

## FINANCIAL FOCUS

**Return on Equity** — Hsin Chong Construction Group Ltd. ("Company", together with its subsidiaries, "Hsin Chong") pays close attention to return on equity for both current businesses and new investment opportunities. Hsin Chong appreciates just being more profitable than other companies of the same industry may not be good enough for some investors. As a manager of public shareholders' capital, Hsin Chong aims to generate risk-adjusted returns on capital that are systematically acceptable to investors taking into account that construction is a cyclical industry. Historically, Hsin Chong's return on equity has ranged from 3.6% to 29.6% (except 1999, which reported a loss on equity of 6.0% due to the sizeable provisions for properties under development). Due to curtailment of the foundation operations which is unable to cover the fixed running cost and the impairment in value of unsold stock and investment properties, current year's loss on equity is 1.1%. It is disappointing comparing with Hsin Chong's track record and target of 15% and well below the specific target of 12% for the year.

**Capital Structure** — Hsin Chong historically adheres to a policy of conservative capital management. We believe a strong balance sheet affords more opportunities upon an industry upturn, inspires greater confidence amongst its clients, bankers, sub-contractors, suppliers and employees. Furthermore, since progress payments in the construction business inherently create high operating leverage, an overlay of high financial leverage over any extended period would not be prudent.

**Executive Remuneration** — Remuneration for executive directors and senior management of Hsin Chong is tied in a meaningful way to profitability. Your Board believes such incentive remuneration best

motivates its staff, aligns management's interests with shareholders' and minimises fixed salary expenses.

## ELEMENTS OF EXECUTIVE COMPENSATION

The compensation package for executive officers of Hsin Chong consists of the following basic elements:

**Base Salary** — The base salaries of executive officers of Hsin Chong are set on an individual basis and are designed to enhance Hsin Chong's ability to attract and retain highly qualified key executives. Salaries bear a direct relationship to the executive's level of responsibility and reflect his/her individual talents and skills.

**Annual Bonus** — The annual bonus paid to executive officers is a critical elements of compensation designed to reward the achievement of corporate goals, as well as individual productivity and performance. Amount of bonus is based upon performance of Hsin Chong during the year and upon the value to Hsin Chong and its shareholders of significant corporate accomplishments during the year, as well as upon the contribution of the individual executive to such performance and accomplishments.

**Share Options** — Share option awards provide the most significant element of long-term compensation from middle management staff to senior executives. Share options provide compensation in a manner that is intrinsically related to long-term corporate performance and stockholder's value, since the value of share options is determined solely by Hsin Chong's share price over the term of the option. Share option awards are discretionary determined by a variety of factors, including the level of responsibility and performance of the executive and his/her ability to affect share value.

**Retirement Plans** — Hsin Chong has designed a retirement benefit program to provide executives and employees with retirement compensation and at the same time promotes staff stability. Under the program, the employee contributes 5% of his/her basic monthly salary which is matched by Hsin Chong's contribution of 5–10%, depending only on the length of service. The retirement benefit programme, first established in 1973 is fully-funded and has received appreciative remarks from both working and retired staff.

Hsin Chong has established Hsin Chong Group Mandatory Provident Fund Scheme in December 2000 to conform with the requirements as stipulated in the Mandatory Provident Fund Schemes Ordinance.

## FINANCIAL POSITION

Hsin Chong maintains its policy of conservative capital management with balance sheet ratios and coverage ratios remaining at prudent levels. Debt to capitalization ratio is 24% at the balance sheet date (2001: 24%). Interest cover is at 6.8x (2001: 2.8x) with debt to cashflow cover of -3.4x (2001: 2.3x). Total bank borrowing amounted to HK\$232.4 million (2001: HK\$242.6 million), of which, 81% (2001: 94%) falls due after one year. The applicable interest rates for Hsin Chong's borrowing, which are largely at a spread to HIBOR, averaged 4.9%. Up to 30th June, 2002, total credit facilities available to Hsin Chong amounted to HK\$570.7 million with an undrawn balance of HK\$375.0 million. Land and buildings with a net book value of HK\$203.6 million (2001: HK\$212.7 million) have been pledged to secure a related mortgage loan. In respect of Guangzhou Wen Chang Square first phase development in which Hsin Chong has an effective interest of 42%, a project bank loan of RMB130 million is under negotiation. Hsin Chong's other financing requirements for the

coming year are expected to be met by available cash as at balance sheet date, cash generated by operations and bank credit facilities.

As of 31st March, 2002, net working capital amounted to HK\$333.5 million (2001: HK\$378.3 million). Cash balances and short term investments are 24% lower at HK\$603.7 million compared with last year end (HK\$794.3 million) with 88% (2001: 91%) as cash and cash equivalents. The Finance Committee has set out criteria on the credit ratings of financial institutions and the limits on counterparty exposures for placing fixed deposits. Actual exposures to each bank are closely monitored so as not to exceed the pre-set limit. In this way, counterparty exposures to banks with deposits placed are adequately managed.

