FINANCIAL REVIEW

Overall analysis of results

Profit attributable to equity holders of the Group for the year 2011 was US$388,771,000 (2010: US$361,307,000), a 7.6% increase compared with last year. Excluding the non-recurring items, profit attributable to equity holders in 2011 was US$364,373,000 (2010: US$269,577,000), a 35.2% increase compared with last year. Non-recurring items include gain of US$11,841,000 on release of exchange reserve upon reclassification of Guangzhou South China Oceangate Terminal from a jointly controlled entity to a subsidiary in 2011, profit of US$12,557,000 on the disposal of Qingdao Cosport Terminal in 2011, profit of US$84,710,000 on the disposal of COSCO Logistics in 2010 and profit of US$7,020,000 on the disposal of Dalian Port Container in 2010.

Taking into account the non-recurring items of the profit of US$12,557,000 on the disposal of Qingdao Cosport Terminal in 2011 and the profit of US$7,020,000 on the disposal of Dalian Port Container Terminal Co. Ltd. in 2010, profit from the terminal business in 2011 was US$184,890,000 (2010: US$119,882,000), a significant increase of 54.2% compared with last year. Excluding these two non-recurring items, profit from the terminal business in 2011 was US$172,333,000 (2010: US$112,862,000), representing an increase of 52.7% compared with last year. In 2011, the throughput of container terminals reached 50,695,897 TEUs (2010: 44,041,723 TEUs), a 15.1% increase compared with last year. The completion of the Group's acquisition of an approximately 10% additional equity interest in Yantian Terminal in June 2010 further intensified the growth in the profit from COSCO Pacific's terminal business. In addition, Piraeus Terminal in Greece and Guangzhou South China Oceangate Terminal, which returned to profitability in September 2010 and the first half of 2011 respectively, showed strong performance during the year, boosting the overall profit from terminal business.

With regard to the container leasing, management and sale businesses, a profit of US$116,508,000 was recorded in 2011 (2010: US$96,366,000), a 20.9% increase compared with last year. As at 31st December 2011, the container fleet size increased to 1,777,792 TEUs (31st December 2010: 1,631,783 TEUs), an 8.9% increase compared with last year.

For CIMC, after the rapid growth in sales of dry cargo containers and persistently high container prices in the first half of 2011, demand for containers slowed down in the second half of the year. COSCO Pacific's profit attributable from CIMC was US$119,799,000 (2010: US$91,871,000) in 2011, representing a 30.4% increase compared with last year.

Financial analysis

Revenue

Revenue of the Group in 2011 was US$599,159,000 (2010: US$446,492,000), a 34.2% increase compared with last year. The revenue was primarily derived from the terminal business, amounting to US$323,339,000 (2010: US$195,594,000), and the container leasing, management and sale businesses, amounting to US$276,547,000 (2010: US$250,898,000). In 2011, total revenue from the terminal business rose significantly by 65.3% compared with last year, which was mainly attributable to the reclassification of Guangzhou South China Oceangate Terminal from a jointly controlled entity to a subsidiary since 1st January 2011, resulting in an increase in total terminal revenue in 2011. Throughput of Guangzhou South China Oceangate Terminal was 3,914,348 TEUs, recording a revenue of US$94,889,000 for the year. In addition, throughput of Piraeus Terminal in Greece rose to 1,188,148 TEUs (2010: 684,881 TEUs) in 2011, contributing revenue of US$101,420,000 (2010: US$83,303,000) to the Group during the year.

Revenue from the container leasing, management and sale businesses primarily included container leasing income and revenue from the disposal of returned containers. As at 31st December 2011, the fleet capacity of owned containers and sale-and-leaseback containers reached 874,160 TEUs and 229,283 TEUs respectively (31st December 2010: 813,625 TEUs and 118,094 TEUs respectively). Revenue from container leasing for the year was US$246,782,000 (2010: US$207,245,000), a 19.1% increase from last year. The number of returned containers disposed of during 2011 was 9,826 TEUs (2010: 28,674 TEUs), and the revenue from the sale of returned containers was US$18,245,000 (2010: US$33,895,000).

Cost of sales

Cost of sales mainly comprised depreciation charges on owned containers, net carrying amount of returned containers disposed of, container rental expenses and operating expenses of the terminal companies with controlling stakes. Cost of sales in 2011 was US$340,141,000 (2010: US$279,768,000), an increase of 21.6% compared with last year. The increase was mainly attributable to the consolidation of the cost of sales incurred by Guangzhou South China Oceangate Terminal starting from 1st January 2011. For container leasing, depreciation charges for containers were US$87,191,000 (2010: US$84,665,000) for the year. In addition, the drop in the number of returned containers sold reduced the net carrying amount of disposed returned containers to US$10,232,000 (2010: US$25,347,000).

