



中裕燃氣控股有限公司

ZHONGYU GAS HOLDINGS LIMITED

(incorporated in the Cayman Islands with limited liability)

(Stock Code : 8070)

**THIRD QUARTERLY REPORT
FOR THE NINE MONTHS ENDED
30TH SEPTEMBER, 2009**

CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (“GEM”) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE “STOCK EXCHANGE”)

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This report, for which the directors of Zhongyu Gas Holdings Limited (the “Company”) collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company and its subsidiaries (collectively the “Group”). The directors of the Company (the “Directors”), having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

FINANCIAL HIGHLIGHTS

	For the nine months ended 30th September,		
	2009 <i>HK\$'000</i>	2008 <i>HK\$'000</i>	% of changes
Turnover	543,787	436,913	24.5%
Sales of piped gas	338,705	275,613	22.9%
Connection revenue from gas pipeline construction	132,371	125,650	5.3%
Operation of CNG filling stations	41,126	5,943	592.0%
Gross profit	165,548	122,991	34.6%
Gross margin	30.4%	28.1%	2.3%
Profit attributable to equity holders of the Company	40,123	744	5,392.9%
EBITDA	95,368	61,247	55.7%

The board of Directors (the “Board”) is pleased to announce the unaudited condensed consolidated results of the Group for the nine months ended 30th September, 2009, together with the comparative figures for the corresponding period in 2008, which are set out as follows:

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE NINE MONTHS ENDED 30TH SEPTEMBER, 2009 (UNAUDITED)

	Notes	Three months ended 30th September,		Nine months ended 30th September,	
		2009 HK\$'000	2008 HK\$'000 (re-presented)	2009 HK\$'000	2008 HK\$'000 (re-presented)
Turnover	3	195,874	167,575	543,787	436,913
Cost of sales		(128,957)	(113,087)	(378,239)	(313,922)
Gross profit		66,917	54,488	165,548	122,991
Other income		5,706	3,007	9,403	10,565
Other gains and losses	5	(2,679)	14,224	41,099	(4,989)
Selling and distribution costs		(5,401)	(4,505)	(15,733)	(13,056)
Administrative expenses		(30,689)	(22,601)	(79,414)	(67,450)
Share-based payment		(1,892)	(1,347)	(5,674)	(5,917)
Finance costs	6	(12,524)	(6,719)	(36,671)	(32,584)
Profit before tax		19,438	36,547	78,558	9,560
Income tax charge	7	(5,735)	(1,970)	(20,047)	(4,318)
Profit for the period	8	13,703	34,577	58,511	5,242
Other comprehensive income					
Exchange differences arising on translation of foreign operations		-	-	63	58,060
Total comprehensive income for the period		13,703	34,577	58,574	63,302
Profit for the period attributable to:					
Equity holders of the Company		5,036	32,482	40,123	744
Minority interests		8,667	2,095	18,388	4,498
		13,703	34,577	58,511	5,242
Total comprehensive income attributable to:					
Equity holders of the Company		5,036	32,482	40,186	63,302
Minority interests		8,667	2,095	18,388	4,498
		13,703	34,577	58,574	67,800
Earnings per share	9				
Basic (HK cent per share)		0.2604	1.6780	2.0746	0.0384
Diluted (HK cent per share)		0.2578	N/A	2.0579	N/A

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE NINE MONTHS ENDED 30TH SEPTEMBER, 2009

1. BASIS OF PREPARATION

The condensed consolidated financial statements have been prepared in accordance with the applicable disclosure requirements of the GEM Listing Rules and with Hong Kong Accounting Standard 34, *Interim Financial Reporting*.

2. SIGNIFICANT ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared under the historical cost convention, except for certain financial instruments that are measured at revalued amounts or fair values, as appropriate.

A number of new or revised Standards and Interpretations are effective for the financial year beginning on 1st January, 2009. Except as described below, the same accounting policies, presentation and methods of computation have been followed in these condensed consolidated financial statements as were applied in the preparation of the Group's financial statements for the year ended 31st December, 2008.

HKFRS 8 *Operating Segments*

(effective for annual periods beginning on or after 1st January, 2009)

HKFRS 8 is a disclosure Standard that has resulted in a redesignating of the Group's reportable segments, but has had no impact on the reported results or financial position of the Group.

HKAS 1 (revised 2007) *Presentation of Financial Statements*

(effective for annual periods beginning on or after 1st January, 2009)

HKAS 1 (revised 2007) has introduced a number of terminology changes (including revised titles for the condensed consolidated financial statements) and has resulted in a number of changes in presentation and disclosure. However, HKAS 1 (revised 2007) has had no impact on the reported results or financial position of the Group.

3. TURNOVER

Revenue represents the net amounts received and receivable for goods sold and services rendered by the Group to outside customers, less returns and allowances. An analysis of the Group's revenue for the nine months ended 30th September, 2009 is as follow:

	Three months ended 30th September,		Nine months ended 30th September,	
	2009 HK\$'000	2008 HK\$'000	2009 HK\$'000	2008 HK\$'000
Sales of piped gas	109,564	96,291	338,705	275,613
Connection revenue from gas pipeline construction	55,641	58,799	132,371	125,650
Operation of compressed natural gas ("CNG") filling stations	18,491	2,544	41,126	5,943
Sales of liquefied petroleum gas	8,170	8,879	22,366	26,993
Sales of stoves and related equipment	4,008	1,082	9,219	2,714
	<u>195,874</u>	<u>167,575</u>	<u>543,787</u>	<u>436,913</u>

4. SEGMENT INFORMATION

The Group has adopted HKFRS 8 *Operating Segments* with effect from 1st January, 2009. HKFRS 8 requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess its performance. In contrast, the predecessor Standard (HKAS 14 *Segment Reporting*) required an entity to identify two sets of segments (business and geographical), using a risks and rewards approach, with the entity's system of internal financial reporting to key management personnel serving only as the starting point for the identification of such segments. As a results, following the adoption of HKFRS 8, the identification of the Group's reportable segments has changed.

