Review of Operating Results

A summary of the performance of the Group's major businesses during the year under review is as follows:

Utilities

The profit contribution from the Water Project was encouraging. During the year, there was an increase in the sales volume of water in the Shenzhen and Dongguan areas, and also an increase in the contracted volume of water supplied to Hong Kong. In addition, effective cost and management controls together with the implementation of an improved water tariff collection mechanism in the Dongguan area has brought about an increase in the operating profit before finance costs of the Water Project (12 months ended 31.12.2001: profit of HK$1,470,951,000;10 days ended 31.12.2000: loss of HK$30,741,000).

The wet climate which resulted in greater reliance on hydro electricity, the prior mode for the generation of electricity in Guangdong Province, caused a lower demand for thermal electricity. It therefore led to a drop in the sales of electricity of the Shaoguan Power Plant D by 8.7% in 2001. In the first six months of 2001, the sales of electricity amounted to only 526 million kwh. Through the effort of the management, electricity sales in the second half of the year increased sharply to 934 million kwh and the total for the year was 1,460 million kwh.

A new associate of Shaoguan Power Plant D, namely, 廣東省韶關粵江發電有限責任公司 (Guangdong Shaoguan Yue Jiang Power Supply Limited), started to generate profit for the Group in the second half of the year. The electricity sold in 2001 was 713 million kwh, and the profit shared by and attributed to the Group was HK$4,539,000.

Sales of electricity by the Group's power plant in Meixian, an investment of an associate, amounted to 1,384 million kwh (2000: 1,454 million kwh), which continued to provide a stable income to the Group.

Infrastructure

In 2001, an after-tax profit of HK$70,645,000 (2000: HK$28,411,000) was generated from the "2 Roads and 2 Bridges" projects, namely the Qinglian Highway, the Guangzhou – Shantou Highway (Huizhou section), the Shantou Haiwan Bridge and the Humen Bridge. The considerable increase in profit was mainly due to large savings in interest expense resulting from the early repayment of the original syndicated bank loan by new refinancing successfully arranged during the year.

Qinglian Highway, which links Qingyuan and Lianzhou in Guangdong Province, recorded a decrease of 12% in the traffic flow, resulting in a decrease in revenue to HK$269,000,000 in 2001 (2000: HK$347,000,000). The average daily traffic in 2001 was 31,551 vehicle trips as compared to 35,700 vehicle trips in 2000. The Company's effective interest in this project is 7.2%.

Infrastructure (continued)

Guangzhou-Shantou Highway (Huizhou Section) recorded a decrease of 3% in the traffic flow, resulting in a decrease in revenue to HK$115,000,000 in 2001 (2000: HK$123,000,000). The average daily traffic in 2001 was 22,072 vehicle trips as compared to 22,712 vehicle trips in 2000. The Company's effective interest in this project is 26.0%.

Shantou Haiwan Bridge had steady traffic flow. The average daily traffic in 2001 was 11,553 vehicle trips while in 2000 it was 11,592 vehicle trips. The annual revenue was HK$109,000,000 in 2001 (2000: HK$109,000,000). The Company's effective interest in this project is 15.3%.

Humen Bridge recorded a growth of 8% in the traffic flow. The average daily traffic in 2001 was 26,082 vehicle trips while in 2000 it was 24,133 vehicle trips. The annual revenue reached HK$336,000,000 in 2001 (2000: HK$308,000,000). The Company's effective interest in the project is 15.3%.

The performance of the two Pak Kong Bridges in Qingyuan remained stable, generating a steady cash return to the Group.

As a result of the stepped up enforcement action taken by the government authorities against overloaded trucks, the average daily traffic of the Yingkeng Highway decreased by 14% in 2001. The Yingkeng Highway has therefore remained unable to meet its revenue target.

Property

Mainland China

Sales of Riverside Garden for the year amounted to only HK$321,000,000 compared to HK$476,000,000 for last year. The current year's after-tax profit for the Riverside Garden project remained the same as last year. In December 2001, the Group sold a 55.2% interest in the Riverside Garden project, reducing the Group's effective interest in the project to 24.8%.

Teem Plaza continued to enjoy high occupancy rates and high rental income. In particular, rental income increased by HK$55,703,000 to HK$257,491,000 (2000: HK$201,788,000).

Most of the residential units and shop units in the Suzhou GD Plaza project were sold during the year and the proceeds were used to settle partially the outstanding creditor payables of the project. Total sales amounted to HK$78,994,000 (2000: HK$40,074,000). The Company expects to complete the sale of the remaining units in Suzhou GD Plaza in 2002.

Property (continued)

Hong Kong

The occupancy rate of Guangdong Investment Tower (the "GDI Tower") was maintained at 100%. However, given the current depressed state of the local commercial rental market, there has been a slight reduction in the average rentals in respect of lease renewals and new leases. Rental for the GDI Tower amounted to HK$26,172,000 (2000: HK$22,286,000).

