Chairman's Letter

RESULTS FOR 2002

The performance of Orient Overseas (International) Limited and its subsidiaries (the "Group") for the year of 2002 as a whole has turned out to be much better than expected. In my statement on 16th August 2002 in the Interim Report, I referred to the first half of 2002 as having been one of the worst business environments in the history of the industry but I also intimated that at that time there were some signs that, for our core business of containerisation transportation, the imbalance between supply and demand was beginning to right itself. This indeed proved to be the case and I am pleased to be able to report that the Group recorded a profit before tax and minorities of US$62.9 million for the financial year 2002. A profit attributable to shareholders of US$51.7 million was recorded which represents a fall of just 16% from the attributable profit of US$61.3 million which we recorded in 2001. We should view this result as a commendable achievement in the light of the prevailing economic conditions throughout much of the year during which the industry as a whole experienced considerable difficulties.

The Board of Directors recommends the payment of a final dividend of US2.5 cents (HK19.5 cents) per share to ordinary shareholders. Over the years the Board of Directors has maintained a policy of proposing the dividend at a level which reflects the performance of the Group for the period in question but balanced by the capital needs of the company in the light of both the then prevailing and predicted future business conditions. It was for these reasons that the Board of Directors considered it imprudent to recommend a dividend at the interim stage for 2002. However, the result for the year as a whole is a significant improvement over that predicted in the middle of 2002 and the forecast trading conditions for 2003 have also improved over the last six months. The recommended final dividend of US2.5 cents (HK19.5 cents) maintains the dividend at the same level as was paid for the year of 2001 as a whole.

The Group's operations remain organised into two distinct operating entities a structure which continues to give each the required independence and ability to concentrate on their respective businesses.

Our International Transportation, Logistics and Terminals division performed admirably during 2002. The end of 2001 and the beginning of 2002 was a period during which business sentiment was possibly at one of its lowest ebbs ever, certainly in relation to the container liner industry. Business confidence had fallen steadily during 2001, made still worse by the sad events of 11th September 2001, as world economic growth slowed and amidst forecasts of a further world-wide slowdown and of a recession in the US, still the dominant driver of world trade and economic activity. The supply side projections exacerbated the situation with projections of significant tonnage increases to be deployed during the year which would serve only to perpetuate the problem of inadequate freight rates. It was in this environment in early 2002 of poor volume growth forecasts and pessimistic projections of significant tonnage increases in which we were obliged to negotiate the service contracts, under which we carry the majority of our containers, for the contract year 2002/2003. They were perhaps the worst business conditions for many years and, as a result, contract rates for the industry in general were set at almost unsustainably low levels.

Against this background of severely depressed trading conditions we placed an even greater emphasis on improving our cost efficiency. In the event however, and as so often transpires, container volume growth in 2002 exceeded all expectations and the introduction of new tonnage into service was at a lower rate than forecast. During the traditional peak season, rather than ships sailing the oceans half full as the pessimists had been predicting there was a marked shortage of space. This situation was then accentuated by the temporary work stoppage at US West Coast ports. However, this latter event had the effect of once again driving home the point to shippers as a whole, that quality of service, the certainty of available space and both the promptness and reliability of delivery, should remain or indeed be reinstated at the top of their priority list. During the second half of 2002 therefore, better utilisation levels led to stronger freight rates as the availability of space tightened. However, the full impact upon freight rates is delayed until the current service contracts either expire, the majority on 30th April 2003, or are fulfilled in terms of their minimum quantity requirements.

Our container terminal businesses in North America enjoyed mixed fortunes in 2002 as they had in 2001. Overall, the four terminals, two in New York and two in Vancouver, achieved a 3.9% increase in throughput. However, both the volume growth and performance varied significantly between the individual operations. In Vancouver the two terminals, Vanterm and Deltaport, performed commendably and achieved a combined increase of 26% in throughput, in terms of actual lifts, and a 75% improvement in operating profits. We expect them to maintain this level of performance in 2003.

