

Financial Review

Commentary on major variances in the Consolidated Profit and Loss Account and Balance Sheet

	2000 HK\$M	1999 HK\$M
Consolidated Profit and Loss Account		
Turnover		
In the Property Division, there was a slight fall in gross rental income in Hong Kong and reduced proceeds from the sale of trading and investment properties in the USA. Improved vessel utilisation and charter rates in Swire Pacific Offshore accounted for the increase in turnover in the Marine Services Division. The Trading & Industrial Division suffered a decrease in turnover due to the disposal of The Eagle's Eye, Swire & Maclaine and Camberley Enterprises at the end of 1999 and Swire Loxley in February 2000. However, increased turnover was recorded in the car businesses in Taiwan and Mainland China and from the retailing of sportswear in Hong Kong.	15,050	16,862
Operating profit		
The Property Division suffered a fall in both net rental income and contribution from the sale of development and investment properties. Operating profits were further reduced by the provision for land premium relating to Horizon Gardens. The Beverages Division saw improved profits due to volume growth in the USA following the acquisition of the Ogden franchise in April 2000, and a slight increase in margins. The Marine Services Division recorded an increase in operating profit due to the improving offshore oil services market and the consequent increase in charter rates and vessel utilisation. The increase in operating profit in the Trading & Industrial Division is mainly attributable to improved operating results from Taikoo Motors Offshore's car businesses in Taiwan and from sportswear and apparel in Hong Kong.	3,845	3,884
Net finance charges		
The decrease of HK\$53 million in net finance charges was due to lower floating interest rates and an increase in interest capitalised into development properties.	(432)	(485)
Share of profits less losses of jointly controlled companies		
The marked decrease reflects a non-recurring provision for diminution in value of the Ocean Shores property development and the loss on sale of Carlsbrew Brewery (Shanghai).	(1,636)	256

Share of profits less losses of associated companies

Cathay Pacific contributed the majority of the increase in profit, with an increase in demand for passenger and cargo services leading to high yields and load factors across the network. An improvement in HAECO's operating profitability following the restructuring of the cost base in 1999 was augmented by non-recurring profits from the sale of shareholdings in jointly controlled companies and surplus properties.

2,964 1,432

Taxation

The effective rate of tax rose to 11.9% as a result of non-deductible provisions totalling HK\$1,832 million. The low effective rate of tax reflects brought-forward losses and, in 1999, a rebate for Hong Kong profits tax.

565 416

Minority interests

The increase in minority interests is primarily due to improved results from Hong Kong Air Cargo Terminals and increased net rental income at Festival Walk.

287 236

Profit attributable to shareholders

Profit attributable to shareholders decreased by 12.3%, primarily due to non-recurring provisions in the Property and Trading & Industrial Divisions, partially offset by a significant increase in the profit contribution from Cathay Pacific.

3,889 4,435

Consolidated Balance Sheet

Fixed assets

The increase in fixed assets was mainly due to the upward revaluation of the investment property portfolio in Hong Kong and capital expenditure on investment properties.

77,265 65,393

Investments in jointly controlled companies

The decrease reflects the provision for diminution in value of the Ocean Shores property development, dividends received and the loss on sale of the Carlsbrew Brewery (Shanghai), partially offset by loans advanced to jointly controlled companies in the Property Division and profits retained during the year.

6,953 8,196

Investments in associated companies

The increase in investments in associated companies reflects profits retained during the year, and the share of the increase in the cash flow hedge reserve in the Cathay Pacific Group.

17,493 15,307

Properties for sale

The increase was mainly due to land premium and development costs incurred on the Taikoo Valley Site V residential site in Hong Kong and Three Tequesta Point in the USA. This increase was partially offset by the sale of apartments within the StarCrest development in Hong Kong and the sale of trading properties in the USA.

1,958 1,625

Trade and other payables

The increase was mainly due to the provision for land premium and accrued interest on Cityplaza Four, Cityplaza Three, Cityplaza One and Horizon Gardens amounting to HK\$4,500 million.

9,623 5,175

Bank overdraft and short-term loans/long-term loans and bonds due within one year

The decrease was mainly due to the refinancing of short-term loans with term bank loans and bonds.

