

REVIEW OF OPERATION

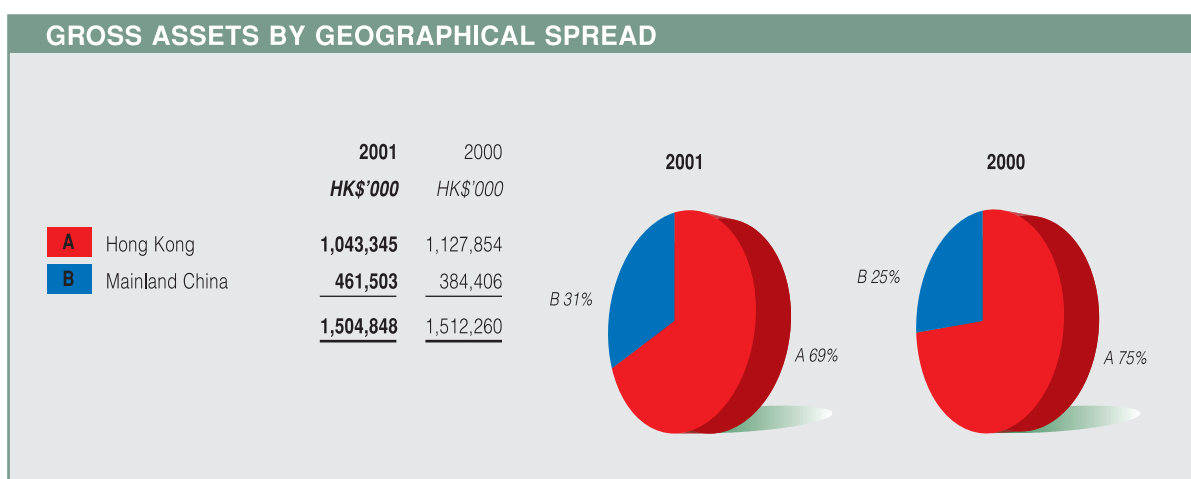
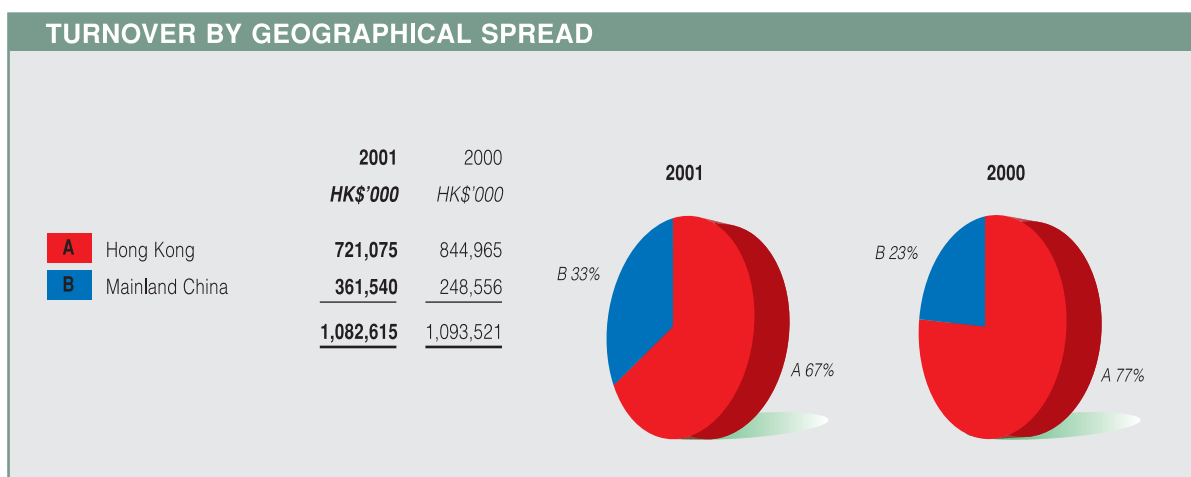
Overview

Turnover and profit before taxation for the year ended 31st December 2001 were HK\$1,083 million and HK\$128 million as compared to HK\$1,094 million and HK\$190 million respectively. Despite weaker market we are able to maintain turnover at the same level as last year; however, profit before tax decreased by 33%.