## FINANCIAL HEDGING AND OTHER OFF BALANCE SHEET FINANCIAL INSTRUMENTS

With Hsin Chong's borrowings and cash balances primarily denominated in Hong Kong and US dollars, Hsin Chong has no significant exposure to foreign currency fluctuations. In addition, Hsin Chong adopts hedging policies for mitigating interest rate risk and exchange rate risk associated with respective assets or liabilities, rights or obligations. Such policies ensure effective cost controls on construction cost as early as at the tendering stage and controllable borrowing cost for operation and investment needs.

Interest rate risk and exchange rate risk are risks to earnings or capital arising from movement of respective rates. The former mainly arises from bank borrowings by Hsin Chong and the latter comprises exposure due to currency needs from normal business operation for material procurements and services requirements. Hsin Chong has established policies and procedures to the assessment, booking

and monitoring of all such off balance sheet financial instruments under limits approved by the Finance Committee. Such policies and procedures have been reviewed by the internal audit personnel and reported to the Audit Committee in June 1999. The controls and procedures governing such activities were overall considered adequate for their intended purposes.

Gain or loss arising from relevant hedging transactions will be booked against profit and loss associated with underlying assets or liabilities. For example, any differential interest receipts and payments, arising from interest rate swap agreements are accrued so as to match the net income or cost of such agreement with the related finance expenses from the underlying borrowings.

To date, none (2001: 23.8%) of Hsin Chong's long-term borrowings have been hedged by any interest rate swap agreement due to the easing of interest rate in light of the current or continuing slack economic weather. The Finance Committee pays close attention to financial markets and monitors market condition changes.

### **OPERATIONAL REVIEW ON CONTRACTS**

Over the past twelve months, the construction and civil engineering arms received HK\$2,322.3 million of new contracts with 78% derived from the private sector. Major awards in the private sector included IL8969 Cyberport Development at Telegraph Bay, Pokfulam, Hong Kong — Contract C3/C4, a construction contract for Cambridge House at 981 King's Road, Quarry Bay, a proposed Alteration and Addition Works at No. 3 Dai Kwai Street, Tai Po Industrial Estate and a proposed Residential Development at 117 Repulse Bay Road. The

remaining major new orders were the construction and foundation works for Shek Lei Estate Phase 12 from the Hong Kong Housing Authority, the construction work of Senior Citizen Residence at Jordan Valley for the Hong Kong Housing Society and a civil engineering contract in respect of the construction of Pok Wai Drainage Channel for the Drainage Services Department. The foundation subsidiaries, on the other hand, received few orders with a net sum of HK\$22.6 million.

Contracts totalling HK\$3,743.9 million were completed with HK\$3,498.4 million derived from the building construction and the balance from the foundations segment. Major completions included the design and construction work of Disciplinary Staff Quarters at Lee On Road, Kwun Tong for the Architectural Services Department, Tin Shui Wai Area



101 Phase 1 and Lai Chi Kok Phase 1 for the Hong Kong Housing Authority and three other contracts from the private sector, including the optic fibre factory at No. 3 Dai Kwai Street, Tai Po Industrial Estate and the residential developments at 5–7 Blue

Pool Road and 31 San Shan Road, KIL 11032 respectively.

The breakdown in outstanding contracts of Hsin Chong's construction subsidiaries is as follows:

	31/3/2001	Contracts Received	Contracts Completed	31/3/2002
	HK\$ million	HK\$ million	HK\$ million	HK\$ million
Building Construction and Civil Engineering Foundations	5,351.6 234.9	2,322.3 22.6	(3,498.4) (245.5)	4,175.5 12.0
Total	5,586.5	2,344.9	(3,743.9)	4,187.5

The split of outstanding contracts at the balance sheet date is as follows:

	Amount	%
	HK\$ million	
Government	937.1	22.3
Housing Authority	1,422.2	34.0
Public, Charitable or Non-Profit Institutions	29.2	0.7
Private Developers	1,799.0	43.0
Total	4,187.5	100.0

Profit before taxation for building construction and civil engineering increased by HK\$21.7 million to HK\$131.8 million. Major contributors included the HK\$2.1 billion Design and Build construction contract of Disciplinary Staff Quarters at Lee On Road, Kwun Tong (in which Hsin Chong have 60% share of interest) which was completed during the year.

With reduced turnover of 77.5% to HK\$29.5 million, the foundation operations incurred a loss of HK\$32.0 million this year (2001: HK\$73.9 million) due to uncovered fixed overheads such as depreciation cost of idle plant and machinery. On 18th June, 2002, the

board of directors of the foundation subsidiaries unanimously resolved to cease the foundation operations of Hsin Chong having regard to the current highly competitive and onerous contractual terms of such business.