2,142 3,852

Long-term loans and bonds

The increase in long-term loans and bonds reflects the refinancing of short-term bank borrowing with term loans and floating rate bonds.

10,486 9,048

Minority interests

The increase reflects the minority share of property revaluations and retained profits during the year, partially offset by the repayment of shareholders' loans to minority interests in the Property Division.

5,203 4,280

Shareholders' funds

The increase relates principally to an increase in the property valuation reserve and to profits retained during the year.

76,064 68,509

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Set out below is further information which will assist in the formation of a balanced assessment of the financial position and results for the year of the Swire Pacific group.

Review of Operating Results

The principal activities of the Swire Pacific group, together with the contribution of each activity to group results, are as follows:

The Company and its subsidiaries:

	Turnover		Operating profit/(loss)	
	2000	1999	2000	1999
	HK\$M	HK\$M	HK\$M	HK\$M
Property:				
Property investment	4,692	4,776	3,354	3,384
Property trading	1,114	1,749	145	209
Sale of investment properties	–	515	–	54
Provision for land premium	–	–	(151)	–
Beverages	4,584	4,590	256	211
Marine Services	843	812	227	210
Trading & Industrial	3,871	4,488	174	72
Other net expenses and consolidation adjustments	(54)	(68)	(160)	(256)
	15,050	16,862	3,845	3,884

Jointly controlled companies:

	Share of profits/(losses) before taxation	
	2000	1999
	HK\$M	HK\$M
Property:		
Property investment and trading	15	51
Provision for diminution in value of development property	(1,700)	–
Beverages	69	81
Marine Services:		
Ship repair, land engineering and harbour towage	66	58
Container handling	23	13
Shipowning and operating	4	(4)
Trading & Industrial:		
Normal operations	21	(4)
Non-recurring items	(132)	66
Others	(2)	(5)
	(1,636)	256

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Associated companies:

	Share of profits/(losses) before taxation	
	2000 HK\$M	1999 HK\$M
Property:		
Hotels and restaurants	73	34
Aviation:		
Airline services and airline catering	2,302	1,110
Aircraft engineering	166	27
Cargo handling	129	(8)
Marine Services:		
Container handling	294	276
Insurance	–	(7)
	2,964	1,432

The activities of the Swire Pacific group are based mainly in Hong Kong. An analysis of group turnover and contribution to group operating profit by principal markets is outlined below:

	Turnover		Operating profit/(loss)	
	2000 HK\$M	1999 HK\$M	2000 HK\$M	1999 HK\$M
Hong Kong	8,545	8,916	3,273	3,578
Asia (excluding Hong Kong)	3,128	2,596	157	51
North America	2,529	3,937	188	121
Europe	5	604	–	(76)
Shipowning and operating	843	809	227	210
	15,050	16,862	3,845	3,884

Shipowning and operating activities are carried out internationally and cannot be attributed to specific geographical areas.

An analysis of group attributable profit/(loss) by division is as follows:

	Attributable profit/(loss)	
	2000 HK\$M	1999 HK\$M
Property	947	3,002
Aviation	2,510	1,038
Beverages	185	187
Marine Services	501	472
Trading & Industrial	(84)	195
Other net expenses and consolidation adjustments	(170)	(459)
	3,889	4,435

Financial Risk Management Policy

Financing for Swire Pacific subsidiaries in Hong Kong is provided primarily by Swire Pacific, which raises funds both directly and through wholly-owned finance subsidiaries. Certain

working capital lines and overdraft facilities are arranged by individual subsidiaries. All areas of financial risk management activity are subject to policies, guidelines, exposure limits, and systematic authorisation and reporting. The group's listed associated companies, Cathay Pacific and HAECO, arrange their financial affairs on a stand-alone basis. Their financing activities are undertaken in a manner consistent with the overall financial policies of the group.

Use of Derivatives

In the normal course of business, Swire Pacific and Cathay Pacific use interest rate and currency swaps in connection with their borrowings. Such derivative transactions are entered into in order to manage exposure to fluctuations in foreign currency exchange rates and interest rates. In addition, Cathay Pacific is a party to forward contracts and options for the purchase of aviation fuel. It is the policy of the Swire Pacific group not to enter into derivative transactions for speculative purposes. The implementation of the hedging policy is only undertaken following approval from the Board.