In prior years, segment information reported externally was analysed on the basis of the types of goods supplied by the Group's operating divisions (i.e. sales of piped gas, connection revenue from gas pipeline construction, sales of liquefied petroleum gas, operation of CMG filling station and sales of coalbed methane ("CBM")). The Group's reportable segments under HKFRS 8 are as follows:

Sales of piped gas

Connection revenue from gas pipeline construction

Operation of CNG filling stations

Sales of liquified petroleum

Sales of CBM

Other operations include the sale of stove.

Information regarding these segments is presented below. Amounts reported for the prior period have been restated to conform to the requirements of HKFRS 8.

The following is an analysis of the Group's turnover and results by operating segment for the periods under review:

For the nine months ended 30th September, 2009

	Sales of piped gas	Connection revenue from gas pipeline construction	Operation of CNG filling stations	Sales of liquified petroleum gas	Sales of CBM	Other operations	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover	<u>338,705</u>	<u>132,371</u>	<u>41,126</u>	<u>22,366</u>	-	<u>9,219</u>	<u>543,787</u>
Segment results	<u>17,519</u>	<u>66,836</u>	<u>9,542</u>	<u>184</u>	<u>(3,226)</u>	<u>4,446</u>	95,301
Unallocated corporate income							9,403
Unallocated corporate expenses							(30,574)
Finance costs							(36,671)
Change in fair value of derivative financial instruments							37,362
Gain on the repurchase of convertible bonds							<u>3,737</u>
Profit before tax							78,558
Income tax charge							<u>(20,047)</u>
Profit for the period							<u>58,511</u>

For the nine months ended 30th September, 2008

	Sales of piped gas <i>HK\$'000</i>	Connection revenue from gas pipeline construction <i>HK\$'000</i>	Operation of CNG filling stations <i>HK\$'000</i>	Sales of liquefied petroleum gas <i>HK\$'000</i>	Sales of CBM <i>HK\$'000</i>	Other operations <i>HK\$'000</i>	Total <i>HK\$'000</i>
Turnover	<u>275,613</u>	<u>125,650</u>	<u>5,943</u>	<u>26,993</u>	<u>-</u>	<u>2,714</u>	<u>436,913</u>
Segment results	<u>10,770</u>	<u>58,170</u>	<u>1,201</u>	<u>(1,442)</u>	<u>(4,904)</u>	(44)	63,751
Unallocated corporate income							10,565
Unallocated corporate expenses							(27,183)
Finance costs							(32,584)
Change in fair value of derivative financial instruments							(4,989)
Gain on the repurchase of convertible bonds							<u>-</u>
Profit before tax							9,560
Income tax charge							<u>(4,318)</u>
Profit for the period							<u>5,242</u>

5. OTHER GAINS AND LOSSES

	Nine months ended 30th September,	
	2009	2008
	<i>HK\$'000</i>	<i>HK\$'000</i>
Change in fair value of derivative financial instruments	37,362	(4,989)
Gain on the repurchase of convertible bonds (<i>Note</i>)	<u>3,737</u>	<u>-</u>
	<u>41,099</u>	<u>(4,989)</u>

Note:

On 11th March, 2009, the Group entered into a purchase agreement with one of the holders ("Bond Holder A") of the convertible bonds ("Bonds") in an aggregate principal amount of US\$40,000,000 due 2012 issued by the Company to five institutional subscribers on 25th June, 2007 pursuant to which the Company agreed to repurchase and the Bond Holder A agreed to sell an aggregate outstanding principal amount of the Bond amounting to US\$5,000,000 at 80% of the principal amount. In addition, the Company paid all the accrued interest to Bond Holder A up to the date of completion of the said agreement. The aforesaid transaction was completed on 14th March, 2009.

On 25th March, 2009, the Group entered into a conditional agreement ("Amendment Agreement") with the holders ("Bond Holders B") of the Bonds pursuant to which the Company and the Bond Holders B had conditionally agreed to alter the existing terms and conditions of the Bonds in an aggregate principal amount of US\$35 million due 2012 issued by the Company to the Bond Holders B on 25th June, 2007 in accordance with the bond subscription agreement dated 28th May, 2007 in exchange for the repurchase by the Company of the 40% of the outstanding Bonds in an aggregate principal amount of US\$14 million (the "Repurchase Bonds") from the Bond Holders B at a purchase price representing 110% of the principal amount of the Repurchase Bonds, together with all accrued and unpaid interest on the Repurchase Bonds up to 18th May, 2009 and the payment of the fee in an aggregate amount of US\$150,000 to the Bond Holders B. For details of the aforesaid transaction, please refer to the Company's circular ("Circular") dated 15th April, 2009.

On 4th May, 2009, an ordinary resolution approving the Amendment Agreement was duly passed by the independent Shareholders by way of poll at an extraordinary general meeting of the Company. The aforesaid connected transaction was completed on 18th May, 2009.

