

MANAGEMENT DISCUSSION AND ANALYSIS

BUSINESS REVIEW

Primary and Secondary Residential Markets in Guangzhou Continued to Improve

In spite of termination of state owned enterprises purchase in 2000, total sales volume of the Guangzhou primary residential market was maintained at 53.262 million sq. feet and was down only slightly by 8.8 per cent year on year. Average selling price remained steady at approximately Rmb454.09 per sq. feet which was up by 3.4 per cent year on year, and reversed the gradual downtrend of the last few years. Transaction volume in the secondary market was also up substantially by 98.4 per cent to 13.45 million sq. feet.

These figures indicated that the primary and secondary residential markets in Guangzhou remained active underpinned by improving affordability. Housing prices have remained steady over the past few years while personal income has been growing. With continuous implementation of a series of policy reforms including termination of state owned enterprises purchase, the reduction of property income tax, a low level of interest rate, and expansion of mortgage financing from primary to secondary markets, increasing number of consumers are attracted to become home owners.

Sales of Residential Properties in Guangzhou Expanded

The Guangzhou residential market remained competitive in 2000 and the Group has stepped up efforts in marketing which include project positioning, advertising and promotional activities. For example, Greenland Garden (formerly known as Zhuang Tou) is a mass market project with only basic finishing but affordable sale price. Galaxy City (formerly known as Zhu Jiang Estate Zone E2) is a high end project with intelligent management system and 24 hours distilled water supply. The gardening of green area of these projects were speeded up to promote sales. Based on such efforts, responses to both Greenland Garden and Galaxy City have been positive. Coupled with the continuous sales of Nan Hin Court of Jiang Nan Estate and Jin Hui Residential Building located at Haizhu and Tianhe Districts respectively, total sales area of major projects in 2000 was 686,348.66 sq. feet, which was up by about 41.9 per cent compared with 1999.

Major projects offered in 2000	Sales area (sq. feet)
Nan Hin Court of Jiang Nan Estate	83,009.31
Jin Hui Residential Building	216,039.71
Greenland Garden Phase I	194,250.82
Galaxy City	148,358.88
Huangshi Garden and others	44,689.94
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	686,348.66

Apart from stepping up its marketing efforts, the Group continued to reduce cost through tendering system which was expanded from construction works to include sourcing of construction materials, environmental, finishing and gardening works. This tendering system is expected to have positive effect on cost control and quality improvement.

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The Group believes that customer centred service and project brand building are vital to maintain competitiveness in the Guangzhou property market. The Group has strengthened its after sales service by centralizing functions of property maintenance and management so that it can be more responsive to needs of home owners. Since the second half of 2000, the Group has strengthened the cooperation with its local partner, Guangzhou City Construction and Development Holdings Ltd. ("City Construction"). The Group believes that such cooperation with City Construction could facilitate the brand building of joint venture property projects.

To step up development efforts, the Group increased total gross floor area of joint venture projects under construction to 6.252 million sq. feet as at the end of 2000 which was up by 15 per cent year on year. In 2001, major projects to be offered will include Galaxy City, Greenland Garden Phase I, Jiang Nan Estate Phase 3-11 and Dalian Yuexiu Plaza. Expected sales area will be approximately 1 million sq. feet and the Group will be well positioned to capture the steadily growing demand for residential properties in Guangzhou.

A new extension of Guangzhou Metro to connect the eastern Zhu Jiang Estate and the southern Panyu suburban area is under planning. Such development is most beneficial to the Group and will increase the value of its land bank located at Zhu Jiang Estate. This portion of residential land has total gross floor area of over 3.228 million sq. feet.

Regarding the Hong Kong projects, the residential sites located in Western District and Pokfulam Road on Hong Kong Island are under planning. Constructions will be completed in 2003. The Yau Tong site was approved residential and commercial land use by the Hong Kong Government and constitutes part of the Group's land bank in Hong Kong with total gross floor area of 560,000 sq. feet.