In New York, our terminal at Howland Hook has now begun to reap the benefits of the management changes we made in late 2001 and which I outlined in my Letter last year. For the year 2002, and for the first time albeit in its relatively short history, it has made a meaningful contribution to Group profits on a total throughput much unchanged from 2001. Unfortunately it did suffer the loss of one customer in the latter part of 2002 but our continued efforts to negotiate a lower cost base together with the gradual replacement of this lost throughput, provide us with the confidence that an even better performance will ensue in 2003.

I have to report on the other hand however, that Global Terminal in New Jersey experienced a very difficult 2002. I mentioned last year that due to bankruptcy it had lost one of its two major customers and this unfortunately was followed in 2002 by the loss of its other major customer as a result of the exercise in the rationalisation of services undertaken by many of the major liner companies during the early part of last year. As a consequence, Global Terminal experienced a near 60% fall in throughput thereby producing a negative result for the year. However, I am pleased to report that as a result of a noteworthy and collective management effort to secure new business, a significant level of replacement throughput has been contracted to the extent that, with the number of vessel calls already increased during February 2003, Global Terminal has now returned to profitability. These measures, combined also with being the recipient of diverted services caused by the congestion at some other terminals as the supply and demand balance improves in the Port of New York and New Jersey, gives us a degree of confidence that for 2003 Global Terminal will have returned to a more adequate level of profitability as it returns to operating at 85 to 90% of capacity.

We continue to invest significantly into these terminal facilities as we upgrade both the equipment and the services we provide to our customers. In addition we remain alert to the opportunities which arise from time to time to invest in other new terminal projects in which we see good prospects in terms of location, hinterland and future profitability.

During 2002 we have continued the development of our automated IT platforms. Cargo*Smart*, the award winning neutral portal developed by us for the container transportation industry, is designed to allow customers a faster response time and self-directed and automated services providing better cost efficiencies. Today, it is employed daily by over 5,000 different companies and currently holds over 800,000 managed shipments. To enhance efficiency and effectiveness amongst carriers and vendors, further enhancements to Depot*Smart*, the neutral online depot operations network, have been delivered. All processes and amendments are fully transparent and simultaneously updated to prevent errors and to provide operational cost savings as well as to streamline operational and communications efficiency. Today, over 380 depots around the world are using Depot*Smart*. Internally, we continue to enhance our award winning object-oriented enterprise system, IRIS-2. It remains the driver within the organisation towards the continuing improvement of our products and services for the benefit of our customer base as a whole. It also continues to provide us with greater business efficiencies and cost savings which have become evermore crucial as a result of the difficult economic conditions of 2002.

OOCL Logistics, formerly known as Cargo System, is the Group's international logistics management division. Founded as a global freight services provider and through leading-edge IT applications, OOCL Logistics today serves as a Lead Logistics Provider ("LLP"). By integrating a wide range of value added services through its worldwide network, it provides customers with integrated international logistics solutions, managing and optimising multiple carriers, service providers and transportation modes with visibility and event management capabilities. While bearing the well-recognised OOCL brand name, OOCL Logistics is a neutral LLP, with the goal to maximise value for its customers. It is well positioned to expand in the rapidly growing marketplace in a manner consistent with the Group's short and long term business objectives. To extend its IT logistics leadership OOCL Logistics has also launched the Horizon Project which seeks to manage the entire supply chain from manufacture through to retail. It will further enhance and improve our supply chain logistics products and services to our customers.

Consistent with the Group's overall goal of the significant expansion of its logistics services capabilities, OOCL Logistics will focus upon Service Quality and the continual improvement of customer satisfaction. It will create cost efficiencies by creating programs and services that measurably save time and money both internally and for customers. Through the introduction of new products and services it will meet growing customer needs for expanded global freight management and logistics services. It will also place yet further emphasis on and build upon its long-standing presence and experience in China, which we continue to view as the market in which we lead in expertise and which possesses the greatest potential. OOCL Logistics will expand its distribution capabilities and facilitate the effective customer utilisation of business practices and, with its Information Technology, it will continue to deliver advanced, integrated, web-based solutions that support a full range of transportation, warehouse management, network collaboration and management reporting requirements.