6. FINANCE COSTS

	Nine months ended	
	30th September,	
	2009	2008
	HK\$'000	HK\$'000
Interest on bank borrowings	14,995	17,247
Effective interest expense on convertible bonds	21,676	15,337
	<u>36,671</u>	<u>32,584</u>

7. INCOME TAX CHARGE

	Nine months ended 30th September,	
	2009 HK\$'000	2008 HK\$'000
PRC Enterprise Income Tax	13,408	4,318
Dividend Withholding Tax	6,639	-
	<u>20,047</u>	<u>4,318</u>

On 26th June, 2008, the Hong Kong Legislative Council passed the Revenue Bill 2008 which reduced corporate profits tax rate from 17.5% to 16.5% effective from the year of assessment 2008/2009. Therefore, Hong Kong Profits Tax is calculated at 16.5% of the estimated assessable profit for the year.

On 16th March, 2007, the PRC promulgated the Law of the PRC on Enterprise Income Tax (the "New Law") by Order No. 63 of the President of the PRC. On 6th December, 2007, the State Council of the PRC issued Implementation Regulation of the New Law. Under the New Law and Implementation Regulation, the Enterprise Income Tax of the Group's subsidiaries in the PRC was reduced from 33% to 25% from 1st January, 2008 onwards. Therefore, the PRC Enterprise Income Tax is calculated at a tax rate of 25%, which is the prevailing tax rate in the PRC.

No provision for Hong Kong Profits Tax has been made in the consolidated financial statements as the Company and its subsidiaries had no assessable profits arising in Hong Kong.

Pursuant to the relevant laws and regulations in the PRC, certain PRC subsidiaries of the Group and the jointly controlled entity are exempted from PRC Enterprise Income Tax for two years starting from their first profit-making year, followed by a 50% reduction for the next three years. The tax concession arrangement of the aforesaid PRC subsidiaries will be expired from 2009 to 2011. According to New Law, the tax concession arrangement will not be granted to all new applicants incorporated after 16th March, 2007. As for the existing group entities entitle such tax concession but have not commenced their first profit-making year will be exempted from PRC Enterprise Income Tax for two years, followed by a 50% reduction for the next three years regardless of its reported results commencing from 1st January, 2008 and the charge of PRC Enterprise Income Tax for the year has been provided for after taking these tax incentive into account.

10. DIVIDENDS

No dividend was paid or proposed during the nine months ended 30th September, 2009, nor has any dividend been proposed since 30th September, 2009 (2008: nil).

11. PROPERTY, PLANT AND EQUIPMENT

During the period under review, the addition to property, plant and equipment was approximately HK\$63,273,000 (2008: HK\$65,176,000).

12. CONVERTIBLE BONDS

The movement of embedded derivative of the convertible bonds during the nine months ended 30th September, 2009 is set out below:

	Liability	Embedded derivatives	Total
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
At 1st January, 2009	233,141	101,961	335,102
Repurchased during the period, net of cost incurred	(116,513)	(40,840)	(157,353)
Interest charged	21,676	–	21,676
Interest paid	(1,339)	–	(1,339)
Gain arising on change in fair value	–	(37,362)	(37,362)
	<u> </u>	<u> </u>	<u> </u>
At 30th September, 2009	<u>136,965</u>	<u>23,759</u>	<u>160,724</u>

13. ACQUISITIONS, DISPOSALS AND SIGNIFICANT INVESTMENTS

Save as disclosed herein, the Group had no acquisitions, disposals nor significant investments for the nine months ended 30th September, 2009.

14. Reserve

	Property						Total
	Share premium	Share options reserve	Share options reserve	Other reserve	Translation reserve	Accumulated losses	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Balance at 1st January, 2008 (audited)	<u>623,920</u>	<u>14,071</u>	<u>1,128</u>	<u>7,607</u>	<u>52,302</u>	<u>(21,871)</u>	<u>677,157</u>
Profit for the period	-	-	-	-	-	744	744
Exchange differences arising on translation of foreign operations	-	-	-	-	53,473	-	53,473
Total comprehensive income for the period	-	-	-	-	53,473	744	54,217
Shares repurchased and cancelled	(4,793)	-	-	-	-	-	(4,793)
Equity-settled share-based payments	-	5,917	-	-	-	-	5,917
Balance at 30th September, 2008 (unaudited)	<u>619,127</u>	<u>19,988</u>	<u>1,128</u>	<u>7,607</u>	<u>105,775</u>	<u>(21,127)</u>	<u>732,498</u>
Balance at 1st January, 2009 (as restated)	<u>617,376</u>	<u>20,971</u>	<u>1,128</u>	<u>7,607</u>	<u>104,032</u>	<u>(114,668)</u>	<u>636,446</u>
Profit for the period	-	-	-	-	-	40,123	40,123
Exchange differences arising on translation of foreign operations	-	-	-	-	63	-	63
Total comprehensive income for the period	-	-	-	-	63	40,123	40,186
Exercise of share option	3,678	(168)	-	-	-	-	3,510
Shares repurchased and cancelled	(397)	-	-	-	-	-	(397)
Equity-settled share-based payments	-	5,674	-	-	-	-	5,674
Transfer	-	-	-	20,204	-	(20,204)	-
Balance at 30th September, 2009 (unaudited)	<u>620,657</u>	<u>26,477</u>	<u>1,128</u>	<u>27,811</u>	<u>104,095</u>	<u>(94,749)</u>	<u>685,419</u>

BUSINESS REVIEW

Overall

We are an early mover in developing a vertically integrated gas operation from upstream resource development to downstream distribution in the PRC. During the year under review, we are principally engaged in (i) the exploration, exploitation and development of coalbed methane (“CBM”) and (ii) the development, construction of gas pipeline network, sales of piped gas and sales of natural gas from compressed natural gas (“CNG”) filling station for vehicles in the People’s Republic of China (the “PRC”).