Hong Kong and Guangzhou Property Rental Remained Steady

The Group has investment property of 910,000 sq. feet lettable area in Hong Kong. Aggregated rental income of the Group's investment properties in Hong Kong was increased moderately in 2000 due to leasing out more lettable area as a result of the Group's effort in renovating these investment properties. As at the end of December 2000, the Group leased out approximately 94 per cent of the commercial units in Yue Xiu Plaza, 100 per cent of lettable area in Yue Hing Building, approximately 94 per cent of Tsuen Wan International Centre, 100 per cent of Lung Wah International Godown in Hong Kong. In the Guangzhou market, almost 100 per cent of Jin Han Building was leased while part of the Group's land bank is leased as shops and car parks.

Pulp and Paper Business Continued to Grow

Trial production of the new production line to increase the newsprint production capacity of Guangzhou Paper Limited ("Guangzhou Paper") to 290,000 tonnes per annum was completed in August 2000. The plant was able to respond to the rising demand from major newspapers in Guangdong Province on time. In 2000, Guangzhou Paper sold 239,700 tonnes of newsprint which were 38.8 per cent higher than 1999. Average newsprint price in 2000 was 3.3 per cent higher than the level in 1999.

In spite of higher cost for raw materials such as recycled paper and chemical wood pulp in 2000, the plant has implemented various cost control measures including downsizing and reduction of water, pulp, coal and electricity consumptions. The plant's new in-house electricity supply system has mitigated pressure of higher cost of external electricity supply. However, unit manufacturing costs of newsprint per tonne was increased moderately by 5.75 per cent year on year due to full year depreciation charge on the new newsprint machines.

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In 2000, Guangzhou Paper had allocated extra resources on environmental works. The plant started to operate the new sewage and industrial waste treatment lines and modified the current manufacturing process to recycle more waste water resulting in lower consumption of both water and pulp. In 2000, most of the environmental facilities achieved satisfactory results.

In 2000, the plant continued to maintain the biggest market share of 24.44 per cent in the domestic newsprint market and was ranked the top in China in terms of sales volume. Capacity utilization in 2000 was 100 per cent. With continuous improvement of product quality and provision of customer oriented services, the plant was awarded "Customers Satisfactory Unit" by the China Newspaper Association for the ninth consecutive year in 2000.

Although the newsprint market is expected to remain competitive in 2001, the Group is optimistic with the plant's performance given its location in the fast growing southern China where major newspapers are expanding the types and quantity of their publications to capture fast growing advertisements. With total newsprint production capacity expanded to 290,000 tonnes per annum, the plant may convert part of the former newsprint production capacity to the production of light weight coated paper if its demand recovers later in 2001.

Fujian Yue Xiu Shao Wu Pulp and Paper Manufacturing Company Limited ("Shao Wu Pulp and Paper") in Fujian Province has passed trial production and sales result was satisfactory in 2000. Shao Wu Pulp and Paper achieved an annual pulp production volume of 45,397 tonnes.

Toll Road Business Continued to Perform Steadily

Although traffic growth was deterred by certain road maintenance works around Guangzhou, GZI Transport Limited ("GZI Transport"), the toll road subsidiary of the Company, achieved net profit growth of 5.7 per cent to HK\$282.5 million in 2000. Such growth was achieved by reduction of administrative expenses and financial costs, and outstanding performance of the associated company which operates Humen Bridge. As the toll road business is a cash flow business underpinned by continuous growth of individual car ownership, GZI Transport will continue to expand this business.

Cement Business in Consolidation

The Guangzhou cement market entered into a period of consolidation in 2000 due to completion of certain government infrastructure projects such as the Inner Ring Road. Aggregate sales volume of cement and clinker of China Century Cement Limited ("CCC"), the cement subsidiary of the Company joint ventured with German cement group Heidelberg Zement, decreased by approximately 4.4 per cent to 2,552,000 tonnes year on year. The downstream business was also affected by a consolidating market in 2000. Combined sales volume of ready-mixed concrete in Guangzhou dropped by 17.6 per cent. Average selling price of cement decreased by approximately 6.7 per cent which reflected the market adjustment mechanism. On the other hand, unit manufacturing costs of cement per tonne was increased by about 3.7 per cent in 2000 due to higher energy cost and higher per unit sharing of fixed cost caused by lower level of cement production.

