect on our consolidated net profit and consolidated net assets is set out below: REVALUATION OF FIXED ASSETS In connection with the restructuring undertaken for our initial public offering, we revalued our fixed assets on March 6, 1996 and we recorded a revaluation surplus of fixed assets amounting to approximately RMB1.5 billion. We carried out a further revaluation as of September 30, 2002, which did not result in a material difference from the carrying amounts and no revaluation surplus or deficit was recorded. See note 13 to our audited financial statements included elsewhere in this annual report. Under IFRS, revaluation of fixed assets is permitted and depreciation is based on the revalued amount. Additional depreciation arising from the revaluation surplus was approximately RMB38.5 million for the year ended December 31, 2003 compared to approximately RMB48.4 million in 2002. Under US GAAP, fixed assets are required to be stated at their original cost. Hence, no additional depreciation from revaluation will be recognized under US GAAP. However, a deferred tax asset related to the revaluation surplus amounting to approximately RMB223.8 million was created under US GAAP with a corresponding increase in equity since the revaluation resulted in a higher tax base which will be realized through additional depreciation for PRC tax purposes. The effects on our consolidated net profit resulting from the significant differences between IFRS and US GAAP are summarized below: YEAR ENDED DECEMBER 31, ---------------------------------------------------- 2001 2002 2003 2003 ---- ---- ---- ---- RMB IN RMB IN RMB IN US$(1) IN THOUSANDS THOUSANDS THOUSANDS THOUSANDS (Unaudited) Net profit under IFRS.......................................... 533,495 557,083 511,762 61,807 US GAAP adjustments: Reversal of additional depreciation charges arising from the revaluation surplus on fixed assets.......................................... 48,422 48,422 38,548 4,655 Effect of US GAAP adjustment on taxation.................... (7,263) (7,263) (5,782) (698) ------- ------- ------- ------ Consolidated net profit under US GAAP............................ 574,654 598,242 544,528 65,764 ======= ======= ======= ====== Earnings per share under US GAAP................................ 0.13 0.14 0.13 0.02 ======= ======= ======= ====== 47 Earnings per equivalent ADS under US GAAP.................................................. 6.63 6.90 6.28 0.76 ==== ==== ==== ==== -------------- (1) Translated solely for the convenience of the reader into U.S. dollars at the noon buying rate prevailing on December 31, 2003 of US$1.00 to RMB8.28. The effects on our consolidated net assets resulting from the significant differences between IFRS and US GAAP are summarized below: YEAR ENDED DECEMBER 31, --------------------------------------------- 2002 2003 2003 ---- ---- ---- RMB IN RMB IN US$(1) IN THOUSANDS THOUSANDS THOUSANDS (Unaudited) Consolidated net assets under

IFRS...................................... 10,244,151 10,322,358 1,246,662 US GAAP adjustments: Reversal of the revaluation surplus on fixed assets............... (1,492,185) (1,492,185) (180,216) Reversal of additional depreciation charges arising from the revaluation surplus on fixed assets.............................. 330,884 369,432 44,617 Deferred tax assets created....................................... 174,195 168,413 20,340 --------- --------- --------- Consolidated net assets under US GAAP.................................... 9,257,045 9,368,018 1,131,403 ========= ========= ========= --------------- (1) Translated solely for the convenience of the reader into U.S. dollars at the noon buying rate prevailing on December 31, 2003 of US$1.00 to RMB8.28. There are no significant differences between IFRS and US GAAP that would affect the classification in the balance sheet and the income statement that would not also affect our net income or shareholders' equity. RECENTLY ISSUED U.S. ACCOUNTING STANDARDS In 2003, the Financial Accounting Standards Board, or "FASB", issued Statement of Financial Accounting Standards No.150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity, or "SFAS 150", and FASB Interpretation No.46, Consolidation of Variable Interest Entities, or "FIN 46". SFAS 150 established standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that issuer classify a financial instrument that is within its scope as liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. Some of the 48 provisions of this Statement are consistent with the current definition of liabilities in FASB Concepts Statement No.6, Elements of Financial Statements. The remaining provisions of this Statement are consistent with the Board's proposal to revise that definition to encompass certain obligations that a reporting entity can or must settle by issuing its own equity shares, depending on the nature of the relationship established between the holder and the issuer. In addition, SFAS 150 concludes the first phase of the Board's redeliberations of the Exposure Draft, Accounting for Financial Instruments with Characteristics of Liability, Equity, or Both. SFAS 150 is effective for financial instruments entered into or modified after 31 May, 2003, and otherwise is effective at the beginning of the first interim period beginning after 15 June, 2003, except for mandatorily redeemable financial instruments of non-public entities. We do not expect that the adoption of SFAS 150 will any material impact on our financial statements. FIN 46 provides guidance on the identification of and financial reporting for entities over which controls is achieved through means other than voting rights. This interpretation requires existing unconsolidated variable interest entities to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. FIN 46 applies immediately to variable interest entities created after 31 January, 2003, and to variable interest entities in which an enterprise obtains an interest after the date. It applies in the first fiscal year or interim period beginning after 15 June, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before 1 February, 2003. We do not expect that the adoption FIN 46 will have any material impact on our financial statements. 49 ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES ITEM 6A. DIRECTORS AND SENIOR MANAGEMENT DIRECTORS All of our directors were duly elected at meetings of our shareholders. At our general shareholders' meeting held on June 10, 2004, Mr. Wilton Chau was elected as a director of our Company. The business address of each of our directors is No. 1052 Heping Road, Shenzhen, People's Republic of China 518010. The table below sets forth the information relating to our directors: DATE FIRST ELECTED OR NAME AGE POSITION APPOINTED ---- --- -------- --------- Wu Junguang 55 Chairman of the Board of Directors 2003 Feng Qifu 55 Director and General Manager 2003 Hu Lingling 40 Director 2003 Wu Houhui 55 Director 1999 Wen Weiming 41 Director 2003 Li Qingyun 40 Director and Deputy General Manager 2000 Li Peng 57 Director and Chairman of the Trade Union 1998 Chang Loong Cheong 58 Director 1996 Deborah Kong 44 Director 1996 Wilton Chau 42 Director 2004 Wu Junguang, age 55, was elected the chairman of the board of directors of Guangshen Railway on June 10, 2003. Mr. Wu graduated from South China Normal University. Since 1964, Mr. Wu has served in various managerial positions including general manager of Yangcheng Railway Company and our predecessor, Guangzhou Railway Sub-administration. Mr. Wu has served as the general manager of our Parent Company since April 2002 and as the chairman of our Parent Company since June 2003. Feng Qifu, age 55, was elected a director of Guangshen Railway in 2003 and is currently our general manager. Mr. Feng is an economist and graduated from the Party's School of Guangdong Provincial. He has over 30 years of experience in the railway industry. Since 1993, Mr. Feng has served as the general manager of the Changsha Railway Company and as the assistant to the general manager and the deputy general manager of our Parent Company. Mr. Feng was appointed our general manager on May 8, 2003. Hu Lingling, age 40, was elected a director of Guangshen Railway in 2003. Mr. Hu is an engineer and graduated from Changsha Railway Institute. Mr. Hu has served as the deputy chief engineer, the deputy stationmaster of Shaoguan Railway station of Yangcheng Railway Company, the deputy chief engineer, the deputy general manager of Yangcheng Railway Company and the director of the transportation department of our Parent Company Chronologically. Presently he serves as the deputy general manager of our Parent Company. 50 Wu Houhui, age 55, was elected a director of Guangshen Railway in 1999. He is a graduate of Dalian Railway College and a senior economist. Mr. Wu served in various managerial position, including the position of director of the Enterprise Management Office, at our Parent Company from 1984 to 2000. Since November 2001, Mr. Wu has served as the deputy chief economist of our Parent Company. Wen Weiming, age 41, was elected a director of Guangshen Railway in 2003. Mr. Wen is an accountant and graduated from Guangzhou Railway Workers' College. He has over 10 years expereice in the railway industry, and has served as the director of the accounting and finance department, the chief accountant of the diversified businesses sub-section, and the director of the finance sub-section of Yangcheng Railway Company. Since May 2001, Mr. Wen has served as the deputy director of the finance department of our Parent Company. Li Qingyun, age 40, was elected a director of Guangshen Railway in 2000 and is currently our deputy general manager. Mr. Li graduated from North Communications University in 1989. He holds a master's degree in railway transportation and organization. He served in managerial positions in various technical and transportation departments of our Parent Company from 1989 to August 1999. He joined us in September 1999. Li Peng, age 57, was elected a director of Guangshen Railway in 1998 and is also acting as the chairman of our trade union. Mr. Li is a graduate of the East China Civil Engineering Institute and has served in various executive and labor organizational positions in Yangcheng Railway Company since 1977. He was the deputy general manager of Guangzhou Railway Company and the Guangshen Railway Enterprise Development Company from 1992 to 1997. Mr. Li joined us in December 1997. Chang Loon Cheong, age 58, was elected an independent non-executive director of Guangshen Railway in 1996. He holds a management certificate from the Hong Kong Management Association and is an independent non-executive director of Guangshen Railway. Mr. Chang is also a director of Shanghai Xinhua Iron & Steel Company Limited and Orient International (Shanghai) Limited. Mr. Chang has acted as a manager of Cathay Restaurant in Lagos, Nigeria, a member of the senior management of Island Navigation Corporation International Limited and Orient Overseas Container Line Limited in West Africa, and the general manager and a director of Noble Ascent Company Limited. Deborah Kong, age 44, was elected an independent non-executive director of Guangshen Railway in 1996. Ms. Kong is currently an executive director of Centennial Resources Holding Company Limited. Ms. Kong holds a bachelor of arts degree from Sydney University and a one-year master degree course of finance degree from Macquarie University in Australia. She is a member of the Standing Committee of the People's Political Consultative Conference of Shandong Province in the PRC. Wilton Chau, age 42, was elected an independent non-executive director of Guangshen Railway in 2004. Mr. Chau holds a bachelor degree in applied mathematics from University of Hong Kong, a LLB degree from University of Wolverhampton and a Master of Business Administration from the University of Wales. Mr. Chau is a fellow member of the Association of Chartered Certified Accountants, a member of Singapore Institute of Arbitrators and Council 51 member of Hong Kong Biotechnology Association. Since 1987, Mr. Chau has served several financial institutions in various senior positions overseeing investment and development in railway, road and airport infrastructure projects. Mr. Chau is currently the chairman of Qleap Venture Limited. SUPERVISORS The table below sets forth the information relating to our supervisors: DATE FIRST ELECTED NAME AGE POSITION OR APPOINTED ---- --- -------- ------------ Yao Muming 50 Supervisor 1999 Tang Dinghong 55 Supervisor 2004 Zhao Genrong 58 Supervisor 2000 Chen Yongbao 52 Supervisor 2002 Chen Yunzhong 51 Supervisor 2001 Yang Rongjiu 56 Supervisor 2002 Yao Muming, age 50, was appointed as a Supervisor of Guangshen Railway in 1999. Mr. Yao graduated from South China Normal University and previously served as the Deputy Director of the Guangzhou and Zhuhai Animal and Plant Quarantine Bureaus. From 1997 to 2003, he was a member of the senior management of the Company. Since July 2003, Mr. Yao has been a member of the senior management of our Parent Company. Since July 2003, he has served the chairman of the supervisory board. Tang Dinghong, age 55, was appointed as a supervisor of Guangshen Railway in 2004. Mr. Tang graduated from Zhongshan University. He started to work in the railway industry since 1969 and had served in various senior managerial positions of Guangzhou Railway (Group) Company. Mr. Tang joined us in July 2003. Zhao Genrong, age 58, was appointed as a supervisor of Guangshen Railway in 2000. Mr. Zhao is a graduate of North Communications University. He served in various financial positions in Hengyang Railway Company from 1968. Since 1983, Mr. Zhao has served as the deputy director and subsequently as the director of the financial department of our Parent Company. Since August 1999, Mr. Zhao has served as the director of the audit department of our Parent Company. Chen Yongbao, age 52, was appointed as a supervisor of Guangshen Railway in

2002. Mr. Chen graduated from Zhuzhou Railway Mechanical School. Since 1975, he has served in various managerial positions in Guangzhou Railway Company and Yangcheng Railway Company. From 1997 to 2001, Mr. Chen served in the administration supervisory position at our Parent Company. Since May 2001, Mr. Chen has served as the chief of the supervision department of our Parent Company. Chen Yunzhong, age 51, was appointed as a supervisor of Guangshen Railway in 2001. Mr. Chen graduated from Guangzhou Railway Driver's School, Guangdong Jinan University and the Central Administration Academy. He was a member of the senior management of Hainan Railway Company. Mr. Chen joined us in May 2000. 52 Yang Rongjiu, age 56, was appointed as a supervisor of Guangshen Railway in 2002. Mr. Yang graduated from Cadres Further Education (Secondary School) at Guangzhou Zhongshan University. He has served in various PRC railway departments since 1964 and was the Stationmaster of Shenzhen Station. In May 2001, Mr. Yang served as the deputy chairman of our company's trade union. SENIOR MANAGEMENT The table below sets forth information relating to our senior management: DATE FIRST ELECTED OR NAME AGE POSITION APPOINTED ---- --- -------- --------- Luo Qingming 47 Deputy General Manager and Chief Engineer 1999 Shao Huaping 46 Deputy General Manager 2004 Wu Weimin 46 Deputy General Manager 2004 Li Ruizhi 48 Chief Accountant 2004 Guo Xiangdong 38 Company Secretary 2004 Luo Qingming, age 47, is a Deputy General Manager and the Chief Engineer of Guahgshen Railway. In 1982, Mr. Luo graduated from Changsha Railway Institute with major in railway engineering. He is a senior engineer and had previously served as an engineer, the Chief Engineer, a Deputy Section Chief and the Section Chief of Guangshen Engineering Section of our company. He received a government allowance awarded by the State Council of the PRC in 1999. Shao Huaping, age 46, is a Deputy General Manager of Guahgshen Railway. Mr. Shao graduated from the Huazhong University of Science and Technology with a master's degree in engineering and is a senior engineer. Since 1979, he had served in various managerial positions of Wuhan Railway Sub-administration and Shenzhen Pingyan Railway Company. From August 1998 to September 2001, he served as the Deputy Section Chief of Shenzhen Power Section of Guahgshen Railway. Mr. Shao was the Deputy Director of Locomotive Department of Guangzhou Railway (Group) Company before joining Guahgshen Railway as a Deputy General Manager in January 2004. Wu Weimin, age 46, is a Deputy General Manager of Guahgshen Railway. Mr. Wu graduated from Guangdong Radio & TV University and is an engineer. Since 1984, he has served in various managerial positions in the Material and Equipment Department, the Planning and Statistic Department and the Labour and Wage Department of Yangcheng Railway Company. He has also served as an engineer in the Material and Equipment Section, the Deputy Director and the Director of the Planning and Statistic Sub-department of Yangcheng Railway Company. Mr. Wu was the Director of Labour Sub-department and Director of Social Insurance Centre of Yangcheng Railway Company before joining Guahgshen Railway as a Deputy General Manager in January 2004. 53 Li Ruizhi, age 48, is the Chief Accountant of Guahgshen Railway. Ms. Li graduated from Economy and Management Department of School of the Central Party Committee and is an accountant. Since 1984, she has served in various finance and accounting positions at different PRC railway departments. She has 20 years of experience in finance and accounting areas. Ms. Li previously served as the deputy section-chief of the Finance Department and the Deputy Director of Guangzhou Railway Settlement Centre of Guangzhou Railway (Group) Company before joining Guangshen Railway in January 2004. Guo Xiangdong, age 38, is the Company Secretary and the Director of Secretariat of the Board of Directors. Mr. Guo graduated from the Central China Normal University with a Bachelor of Laws degree and is an economist. He joined the Company in 1991, and previously served as the Deputy Section Chief, Deputy Director and the Director of Secretariat of the Board of Directors of Guangshen Railway. Mr. Guo has been as the Company Secretary since January 2004. There are no family relationships between any director or executive officer and any other director or executive officer. Of the members of the board of directors, our chairman, Mr. Wu Junguang, is both the chairman and the general manager of our Parent Company. Mr. Feng Qifu is the chairman of the board of directors of Guangzhou Tiecheng Industrial Company and a director of Sanmao Railway Industrial Company. Mr. Wu Houhui is the director of Guangmeishan Railway Company, Sanmao Railway Company and Shichang Railway Company. Mr. Hu Lingling is a director of Nanhai Saiyanqiao Railway Freight Yard and Storage Company, Sanmao Railway Company and Guangdong Railway Youth Travel Service Co., Ltd.. Mr. Wen Weiming is a supervisor of Guangzhou Railway Engineering (Group) Company and Guangdong Railway Youth Travel Service Co., Ltd.. The lines operated by Guangmeishan Railway Company, Sanmao Railway Company and Shichang Railway Company are local railroads. Guangzhou Tiecheng Industrial Company is our joint venture partner. We are currently envolved in certain litigation proceedings relating to this joint venture. See Item 8A.7 Legal Proceedings. We have business relationships relating to railroad transportation with Guangmeishan Railway Company and Sanmao Railway Company. ITEM 6B. BOARD COMPENSATION DIRECTORS AND SENIOR MANAGEMENT Total remuneration of our directors, supervisors and senior officers during 2003 included wages and bonuses. Directors or supervisors who are also officers and employees of Guangshen Railway receive certain other benefits in kind from our Parent Company and GEDC, such as subsidized or free health care services, housing and transportation, as customarily provided by 54 companies in the PRC to their employees. The aggregate amount of cash remuneration paid by Guangshen Railway in 2003 to all individuals who are currently our directors, supervisors and senior officers was approximately RMB1.72 million, of which approximately RMB1.14 million was paid to directors and supervisors and approximately HK$0.31 million was paid to the two independent non-executive directors. The aggregate amount of cash remuneration we paid during the year ended December 31, 2003 for pension and retirement benefits to all individuals who are currently our directors, supervisors and senior officers was approximately RMB121,000. ITEM 6C. BOARD PRACTICES BOARD OF DIRECTORS In accordance with the 4th Amendment to our Articles of Association, which was approved at our general shareholders' meeting held on June 10, 2004, our board of directors consists of ten directors, one of whom is the chairman. Directors are appointed at our general shareholders' meeting through voting, and serve for terms of three years. Upon the expiration of the term of their office, they can serve consecutive terms if re-appointed at the general shareholders' meeting. The service contracts that we have entered into with our directors do not provide for any payment of compensation upon termination. SUPERVISORY COMMITTEE We have a supervisory committee consisting of five to seven supervisors. Supervisors serve a term of three years. Upon the expiration of their terms of office, they may be re-appointed to serve consecutive terms. The supervisory committee is presided over by a chairman who may be elected or removed with the consent of two-thirds or more of the members of the supervisory committee. The term of office of the chairman is three years, renewable upon re-election. Our supervisory committee was appointed at the general shareholders' meeting held on June 28, 2002 and consists of five representatives of the shareholders who may be elected or removed by our shareholders and one representative of our employees who may be elected or removed by our employees. At the general shareholders' meeting held on June 10, 2004, Gu Hongxi was substituted by Tang Dinghong due to Gu Hongxi's change of position. Members of our supervisory committee may also observe meetings of the board of directors. The current members of the supervisory committee are: Yao Muming, Tang Dinghong, Zhao Genrong, Chen Yongbao, Chen Yunzhong, and Yang Rongjiu. The term of this supervisory committee will expire in 2005. Supervisors attend board meetings as non-voting members. The supervisory committee is responsible to our shareholders and has the follow duties and responsibilities: - to supervise our handling of our financial matters; - to supervise our directors, general manager, deputy general manager and other senior officers for compliance with laws, administrative regulations or our articles 55 of association; - to regulate any acts of directors, the general manager, deputy general manager and other senior officers that are detrimental to the interests of Guangshen Railway; - to verify such financial information as financial reports, business reports and profit distribution plans submitted by the board of directors to the general shareholders' meeting, and arrange certified public accounts and auditors to verify issues; - to convene interim general shareholders' meetings as requested; and - to initiate legal proceedings against directors on behalf of Guangshen Railway. AUDIT COMMITTEE In accordance with the Listing Rules of the Stock Exchange of Hong Kong that encourage the establishment of an audit committee, and the "Guidance for the Formation of An Audit Committee" promulgated by the Hong Kong Accountants' Association in December 1997, we have an audit committee consisting of two independent non-executive directors. The current members of our audit committee, appointed by the board of directors, are: Mr. Chang Loong Cheong and Ms. Deborah Kong. Mr. Chang and Ms. Kong are "independent directors" of our Company as defined in Section 303A.02 of the New York Stock Exchange's Listed Company Manual. The audit committee must convene at least two meetings each year, and may invite the executive directors, persons in charge of the financial and audit departments and our independent auditors. The audit committee must convene at least one meeting with the auditors each year without any executive directors present. The duties of our audit committee include: 56 - reviewing the reports prepared by the board of directors, the annual and interim reports on our operating results, the annual financial report and public announcements of our operating results; - reviewing our financial reports and the reports prepared by our independent auditor and its supporting documents, including the review of our internal controls and disclosure controls and procedures, and to discuss with the auditor our annual audit plan and solutions to problems in the previous year; - reviewing and approving the selection of and remuneration paid to our independent auditor; and - reviewing audit matters specifically identified by the board of directors, and determining whether such projects are in compliance with industrial practices and market rules, and performing statutory duties and safeguarding our interests and the interests of our shareholders. ITEM 6D. EMPLOYEES As of December 31, 2001, 2002 and 2003, we had approximately 9,132,9,258 and 9,029 employees, respectively. The following chart sets forth the number of our employees by function as of December 31, 2003: FUNCTION EMPLOYEES Passenger transportation personnel ...... 1,432 Freight transportation personnel ........ 429 Transportation personnel ................ 4,547 Supporting personnel .................... 316 Other business personnel ................ 1,042 Administrative and managerial personnel.. 1,263 Total ............................. 9,029 A substantial majority of our employees are located in the Guangdong Province and in Shenzhen. The number of our employees decreased by 229 in 2003 mainly because we laid off some of our temporary employees in order to increase our operational efficiency and to reduce operation costs. We have established a trade union to protect employees' rights, assist in the fulfillment of their economic objectives, encourage employee participation in management decisions and assist in mediating disputes between the management and union members. Each of our train stations has a separate branch of the trade union. Most of our employees belong to the trade union. We have not experienced to any strikes or other labor disturbances that have interfered with our operations in the past, and we believe that our relations with our employees are good. We have implemented a salary policy which links our employees' salaries with operating results, labor efficiency and individual performance. Employees' salaries distribution is subject to 57 macro-control and is based on their performance records and reviews. We paid approximately RMB347.6 million in salaries and benefits for our railroad businesses in 2003. Pursuant to applicable state policies and regulations, our employees enjoy the following benefits: (1) retirement pension -we are required to set aside a sum equivalent to 18% of the aggregate amount of salaries of all of our employees for the year and 5% of the aggregate amount of salaries of all of its employees for the year as employees' retirement pension and supplemental retirement pension, respectively; (2) welfare fund - we are required to set aside 14% of the aggregate amount of our employees' salaries for the year as their welfare fund contributions and medical service fees; and (3) housing fund - both we and our employees are required to deposit 7% (for residents in Guangzhou area or along the Guangzhou-Shenzhen route), or 13% (for Shenzhen residents) of the employee's monthly salary into the employee's personal housing fund account. Save as disclosed, we have not participated in any other employees' basic medical insurance schemes. We had previously constructed and purchased new residential properties for our employees to improve their living conditions. Under a housing benefit scheme introduced by the Ministry of Finance, we sold these residential properties to our employees at a price approved by the government. The losses arising from the difference between the net book value and the proceeds from the sales of staff quarters to the employees was approximately RMB226.4 million as of December 31, 2003. Pursuant to the prevailing policies of the Ministry of Finance, the aforesaid losses should be credited to retained earnings in the statutory accounts as of January 1, 2001, or in case of a debit balance, to offset against statutory public welfare fund, statutory surplus reserve, discretionary surplus reserve and capital surplus reserve upon the approval of the Board. Such treatment conforms to the accounting principles and regulations applicable to us in the PRC. In our financial statements for the year ended December 31, 2003 prepared in accordance with IFRS, we accounted for the losses arising from housing scheme as follows: losses from the sale of completed staff quarters to employees, or from the sale of premises under construction of which could be reasonably estimated for future services was approximately RMB226.4 million. Such losses were amortized on a straight-line basis over the estimated remaining average service period of employees of 15 years from the time of such sales. During the year ended December 31, 2003, the amortization charged to the deferred labor costs of the consolidated income statement was RMB15.09 million and the accumulated amortization amounted to RMB60.37 million. As of December 31, 2003, the unamortized deferred losses, which were recorded as deferred staff costs in our balance sheet, were RMB166.0 million. ITEM 6E. SHARE OWNERSHIP As of June 23, 2004, none of our directors, supervisors or senior management own any interest in any shares or options to purchase our shares. 58 ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS ITEM 7A. MAJOR SHAREHOLDERS We are a joint stock company organized under the laws of the PRC in March 1996. The Parent Company, a state-owned enterprise under the administration of the Ministry of Railways owns 67% of our outstanding common shares. The Parent Company is the sole shareholder of all of our domestic shares in the form of state legal person shares and is entitled to exercise all rights as our controlling shareholder according to the relevant laws, rules and regulations. The Parent Company has substantial influence over our operations, not only in its capacity as controlling shareholder, but also because of its role as an administrative agent of the Ministry of Railways that controls and coordinates railway operations in Guangdong Province, Hunan Province and Hainan Province. As an instrumentality of the Ministry of