Guangdong Parking Limited's interest in the car park located in North Point continued to show a minor operating loss (before the property revaluation deficit) of HK$1,880,000 (2000: HK$4,100,000).

Hotels

Mainland China

While the average occupancy rate of Guangdong Hotel Shenzhen has only slightly decreased to 91.8% (2000: 93.4%), the average occupancy rate of 珠海粵海酒店 (Yue Hai Hotel, Zhuhai) was adversely affected by the aftermath of the "September 11 Incident" together with the decrease in the number of Taiwanese guests. The occupancy rate of the latter, on average, reduced from 76.2% in 2000 to 71.8% in 2001.

Hong Kong

Local tourism experienced a sharp decline in the aftermath of the "September 11 Incident". The number of visitors arriving in Hong Kong recorded a negative growth in September and October 2001, with visitors from the United States dropping sharply by 18%. However, the Mainland China market was not affected and the number of visitors to Hong Kong continued to grow steadily, with a year-on-year growth of 37% in the fourth quarter of the year.

Despite the keen competition in the Hong Kong hotel market in 2001, the average occupancy rate of both the Wharney Hotel and Guangdong Hotel remained high at 88% (2000: 87%) and 85% (2000: 84%) respectively.

Cost controls and effective utilisation of available resources have improved the hotel group business (before the hotel property revaluation deficit) from a loss of HK$8,041,000 for last year to a profit of HK$8,022,000 for this year.

Other Businesses

Brewery

The beer market in South China continued to be very competitive. The consolidated turnover and sales volume of Guangdong Brewery Holdings Limited ("GD Brewery"), dropped to HK$543,922,000 (2000: HK$613,892,000) and 161,000 tonnes (2000: 171,000 tonnes) respectively. However, because of effective cost control measures, interest savings and credit control, GD Brewery was able to improve its attributable profit from HK$10,242,000 for 2000 to HK$34,434,000 for 2001.

Tannery

The performance of Guangdong Tannery Limited was adversely affected by substantial provisions of HK$91,916,000 which were mostly in respect of provisions against properties and impairment of assets.

Sales increased by 6% compared with 2000 while the profit margin dropped slightly from 10.98% in 2000 to 10.58% in 2001.

Nevertheless the loss after tax for the year was reduced to HK$77,858,000 (2000: HK$113,745,000).

Malting

Notwithstanding keen competition from major competitors in northern China, the Group's malting business achieved a record high production of 183,000 tonnes (2000: 153,000 tonnes) in its Guangzhou plant, while its Ningbo plant was able to increase its production to 135,000 tonnes (2000: 114,000 tonnes). Revenue for Guangzhou plant and Ningbo plant amounted to HK$439,465,000 (2000: HK$356,240,000) and HK$301,199,000 (2000: HK$261,996,000) respectively.

Tours/Travel

By means of effective cost control measures, interest savings and substantial reduction in provisions, the Group managed to turnaround the operating loss of the tours and travel business in 2000 and reported a profit in 2001 (2001: a profit of HK$20,619,000; 2000: a loss of HK$227,058,000).

Liquidity, Gearing and Financial Resources

As at 31 December 2001, cash and bank balances of the Group fell by HK$487 million to HK$1,605 million (2000: HK$2,092 million), balances of which are mostly denominated in Hong Kong dollars (HK$283,100,000) and Renminbi (HK$1,258,513,000). This is mainly due to the repayment and prepayment of bank borrowings under debt restructuring agreements during the year. As at 31 December 2001, the Group had financial borrowings amounting to HK$19,390 million (2000: HK$21,221 million). Of the Group's total financial borrowings, HK$541 million was repayable within one year while the remaining balances of HK$5,732 million and HK$13,117 million would be repayable before or in 2005, and after 2005, respectively.

As at 31 December, 2001, the Group's total available credit facilities amounted to HK$21,033 million, of which HK$19,390 million have been utilised (2000: HK$23,483 million and HK$21,221 million, respectively). The unutilised banking facilities amounted to HK$1,643 million (2000: HK$2,262 million).

The gearing for the Group at the balance sheet date was 2.22 times, while last year's was 2.57 times. The improvement mostly reflected the reduction in the level of the Group's financial borrowings due to early prepayments in 2001, together with an increase in net asset value of the Group.

The existing cash resources and available credit facilities of the Group, together with steady cash flows generated from its operations, are sufficient to meet its payment obligations and business requirements.

Pledge of Assets

At 31 December 2001, certain of the Group's fixed assets, investment properties and bank deposits, with a total net book value of HK$1,560,761,000 (2000: HK$1,104,872,000) were pledged to secure general banking facilities granted to the Group.

