Financial Review

Profit attributable to shareholders of the Company for 2007 was RMB2,462 million, an increase of 115% over 2006 (2006: RMB1,146 million)

Turnover decreased by 3% to RMB4,570 million (2006: RMB4,729 million) primarily due to management's decision to sell Shanghai Taipingqiao, Lot 113 (Lakeville 3) in planned phases over 2008 and 2009, thereby building on our continued success in Shanghai Taipingqiao.

Property sales for the year amounted to RMB4,085 million (2006: RMB4,283 million) and was generated from the sales of residential GFA aggregating approximately 138,000 sq.m. (2006: 123,000 sq.m.). Shanghai Taipingqiao, Lot 114 (Lakeville Regency) continued to be the key contributor to both turnover and gross profit for 2007.

Rental income increased by 12% to RMB401 million (2006: RMB358 million) as a result of increases in the average rental rates in Shanghai Xintiandi and Shanghai Corporate Avenue and increased occupancy rates for investment properties that were completed in 2006 and 2007, namely at Shanghai Knowledge and Innovation Community (KIC Plaza Phase 1 and KIC Village, R1) and at Wuhan Tiandi.

Gross profit was RMB2,685 million (2006: RMB3,140 million) and the gross margin was 59% (2006: 66%). The decrease in the gross margin occurred mainly on property sales and was due to lower sales in 2007 than in 2006 from Shanghai Taipingqiao, Lot 114 (Lakeville Regency) which generated higher gross profit margins. The lower margin from the sales of residential units in Wuhan and in Shanghai Knowledge and

Shanghai KIC Plaza

Innovation Community (KIC Village, R1) also accounted for the reduced overall gross margin in 2007.

Other income increased by 51% to RMB269 million (2006: RMB178 million) primarily due to higher interest income from deposits of subscription monies received from the Company's initial public offering in October 2006 coupled with the generally higher interest rates in 2007 than in 2006.

Selling and marketing expenses decreased by 24% to RMB114 million (2006: RMB150 million) due mainly to higher expenses incurred in 2006 in promoting the sales and leasing KIC Plaza Phase 1 and KIC Village R1 of our Shanghai Knowledge and Innovation Community and Phase 2 of our Shanghai Rui Hong Xin Cheng development projects than those incurred in 2007. The decline was however partially offset by expenses incurred in the promotion of the maiden launch of our Wuhan Tiandi development project, Lot A9 (The Riverview) in 2007.

In 2007, the *general and administrative expenses* increased by 62% to RMB543 million (2006: RMB335 million) on account of higher employee benefits expenses and higher level of professional and consulting fees. The increase in employee benefits expenses included share compensation costs of RMB36 million (2006: nil) in respect of share options granted to staff in 2007, the effect of an increase in the number of average headcount to 1,031 in 2007 (2006: 929) and general salary increments in 2007 over 2006.

The higher level of professional and consulting fees was incidental to our Group's business expansion in 2007.

Other expenses decreased to RMB13 million (2006: RMB658 million) due mainly to reduced losses on change in fair value of derivative financial instruments. In 2006, we incurred losses on changes in the fair value of our warrants and on the conversion options of our preference shares amounting to RMB500 million. All warrants exercisable for shares of the Company were exercised and all preference shares were also mandatorily converted into shares of the Company at the same time upon the Company's successful initial public offering in October 2006. In addition, non-recurring professional fees totaling RMB152 million were incurred in 2006 for obtaining our listing on the Hong Kong Stock Exchange.

Operating profit increased by 5% to RMB2,284 million (2006: RMB2,175 million). The increase was due mainly to the various items referred to above.

Increase in fair value of investment properties has given rise to a gain of RMB577 million in 2007 (2006: RMB145 million).

Gains on partial disposal of equity interests in subsidiaries and gain on acquisition of additional equity interest in a subsidiary are all contained in the paragraph headed "Accelerating Growth through Strategic Partnerships" in the Business Review Section referred to above.

Finance costs amounted to RMB125 million (2006: RMB118 million) and comprised mainly interest costs of RMB458 million less amount capitalised to properties under development of RMB358 million (2006: RMB854 million less capitalisation to properties under development of RMB643 million). The lower level of total finance costs was due mainly to the conversion of all the preference shares into shares of the Company at the time of the initial public offering in October 2006. Prior to that preference share dividends had been treated as interest costs.