#### BUILDING CONSTRUCTION AND CIVIL ENGINEERING

Both total turnover decreased by 28.2% to HK\$2,118.2 million and outstanding orders decreased by 22.0% to HK\$4,175.5 million for 2001/2002. However, profit margins improved to 6.2% in this year from 3.7% of last year.

Major contracts received during the year include:

Contract	Location	Type	Amount
			HK\$ million
Cyberport Development C3/C4	Telegraph Bay	Commercial	1,131.7
Cambridge House	Quarry Bay	Commercial	383.5
Senior Citizen Residence	Jordan Valley	Residential	272.8
Shek Lei Estate Phase 12	Shek Lei	Residential	141.0
Alteration and addition works at No. 3 Dai Kwai Street, Tai Po Industrial Estate	Tai Po	Industrial	118.9
Proposed residential development at 117 Repulse Bay Road	Repulse Bay	Residential	102.0
Pok Wai Drainage Channel	Yuen Long	Civil Work	51.0



Lai Chi Kok, Phase 1

Major contracts completed during the year include:



No. 3 Dai Kwai Street, Tai Po Industrial Estate

Contract	Location	Type	Amount
			HK\$ million
Disciplinary Staff Quarters at Lee On Road	Kwun Tong	Design and Build	2,075.9
Tin Shui Wai Area 101 Phase 1	Tin Shui Wai	Residential	611.3
Lai Chi Kok Phase 1	Lai Chi Kok	Residential	507.9
5-7 Blue Pool Road, Happy Valley	Happy Valley	Residential	187.7
Alteration and addition works at No. 3 Dai Kwai Street, Tai Po Industrial Estate	Tai Po	Industrial	118.9



Interior of optical fibre factory at No. 3 Dai Kwai Street, Tai Po Industrial Estate

## FOUNDATIONS

With thin volume of workload brought forward and minimal orders received during the year, turnover for the year decreased by 77.5% from last year to HK\$29.5 million. During the year, HK\$22.6 million new contracts were received against HK\$245.5 million completion. With order book decreased by HK\$222.9 million, contracts on hand reduced to a nominal level of HK\$12.0 million.



Major completions are mainly bored pile works including those subcontracted from the construction arm, namely, Disciplinary Staff Quarters at Lee On Road for HK\$102.1 million, Sewage Treatment Plant of Cyberport for HK\$37.0 million and the other piling contracts from outsiders, including 166–167 Wai Yip Street for HK\$31.7 million, Development Scheme K2 at Argyle Street/Shanghai Street — Site B for HK\$25.9 million, Lady Ho Tung Hall, The University of Hong Kong for HK\$19.6 million and Senior Citizen Residences at Tseung Kwan O Area 44 for HK\$15.6 million.

As referred to in note 32 to the accounts, the foundation operations ceased business subsequent to the year end.

## ASSOCIATES

With contracts on hand of HK\$598.2 million (2001: HK\$629.2 million), Hsin Chong Aster (the 50% owned building services associate) decreased its order book by 4.9% over last year's level. Building services contracts amounting to HK\$124.0 million were received with HK\$155.0 million completed. The principal awards included electrical and mechanical works for the Student Hostels Phase II Development of the City University of Hong Kong of HK\$45.4



million, Senior Citizen Residence at Tseung Kwan O Area 44 of HK\$19.2 million and Cyberport Development at Telegraph Bay, Pokfulam, Hong Kong — Contract C3/C4 of HK\$20.8 million.

The breakdown in outstanding contracts of Hsin Chong's construction associates is as follows:

	31/3/2001	Contracts Received	Contracts Completed	31/3/2002
	HK\$ million	HK\$ million	HK\$ million	HK\$ million
Hsin Chong Aster	629.2	124.0	(155.0)	598.2

Note: The amounts shown above are gross and do not reflect Hsin Chong's net attributable share.

**CONSTRUCTION RELATED PROPERTY DEVELOPMENTS****Lung Mun Oasis, Tuen Mun, Hong Kong**

At the balance sheet date, 270 carparking spaces remain unsold. These carparking spaces are currently available either monthly or on an hourly basis for rental income. In light of the restricted selling market for the carparking spaces (limited to owners of the Private Sector Participation Scheme development), a provision for diminution in value of HK\$21.9 million for the property assets was made during the year. To reduce Hsin Chong's administrative cost with aligned marketing strategy, Hsin Chong has acquired the remaining 15% interest in the development in December 2001 from the minority shareholder with the purchase consideration satisfied by the issuance of 4,000,000 shares of the Company.