In addition to the above, a property under development in Mainland China held under a long term lease with a carrying amount of HK$64,000,000 as at 31 December 2001 was held by the court in Mainland China as security for the Group's legal proceeding against the recovery from a debtor of the Group.

Capital Expenditure

The Group's total capital expenditure for fixed assets were HK$135 million in 2001, a decrease of HK$23 million from HK$158 million in 2000. The Group's 2001 capital expenditure related principally to the upgrading of certain facilities of the Water Project and the additions of plant and machinery for the power plant.

Exposure to Fluctuations in Exchange Rates and Related Hedges

As at 31 December 2001, total foreign currency borrowings amounted to HK$7,522 million, of which HK$951 million was Renminbi (2000: HK$8,805 million, of which HK$340 million was Renminbi).

Certain of the Group's foreign currency borrowings which are denominated in United States dollars and Euro (and which amounted to HK$3,113 million as at 31 December 2001) are hedged by currency swap agreements.

Contingent Liabilities

– During the year and subsequent to the balance sheet date, Guangdong (H.K.) Tours Company Limited ("GD Tours"), a wholly-owned subsidiary of the Company, received certain claims in respect of traffic accidents in Mainland China involving members of tour groups organised by GD Tours. However, up to the date of this report, no legal proceedings have been commenced.

  Based on legal advice, the directors are of the opinion that it is premature to estimate the outcome and hence, no provision has been made in the financial statements on account of the claims.

  In any event, according to legal advice, GD Tours is not at fault. It has therefore already denied liability and will further vigorously contest any such claim which may be brought.

– In March 2001, Yue Sheng Finance Limited ("Yue Sheng"), a wholly owned subsidiary of the Company, commenced legal proceedings in Mainland China to recover two outstanding loans in the total sum of HK$40,000,000 together with interest from the two Chinese parties who were the guarantors for those loans. As at the date of this report, the legal proceedings are still in progress.

  After trying without success to dispute the jurisdiction of the Chinese Court in the aforesaid proceedings, the two guarantors together with the borrower of those two loans commenced legal proceedings in Hong Kong against Yue Sheng and a former subsidiary of the Group in July 2000 seeking, inter alia, a declaration that they were under no legal obligation to repay the two loans and compensation. Steps are being taken by Yue Sheng to stay or alternatively to strike out the action. The interlocutory appeal thereon is pending.

  Based on legal advice, the directors are of the view that the claim brought against Yue Sheng is without merit and no provision for the claims of the guarantors and the borrower was considered necessary as at 31 December 2001.

Contingent Liabilities (continued)

– In January 2001, Guangdong Enterprises (North America) Fur Holdings Limited ("GDNA") and Harbour Hill International Limited ("Harbour Hill"), both subsidiaries indirectly held by the Company, commenced an action in the Southern District of New York against a company called Hennessy International Group, Inc. ("HIGI") and its owners/controllers. HIGI is one-third held by GDNA and is an associate of the Group. GDNA and Harbour Hill are attempting to recover from the corporate defendant and the individual defendants approximately US$2.25 million in financing that GDNA and Harbour Hill provided to HIGI. Defendants have counterclaimed for US$2 million, claiming that GDNA and Harbour Hill wrongly terminated HIGI's financing. Both plaintiffs and defendants are moving for summary judgment, which motions have been fully submitted to the court by 8 March 2002.

  The Directors, based on legal advice, believe that the case for the claim against the Group is not a strong one and accordingly, no provision has been made as at 31 December 2001.

Number and Remuneration of Employees

As at 31 December 2001, the Group had a total of 7,641 employees. Among the employees, 6,869 were employed by subsidiaries in Mainland China and 772 were employed by the head office and subsidiaries in Hong Kong. Out of the total number, 1,483 were managerial employees of the head office and its subsidiaries. The Group recruits and promotes individuals based on merit and their development potential for the positions offered. Performance of staff is reviewed at least annually and employees' compensation is performance driven. The Group's remuneration and benefits policies are based on the business performance of the relevant employee's company. Year-end bonuses will be granted to those employees with outstanding performance. People are the Company's key assets and key to success. The Group encourages employees to participate in external training programmes to develop themselves on a continuous basis. For existing employees' career development, the Group provides opportunities through on-the-job training by regular job rotation, so as to improve staff quality to meet future challenges and gain a competitive edge.

The Group advocates a corporate culture which seeks to excel in terms of financial performance and economic benefit and to effectively deploy its human resources strictly on merit. It also aims to continuously streamline the organizational structure leading to further cost reduction and manage and equip staff in key positions through the performance appraisal system and incentive/penalty system in order to enhance staff motivation for achieving various goals.