Railways, our Parent Company performs direct regulatory oversight functions with respect to us, including determining and enforcing technical standards and implementing special transportation directives. The following table sets forth information regarding ownership of our issued and outstanding capital stock as of December 31, 2003. Note that it includes all persons who are known by us to own, either as beneficial owners or holders of record, five percent or more of our capital stock. TITLE OF CLASS IDENTITY OF PERSON OR GROUP AMOUNT OWNED PERCENT OF CAPITAL -------------------------- -------------------------- ----------- ------------------ (THOUSAND SHARES) Common Shares (Domestic Shares) The Parent Company 2,904,250 66.99% The following table sets forth all persons who are known by us to own, as holders of record, five percent or more of our issued and outstanding H shares as of December 31, 2001. TITLE OF CLASS IDENTITY OF PERSON OR GROUP AMOUNT OWNED PERCENT OF CAPITAL ----------------------- -------------------------- ----------- ------------------ (THOUSAND SHARES) Common Shares (H Shares) Marathon Asset Management Ltd. 115,706 8.08% Common Shares (H Shares) Sumitomo Life Insurance Company(1) 71,692 5.00% Common Shares (H Shares) Sumitomo Mitsui Asset Management 71,692 5.00% Company, Limited ------------- (1) As at December 31, 2003, Sumitomo Life Insurance Company was deemed to be interested in 71,692,000 H Shares (representing 5.00% of the total H Shares of the Company or 1.65% of the total share capital of the Company) held by Sumitomo Mitsui Asset Management Company, Limited, a controlled corporation of Sumitomo Life Insurance Company. As of the date of this report, we are not aware of any arrangement that may at a subsequent date result in a change of control of Guangshen Railway. As an owner of at least 30% of our issued and outstanding shares, our Parent Company is deemed a controlling shareholder (defined in Item 10 below), and therefore may not exercise our voting rights with respect to various matters in a manner prejudicial to the interests of our other shareholders. See "Item 10. Additional Information -- Memorandum and Articles of Association -- Restrictions on Controlling Shareholders". In accordance with our articles of association, each share of our capital stock has one vote and the shares of the same class have the 59 same rights. Other than the restrictions noted in the first sentence of this paragraph, the voting rights of our major holders of domestic shares are identical to those of any other holders of our domestic shares, and the voting rights of our major holders of H shares are identical to those of our other holders of H shares. Holders of domestic shares and H shares are deemed to be shareholders of different classes for some matters, which may affect their respective interests. Holders of H shares and domestic shares are entitled to the same voting rights. ITEM 7B. RELATED PARTY TRANSACTIONS As part of the restructuring carried out in 1996 in preparation for our initial public offering, we assumed from Guangshen Railway Company, our predecessor, Guangzhou Railway (Group) Company, our Parent Company, assets and liabilities that relate to the businesses now conducted by us, including the high-speed passenger train project and equity interests in subsidiaries and joint ventures engaged in the operation of warehouses or freight yards. We also assumed from Yangcheng Railway certain assets, including 14 shunting locomotives and passenger coaches that Yangcheng Railway had previously leased to us. Our predecessor company retained the assets, liabilities and businesses not assumed by us, including units providing staff quarters and social services such as health care, educational and public security services and other ancillary services, as well as subsidiaries or joint ventures whose businesses do not relate to railroad operations and do not compete with our businesses. As part of our restructuring, our predecessor was renamed Guangzhou Railway (Group) Guangshen Railway Enterprise Development Company, or GEDC. The Parent Company and GEDC on the one hand and us on the other have agreed to certain mutual indemnities arising from or in respect of the various assets and liabilities transferred to or retained by the parties. The purpose of the indemnities is to ensure that none of Guangshen Railway, our Parent Company or GEDC will bear liabilities that it has not agreed to assume, even in cases where third parties have not consented to the division of liabilities among them and continue to make claims against an entity that has not assumed the relevant liability. The Parent Company and GEDC have agreed to indemnify Guangshen Railway against any claims arising from facts or events prior to the restructuring as well as any claims against Guangshen Railway in respect of assets and liabilities retained by them in the restructuring. As a result of the restructuring, GEDC, Yangcheng Railway and our Parent Company (together with some of its subsidiaries) continue to provide social services to Guangshen Railway on a contractual basis. These services include medical care for our employees and their family members, kindergarten, elementary and secondary school education for the children of employees, room and board for our employees traveling on business, employee housing management and maintenance and public security in our stations and on-board our trains. GEDC provides most of these services through its facilities in Shenzhen. The Parent Company and Yangcheng Railway provide to Guangshen Railway in Guangzhou other services, including health care, employee training and childcare. For the services rendered, Guangshen Railway pays our Parent Company, Yangcheng Railway or GEDC, as the case may be, reasonable, arms-length fees. Some transactions between Guangshen Railway and our Parent Company and its subsidiaries have continued after the restructuring, in the form of a cross-provision of goods and 60 services. The principal goods and services provided by our Parent Company and some of its subsidiaries (including Yangcheng Railway and GEDC) to Guangshen Railway include the following: - locomotives, railcars and operating personnel; - leasing of regular speed passenger coaches; - maintenance services for regular speed locomotives and passenger coaches; - railroad transportation related services; - fuel for the operation of locomotives; - railway related materials; - overhaul and emergency repair of our track and bridges; - medical and health care services; - public security; - educational services; and - employee housing. The aggregate costs to us of these goods and services in 2001, 2002 and 2003 were RMB243.2 million, RMB153.4 million and RMB167.2 million, respectively. The principal goods and services provided by us to our Parent Company and its subsidiaries include railroad transportation related services, sale of duty free goods on-board of our Hong Kong through trains and at Guangzhou station and Guangzhou East Station, and advertising space at our Shenzhen station. Under an agreement with Yangcheng Railway, Yangcheng Railway and Guangshen Railway provide each other and their passengers with services at Guangzhou Station, including, among other things, passenger boarding, ticket collection and on-board water supply. The prices at which these goods and services are provided are different in each case. In general: - prices for railroad transportation-related services are determined in accordance with the actual costs incurred in providing these services plus a profit margin of 8% of aggregate chargeable costs (fuel expenses, asset depreciation and water utility fees are not counted as chargeable costs for purposes of this calculation), which amount, Guangshen Railway believes, is consistent with that which would be charged in an arm's-length transaction; - the rental amounts for the high-speed passenger coaches leased to Guangshen Railway by our Parent Company equal 6% of our Parent Company's purchase price for the coaches, approximating our Parent Company's depreciation expenses for the coaches; Guangshen Railway also bears all costs of maintenance and overhaul of these coaches; - the prices for social and related services provided by Yangcheng Railway (i.e., educational) and GEDC (i.e., security, medical, educational and housing) are determined based on the actual cost of providing these services; 61 - the prices for social and related services provided by our Parent Company are determined on the following basis: - medical services : in accordance with the relevant local standards, subject to a 20% discount (except in respect of medicine and registration fees); - educational services : in accordance with the standards set by our Parent Company; - child care services : in accordance with the actual cost incurred for providing such services; - newspaper supply services : at an agreed cost of approximately RMB25 per year per copy of newspaper supplied, which cost may change based on cost changes to our Parent Company; - the prices for the supply of railroad transportation related materials are determined in accordance with the relevant regulations issued by our Parent Company (which regulations are applicable to other railroads under the jurisdiction of our Parent Company); - the prices for the provision of overhaul and large scale maintenance services for our track and bridges are based on the relevant approved estimates plus a profit margin of 8%, and the prices for other maintenance services are to be agreed by the parties on a case-by-case basis; and - Guangshen Railway is entitled to 45% of the profits derived from the advertising businesses at its Shenzhen station. The agreement with Yangcheng Railway was revised on March 6, 1996 and provides for a 10-year lease period starting from 1996. The lease with the Ministry of Railways is renewable annually. Substantially all the above transactions will continue in the future, although not necessarily on the same terms. The chart below sets forth a breakdown by category of the material transactions between our Parent Company and its affiliates and us in 2001, 2002 and 2003. DESCRIPTION OF TRANSACTION 2001 2002 2003 ------------------------- ---- ---- ---- (RMB THOUSANDS) Lease of locomotives and related services from Yangcheng Railway(1)............. 70,345 42,047 40,882 Provision of trains and related services from Guangmeishan Railway Company, a subsidiary of our Parent Company............................................ 5,205 4,864 5,305 62 DESCRIPTION OF TRANSACTION 2001 2002 2003 ------------------------- ------------------------ (RMB THOUSANDS) Purchase of materials and supplies from Guangzhou Railway Material Supply Company, a subsidiary of our Parent Company......................................... 36,544 33,074 50,687 Social services (employee housing, health care, educational and public security services and other ancillary services) provided by our Parent Company and affiliates (including GEDC)......................................................... 56,800 66,744 68,079 Operating lease rentals paid to the Ministry of Railways.............................. 52,296 57,298 58,904 Provision of trains and related services by the Ministry of Railway.................... 66,475 211,667 201,870 Train use fees and related service fees paid to Guangzhou Railway

(Group) Passenger Transportation Company, a subsidiary of our Parent Company................ 7,844 6,681 2,207 Interest expenses paid to our Parent Company(ii)...................................... 1,178 2,443 2,037 Interest received from the Ministry of Railways' Railroad Deposit-taking Center........ 11,887 3,239 3,516 Interest received from Pingnan Railway, an affiliate of our Parent Company(ii)......... 1,866 806 827 Interest received from Guangmeishan Railway Company(ii)................................ 1,291 1,884 901 ------------------ (i) The lease agreement with Yang Cheng Railway Company was revised on March 6, 1996 and provides for a 10-year lease period starting from 1996. The lease with MOR is based on the uniform rate set by MOR and is renewable annually. (ii) The interest was resulted from the long-distance transportation services, which was calculated based on the average balances due from/to related parties on a quarterly basis, at the prevailing interest rates of six-month bank loans. As of December 31, 2003, we had the following material balances with our related parties: 31 December, -------------------------- 2001 2002 2003 -------------------------- RMB THOUSANDS Temporary cash investments in the MOR's Railroad Deposit-taking Center 250,152 168,000 168,000 Bank deposits in the MOR's railroad Deposit-taking Center 38,767 206,452 321,985 Due from Parent Company 29,499 39,374 - Due to Parent Company - - (37,230) Due from related parties 276,013 267,885 199,921 - Trading balance 82,923 54,425 10,608 - Non-trading balance 193,090 213,460 189,313 Due to related parties (58,650) (158,199) (120,605) - Trading balance (40,196) (125,847) (60,128) - Non-trading balance (18,454) (32,352) (60,477) 63 As of 31 December, 2003, the balances with the MOR, the Parent Company and related parties are unsecured, non-interest bearing and repayable on demand, except for those disclosed in notes 10(b) and 24(a) to the audited financial statements included elsewhere in this annual report and bank deposits in MOR's railroad Deposit-taking centre. These balances resulted from transactions between our related parties and us in the ordinary course of business. The balances with our Parent Company are all non-trading in nature. The balances with our related parties, which are trading in nature, are all due within one year. Our related party transactions have been carried out on usual terms according to the conditions and waiver granted by The Stock Exchange of Hong Kong Limited and the contracts entered into between our related parties and us. Our independent non-executive directors confirmed that these transactions (which are "connected transactions" as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited) entered into by us during 2003 were entered into in the ordinary and usual course of our business on normal commercial terms or on terms that were fair and reasonable so far as our shareholders were concerned, or in accordance with the terms of an agreement governing such transactions or, where there was no such agreement, on terms no less favorable than those offered to (or from) independent third parties. ITEM 7C. INTERESTS OF EXPERTS AND COUNSEL Not applicable. 64 ITEM 8. FINANCIAL INFORMATION ITEM 8A. CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION ITEM 8A.1 - ITEM 8.A.6: See pages F-1 to F-41 following Item 19. ITEM 8A.7 LEGAL PROCEEDINGS As of December 31, 2003, our interest in an associated company, Guangzhou Tiecheng Enterprise Company Limited, or "Tiecheng," amounted to approximately RMB140 million. In 1996, Tiecheng and a Hong Kong incorporated company jointly established Guangzhou Guantian Real Estate Company Limited, or "Guangzhou Guantian", a sino-foreign cooperative joint venture to develop certain properties near a railway station owned and operated by us. On October 27, 2000, Guangzhou Guantian together with Guangzhou Guanhua Real Estate Company Limited, or "Guangzhou Guanhua," and Guangzhou Guanyi Real Estate Company Limited, or "Guangzhou Guanyi," agreed to act as joint guarantors, or, collectively, the "Guarantors," of certain payables of Guangdong Guangcheng Real Estate Company Limited, or "Guangdong Guancheng," owned to an independent third party. The Guarantors, Guangdong Guancheng were related companies with a common chairman. Guangdong Guancheng failed to repay these payables, and the Guarantors were found liable under a court verdict made on November 4, 2001 to pay the independent third party an amount of approximately RMB257 million plus interest. On December 15, 2003, Guangzhou Guantian applied to the High People's Court of Guangdong Province, or "the Court," to discharge the aforesaid guarantee, which application was heard by the court on March 18, 2004. The Court has yet to complete the procedures for its reassessment of the previous court verdict. If Guangzhou Guantian were held responsible for the guarantee, we may need to provide for impairment on our interest in Tiecheng. However, based on counsel's advice, the directors are of the opinion that the guarantee arrangement is invalid under the relevant PRC rules and regulations. Accordingly, the directors consider that the chance of Guangzhou Guantian to settle the above claim is remote and no provision for impairment on the interests in Tiecheng was made in the accounts. Except as disclosed, we are not a party to any material legal proceeding and no material legal proceeding is known to us to be pending against us or with respect to our properties. ITEM 8A.8 DIVIDEND DISTRIBUTIONS We make decisions concerning the payment of dividends on an annual basis. Any dividends are paid at the discretion of our board of directors, which makes a recommendation in this regard that must be confirmed at our annual general shareholders' meeting. Our articles of association permit us to distribute dividends from profits more than once a year. The amount of these interim dividends cannot exceed 50% of our distributable income as stated in our interim 65 profit statements. In accordance with our articles of association, the amounts available for the purpose of paying dividends will be deemed to be the lesser of: - net after-tax income determined in accordance with PRC accounting standards and regulations; and - net after-tax income determined in accordance with either international accounting standards or the accounting standards of the countries in which our shares are listed. See "Item 10. E Taxation" for a discussion of the tax consequences related to the receipt of dividends. Our articles of association prohibit us from distributing dividends without first making up for cumulative losses from prior periods (determined in accordance with PRC accounting standards) and making all tax and other payments required by law. Further, prior to the payment of dividends, our profits are subject to deductions such as allocations to a statutory common reserve fund and into a public welfare fund. The common reserve fund may be used to make up losses or be converted into share capital or reinvested. Our articles of association require that cash dividends in respect of H shares be declared in renminbi and paid in Hong Kong dollars at the average of the People's Bank of China rate for each day of the calendar week preceding the date of the dividend declaration. To the extent that we are unable to pay dividends in Hong Kong dollars from our own foreign exchange resources, we will have to obtain Hong Kong dollars through the interbank system or by other permitted means. Hong Kong dollar dividend payments will be converted by the depositary and distributed to holders of ADSs in U.S. dollars. On April 20, 2004, the Board proposed a final dividend distribution of RMB0.105 per share to our shareholders for the year ended December 31, 2003. The final dividend payment has been approved by the shareholders at our 2003 annual general meeting held on June 10, 2004. ITEM 8B. SIGNIFICANT CHANGES Other than events already mentioned in this annual report, there have been no significant changes since December 31, 2003. 66 ITEM 9. THE OFFER AND LISTING ITEM 9A. THE OFFER AND LISTING DETAILS PRICE RANGE OF OUR H SHARES AND ADSS As of December 31, 2003 and June 18, 2004, there were 1,431.3 million H shares issued and outstanding. As of December 31, 2003 and June 18, 2004, there were, respectively, 4,862,581 and 5,003,261 ADSs outstanding held by 177 and 174 registered holders. Since a percentage of the ADSs are held by nominees, these numbers may not be representative of the actual number of U.S. beneficial holders of ADSs or the number of ADSs beneficially held by U.S. persons. The depositary for the ADSs is JPMorgan Chase Bank. The Stock Exchange of Hong Kong is the principal non-US trading market for our H shares. The ADSs, each representing 50 H shares, have been issued by the JPMorgan Chase Bank as depositary and are listed on the New York Stock Exchange. The following table sets forth, for the periods indicated, the reported high and low closing sales prices for our securities on each of these two stock exchanges: NEW YORK STOCK EXCHANGE STOCK EXCHANGE OF HONG KONG ---------------------- -------------------------- CALENDAR PERIOD HIGH LOW HIGH LOW -------------- ----- ----- ---- ---- (US$ PER ADS) (HK$ PER H SHARE) 1999 ....................... 7.625 4.8125 1.19 0.72 2000 ....................... 7.625 4.5625 1.23 0.7 2001 ....................... 10.48 6.19 1.76 0.90 2002 January to March ......... 9.60 8.38 1.47 1.30 April to June ............ 10.24 8.87 1.58 1.42 July to September ........ 9.60 8.30 1.49 1.33 October to December ...... 8.90 8.05 1.39 1.27 2003 January to March ......... 9.4 8.69 1.47 1.32 April to June ............ 9.68 8.20 1.48 1.26 July to September ........ 13.7 9.15 2.125 1.42 October to December ...... 14.84 12.88 2.25 1.95 2004 January .................. 17.25 14.20 2.65 2.25 February ................ 15.35 13.95 2.40 2.15 March ................... 15.60 14.47 2.475 2.30 April ................... 15.54 13.39 2.45 2.05 May ..................... 14.45 11.77 2.275 1.77 June (through June 18) ... 17.9 12.93 2.20 2.00 During the year ended December 31, 2001, we did not purchase, sell or redeem any of our shares. ITEM 9B. PLAN OF DISTRIBUTION Not applicable. 67 ITEM 9C. MARKETS Our H shares are listed on the Stock Exchange of Hong Kong under the stock code "0525" and American Depositary Shares representing our H shares are listed on the New York Stock Exchange under the stock code "GSH". ITEM 9D. SELLING SHAREHOLDERS Not applicable. ITEM 9E. DILUTION Not applicable. ITEM 9F. EXPENSES OF THE ISSUE Not applicable. 68 ITEM 10. ADDITIONAL INFORMATION We were established as a joint stock limited company under the Company Law of the PRC on March 6, 1996. Our legal name is [COMPANY NAME IN CHINESE], and its English translation is Guangshen Railway Company Limited. ITEM 10A. SHARE CAPITAL Not Applicable. ITEM 10B. MEMORANDUM AND ARTICLES OF ASSOCIATION Described below is a summary of the significant provisions of our articles of association as currently in effect. As this is a summary, it does not contain all the information that may be important to you. A copy of our complete articles of association was filed with the U.S. Securities and Exchange Commission (the

