

I have pleasure to present to shareholders the annual report of Paul Y. - ITC Construction Holdings Limited (the "Company", together with its subsidiaries, the "Group") for the year ended 31st March, 2004.

## REVIEW

### Financial Performance and Positions

For the fiscal year ended 31st March 2004, the Group's consolidated turnover decreased by 7% to approximately HK\$3,382 million when compared with that of last year. When comparing the annual drop of turnover of 32% for the year before, it shows that the continuing downturn in the Hong Kong construction sector in previous years had come to an end and there were signs of a recovery.

In spite of the drop in revenue, the Group's gross profit increased by 310% to approximately HK\$98 million which represents 3% of the turnover due to the persistent effort in implementing risk management and cost saving measures. As a result, the loss from operations was also narrowed down to HK\$26 million as compared with HK\$260 million which included an impairment loss on property of HK\$110 million for last year.

During the year, the Group has disposed of 28.75 million ordinary shares of Downer EDI Limited ("Downer"), which contributed a profit of HK\$179 million to the Group. There were also losses on dilution in relation to investment in associates including China Strategic Holdings Limited ("China Strategic") of HK\$26 million. Share of results of associates and jointly controlled entities registered a profit of about HK\$143 million, showing an increase of 20% which was mainly attributable to the growth of

Downer. With the strong contribution from Downer arising in the share disposal and share of its results, the Group attained a profit before tax of HK\$209 million for the year.

Due to the adoption of the SSAP 12 (Revised), details of which is outlined in note 2 to the financial statements, there is an increase in taxation charge to HK\$46 million, representing mainly the overseas tax in respect of dividend received from and share of results of Downer. Profit for the year was HK\$164 million and basic earnings per share was 14.6 cents.

When compared with the Group's financial position as at last year end, the total assets of the Group remained at HK\$4,862 million, similar to that of last year end. Net current assets increased by 71% to some HK\$895 million. Current assets have consequently been improved from 1.3 times to 1.6 times of current liabilities and the net debt to equity ratio decreased significantly from 0.2 to 0.1 times at this year end. Due to the appreciation of the Australian dollars in relation to the Group's interest in Downer, translation reserve increased by some HK\$93 million. Coupled with the issue of shares for HK\$4

## CHAIRMAN'S STATEMENT

million, the share of China Strategic's reserve of HK\$7 million since it has been an associate, the net profit of HK\$164 million during this year net of dividends paid of HK\$154 million, the shareholders' funds increased by 4% to HK\$2,771 million representing HK\$2.06 per share.

Net cash outflow from operations was about HK\$25 million and inflow of HK\$44 million in respect of investing and financing, resulting in a net increase in cash of about HK\$19 million for the year.

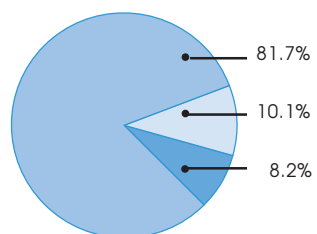
## OPERATIONS

### Contracting and Construction Materials

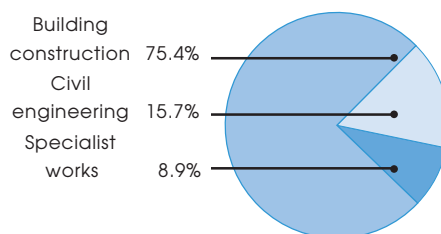
Construction sector output in Hong Kong has been declining for a few years due to reducing capital expenditure by both public and private sectors. This had led to severe competition and eroded the Group's gross margin. Consequently all construction and engineering divisions recorded slight losses. The construction material division was still facing weak demand and experienced losses in operation. As the Group's gross margin work-on-hand is now on uptrend, gross and operating margin is expected to improve.

### Profile of Contracts On Hand as at 31st March, 2004

Value of contracts on hand  
HK\$11,211 million



Value of work remaining  
HK\$4,928 million



## CHAIRMAN'S STATEMENT (Continued)

During the year, the Group secured new contracts with an aggregate attributable value of approximately HK\$3,593 million, which comprised HK\$1,906 million of building construction contracts, HK\$1,388 million of civil engineering contracts and HK\$299 million of specialist works. When compared with last financial year end, contracts on hand increased by 8% to approximately HK\$11,211 million and the value of work remaining stayed at a similar level of approximately HK\$4,928 million at this year end.

Subsequent to the year end, the Group secured further new contracts with an aggregate attributable value of approximately HK\$2,026 million, which comprised HK\$1,588 million of building construction contracts and HK\$438 million of civil engineering contracts.

### Property Operations

Total value of the property portfolio, excluding those self-used properties, amounted to some HK\$515 million as at the year end, equivalent to 11% of the total assets of the Group. Included in the property portfolio are Paul Y. Centre, the Group's headquarter in Kwun Tong and In-Zone, a shopping arcade in Wanchai. During the year, certain investment properties in the PRC were disposed of at approximately their carrying value for some HK\$47 million.