Responding to the specialized requirements of infrastructure projects, CCC has developed new cement product to enhance quality. After successful trial production in November 2000, the Group introduced the modified "P II" cement which releases lesser hydro heat, and was well received by the market. This new product is now widely used in sizable infrastructure project such as the new Guangzhou International Airport and expressways around Guangzhou.

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CCC took the opportunity of a slow market in 2000 to conduct major modification works for certain equipments. Guangzhou Zhujiang Cement Co. Ltd. under CCC has finished expansion work in May 2000 resulting in total annual cement production capacity reaching 1.5 million tonnes. Total annual cement production capacity of CCC was consequently raised to 2.9 million tonnes. Total cost of Rmb40 million for such expansion was 20 per cent below the original budget. Coupled with other major maintenance works completed, CCC has laid a solid base for a moderate market recovery started in late 2000 which was underpinned by construction work of several new infrastructure projects in Guangzhou.

To maintain competitiveness in 2001, CCC will reduce part of the workforce and study the making use of waste-heat from kilns for power generation and increase usage of the lower priced white coal to contain rising energy costs. CCC also considers to move its subsidiary, Guangzhou Cement Factory, away from urban area of Guangzhou Municipality and enhance its production capacity at appropriate times.

Selective Investments in High Technology Business

After acquiring a 32.75 per cent attributable interest in Guangzhou Jinpeng Group Co., Ltd. in 1999, which is involved in mobile network business such as hardware manufacturing, packaging, installation and related maintenance engineering services for mobile phone network operators in China, the Group acquired a 46.7 per cent attributable interest in China Information Technology Industry Co., Limited ("China ITI") in August 2000. China ITI is a joint venture with the Chinese Academy of Sciences in Beijing and is mainly engaged in the development of mapping software, related information products and applications based on Geographic Information System ("GIS") technology. The Group believes that such GIS based technology will have substantial market potential along with the increasing popularity of wireless communication.

FINANCIAL REVIEW

Analysis of Results

For the year of 2000, the Group's China property, newsprint and toll road businesses all performed satisfactorily which had offset the slow cement business. Turnover grew to HK\$ 3,380,717,000, representing a 25 per cent increase mainly driven by the newsprint and property businesses. Total cost of sales increased by 27 per cent to HK\$ 2,134,352,000 primarily due to higher raw material, energy costs of the industrial businesses and depreciation charged on the new newsprint production line. Overall gross profits still increased by 24 per cent to HK\$1,246,365,000 with the China property and newsprint businesses as the growth drivers. Other revenues decreased by 30 per cent to HK\$114,432,000 mainly due to termination of business tax rebate policy related to the toll road business. Administrative expenses increased by 20 per cent mainly due to the environmental and technology development expenses of the industrial businesses. However, other net operating expenses decreased sharply by 86 per cent as no more devaluation provision was required to be made on Hong Kong properties. Finance costs increased by 7 per cent as a result of less interest being capitalized for properties and production facilities under construction in 2000. Share of profits from associated companies decreased by 39 per cent to HK\$121,310,000 primarily due to below expectation performance of selective property projects. As a result, profit attributable to shareholders amounting to HK\$111,554,000 increased dramatically by 493 per cent compared with 1999.

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Earnings Per Share

	2000	1999
Profit attributable to shareholders	HK\$111,554,000	HK\$18,826,000
Weighted average number of shares in issue	3,936,567,892	3,619,850,539
Basic earnings per share	2.83 cents	0.52 cent
Fully diluted earnings per share	2.81 cents	0.52 cent

Dividend

The Directors do not recommend the payment of a final dividend for 2000 (1999: nil). There was no payment of interim dividend for the year (1999: nil).