"SEC") as an exhibit to the registration statement on Form F-1 (Registration No.333-3382) under the Securities Act in connection with our global offering of H shares and related American depositary shares on May 13, 1996. GENERAL We are a joint stock limited company established in accordance with the Company Law of China, the State Council's special regulations regarding the issue of shares overseas and the listing of shares overseas by companies limited by shares and other relevant laws and regulations of the PRC. Guangshen Railway was established by way of promotion with approval evidenced by the document "Ti Gai Sheng" [1995] No.151 of the PRC's State Commission For Restructuring The Economic System. We were registered with and obtained a business licence from the Administration Bureau of Industry And Commerce of Shenzhen, Guangdong Province on March 6, 1996. The number of our business licence is Shen Si Zhi N12183. Article 12 of our articles of association states that our object is to carry on the business of railway transportation. SIGNIFICANT DIFFERENCES BETWEEN H SHARES AND DOMESTIC SHARES Holders of H shares and domestic shares, with minor exceptions, are entitled to the same economic and voting rights. However, our articles of association provide that holders of H shares will receive dividends in Hong Kong dollars while holders of domestic shares will receive dividends in renminbi. Other differences between the rights of holders of H shares and domestic shares relate primarily to ownership and transferability. H shares may only be subscribed for and owned by legal and natural persons of Taiwan, Hong Kong, Macau or any country other than the PRC, and must be subscribed for, transferred and traded in a foreign currency. Other than the limitation on ownership, H shares are freely transferable in accordance with our articles of association. Domestic shares may only be subscribed for and owned by legal or natural persons in the PRC, and must be subscribed for and traded in renminbi. Transfers of domestic shares are subject to restrictions set forth under PRC rules and regulations, which are not applicable to H shares, and also to restrictions on transfers of shares owned by the PRC government, and by our directors or employees. Domestic shares and H shares are also distinguished by differences in administration and procedure, including provisions relating to notices and financial reports to be 69 sent to shareholders, dispute resolution, registration of shares on different parts of the register of shareholders, the method of share transfer and appointment of dividend receiving agents. RESTRICTIONS ON TRANSFERABILITY H shares may be traded only among foreign investors, and may not be sold to PRC investors (except investors from Hong Kong, Macau and Taiwan). PRC investors (except investors from Hong Kong, Macau and Taiwan) are not entitled to be registered as holders of H shares. Under our articles of association, we may refuse to register a transfer of H shares unless: - relevant transfer fees are paid, if any; - the instrument of transfer only involves H shares; - the stamp duty chargeable on the instrument of transfer has been paid; - the relevant share certificate and, upon the reasonable request of the board of directors, any evidence in relation to the right of the transferor to transfer the shares have been submitted; - if the shares are being transferred to joint owners, the maximum number of joint owners does not exceed four; and - we do not have any lien on the relevant shares. DIVIDENDS Unless otherwise resolved by a general shareholders' meeting, we may distribute dividends more than once a year, provided that the amount of interim dividends distributed shall not exceed 50% of the distributable income as stated in our interim profit statement. In accordance with our articles of association, our net income for the purpose of income distribution will be deemed to be the least of the amounts determined in accordance with: - PRC accounting standards and regulations, - international accounting standards; and - the accounting standards of the countries in which our shares are listed. The articles of association allow for distributions of cash dividends or shares. Dividends may only be distributed, however, after allowance has been made for: - making up losses, if any, for prior years; - allocations to the statutory common reserve fund; 70 - allocations to the statutory public welfare fund; and - allocations to a discretionary common reserve if approved by the shareholders. Our articles of association require us to appoint on behalf of the holders of H shares receiving agents to receive on behalf of these shareholders dividends declared and all other moneys owing by us in respect of the H shares. The receiving agent appointed shall be a company that is registered as a trust company under the Trustee Ordinance of Hong Kong. Our articles of association require that cash dividends in respect of H shares be declared in renminbi and paid by us in Hong Kong dollars. If we record no profit for the year, we may not normally distribute dividends for the year. VOTING RIGHTS AND SHAREHOLDER MEETINGS General shareholders' meetings can be annual general shareholders' meetings or extraordinary general meetings. Shareholders' meetings shall be convened by the board of directors. The board of directors shall convene an annual shareholders' meeting within six months of the end of each financial year. The shareholders provide us with principal authority at general meetings. We exercise our functions and powers in compliance with our articles of association and our by-laws. We shall not enter into any contract with any person other than a director, supervisor, general manager or other senior officer of Guangshen Railway whereby the management and administration of the whole or any substantial part of any business of Guangshen Railway is to be handed over to such person without the prior approval of the shareholders in a general meeting. The board of directors shall convene an extraordinary shareholders' meeting within two months if any one of the following circumstances occurs: - the number of directors falls short of the number stipulated in our by-laws or is below two-thirds of the number required in our articles of association; - our accrued losses amount to one-third of our total share capital; - shareholders holding not less than 10% of our issued shares carrying the right to vote make a request in writing to convene an extraordinary general meeting; or - the board of directors considers it necessary or the supervisory committee proposes to convene such a meeting. Where we convene a general shareholders' meeting (when we have more than one shareholder), we shall, not less than 45 days before the meeting, issue a written notice to all shareholders whose names appear in the share register of the items to be considered and the date and venue of the meeting. Any shareholder intending to attend the general shareholders' meeting 71 shall give us a written reply stating his or her intention to attend the meeting 20 days prior to the date of the meeting. Where we convene an annual general meeting, shareholders holding not less than five percent of our total shares shall be entitled to submit new motions in writing to us. We shall include in the agenda of the meeting all items in the motion that fall within the scope of the general shareholders' meeting. An extraordinary shareholders' meeting shall not decide on matters that are not specified in the notice. Based on the written replies received by us 20 days before a general shareholders' meeting, we shall calculate the number of voting shares represented by shareholders who have indicated their intention to attend the meeting. Where the number of voting shares represented by those shareholders reaches half of our total number of shares, we may convene the general shareholders' meeting. Otherwise, we shall, within five days, inform the shareholders again of the motions to be considered, the date and the venue of the meeting by way of a public announcement. After making the announcement, the general shareholders' meeting may be convened. A notice of meeting of shareholders shall: - be in writing; - specify the place, day and the time of the meeting; - state the motions to be discussed at the meeting; - provide such information and explanations as are necessary for the shareholders to exercise an informed judgment on the proposals before them. Without limiting the generality of the foregoing, where a proposal is made to amalgamate Guangshen Railway with another entity, to repurchase the shares of Guangshen Railway, to reorganize its share capital or to restructure Guangshen Railway in any other way, the terms of the proposed transaction must be provided in detail, together with copies of the proposed agreement, if any, and the cause and effect of the proposal must be properly explained; - contain disclosure of the nature and extent, if any, of material interests of any director, supervisor, general manager or other senior officer of Guangshen Railway in the transaction proposed and the effect of the proposed transaction on them in their capacity as shareholders in so far as it is different from the effect on the interests of shareholders of the same class; - contain the text of any special resolution proposed to be moved at the meeting; - contain conspicuously a statement that a shareholder entitled to attend and vote is entitled to appoint one or more proxies to attend and vote instead of him or her and that a proxy need not also be a shareholder; and 72 - state the time within which and the address to which the relevant instruments appointing the proxies for the meeting are to be delivered. Notice of general meetings of shareholders shall be served on each shareholder whether or not entitled to vote at that meeting, by personal delivery or prepaid mail to the address of the shareholder as shown in the share register. For the benefit of holders of domestic shares, notice of general meetings of shareholders may also be given by way of public announcement by publication in one or more newspapers specified by the securities regulatory authorities on any day within 45 to 50 days prior to the meeting. This public announcement shall be deemed receipt by each holder of domestic shares of notice of the relevant meeting. The accidental omission to give notice of a meeting to, or the non-receipt of notice of a meeting by any person entitled to receive notice shall not invalidate the meeting and the resolutions adopted. Where we convene an annual general meeting, we shall include in the notice of the meeting any resolutions submitted by shareholders (including proxies) who hold five percent or more of the total number of shares, provided that these resolutions fall within the scope of a general shareholders' meeting. The following matters shall be resolved by way of ordinary resolution of the general shareholders' meeting: - work reports of the board of directors and the supervisory committee; - profit distribution proposals and loss recovery proposals formulated by the board of directors; - appointment and removal of members of the board of directors and the supervisory committee, their remuneration and methods of payment; - our annual financial budget, final accounts, balance sheet, profit and loss account and other financial statements; and - matters other than those that are required by laws, administrative regulations or our articles of association to be adopted by way of special resolution. The following matters shall be resolved by way of special resolution of the general shareholders' meeting: - increase or reduction of our share capital and the issuance of shares of any class, warrants and other similar securities; - issuance of company debentures; - division, merger, dissolution and liquidation of Guangshen Railway; - amendment to our articles of association; and - any other matter that, according to an ordinary resolution of the shareholders 73 meeting, may have a significant impact on Guangshen Railway and requires adoption by way of a special resolution. Shareholders have the right to attend general meetings of shareholders and to exercise their voting rights, in person or by proxy, in relation to the amount of voting shares they represent. Each share carries the right to one vote. At any meeting of shareholders a resolution shall be decided by a show of hands unless a poll is demanded before or after any vote by show of hands: - by the chairman of the meeting; - by at least two shareholders who possess the right to vote, present in person or by proxy; or - by one or more shareholders (including proxies) representing either separately or in aggregate, not less than one-tenth of all shares having the right to vote at the meeting. Unless a poll is demanded, a declaration by the chairman of the meeting that a resolution has on a show of hands been carried and an entry to that effect in the minutes of the meeting shall be conclusive evidence of the fact, without proof of the number or proportion of the votes recorded in favor of or against that resolution, that the resolution has been carried. A demand for a poll may be withdrawn. A poll demanded on the election of the chairman, or on a question of adjournment, shall be taken. A poll demanded on any other question shall be taken at such time as the chairman of the meeting directs, and any business other than that on which the poll has been demanded may be proceeded with, pending the taking of the poll. The result of the poll shall be deemed to be the resolution of the meeting at which the poll was demanded. On a poll taken at a meeting, a shareholder entitled to two or more votes need not cast all his or her votes in the same way. In the case of a tie, the chairman of the meeting shall be entitled to one additional vote. BOARD OF DIRECTORS Where a director is interested in any resolution proposed at a board meeting, the director shall not be present and shall not have a right to vote. That director shall also not be counted in the quorum of the relevant meeting. Our directors' compensation is determined by resolutions approved at the general shareholders' meeting. Our directors have no power to decide their own compensations. Our directors are not required to hold shares of our Company. There is no age limit requirement with respect to retirement or non-retirement of our directors. LIQUIDATION RIGHTS In the event of the termination or liquidation of Guangshen Railway, ordinary shareholders of Guangshen Railway shall have the right to participate in the distribution of surplus assets of Guangshen Railway in accordance with the number of shares held by those shareholders. 74 LIABILITY OF SHAREHOLDERS The liability of holders of our shares for our losses or liabilities is limited to their capital contributions in Guangshen Railway. INCREASES IN SHARE CAPITAL AND PREEMPTIVE RIGHTS Our articles of association require that approval by a special resolution of the shareholders and by special resolution of holders of domestic shares and H shares at separate shareholder class meetings be obtained prior to authorizing, allotting, issuing or granting shares, securities convertible into shares or options, warrants or similar rights to subscribe for any shares or convertible securities. No approval is required if, but only to the extent that, Guangshen Railway issues domestic shares and H shares, either separately or concurrently, in numbers not exceeding 20% of the number of domestic shares and H shares then in issue, respectively, in any 12 month period, as approved by a special resolution of the shareholders. New issues of shares must also be approved by relevant PRC authorities. REDUCTION OF SHARE CAPITAL AND PURCHASE BY US OF OUR SHARES We may reduce our registered share capital. In the following circumstances, we may repurchase shares, that we issued in the market, subject to a resolution passed in accordance with the provisions of our articles of association and approval by the securities regulatory authorities: - to cancel shares by way of reduction of capital; - to merge with another company that holds our shares; or - other circumstances permitted by laws and regulations. Subject to approval by PRC securities regulatory authorities and compliance with applicable law, we may carry out a share repurchase by one of the following methods: - under a general offer; - on a stock exchange; or - by off-market contract. We may, with the prior approval of shareholders in general meeting obtained in accordance with our articles of association, repurchase our shares by an off-market contract, and we may rescind or vary such a contract or waive any of our rights under the contract with the prior approval of shareholders obtained in the same manner. A contract to repurchase shares includes (without limitation) an agreement to become obliged to repurchase and an agreement to acquire the right to repurchase our shares. We shall not assign a contract to repurchase our own shares or any rights provided thereunder. 75 Shares repurchased by us shall be canceled and the amount of our registered capital shall be reduced by the par value of those shares. To the extent that shares are repurchased out of an amount deducted from our distributable profits, the amount of our registered capital so reduced shall be transferred to our share common reserve account. Unless we are in the process of liquidation: - where we repurchase our shares at par value, the amount of the total par value shall be deducted from our distributable profits or out of the proceeds of a new issue of shares made for that purpose; and - where Guangshen Railway repurchases its shares at a premium, an amount equivalent to their total par value shall be deducted from our distributable profits or the proceeds of a fresh issue of shares made for that purpose. Payment of the portion in excess of their face value shall be effected as follows: - if the shares being repurchased were issued at par value, payment shall be made out of our distributable profits; and - if the shares being repurchased were issued at a premium, payment shall be made out of our distributable profits or out of proceeds of a new issue of shares made for that purpose, provided that the amount paid out of the proceeds of the new issue may not exceed the lesser of the aggregate of premiums received by us on the issue of the shares repurchased or the current balance of our capital common reserve account (inclusive of the premiums from the fresh issue). Payment by us in consideration for: - the acquisition of rights to repurchase our shares; the variation of any contract to repurchase our shares; or - the release of any of our obligations under any contract to repurchase our shares; shall be made out of our distributable profits. RESTRICTIONS ON CONTROLLING SHAREHOLDERS In addition to obligations imposed by law or required by the stock exchanges on which our shares are listed, a controlling shareholder (as defined below) shall not exercise his or her voting rights in respect of the following matters in a manner prejudicial to the interests of the shareholders generally or of our other shareholders: - to relieve a director or supervisor of his or her duty to act honestly in our best interests; - to approve the expropriation, by a director or supervisor (for his or her own benefit or for the benefit of another person), in any guise, of our assets, including without 76 limitation opportunities advantageous to us; or - to approve the expropriation by a director or supervisor (for his or her own benefit or for the benefit of another person) of the individual rights of other shareholders, including without limitation rights to distributions and voting rights, save and except where it was done pursuant to a restructuring submitted to and approved by our shareholders in accordance with our articles of association. "Controlling shareholder" means a person or a group of persons who satisfies one or more of the following conditions: - he or she alone or the group acting in concert has the power to elect more than half the board of directors; - he or she alone or acting in concert with others has the power to exercise or to control the exercise of 30% or more of our voting rights; - he or she alone or acting in concert with others holds 30% or more of our issued and outstanding shares; or - he or she alone or acting in concert with others in any other manner controls us in fact. CHANGING RIGHTS OF A CLASS OF SHAREHOLDERS Rights conferred on any class of shareholders in the capacity of shareholders may not be varied or abrogated unless approved by a special resolution of shareholders at a general meeting and by holders of shares of that class at a separate meeting conducted in accordance with our articles of association. DUTIES OF DIRECTORS, SUPERVISORS AND OTHER SENIOR OFFICERS IN INTERESTED TRANSACTIONS Where a director, supervisor or other senior officer (or an associate thereof) of ours is in any way materially interested in a contract or transaction or proposed contract or transaction with us (other than his or her contract of service with us), he or she shall declare the nature and extent of his or her interest to the board of directors at the earliest opportunity, whether or not the contract, transaction or proposal is subject to the approval of the board of directors. Unless the interested director, supervisor or other senior officer discloses his or her interests and the contract or transaction is approved by the board of directors at a meeting in which the interested director, supervisor or other senior officer is not counted in the quorum and refrains from voting, a contract or transaction in which that director, supervisor or other senior officer is materially interested is voidable by us except as against a bona fide party to the contract or transaction acting without notice of the breach of duty by the interested director or supervisor or other senior officer. 77 We shall not make a loan to or provide any guarantees in connection with a loan to a director, supervisor or other senior officer of Guangshen Railway or any of their respective associates. However, the following transactions are not subject to this prohibition: - the provision by us of a loan or a guarantee of a loan to one of our subsidiaries; - the provision by us of a loan or a guarantee in connection with a loan or any other funds to any of our directors, supervisors or other senior officers to pay expenditures incurred or to be incurred on our behalf by him or her or for the purpose of enabling him or her to perform his or her duties properly, in accordance with the terms of a service contract approved by the shareholders at a general meeting; and - the provision by us of a loan or a guarantee in connection with a loan to any of our directors, supervisors or other senior officers or their respective associates in the ordinary course of our business on normal commercial terms, provided that the ordinary course of business includes the lending of money or the giving of guarantees. ITEM 10C. MATERIAL CONTRACTS We believe that the material contracts we entered into during the fiscal year of 2003 were all made in the ordinary course of business. ITEM 10D. EXCHANGE CONTROLS The PRC government imposes control over its foreign currency reserves in part through direct regulation of the conversion of renminbi into foreign exchange and through restrictions on foreign trade. Effective January 1, 1994, the dual foreign exchange system in China was abolished in accordance with the notice of the People's Bank of China concerning future reform of the foreign currency control system issued December 1993. The conversion of renminbi into U.S. dollars in China currently must be based on the People's Bank of China rate. The People's Bank of China rate is set based on the previous day's Chinese interbank foreign exchange market rate and with reference to current exchange rates on the world financial markets. Any future devaluation of the renminbi against the U.S. dollar (whether due to a decrease in the foreign currency reserves held by the PRC government or any other reason) will have an adverse effect upon the U.S. dollar equivalent and Hong Kong dollar equivalent of our net income and increase the effective cost of foreign equipment and the amount of foreign currency expenses and liabilities. We have no plans to hedge our currency exposure in the future. No assurance can be given that the Hong Kong dollar to U.S. dollar exchange rate link will be maintained in the future, or, therefore, that the Hong Kong dollar revenues of Guangshen Railway will insulate Guangshen Railway from changes in the renminbi-U.S. dollar and renminbi-HK dollar exchange rates. Furthermore, any change in exchange rates that has a negative effect on the market for the H shares in either the United States or Hong Kong is likely to result in a similar negative effect on the other market. 78 We have been, and will continue to be, affected by changes in exchange rates in connection with our ability to meet our foreign currency obligations and will be affected by such changes in connection with our ability to pay dividends on H shares in Hong Kong dollars and on ADSs in U.S. dollars. As of December 31, 2003, we maintained the equivalent of approximately RMB974.0 million in U.S. dollar or Hong Kong dollar-denominated balances for purposes of satisfying our foreign currency obligations (e.g., to purchase foreign equipment) and paying dividends to our overseas shareholders. See Note 32 to our audited consolidated financial statements. Guangshen Railway believes that it has or will be able to obtain sufficient foreign exchange to continue to satisfy these obligations. Guangshen Railway does not engage in any financial contract or other arrangement to hedge its currency exposure. We are not aware of any other PRC laws, decrees or regulations that restrict the export or import of capital or that affect the remittance of dividends, interest or other payments to non-resident holders. ITEM 10E. TAXATION PRC TAXATION TAX BASIS OF ASSETS As of June 30, 1995, our assets were valued in conjunction with the restructuring. This valuation, which was confirmed by the State Assets Administration Bureau, establishes the tax basis for these assets. INCOME TAX Since January 1, 1994, income tax payable by PRC domestic enterprises, including state-owned enterprises and joint stock companies, has been governed by the PRC Enterprise Income Tax Provisional Regulations and its implementation measures, or EIT regulations, which provide for an income tax rate of 33%, unless a lower rate is provided by law, administrative regulations or State Council regulations. Guangshen Railway is generally subject to tax at a rate of 33% pursuant to the EIT Regulations. However, as a result of our incorporation in the Shenzhen Special Economic Zone, our corporate income tax rate is reduced to 15%. Pursuant to an approval from the Shenzhen Local Tax Bureau dated November 12, 1997, Guangshen Railway was also entitled to a 50% further reduction of income tax arising from our high-speed train services in 1997, 1998 and 1999. To the extent that Guangshen Railway engages in other businesses through subsidiaries, those other companies are subject to corporate income tax rates of either 15% or 33% (applicable to places other than Shenzhen), depending mainly on their places of incorporation. VALUE ADDED TAX Pursuant to the Provisional Regulations of the PRC Concerning Value Added Tax effective from January 1, 1994 and its implementing rules, any goods sold by Guangshen Railway, including any sales at concession stands operated by Guangshen Railway, are subject to value added tax. Value added tax payable is calculated by "output value added tax" minus "input value added tax." Input value added tax payable by Guangshen Railway on purchases is 79 recoverable out of the output value added tax collected from the customers, and any excess of output value added tax over input value added tax paid is payable to the tax authority. The rate of value added tax on inputs and outputs is 17%. BUSINESS TAX Pursuant to the Provisional Regulations of the PRC Concerning Business Tax effective from January 1, 1994 and its implementing rules, business tax is imposed on enterprises that provide transportation services in the PRC. Business tax is levied at a rate of 3% on the transport of passengers and goods in or out of the PRC. TAX ON DIVIDENDS For an Individual Investor. According to the Provisional Regulations of the PRC Concerning Questions of Taxation on Enterprises Experimenting with the Share System promulgated on June 12, 1992, referred to herein as the provisional regulations, an income tax of 20% shall be withheld in accordance with the Individual Income Tax Law of the PRC on dividend payments from such enterprises to an individual. For a foreign individual who is not a resident of the PRC, the receipt of dividends from a company in the PRC is normally subject to this 20%