Investment income

Investment income, comprising mainly dividend income, was US$1,992,000 (2010: US$1,612,000). The amount was primarily a dividend of US$1,628,000 declared by Tianjin Five Continents Terminal in 2011 (2010: US$1,485,000).

Administrative expenses

Administrative expenses in the year were US$89,323,000 (2010: US$59,823,000), an increase of 49.3% compared with last year. The increase was mainly attributable to the consolidation of administrative expenses incurred by Guangzhou South China Oceangate Terminal during the year and an increase in the initial costs of Xiamen Ocean Gate Terminal which is expected to commence operation in the second quarter of 2012. These caused an increase in the overall administrative expenses in 2011.

Other operating income, net

Net other operating income in 2011 was US$7,713,000 (2010: US$4,754,000), which included a net exchange gain of US$4,305,000 (2010: a net exchange loss of US$2,999,000) for the year. In addition, the subsidiaries received government subsidies in an aggregate of US$3,773,000 in 2011. On the other hand, a profit of US$7,020,000 generated from the disposal of Dalian Port Container was included in 2010. No such profit was recorded in 2011.

Finance costs

The Group's finance costs in 2011 were US$58,419,000 (2010: US$29,439,000). Finance costs included interest expenses and the amortisation of transaction costs over bank loans and notes. The increase in finance costs was primarily due to the consolidation of finance costs of Guangzhou South China Oceangate Terminal during the year. Upon the consolidation of the bank loans of Guangzhou South China Oceangate Terminal, the average balance of bank loans was US$2,076,681,000 (2010: US$1,579,766,000), a 31.5% increase compared with last year. In addition, the upward adjustment of the benchmark interest rate for RMB loans in the PRC led to increased finance costs for the year. Excluding the interest expenses on loans from a jointly controlled entity and non-controlling shareholders of subsidiaries, the average cost of borrowing in 2011, including the amortisation of transaction costs over bank loans and notes, was 2.66% (i.e. an average 6-month LIBOR of approximately 0.52% plus 214 basis points), while that for last year was 1.86% (i.e. an average 6-month LIBOR of approximately 0.51% plus 135 basis points).

Share of profits less losses of jointly controlled entities and associates

The net profit contribution from jointly controlled entities in 2011 amounted to US$96,638,000, representing a 29.4% increase compared with US$74,654,000 last year. The increase was mainly attributable to Qingdao Qianwan Terminal and the reclassification of Guangzhou South China Oceangate Terminal to a subsidiary. The throughput of Qingdao Qianwan Terminal increased to 12,426,090 TEUs (2010: 10,568,065 TEUs) in 2011, a 17.6% increase compared with last year. During the year, a share of profit from Qingdao Qianwan Terminal amounting to US$35,513,000 (2010: US$25,563,000) was recorded, representing a 38.9% increase. In addition, Guangzhou South China Oceangate Terminal was previously a jointly controlled entity of COSCO Pacific. Starting from 1st January 2011, COSCO Pacific has accounted for Guangzhou South China Oceangate Terminal as a subsidiary and consolidated to COSCO Pacific's financial statements. Accordingly, in 2011, the profit of Guangzhou South China Oceangate Terminal was not stated as share of a jointly controlled entity, while Guangzhou South China Oceangate Terminal stated as share of a jointly controlled entity recorded a loss of US$5,088,000 last year.

During the year, the share of net profit from associates increased significantly to US$179,290,000, representing a 35.7% increase compared with US$132,120,000 last year. The increase was primarily contributed by CIMC and the acquisition of a further interest in Yantian Terminal in 2010. After the completion of the acquisition of a further interest in Yantian Terminal in June 2010, the Group's investment in Yantian Terminal was reclassified from an available-for-sale financial asset to an associate and is accounted for using the equity method. The share of full-year profit from Yantian Terminal to the Group was US$51,011,000 (2010: US$30,216,000) in 2011, representing an increase of 68.8% compared with last year. With regard to the container manufacturing business, the sale of dry containers grew rapidly and the price was maintained at a high level in the first half of 2011. However, the demand for containers dropped in the second half of the year as the Eurozone sovereign debt crisis intensified and the shipping market was turning weak. CIMC's profit contribution to the Group was US$119,799,000 (2010: US$91,871,000) in 2011, a 30.4% increase compared with last year.

