Chairman's Letter

RESULTS FOR 2005

Last year I was able to report that 2004 had exceeded all expectations and that the Group had achieved a record performance. I am immensely pleased therefore to report that 2005 has largely matched that performance at the Group level as well as at the individual levels of both our International Container Transport and Terminals businesses.

I suggested last year that the cyclicality in our industry had changed markedly. In the past we had felt that stability had been achieved were we to experience two consecutive half year periods of strong volume growth balanced against a reasonable tonnage supply growth to result in firm freight rates. 2004 had ended with an unprecedented fifth consecutive half year period of strong market conditions but with doubts that such a strong business environment could sustain itself through the coming year. In the event, it did and we have now enjoyed an unprecedented seventh consecutive half year period of strong container volume growth, firm freight rates and sustained margins. However, the pattern changed markedly last year. In 2004 the market continued to strengthen during the year with an unseasonal and exceptionally strong fourth quarter. This strength endured through into 2005 providing an extremely good start to the year but began to wane as the year progressed due to a slightly slower rate of volume growth compounded by the pick up in the rate of new tonnage being deployed.

The year of 2005 can be described as having been a struggle to contain increasing costs. With overall revenues per TEU generally unchanged, although slightly stronger, the task was to ensure that the bottom line benefit of higher volumes at least matched the impairment of higher overall costs. In this exercise we were largely successful and I am pleased therefore to be in a position to report that Orient Overseas (International) Limited and its subsidiaries (the "Group") recorded a profit before tax of US$690.1 million for the financial year ended 31st December 2005, just 0.9% below what was achieved inclusive of non-recurrent items the year before. A profit attributable to shareholders of US$650.9 million was recorded which represents a decrease of 2.9% from the attributable profit of US$670.4 million which we recorded in 2004. This remains another commendable achievement by the Group in the light of the higher cost environment faced, higher charterhire costs, the direct impact of higher bunker charges and the indirect effect of those higher fuel costs on both terminal and third party transportation costs, the latter also increasing as a result of stronger demand.

The Board of Directors recommends the payment of a final dividend of US15 cents (HK$1.17) per share to ordinary shareholders. Together with the interim dividend, this represents approximately the same payment as was made for last year after adjustment for the bonus issue announced in 2005. This maintains the dividend payment level at approximately 25% of profits attributable to shareholders.

The Group's operations remain unchanged and are organised into two distinct operating entities to provide each with the required independence and ability to concentrate upon their respective businesses.

Our Container Transport, Logistics and Terminals division enjoyed another exceptional trading environment during 2005. Container volume growth continued at above the long-term trend level and largely kept pace with the rate at which new tonnage was deployed. At the same time there was little if any increase in container terminal capacity in the areas in which the Group's terminals operate.

For Container Transport and Logistics, business confidence remained buoyant until the very end of the year and, as a result, total liftings increased by a further 7.8%. This increase compares with the unprecedented 21.6% by which total liftings increased in 2004. Total liftings in 2005 were, to a degree however, restrained by just an 8.8% increase in loadable capacity compared with an 18.2% increase during 2004. The overall load factor for 2005 remained unchanged from 2004.

The Group's terminal division operates four principal container terminals at major ports in North America, with two in British Columbia and one each in New York and New Jersey. I am pleased also to report that with the combined number of box lifts rising 12.4% from a year ago, total revenue from container operations at the four terminals grew by 21.4% and pre-tax earnings topped 2004 results by 52.0%. With many larger vessels being introduced into service and little growth in berth capacity throughout North America, the outlook for the terminal division remains quite positive.

The terminal division remains sensitive to the needs of the shipping lines which utilise its terminals and remains committed to providing the best possible service in order to allow its customers to meet tight sailing schedules. In addition to an ongoing program of upgrading and replacing existing equipment, the terminal division has embarked upon plans and undertaken studies related to an increase in berth and throughput capacity at several of its facilities before the end of the decade. In addition, the Group began to investigate the potential for new investments into terminal facilities in China.

As in prior years, OOIL has continued to put resources into strengthening the technology infrastructure of the Group with an ultimate aim to provide reliable and efficient services to customers. In 2005, our focus on information technology developments was placed in three different directions. For carriers, further enhancements have been made to IRIS-2, OOCL's central carrier information system, to improve its functionality as a pioneer carrier system. For Logistics Services Providers, we have developed tailor-made logistics solutions relating to inventory management and reefer cargo handling. Lastly, for importers/exporters and carriers, we have introduced greater functionality to our award winning Internet portal, Cargo*Smart*, to further enhance its capacity as a multiple-carrier portal for customers.

OOCL Logistics for the full year of 2005 was in operation under its new organisation structure. We were pleased with the progress of each of the three newly created business units, namely, International Logistics, China Logistics and E-Business.

Our International Logistics business, in addition to our traditional markets of Asia to North America and Asia to Europe, entered the Asia to Australia and Intra-Asia markets with encouraging results. Internally, we have been enhancing our overall capabilities in serving our customers by improving our organisational and people structures as well as various system capabilities.

The China Logistics group adopted a warehouse-centric logistics network business model and established warehouse operations in many cities in China. We also acquired a piece of land in Tianjin of around 25,000 sq m inside the Logistics Park on which we shall construct our own warehouse. We shall continue this expansion of our capabilities during 2006.