PRC withholding tax unless reduced by an applicable double-taxation treaty. However, on July 21, 1993, the PRC State Tax Bureau issued a Notice Concerning the Taxation of Gains on Transfers and Dividends from Shares (Equities) Received by Foreign Investment Enterprises, Foreign Enterprises and Foreign Individuals, referred to herein as the tax notice, which stipulates that dividends from a PRC company on shares listed on an overseas stock exchange, or overseas shares, such as H shares (including H shares represented by ADSs), would not for the time being be subject to PRC withholding tax. The relevant tax authority has thus far not collected any withholding tax on dividend payments on overseas shares. Amendments to the Individual Income Tax Law of the PRC were promulgated on October 31, 1993 and became effective on January 1, 1994. These amendments stipulate that any provisions of prior administrative regulations concerning individual income tax that contradict the amendments shall be superseded by the amendments. The amendments and the amended Individual Income Tax Law may be interpreted as meaning that foreign individuals will be subject to a withholding tax on dividends received from a company in the PRC at a rate of 20% unless such income is specifically exempted from individual income tax by the financial authority of the State Council. However, in a letter dated July 26, 1994 to the State Commission for Restructuring the Economic System, the State Securities Commission and the China Securities Regulatory Commission regarding "Relevant Tax Issues on Dividends Received by Foreigners Who Hold Shares of Listed PRC Companies," the State Tax Bureau reiterated the temporary tax exemption stated in the Tax Notice for dividends received from a PRC company listed overseas. As long as this letter is in effect, foreign individual investors will not be subject to the 20% withholding tax on dividends received from such a company. For an Enterprise. When a foreign enterprise with no establishment or office in the PRC receives dividends from a company in the PRC, the foreign enterprise is normally subject to PRC 80 withholding tax of 20% under the IncomeTax Law of the PRC Concerning Enterprises with Foreign Investment and Foreign Enterprises. With respect to dividends paid by a company incorporated in the Shenzhen Special Economic Zone (such as Guangshen Railway), the withholding tax rate is 10%. However, according to the Tax Notice, a foreign enterprise without an establishment in the PRC receiving a dividend payment on overseas shares, such as H shares or ADSs, will not be subject to withholding tax on the dividend payment. CAPITAL GAINS TAX For An Individual Investor. Although the Provisions of Implementation of Individual Income Tax Law of the PRC, issued on January 28, 1994, stipulate that gains realized on the sale of shares by an individual would be subject to income tax at a rate of 20% and empower the Ministry of Finance to draft detailed rules on the mechanism of collecting this tax, the Tax Notice provides that gains realized by holders (both individuals and enterprises) of H shares or ADSs will not be subject to income tax. For An Enterprise. A foreign enterprise with no establishment or office in the PRC is generally subject to a 20% tax on capital gains from the sale of shares in a company in the PRC. However, We believe that the tax exemption on capital gains enjoyed by foreign enterprises pursuant to the Tax Notice continues to be valid. TAX TREATIES Foreign enterprises with no establishment in the PRC and individuals not resident in the PRC and who are resident in countries that have entered into double taxation treaties with the PRC may be entitled to a reduction of any withholding tax imposed on the payment of dividends from a PRC company. The PRC currently has double taxation treaties with a number of countries, including Australia, Canada, France, Germany, Japan, Malaysia, the Netherlands, Singapore, the United Kingdom and the United States. The Agreement Between the Government of the United States of America and the PRC Government for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income, together with related protocols, referred to herein as the US-PRC tax treaty, currently limit the rate of PRC withholding tax upon dividends paid by Guangshen Railway to a United States holder who is a United States resident for purposes of the US-PRC tax treaty to 10%. It is uncertain if the US-PRC tax treaty exempts from PRC tax the capital gains of a U.S. holder arising from the sale or disposition of H shares or ADSs. U.S. holders are advised to consult their tax advisors with respect to these matters. UNITED STATES FEDERAL INCOME TAXATION The following is a general discussion of the material United States federal income tax consequences of purchasing, owning and disposing of the H shares or ADSs if you are a U.S. holder, as defined below, and hold the H shares or ADSs as capital assets within the meaning of Section 1221 of the Internal Revenue Code of 1986, as amended (the "Code"). This discussion does not address all of the tax consequences relating to the purchase, ownership and disposition of the H shares or ADSs, and does not take into account U.S. holders who may be subject to special rules including: 81 - tax-exempt entities; - certain insurance companies; - broker-dealers; - traders in securities that elect to mark to market; - U.S. holders liable for alternative minimum tax; - U.S. holders that own 10% or more of our voting stock; - U.S. holders that hold the H shares or ADSs as part of a straddle or a hedging or conversion transaction; or - U.S. holders whose functional currency is not the U.S. dollar. This discussion is based on the Code, its legislative history, final, temporary and proposed United States Treasury regulations promulgated thereunder, published rulings and court decisions as in effect on the date hereof, all of which are subject to change, or changes in interpretation, possibly with retroactive effect. In addition, this discussion is based in part upon representations of the depositary and the assumption that each obligation in the deposit agreement and any related agreements will be performed according to its terms. You are a "U.S holder" if you are: - a citizen or resident of the United States for United States federal income tax purposes; - a corporation, or other entity treated as a corporation for United States federal income tax purposes, created or organized under the laws of the United States or any political subdivision thereof; - an estate the income of which is subject to United States federal income tax without regard to its source; or - a trust: -- subject to the primary supervision of a United States court and the control of one or more United States persons; or -- that has elected to be treated as a United States person under applicable United States Treasury regulations. If a partnership holds the H shares or ADSs, the tax treatment of a partner generally will depend on the status of the partner and the activities of the partnership. If you are a partner of a 82 partnership that holds the H sharesor ADSs, we urge you to consult your tax advisors regarding the consequences of the purchase, ownership and disposition of the H shares or ADSs. This discussion does not address any aspects of United States taxation other than federal income taxation. WE URGE YOU TO CONSULT YOUR TAX ADVISORS REGARDING THE UNITED STATES FEDERAL, STATE, LOCAL AND NON-UNITED STATES TAX CONSEQUENCES OF THE PURCHASE, OWNERSHIP AND DISPOSITION OF THE H SHARES OR ADSs. In general, if you hold ADRs evidencing ADSs, you will be treated as the owner of the H shares represented by the ADSs. The following discussion assumes that we are not a passive foreign investment company ("PFIC"), as discussed under "PFIC Rules" below. DISTRIBUTIONS ON THE H SHARES OR ADSS The gross amount of any distribution (without reduction for any Chinese tax withheld) we make on the H shares or ADSs out of our current or accumulated earnings and profits (as determined for United States federal income tax purposes) will be includible in your gross income as dividend income when the distribution is actually or constructively received by you, in the case of the H shares, or by the depositary in the case of ADSs. Subject to certain limitations, dividends paid to non-corporate U.S. holders, including individuals, may be eligible for a reduced rate of taxation if we are deemed to be a "qualified foreign corporation" for U.S. federal income tax purposes. A qualified foreign corporation includes: - a foreign corporation that is eligible for the benefits of a comprehensive income tax treaty with the United States that includes an exchange of information program; and - a foreign corporation if its stock with respect to which a dividend is paid (or ADSs backed by such stock) is readily tradable on an established securities market within the United States, but does not include an otherwise qualified foreign corporation that is a PFIC. We believe that we will be a qualified foreign corporation so long as we are not a PFIC and we are considered eligible for the benefits of the Agreement between the Government of the United States of America and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income (the "Treaty"). Our status as a qualified foreign corporation, however, may change. Distributions that exceed our current and accumulated earnings and profits will be treated as a return of capital to you to the extent of your basis in the H shares or ADSs and thereafter as capital gain. Any dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from United States corporations. The amount of any distribution of property other than cash will be the fair market value of such property on the date of such distribution. 83 If we make a distribution paid in HK dollars, you will be considered to receive the U.S. dollar value of the distribution determined at the spot HK dollar/U.S. dollar rate on the date such distribution is received by you or by the depositary, regardless of whether you or the depositary convert the distribution into U.S. dollars. Any gain or loss resulting from currency exchange fluctuations during the period from the date the dividend payment is includible in your income to the date you or the depositary convert the distribution into U.S. dollars will be treated as United States source ordinary income or loss for foreign tax credit limitation purposes. Subject to various limitations, any Chinese tax withheld from distributions in accordance with Chinese law, as limited by the Treaty, will be deductible or creditable against your United States federal income tax liability. For foreign tax credit limitation purposes, dividends paid on the H shares or ADSs will be foreign source income, and generally will be treated as "passive income" or, in the case of some U.S. holders, "financial services income." You may not be able to claim a foreign tax credit (and instead may claim a deduction) for non-United States taxes imposed on dividends paid on the H Shares or ADSs if you (i) have held the H Shares or ADSs for less than a specified minimum period during which you are not protected from risk of loss with respect to such shares, (ii) are obligated to make payments related to the dividends (for example, pursuant to a short sale) or (iii) hold the H shares or ADSs in an arrangement in which your expected economic return, after non-United States taxes, is insubstantial. SALE, EXCHANGE OR OTHER DISPOSITION Upon a sale, exchange or other disposition of the H shares or ADSs, you will recognize a capital gain or loss for United States federal income tax purposes in an amount equal to the difference between the U.S. dollar value of the amount realized and your tax basis, determined in U.S. dollars, in such H shares or ADSs. Any gain or loss will generally be United States source gain or loss for foreign tax credit limitation purposes. Capital gain of certain non-corporate U.S. holders, including individuals, is generally taxed at a maximum rate of 15% where the property has been held more than one year. Your ability to deduct capital losses is subject to limitations. If you are paid in a currency other than U.S. dollars, any gain or loss resulting from currency exchange fluctuations during the period from the date of the payment resulting from sale, exchange or other disposition to the date you convert the payment into U.S. dollars will be treated as United States source ordinary income or loss. PFIC RULES In general, a foreign corporation is a PFIC for any taxable year in which, after applying relevant look-through rules with respect to the income and assets of subsidiaries: - 75% or more of its gross income consists of passive income, such as dividends, interest, rents and royalties; or - 50% or more of the average quarterly value of its assets consists of assets that produce, or are held for the production of, passive income. 84 We believe that we will not meet either of the PFIC tests in the current or subsequent taxable years and therefore will not be treated as a PFIC for such periods. However, there can be no assurance that we will not be a PFIC in the current or subsequent taxable years. If we were a PFIC in any taxable year that you held the H shares or ADSs, you generally would be subject to special rules with respect to "excess distributions" made by us on the H shares or ADSs and with respect to gain from your disposition of the H shares or ADSs. An "excess distribution" generally is defined as the excess of the distributions you receive with respect to the H shares or ADSs in any taxable year over 125% of the average annual distributions you have received from us during the shorter of the three preceding years, or your holding period for the H shares or ADSs. Generally, you would be required to allocate any excess distribution or gain from the disposition of the H shares or ADSs ratably over your holding period for the H shares or ADSs. The portion of the excess distribution or gain allocated to a prior taxable year, other than a year prior to the first year in which we became a PFIC, would be taxed at the highest United States federal income tax rate on ordinary income in effect for such taxable year, and you would be subject to an interest charge on the resulting tax liability, determined as if the tax liability had been due with respect to such particular taxable years. The portion of the excess distribution or gain that is not allocated to prior taxable years, together with the portion allocated to the years prior to the first year in which we became a PFIC, would be included in your gross income for the taxable year of the excess distribution or disposition and taxed as ordinary income. The foregoing rules with respect to excess distributions and dispositions may be avoided or reduced if you are eligible for and timely make a valid "mark-to-market" election. If your H shares or ADSs were treated as shares regularly traded on a "qualified exchange" for United States federal income tax purposes and a valid mark-to-market election was made, in calculating your taxable income for each taxable year you generally would be required to take into account as ordinary income or loss the difference, if any, between the fair market value and the adjusted tax basis of your H shares or ADSs at the end of your taxable year. However, the amount of loss you would be allowed is limited to the extent of the net amount of previously included income as a result of the mark-to-market election. The New York Stock Exchange on which the ADSs are traded is a qualified exchange for United States federal income tax purposes. Alternatively, a timely election to treat us as a qualified electing fund under Section 1295 of the Code could be made to avoid the foregoing rules with respect to excess distributions and dispositions. You should be aware, however, that if we become a PFIC, we do not intend to satisfy record keeping requirements that would permit you to make a qualified electing fund election. If you own the H shares or ADSs during any year that we are a PFIC, you must file Internal Revenue Service ("IRS") Form 8621. We encourage you to consult your own tax advisor concerning the United States federal income tax consequences of holding the H shares or ADSs that would arise if we were considered a PFIC. 85 BACKUP WITHHOLDING AND INFORMATION REPORTING In general, information reporting requirements will apply to dividends in respect of the H shares or ADSs or the proceeds of the sale, exchange, or redemption of the H shares or ADSs paid within the United States, and in some cases, outside of the United States, other than to various exempt recipients, including corporations. In addition, you may, under some circumstances, be subject to "backup withholding" with respect to dividends paid on the H shares or ADSs or the proceeds of any sale, exchange or transfer of the H shares or ADSs, unless you - are a corporation or fall within various other exempt categories, and, when required, demonstrate this fact; or - provide a correct taxpayer identification number on a properly completed IRS Form W-9 or a substitute form, certify that you are exempt from backup withholding and otherwise comply with applicable requirements of the backup withholding rules. Any amount withheld under the backup withholding rules generally will be creditable against your United States federal income tax liability provided that you furnish the required information to the IRS in a timely manner. If you do not provide a correct taxpayer identification number you may be subject to penalties imposed by the IRS. HONG KONG TAXATION The following discussion summarizes the material Hong Kong tax provisions relating to the ownership of H shares or ADSs held by you. DIVIDENDS No tax will be payable by you in Hong Kong in respect of dividends paid by us. TAXATION OF CAPITAL GAINS No capital gain tax is generally imposed in Hong Kong in respect of capital gains from the sale of property (such as the H Shares). However, if trading gains from the sale of property by persons as part of profit making are regarded as carrying on a trade, profession or business in Hong Kong, where such gains are derived from or arise in Hong Kong from such trade, profession or business, such trading gains will be chargeable to Hong Kong profits tax, which is currently imposed at the rate of 16% on corporations and at a maximum rate of 15% on individuals. Amendments to increase the Hong Kong profits tax to 17.5% for corporations and 15.5% for individuals have been proposed by the Financial Secretary. However, as of the date of this annual report, such proposals have not yet been adopted. Gains from sales of the H Shares effected on the Hong Kong Stock Exchange will be considered to be derived from or arise in Hong Kong. Liability for Hong Kong profits tax would thus arise in respect of trading gains from sales of H shares realized by persons carrying on a business of trading or dealing in Hong Kong in securities. 86 There will be no liability for Hong Kong profits tax in respect of profits from the sale of ADSs (i.e., the profits derived abroad), where purchases and sales of ADSs are effected outside Hong Kong, e.g. on the New York Stock Exchange. HONG KONG STAMP DUTY Hong Kong stamp duty will be payable by each of the seller and the purchaser for every sale and purchase, respectively, of the H shares. An ad valorem duty is charged at the rate of 0.2% of the value of the H shares transferred and the relevant contract notes shall be stamped (the buyer and seller each paying half of such stamp duty). In addition, a fixed duty of HK$5 is currently payable on an instrument of transfer of H shares. The withdrawal of H shares when ADSs are surrendered, and the issuance of ADSs when H shares are deposited, may be subject to Hong Kong stamp duty at the rate described above for sale and purchase transactions, if the withdrawal or deposit results in a change of legal and beneficial ownership under Hong Kong law. The issuance of ADSs for deposited H shares issued directly to the depositary or for the account of the depositary should not lead to a Hong Kong stamp duty liability. You are not liable for the Hong Kong stamp duty payable on transfers of ADSs outside of Hong Kong. HONG KONG ESTATE DUTY Estate duty is levied on the value of property situated in Hong Kong passing or deemed passing on the death of a person. H shares are regarded as property situated in Hong Kong for estate duty purposes. Currently, for persons dying on or after April 1, 1998, Hong Kong estate duty is imposed on the principal value of a deceased's estate at graduated rates from 5% to 15%. No estate duty is payable where the principal value of the dutiable estate does not exceed HK$7.5 million; the maximum rate of 15% applies where the principal value exceeds HK$10.5 million. ITEM 10F. DIVIDENDS AND PAYING AGENTS Not applicable. ITEM 10G. STATEMENT BY EXPERTS Not applicable. ITEM 10H. DOCUMENTS ON DISPLAY We filed with SEC in Washington, D.C. a registration statement on Form F-1 (Registration No.333-3382) under the Securities Act in connection with our global offering of American depositary shares in May 1996. The registration statement contains exhibits and schedules. For further information with respect to Guangshen Railway and our American depositary shares, please refer to the registration statement and to the exhibits and schedules filed with the registration statement. 87 Additionally, we are subject to the informational requirements of the Exchange Act, and, in accordance with the Exchange Act, we file annual reports on Form 20-F within six months of our fiscal year end, and we will submit other reports and information under cover of Form 6-K with the SEC. You may review a copy of the registration statement and other information without charge at the public reference facilities maintained by the SEC at Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. You may also inspect the registration statement and its exhibits and schedules at the office of the New York Stock Exchange, 11 Wall Street, New York, New York 10005. You may also get copies, upon payment of a prescribed fee, of all or a portion of the registration statement from the SEC's public reference room or by calling the SEC on 1-800-SEC-0330 or visiting the SEC's website at www.sec.gov. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of proxy statements to shareholders. ITEM 10I. SUBSIDIARY INFORMATION Not applicable. ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK The following paragraphs describe the various market risks to which we were exposed as of December 31, 2003. CURRENCY RISK As approved by the PRC foreign exchange administration, Hong Kong dollar-denominated income from our through train service may be deposited by us in Hong Kong dollars up to an amount equivalent to US$18.5 million and need not be converted into renminbi. If necessary, we had U.S. dollar-denominated payment of Hong Kong dollar-denominated and U.S. dollar-denominated dividends on our H shares and ADSs, respectively, in excess of the foregoing limit have to be made after reconverting renminbi at the then applicable People's Bank of China rate into the relevant foreign currency. Some of our vendor contracts and equipment leases for the provision of equipment, parts and services, particularly with respect to the high-speed project, are paid by us in foreign currencies. As of December 31, 2003, time deposits with maturities of more than three months in an amount equivalent to RMB807.8 million, and Hong Kong dollar denominated time deposits with maturities of more than three months in an amount equivalent to RMB91.1 million. Our cash, bank deposits and time deposits with maturities of no more than three months consist of deposits denominated in U.S. dollar in an amount equivalent to RMB9.2 million, and deposits denominated in Hong Kong dollar in an amount equivalent to RMB65.9 million. While our foreign currency deposits are relatively stable, they are insufficient to pay all dividends and operating expenses, therefore, we bear the risk of exchange rate fluctuations when we convert renminbi to pay foreign-currency denominated dividends and operating expenses. However, our management believes that these contingent exposures relating to foreign exchange rate fluctuations have not had and are not likely to have a material effect on our financial position. As a result, we do not enter into any hedging transactions with respect to our exposure to foreign currency movements. Furthermore, we are not aware of any effective financial hedging products that serve as protection against a possible renminbi devaluation. 88 INTEREST RATE RISK Funds that we do not need in the short term are kept as temporary cash deposits in commercial banks and in the Ministry of Railways Deposit-Taking Center in the form of demand or time deposits. We do not hold any market risk-sensitive instruments for trading purposes. As of December 31, 2003, we had no loans outstanding. Accordingly, we are not exposed to any material interest rate risks. As of December 31, 2003, our balances denominated in Hong Kong dollars and U.S. dollars were translated into renminbi at the applicable market exchange rates as of that date and amounted to approximately RMB974.0 million. If the applicable market exchange rates were to change by 10%, this would result in a change in fair value of approximately RMB97.4 million in these balances. For the year ended December 31, 2003, the interest income derived from our cash balances at banks and temporary cash investments amounted to approximately RMB28.0 million. A 10% change in interest rates would have resulted in a change in interest income of approximately RMB2.8 million. Except as described above and in notes 26 and 27 to our audited consolidated financial statements herein, our management believes that as of the end of December 31, 2003, at present and in our normal course of business, we are not subject to any other market-related risks. ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES Not applicable. 89 PART II ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES None. ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS None. ITEM 15. CONTROLS AND PROCEDURES DISCLOSURE CONTROLS AND PROCEDURES Our Chairman of the Board, our General Manager, and our Chief Accountant, after evaluating the effectiveness of our disclosure controls and procedures (as defined in US Exchange Act Rules 13a-15(e)) as of the end of the period covered by this Form 20-F, have concluded that, as of such date, our disclosure controls and procedures were effective. INTERNAL CONTROL OVER FINANCIAL REPORTING There were no changes in our internal control over financial reporting that occurred during the year ended December 31, 2003 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT Our Board of Directors has determined that none of our current audit committee members is an "audit committee financial expert" as defined in the Instruction to paragraph (a) of Item 16A to Form 20-F. We are in discussions with potential candidates who are qualified as such regarding their appointment as audit committee members of our company. We have not been able to agree commercially reasonable terms with these candidates as of the date of this annual report but expect to have such an "audit committee financial expert" appointed to our audit committee by December 31, 2004. ITEM 16B. CODE OF ETHICS We have adopted a code of ethics that applies to our Chief Executive Officer, President, Chief Financial Officer and Corporate Controller. See Exhibit 11.1. ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES On June 10, 2003, resolutions were passed at the annual general meeting of Guangshen Railway to appoint PricewaterhouseCoopers (certified public accountants in Hong Kong, "PwC") as our international auditors for 2003. Resolutions to re-appoint PwC 90 firms as our international auditors for 2004 have been approved at the annual general meeting of Guangshen Railway held on June 10, 2004. PwC was our international