Although the overall rental rates of the investment properties had been reduced, occupancy rate was maintained at the satisfactory level in which Paul Y. Centre remained at an occupancy rate at around 94% at the year end.

Subsequent to the year end, the Group has disposed of its entire interest in In-Zone at approximately its carrying value of some HK\$60 million.

## MAJOR ASSOCIATES

### Downer

Downer reported a revenue of A\$2,680 million (HK\$14,579 million) and A\$1,542 million (HK\$8,388 million) and a net profit after tax of A\$67 million (HK\$364 million) and A\$25 million (HK\$136 million) for the year ended 30th June, 2003 and six months ended 31st December, 2003 respectively. During the year, the Group has arranged for placing of in aggregate of approximately 28.75 million ordinary shares in Downer (adjusted by the consolidation of four ordinary shares in Downer into one ordinary share in Downer on 28th November, 2003) to independent third parties which raised, before tax and expenses, approximately A\$104.1 million (HK\$587.8 million). In addition, the preference shareholders of Downer have exercised their rights to convert the preference shares to 32.5 million ordinary shares in Downer. The Group's shareholding in Downer is maintained at 21.3% as at 31st March, 2004.

Downer provides comprehensive engineering and infrastructure management services to the public and private power, rail, road, telecommunications, mining and minerals processing sectors in Australia, New Zealand, Asia and the Pacific. Its business consists of four main principal activities that have common core competencies. These core competencies include value-adding skills in design, project and facilities management, operations and maintenance to provide clients with single source solutions.

With a healthy work load and highly capable management team, Downer is well positioned to capture attractive opportunity throughout the Asia Pacific Region.

### China Strategic

During the year, the Group and Hanny Holdings Limited ("Hanny") made a voluntary conditional general cash offer for the shares and warrants of China Strategic, other than those owned by the Group and Hanny and parties acting in concert with them and to cancel all the outstanding share options of China Strategic. Upon the closure of the offer in September 2003, the Group held approximately 31.2% interest in shares in China Strategic and as a result, China Strategic becomes an associate of the Group. Due to some issues of ordinary shares by China Strategic upon exercise of warrants and share options, the Group's shareholding in China Strategic was diluted to 29.4% as at 31st March, 2004.

China Strategic is an investment holding company. Through its subsidiaries and associates, China Strategic is engaged in the manufacturing of batteries, property investment, manufacturing and marketing of tires, and the business of providing package tour, travel, hotel operation and other related services. For the year ended 31st December, 2003, China Strategic reported a turnover of some HK\$2,884 million and a loss of some HK\$190 million.

## LIQUIDITY AND CAPITAL RESOURCES

The Group adopts a prudent funding and treasury policy with regard to its overall business operations. A variety of credit facilities is maintained to meet its working capital requirements. During the year, in view of the strong cash inflow generated

from partial disposal of interests in Downer, the Group repaid and reduced its bank borrowing by HK\$215 million. The remaining loans of the Group bear interest at market rates and are with terms of repayment ranging from one year to three years. As at 31st March, 2004, the Group's total borrowings amounted to HK\$561 million with HK\$44 million repayable within one year and HK\$517 million repayable after one year. Cash balances at 31st March, 2004 amounted to HK\$250 million.

As at the year end, all of the Group's borrowings bear interest at floating rates and are denominated in Hong Kong dollars. The Group's gearing ratio decreased from 0.29 at last year end to 0.20 which is calculated based on the total borrowings of HK\$561 million and the Group's shareholders' funds of HK\$2,771 million.

#### NUMBER OF EMPLOYEES, REMUNERATION POLICIES AND SHARE OPTION SCHEME

Including the directors of the Group, as at 31st March, 2004, the Group employed a total of approximately 1,230 full time employees. Remuneration packages comprised of salary and year-end bonuses based on individual merits. In appreciation of our employees' support and contribution in our cost-cutting regime throughout the past few years, a bonus payment to employees was paid during the year. No share options were granted or exercised during the year.

#### PLEDGE OF ASSETS

As at 31st March, 2004, certain of the Group's properties and investment in securities with an aggregate value of approximately HK\$669 million and

the issued shares of certain subsidiaries of the Company have been pledged to banks and financial institutions to secure general credit facilities granted to the Group.

#### CONTINGENT LIABILITIES

As at the year end, the Group has contingent liabilities in respect of outstanding performance bonds on construction contracts of HK\$623 million.

#### PAUL Y. INFRASTRUCTURE

During the year, Paul Y. Infrastructure division was created with a view to deploy the Group's resources into the infrastructure sector in China. In March 2004, the Group acquired at the consideration of HK\$396 million, an effective interest of 54.06% in Yangkou Port in Nantong City of the Jiangsu Province. Yangkou Port is a bulk handling deep sea port currently under construction. Further commitment of HK\$125 million is required to finance the initial phase of development. In addition to the concession granted to operate the port for 50 years, Yangkou Port also owns the marine rights to reclaim 42 square kilometers of land for the purpose of an industrial park development. There is also an option to develop an additional 15 square kilometers of reclaimed land.