Upstream CBM Exploration

With the aim to ensure sufficient and cost-effective gas supply for the Group’s downstream gas projects located in Henan Province, the PRC and enhance the Group’s profitability, the Group tapped into the upper stream CBM supply market in the PRC in 2007.

As at 30th September, 2009, the Group secured eight coal blocks, situated at Jiaozuo, Zhengzhou, Pingdingshan (including Yuzhou and Ruzhou), Hebi, Yima, Yongxia, Henan Province, the PRC to explore, exploit, develop and produce CBM.

As at 30th September, 2009, the Group successfully completed drilling of 33 vertical wells in Jiaozuo and all of them have entered into dewatering and releasing process since third quarter 2008 and some are showing positive result until now. In April 2008, the Group has appointed Netherland, Sewell & Associates, Inc. (“NSAI”), a renowned energy research firm, to prepare an independent report confirming the extent of the Group’s CBM deposits. The estimated low, medium and high gas volumes in Jiaozuo CBM block as of 1st April, 2008 were approximately 4,166.9 BCF (approximately 118.0 bln m³), 5,916.3 BCF (approximately 167.5 bln m³) and 9,275.6 BCF (approximately 262.7 bln m³) respectively. The result indicates an enormous CBM reserves located in our Jiaozuo CBM block, and approximates to the preliminary gas volume estimation which was conducted by the related domestic CBM exploration institutions and announced by the Group before. Going onward, the Group will further extend the trial and exploration in Jiaozuo CBM blocks as well as to better master its reserve estimates, with the aim of hastening the commercial production of the CBM.

Downstream Natural Gas Distribution

The Group’ downstream natural gas distribution business primarily comprises sales of piped gas, gas pipeline construction and sales of natural gas from CNG filling stations for vehicles.

New Gas Projects

During the period under review, the Group secured two new piped gas projects, the details of which are as follows:

Linyi Shanlin Gas Company Limited

On 25th May, 2009, Linyi China Gas City Gas Construction Company Limited (“Linyi China Gas”), a non-wholly owned subsidiary of the Company, entered into an agreement (the “Capital Injection Agreement”) with seven independent third parties in respect of the proposed injection in registered capital of Linyi Shanlin Gas Company Limited (“Linyi Shanlin”) by Linyi China Gas. Pursuant to the Capital Injection Agreement, the registered capital of Linyi Shanlin will be increased by RMB10,160,000 to RMB15,160,000. The increase in the registered capital of Linyi Shanlin will be contributed by Linyi China Gas in cash. Linyi China Gas financed such capital contribution from its internal funds. Apart from the contribution towards the increase in registered capital as set out above, there are no further capital commitments that are required to be contributed by the Group to Linyi Shanlin.

Immediately after completion of the Capital Injection Agreement, Linyi Shanlin is owned as to 67% by Linyi China Gas and as to the remaining 33% by the aforesaid seven independent third parties. Linyi Shanlin is to be an indirect non wholly-owned subsidiary of the Company.

Linyi Shanlin was established on 6th January, 2008 by the aforesaid seven independent third parties and is engaged in the construction and operation of piped natural gas projects on an exclusive basis in the economic development district located in between the west of 臨沂縣城西一路 (Linshuxianchengxiyilu) and the south of 老327國道 (Lao 327 Guodao South), Linyi City, Shandong Province, the PRC. The business activities of Linyi Shanlin include the design and installation of natural gas pipeline network and ancillary facilities and the provision of piped natural gas, as well as sale and maintenance of natural gas appliances. Linyi Shanlin was granted by the Peoples' Government of Linyi City a 30-year exclusive right to engage in the construction and operation of piped natural gas projects in the areas as mentioned above.

For the period between 6th January, 2008, being the date of establishment of Linyi Shanlin, and 31st December, 2008, the turnover, loss before tax and loss after tax of Linyi Shanlin amounted to RMB2,047,438, RMB(920,194) and RMB(920,194) respectively. For the five months ended 31st May, 2009, the turnover, profit before tax and profit after tax of Linyi Shanlin amounted to RMB18,224,811, RMB318,416 and RMB318,723 respectively.

Xiu Wu Zhongyu Gas Development Company Limited

On 18th August, 2009, Jiaozuo China-Gas City Gas Development Company Limited (“Jiaozuo China-Gas”), a non-wholly owned subsidiary of the Company, established a company, namely 修武中裕燃氣發展有限公司 (Xiu Wu Zhongyu Gas Development Company Limited) (“Xiu Wu Zhongyu”) with two individual parties in Jiaozuo City, Henan Province, the PRC. To the best of Directors’ knowledge, information and belief having made all reasonable enquiries, such two individual parties are persons who are not connected persons the meaning ascribed to it in the GEM Listing Rules of the Company (“Independent Third Parties”).

Xiu Wu Zhongyu is owned as to 60% by Jiaozuo China-Gas and as to the remaining 40% by the aforesaid Independent Third Parties.

The registered capital of Xiu Wu Zhongyu is RMB8,000,000 and is contributed as to RMB4,800,000 by Jiaozuo China-Gas in cash and as to the remaining RMB3,200,000 by the aforesaid Independent Third Parties in cash. Upon establishment, Xiu Wu Zhongyu becomes an indirect non-wholly-owned subsidiary of the Company.

Xiu Wu Zhongyu is engaged principally in the construction and operation of piped natural gas projects on exclusive basis for a 30-year in Xiu Wu County, Jiaozuo City, Henan Province, the PRC.