auditors for 2002 and Arthur Andersen was our international auditors for 2001. The following table presents the aggregate fees for professional services and other services rendered by PwC to us in 2003 and 2002. 2003 2002 -------- RMB MILLIONS Audit Fees 2.0 2.0 Audit-related Fees - - Tax Fees - - All Other Fees - - Total 2.0 2.0 Other than the audits performed on our financial statements, PwC did not provide any services to us in 2002 and 2003. The working charter of our audit committee, which was adopted by our board of directors on August 30, 2000 based on the applicable guidelines set forth in the Hong Kong Stock Exchange Listing Rules, provides that our audit committee is responsible for, among other matters, supervising the audit of our Company, including the assessment and evaluation of the nature, quality and scope of work and the fees of our external auditors. Pursuant to paragraph (c)(7)(i)(A) of Rule 2-01 of Regulation S-X, the engagement of PwC to perform these audit services were approved by our audit committee. ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES Not applicable. ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS Not applicable. 91 PART III ITEM 17. FINANCIAL STATEMENTS We have elected to provide the financial statements and related information specified in Item 18 in lieu of Item 17. ITEM 18. FINANCIAL STATEMENTS See pages F-1 to F-44 following Item 19. ITEM 19. EXHIBITS (a) See pages F-1 to F-41 following this item. (b) Index of Exhibits Documents filed as exhibits to this annual report: Exhibit Number Description ---------------- 1.1 Articles of Association 6.1 Statement explaining how earnings per share information was calculated in this annual report 7.1 Statements explaining how certain ratios are calculated in this annual report 8.1 List of significant subsidiaries of Guangshen Railway Company Limited as of December 31, 2003 11.1 Code of Ethics for the Senior Officers 12.1 Section 302 principal executive officers' and principal financial officer's certifications 13.1 Certifications of principal executive officers and principal financial officer pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of the U.S. Sarbanes-Oxley Act of 2002. 92 INDEX TO FINANCIAL STATEMENTS Page ---- GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES Report of Independent Public Accountants F-2 Consolidated Income Statements for the years ended 31 December, 2001, 2002 and 2003 F-4 Consolidated Balance Sheets as of 31 December, 2002 and 2003 F-5 Consolidated Cash Flow Statements for the years ended 31 December 2001, 2002 and 2003 F-6 Consolidated Statements of Changes in Equity for the years ended 31 December 2001, 2002 and 2003 F-7 Notes to the Consolidated Financial Statements F-8 [PRICEWATERHOUSECOOPERS LOGO] REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS To the Board of Directors and Shareholders of Guangshen Railway Company Limited: In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of cash flows and of changes in shareholders' equity present fairly, in all material respects, the financial position of Guangshen Railway Company Limited (the "Company") and its subsidiaries (established in the People's Republic of China) at December 31, 2003 and 2002, and the results of their operations and their cash flows for the years then ended, in conformity with International Financial Reporting Standards. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with International Standards on Auditing issued by the International Federation of Accountants and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. The consolidated financial statements of the Company and its subsidiaries as of December 31, 2001 were audited by other independent accountants who have ceased operations. Those independent accountants expressed an unqualified opinion on those financial statements in their report dated April 23, 2002. International Financial Reporting Standards vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in Note 30 to the consolidated financial statements.
PRICEWATERHOUSECOOPERS Certified Public Accountants Hong Kong April 20, 2004 F-2 THE FOLLOWING REPORT IS A COPY OF A REPORT PREVIOUSLY ISSUED BY ARTHUR ANDERSEN & CO AND HAS NOT BEEN REISSUED BY ARTHUR ANDERSEN & CO: (THE BALANCE SHEET AS OF 31 DECEMBER, 2000 AND THE CONSOLIDATED STATEMENTS OF INCOME, CHANGES IN EQUITY AND CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 1999 AND 2000 ARE NOT REPRODUCED) REPORT OF INDEPENDENT

PUBLIC ACCOUNTANTS To the Shareholders of Guangshen Railway Company Limited: We have audited the accompanying Consolidated Balance Sheets of Guangshen Railway Company Limited (the "Company") and its subsidiaries (established in the People's Republic of China) as of 31 December, 2000 and 2001, and the related Consolidated Statements of Income, Changes in Equity and Cash Flows for the years ended 31 December, 1999, 2000 and 2001, expressed in Chinese Renminbi. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these Consolidated Financial Statements based on our audits. We conducted our audits in accordance with international standards on auditing issued by the International Federation of Accountants and generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the Consolidated Financial Statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Consolidated Financial Statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. In our opinion, the accompanying Consolidated Financial Statements referred to above present fairly, in all material respects, the financial position of the Company and its subsidiaries as of 31 December, 2000 and 2001, and the results of their operations and cash flows for the years ended 31 December, 1999, 2000 and 2001 in conformity with International Financial Reporting Standards. International Financial Reporting Standards do not conform to generally accepted accounting principles in the United States of America. A description of the significant differences between those two generally accepted accounting principles and the approximate effect of those differences on net income and shareholders' equity are set forth in Note 30 to the Consolidated Financial Statements. ARTHUR ANDERSEN & CO Certified Public Accountants Hong Kong April 23, 2002 F-3 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES CONSOLIDATED INCOME STATEMENTS FOR THE YEARS ENDED 31st DECEMBER, 2001, 2002 AND 2003 (Amounts in thousands, except per share and per ADS data) Years ended 31 December, --------------------------------------------------- Notes 2001 2002 2003 2003 ----- --------- --------- --------- ------- RMB RMB RMB US$ Revenues from railroad businesses Passenger 1,426,010 1,846,599 1,754,223 211,352 Freight 567,276 514,036 514,794 62,023 ---------- ---------- ---------- -------- Sub-total 1,993,286 2,360,635 2,269,017 273,375 Revenues from other businesses 160,306 156,893 144,370 17,394 ---------- ---------- ---------- -------- Total revenues 2,153,592 2,517,528 2,413,387 290,769 ---------- ---------- ---------- -------- Operating expenses Railroad businesses Labour and benefits (320,569) (373,781) (347,649) (41,885) Equipment leases and services (262,320) (433,918) (437,739) (52,740) Materials and supplies (144,651) (192,141) (216,993) (26,144) Repair costs, excluding materials and supplies (94,545) (102,377) (89,640) (10,800) Depreciation (342,534) (335,508) (290,014) (34,941) Amortisation of leasehold land payments (15,453) (15,131) (15,602) (1,880) Fees for social services (57,157) (57,385) (62,579) (7,540) General and administrative expenses 4 (150,162) (123,800) (134,688) (16,227) Others (73,238) (101,251) (113,382) (13,660) ---------- ---------- ---------- -------- Sub-total (1,460,629) (1,735,292) (1,708,286) (205,817) ---------- ---------- ---------- -------- Other businesses Materials and supplies (108,930) (124,602) (112,677) (13,576) General and administrative expenses 4 (29,922) (35,137) (29,711) (3,580) ---------- ---------- ---------- -------- Sub-total (138,852) (159,739) (142,388) (17,156) ---------- ---------- ---------- -------- Total operating expenses (1,599,481) (1,895,031) (1,850,674) (222,973) ---------- ---------- ---------- -------- Profit from operations 554,111 622,497 562,713 67,796 Other income 5 12,952 6,575 17,586 2,119 Interest income, net 6 63,621 32,712 27,287 3,288 Share of profits / (losses) of associates 16 609 (323) (2,508) (302) ---------- ---------- ---------- -------- Profit before tax 631,293 661,461 605,078 72,901 Income tax expense 7 (99,297) (104,265) (93,348) (11,247) Minority interests 1,499 (113) 32 4 ---------- ---------- ---------- -------- Profit attributable to shareholders 533,495 557,083 511,762 61,658 ========== ========== ========== ======== Earnings per share - Basic 8 RMB0.12 RMB0.13 RMB 0.12 US$0.01 ========== ========== ========== ======== - Diluted 8 N/A N/A N/A N/A ========== ========== ========== ======== Earnings per equivalent ADS - Basic 8 RMB6.15 RMB6.42 RMB 5.90 US$0.71 ========== ========== ========== ======== - Diluted 8 N/A N/A N/A N/A ========== ========== ========== ======== The accompanying notes are an integral part of these Consolidated Income Statements. ------------------- Translation of amounts from Renminbi ("RMB") into United States dollars ("US$") for the convenience of the reader has been made at the Noon Buying Rate on 31 December, 2003 of US$1.00=RMB8.3 as certified for customs purposes by the Federal Reserve Bank of New York. No representation is made that the RMB amounts could have been, or could be, converted into US$ at that rate on 31 December, 2003. F-4 GUANGSHEN