Hong Kong Construction Materials Division remains the major contributor to the profit of the Group. Market conditions were impacted by the event of 11th September. Profit from Hong Kong operation declined further despite management efforts to contain costs and improve productivity. In contrast the company is upbeat on the Mainland's prospects, in particular, with its Shanghai operation which recorded significant improvement in performance.

Analysis by Geographical Area

	Hong Kong HK\$'000	Mainland HK\$'000	Group HK\$'000
Turnover	<u>721,075</u>	<u>361,540</u>	<u>1,082,615</u>
Operating profit	139,926	9,120	149,046
Finance costs	(15,734)	(1,195)	(16,929)
Share of profits less losses of			
Jointly controlled entities	(157)	2,095	1,938
Associated companies	<u>370</u>	<u>(6,380)</u>	<u>(6,010)</u>
Profit before taxation	<u>124,405</u>	<u>3,640</u>	128,045
Taxation			<u>(14,410)</u>
Profit after taxation			113,635
Minority interests			<u>(834)</u>
Profit attributable to shareholders			<u>112,801</u>

Overview (Cont'd)

Business in Hong Kong

The shrinking economy and slow down of the property and infrastructural developments during the year resulted in a further drop in the overall demand of construction materials in Hong Kong. Despite continued management efforts to ensure that all facets of operations are cost effective, soft demand and competitive pricing in the industry put significant pressure on the profit of the Hong Kong operation.

The rehabilitation works of KWP Quarry Co. Ltd. at Anderson Road in which the Group has a 63.5% interest is proceeding on schedule. In January 2002, the company met its second milestone on time in accordance with its contract with the Hong Kong SAR Government entered into in April 1997. To cope with the changing market conditions and maintain the Group's competitive position as one of the leaders in the industry in Hong Kong, the Group has embarked on certain initiatives. On the operational side, we established a wholly owned new quarry in Huidong, Guandong with an aim to cater primarily to the Hong Kong market. It will commence production by the end of 2002. On the management side, the project that the Group initiated in 2000 for cultural change focusing on alignment of accountability and authority to meet corporate objectives is being carried out successfully. The Group now has an effective organization structure and culture to meet the challenging market conditions ahead of us.

Business in Hong Kong (Cont'd)

The Management is pleased to report that following the successful implementation of PeopleSoft Accounting System for its Hong Kong operation in January 2001, the accounting department of the Group has succeeded in reducing headcount through natural attrition. It is targeting to shorten the month end accounts closing from existing eight working days to five working days by the end of 2002.

Impacted by the 11th September 2001 event, the market in Hong Kong worsened over the last six months which added more pressure on pricing and availability of new orders. However, the Group remains optimistic on the longer term. Our new Financial Secretary in his maiden budget speech on 6th March 2002 highlighted a 21% increase in real terms on capital expenditure for 2002/03. This includes approximately HK\$29 billion allocated for major capital works. The SAR Government was also said to be considering to further reduce the production of public housing thus leaving more freedom for the private sector to develop the market. The Group envisages that all these will provide a basis for restructuring Hong Kong's economy and renew public confidence as well as provide good business opportunities for the Group.

The restructuring of the Hong Kong economy will take time to materialize. Hence, the Group envisages that contributions from the Hong Kong operation would, in the meantime, be further reduced before recovery. The Group's order book is currently maintained at a level lower than that of the corresponding period last year. However, given current market conditions, the Group considers the situation to be fair and satisfactory. To strengthen the Group's position, continuing management efforts will be endeavored to explore opportunities available in the Pearl River Delta in terms of new market and product range.

Business in Mainland China

In general, the overall performance of our Mainland Division reported significant profit improvement as compared to last year.

In Shanghai, the Group is pleased to report that profits contribution from the Shanghai region is better than expected due to an increase in the overall ready-mixed concrete market in 2001 of more than 30%. The Group's ready-mixed concrete sales volume in Shanghai has reached a level where the Group sees the opportunity to create a vertical integration by expanding its production facility to cover upstream products. Along this, the Group has established K. Wah Quarry (Huzhou) Company Limited, a wholly owned subsidiary of the Group. The subsidiary will establish a quarry in Huzhou aiming to serve primarily the Shanghai market. It is scheduled for full production by the end of 2002. In addition, the Group has established Shanghai K. Wah Concrete Piles Company Limited, a co-operative joint venture of which the Group has 100% equity interest. The joint venture company will establish a plant for production of piles also aiming to serve primarily the Shanghai market. It is envisaged that with the continuing improvement of market conditions coupled with the Group's additional investments to expand facilities and product range, Shanghai precast concrete and other construction materials business will further increase its contribution to the Group.