Profit before taxation increased by 32% to RMB3,687 million (2006: RMB2,785 million). The increase was due mainly to the various items referred to above.

Taxation was RMB820 million (effective tax rate: 22%) in 2007 as compared to RMB1,145 million (effective tax rate: 41%) in 2006. The significant reduction in effective tax rate was largely attributable to a non-recurring deferred tax credit adjustment of RMB343 million booked in 2007. As a result of the enactment in March 2007 of the new Corporate Income Tax Law of the PRC, enterprises are subjected to a uniform income tax rate of 25% with effect from 1 January 2008. To reflect this anticipated change in the tax rate from 33% to 25%, the carrying value of deferred tax liabilities was written down by RMB343 million and credited to the income statement in 2007. Excluding the effect of this non-recurring deferred tax credit adjustment, the effective tax rate in 2007 was 32%, which is a decrease when compared to 2006 partly due to certain non-recurring expenses not being deductible for tax purposes such as certain of the professional fees for obtaining our listing on the Hong Kong Stock Exchange incurred in 2006 but not in 2007.

Profit attributable to shareholders of the Company for 2007 was RMB2,462 million, an increase of 115% over 2006 (2006: RMB1,146 million). The effects on profit attributable to shareholders of the change in fair value of the Group's investment properties, net of related tax effect, and fair value change of derivative financial instruments are as follows:

	2007 RMB' million	2006 RMB' million	% Change
Profit attributable to shareholders of the Company after (i) revaluation of investment properties; and (ii) fair value adjustment on derivative financial instruments	**2,462**	1,146	+115%
Revaluation increase on investment properties (net of deferred tax effect and share of minority interest)	**(419)**	(87)	
Loss on change in fair value of derivative financial instruments	**–**	500	
Fair value loss/(gain) on early redemption rights on notes	**17**	(23)	
Profit attributable to shareholders of the Company before (i) revaluation of investment properties; and (ii) fair value adjustment on derivative financial instruments	**2,060**	1,536	+34%

Earnings per share were RMB59 cents or HK61 cents calculated based on a weighted average of approximately 4,185 million shares in issue during the year (2006: RMB48 cents or HK47 cents based on 2,405 million shares in issue).

Capital Structure, Gearing Ratio and Funding

As of 31 December 2007, the Group's utilised project loans, mortgage loans and senior notes amounted to approximately RMB7,072 million (31 December 2006: RMB6,477 million) and our total equity was RMB16,706 million (31 December 2006: RMB15,165 million).

The structure of our borrowings as of 31 December 2007 is summarised below:

	Currency denomination	Total (in RMB equiv) RMB' million	Due within one year RMB' million	Due more than one year but not exceeding two years RMB' million	Due more than two year but not exceeding five years RMB' million	Due more than five year RMB' million
Bank Loans	RMB	1,235	742	103	234	156
	HKD	3,170	772	483	1,915	–
Notes	USD	2,667	2,667	–	–	–
Total		**7,072**	**4,181**	**586**	**2,149**	**156**

Our cash and bank deposits amounted to RMB3,697 million as of 31 December 2007 (31 December 2006: RMB5,654 million), which included RMB854 million (31 December 2006: RMB1,202 million) of deposits pledged to banks. The decrease in our cash balance was due mainly to payments of land costs for Dalian Tiandi • Software Hub and Foshan Tiandi projects, partially offset by proceeds from property sales and from transfers of equity interests to strategic partners.

The Group's net gearing ratio was approximately 20% as of 31 December 2007 (31 December 2006: 5%), calculated on the basis of dividing the excess of the sum of bank loans and notes payable over the sum of bank balances and cash by total equity.

The Group's rental income for 2007 expressed as a percentage of the Group's total interest costs before capitalization to property under development was approximately 88% (2006: approximately 42%).

Total undrawn banking facilities available to the Group were approximately RMB1,718 million as of 31 December 2007 (31 December 2006: RMB2,560 million). Subsequent to 31 December 2007, additional banking facilities of approximately RMB2,616 million have been arranged. We will continue to adopt a prudent financial policy so as to sustain an optimal level of borrowings to meet our funding requirements.