RAILWAY COMPANY LIMITED AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS AS OF 31 DECEMBER, 2002 AND 2003 (Amounts in thousands) 31 December, ------------------------------------ Notes 2002 2003 2003 ----- ---------- ---------- --------- RMB RMB US$ ASSETS Current assets Cash and cash equivalents 1,413,045 1,402,359 168,959 Temporary cash investments 10 567,339 627,440 75,595 Interest receivables 18,851 25,497 3,072 Trade receivables 11 51,457 80,614 9,713 Materials and supplies 34,105 38,692 4,662 Prepayments and other receivables, net 12 241,224 223,463 26,923 Due from Parent Company 39,374 - - Due from related parties 267,885 199,921 24,087 ---------- ---------- --------- Total current assets 2,633,280 2,597,986 313,011 Fixed assets 13 6,798,280 6,952,878 837,696 Construction-in-progress 14 672,827 390,393 47,035 Leasehold land payments 15 656,998 652,083 78,564 Interests in associates 16 140,842 140,494 16,927 Available-for-sale investments 17 166,695 167,962 20,236 Deferred tax assets 18 7,577 6,154 741 Deferred staff costs 19 181,095 166,003 20,000 ---------- ---------- --------- Total assets 11,257,594 11,073,953 1,334,210 ========== ========== ========= LIABILITIES AND EQUITY Current liabilities Trade payables 41,734 34,625 4,172 Payables for construction of fixed assets 181,473 148,258 17,862 Accrued expenses and other payables 20 529,797 358,287 43,167 Due to Parent Company - 37,230 4,486 Due to related parties 158,199 120,605 14,531 Dividend payable 90,663 232 28 ---------- ---------- --------- Total current liabilities 1,001,866 699,237 84,246 ---------- ---------- --------- Minority interests 11,577 52,358 6,308 ---------- ---------- --------- Equity Common stock, par value RMB1.00 per share, 4,335,550 shares authorised and outstanding 21 4,335,550 4,335,550 522,355 Additional paid-in capital 3,984,135 3,984,135 480,016 Dedicated capital 1,287,370 1,368,627 164,895 Retained earnings 637,096 634,046 76,390 ---------- ---------- --------- Total equity 10,244,151 10,322,358 1,243,656 ---------- ---------- --------- Total liabilities and equity 11,257,594 11,073,953 1,334,210 ========== ========== ========= The accompanying notes are an integral part of these Consolidated Balance Sheets. ------------------- Translation of amounts from Renminbi ("RMB") into United States dollars ("US$") for the convenience of the reader has been made at the Noon Buying Rate on 31 December, 2003 of US$1.00=RMB8.3 as certified for customs purposes by the Federal Reserve Bank of New York. No representation is made that the RMB amounts could have been, or could be, converted into US$ at that rate on 31 December, 2003. F-5 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES CONSOLIDATED CASH FLOW STATEMENTS FOR THE YEARS ENDED 31 DECEMBER, 2001, 2002 AND 2003 (Amounts in thousands) Year ended 31 December, ------------------------------------------ 2001 2002 2003 2003 -------- --------- --------- ------- RMB RMB RMB US$ CASH FLOWS FROM OPERATING ACTIVITIES: Profit attributable to shareholders 533,495 557,083 511,762 61,658 Adjustments for: Minority interests (1,499) 113 (32) (4) Income tax expense 99,297 104,265 93,348 11,247 Depreciation 345,949 337,797 291,653 35,139 Amortisation of leasehold land payments 15,453 15,131 15,602 1,881 Loss on disposals of fixed assets 25,448 29,339 16,935 2,040 Amortisation of deferred staff costs 15,721 15,092 15,092 1,818 Share of (profits) / losses of associates (609) 323 2,508 302 Provision for doubtful accounts 29,620 4,598 172 21 Interest expense 2,087 4,064 2,359 284 Interest income (65,708) (36,920) (29,755) (3,585) Decrease / (increase) in current assets Trade receivables 4,597 24,064 (28,621) (3,448) Materials and supplies (4,158) 86 (4,587) (553) Prepayments and other receivables (141,067) 87,676 17,320 2,088 Due from Parent Company 51,105 (9,875) - - Due from related parties (28,081) 8,128 66,179 7,973 Increase / (decrease) in current liabilities Trade payables 7,901 (27,314) (7,109) (857) Due to Parent Company - - (13,821) (1,665) Due to related parties (5,084) 99,549 (37,594) (4,529) Accrued expenses and other payables 102,329 48,529 (10,924) (1,317) Interest paid (2,087) (4,064) (2,359) (284) Tax paid (98,693) (100,487) (99,679) (12,010) -------- --------- --------- ------- Net cash provided by operating activities 886,016 1,157,177 798,449 96,199 -------- --------- --------- ------- CASH FLOWS FROM INVESTING ACTIVITIES: Purchase of fixed assets and payments for construction-in-progress (551,508) (553,337) (339,208) (40,868) Proceeds from sale of fixed assets - 12,369 1,105 133 Increase in interests in associates (17,572) (4,761) (374) (45) Decrease / (increase) in temporary cash investments 74,728 777,898 (60,101) (7,241) Purchase of available-for-sale investments (2,000) (14,108) - - Interest received 65,927 32,942 23,109 2,784 -------- --------- --------- ------- Net cash / (used in) from investing activities (430,425) 251,003 (375,469) (45,237) -------- --------- --------- ------- CASH FLOWS FROM FINANCING ACTIVITIES: Dividends paid to group shareholders (419,957) (356,490) (433,561) (52,236) Dividends paid to minority interests (180) (4,153) (105) (13) -------- --------- --------- ------- Net cash used in financing activities (420,137) (360,643) (433,666) (52,249) -------- --------- --------- ------- Net increase / (decrease) in cash and cash equivalents 35,454 1,047,537 (10,686) (1,287) Cash and cash equivalents, beginning of year 330,054 365,508 1,413,045 170,246 -------- --------- --------- ------- Cash and cash equivalents, end of year* 365,508 1,413,045 1,402,359 168,959 ======== ========= ========= ======= * Analysis of the balances of cash and cash equivalents Year ended 31 December, ---------------------------------------- 2001 2002 2003 2003 ------- --------- --------- ------- RMB RMB RMB US$ Cash and bank deposits 365,508 1,413,045 1,402,359 168,959 ======= ========= ========= ======= The accompanying notes are an integral part of these Consolidated Cash Flow Statements. ------------------ Translation of amounts from Renminbi ("RMB") into United States dollars ("US$") for the convenience of the reader has been made at the Noon Buying Rate on 31 December, 2003 of US$1.00=RMB8.3 as certified for customs purposes by the Federal Reserve Bank of New York. No representation is made that the RMB amounts could have been, or could be, converted into US$ at that rate on 31 December, 2003. F-6 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED 31 DECEMBER, 2001, 2002 AND 2003 (Amounts in thousands) Dedicated capital ------------------------------------ Share capital/ Additional Statutory Statutory Discretionary common paid-in surplus public surplus Retained Note stock Capital reserve welfare fund reserve earnings Total ---- --------- --------- ------- ----------- ------- -------- ---------- RMB RMB RMB RMB RMB RMB RMB Balances at January 1, 2001 4,335,550 3,984,135 375,448 368,706 341,659 615,185 10,020,683 Profit attributable to shareholders - - - - - 533,495 533,495 Appropriation from retained earnings 22 - - 56,660 55,862 - (112,522) - Dividends relating to 2000 9 - - - - - (433,555) (433,555) --------- --------- ------- ------- ------- -------- ---------- Balances at January 1, 2002 4,335,550 3,984,135 432,108 424,568 341,659 602,603 10,120,623 Profit attributable to shareholders - - - - - 557,083 557,083 Appropriation from retained earnings 22 - - 59,301 29,734 - (89,035) - Dividends relating to 2001 9 - - - - - (433,555) (433,555) --------- --------- ------- ------- ------- -------- ---------- Balances at January 1, 2003 4,335,550 3,984,135 491,409 454,302 341,659 637,096 10,244,151 Profit attributable to shareholders - - - - - 511,762 511,762 Appropriation from retained earnings 22 - - 54,165 27,092 - (81,257) - Dividends relating to 2002 9 - - - - - (433,555) (433,555) --------- --------- ------- ------- ------- -------- ---------- Balances at 31 December, 2003 4,335,550 3,984,135 545,574 481,394 341,659 634,046 10,322,358 ========= ========= ======= ======= ======= ======== ========== The accompanying notes are an integral part of these Consolidated Statements of Changes in Equity. F-7 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 1. ORGANISATION AND PRINCIPAL ACTIVITIES Guangshen Railway Company Limited (the "Company") was established as a joint stock limited company in the People's Republic of China (the "PRC") on 6 March, 1996 to take over and operate certain railroad and other businesses (the "Businesses"). Prior to the formation of the Company, the Businesses were carried on by the Company's predecessor, Guangshen Railway Company (the "Predecessor"), and certain of its subsidiaries, and in certain cases, by Guangzhou Railway (Group) Company (the "Parent Company") and certain of its subsidiaries, which were all under the common control and jurisdiction of the PRC Ministry of Railways (the "MOR"). The Predecessor was controlled by and under the administration of the Parent Company. Pursuant to a restructuring agreement entered into among the Parent Company, the Predecessor and the Company on 8 March, 1996 and with effect from 6 March, 1996 (the "Restructuring Agreement"), the Company issued to the Parent Company 100% of its equity interest in the form of 2,904,250,000 shares of ordinary shares (the "State-owned Domestic Shares") in exchange for the assets and liabilities of the Businesses (the "Restructuring"). In May 1996, the Company issued 1,431,300,000 shares, represented by 217,812,000 H Shares ("H Shares") and 24,269,760 American Depositary Shares ("ADSs", one ADS represents 50 H Shares) in a global public offering for cash of approximately RMB4,214,000,000 to finance the capital expenditures and working capital requirements of the Company and its subsidiaries (the "Group"). The principal activities of the Group are railroad passenger and freight transportation. The Group also operate certain other businesses, principally services in the stations and sales of food, beverages and merchandise aboard the trains and in the stations. The directors of the Company considered Guangzhou Railway (Group) Company, a state-owned enterprise established in the PRC, to be the ultimate holding company. The Group conduct their operations in the PRC and accordingly are subject to special considerations and significant risks not typically associated with investments in equity securities of North American and Western European companies. These include risks associated with, among others, the political, economic and legal environments, foreign currency exchange, government regulation of the railway system, development and competition in the transportation industry, insurance, entry by the PRC with the World Trade Organisation (the "WTO"), and the ability to obtain sufficient financing. These are described further in the following paragraphs: (a) Political environment The operating results of the Group may be adversely affected by changes in the political and social conditions in the PRC and by changes in governmental policies with respect to laws and regulations, inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things. While the PRC's government is expected to continue its economic reform policies, many of the reforms are new or experimental and may be refined or changed. It is also possible that a change in the PRC's leadership could lead to changes in economic policy. F-8 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 1. ORGANISATION AND PRINCIPAL ACTIVITIES (CONT'D) (b) Economic environment The economy of the PRC differs significantly from the economies in the North America and Western Europe in many respects, including its structure, levels of development and capital reinvestment, growth rate, government involvement, resource allocation, self-sufficiency, rate of inflation and balance of payments position. The adoption of economic reform policies since 1978 has resulted in a gradual reduction in the role of state economic plans in the allocation of resources, pricing and management of such assets, and increased emphasis on the utilization of market forces, and rapid growth in the PRC's economy. However, such growth has been uneven among various regions of the country and among various sectors of the economy. The central government has from time to time adopted various measures designed to stabilize the economy, regulate growth and contain inflation. All such economic events and measures could adversely affect the results of operations and expansion plans of the Group. (c) Legal environment The PRC legal system is based on written statutes under which prior court decisions may be cited as authority but do not have binding precedential effect. The PRC's legal system is relatively new, and the government is still in the process of developing a comprehensive system of laws, a process that has been ongoing since 1979. Considerable progress has been made in the promulgation of laws and regulations dealing with economic matters such as corporate organization and governance, foreign investment, commerce, taxation and trade. Such legislation has significantly enhanced the protection afforded to foreign investors. However, experience with respect to the implementation, interpretation and enforcement of such laws is limited. (d) Foreign currency exchange The books and records of the Group are maintained in RMB, their functional currency. RMB is not freely convertible into foreign currencies. All foreign exchange transactions involving RMB must take place through the banks and other institutions authorised by the People's Bank of China ("PBOC") to buy and sell foreign exchange. The applicable market exchange rates used for the transactions are administered by the PBOC. Enterprises can deal with an approved bank for foreign exchange on recurring items and approved capital items. A major portion of the Company's revenues is denominated in RMB. A portion of such revenues will need to be converted into other currencies to meet foreign currency obligations such as payment of any dividends declared. The existing foreign exchange limitations under PRC law could affect the Group's ability to obtain foreign exchange through debt financing, or to obtain foreign exchange for capital expenditures or for distribution of dividends on H shares and ADSs. F-9 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 1. ORGANISATION AND PRINCIPAL ACTIVITIES (CONT'D) (e) Government regulation of the railway system The PRC's national railway system is principally state-owned and operated as a single unified system, and is subject to operational and regulatory control by the MOR and, with respect to price setting for transport services, by the State Council of the PRC (the "State Council"). Prior to the Restructuring, the Company operated substantially within this system in which the MOR exercised overall authority over transportation operations, equipment and materials procurement, engineering and construction, revenue and expenditure controls, as well as other aspects of railroad operations. In connection with the Restructuring, the Company was granted special flexibility and autonomy in areas such as obtaining freight cars, scheduling services and determining the mix of passenger seat classes within its own line, routing trains through bottlenecks and dispatching empty freight cars to destinations beyond its rail line. In addition, in February 1996, the State Council granted the Company, with effect from April 1, 1996, increased flexibility and autonomy with respect to the setting of passenger fares and freight tariffs. This regulatory flexibility and autonomy allows the Company a greater degree of control over its operations and the ability to adjust its services to meet market demand. Further, in preparation for the offering in 1996, the Company received legal clarification and confirmation of its asset ownership, corporate powers and relationships with service providers and other entities in the national railway system. Although the operating flexibility and autonomy were granted to the Company without a fixed time limit, there can be no assurance that these will not be changed in the future or that other railway operators will not be granted similar treatment. Apart from the special dispensations granted in connection with the Restructuring, the Company, as a part of the national railway system, is generally subject to industry regulation by the MOR and must coordinate as required with other entities in the railway system. PRC government regulation has a significant impact on the Group' businesses. The price of railway transportation in particular is an important factor and has a substantial impact on the Group' business income. The regulatory framework with respect to the pricing of railway services may limit the Group's flexibility to respond to market conditions, competition or changes in the Group's cost structure. (f) Development and competition in the transportation industry As the industrial structure in the PRC is increasingly upgraded, advanced technological products, such as computer components, will gradually replace traditional industrial products as the principal goods in the Group's freight transportation business. These changes will affect the variety, volume and price of the Group's freight transportation and could have an adverse effect on the Group's results of operations. Intensifying competition from other forms of transportation may affect the Group's profitability and growth. With the gradual implementation of the PRC government's policies of supporting infrastructure industries, the railway transportation sector, particularly the passenger transportation business, is facing increasing competition from other means of surface, air and water transportation. The Group, in particular, face significant competition from bus services operating in the Pearl River Delta. F-10 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 1. ORGANISATION AND PRINCIPAL ACTIVITIES (CONT'D) (g) Insurance The Company does not currently maintain any insurance coverage with third party carriers against third party liabilities. Pursuant to applicable PRC regulations and the practice of national railway companies, the Company is liable for (i) personal injury to or death its passengers in the case of accidents for up to RMB20 per passenger and (ii) personal injury to or death of passengers for fault for up to RMB60 per passenger . With respect to loss of or damage to baggage, parcels and freight, the Company's customers may elect to purchase insurance administered by the MOR for up to their declared value. Passengers who do not elect to purchase insurance in respect of their baggage and/or parcels may nevertheless recover up to RMB0.03 for each 10-kilogram of damaged baggage and/or parcels. Similarly, freight transport customers who elect not to purchase insurance may recover up to RMB0.1 for each ton of damaged freight. Consistent with what it believes to be the customary practice among railway operators in the PRC, the Company does not maintain insurance coverage for its property and facilities (other than for its automobiles), for business interruption or for environmental damage arising from accidents on Company property or relating to Company operations. As a consequence, in the event of an accident or other event causing loss, destruction or damage to the Company's property or facilities, causing interruption to the Company's normal operations or causing liability for environmental damage or clean-up, the Company will be reliant on its own resources to cover losses and damages. With respect to its employees, the Company does not maintain medical insurance or disability insurance with any third party insurance carriers. The Company has adopted internal rules to provide for medical and disability benefits to its employees, consistent with MOR regulations and practices and relevant regulations of the Shenzhen municipality. The Company has entered into service agreements with the Parent Company and Guangzhou Railway (Group) Guangshen Railway Enterprise Development Company ("GEDC"), a wholly-owned subsidiary of the Parent Company, pursuant to which the health care facilities owned by these entities provide medical services to the Company's employees and their families. (h) Entry by the PRC with the WTO Entry by the PRC with the WTO, may increase competition for the Group's business. With the PRC's entry into the WTO, other Chinese coastal cities' significance in trading will be enhanced. Part of the freight currently transferred through ports in Hong Kong and Shenzhen will be shipped to other ports in the PRC, which will adversely affect the Group's railway freight business. In addition, as the PRC government lifts control over foreign investments, including allowing foreign participation in railway construction, the Company's railway monopoly position in its region may be challenged by foreign strategic investment, and potential competitors may arise in the Pearl River Delta. F-11 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 1. ORGANISATION AND PRINCIPAL ACTIVITIES (CONT'D) (i) Ability to obtain sufficient financing The Company may be unable to obtain sufficient financing to fund its substantial capital requirements, which could limit its growth potential. The Company estimates that it will require approximately RMB1,550,000 for capital expenditures in 2004, mainly including the construction of its fourth track between Guangzhou and Shenzhen, the construction of a technical support and maintenance depot in northern Shenzhen, the purchase of additional locomotives and trains. The Company's actual capital requirements may be greater. The Company may not be able to obtain sufficient funds on commercially acceptable terms. If adequate capital is not available, the Company's planned capital expenditure and business prospects could be adversely affected. 2. PRINCIPAL ACCOUNTING POLICIES The principal accounting policies adopted in preparing the financial statements of the Group are as follows: (a) Basis of presentation The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). This basis of accounting differs in certain material respects from that used in the preparation of the Group's statutory accounts in the PRC, which have been prepared in accordance with generally accepted principles and relevant financial regulations in the PRC ("PRC GAAP"). In preparing these financial statements, appropriate adjustments have been made to the Group's statutory accounts to conform with IFRS. Differences arising from the adjustments are not incorporated in the accounting records of the Group. The principal adjustments made to conform to IFRS include the following: - Additional depreciation charges on fixed assets; - Write-down of reclaimed rails to realisable value; - Difference in the recognition policy on housing benefits to the employees; - Recording of deferred tax impact according to IFRS; - Difference in depreciation charges on fixed assets resulting from reclassification; and - Recognition of government grants by deducting the carrying value of fixed assets. The financial statements have been prepared under the historical cost convention except that, as disclosed in the accounting policies below, certain fixed assets are stated at valuation less accumulated depreciation and impairment losses. The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of current event and actions, actual results ultimately may differ from those estimates. F-12 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (a) Basis of presentation (Cont'd) During the year, there was a change of accounting estimate in respect of the useful lives of certain fixed assets. Details of such change are set out in Note 2(g) and Note 13. The Consolidated Financial Statements reflect certain reclassification and additional disclosures to conform more closely to presentations customary in filings with the Securities and Exchange Commission of the United States of America. Differences between IFRS and generally accepted accounting principles in the United States of America ("US GAAP") are set forth in Note 30. Translation of amounts from RMB into US$ for the convenience of the reader has been made at the Noon Buying Rate on 31 December, 2003 of US$1.00=RMB8.3 as certified for customs purposes by the Federal Reserve Bank of New York. No representation is made that the RMB amounts could have been, or could be, converted into US$ at that rate on 31 December, 2003. (b) Group accounting The consolidated financial statements include those of the Company and its subsidiaries and also incorporate the Group's interest in associates on the basis as set out in Note 2(c) and 2(d) below. The equity and net income attributable to minority shareholders' interests are shown separately in the consolidated balance sheet and consolidated income statement, respectively. All significant intercompany balances and transactions, including intercompany profits and unrealised profits and losses are eliminated on consolidation; unrealised losses are also eliminated unless cost cannot be recovered. Consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. (c) Subsidiaries Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies are consolidated. In the Company's financial statements, the Company's share of the post-acquisition profits or losses of subsidiaries is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the cost of the investment. An assessment of interests in subsidiaries is performed when there is an indication that the asset has been impaired or the impairment losses recognised in prior years no longer exist. (d) Associates Associates are entities over which the Group generally has between 20% and 50% of the voting rights, or over which the Group has significant influence, but which it does not control. F-13 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (d) Associates (Cont'd) Investments in associates are accounted for by the equity method of accounting. Under this method the Company's share of the post-acquisition profits or losses of associates is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the cost of the investment. Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. When the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not to recognise further losses, unless the Group has incurred obligations or made payments on behalf of the associates. (e) Foreign currency transactions The Group maintains its books and records in RMB. Foreign currency transactions are translated into RMB using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement in the period in which they arise. Translation differences on monetary assets measured at fair value are recognised in foreign exchange gains and losses. The Group did not enter into any hedge contracts during any of the periods presented. No foreign currency exchange gains or losses were capitalised for any periods presented. (f) Financial instruments Financial assets and financial liabilities carried on the balance sheet include cash and cash equivalents, temporary cash investments, trade receivables and payables, other receivables and payables and available-for-sale investments. The accounting policies on recognition and measurement of these items are disclosed in the respective accounting policies. The Group had no derivative financial instruments in any of the years presented. (g) Fixed assets Fixed assets are initially recorded at cost less accumulated depreciation and impairment loss. Cost represents the purchase price of the asset and other costs incurred to bring the asset into existing use. Subsequent to the initial recognition, fixed assets are stated at cost or valuation less accumulated depreciation and impairment losses (see Note 13). Independent valuations, on a market value basis or depreciated replacement cost basis when there is no evidence of market value for such an item, are performed at least every five years or sooner if considered necessary by the directors. In the intervening years, the directors review the carrying values of the fixed assets and adjustment is made where there has been a material change. Increases in valuation are credited to the revaluation reserve. F-14 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (g) Fixed assets (Cont'd) Decreases in valuation of fixed assets are first offset against increases from earlier valuations in respect of the same asset and are thereafter charged to the income statement. Any subsequent increases are credited to the income statement up to the amount previously charged. Upon the disposal of the fixed assets, the relevant portion of the realised revaluation reserve of previous valuations is transferred from the revaluation reserve to retained earnings and is shown as a movement in reserves. Depreciation is calculated using the straight-line method to write off the cost or revalued amount, after taking into account the estimated residual value of 4% to 10% of cost, of each asset over its estimated useful life. Effective from 1 January, 2003, the Group changed the estimated useful lives of track, bridges and service roads from 44 years to a range from 55 years to 100 years and changed the useful lives of locomotives and rolling stock from 16 years to 20 years. Effect of such change of accounting estimates to the consolidated income statement for the year ended 31 December 2003 is set out in Note 13. The estimated useful lives are as follows: Buildings 25 to 40 years Leasehold improvements over the lease terms Track, bridges and service roads 55 to 100 years Locomotives and rolling stock 20 years Communications and signaling systems 8 to 20 years Other machinery and equipment 7 to 25 years Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in the income statement. When revalued assets are sold, the amounts included in fair value and other reserves are transferred to retained earnings. Repairs and maintenance are charged to the income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Group. Major renovations are depreciated over the remaining useful life of the related asset. (h) Construction-in-progress Construction-in-progress represents plant and facilities, including railroad stations and maintenance facilities under construction and machinery pending for installation. This includes the costs of construction and acquisition. No depreciation is provided on construction in progress until the asset is completed and put into use. F-15 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (i) Leasehold land payments All land in the PRC is state-owned and no individual land ownership right exists. The Group acquired the right to use certain land for its rail line, stations and other businesses. The premium paid for such leasehold land payments represents pre-paid lease payments, which are amortised over the lease terms of 36.5 to 50 years. (j) Impairment of long lived assets Fixed assets and other non-current assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows. (k) Available-for-sale investments Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for sale investments; these are included in non-current assets unless management has the express intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets. All purchases and sales of available-for-sale investments are recognised on the date that the transaction is effective. Cost of purchase includes transaction costs. Available-for-sale investments are not subsequently fair-valued because they do not have quoted market prices in active markets and whose fair values cannot be reliably measured. These investments are carried at cost, and are subject to review for impairments. (l) Deferred staff costs The Group have finalised a scheme for selling staff quarters to its staff in 2000. Under the scheme, the Group sold certain staff quarters to their employees at preferential prices as housing benefits to the employees. The total housing benefits, which represented the difference between the net book value of the staff quarters sold and the proceeds collected from the employees, are expected to benefit the Group over 15 years, which is the estimated remaining average service lives of the employees participating in the scheme. Upon the sales of staff quarters to the employees, the housing benefits incurred are recorded as deferred staff costs and amortised over the remaining average service lives of the employees participating in the scheme. (m) Operating leases Leases where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease. (n) Materials and supplies Materials and supplies consist mainly of items for repair and maintenance of track, and are stated at weighted average cost. Materials and supplies are expensed when used. F-16 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (o) Receivables Receivables are carried at original invoice amount less provision made for impairment of these receivables. A provision for impairment of receivables is established when there is an objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for similar borrowers. (p) Temporary cash investments Temporary cash investments represent short-term deposits with original maturities ranging from three months to one year, which are held for investment purpose and are stated at cost. (q) Cash and cash equivalents Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks and other financial institutions, other short-term highly liquid investments with original maturities of three months or less. (r) Income tax expense The Group provides for income tax expense on the basis of the results for the year as adjusted for items which are not assessable or deductible for income tax purposes. Taxation of the Group is determined in accordance with the relevant tax rules and regulations applicable to enterprises established/incorporated in the PRC. Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Currently enacted tax rates are used in the determination of deferred income tax. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future. (s) Employee benefits Pursuant to the PRC laws and regulations, contributions to the basic old age insurance for the Group's local staff are to be made monthly to a government agency based on 26% of the standard salary set by the provincial government, of which 18%