In Guangzhou, the performance is disappointing. This is due to worsening market condition and the closure of Huang Pi Quarry and Jia Fang Concrete batching plant. Huang Pi's application to the Guangdong Provincial High Court to revoke the closure notice was heard on 28th December 2001. The Group is still awaiting the outcome of the legal proceeding.

The Group is pleased to report that with the Group's continued efforts in improving productivity, the total production output of Guangzhou K. Wah Nanfang Cement Limited in which the Group has 50% equity interest, increased by 14% over the previous year. This benefit from increased production capacity is offset by intensifying market competition and considerable drop in prices. Despite all these the joint venture company is making a contribution to profit.

Business in Mainland China (Cont'd)

The Group is also pleased to report that agreement has been reached with the Mainland partner for the Group to continue its management of Guangzhou K. Wah Nanfang Cement Limited for another term of four years following the expiry of the existing term in November 2002.

In the long run, through leveraging the Group's strong financial strength and its invaluable years of management experience in the Mainland, the Group is confident of grasping the opportunities arising from China's entry to WTO and the commencement works for Beijing's 2008 Olympics. It is also the Group's strategy to expand its product range and business presence to other major cities in the Mainland.

Technology Investments

The Group has been proceeding prudently with its diversified investment plan and so far has invested HK\$111 million on technology investments. It has also achieved a balanced investment portfolio in various segments, both in Hong Kong and in Mainland China.

The Group will prudently explore technology investments within the current strategic mandate that will bring satisfactory return in the medium to long term. We will also continue to explore our relationship with existing partners to create synergy that will bring to the Group more investment opportunities from the Mainland and from overseas. In selecting investment projects, the Group places emphasis on management skill, technical expertise, innovation and technological advancement. We are confident that our prudent investment approach can capitalize the market potential available from this new economic frontier.

AWARDS

In pursuit of improvement, the Group has participated in various competitions during 2001 and your Group is pleased to report the following awards:

Awards in Hong Kong

Certificate of Merit in Corporate Governance

The Board of Directors of K. Wah Construction Materials Limited was presented with a Certificate of Merit in Corporate Governance in the Directors of the Year Awards 2001. The competition was organized by The Hong Kong Institute of Directors and it aimed to give recognition to outstanding performers in corporate governance.

Good People Management Award 2001

K. Wah Quarry Company Limited, a wholly owned subsidiary of the Group, was given the Good People Management Award 2001 by the Labour Department. The winning of the award was the result of an open and equitable management system, a fair reward system, mutual communication, continuous learning and a balanced lifestyle.

Awards in Hong Kong (Cont'd)

Certificate of Merit in Environmental Performance

K. Wah Concrete Company Limited, a wholly owned subsidiary of the Group, received the Certificate of Merit in 2001 Hong Kong Awards for Industry: Environmental Performance. The company puts tremendous effort in environmental protection, such as implementing an in-house Environment Management System, using resources effectively, minimizing pollutants and waste and embarking on a greening program in workplaces.

Certificate of Merit in Good Housekeeping Plan/Certificate of Performance in Occupational Safety and Health Enhancement Forum

K. Wah Concrete Company Limited, a wholly owned subsidiary of the Group, received the Certificate of Merit in Good Housekeeping Plan and the Certificate of Performance in Occupational Safety and Health Enhancement Forum organized by the Occupational Safety and Health Council.

Awards in Mainland

Huang Pi Quarry was accredited by China Sandstone Association and China Quarries Association as “**The Country’s Best Model Quarry in Conserving and Utilising Sandstone Resource**”. The award is hailed with significance in that it recognizes Huang Pi Quarry’s high industry standards and sets a model example for other Mainland China quarries.