Analysis of cash flows and borrowings

As at 31st December 2000, the Group had bank deposits, cash and bank balances of approximately HK\$1,330 million. The Group had generated net cash inflow of approximately HK\$629 million from operating activities. These internally generated cash were largely applied to repayment of bank borrowings and funding capital expenditures.

As at 31st December 2000, the Group had bank borrowings excluding bank overdraft ("Bank borrowing") and convertible bonds outstanding of approximately HK\$3,118 million and HK\$581 million respectively. The Group had net repaid bank borrowings in aggregate sum of approximately HK\$312 million from internal funds.

Approximately 39 per cent of the Group's bank borrowings were denominated in Rmb and approximately 38 per cent in US dollars and the remaining 23 per cent in HK dollars. The convertible bonds were denominated in HK dollars. The following table shows the repayment term of the Group's bank borrowings and convertible bonds:

	Repayable within				Total HK\$'000
	one year HK\$'000	one to two years HK\$'000	two to five years HK\$'000	over five years HK\$'000	
Bank borrowings					
Rmb loans	1,092,280	89,720	21,028	–	1,203,028
US dollars loans	907,590	205,920	70,200	–	1,183,710
HK dollars loans	186,283	304,361	238,465	1,757	730,866
	<u>2,186,153</u>	<u>600,001</u>	<u>329,693</u>	<u>1,757</u>	<u>3,117,604</u>
Convertible bonds	<u>95,000</u>	<u>249,450</u>	<u>237,023</u>	<u>–</u>	<u>581,473</u>
	<u><u>2,281,153</u></u>	<u><u>849,451</u></u>	<u><u>566,716</u></u>	<u><u>1,757</u></u>	<u><u>3,699,077</u></u>

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Approximately 70 per cent of the bank borrowings will be repayable within one year. The management has confidence that these bank borrowings will be refinanced. Approximately 16 per cent, 43 per cent and 41 per cent of the convertible bonds are redeemable in 2001, 2002 and 2003 respectively. The convertible bonds redeemable in 2001 were issued by GZI Transport. On maturity, those bonds which have not been converted into ordinary shares at a price of HK\$2.0424 per share are to be repaid at their principal amount with accrued interest. The convertible bonds redeemable in 2002 and 2003 were issued by the Company. On maturity, those bonds which have not been converted into ordinary shares of the Company at a price of HK\$0.76 and HK\$0.6168 per share respectively are to be repaid at 105 per cent of their principal amount with accrued interest. Details of the convertible bonds are set out in note 27 to the audited accounts on page 69. Approximately 43 per cent of the Group's bank borrowings were secured and the rest were unsecured.

Analysis of Capital Commitments and Expenditures

The details of the Group's capital commitments of HK\$1,953 million as at 31st December 2000 are set out in note 33 to the audited accounts on page 75. These capital commitments over the next few years are mainly for the addition of fixed assets, including toll road and properties under development; and also the capital commitments in associated companies and jointly controlled entities.

In 2000, the Group's capital expenditures primarily in installing a new newsprint production line which amounted to approximately HK\$325 million. In February 2001, the Group completed the acquisition of the remaining 49 per cent interests in Xian Expressway. This acquisition was mainly financed by a HK\$170.0 million five-year term loan raised in 2001 and secured by the Group's interest in Xian Expressway. The Group's strategy is to use as much as practicable re-invested profits and debt financing denominated in Rmb to match the Rmb capital expenditure and take advantage of the prevailing low interest rate in China. Equity and debt financing denominated in foreign currency will be used selectively as supplementary funds.