**No. 3 Lockhart Road, Wanchai, Hong Kong**

The development is a 26-storey office building. Hsin Chong has a 20-year freely-assignable master lease for the 11th–30th floors, comprising approximately 77,000 square feet which is substantially let. Hsin Chong's cost thereof is amortised on a straight-line basis over 20 years. The residual lease term is around 12 years.

**Novotel Century Harbourview (formerly known as Century Harbour Hotel), Sai Wan, Hong Kong**

The property is a 3-star hotel with 276 rooms (including 12 suites). Hsin Chong has an effective interest of 22.5% in the investment at a carrying value of HK\$47.7 million (2001: HK\$47.1 million). As generally experienced by the hotel industry after the tragical 9-11 incident, the average achieved room rate decreased though it was compensated by high occupancy rate. However, the overall performance still needs to be improved and active measures are being taken.

**Hsin Chong Center, Kwun Tong, Hong Kong**

The property has been used as headquarter of Hsin Chong since April 1999 with some office space taken up by certain related companies on market rental.

**18A La Salle Road, Kowloon Tong, Hong Kong**

The luxury development, in which Hsin Chong holds a 25% interest comprises of six residential houses with gross floor area ranging from 5,544 square feet to 6,518 square feet each. One of these with gross floor area of 6,516 square feet was sold for HK\$46.8 million in April 2001. The project was re-launched in May this year and is being actively marketed both for sale and for rental.

**Guangzhou Wen Chang Square, PRC**

The project, comprising a total site area of 18,215 square metres (approximately 196,000 square feet) which is bound on the East by Wen Chang Road North, on the South by Yao Hua Jie North, Guangzhou City, PRC, is intended to be developed into residential units and shops in phases. Phase I comprises a total floor area of approximately 38,193 square metres for sale with 81 car parks at an estimated cost of approximately HK\$340 million. Hsin Chong has an effective 42% interest in the project.

To date, Hsin Chong's investment amounts to HK\$139.5 million (2001: HK\$129.5 million). In light of the slight market oversupply in Guangzhou City, a cumulative provision for impairment in value of HK\$59.5 million had been booked at the year end date. At the reporting date, banking facilities for the financing of the project cost amounting to RMB130 million is under active negotiation with a major bank.

**Taifeng Industrial Park, Tianjin, PRC**

Hsin Chong has a 95% interest in the intended development of 'standard ready for use' light industry factory buildings in Tianjin Economic Development Zone, Tianjin, PRC. The project's development cost is carried at HK\$23.9 million (2001: HK\$23.7 million). Development plans have been put on hold due to unattractive market conditions. As of today, a provision of HK\$17.0 million has been made for the impairment in value of the property interest.

**SuCasa Service Apartments, Kuala Lumpur, Malaysia**

SuCasa is a 180-room service apartments development with dining, recreational and parking facilities which commenced operations in 1993. Hsin Chong has an attributable 10% interest in SuCasa, carried at a value of HK\$10.1 million. Contribution from the investment is insignificant to Hsin Chong.

**Budi Ikhtiar, Kuala Lumpur, Malaysia**

Hsin Chong has an attributable interest of 20% in the site, which is a joint venture with the Mandarin Oriental Hotel Group. At present, development plans have been put on hold. Total costs remain unchanged at HK\$10.7 million, which is lower than current market value.

Changes in number of shares in issue are as follows:

Date	Number of Shares	Notes
1st April, 2001	637,198,827	Shares in issue
3rd July, 2001	875,079	Shares issued under Employee Share Subscription Scheme at HK\$0.43 each
27th December, 2001	4,000,000	Shares issued for the acquisition of 15% interest in Rife Yard Limited at HK\$1.09 each
3rd January, 2002	823,754	Shares issued under Employee Share Subscription Scheme at HK\$0.37 each
April 2001 – March 2002	(4,044,000)	Shares repurchased and cancelled under the Repurchase Mandate at prices ranging from HK\$0.42 to HK\$0.51 per share
31st March, 2002	638,853,660	Shares in issue

## MAJOR CONTRACTS AND PROJECTS SUBSEQUENT TO YEAR END

**Consolidated**

Subsequent to the year end, no major contracts and projects were awarded and completed. Overall, total outstanding contracts increased slightly to HK\$4,239.6 million as of 30th June, 2002.

**Associates**

No significant jobs were received or completed subsequent to the year end.

**SALE AND PURCHASE OF SHARES**

During the financial year, the Company's repurchase program resulted in a total repurchases and cancellations of 4,044,000 shares at an average price of HK\$0.46 per share. The Company also issued 1,698,833 shares under the Employee Share Subscription Scheme with prices at HK\$0.43 and HK\$0.37 per share. In addition, 4,000,000 shares were also issued for acquisition of interest in Rife Yard Limited. Apart from the above, there was no redemption, purchase, sale or cancellation of shares in the Company made by the Company or any of its subsidiaries during the financial year ended 31st March, 2002.