Derivatives involve, to varying degrees, credit and market risk. With regard to credit risk, the group would be exposed to loss in the event of non-performance by a counterparty. The group controls credit risk through approved counterparty limits and monitoring procedures.

Market risk is the possibility that a movement in interest rates or currency rates will cause the value of a derivative to fluctuate or change the cost of settling the underlying obligations. Derivatives are used solely for management of an underlying risk and the group is not exposed to market risk since gains and losses on the derivatives are offset by losses and gains on the assets, liabilities or transactions being hedged. The group is not required by its counterparties to provide collateral or any other form of security against any change in the market value of a derivative.

Management of Currency Exposure

Exposure to movements in exchange rates on individual transactions in the Swire Pacific group is minimised using forward foreign exchange contracts where active markets for the relevant currencies exist. With the exception of the Perpetual Capital Securities, which have no scheduled maturity, all significant foreign currency borrowings are covered by appropriate currency hedges.

Translation exposure arising on consolidation of the group's overseas net assets is reduced, where practicable, by broadly matching assets with borrowings in the same currency. Substantial proportions of the revenues, costs, assets and liabilities of Swire Pacific and its subsidiary companies are denominated in Hong Kong dollars.

The long-term financial obligations of Cathay Pacific have been arranged primarily in currencies in which it has substantial positive operational cash flows, thus establishing a natural currency hedge. The policy adopted requires that anticipated surplus foreign currency earnings should be at least sufficient to meet the foreign currency interest and principal repayment commitments in any year.

Capital Resources & Liquidity

Swire Pacific's total shareholders' funds have increased to HK\$76,064 million at the end of 2000 compared with HK\$68,509 million at the end of 1999, mainly due to the upward revaluation

of the group's investment property portfolio and retained earnings.

At 31st December 2000, the Swire Pacific group held cash deposits of HK\$404 million whilst bank loans and other borrowings due within one year amounted to HK\$2,142 million.

An analysis of the group's net borrowings by currency at 31st December 2000, including US\$600 million (HK\$4,642 million) of Perpetual Capital Securities, is shown below:

Currency	HK\$M	
Hong Kong Dollar	9,829	59%
United States Dollar	6,301	37%
New Taiwan Dollar	736	4%
Others	(51)	—
	16,815	100%

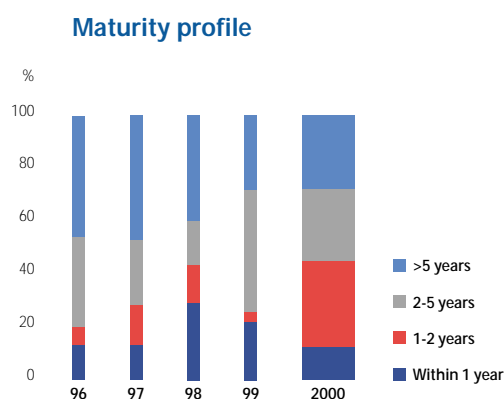
Sources of Finance

At 31st December 2000, committed loan facilities and other financing in place amounted to HK\$18,356 million, of which 13% remained undrawn. In addition, there were uncommitted facilities undrawn at the year end amounting to HK\$3,512 million. Sources of funds at the end of 2000 comprised:

	Available HK\$M	Drawn HK\$M	Undrawn HK\$M
Committed facilities			
Perpetual Capital Securities	4,642	4,642	—
Bonds	2,321	2,321	—
Private Placement	852	852	—
Floating Rate Notes	2,500	2,500	—
Bank and other loans	8,041	5,653	2,388
	18,356	15,968	2,388
Uncommitted facilities			
Money market & others	4,814	1,302	3,512

Maturity Profile

It is group policy to secure adequate funding so as to match cash flows associated with both current and planned investments. The maturity profile of the group's gross borrowings at the end of each of the last five years is set out below.