It is believed that with the continued rapid growth of China's economy, it is vital that larger deep water and river port facilities are developed and that there is a substantial increase in the logistic facilities available for the handling and storage of strategic raw materials and fuel which are essential for the sustained development of the economy and its import and export commodity trades. In addition to recurring income from

the operation of this well sited and sizable facility in Yangkou Port, the reclaimed land reserve of up to 57 square kilometers industrial land bank will also contribute short and medium land development income to the Group. In order to build up an effective logistic network, the Group is also pursuing opportunities to invest in sizable river ports within the Yangtze Delta region.

#### PAUL Y. CONSTRUCTION GROUP

In March 2004, the Company initiated a capital reorganisation, asset and debt restructuring proposal (the "Skynet Restructuring Proposal") for Skynet (International Group) Holdings Limited ("Skynet"), a company whose shares are listed on The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange"). As part of the Skynet Restructuring Proposal, Paul Y. Construction Group, which undertakes the Group's entire engineering and construction activities, will be sold to Skynet at a consideration of HK\$400 million which is to be satisfied by Skynet issuing new shares to the Company at an issue price of HK\$0.04 per share. Further, approximately HK\$94 million of claim held by the Group against Skynet will be capitalised. Additional financial resource of up to HK\$145 million will also be offered to Skynet in the form of a convertible loan facility and an underwritten share issue in an open offer by Skynet. Upon completion of the Skynet Restructuring Proposal, the Group will become interested in approximately 93.4% of the issued share capital of Skynet and steps will be taken to reduce such holding to no more than 75% in order to maintain the listing position of Skynet. Through Skynet, Paul Y. Construction Group and the

## CHAIRMAN'S STATEMENT *(Continued)*

existing marble business of Skynet will become the Group's 75%-owned subsidiary. Being independently managed and financed, Paul Y. Construction Group and Skynet will be poised in a more efficient position to pursue future growth opportunities. The proposal is expected to be completed in October 2004.

### SECURITIES IN ISSUE

During the year, 9,648,758 shares were issued as a result of exercise of outstanding warrants ("2003 Warrants") which confer rights to the holders to subscribe for approximately HK\$82 million in cash for shares at a subscription price of HK\$0.40 per shares. Together with another 272,584,224 shares issued by way of scrip dividend, aggregate 282,232,982 shares were issued during the year.

During the year, the remaining 2003 Warrants expired and share options over 16,100,000 shares at a subscription price of HK\$0.5552 per share lapsed and were cancelled.

As at the period end, there were 1,345,249,019 shares in issue. Save as disclosed above, there was no movement in the issued share capital during the period.

### FINAL DIVIDEND

The board of directors has resolved to recommend the payment of a final dividend of 1.5 cent per share for the year ended 31st March, 2004 (2003: 1.0 cent per share) to shareholders whose names appear on the Company's register of members as at the close of business on 6th October, 2004. The final dividend is expected to be paid to shareholders by post on or around 29th October, 2004.

The board of directors has also proposed that the final dividend should be satisfied by way of a scrip dividend of shares, with an option to elect cash in respect of part or all of such dividend. The market value of the shares to be issued under the scrip dividend proposal will be fixed by reference to the average of the closing prices of the Company's shares for the three consecutive trading days ending 6th October, 2004 less a discount of five per cent. of such average price or the par value of shares, whichever is the higher. The proposed scrip dividend is conditional upon the Hong Kong Stock Exchange granting listing of, and permission to deal in, the new shares to be issued and the passing at the forthcoming annual general meeting of the Company of an ordinary resolution to approve the final dividend. A circular giving full details of the scrip dividend proposal and a form of election will be sent to shareholders.

### PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

During the year ended 31st March, 2004, there were no purchases, sales or redemptions by the Company, or any of its subsidiaries, of the Company's listed securities.

### OUTLOOK

In the past 5 years, the Group successfully managed its way through the economic downturn in Hong Kong and came out with a more focused business strategy and much stronger balance sheet.

Paul Y. Construction Group has subdued the impact from a depressed Hong Kong market and is now on an uptrend. It is now

ready to pursue its growth strategy in China and the regional market under its own roof.

Paul Y. Property managed to divest its non-core properties and is now enjoying healthy recurring rental income from its only major asset, which being the Group's headquarters – Paul Y. Centre in Kwun Tong, Kowloon.

Downer will continue to be a significant contributor to the Group. The investments and business of China Strategic will provide long-term benefits in China.

Paul Y. Infrastructure, having a strategic focus in the transportation and energy sector, will not only capture the benefit from the sustained high growth economy in China, but also significantly enhance the overall value of the Group.

Barring unforeseeable circumstances, the Group is poised to meet the challenges ahead.

### APPRECIATION

On behalf of the board of directors, I would like to take this opportunity to express my appreciation to the shareholders for their support, to the management and staff for their dedicated efforts and to our client, consultants and partners for all their valuable assistance offered during this past year.

**Dr. Chan Kwok Keung, Charles**  
*Chairman*

Hong Kong, 23rd July, 2004