Gain on release of exchange reserve upon reclassification from a jointly controlled entity to a subsidiary

Guangzhou South China Oceangate Terminal was previously a jointly controlled entity of the Group. By virtue of the clause in an agreement entered into by the Group and the other shareholder of CP Nansha, the joint control of Guangzhou South China Oceangate Terminal expired on 31st December 2010 and COSCO Pacific has the power to govern the operating and financial policies of Guangzhou South China Oceangate Terminal. Accordingly, the Group has accounted for Guangzhou South China Oceangate Terminal as a subsidiary from 1st January 2011. During the year, a gain of US$11,841,000 on release of exchange reserve was recorded upon reclassification from a jointly controlled entity to a subsidiary.

Profit on disposal of a jointly controlled entity, net of tax

To optimise the Group's terminal business structure, on 10th March 2011, the Group entered into an agreement with Qingdao Port Group, the remaining shareholder of Qingdao Cosport Terminal, to dispose of its 50% equity interest in Qingdao Cosport Terminal at a consideration of RMB184,000,000 (equivalent to approximately US$28,000,000). The disposal was completed on 28th April 2011, generating a profit after tax of US$12,557,000.

Income tax expenses

During the year, income tax expenses amounted to US$28,771,000 (2010: US$15,653,000). This included a provision of approximately US$20,808,000 (2010: US$12,900,000) for withholding income tax in respect of the profit distribution by certain investments of the Group in the PRC.

Profit from discontinued operations

Profit from discontinued operations in 2010 represented the profit generated from the disposal of COSCO Logistics. In March 2010, the Group completed the disposal of COSCO Logistics which resulted in a profit (net of direct expenses and tax) of US$84,710,000. No such profit was recorded in 2011.

Financial position

Cash flow

Cash inflow of the Group remained steady in 2011. During the year, net cash from operating activities amounted to US$331,933,000 (2010: US$255,702,000). The Group borrowed bank loans of US$605,318,000 (2010: US$202,401,000) and repaid US$536,866,000 (2010: US$265,153,000) in 2011.

The Group's cash outflow for the purchase of property, plant and equipment in 2011 amounted to US$666,969,000 (2010: US$375,342,000). The cash was used for the expansion of berths and the purchase of property, plant and equipment, of which US$458,282,000 (2010: US$239,607,000) was for the acquisition of containers. In addition, in 2011, the total cash outflow for capital investments by the Group amounted to US$4,689,000, mainly comprising an investment balance of US$3,974,000 in Jinjiang Pacific Terminal and an investment cost of US$712,000 invested in Piraeus Consolidation and Distribution Centre S.A. The total cash outflow for capital investments and shareholders' loans of the Group in 2010 amounted to US$570,871,000, mainly comprising US$520,000,000 used for the acquisition of an approximately 10% equity interest in Yantian Terminal, US$27,996,000 used for reinvestment of dividends from Yantian Terminal, US$9,052,000 used for capital injection in Nanjing Longtan Terminal, US$7,030,000 used for capital injection in Dalian Automobile Terminal and US$3,352,000 used for providing a shareholder's loan to Antwerp Gateway.

Financing and credit facilities

Upon the consolidation of Guangzhou South China Oceangate Terminal, the total bank loans of COSCO Pacific increased to US$2,167,994,000 (31st December 2010: US$1,558,755,000) as at 31st December 2011, with a cash balance of US$581,069,000 (31st December 2010: US$524,274,000). Banking facilities available but unused amounted to US$1,041,658,000 (31st December 2010: US$1,099,127,000).

Assets and liabilities

As of 31st December 2011, the Group's total assets and total liabilities increased to US$6,472,184,000 (31st December 2010: US$5,251,917,000) and US$2,592,025,000 (31st December 2010: US$1,758,055,000) respectively as a result of the consolidation of Guangzhou South China Oceangate Terminal into COSCO Pacific during the year. Net assets were US$3,880,159,000, an increase of 11.1% as compared with US$3,493,862,000 as at the end of 2010. Net current assets as at 31st December 2011 amounted to US$50,698,000 (31st December 2010: US$439,366,000). As at 31st December 2011, the net asset value per share of the Company was US$1.43 (31st December 2010: US$1.29), representing an increase of 10.9% compared with last year.