is borne by the Company or its subsidiaries and the remainder 8% is borne by the staff. The government agency is responsible for the pension liabilities relating to such staff on their retirement. The Group accounts for these contributions on an accrual basis and charges the related contributions to income in the year to which the contributions relate. F-17 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (t) Government grants Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions. Government grants relating to the purchase of fixed assets are deducted against the carrying value of the fixed assets and are credited to the income statement on a straight-line basis over the useful lives of the fixed assets. (u) Provisions Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. (v) Revenue recognition Provided it is probable that the economic benefits associated with a transaction will flow to the Group and the revenues and costs, if applicable, can be measured reliably, revenue is recognised on the following bases: (i) Rendering of services and sales of goods Railroad revenues are recognised when services are performed. Revenues from other businesses include sales aboard the trains and in the stations of food, beverages and other merchandise and revenues from operating restaurants in major stations. Revenues from operating restaurants are recognised when services are rendered. Sales aboard the trains and in the stations of food, beverages and merchandise are recognised upon delivery, when the significant risks and rewards of ownership of these goods have been transferred to the buyers. Revenues are net of turnover tax. (ii) Interest income Interest income from bank deposits is recognised on a time proportion basis, taking into account of the principal outstanding and the effective rate over the period to maturity, when it is determined that such income will accrue to the Group. (iii) Dividend income Dividend income is recognised when the right to receive payment is established. (w) Dividends Dividends are recorded in the Group's financial statements in the period in which they are approved by the Group's shareholders. F-18 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 2. PRINCIPAL ACCOUNTING POLICIES (CONT'D) (x) Segments Business segments: for management purposes the Group is organised into railroad transportation and other business operations. The divisions are the basis upon which the Group reports their primary segment information. Financial information on business segments is presented in Note 3. Intersegment transactions: segment revenues, segment expenses and segment performance include transfers between business segments. Those transfers are eliminated on consolidation. 3. SEGMENTAL INFORMATION (a) Business segments The Group conducts the majority of its business activities in railroad and other business operations (see Note 1). These segments are determined primarily because the senior management makes key operating decisions and assesses performance of the segments separately. The accounting policies of the Group's segments are the same as those described in the principal accounting policies in Note 2. The Group evaluates performance based on profit from operations. Segment assets consist primarily of fixed assets, materials and supplies, receivables and operating cash, and mainly exclude deferred tax assets and interests in associates. Segment liabilities comprise operating liabilities and exclude taxes payable. Capital expenditure comprises additions to fixed assets (see Note 13) and construction-in-progress (see Note 14). F-19 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands,except number of shares and ADSs,per share and per ADS data and unless otherwise stated) 3. SEGMENTAL INFORMATION (a) Business segments (Cont'd) An analysis by business segment is as follows: Railroad businesses Other businesses Unallocated --------------------- --------------- --------------- 2003 2002 2003 2002 2003 2002 ---------- ---------- ------- ------- ------- ------- RMB'000 RMB'000 RMB'000 RMB'000 RMB'000 RMB'000 Revenues - External 2,269,017 2,360,635 144,370 156,893 - - - Inter-segment - - 52,172 75,188 - - ---------- ---------- ------- ------- ------- ------- 2,269,017 2,360,635 196,542 232,081 - - ========== ========== ======= ======= ======= ======= Segment result 560,731 625,343 1,982 (2,846) - - Other income 16,809 1,411 777 5,164 - - Interest income 29,349 36,281 406 639 - - Finance costs - - - - (2,468) (4,208) Share of losses of associates (2,508) (323) - - - - Income tax expense Minority interests Profit attributable to shareholders Other information Segment assets 10,082,637 10,147,098 844,668 962,077 - - Deferred tax assets - - - - 6,154 7,577 Interests in associates 140,494 139,972 - 870 - - Total assets Segment liabilities 429,123 678,303 220,620 251,719 - - Taxes payable - - - - 49,494 71,844 Total liabilities Capital expenditure 298,890 526,700 7,103 8,330 - - Non-cash expenses - Depreciation 290,014 335,508 1,639 2,289 - - - Amortisation of leasehold land payments 15,602 15,131 - - - - - Provision for doubtful accounts 123 4,257 49 341 - - - Amortisation of deferred staff costs 15,092 15,092 - - - - Consolidation Total --------------- --------------------- 2003 2002 2003 2002 ------- ------- ---------- ---------- RMB'000 RMB'000 RMB'000 RMB'000 Revenues - External - - 2,413,387 2,517,528 - Inter-segment (52,172) (75,188) - - ------- ------- ---------- ---------- (52,172) (75,188) 2,413,387 2,517,528 ======= ======= ========== ========== Segment result - - 562,713 622,497 Other income - - 17,586 6,575 Interest income - - 29,755 36,920 Finance costs - - (2,468) (4,208) Share of losses of associates - - (2,508) (323) Income tax expense (93,348) (104,265) Minority interests 32 (113) ---------- ---------- Profit attributable to shareholders 511,762 557,083 ========== ========== Other information Segment assets - - 10,927,305 11,109,175 Deferred tax assets - - 6,154 7,577 Interests in associates - - 140,494 140,842 ---------- ---------- Total assets 11,073,953 11,257,594 ========== ========== Segment liabilities - - 649,743 930,022 Taxes payable - - 49,494 71,844 ---------- ---------- Total liabilities 699,237 1,001,866 ========== ========== Capital expenditure - - 305,993 535,030 ========== ========== Non-cash expenses - Depreciation - - 291,653 337,797 ========== ========== - Amortisation of leasehold land payments - - 15,602 15,131 ========== ========== - Provision for doubtful accounts - - 172 4,598 ========== ========== - Amortisation of deferred staff costs - - 15,092 15,092 ========== ========== For the years ended 31 December, 2001, 2002 and 2003, no revenues from a single customer counted for 10 percent or more of the Group's total revenues F-20 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands,except number of shares and ADSs,per share and per ADS data and unless otherwise stated) 3. SEGMENTAL INFORMATION (CONT'D) (b) Geographic segments For the year ended 31 December, 2003, all of the Group's business operations are conducted in the PRC. 4. GENERAL AND ADMINISTRATIVE EXPENSES Year ended 31 December, --------------------------- 2001 2002 2003 ------- ------- -------- RMB RMB RMB Wages and bonus 15,026 16,226 14,936 Retirement and employee benefits 50,553 49,722 58,778 Utility expenses 361 195 219 Selling expenses 5,397 - - Office expenses 14,394 15,538 15,414 Construction duty, land use fees and other duties 3,664 3,761 3,539 Depreciation 3,392 1,625 1,693 Amortisation of deferred staff costs 15,721 15,092 15,091 Provision for doubtful accounts 29,620 4,598 172 Others 41,956 52,180 54,557 ------- ------- ------- 180,084 158,937 164,399 ======= ======= ======= Attributable to: Railroad businesses 150,162 123,800 134,688 Other businesses 29,922 35,137 29,711 ------- ------- ------- 180,084 158,937 164,399 ======= ======= ======= 5. OTHER INCOME Year ended 31 December, --------------------------- 2001 2002 2003 ------- ------- -------- RMB RMB RMB Exchange (gain) / losses (1,069) 799 (1,356) Others 14,021 5,776 18,942 ------- ------- -------- 12,952 6,575 17,586 ======= ======= ======== F-21 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 6. INTEREST INCOME, NET Year ended 31 December, ----------------------------- 2001 2002 2003 ------ ------ ------ RMB RMB RMB Finance costs (2,087) (4,208) (2,468) Interest income 65,708 36,920 29,755 ------ ------ ------ 63,621 32,712 27,287 ====== ====== ====== 7. INCOME TAX EXPENSE Enterprises established in Shenzhen Special Economic Zone are subject to income tax at a reduced rate of 15% as compared with the standard rate for PRC companies of 33%. The Shenzhen Municipal Tax Bureau confirmed in 1996 that the Company is subject to a reduced income tax rate of 15% starting from the same year. The income tax rate of the Company for the year ended 31 December, 2003 is 15%. According to the relevant income tax laws, other businesses of the Group are subject to income tax rates of 15% or 33%, depending mainly on their places of incorporation/establishment. Furthermore, certain subsidiaries engaged in other businesses are Sino-foreign joint ventures which are entitled to full exemption from the PRC income tax for two years and a 50% reduction in the next three years starting from the first profit-making year, after offsetting available tax losses carried forward from prior years. Save as described above, the directors of the Company are not being informed of any change in the enterprise income tax treatment applicable to the Group. Details of taxation charged to the consolidated income statement during the year were as follows: Year ended 31 December, -------------------------------- 2001 2002 2003 ------- ------- ------ RMB RMB RMB Provision for PRC income tax 106,823 106,649 91,925 Deferred tax loss (income) resulting from provision for doubtful accounts (4,175) (1,173) 316 Deferred tax loss (income) resulting from loss on the disposals of fixed assets (3,351) (1,211) 1,107 ------- ------- ------ 99,297 104,265 93,348 ======= ======= ====== F-22 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED

FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 7. INCOME TAX EXPENSE (CONT'D) The tax on the Group's profit before tax differs from the theoretical amount that would arise using the applicable tax rate of the Company as follows: 2001 2002 2003 ---------- ---------- ---------- Percentage Percentage Percentage Weighted average statutory tax rate 15.0% 15.0% 15.0% Tax effect of expenses that are not deductible in determining taxable profit: - Amortisation of deferred staff costs 0.4% 0.3% 0.4% Effect of different tax rates for certain subsidiaries 0.4% 0.4% - ---- ---- ---- Effective income tax rate 15.8% 15.7% 15.4% ==== ==== ==== 8. EARNINGS PER SHARE AND PER EQUIVALENT ADS The calculation of basic earnings per share and per equivalent ADS were based on the profit attributable to shareholders for the year attributable to ordinary shareholders of RMB511,762 (2002: RMB557,083), divided by the weighted average number of ordinary shares and equivalent ADS outstanding during the year of 4,335,550,000 and 86,711,000 respectively (2002: 4,335,550,000 and 86,711,000 respectively). No diluted earnings per share and per equivalent ADS were presented as there were no dilutive potential ordinary shares as of year end. 9. DIVIDENDS In 2003, the directors have recommended and declared a final dividend of RMB0.10 (2002: RMB0.10) per share in respect of the financial year ended 31 December, 2002, totaling RMB433,555 (2002: RMB433,555). 10. TEMPORARY CASH INVESTMENTS 31 December, --------------------- Note 2002 2003 ---- ------- ------- RMB RMB Time deposits with maturities over three months in banks (a) 399,339 459,440 Time deposits with maturities over three months in the MOR's Railway Deposits-taking Center (b) 168,000 168,000 ------- ------- 567,339 627,440 ======= ======= F-23 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 10. TEMPORARY CASH INVESTMENTS (CONT'D) (a) Time deposits with maturities over three months in banks consist of short-term deposits denominated in RMB and US$ (2002: RMB, Hong Kong dollars "HK$", and US$) with original maturities ranging from six months to one year, placed with banks in the PRC. The annual interest rate of RMB deposits was 1.98% in 2003 (2002: 1.98%), the annual interest rate of HK$ deposit was 1.13% in 2002, and the annual interest rates of US$ deposits were LIBOR plus a floating rate ranged from -0.2% to 0% (2002: from -0.2% to 0.1%). Total interest earned from such deposits amounted to approximately RMB 11,868 for the year (2002: approximately RMB15,121). (b) Time deposits with maturities over three months in the MOR's Railroad Deposit-taking Center consist of short-term deposits denominated in RMB (in 2002 included both RMB and USD) with original maturities of one year (2002: ranging from six months to one year). The annual interest rate of RMB deposits was 1.98% in 2003 (2002: 1.98% ) and the annual interest rates of US$ deposits were LIBOR plus a floating rate ranged from -0.2% to 0.1% in 2002. Total interest earned from such deposits amounted to approximately RMB3,326 (2002: approximately RMB3,239) for the year (see Note 24). 11. TRADE RECEIVABLES, NET 31 December, ------------------------- 2002 2003 ------ ------ RMB RMB Trade receivables 67,416 96,037 Less: Provision for doubtful accounts (15,959) (15,423) ------ ------ 51,457 80,614 ====== ====== The credit terms of trade receivables are within one year. The aging analysis of trade receivables, net was as follows: 31 December, ------------------------- 2002 2003 ------ ------ RMB RMB Within 1 year 44,986 75,674 Over 1 year but within 2 years 3,490 4,719 Over 2 years but within 3 years 1,652 221 Over 3 years 1,329 - ------ ------ 51,457 80,614 ====== ====== Concentrations of credit risk with respect to trade receivables are limited due to the Group's large number of customers, who are widely dispersed. Due to this factor, management believes that no additional credit risk beyond amounts provided for collection losses is inherent in the Group's trade receivables. F-24 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 11. TRADE RECEIVABLES (CONT'D) Movements of provision for doubtful accounts: Year ended 31 December, ------------------------- 2002 2003 ------ ------ RMB RMB At beginning of year 24,040 15,959 Utilisation during the year (8,081) (536) ------ ------ At end of year 15,959 15,423 ====== ====== 12. PREPAYMENTS AND OTHER RECEIVABLES, NET 31 December, -------------------------- 2002 2003 ------- ------- RMB RMB Other receivables 149,385 157,690 Less: Provision for doubtful accounts (39,898) (38,288) ------- ------- Other receivables, net 109,487 119,402 Prepayments 131,737 104,061 ------- ------- 241,224 223,463 ======= ======= Movements of provision for doubtful accounts: Year ended 31 December, ------------------------- 2002 2003 ------ ------ RMB RMB At beginning of year 34,008 39,898 Addition of provision during the year 5,890 172 Utilisation during the year - (1,782) ------ ------ At end of year 39,898 38,288 ====== ====== As of 31 December, 2003, the Company had fixed deposit with the principal amount of approximately RMB31.365 million in Zeng Cheng City Li Cheng Credit

Cooperative ("Li Cheng"). The Company had not been able to recover the principal from Li Cheng upon the expiry of the fixed deposit term. In March 1999, the Company instituted legal proceedings against Li Cheng to recover the deposit and the related interest. According to the court verdict dated 12 October, 1999, Li Cheng was required to repay the deposit principal and the related interest to the Company. As Li Cheng failed to execute the court ruling, the Company further applied to the court for compulsory enforcement of the court order. In July 2000, Li Cheng filed a petition to the court for winding up. On 9 November, 2000, the court ordered the suspension of execution of the court ruling dated 12 October, 1999, while Li Cheng was undergoing a winding-up. On 23 November, 2000, the Company applied to the Guangdong Provincial Government for allocation of special funds by the government to Li Cheng for repayment of the Company's deposit principal. The provincial government accepted the petition and requested the municipal government to follow up on the case. As of the date of this report, the fixed deposit has not yet been collected. Accordingly, the Company reclassified such amount from temporary cash investments to other receivables and accounted for provision for doubtful accounts pursuant to management's estimates. F-25 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 13. FIXED ASSETS, NET Track, Locomotives Communications Other Lease hold bridges and and rolling and signaling machinery and Buildings improvement service roads stock systems equipment Total --------- ----------- ------------- ----------- -------------- ------------- --------- RMB RMB RMB RMB RMB RMB RMB Cost/valuation As of 1 January, 2002 2,066,545 38,500 4,070,016 1,004,211 490,724 1,522,774 9,192,770 Additions 25,985 - 22,871 23,620 1,475 78,161 152,112 Transfer from construction-in-progress 40,852 - 43,791 870 46,372 14,401 146,286 Reclassification (124,057) - 122,752 - (42,484) 43,789 - Disposals (68,169) - (13,884) (2,496) (198,981) (73,413) (356,943) --------- ------ --------- --------- ------- --------- --------- As of 31 December, 2002 1,941,156 38,500 4,245,546 1,026,205 297,106 1,585,712 9,134,225 Additions 260 - - 21,679 916 32,823 55,678 Transfer from construction-in-progress 209,479 - 123,832 - 720 198,718 532,749 Government grants (17,000) - - - - - (17,000) Reclassification (154,024) - (37,113) - 5,936 185,201 - Disposals (92,503) - (16,560) (4,992) (4,600) (33,116) (151,771) --------- ------ --------- --------- ------- --------- --------- As of 31 December, 2003 1,887,368 38,500 4,315,705 1,042,892 300,078 1,969,338 9,553,881 --------- ------ --------- --------- ------- --------- --------- Representing: At cost 220,433 38,500 164,088 22,549 48,092 287,127 780,789 At 2003 professional valuation 1,666,935 - 4,151,617 1,020,343 251,986 1,682,211 8,773,092 --------- ------ --------- --------- ------- --------- --------- 1,887,368 38,500 4,315,705 1,042,892 300,078 1,969,338 9,553,881 --------- ------ --------- --------- ------- --------- --------- Accumulated depreciation As of 1 January, 2002 345,429 5,775 932,060 212,925 266,582 398,959 2,161,730 Charges for the year 58,739 7,700 92,400 60,723 23,962 94,273 337,797 Reclassification (22,652) - 18,404 - (4,256) 8,504 - Disposals (5,324) - (5,311) (2,496) (107,891) (42,560) (163,582) --------- ------ --------- --------- ------- --------- --------- As of 31 December, 2002 376,192 13,475 1,037,553 271,152 178,397 459,176 2,335,945 Charges for the year 54,399 7,700 46,476 47,648 34,144 101,286 291,653 Reclassification - - (16,682) - 563 16,119 - Disposals (921) - (2,550) (4,992) (4,417) (13,715) (26,595) --------- ------ --------- --------- ------- --------- --------- As of 31 December, 2003 429,670 21,175 1,064,797 313,808 208,687 562,866 2,601,003 --------- ------ --------- --------- ------- --------- --------- Net book value At end of year 1,457,698 17,325 3,250,908 729,084 91,391 1,406,472 6,952,878 ========= ====== ========= ========= ======= ========= ========= At beginning of year 1,564,964 25,025 3,207,993 755,053 118,709 1,126,536 6,798,280 ========= ====== ========= ========= ======= ========= ========= Had the fixed assets been carried at cost less accumulated depreciation, the carrying amounts at year end would have been: Cost 1,048,829 38,500 3,537,104 1,019,170 269,152 1,853,887 7,766,642 Accumulated depreciation 214,612 21,175 696,853 256,906 189,263 513,581 1,892,390 --------- ------ --------- --------- ------- --------- --------- 834,217 17,325 2,840,251 762,264 79,889 1,340,306 5,874,252 ========= ====== ========= ========= ======= ========= ========= * During the year ended 31 December, 2003, based on the construction completion reports, the directors reclassified certain fixed assets to appropriate categories. Accordingly, the carrying amounts of the aforesaid fixed assets are depreciated over their remaining useful lives under the respective categories. On 6 March, 1996, the fixed assets of the Group were revalued by Vigers Hong Kong Limited (the "Valuer"), a qualified independent valuer in Hong Kong, using a replacement cost approach and open market value approach. The replacement cost approach considers the cost to replace in new condition the assets appraised for similar assets, and includes purchase price, delivery charge and installation cost. The purchase price is based on the open market value. The Valuer assumed that the assets will be used for the purposes for which they are presently used and did not consider alternative uses. The total revalued amount based on the aforesaid 1996 revaluation was RMB 5,318,202. The revaluation surplus of fixed assets amounting to approximately RMB1,492,185 was recorded by the Group as of 6 March, 1996, and depreciation on the increment to fixed assets commenced on that date. Upon the Restructuring, the revaluation surplus was converted to shares allotted to the Parent Company. F-26 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 13. FIXED ASSETS, NET (CONT'D) On 30 September, 2002, the fixed assets were revalued by Pan-China (Schinda) Certified Public Accountants, a qualified independent valuer registered in the PRC, on a replacement cost approach and open market value approach, where applicable. These fixed assets were stated at their revalued amounts in the financial statements as of 30 September, 2002. The directors of the Company are of the opinion that the carrying values of fixed assets as of 31 December, 2003 approximated to their fair values. With reference to "Cai Jian Han (2002) No. 42" and "Cai Jian Han (2002) No. 349" issued by Ministry of Finance ("MOF") and "Ban Cai Fa (2003) No. 10" issued by MOR and to further comply with international practice in railway industry, the management reassessed the estimated useful lives and depreciation rates of fixed assets as of 1 January 2003. The assessment is based on the experience and maintenance program established by the management and the engineering personnel. Effective from 1 January, 2003, the Group changed the estimated useful lives of track, bridges and service roads from 44 years to a range from 55 years to 100 years and changed the useful lives of locomotives and rolling stock from 16 years to 20 years. This change in accounting estimates resulted in a decrease in depreciation expenses and an increase in profit attributable to shareholders for the year ended 31 December, 2003 by approximately RMB 63,610. 14. CONSTRUCTION-IN-PROGRESS 31 December, ------------------------------ 2002 2003 ------- ------- RMB RMB At beginning of year 446,399 672,827 Additions 382,918 250,315 Disposals (10,204) - Transfer to fixed assets (146,286) (532,749) ------- ------- At end of year 672,827 390,393 ======= ======= As of 31 December, 2003, there was no interest capitalised in the construction-in-progress as the Group had no borrowings. Disposals in 2002 mainly represented injection in available-for-sale investments (see Note 17). F-27 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 15. LEASEHOLD LAND PAYMENTS Year ended 31 December, ----------------------- 2002 2003 ------- ------- RMB RMB Cost At beginning of year 762,087 760,087 Additions - 10,687 Disposals (2,000) - ------- ------- At end of year 760,087 770,774 ------- ------- Accumulated amortisation At beginning of year 88,341 103,089 Charges for the year 15,131 15,602 Disposals (383) - ------- ------- At end of year 103,089 118,691 ------- ------- Net book value At end of year 656,998 652,083 ======= ======= At beginning of year 673,746 656,998 ======= ======= 16. INTERESTS IN ASSOCIATES 31 December, ------------------- 2002 2003 -------- -------- RMB'000 RMB'000 Share of net assets, beginning of year 117,477 136,574 Addition 19,420 - Share of losses (323) (2,508) -------- -------- Share of net assets, end of year 136,574 134,066 Due from associates 48,095 48,437 Due to associates (40) (8) -------- -------- 184,629 182,495 Less: Provision for impairment in value (29,689) (29,689) Provision for doubtful accounts (14,098) (12,312) -------- -------- 140,842 140,494 ======== ======== The amounts due from/to associates are unsecured, interest free and had no fixed repayment terms. The provision for impairment in value and provision for doubtful accounts were provided for Zengcheng Lihua Stock Company Limited ("Zengcheng Lihua") as Zengcheng Lihua is in financial difficulty. F-28 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 16. INTERESTS IN ASSOCIATES (CONT'D) Movements of provision for impairment in value and for doubtful accounts are as follows: Year ended 31 December, ----------------------- 2002 2003 ------- ------- RMB RMB Beginning of year 62,400 43,787 Utilisation during the year (18,613) (1,786) ------- ------- End of year 43,787 42,001 ======= ======= As of 31 December, 2002, the Company had direct or indirect interests in the following companies which were incorporated/established and are operating in the PRC: Percentage of Date of equity interest incorporation / attributable to Name of the entity establishment the Company Paid-up capital Principal activities ----------------- -------------- -------------- -------------- ------------------- Directly held by the Company Guangzhou Tiecheng Enterprise 2 May, 1995 49% RMB245,000,000 Properties management Company Limited and trading of merchandise Zengcheng Lihua Stock Company 30 July, 1992 27% RMB100,000,000 Real estate, warehousing, Limited cargo loading and unloading Indirectly held by the Company Guangzhou Tielian Economy 27 December, 1994 34% RMB 1,000,000 Warehousing and freight Development