Guangzhou K. Wah Nanfang Cement Limited won a total of three outstanding awards in 2001. They are “**2000 Provincial Advance Entity in Bulk Cement Development**” accredited by Guangdong Province Construction Development Bureau; “**Certificate of Excellence in recognition of its Advanced Bulk Cement Works**” accredited by Guangzhou Construction Board and “**Certificate of Construction Products Assurance**” accredited by Guangzhou Construction Industry Association.

Hong Kong	
Company	Award
Board of Directors — K. Wah Construction Materials Ltd.	Certificate of Merit in Corporate Governance, Directors of the Year Awards 2001
K. Wah Quarry Co. Ltd.	Good People Management Award 2001
KWP Quarry Co. Ltd.	— Certificate of Merit, Outstanding Good Housekeeping Plan — 建造業良好工地管理銀獎
K. Wah Concrete Co. Ltd.	— 2001 Business Environment Council Certificate of Merit in Environmental Performance — Certificate of Performance — "Safety Chain Device" for the Extension Chute of Truck Mixer, Occupational Safety and Health Enhancement Forum 2001 — Certificate of Merit, Outstanding Good Housekeeping Plan
K. Wah Stones (Zhu Hai) Co. Ltd.	— Double Best Enterprise of the Nation's Foreign Investment 1999
Shanghai	
Company	Award
Shanghai Bao Jia Concrete Co. Ltd.	— 《2000年度預拌混凝土生產質量優良》
Shanghai Gang Hui Concrete Co. Ltd.	— 《2000年納稅百萬元企業》 — 《2000年度上海市預拌混凝土生產企業質量業績考核第二名》 — 《1999年度上海市預拌(商品)混凝土生產企業質量業績考評第二名》 — 《1999年納稅百萬元企業》
Shanghai Jiafu Concrete Co. Ltd.	— 《2000年度預拌混凝土生產質量優良》 — 《1999年度上海市預拌(商品)混凝土生產企業質量業績考評第五名》
Shanghai Xincai Concrete Co. Ltd.	— 《2000年度外商投資企業稅收先進單位》榮譽證書
Shanghai Jiajian Concrete Co. Ltd.	— 《2000年度外商投資企業稅收先進單位》榮譽證書
Guangzhou	
Company	Award
Guangzhou K. Wah Nanfang Cement Ltd.	— 先進會員單位 — 先進個人 — 鍾福榮 — 廣州市推薦使用建材(建設工業)產品證書 — 計量水平確認證書 — 第七次全國水泥分析大對比「合格單位」稱號 — 2000年推廣散裝水泥全省先進單位 — 中國主要建材企業及知名建材產品推薦證書 — 信得過產品證書 — 安全文明生產先進單位 — 安全生產先進單位 — 98—99年武裝工作先進單位 — 質量體系認證證書

* Awards are listed according to the year of presentation.