Treasury Policies

The Group's overall treasury and funding policy is that of risk management and liquidity control. Bank balances are generally placed in short term fixed rate deposits in bank accounts in Hong Kong, China and overseas. No fund is placed in non-bank institutions or invested in securities. The management believes that the steady inflow of HK dollars, Rmb, and US dollars funds generated and/or repatriated from the Group's subsidiaries, associated companies, and jointly controlled entities in Hong Kong, China and overseas are sufficient to meet the Group's short to medium term Rmb, US dollars and HK dollars borrowings, finance costs and dividend payments.

Since the Group's principal operations are in China and most of the income is denominated in Rmb, the management is aware of possible exchange rate exposure. As a hedging strategy, the management emphasizes on using Rmb borrowings to finance the Group's future investments and capital expenditures.

The management is also aware of the prevailing interest rate differential and the associated borrowing costs difference between Rmb loans and US dollar loans. To take advantage of the low interest rate and the low borrowing costs of Rmb loans, the management strictly adheres to its Rmb based borrowing policy.

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Return on Shareholders' Equity

As at 31st December 2000, the Group's shareholders' equity decreased slightly from approximately HK\$6,629 million in 1999 to approximately HK\$6,486 million was mainly attributable to the decrease in capital reserve, which was mainly goodwill arising from the acquisition of subsidiaries, associated companies and jointly controlled entities, by approximately HK\$260 million out-weighted the increase in retained earnings of HK\$112 million. The returns on shareholders' equity for the last three years are as follows:

	2000 HK\$'000	1999 HK\$'000	1998 HK\$'000
Profit attributable to shareholders	111,554	18,826	100,288
Shareholders' equity	6,485,546	6,629,095	6,543,870
Return on shareholders' equity	1.7%	0.3%	1.5%

The Group was not able to achieve satisfactory returns on shareholders' equity over the last few years due to the impacts of the Asian financial crisis.

Capital Structure and Interest Coverage

The following table summarises the components of the Group's capital structure:

Capital Structure	2000		1999	
	HK\$'000	%	HK\$'000	%
Bank borrowings	3,117,603	30	3,429,562	33
Convertible bonds	581,473	6	344,450	3
Debts	3,699,076	36	3,774,012	36
Shareholders' equity	6,485,546	64	6,629,095	64
Total capitalization	10,184,622	100	10,403,107	100
Gearing Ratio	36%		36%	

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The decrease in shareholders' equity and the decrease in debts resulted in a similar level of gearing ratio of 36 per cent in 1999 and in 2000.

Interest Coverage

	2000 HK\$'000	1999 HK\$'000
Profit before taxation, interests and non-cash items	1,026,328	880,118
Interest expenses	299,011	300,484
Interest coverage	3.4 times	2.9 times

As the profit before taxation, interests and non-cash items have increased significantly, interest coverage improved from about 2.9 times in 1999 to about 3.4 times in 2000.

Financial Assistance and Guarantees

As at 31st December 2000, the Group had provided guarantees of approximately HK\$1,050 million equivalent in connection with bank loans granted to jointly controlled entities, of which approximately HK\$953 million equivalent was provided by GZI Transport. In addition, as at 31st December 2000, the Group charged the income derived from GZI Transport's 24.3 per cent effective interest in an associated company involving in toll road business to a bank in favour of one of the shareholders of that associated company, (the "Shareholder") in respect of the Shareholder's repayment of bank loan amounted to Rmb500 million (approximately HK\$467 million) and interest thereon (collectively referred to as "Relevant Loan"). A counter-indemnity has been provided by the Shareholder to GZI Transport against all liabilities arising from such charge. In case of any shortfall under the Shareholder's counter-indemnity, Yue Xiu Enterprises (Holdings) Limited, the Company's controlling shareholder, is responsible to indemnify GZI Transport.

Employees

As at 31st December 2000, the Group had approximately 13,330 employees of which approximately 12,790 employees were primarily engaging in the supervision and management of toll roads and the operations of the six cement and paper factories. The Group remunerates its employees largely based on industry practice, including contributory provident funds and other staff benefits. The Group has also adopted share option schemes which award its employees according to the performance of the Group and individual employees.