

Discussion and Analysis of Annual Results

Due to the global economy downturn in 2001, the operating environment in Hong Kong and other Asian countries remained difficult. The economic slowdown accelerated in the third quarter. Banking, property, securities and other investment sectors were all adversely affected. During the year, the under-performed operating results of the Group's banking businesses and the further provisions made for the Group's properties and securities investment portfolio resulted in a net loss for the year. The loss was mitigated by the Group's effort to reduce the borrowing costs. Consolidated net loss attributable to shareholders for the year amounted to HK\$551 million, representing a decrease of 18 per cent. when compared with last year's loss of HK\$671 million.

Subsequent to the year end, on 17th January, 2002, Hongkong Chinese Limited ("HKCL", formerly known as The HKCB Bank Holding Company Limited), a listed subsidiary of the Company, completed the disposal of its entire interest in The Hongkong Chinese Bank, Limited ("HKCB"), a then banking subsidiary of HKCL, for a consideration of HK\$4.2 billion (the "Disposal"). The consideration represented a premium of 30 per cent. over the consolidated net assets of HKCB at the end of 2001. On the same day, the Company also completed the acquisition of a further 35.2 per cent. effective interest in HKCL for an aggregate consideration of approximately HK\$1.8 billion (the "Acquisition"), which increased the Group's effective interest therein to 64.6 per cent. No material profit or loss is expected to arise from the Disposal for the year ending 31st December, 2002. Further details of the Disposal and the Acquisition are set out in Note 41 to the financial statements.

Accordingly, results generated from banking businesses were accounted for as discontinuing operations.

TURNOVER

Turnover for the year dropped 14 per cent. to HK\$1.8 billion (2000 – HK\$2.1 billion) after accounting for the non-recurring sale proceeds of an investment property of HK\$0.3 billion in 2000. With such proceeds excluded, turnover remained approximately the same for both years and contribution from property investment, food businesses and banking businesses was also similar to last year at 6 per cent., 29 per cent. and 25 per cent. of the total turnover respectively. Turnover contribution from securities investments increased to 17 per cent. from 4 per cent.

Turnover generated from the discontinuing operations accounted for 25 per cent. (2000 restated – 26 per cent.) of the total turnover.

OPERATING RESULTS FOR THE YEAR

Banking

HKCB had a disappointing year. Consolidated profit before tax reduced significantly by HK\$78 million to HK\$33 million (2000 – HK\$111 million).

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Property

Given the uncertainty in the property market, the value of the Group's existing property portfolio fell further. HK\$0.2 billion of the shortfall was charged to the profit and loss account and HK\$0.1 billion was debited against revaluation reserve. Against this, the Group was able to achieve an impressive income from property rentals. With higher renewal rates and satisfactory occupancy level, particularly for Lippo Plaza in Shanghai, during the year, rental income generated from the existing portfolio rose significantly by 19 per cent.

Securities investment

During the year, the Group made a provision of HK\$61 million (2000 – HK\$55 million) for its investment securities. As a result of the adverse conditions in the volatile stock markets which adverse impact was aggravated by the repercussions of the terrorist attack of 11th September, net realised and unrealised holding losses on other investments amounted to HK\$75 million (2000 – HK\$46 million when an exceptional gain on disposal of listed shares in Hong Kong Exchanges and Clearing Limited was excluded).

Finance costs

Amid these unfavourable operating conditions, the Group had devoted much effort in reducing its funding costs by restructuring borrowings to obtain lower cost financing. In addition, it was able to realise its entire interest in Tung Chung Station Development Package Two and applied the sales proceeds thereof to repay a substantial portion of its borrowings. During the year, total borrowings reduced by HK\$257 million. Together with the effect of successive interest rate cuts, finance costs dropped significantly to HK\$83 million (2000 – HK\$204 million), being 59 per cent. less than 2000.

Other

Included in share of results of associates was a loss attributable to the Group's 25 per cent. interest in the Meizhou Wan power plant project in Fujian Province. Upon completion of the construction work in 2001, expenses incurred were no longer capitalised. The provincial authorities and power offtaker have been trying to re-negotiate, among other things, the electricity tariff and the formal commercial operation of the whole facility has been postponed. As a result of the delay, there was a revenue shortfall, resulting in a loss of HK\$89 million shared by the Group.

FINANCIAL POSITION

As at 31st December, 2001, total assets of the Group dropped by 10 per cent. to HK\$9.4 billion (2000 – HK\$10.4 billion) whereas total liabilities reduced correspondingly by 15 per cent. to HK\$1.3 billion (2000 – HK\$1.6 billion) because certain assets were realised to repay the Group's borrowings and the provisions for diminution in values of the Group's assets were made. The shareholders' funds of the Group amounted to HK\$4.2 billion (2000 – HK\$4.8 billion) with consolidated net asset value per share stood at HK\$0.46 (2000 – HK\$0.52).

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Liquidity ratio of the Group as at 31st December, 2001 increased significantly to 3.13 from last year's 2.75. Despite the drop in the shareholders' equity, gearing ratio (total borrowings to shareholders' equity) reduced from 26 per cent. to 24 per cent. It was well below the average among companies in the same industry. The borrowings of the Group comprised of secured bank loans of HK\$937 million (2000 – HK\$1,157 million), of which 28 per cent. (2000 – 25 per cent.) was repayable within one year, and an unsecured loan note of HK\$73.5 million (2000 – HK\$110 million) issued by the Company.

The Group's banking facilities (other than those relating to banking operations) were secured by certain leasehold land and buildings, investment properties and shares in certain subsidiaries, with interest carried at floating rates. As at 31st December, 2001, 75 per cent. (2000 – 77 per cent.) of such bank loans were denominated in United States Dollars or Hong Kong Dollars. When appropriate, hedging instruments including forward contracts, swaps and currency loans are used to manage foreign exchange exposures.

Other than those attributable to HKCB and its subsidiaries, the Group did not have material contingent liabilities as at 31st December, 2001.

Save as the Acquisition, the Group did not have material commitments as at 31st December, 2001.

CHANGES IN ACCOUNTING POLICIES

Following the adoption of the new or revised accounting standards issued by the Hong Kong Society of Accountants, certain accounting policies of the Group were changed with details as set out in Note 4 to the financial statements. There were no significant impact on the profit and loss account nor the balance sheet of the Group for previous years except that impairment losses of goodwill arising on acquisition of subsidiaries and associates previously eliminated against reserves totalling HK\$481,640,000 were quantified and recognised retrospectively with details stated in Note 3 to the financial statements.

STAFF AND REMUNERATION

The Group had approximately 1,300 employees as at 31st December, 2001. Total staff costs incurred during the year amounted to HK\$412 million (2000 – HK\$381 million). The Group offered competitive remuneration packages to its employees. Certain employees of the Group were granted options under share option schemes of their respective companies. After the completion of the Disposal, total number of employees was reduced to approximately 800.

CONCLUSION

Following the Disposal and the Acquisition, the Group is currently interested in 64.6 per cent. of HKCL. HKCL and its subsidiaries, after the Disposal, has a very strong financial position and are well-positioned to take advantage of any good investment opportunities. The Group believes that the increase in the stake of HKCL would enhance the shareholders' value of the Company. Given the Group's strong financial position, it will continue to take a cautious approach in seeking further investment opportunities with attractive long-term returns.