Awards 2000-2001

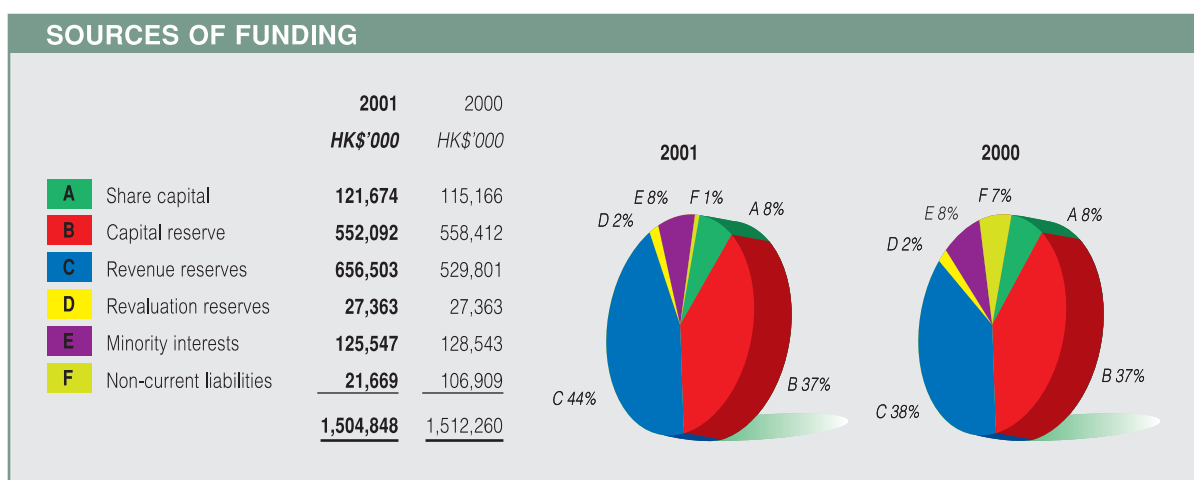


1. The Board of Directors of K.Wah Construction Materials Ltd. was presented with a Certificate of Merit in Corporate Governance in the Directors of the Year Award 2001 by The Hong Kong Institute of Directors.
2. K.Wah Quarry Company Ltd. was given the Good People Management Award 2001 by the Labour Department.

FINANCIAL POSITION AND GEARING RATIO

The financial position of the Group has continuously improved during the year. At 31st December 2001, the shareholders funds increased by 6% to HK\$1,358 million from HK\$1,277 million as at 31st December 2000 and the Group's gross assets employed decreased by 0.5% to HK\$1,505 million from HK\$1,512 million as at 31st December 2000.

The gearing ratio, defined as the ratio of total loans outstanding less cash balances to total assets, was practically at a debt free level at 31st December 2001 as compared to 3% at 31st December 2000.



LIQUIDITY AND FINANCIAL RESOURCES

The Group continues to maintain a strong cash position. As at 31st December 2001 total cash and bank balances were HK\$299 million as compared to HK\$234 million as at 31st December 2000. Outstanding bank loans as at year-end decreased to HK\$285 million from HK\$288 million as at 31st December 2000. All outstanding bank loans were on a floating rate basis and are repayable in 2002. The Group's gearing ratio and liquidity remains strong and the Group has sufficient funds to meet its commitment and working capital requirements.

TREASURY POLICY

The Group continues to adopt a conservative treasury policy with all bank deposits in either Hong Kong Dollars, United States Dollars or in the local currencies of the operating subsidiaries, keeping a minimum exposure to foreign exchange risks. All of the Group's borrowings are in either Hong Kong Dollars or Renminbi. Forward foreign exchange contracts are utilized when suitable opportunities arise and when considered appropriate, to hedge against foreign exchange exposure. The Group has not engaged in the use of other derivative products, which are considered not necessary for the Group's treasury management activities.

CHARGES ON GROUP ASSETS

Details of charges on group assets are set out in note 13 to the financial statements.

CONTINGENT LIABILITIES

Details of contingent liabilities are set out in note 33 to the financial statements.

EMPLOYEES

Employees and Remuneration Policy

The Group, excluding associated companies and jointly controlled entities, employs over 1,200 employees in Hong Kong and the Mainland. Employee costs, excluding Director's emoluments, amounted to HK\$145,157,000.

The Group recruits and promotes individuals based on their competencies, merit and development potential and ensures remuneration packages are competitive. In 2001, with the support of an external consultant, the Group has designed and implemented a new performance management system for its executives. Specific objectives are agreed at the beginning of the year with regular achievement reviews.

The Group has implemented a share option scheme for executives from 1991 following approval by its shareholders for the purpose of providing competitive package and long term retention of management talents.

Human and Organization Development

We continue to promote learning by sponsoring employees to attend external and internal training courses in a wide range of areas such as knowledge of the Group and its businesses, business integrity and ethics, presentation and technical skills, quality awareness and safety, language and computer software applications in addition to tailor-made management development programs.

To augment the Group's present expansion, localisation plan and future development in the Mainland, we continue with our Management Trainee Program to recruit high potential graduates and develop them to be our future managers. In alliance with Tongji University, Shanghai, a training plan was formulated to upgrade and strengthen the technical and managerial competencies of our technical, middle and senior managerial employees.

Health, safety and environmental protection

Health, safety and environmental protection (HSE) are integral parts of the Group's business. It is a shared initiative between the Company and all those concerned to give due consideration to stakeholders' HSE needs in our operations.

The Group benchmarks both international and local standards and practices, and adopts overall goals of keeping industrial accidents to the lowest level. It strives to provide a healthy and safe workplace for its staff and workers. It also emphasizes on environmental protection.