Our Property Development and Investment division enjoyed another good year in 2002. Our development projects in Shanghai benefited yet again from the increasingly active and rising residential real estate market. During the year, we continued our efforts to maximise the returns from our existing projects, to source new projects and, even more firmly, to consolidate what is already a profitable business unit. We believe that this has already largely been achieved and the reputation of Orient Overseas Developments Ltd ("OODL") in Shanghai yet further enhanced. We look forward to being able to take additional advantage of the experience and expertise already gained to create an independent, professional and firmly profitable business.

We believe that both China's entry to the WTO and the gradual build up to the 2008 Olympic Games will slowly but surely benefit all sectors of the Beijing property market but in the longer term. Beijing Oriental Plaza, in which the Group continues to hold an 8% interest, will also therefore begin to enjoy the better returns from a stronger market environment as existing leases fall due for renewal. At the present time however it remains a long-term investment and is unlikely to begin to produce a return in the shorter term.

At the operational level, Wall Street Plaza performed less well than it did in 2001. It began 2002 with a 100% occupancy rate and with the vast majority of its rentable space leased through until 2004. However, as I had last year intimated might happen, one major tenant, under Chapter XI protection, handed back a significant proportion of the lettable space. This had an obvious effect upon the performance for the year but nevertheless the return from this investment remained healthily positive although below budget. Great efforts have been made over the past months to re-let this space and we are confident that by the end of March 2003 the vacancy rate will have been reduced to under just 3%. However, the events of 11th September 2001 continue to overhang sentiment and the demand for prime office space in Lower Manhattan. Rental levels have suffered accordingly. Last year we took the prudent measure of writing down the book value of this investment property and, as a result, we have been able to leave it unchanged for this year.

To predict the outcome for the current year is possibly a little easier than it was at this time last year. I can certainly be a little more confident of our overall performance than I was last time. Although there are some conflicting indicators, the recovery of the US economy appears to be entrenched if at a modest pace. While the measures of consumer confidence reflect some volatility the actual levels of consumer demand for imported goods have of late remained relatively strong. This pattern broadly is repeated in Europe as a whole although there are some pockets of concern such as in Germany where rising unemployment and falling consumer confidence do give rise to some apprehension. It is of course the levels of domestic consumer spending and the behaviour of the consumer which has by far the greatest direct impact upon container volumes. There are therefore a number of issues which could seriously impact upon our business this year and about which we must be concerned. The geopolitical climate around the world is perhaps more fragile right now than it has been for a long time. The continuing conflicts centred on the Middle East cause uncertainty and trepidation in the global economy and serve at the very least to destabilise consumer markets throughout the world. This, combined with the troubles in Venezuela, has served to push up the price of oil significantly which, in addition to inflating our cost base through much higher bunker prices, now has the potential to exert recessionary pressures on the major world economies. More directly, we must also continue to be conscious of the delicate supply and demand balance between container volumes and new tonnage deployment in the major container trades in which we operate. There has been a return over the last six months to a better equilibrium to the extent that there now exists the potential for an excess of demand over supply during the critical peak season. We cannot be confident that this situation will continue into the medium term however. I have already outlined the threats on the demand side but on the supply side orders continue to be placed for new tonnage at prices which appear attractive when compared with their recent heights. Any further increase in this rate of ordering will have the potential to return us together with the remainder of the industry to the situation in which freight rates are unsustainably low. Nevertheless, in the shorter term, we can be marginally more confident with demand seemingly set to remain strong and there being no availability of berth space at the shipyards for newbuilding tonnage until well into 2005.

Each year I pay tribute to the people who work so dedicatedly within the Group and it is possibly even more appropriate this year. They now number some 4,743, both on land and at sea, and it is only through their diligence, perseverance and indeed sometimes both sweat and inspiration, that the Group has been able to achieve the level of performance it has in a year which started so poorly and for so long seemed set to remain poor.

C C Tung
Chairman and Chief Executive Officer
Hong Kong, 14th March 2003

Supply Chain

As a total logistics service provider, drawing on the strengths of our powerful information system, we offer customers integrated and tailor-made logistics solutions at every stage in the supply chain.


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