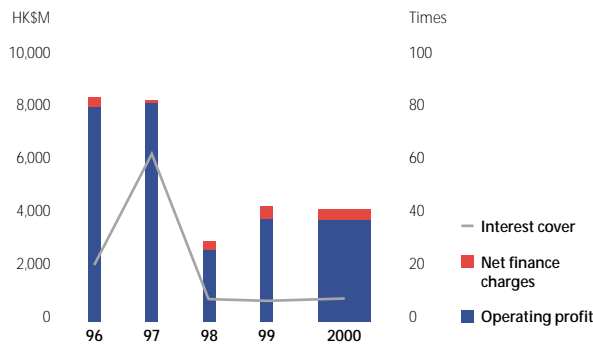
Interest Rate Profile

In addition to raising funds on a fixed rate basis, the group uses interest rate swaps and other instruments where appropriate in the management of its interest rate profile. At 31st December 2000, 45.8% of the group's gross borrowings were on a floating rate basis and 54.2% were on a fixed rate basis.

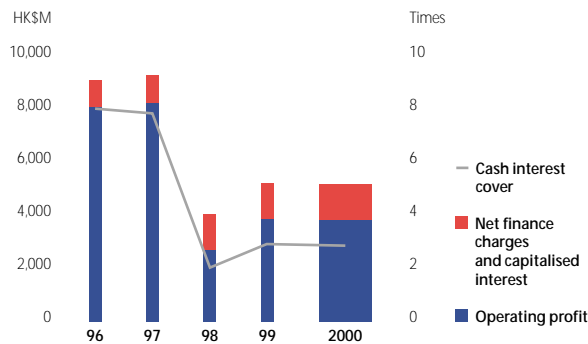
Interest Cover and Gearing

The following graphs illustrate interest cover, cash interest cover and gearing ratios for each of the last five years. Interest cover for the year ended 31st December 2000 was 8.90 times while cash interest cover, calculated by reference to total interest charges including those capitalised, was 2.87 times. The gearing ratio was 0.21 at the end of 2000.

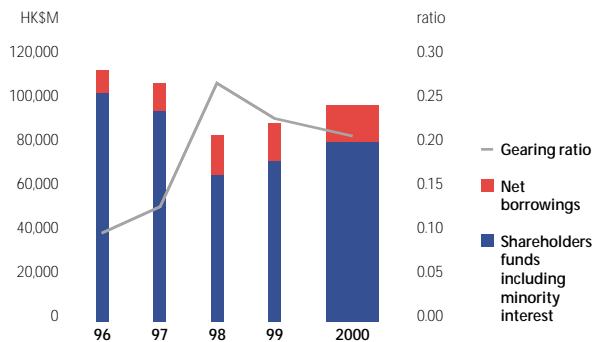
Interest cover



Cash interest cover

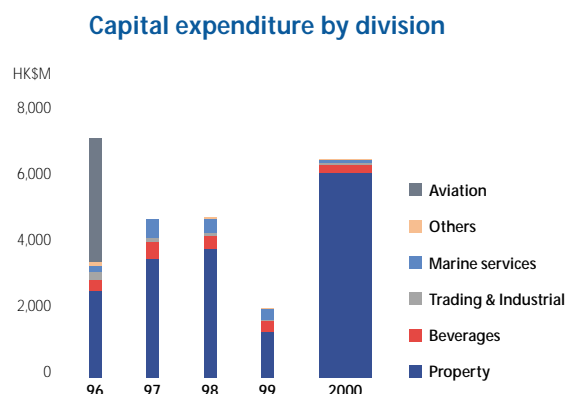


Gearing ratio



Capital Expenditure

Capital expenditure incurred by the group in 2000 was HK\$6,595 million. The graph below illustrates capital expenditure by division over the last five years:



The major outgoings during 2000 in the Property Division related to expenditure on Cambridge House, the Cityplaza renovation and the provision in respect of the Taikoo Shing arbitration. Expenditure in the Beverages Division was mainly on property, production and distribution equipment, including the acquisition, during the year, of fixed assets relating to the Ogden franchise. Within the Marine Services Division, capital expenditure related principally to instalment payments on six new offshore support vessels for delivery from 2001 to 2003.