Infrastructure Investments – Transportation

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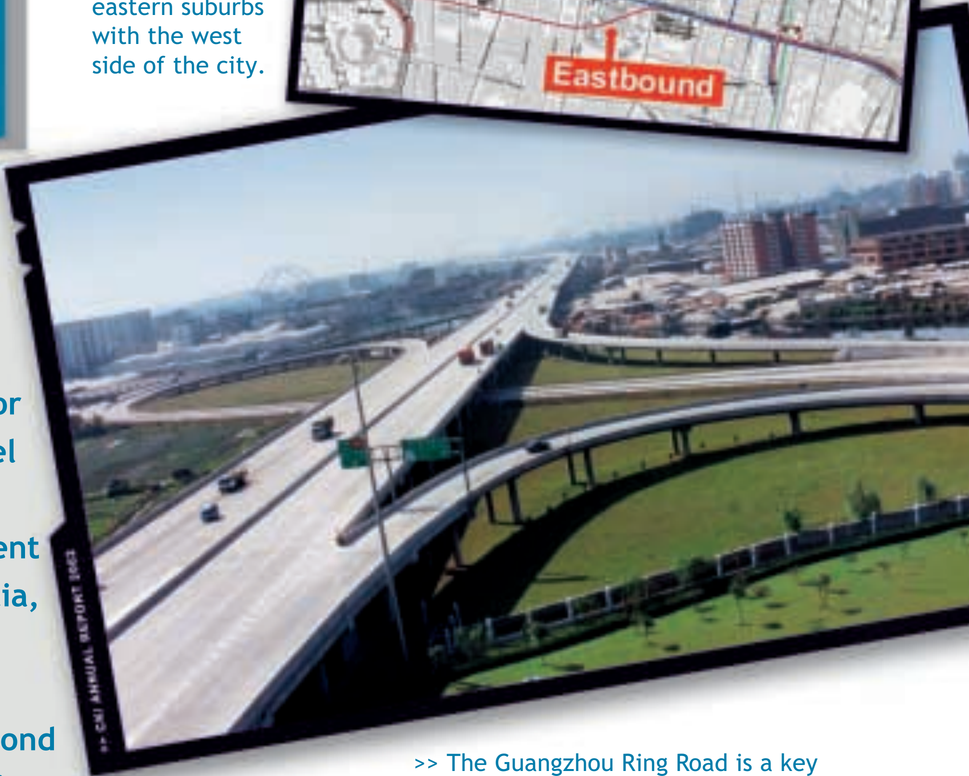
>> The Cross City Tunnel will be linking Sydney's eastern suburbs with the west side of the city.



>> The Guangzhou Ring Road is a key expressway surrounding the eastern, southern and western areas of the Guangzhou City.

An exciting milestone achievement of CKI Transportation in 2002 was the winning of the tender for the Sydney Cross City Tunnel project. The tunnel is CKI's first infrastructure investment in New South Wales, Australia, and is also the Group's first step in expanding its transportation portfolio beyond Hong Kong and Mainland China. The transportation division has followed the successful formula of the energy division by diversifying its business and expanding geographically. Apart from roads and bridges, the Group has explored other transportation investments such as airports and cable-car transit systems.

The Sydney Cross City Tunnel

In December 2002, the Cross City Motorway Consortium, in which CKI has a 50 per cent. interest, was awarded the Cross City Tunnel project in Sydney by the New South Wales Government. Construction work began in early 2003 and is targeted for completion in 2006.

The A$1 billion toll tunnel will be over two kilometers long, linking Sydney's eastern suburbs with the west side of the city. It is expected to carry about 90,000 vehicles per day at opening, forming a vital part of Sydney's future transportation planning.

The financing of the investment was arranged with 55 per cent. non-recourse project loans, and shareholders' equity was funded by guaranteed project loans. According to this financing model, no funding cost will be carried by the Group during the construction period. This investment is expected to be another premium asset for CKI, delivering a favourable investment return upon completion.

Road Projects in Guangdong

The spectacular growth and development of Guangdong, particularly in the Pearl River Delta, has led to an increase in privately-owned vehicles and goods transportation activities. All the toll roads and bridges owned and operated by CKI have benefited from increased economic activities and the consequent growth in traffic flow, resulting in double digit increment in toll revenue.