The E-Business team made the first logistics system solution sale of our Reefer Podium product in 2005. We shall continue to leverage OOCL Group's IT capability to offer a greater and wider choice to our customers. Also, by adopting a decentralised and empowered management philosophy, we have witnessed a wealth of regional initiatives in providing a wide range of and variety of services to customers. Our emphasis will remain focused upon enabling our customers to retain ultimate control and flexibility of their supply chains.

Our Property Development and Investment division was successful in the acquisition of new projects during the 2005. In particular, we successfully tendered for two parcels of land in Central Shanghai. We believe that both these sites, given their location and expected cost structures, will produce good returns for the Group upon their completion. In total, our project pipeline has reached approximately one million sq m of gross floor area in Shanghai and Jiangsu Province. Going forwards, we shall continue to seek property investment and development opportunities in China.

Our Property Development business, whilst remaining thus far only a modest contributor to Group profits, nevertheless produced satisfactory results in 2005. However, due to the timing of previous land acquisitions and our considered views of the market, property development income will slow dramatically during the coming two years of 2006 and 2007. Our Property Investment business produced a result for 2005 in line with expectations. We continue to hold an 8% interest in Beijing Oriental Plaza. As at 31st December 2005, Wall Street Plaza was valued at US$100 million. The property enjoyed an occupancy rate of 99% for the better part of the year. We expect both investments to contribute to Group profitability going forwards.

Given our real estate experience in China over the last decade, and our land acquisitions conducted over the past few years, we expect real estate to produce a meaningful contribution in the future, and we continue to work towards the creation of a stand alone real estate development and investment business in China.

The overall Group result for the year of 2005 compares satisfactorily with that of 2004 especially when the much higher costs are taken into account. The result is also reflective of a much stronger market than was being predicted earlier in the year. As at the beginning of last year, the then predictions for the coming year were for a much softer market as container volume growth was forecast to slow against a known to be increasing rate of new tonnage deployment. As always, those forecasts for demand side container volume growth proved in the event to be under-estimates. Conversely, supply side tonnage growth forecasts always prove to be an over-estimate of the true increase in effective loadable capacity. Nevertheless, sentiment tends always to prevail and current sentiment suggests strongly that the deployment of new tonnage during 2006 will outpace the rate at which container volumes will grow, the extent of this imbalance being variously forecast at between 3% and 5%. As a result, the freight rate forecasts are for a softer market and, on some trade routes, we have already seen this begin to happen. However, much remains uncertain. Consumer confidence and retail sales demand remain fairly buoyant throughout the major consumer economies. To take the Trans-Pacific eastbound trade as an example, the single most important trade in revenue terms, the third and fourth quarters of 2005 saw volumes grow 15.7% and 14.2% respectively over the exceptional corresponding periods of 2004. This strength has carried over into 2006 although with the vagaries of the timing of Chinese New Year it is not possible, at the time of writing, to compare month by month statistics. Even for the Asia-Europe trade routes, for which the forecasts are most pessimistic, overall conference volumes grew by 11.6% and 11.8% year-on-year during the third and fourth quarters of 2005 respectively and again, this rate of volume growth has carried over into 2006.

As we enter this period of supply side growth outpacing the demand side, industrial load factors may or indeed will fall below the exceptional percentages, in the high nineties, experienced on the head haul legs during the past two years or so, but we believe that they will not fall to the dire levels of some five years ago. For the good of the industry as a whole, we are hopeful that carriers will accept and operate under these slightly lower load factors, temporary as they will be whilst we endure this bulge in the newbuilding delivery schedule, rather than lower rates in what in the event will turn out to be the vain attempt to regain the exceptional load factors of the recent past. The consolidation which has taken place within the industry should assist in producing this readier acceptance of load factor decline and therefore a greater resistance to freight rate erosion.

Overall performance, of course, will remain dependent not only upon volumes and freight rates but also upon relative cost levels. Oil prices are critical not only due to their direct effect on bunker prices but also due to their indirect effect of driving up terminal and third party transportation costs. Some of these cost increases are recoverable but many if not most are not. In 2004 our average bunker cost was US$174 per ton. For 2005 it had risen to US$250 per ton and we purchased just under 1.7 million tons during the year!

2005 has produced another commendable result for the Group and I again, must pay tribute to the staff who have made this possible. OOIL now has a full-time staff on land and at sea of just over 6,000 people. They remain committed as much as the Group remains committed to its "People", one of its Core Values, and to "People Development" throughout the whole organisation. This is and will remain a cornerstone of corporate policy. It is this consistency in the investment in people, as well as in IT and the quality processes, which has established a strong cost structure and culture that supports and enhances our performance through the various business cycles. This is further enhanced by the concentration on customer service and the continued drive to "Simplify, Standardise and Automate".

The quality of our services and products has always been our focus and now, with our positioning as a knowledge based organisation as we continue our IT investment programmes, we place an even greater emphasis on the development of our people. We aim to provide an environment in which they may extend their personal horizons and realise their full potential in partnership with the Company as a whole. Their contributions to the communities in which they work are described elsewhere in this report and I commend them wholeheartedly for the efforts which they put into this responsibility.

C C Tung
Chairman
Hong Kong, 10th March 2006

  

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.


OOCL








OOCL
Logistics