The Directors are of the view that the entering into of the Capital Injection Agreement and the establishment of Xiu Wu Zhongyu could provide an opportunity for the Group to further invest in the natural gas business in the PRC in order to enlarge the geographical coverage of its operations. In addition, having considered that the natural gas projects operated by Linyi Shanlin and Xiu Wu Zhongyu are on an exclusive basis and the increase in demand of natural gas in the PRC, the Directors are of the view that Linyi Shanlin and Xiu Wu Zhongyu could provide a steady cash inflow to the Group. Besides, since the Linyi Shanlin and Xiu Wu Zhongyu is accounted for as a non wholly-owned subsidiary of the Company, the Directors consider that the capital injection in Linyi Shanlin and the establishment of Xiu Wu Zhongyu would not have any material adverse impact on the Group’s net assets or the Group’s net tangible assets.

The entering into of the Capital Injection Agreement and the establishment of Xiu Wu Zhongyu do not constitute discloseable transactions on the part of the Company under Chapter 19 of the GEM Listing Rules.

As at 30th September, 2009, the Group secured eleven exclusive gas projects, three in Shandong Province, the PRC and eight in Henan Province, the PRC.

The cities in which the Group’s gas projects operate currently have a total connectable urban population of approximately 3,084,000. It is estimated that there are an aggregate of approximately 881,000 connectable residential households in such cities.

CNG Filling Stations

With the aim to enhance the Group's turnover and results, the Group has commenced to develop CNG vehicle gas filling business in the PRC since September 2007. In September 2007, one CNG filling station has been erected and commenced its operation in Linyi City, Shangdong Province, the PRC. In October 2008, the Group has completed construction of a new CNG filling station in Luohe City, Henan Province, the PRC. The commercial operation of such CNG filling station has been commenced from the end of November 2008. In March 2009, the Group has completed the construction of a new CNG filling station in Jiyuan City, Henan Province, the PRC, and such CNG filling station commenced commercial operation on 1st April, 2009. As at 30th September, 2009, one more CNG filling station located in Sanmenxia City, Henan Province, the PRC is under construction. We anticipate that the construction works of such CNG filling station will be completed by the end of 2009. In future, the Group plans to erect five new CNG filling stations in Luohe City, Jiyuan City and Senmenxia respectively by 2010 in order to increase the Group's market share.

On 7th September, 2009, Mr. Zhao Wei Liang ("Mr. Zhao") as vendor and Zhongyu (Henan) Energy Holdings Limited ("Zhongyu Henan"), a wholly-owned subsidiary of the Company, as purchaser entered into the equity transfer agreement ("Equity Transfer Agreement"), pursuant to which Mr. Zhao has conditionally agreed to sell to Zhongyu Henan the entire equity interest held by him in 南京裕聯壓縮氣有限公司 (Nanjing Yulian Compressed Gas Company Limited) ("Nanjing Yulian"), a company established in the PRC with limited liability, in accordance with the terms of the Equity Transfer Agreement, the details of which are disclosed in the Company's announcement dated 7th September, 2009.

Nanjing Yulian, which is wholly-owned by Mr. Zhao, was established on 19th October, 2007 in the PRC. It is an investment holding company and has no other business save for the holding of 70% equity interests in 南京裕聯天然氣加氣有限公司 (Nanjing Yulian Natural Gas Filling Company Limited) ("Nanjing Yulian NG Filling"). Nanjing Yulian obtained approval from local authorities of Nanjing, the PRC to construct a total of eight CNG filling stations in Nanjing.

Nanjing Yulian NG Filling was established on 18th February, 2009 in the PRC. It is owned as to 70% equity interests by Nanjing Yulian and the remaining 30% equity interests by 南京市汽車工業銷售股份有限公司 (Nanjing City Vehicle Industry Sales Shareholding Company Limited). Nanjing Yulian NG Filling is mainly engaged in the operation of CNG vehicle filling station in Nanjing, the PRC.

To the best of the Directors' knowledge, information and belief having made all reasonable enquiry, Mr. Zhao, Nanjing Yulian and Nanjing Yulian NG Filling are third parties independent of the Company and its connected persons.

In order to ease shortage of the natural gas supply and to meet robust demand for clean energy, the construction works for building of West-East natural gas transmission project Project's second pipeline progresses commenced in 2008. The construction works were projected to be completed at the end of 2009 and the commercial operation was planned to be commenced in early 2010. With the aim to secure the Group's future natural gas supply and further develop the Group's downstream natural gas distribution business in Luohe City, Jiyuan City and Senmenxia City, where West-East natural gas pipeline branch networks will cover, the Group has entered into 3 outline agreements of natural gas sales and transportation with the local natural gas suppliers respectively.

Sales of Piped Gas

Approximately 90% of total sales of piped gas for the nine months ended 30th September, 2009 was derived from provision of natural gas. During the period under review, the total unit of natural gas provided by the Group to its customers was approximately 162,580,000 m³ (2008: 130,529,000 m³).

Gas Pipeline Construction

During the nine months ended 30th September, 2009, the Group made new gas pipeline connection for 45,751 residential households (2008: 36,154 residential households) and 169 industrial/commercial customers (2008: 168 industrial/commercial customers). As at 30th September, 2009, the Group have the accumulated number of residential households of 282,813 (2008: 234,782 residential households) and industrial/commercial customers of 1,195 (2008: 955 industrial/commercial customers). As at 30th September, 2009, the Group's penetration rate reached 32% (2008: 27%) (represented by the percentage of accumulated number of residential households to estimated an aggregate of connectable residential households).

Sales of Natural Gas From CNG Filling Stations

During the period under review, the total unit of CNG provided by the Group to its customers was approximately 12,713,000 m³ (2008: 3,597,000 m³).

Sales of LPG

Sales of LPG are not a core business of the Group. During the period under review, the Group sold approximately 4,900 tons of bottled LPG (2008: 3,200 tons).