Significant Transactions

The Group has continued to press on with its business and assets restructurings. Significant transactions during the year include the following:

- In January 2001, the Company sold to GDH Limited its entire 70% equity interest in Guangdong Group (Shenzhen) Ltd. ("GD Shenzhen") together with a receivable of approximately RMB1,420,000 due from GD Shenzhen to the Company for a total consideration of HK$206,000,000. The disposal was approved by the Company's independent shareholders at an extraordinary general meeting held in February 2001 and was subsequently completed in April 2001.

- In February 2001, the Company disposed of its entire 57.16% equity interest in Guangdong Building Industries Limited ("GD Building") to an independent third party for a consideration of approximately HK$31,483,000. The transaction was completed in March 2001.

- In February 2001, the Company contracted for the disposal of its equity interest in and its shareholder's loans to Zhongshan Power (Hong Kong) Limited ("ZPHK"). The consideration, including the right for the Company to receive certain guaranteed profits, is approximately US$16,760,000. In addition, as a condition precedent for the completion of the sale, 中山火力發電有限公司 ("Zhongshan Power Plant"), the co-operative joint venture held by ZPHK, is required to fully repay all its indebtedness to Yue Sheng together with interest. The transaction is still in progress.

- In February 2001, GD Tours, a wholly owned subsidiary of the Company, disposed of part of its hotel properties and investment properties to an independent third party at a consideration totaling HK$300,000,000. The transaction was completed in November 2001.

- In March 2001, the Company entered into a preliminary agreement with an independent third party for the disposal of 70% equity interest in Guang Dong Nanhua Cement Limited held by Guangdong Construction Materials (International) Limited ("GCM") for a total consideration of RMB30,000,000. GCM, which is a wholly owned subsidiary of the Company, has been deconsolidated from the Group's financial statements in prior years. The transaction is however still in progress.

- In October 2001, a wholly owned subsidiary of the Company, Guangdong Properties Holdings Limited ("GD Property"), entered into a conditional sale and purchase agreement with 廣東粵港投資控股有限公司 (Guangdong Yue Gang Investment Holdings Company Limited) ("Yue Gang") whereby GD Property agreed to sell to Yue Gang or its nominees a 55.2% interest in GZ Panyu for a consideration of RMB220,890,000 exclusive of a 2001 interim dividend, in respect of such 55.2% interest to be sold, which was already declared by GZ Panyu prior to the date of the completion of the sale. The disposal was approved by the Company's independent shareholders at an extraordinary general meeting held in November 2001 and was subsequently completed in December 2001.

Significant Transactions (continued)

– In October 2001, GD Tours entered into a sale and purchase agreement with an independent third party for the sale of Guangdong Tours Building for a total consideration of HK$71,500,000. Deposits of HK$14,300,000 have been duly received up to the end of February 2002 and the date of completion is scheduled to be in April 2002.

Group Debt Restructuring

In order to rationalise the Group's debt structure, the Group has successfully arranged refinancing at a lower cost with certain banks in Mainland China for a non-wholly owned subsidiary and a jointly-controlled entity. Through an internal funding arrangement, the Group has also completed another refinancing for another two non-wholly owned subsidiaries which resulted in interest savings for the year.

Under the Company's group debt restructuring agreements signed in December 2000, the total "restructured bank debts" amounted to HK$6.8 billion. In 2001, the Company and those standalone companies have successfully reduced HK$3.0 billion of "restructured bank debts" representing 44% of the total. Excluding savings of HK$132,000,000 in interest expenses due to the successive reduction in both the United States and Hong Kong interest rates during the year, the Group saved HK$58,000,000 in interest due to the repayment or refinancing of "restructured bank debts".

In 2001, the Company reduced its own "restructured bank debts" by HK$1.3 billion, of which HK$1.05 billion was early repayment ahead of schedule. With such early repayment, not only all debt repayment milestones scheduled for 2002, but also a substantial part of the debt repayment milestones scheduled in 2003 have been met. With more than 22.5% of all the participating bank debts already repaid, the interest margin has reduced by 0.375%, thereby bringing down the Company's interest cost in the coming years.

Most of the standalone companies under their own debt restructuring scheme have also made early repayment, amounting to HK$397 million in aggregate, to their "restructured bank debts". As at 31 December 2001, the "restructured bank debts" owed by such standalone companies were reduced by HK$1.7 billion to HK$577 million.

During the year, certain standalone companies have further been released from their own debt restructuring scheme upon successful refinancing at a lower cost.

As part of the acquisition of the Water Project in December 2000, substantial debts (including but not limited to Tranche A and B Credits and Tranche C Note) amounting in aggregate to no less than HK$14 billion, were brought into the Group. Due to better performance of the water supply business and successful cost savings exercises, better cash flow has been generated in 2001 to reduce the Tranche A Credits by HK$359 million, which was well ahead of the existing scheduled repayments of HK$136 million, resulting in a saving in interest costs for the year of HK$9.7 million.