Other Transportation Projects in Mainland China

Government policies and major road rehabilitation programmes were introduced on transportation projects outside Guangdong. Nevertheless, CKI's investment targets for these projects were largely met.

Consolidation of China Infrastructure Portfolio

During the year, the Zengcheng Lixin Road was sold for HK$132 million and generated a gain of approximately HK$50 million; disposal of the Nanhai Road Network was also largely completed with about HK$1.4 billion recouped.

The Group's consolidation strategy also includes the impending sales of the Shenyang Roads and Bridges and the Jiangmen Jianghe Highway, which are expected to be concluded in 2003. In accordance with new government regulations, some of the Group's assured-return contracts will be converted into new joint-venture contracts on risk sharing basis. CKI's consolidation of its infrastructure investments in China will soon be completed.

Hong Kong Eastern Harbour Crossing Tunnel

In Hong Kong, the Group took a 50 per cent. stake in the Eastern Harbour Crossing Company Limited, which owns the rail tunnel connecting eastern Hong Kong and eastern Kowloon. During the year, the tunnel generated satisfactory returns as well as stable cash flow for the Group.

>> The Shantou Bay Bridge recorded double digit growth in toll revenue in 2002.

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Infrastructure Materials and Infrastructure-related Businesses

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Infrastructure Materials and Infrastructure-related Businesses encompass both the Group's on-going operations in infrastructure materials and new initiatives in environmental and electronic infrastructure. While Green Island Cement and Anderson Asia are well recognised market leaders in the domestic cement and concrete industries, the Group's ventures in selective infrastructure-related businesses, such as environmentally friendly hydrogen system technology and electronic infrastructure initiatives are also growing in importance.

>> Electronic security systems involving smart card and biometrics have gained broader recognition and acceptance.

Infrastructure Materials

As a result of the deflationary environment and declining property market, both domestic consumption of and prices for cement, concrete and aggregates suffered further declines in 2002. The slowdown of public housing works and the recent decision to stop all government ownership-housing programmes are expected to further dampen infrastructure materials prices and volumes in 2003.

In such a challenging market, Green Island Cement and Anderson Asia have continued to impose stringent cost control measures, while striving to deliver the best possible customer service and most reliable product supply for users. Though profit contribution further reduced and represented a modest percentage of CKI's total profit contribution, both Green Island Cement and Anderson Asia maintained strong cash balances due to slim capital expenditure programmes and strong cash inflow from non-cash items such as depreciation expenses.

As with the Hong Kong domestic market, Green Island Cement's infrastructure materials business in Mainland China also faced strong price pressure and so saw a further reduction of profit margin. An over-supply situation continued in many cities amid a slowdown in construction activities.

During the year, Anderson Asphalt continued to maintain its market share and contributed a satisfactory profit as budgeted. The order book on

>> Green Island Cement is the market leader in the domestic cement industry.

>> Hydrogen generation and supply system for hydrogen vehicle fuelling.

hand remains healthy and the business is expected to continue to be profitable in 2003.

Environmental Commitments

During the year, the Group continued to focus on environmental initiatives in waste handling and recycling, waste to energy conversion and clean energy.

Waste Material Recycling

Green Island International has been working with the Hong Kong University of Science and Technology on a 24-month pilot programme to study "integrated co-combustion cement manufacturing facility for waste minimisation and energy optimisation". The research programme studies waste handling via a thermal process at 1,200 degree Celsius, an extremely high temperature made possible using a burning kiln rather than a conventional incinerator. The heat generated can also be picked up and converted into electricity to drive cement production facilities, and the residual ash can be recycled as raw material for cement manufacturing.

Water Treatment

In China, CKI has a water treatment joint venture committed to providing quality water supply in Yueyang, Hunan Province. The tariff was raised in 2002.

Polymer Modified Asphalt

In Canada, CKI has a 63.4 per cent. stake in Polyphalt Inc., a technology company that develops and commercialises polymer modified asphalt products and technology for North American and international markets. During the year, the Liaohe Refinery in Liaoning Province started polymer modified asphalt production as planned.

>> CKI's water plant investment in Yueyang, Hunan.