Pledged Assets

As of 31 December 2007, the Group had pledged land use rights, completed properties for investment and sale, properties under development and bank and cash balances totaling approximately RMB11,663 million to secure our borrowings of RMB3,843 million, or 54% of our total borrowings.

Capital and Other Development Related Commitments

As of 31 December 2007, the Group had contracted commitments for capital expenditure in the amount of RMB5,065 million.

The Group has also committed to building certain educational facilities to be located in the Taipingqiao area of the Luwan District as compensation for the removal of those educational facilities originally located in the area. As of 31 December 2007, the Group had not entered into any construction contracts relating to such education facilities.

In addition, the Group entered into a Confirmation Agreement with the Land Exchange Centre confirming the Group's successful bid for a plot of land in Foshan. Under this Confirmation Agreement, a total consideration for acquiring the land use rights of the land is RMB7,510 million, against which a deposit of RMB1,200 million has been paid to the Land Exchange Centre as of 31 December 2007 and a further installment of RMB1,053 million has been paid in January 2008; the remaining balance of RMB5,257 million will be paid in stages in line with the relocation progress of the land that is expected to be completed by or around 2010.

Future Plans for Material Investments and Sources of Funding

We intend to continue growing organically by pursuing more property development projects through competitive bids or auctioning to diversify the geographical span of our projects to selected regions in new cities.

We actively screen cities in different regions of the Chinese Mainland to identify suitable locations for our projects and are continually exploring new opportunities.

We may also pursue other plans, including other ways of acquiring land development rights for the purpose of undertaking property projects, or other ways to increase the scale of our operations by leveraging on our master planning expertise, if we feel the right opportunity presents itself.

While our primary focus is on city-core development projects and integrated residential development projects, we will, in appropriate cases, consider other opportunities to participate in projects of various scale where we can leverage our competitive strengths. Our track record, good relationships with business partners and well established reputation may give rise to such other opportunities.

Material investments will be funded, in the main, by using a combination of project construction loans, mortgage and other loans, and cash provided by operating activities, including from the rental, sales and pre-sales of properties, and proceeds from sale of equity interests in our projects to strategic partners, as appropriate.

Cashflow Management and Liquidity Risk

Cashflow of all subsidiaries is managed on a centralised basis so as to enhance cost-efficient funding.

Our objective is to maintain a balance between continuity of funding and flexibility through a combination of internal resources, and bank and other borrowings, where appropriate. We will continue to maintain a reasonable liquidity buffer to ensure sufficient funds are available to meet liquidity requirements at all times. The repayment profile of liabilities is closely monitored and sources of payment are planned in advance.

Interest Rate and Exchange Rate Risks

The Group's exposure to cash flow interest rate risk resulted from fluctuation in interest rates. All of the bank borrowings of the Group consist of variable rate debt obligations with original maturities ranging from two to four years for the project construction loans; and five to ten years for the mortgage loans. Increase in interest rates would increase interest expenses relating to the outstanding variable rate borrowings and increase the cost of new debt. Fluctuations in interest rates can also lead to significant fluctuations in the fair value of the debt obligations. The Group has been following a policy of developing long term banking facilities to match our long-term investment plans. This will enable us to avoid high borrowing costs from short term financing for long-term investment. Our policy on interest rate risk management also involves close monitoring of interest rate movements and to replace and enter into new banking facilities when good pricing opportunities arise. Interest rate swaps to hedge exposure to floating rates are used where appropriate.

All of the turnover of the Group is denominated in Renminbi. A portion of the turnover in Renminbi, however, is converted into other currencies to meet the foreign currency denominated debt obligations, such as the bank loans denominated in Hong Kong dollars and the senior note denominated in US dollars. As a result, the Group is exposed to fluctuations in foreign exchange rates.

Considering (i) a relatively stable currency regime with regard to the Renminbi is maintained by the PRC government which only allows the exchange rate to fluctuate within a narrow range; and (ii) it is the Group's view that it is more probable that the value of the Renminbi will appreciate than depreciate relative to the Hong Kong dollar/US dollar in the foreseeable future, the Group expects that any adverse effect of fluctuation of the exchange rate between Renminbi, Hong Kong dollar and US dollar is insignificant. The Group is monitoring the situation closely and will implement an effective hedging arrangement whenever it considers there is any sign that the currently benign environment will change in the future.


88 Xintiandi in Shanghai