FINANCIAL REVIEW

For the nine months ended 30th September, 2009, turnover increased by 24.5% to approximately HK\$543,787,000 from approximately HK\$436,913,000 for the corresponding period in 2008. The growth in turnover was mainly attributable to the robust growth in sales of piped gas, connection revenue from gas pipeline construction and sales of natural gas from operation of CNG filling stations.

Sales of piped gas for the nine months ended 30th September, 2009 increased by approximately 22.9% to approximately HK\$338,705,000, accounting for approximately 62.3% of the Group's total turnover. The rapid growth in sales of piped gas was mainly attributable to the increase in the number of households and industrial/commercial users connected as well as the increase in the total gas consumption.

Connection revenue from gas pipeline construction for the nine months ended 30th September, 2009 increased by approximately 5.3% to approximately HK\$132,371,000, accounting for approximately 24.3% of the Group's total turnover. The increase in connection revenue from gas pipeline construction was mainly attributable to the increase in construction work of gas pipeline connection completed for residential households during the period under review.

Sales of natural gas from CNG filling stations for the nine months ended 30th September, 2009 increased by approximately 592.0% to approximately HK\$41,126,000, accounting for approximately 7.6% of the Group's total turnover. Such increase was mainly attributable to the increase in number of CNG vehicle gas refueling stations.

Gross profit margin

The overall gross profit margin for the nine months ended 30th September, 2009 amounted to approximately 30.4% (2008: 28.1%). The increase was mainly due to the increase in the gross profit margin of connection revenue from gas pipeline construction resulting from the increase in average connection fee charged to each residential household.

Other gains and loss

The Group recorded a non-cash gain arising on change in fair value of derivative financial instruments which was issued by the Company in June 2007 of approximately HK\$37,362,000 for the nine months ended 30th September, 2009 (2008: Loss: HK\$(4,989,000)). Also the Group recorded a gain of approximately HK\$3,737,000 on the repurchase of Bonds of USD19,000,000 during the period under review.

Operating expenses

Operating expenses, including selling and distribution costs and administrative expenses increased by 18.2% to approximately HK\$95,147,000 for the nine months ended 30th September, 2009 from approximately HK\$80,506,000 for the corresponding period in 2008. The increase was mainly attributable to the increase in PRC staff salary cost and amortisation of other intangible assets.

Share-based payment

The Group recorded a share-based payment expense of approximately HK\$5,674,000 for the share options granted on 3rd April, 2008 for the nine months ended 30th September, 2009 (2008: HK\$5,917,000).

Finance costs

Finance costs increase by 12.5% to approximately HK\$36,671,000 for the nine months ended 30th September, 2009 from approximately HK\$32,584,000 for the corresponding period in 2008. The increase was mainly attributable to the increase in non-cash effective interest expense charged on convertible bonds to approximately HK\$21,676,000 for the nine months ended 30th September, 2009 (2008: HK\$15,337,000) which was partially offset by the decrease in the interest on bank borrowings to approximately HK\$14,995,000 for the nine months ended 30th September, 2009 (2008: HK\$17,247,000) resulting from the decrease in the average borrowings.

Income tax expenses

No provision of Hong Kong Profits Tax has been made as the Group had no assessable profits arising in Hong Kong for the year 2009 and 2008.

Pursuant to the relevant laws and regulations in the PRC, certain PRC subsidiaries of the Group and the jointly controlled entity are exempted from PRC Enterprise Income Tax for two years starting from their first profit-making year, followed by a 50% reduction for the next three years. The tax concession arrangement of the aforesaid PRC subsidiaries will be expired from 2009 to 2011. According to New Law, the tax concession arrangement will not be granted to all new applicants incorporated after 16th March, 2007. As for the existing group entities entitle such tax concession but have not commenced their first profit-making year will be exempted from PRC Enterprise Income Tax for two years, followed by a 50% reduction for the next three years regardless of its reported results commencing from 1st January, 2008 and the charge of PRC Enterprise Income Tax for the year has been provided for after taking these tax incentive into account.

The Group paid dividend withholding tax of approximately HK\$6,639,000 in the event of inter-group dividend distribution during the nine months ended 30th September, 2009 (2008: nil).

Accordingly, the income tax expenses for the nine months ended 30th September, 2009 amounted to approximately HK\$13,408,000 (2008: HK\$4,318,000).

Profit attributable to equity holders of the Company

As a result of the above, profit attributable to equity holders of the Company amounted to approximately HK\$40,123,000 for the nine months ended 30th September, 2009 (2008: HK\$744,000).

Earnings before interests, taxation, depreciation, amortisation (“EBITDA”)

For the nine months ended 30th September, 2009 excluding other income and other gains and loss, the Group’s EBITDA increased by 55.7% to approximately HK\$95,368,000 from approximately HK\$61,247,000 for the corresponding period in 2008.

Connected Transaction

On 25th March, 2009, the Group entered into a conditional agreement (“Amendment Agreement”) with the holders (“Bond Holders B”) of the Bonds pursuant to which the Company and the Bond Holders B had conditionally agreed to alter the existing terms and conditions of the Bonds in an aggregate principal amount of US\$35 million due 2012 issued by the Company to the Bond Holders B on 25th June, 2007 in accordance with the bond subscription agreement dated 28th May, 2007 in exchange for the repurchase by the Company of the 40% of the outstanding Bonds in an aggregate principal amount of US\$14 million (the “Repurchase Bonds”) from the Bond Holders B at a purchase price representing 110% of the principal amount of the Repurchase Bonds, together with all accrued and unpaid interest on the Repurchase Bonds up to 18th May, 2009 and the payment of the fee in an aggregate amount of US\$150,000 to the Bond Holders B. For details of the aforesaid transaction, please refer to the Company’s circular (“Circular”) dated 15th April, 2009.