Hydrogen Energy

While new shares were issued for the acquisition of Vandenborre Technologies, N.V., CKI's investment in Stuart Energy Systems Corp., the leading global developer and supplier of integrated hydrogen solutions, was slightly diluted to around 9 per cent. Other than conventional industrial hydrogen applications, the alternative clean energy will also cover distributed energy and hydrogen fuelled vehicle markets.

In addition to the equity investment, CKI also holds an exclusive distribution right for the hydrogen fuelling technology in Asia Pacific until 2012.

Electronic Infrastructure

Electronic security systems involving smart cards and biometrics have gained broader recognition and acceptance as a result of increasing concerns about security. The Group has been working with different technology providers to develop and deliver one-stop security solutions by integrating different electronic biometrics and security technologies.

Financial Review

Financial Resources, Treasury Activities and Gearing Ratio

The Group's capital expenditure and investments were funded from cash in hand, internal cash generation, syndicated loans, notes issued and other project loans.

As at 31st December, 2002, total borrowings of the Group amounted to HK$12,645 million, which included Hong Kong dollar syndicated loan of HK$3.8 billion, foreign currency borrowings of HK$8,754 million and RMB bank loans of HK$91 million. Of the total borrowings, 18 per cent. were repayable in 2003, 66 per cent. repayable in 2004 to 2007 and 16 per cent. repayable beyond 2007. The Group's financing activities continue to be well received and fully supported by its bankers.

The Group adopts conservative treasury policies in cash and financial management. To achieve better risk control and minimise the cost of funds, the Group's treasury activities are centralised. Cash is generally placed in short-term deposits mostly denominated in Hong Kong dollars, U.S. dollars or Australian dollars. The Group's liquidity and financing requirements are reviewed regularly. The Group will consider new financing while maintaining an appropriate level of gearing in anticipation of new investments or maturity of bank loans.

As at 31st December, 2002, the Group maintained a gearing ratio of 19 per cent. which was based on its net debt of HK$5,454 million and equity of HK$28,853 million. This ratio was higher than the gearing ratio of 16 per cent. at the year end of 2001 due to drawdown of a short-term Australian dollars bridging loan of HK$1,823 million for the acquisition of CitiPower I Pty Ltd. during the year. For potential project financing requirements from business growth, the Group issued foreign currency fixed rate notes totalling HK$1,813 million in March 2002 under the Group's US$2 billion medium term note programme established in March 2001. In addition, the Group entered into a syndicated loan facility agreement of HK$3.8 billion in May 2002 which was fully drawn in September 2002 to refinance the HK$3.1 billion syndicated loan.

To minimise currency risk exposure in respect of its investments in other countries, the Group has a policy of hedging those investments with the appropriate level of borrowings denominated in the local currencies of those countries. As at 31st December, 2002, the Group has swapped the floating interest rates of its borrowings totalling HK$6,539 million into fixed interest rates. The Group will consider entering into further interest and currency swap transactions to hedge against its interest rate and currency risk exposures, as appropriate.

Charge on Group Assets

As at 31st December, 2002:

- certain of the Group's land and buildings and other assets with carrying values totalling HK$78 million were pledged to secure bank borrowings totalling HK$24 million; and
- the Group's interests in an affiliated company with carrying value of HK$1,982 million were pledged as part of the security to secure bank borrowings totalling HK$4,778 million granted to the affiliated company.

Contingent Liabilities

As at 31st December, 2002, the Group was subject to the following contingent liabilities:

HK$ million	
Guarantees in respect of bank loans drawn by affiliated companies	1,031
Performance bonds	25
Total	**1,056**

Employees

The Group, including its subsidiaries but excluding affiliated companies, employs a total of 1,898 employees. Employees' cost (excluding directors' emoluments) amounted to HK$370 million. The Group ensures that the pay levels of its employees are competitive and that its employees are rewarded on a performance related basis within the general framework of the Group's salary and bonus system.

Preferential subscription of 2,978,000 new shares of the Company was given to those employees who had submitted the pink application forms to subscribe for shares of HK$1.00 each in the Company at HK$12.65 per share on the flotation of the Company in 1996. The Group does not have any share option scheme for employees.