As at 31st December 2011, the net debt-to-total equity ratio was 40.9% (31st December 2010: 29.6%), and the interest coverage was 8.3 times (2010: 11.1 times, excluding profit on disposal of logistics business). As at 31st December 2011, certain of the Group's property, plant and equipment with an aggregate net book value of US$19,277,000 (31st December 2010: US$20,896,000) were pledged as securities against bank borrowings of US$130,682,000 (31st December 2010: US$64,180,000).

Debt analysis

	As at 31st December 2011		As at 31st December 2010	
	US$	(%)	US$	(%)
By repayment term				
Within the first year	**594,524,000**	**27.4**	169,109,000	10.8
Within the second year	**732,863,000**	**33.8**	297,490,000	19.1
Within the third year	**328,158,000**	**15.1**	668,458,000	42.9
Within the fourth year	**48,307,000**	**2.2**	173,001,000	11.1
Within the fifth year and after	**464,142,000**	**21.5**	250,697,000	16.1
	2,167,994,000*	**100.0**	1,558,755,000*	100.0
By category				
Secured borrowings	**130,682,000**	**6.0**	64,180,000	4.1
Unsecured borrowings	**2,037,312,000**	**94.0**	1,494,575,000	95.9
	2,167,994,000*	**100.0**	1,558,755,000*	100.0
By denominated currency				
US dollar borrowings	**1,175,832,000**	**54.3**	1,165,404,000	74.8
RMB borrowings	**861,480,000**	**39.7**	329,171,000	21.1
Euro borrowings	**130,682,000**	**6.0**	64,180,000	4.1
	2,167,994,000*	**100.0**	1,558,755,000*	100.0

* Net of unamortised discount on notes and transaction costs on borrowings and notes.

Financial guarantee contracts

As at 31st December 2011, the Group provided guarantees on a loan facility granted to an associate of US$27,513,000 (31st December 2010: US$29,505,000).

Contingent liabilities

A statement of claim was issued on 19th October 2009 by ADK against the Company and Piraeus Terminal, a wholly owned subsidiary of the Company, in a civil claim at the Court of First Instance of Athens in Greece, alleging non-payment of fees for design services and project management services. The plaintiff has claimed approximately Euro 5,800,000 (equivalent to approximately US$7,500,000) in total. The Company and Piraeus Terminal defended all material claims at the trial hearing held on 30th November 2010.

The Court of First Instance of Athens has issued (pronounced) judgment on the case and has dismissed the aforementioned statement of claim in its entirety both as regards the Company and as regards Piraeus Terminal, and has awarded to the Company and Piraeus Terminal part of the legal expenses in the amount of Euro 30,000 (equivalent to approximately US$39,000) against the plaintiff (ADK). The plaintiff has filed an appeal against the judgment of the Court of First Instance of Athens before the Court of Appeals of Athens according to Greek procedural law. The hearing of this appeal has been set to take place before the Court of Appeals of Athens on 13th November 2012. The directors and management of the Company, having taken legal advice, are of the view that the Company and Piraeus Terminal have good rebuttal to the arguments set forth in the appeal document. Nonetheless, it is still not possible to predict the final outcome of this litigation with certainty. No provision has been made for the claims.

Treasury policy

The Group manages its foreign exchange risk by matching the currencies of its loans with the Group's functional currency of major cash receipts and underlying assets as far as possible. Borrowings for container leasing business are mainly denominated in US dollars, which is the same currency as the majority of its revenue and expenses so as to minimise potential foreign exchange exposure.

The financing activities of jointly controlled entities and associates were denominated in their respective functional currencies so as to minimise foreign exchange exposure in investments.

The Group continues to exercise stringent control over the use of financial derivatives to hedge against its interest rates exposure. As at 31st December 2011, outstanding interest rate swap contracts comprised nominal principal amounting to US$200,000,000 (31st December 2010: US$200,000,000) in total, whereby the Group agreed to pay the banks interest at floating rates ranging from 105 basis points to 116 basis points (31st December 2010: 105 basis points to 116 basis points) above 6-month LIBOR in return for receiving interest from the banks at a fixed interest rate of 5.875% per annum (31st December 2010: 5.875%).

As at 31st December 2011, after adjustment of the fixed rate borrowings for the interest rate swap contracts, 4.6% (31st December 2010: 6.4%) of the Group's borrowings were fixed rate bank loans. The Group continues to monitor and regulate its fixed and floating rate debt portfolio from time to time in light of the market conditions, with a view to minimising its potential interest rate exposure.