One of the Bond Holders B, Perry Capital LLC, is a substantial Shareholder of the Company which, as at 14th April 2009, being the latest practicable date prior to the printing of the Circular, holds 254,298,000 Shares, representing approximately 13.15% of the issued share capital of the Company. As such, the entering into by the Company of the Amendment Agreement with Perry Capital LLC constitutes a connected transaction for the Company under rule 20.13(1)(a) of the GEM Listing Rules and is subject to independent Shareholders’ approval requirement pursuant to rule 20.18 of the GEM Listing Rules.

The terms and conditions of the Bonds outstanding after completion of the Amendment Agreement, in an aggregate principal amount of US\$21,000,000 (the "Outstanding Bonds") held by Bond Holders B have been amended, the coupon rate will be revised to 2% per annum, and will mature on 25th June, 2012. The mandatory redemption option held by the Bond Holders B has been cancelled. The Company must redeem a portion of the outstanding principal amount of the Outstanding Bonds in the amount and at the redemption prices set out below and in one of the following ways:

- (a) on 25th June, 2010, redeem not less than US\$1,050,000 in principal amount of the Outstanding Bonds, at the redemption price of 110% of the US\$ principal amount of Convertible Bonds so redeemed, together with any accrued and unpaid interest; and
- (b) on 25th June, 2011,
 - (i) if less than US\$2,100,000 in principal amount of the Outstanding Bonds were redeemed on 25 June 2010, redeem not less than US\$3,150,000 in principal amount of the Outstanding Bonds, at the redemption price of 120% of the US\$ principal amount of Convertible Bonds so redeemed, together with any accrued and unpaid interest; or
 - (ii) if US\$2,100,000 or more in principal amount of the Outstanding Bonds were redeemed on 25th June, 2010, redeem not less than US\$2,100,000 in principal amount of the Outstanding Bonds, at the redemption price of 110% of the US\$ principal amount of Convertible Bonds so redeemed, together with any accrued and unpaid interest.

The Bond Holders B can convert the remaining outstanding principal amount of the Outstanding Bonds into ordinary shares of the Company at HK\$0.7 per share from the completion date of the Amendment Agreement to 25th June, 2012.

On 4th May, 2009, an ordinary resolution approving the Amendment Agreement was duly passed by the independent Shareholders by way of poll at an extraordinary general meeting of the Company. The aforesaid connected transaction is completed on 18th May, 2009.

Prospects

The Group is confident in its future prospects since the natural gas market in China will continue to boom amid the global economic downturn. Striving for energy independence, the Chinese government is supporting the exploration and development of domestic energy sources. Along with the rising awareness to environmental protection, the demand for clean energy in China will remain its growth momentum. In order to capture this growing demand, the Group is expanding its downstream natural gas distribution with a focus on high margin commercial and industrial users and compressed natural gas filling stations. It will also increase the number of residential users to further enhance its penetration rate in the nine cities it is operating in. Meanwhile, the Group will hasten the commercialization of its CBM production by advancing the exploration technology as well as extending the exploration of CBM to coal block outside Jiaozuo city, optimizing our vertically integrated value chain and rendering our future prospect promising. The constant revenue growth in the downstream projects coupled with the promising outlook of the upstream resources exploration, we are confident to further enhance our market position as well as our financial performance.

In addition to the abovementioned strategies, the Group is cautiously seeking for suitable investment opportunities. With our healthy financial position, coupled with the constant cash inflow generated by our downstream projects, we believe that we would be able to prudently increase our market penetration. At the same time, we will strive to enhance our operation efficiency by cooperating with promising peers in the industry. We believe that Zhongyu Gas is well-positioned to tackle the challenges imposed by the global economic environment and maximize our shareholders' returns.

DISCLOSURE OF INTERESTS

(a) Interests of Directors

As at 30th September, 2009, the interests and short positions of the Directors and the Chief Executive of the Company and their associates in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Future Ordinance (the "SFO")) (a) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO); or (b) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (c) which were required to be notified to the Company and the Stock Exchange pursuant to Rules 5.46 to 5.67 of the GEM Listing Rules relating to securities transactions by Directors, were as follows:

Long positions in the Shares of the Company:

Name of Directors	Notes	Nature of Shares and/or underlying Shares	Type of Interests	Approximate percentage of issued share capital
Mr. Wang Wenliang	1	956,923,542	Beneficial and interest in corporation	49.39%
Mr. Hao Yu	2	1,010,759,542	Beneficial and interest in corporation	52.16%
Mr. Lu Zhaoheng	3	8,004,000	Beneficial	0.41%
Mr. Xu Yongxuan	4	5,004,000	Beneficial	0.26%
Mr. Lui Siu Keung	5	12,000,000	Beneficial	0.62%
Dr. Luo Yongtai	6	2,000,000	Beneficial	0.10%
Mr. Hung, Randy King Kuen	6	2,000,000	Beneficial	0.10%

Notes:

1. Among these Shares and/or underlying Shares, 945,755,542 Shares are held by Hezhong Investment Holding Company Limited (“Hezhong”). Mr. Wang Wenliang is beneficially interested in 60% of the issued share capital of Hezhong. 10,002,000 of the remaining 11,168,000 underlying Shares are to be allotted and issued upon exercise the rights attaching to the share options granted at an exercise price of HK\$0.31 per share under the share option scheme adopted by the Company on 24th October, 2003.
2. Among these Shares and/or underlying Shares, 945,755,542 Shares are held by Hezhong. Mr. Hao Yu is interested in 40% of the issue share capital of Hezhong. The remaining 8,004,000 and 57,000,000 underlying Shares are to be allotted and issued upon exercise the rights attaching to the share options granted at an exercise price of HK\$0.31 per share and HK\$0.56 per share respectively under the share option scheme adopted by the Company on 30th September, 2003.
3. 5,004,000 and 3,000,000 underlying Shares are to be allotted and issued upon exercise the rights attaching to the share options granted at an exercise price of HK\$0.31 per share and HK\$0.80 per share respectively under the share option scheme adopted by the Company on 30th September, 2003.