Company Limited transport agency Guangzhou Huangpu Yuehua Freight 20 July, 1990 33.3% RMB 6,610,000 Cargo loading and unloading, Transportation Joint Venture warehousing, freight Company Limited transport agency 17. AVAILABLE-FOR-SALE INVESTMENTS 31 December, ----------------- Name of the investee company 2002 2003 --------------------------- ------- ------- RMB'000 RMB'000 China Railway Communication Company Limited ("China Railcom")* 120,587 121,854 Shenzhen Innovation Technology Investment Company Limited 30,000 30,000 China Railway Express Company Limited 13,608 13,608 Shenzhen Huatie Enterprise Company Limited 2,000 2,000 Zhongtie Information Company Limited 500 500 ------- ------- 166,695 167,962 ======= ======= F-29 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 17. AVAILABLE-FOR-SALE INVESTMENTS (CONT'D) The Company's share of equity interests in each of the respective companies is not more than 10%. No quoted market prices are available for the above unlisted companies as of year end. * In 2003, the Company invested in China Railcom by injecting certain communication and signalling systems with their respective carrying value of approximately RMB1,267 (in 2002 the Company invested in China Railcom by injecting certain communication and signalling systems and construction-in progress with carrying value of approximately RMB120,587). China Railcom has confirmed in writing that the Group is entitled to the 0.69% equity interest in China Railcom as of 31 December, 2003 (2002: 0.85%). The relevant legal registration procedures are still in progress. 18. DEFERRED TAX ASSETS 31 December, -------------- 2002 2003 ----- ------ RMB RMB Deferred tax assets: - Provision for doubtful accounts 3,015 2,699 - Losses on disposals of fixed assets 4,562 3,455 ----- ------ 7,577 6,154 ===== ====== The movements of deferred taxation during the years are as follows: Year ended 31 December, ---------------------- 2002 2003 ------ ------ RMB RMB At beginning of year 5,193 7,577 Credit (debit) to consolidated profit during the years 2,384 (1,423) ------ ------ At end of year 7,577 6,154 ====== ====== 19. DEFERRED STAFF COSTS 31 December, ------------------- 2002 2003 -------- -------- RMB'000 RMB'000 Cost, at beginning and end of year 226,369 226,369 -------- -------- Accumulated amortisation At beginning of year (30,182) (45,274) Charges for the year (15,092) (15,092) -------- -------- At end of year (45,274) (60,366) -------- -------- Net book amount At end of year 181,095 166,003 ======== ======== At beginning of year 196,187 181,095 ======== ======== F-30 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 20. ACCRUED EXPENSES AND OTHER PAYABLES 31 December, ---------------- 2002 2003 ------- ------- RMB RMB Advances from customers 143,388 89,840 Accrued expenses 79,790 24,000 Salary and welfare payables 21,260 15,138 Taxes payables 71,844 49,494 Other payables 213,515 179,815 ------- ------- 529,797 358,287 ======= ======= Other payables mainly represented various payables and deposits for daily operation of business. Pursuant to Caishui [2004] No.36 and Caishui [2003] No.149 issued by MOF and State Administration of Taxation, the Group exempt from certain real estate taxes amounting to approximately RMB12,000 during the year ended 31 December, 2003. The grant of such exemption is subject to the acknowledgement of relevant authorities that the Company is a transportation company under the MOR. The directors believe that the Group is qualified for such exemption and is in the process of seeking the acknowledgement from the relevant authorities. Accordingly, such real estate taxes have not been accrued for in the accompanying financial statements. 21. SHARE CAPITAL As of 31 December, 2003, the authorised capital of the Company consisted of ordinary shares of par value RMB1.00 per share: Percentage Number Nominal of capital of shares value stock --------- ------- ---------- '000 RMB Authorised, issued and fully paid: State-owned Domestic Shares 2,904,250 2,904,250 67% H Shares 1,431,300 1,431,300 33% --------- --------- --- 4,335,550 4,335,550 100% ========= ========= === 22. DISTRIBUTION OF INCOME According to the articles of association of the Company, when distributing Profit attributable to shareholders of each year, the Company shall set aside 10% of its Profit attributable to shareholders after tax based on the Company's local statutory accounts for the statutory surplus reserve (except where the reserve has reached 50% of the Company's registered share capital) and 5% to 10% for the statutory public welfare fund at a percentage determined by the directors. The Company may make appropriation from its Profit attributable to shareholders to the discretionary surplus reserve provided it is approved by a resolution of a shareholders' general meeting. These reserves cannot be used for purposes other than those for which they are created and are not distributable as cash dividends without prior approval from a shareholders' general meeting under certain conditions. When the statutory surplus reserve is not sufficient to make good for any losses of the Company from previous years, current year Profit attributable to shareholders shall be used to make good the losses before allocations are set aside for the statutory surplus reserve or the statutory public welfare fund. F-31 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 22. DISTRIBUTION OF INCOME (CONT'D) The statutory public welfare fund is used to build or acquire capital items, such as dormitories and other facilities for the Company's employees and cannot be used to pay for welfare expenses. Title of these capital items will remain with the Company. The statutory surplus reserve, the discretionary surplus reserve and the share premium may be converted into capital stock provided it is approved by a resolution at a shareholders' general meeting and the balance of the statutory surplus reserve does not fall below 25% of the registered capital stock. The Company may either distribute new shares in proportion to the number of shares held by shareholders, or increase the par value of each share. In accordance with the articles of association of the Company, dividends are determined based on the least of retained earnings determined in accordance with (a) PRC GAAP, (b) IFRS and (c) the accounting standards of the countries in which its shares are listed. As the statutory accounts have been prepared in accordance with PRC GAAP, the retained earnings as reported in the statutory accounts may be different from the amount reported in the accompanying statement of changes in shareholders equity. As of 31 December, 2003, the reserve of the Company available for distribution was approximately RMB656,893 (2002: approximately RMB667,416). 23. RETIREMENT BENEFITS All the full-time staff of the Group are covered by a defined-contribution pension scheme. Pursuant to a circular dated 24 October, 1995 issued by the Parent Company, the Company is required to pay to the Parent Company an amount equivalent to 19% of the salary and certain amount of bonus of the staff for pension benefits, and the Parent Company is responsible for the ultimate pension liability to the staff. Starting from December 2000, the percentage borne by the Company changed to 18% pursuant to another circular dated 21 December, 2000 issued by the Parent Company. As of 31 December, 2003, payable for pension obligations was nil (2002: nil). 24. RELATED PARTY TRANSACTIONS Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. (a) During the year, the Group had the following material transactions with related parties: Recurring transactions A significant portion of transactions undertaken by the Group during the year was with related PRC state-owned enterprises and on such terms as determined by the relevant PRC authorities and stipulated in the related agreements entered into with these parties. The following is a summary of significant recurring transactions carried out in the ordinary course of business by the Group with its related parties during the year: F-32 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 24. RELATED PARTY TRANSACTIONS (CONT'D) Recurring transactions (Cont'd) Year ended 31 December, -------------------------- 2001 2002 2003 ------- ------- ------- RMB RMB RMB Lease of locomotives and related services from Yang Cheng Railway Company, a subsidiary of the Parent Company(i) 70,345 42,047 40,882 Provision of trains and related services from Guangmeishan Railway Company Limited, a subsidiary of the Parent Company 5,205 4,864 5,305 Purchases of materials and supplies from Guangzhou Railway Material Supply Company, a subsidiary of the Parent Company 36,544 33,074 50,687 Social services (employee housing, health care, educational and public security services and other ancillary services) provided by the Parent Company and related parties (including Guangzhou Railway (Group) Guangshen Railway Enterprise Development Company) 56,800 66,744 68,079 Operating lease rentals paid to the MOR(i) 52,296 57,298 58,904 Provision of trains and related service through MOR 66,475 211,667 201,870 Provision of trains usage and related services from Guangzhou Railway (Group) Passenger Transportation Company, a subsidiary of the Parent Company 7,844 6,681 2,207 Interest expenses paid to the Parent Company (ii) 1,178 2,443 2,037 Interest received from the MOR's Railroad Deposit-taking Centre (see Note 10(b) and 24(b)) 11,887 3,239 3,516 Interest received from Pingnan Railway Company Limited, an associate of the Parent Company (ii) 1,866 806 827 Interest received from Guangmeishan Railway Company Limited (ii) 1,291 1,884 901 (i) The lease agreement with Yang Cheng Railway Company was revised on March 6, 1996 and provides for a 10-year lease period starting from 1996. The lease with MOR is based on the uniform rate set by MOR and is renewable annually. F-33 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 24. RELATED PARTY TRANSACTIONS (CONT'D) Recurring transactions (Cont'd) (ii) The interest was resulted from the long-distance transportation services, which was calculated based on the average balances due from/to related parties on a quarterly basis, at the prevailing interest rates of six-month bank loans. (b) As of 31 December, 2002, the Group had the following material balances with related parties: 31 December, ------------------- 2002 2003 -------- -------- RMB RMB Temporary cash investments in the MOR's Railroad Deposit-taking Center (see Note 10(b)) 168,000 168,000 Bank deposits in the MOR's railroad Deposit-taking Center 206,452 321,985 Due from Parent Company 39,374 - Due to Parent Company - (37,230) Due from related parties 267,885 199,921 -------- -------- - Trading balance 54,425 10,608 - Non-trading balance 213,460 189,313 -------- -------- Due to related parties (158,199) (120,605) -------- -------- - Trading balance (125,847) (60,128) - Non-trading balance (32,352) (60,477) -------- -------- As of 31 December, 2003, the balances with the MOR, the Parent Company and related parties are unsecured, non-interest bearing and repayable on demand, except for those disclosed in Notes 10(b), 24(a) and bank deposits in MOR's railroad Deposit-taking centre. These balances resulted from transactions carried out by the Group with related parties in the ordinary course of business. The balances with the Parent Company are all non-trading in nature. The balances with related parties, which are of trading in nature, all aged within one year. 25. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT Non-cash transactions (i) During the year ended 31 December, 2003, the Group disposed certain staff quarters of approximately RMB92 million (2002: approximately RMB63 million) to their employees pursuant to its housing benefit scheme. (ii) During the year ended 31 December, 2003, the Company and the minority shareholder increased their investments in a subsidiary by capitalising approximately RMB42 million and RMB41 million due from that subsidiary respectively. F-34 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 25. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONT'D) Non-cash transactions (Cont'd) (iii) During the year ended 31 December, 2003, the Company invested of approximately RMB1,267 (2002: approximately RMB120,587) in China Railcom by injecting certain communication and signalling systems (see note 17). 26. FINANCIAL INSTRUMENTS The carrying amounts of the cash and cash equivalents, temporary cash investments and accounts receivable and payables of the Group approximate their fair values because of the short maturity of those instruments. Cash and cash equivalents and temporary cash investments denominated in foreign currencies have been translated at the applicable market exchange rates prevailing at the balance sheet date. The Company has not had and does not believe it will have any difficulty in exchanging its foreign currency cash and cash equivalents for RMB. As of 31 December, 2003, cash and cash equivalents and temporary cash investments were mainly maintained with commercial banks in the PRC and the MOR's Railroad Deposit-taking Centre. As of 31 December, 2003, balances denominated in US$ and HK$ have been translated into RMB at the applicable market exchange rates as of that date. 27. CONCENTRATION OF RISKS (a) Credit risk The carrying amount of cash and cash equivalents, accounts receivable and other receivables, and due from related parties and other current assets except for prepayments and deferred tax assets, represent the Group' maximum exposure to credit risk in relation to financial assets. The majority of the Group's accounts receivable relate to the rendering of services or sales of products to third party customers. The Group perform ongoing credit evaluations of their customers' financial condition and generally do not require collateral on accounts receivable. The Group maintain a provision for doubtful accounts and actual losses have been within management's expectation. No other financial assets carry a significant exposure to credit risk. (b) Interest rate risk The directors of the Group believe that the exposure to interest rate risk of financial assets and liabilities as of 31 December, 2003 was minimum since their deviation from their respective fair values was not significant. F-35 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 27. CONCENTRATION OF RISKS (CONT'D) (c) Currency risk Substantially all of the revenue-generating operations of the Group are transacted in Renminbi, which is not freely convertible into foreign currencies. On 1 January, 1994, the Mainland China government abolished the dual rate system and introduced single rate of exchange as quoted by the People's Bank of China. However, the unification of the exchange rate does not imply free convertibility of Renminbi into foreign currencies. All foreign exchange transactions continue to take place either through the People's Bank of China or other banks authorised to buy and sell foreign currencies at the exchange rates quoted by the People's Bank of China. Approval of foreign currency payments by the People's Bank of China or other institution requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts. 28. COMMITMENTS (a) Capital commitments As of

31 December, 2003, the Group had the following capital commitments: 31 December, -------------------- 2002 2003 -------- -------- RMB RMB Authorised and contracted for 10,158 - ======== ======== (b) Operating lease commitments Total future minimum lease payments under non-cancelable operating leases were as follows: 31 December, ------------------------------- 2002 2003 ------- -------- RMB RMB Machinery and equipment - not more than one year 108,000 108,000 - more than one year but not more than two years 108,000 108,000 - more than two years but not more than three years 108,000 75,375 - more than three years but not more than four years 75,375 - - more than four years but not more than five years - - ------- ------- 399,375 291,375 ======= ======= F-36 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 29. CONTINGENCY As of 31 December, 2003, the Company's interest in an associated company, Guangzhou Tiecheng Enterprise Company Limited ("Tiecheng"), amounted to approximately RMB140,000,000. In 1996, Tiecheng entered into an agreement with a Hong Kong incorporated company to establish Guangzhou Guantian Real Estate Company ("Guangzhou Guantian"), a sino-foreign contractual joint venture to develop certain properties near a railway station operated by the Group. On 27 October, 2000, Guangzhou Guantian together with Guangzhou Guanhua Real Estate Company Limited ("Guangzhou Guanhua" ) and Guangzhou Guanyi Real Estate Company Limited ("Guangzhou Guanyi") agreed to act as joint guarantors (the "Guarantors") of certain payables of Guangdong Guancheng Real Estate Company Limited ("Guangdong Guancheng") to an independent third party. Guangzhou Guantian, Guangzhou Guanhua, Guangzhou Guanyi and Guangdong Guancheng were related companies with a common chairman. As Guangdong Guancheng failed to repay the payables, according to a court verdict on 4 November, 2001, Guangzhou Guantian, Guangzhou Guanhua and Guangzhou Guanyi were liable to the independent third party to recover an amount of approximately RMB257,000 plus interest from Guangdong Guancheng. As such, if Guangzhou Guantian were held responsible for the guarantee, the Company may need to provide for impairment on its interests in Tiecheng. On 15 December, 2003, the High People's Court of Guangdong Province (the "Court") received the Guangzhou Guantian's application for discharging the aforesaid guarantee. As a necessary procedure for the Court to decide to reassess the previous court verdict, a hearing was held on 18 March, 2004. In this respect, Guangzhou Guantian appointed an independent lawyer to represent on its behalf to attend the hearing. Up to the date of this report, the Court is yet to finish the necessary procedures before making decision to reassess the previous court verdict. However, having consulted that independent lawyer, the directors are of the opinion that the guarantee arrangement should be invalid according to the relevant PRC rules and regulations. Accordingly, the directors consider that as of the date of this report, the chance of Guangzhou Guantian to settle the above claim is remote and no provision for impairment on the interests in Tiecheng was made in the accounts. 30. DIFFERENCE BETWEEN IFRS AND US GAAP The accompanying financial statements conform to IFRS which differ in certain respects from those prepared under Generally Accepted Accounting Principles in the United States of America ("US GAAP"). A major difference between IFRS and US GAAP, which has a significant effect on consolidated profit attributable to shareholders and consolidated net assets is set out below: Revaluation of fixed assets As stated in Note 13, the Group revalued their fixed assets on March 6, 1996. The revaluation surplus of fixed assets amounting to approximately RMB1,492,185 was recorded by the Group on that date. The revaluation as of September 30, 2002 did not result in a material difference from the carrying amounts and no revaluation surplus or deficit was recorded. Under IFRS, revaluation of fixed assets is permitted and depreciation is based on the revalued amount. Additional depreciation arising from the revaluation surplus was approximately RMB38,548 for the year ended 31 December, 2003 (2002: approximately RMB48,422). F-37 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 30. DIFFERENCE BETWEEN IFRS AND US GAAP (CONT'D) Revaluation of fixed assets (Cont'd) Under US GAAP, fixed assets are required to be stated at original cost. Hence, no additional depreciation from revaluation will be recognised under US GAAP. However, a deferred tax asset related to the revaluation surplus amounting to approximately RMB223,828 was created under US GAAP with a corresponding increase in equity since the revaluation resulted in a higher tax base which will be realised through additional depreciation for PRC tax purposes. Effects on the consolidated profit attributable to shareholders of significant differences between IFRS and US GAAP are summarised below: Year ended 31 December, ------------------------------------------ 2001 2002 2003 2003 -------- -------- -------- -------- RMB RMB RMB US$ Consolidated profit attributable to shareholders under IFRS 533,495

557,083 511,762 61,658 US GAAP adjustments: Reversal of additional depreciation charges arising from the revaluation surplus on fixed assets 48,422 48,422 38,548 4,644 Effect of US GAAP adjustment on deferred tax provision (7,263) (7,263) (5,782) (697) -------- -------- -------- -------- Consolidated profit attributable to shareholders under US GAAP 574,654 598,242 544,528 65,605 ======== ======== ======== ======== Earnings per share under US GAAP RMB0.13 RMB0.14 RMB0.13 USD0.02 ======== ======== ======== ======== Earnings per equivalent ADS under US GAAP RMB6.63 RMB6.90 RMB6.28 USD0.76 ======== ======== ======== ======== F-38 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 30. DIFFERENCE BETWEEN IFRS AND US GAAP (CONT'D) Effects on consolidated net assets of significant differences between IFRS and US GAAP are summarised below: Year ended 31 December, ------------------------------------------- 2002 2003 2003 ---------- ---------- --------- RMB RMB US$ Consolidated net assets under IFRS 10,244,151 10,322,358 1,243,656 US GAAP adjustments: Reversal of the gross revaluation surplus on fixed assets (1,492,185) (1,492,185) (179,781) Reversal of accumulated depreciation on the revaluation surplus on fixed assets 330,884 369,432 44,510 Deferred tax assets related to net revaluation surplus 174,195 168,413 20,291 --------- --------- --------- Consolidated net assets under US GAAP 9,257,045 9,368,018 1,128,676 ========= ========= ========= There are no significant differences between IFRS and US GAAP which affect classification in the balance sheet and the income statement but do not affect net income or shareholders' equity. In 2003, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No.150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity ("SFAS 150") and FASB Interpretation No.46, Consolidation of Variable Interest Entities ("FIN 46"). SFAS 150 established standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that and issuer classify a financial instrument that is within its scope as liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. Some of the provisions of this Statement are consistent with the current definition of liabilities in FASB Concepts Statement No.6, Elements of Financial Statements. The remaining provisions of this Statement are consistent with the Board's proposal to revise that definition to encompass certain obligations that a reporting entity can or must settle by issuing its own equity shares, depending on the nature of the relationship established between the holder and the issuer. SFAS 150 is effective for financial instruments entered into or modified after 31 May, 2003, and otherwise is effective at the beginning of the first period beginning after 15 June, 2003. F-39 GUANGSHEN RAILWAY COMPANY LIMITED AND SUBSIDIARIES NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Amounts in thousands, except number of shares and ADSs, per share and per ADS data and unless otherwise stated) 30. DIFFERENCE BETWEEN IFRS AND US GAAP (CONT'D) The Company considered the effect of adoption SFAS 150 and do not expect any material impact on the financial statements. FIN 46 provides guidance on the identification of and financial reporting for entities over which controls is achieved through means other than voting rights. This interpretation requires existing unconsolidated variable interest entities to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. FIN 46 applies immediately to variable interest entities created after 31 January, 2003, and to variable interest entities in which an enterprise obtains an interest after the date. It applies in the first fiscal year or interim period beginning after 15 June, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before 1 February, 2003. The Company considered the effects of adoption FIN 46 and do not expect any material impact on the financial statements. 31. POST BALANCE SHEET EVENTS Pursuant to a board resolution dated 20 April, 2004, the directors recommended the payment of a final dividend of RMB0.105 per share, totaling RMB455,233. 32. FOREIGN CURRENCY EXCHANGE The books and records of the Group are maintained in RMB, their functional currency. RMB is not freely convertible into foreign currencies. All foreign exchange transactions involving RMB must take place through the banks and other institutions authorised by the People's Bank of China ("PBOC") to buy and sell foreign exchange. The applicable market exchange rates used for the transactions are administered by the PBOC. Enterprises can deal with an approved bank for foreign exchange on recurring items and approved capital items. 33. APPROVAL OF ACCOUNTS The financial statements were approved by the Board of Directors on 20 April, 2004. F-40 SIGNATURE The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf. GUANGSHEN RAILWAY COMPANY LIMITED Date: June 29, 2004 By: /s/ Wu Junguang ----------------------------------- Wu Junguang

Chairman of the Board of Directors