4. 5,004,000 underlying Shares are to be allotted and issued upon exercise the rights attaching to the share options granted at an exercise price of HK\$0.31 per share under the share option scheme adopted by the Company on 30th September, 2003.
5. 9,000,000 and 3,000,000 underlying Shares entitle the holder thereof to subscribe for Shares at an exercise price of HK\$0.56 per share and HK\$0.80 per share respectively under the share option scheme adopted by the Company on 30th September, 2003.
6. These underlying Shares entitle the holders thereof to subscribe for Shares at an exercise price of HK\$0.80 per share under the share option scheme adopted by the Company on 30th September, 2003.

Save as disclosed above, as at 30th September, 2009, none of the Directors nor the chief executive of the Company had or was deemed to have any interests and short positions in the shares, underlying shares or debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which were required (i) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of the SFO); or (ii) are required, pursuant to section 352 of the SFO, to be entered in the register referred to therein; or (iii) are required, pursuant to Rules 5.46 to 5.67 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange.

(b) Interests of substantial shareholders of the Company

So far as is known to the Directors, as at 30th September, 2009, the following entities (not being Directors or chief executive of the Company) had, or were deemed to have, interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO or who were directly or indirectly interested in 5% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group.

Long positions in the shares

Name of Shareholder	Type of interests	Number of Shares	Approximate percentage of interests
Hezhong	Beneficial	945,755,542	48.81%
Perry Capital (Asia) Limited	Investment manager	367,794,657	19.01%
Perry Capital LLC	Investment manager	367,794,657	19.01%
Perry Corp.	Investment manager	367,794,657	19.01%
Perry Richard Cayne	Interest in corporation	367,794,657	19.01%
Perry Partners International, Inc.	Beneficial	305,311,668	16.00%

Notes:

1. Hezhong is beneficially interested in 945,755,542 shares. Mr. Wang Wenliang and Mr. Hao Yu are beneficially interested in 60% and 40% of the issued share capital of Hezhong respectively.
2. According to the disclosure of interests pages as shown in the website of the Stock Exchange, Perry Richard Cayne holds as to 100% equity interests of Perry Corp. Perry Corp. holds as to 40% equity interest of Perry Capital LLC. Perry Capital LLC holds as to 100% equity interests of Perry Capital (Asia) Limited. Apart from the information ascertained in the disclosure of interests pages as shown in the website of the Stock Exchange, the Company has no further information.

Save as disclosed above, as at 30th September, 2009, the Directors were not aware of any other person (other than the Directors and the chief executive of the Company) who had, or was deemed to have, interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was directly or indirectly interested in 5% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any members of the Group.

COMPETING INTEREST

During the period under review, none of the directors, the management shareholders or substantial shareholders of the Company or their respective associates (as defined in the GEM Listing Rules) had any interest in a business which competed with or might compete with the business of the Group.

CODE OF CORPORATE GOVERNANCE PRACTICES

The Company has complied with all the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 15 of the GEM Listing Rules with deviation as mentioned below.

Code provision A.4.1 provides that non-executive directors should be appointed for specific term, subject to re-election. The Company has deviated from this provision in that all non-executive Directors are not appointed for specific term. They are, however, subject to retirement by rotation at each annual general meeting of the Company and eligible for re-election according to the Company's articles of association.

AUDIT COMMITTEE

The Company's Audit Committee, comprising Mr. Wang Shunlong, Dr. Luo Yongtai and Mr. Hung, Randy King Kuen, as the independent non-executive Directors, has reviewed with the Company's management the accounting principles and practices adopted by the Group and discussed internal controls and financial reporting matters including a review of the unaudited results of the Group for the nine months ended 30th September, 2009.

BOARD PRACTICE AND PROCEDURES

The Company has complied with the requirement of Board Practices and Procedures as set out in Rules 5.34 of the GEM Listing Rules during the nine months ended 30th September, 2009.

PURCHASE, SALE OR REDEMPTION OF SHARES

During the nine months ended 30th September, 2009, the Company repurchased a total of 1,050,000 (2008: Nil) shares through the Stock Exchange at a price ranged from HK\$0.38 to HK\$0.39 (2008: NA) per share at an aggregate consideration of HK\$405,750 (2008: NA). All Shares were cancelled.

Save as disclosed above, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the shares during the nine months ended 30th September, 2009.

BOARD OF DIRECTORS

As at the date of this report, the Board comprises Mr. Wang Wenliang (*Chairman*), Mr. Hao Yu (*Chief Executive Officer*), Mr. Lu Zhaoheng and Mr. Lui Siu Keung (*Chief Financial Officer*), as the executive Directors, Mr. Xu Yongxuan (*Vice-Chairman*), as the non-executive Director and Mr. Wang Shunlong, Dr. Luo Yongtai and Mr. Hung, Randy King Kuen, as the independent non-executive Directors.

By Order of the Board
Wang Wenliang
Chairman

Hong Kong, 30th October, 2009