



Zen Wei Pao, William
Chairman

Dear shareholders,

The board of directors (the "Board") of the Company announces that the Group's audited turnover and share of turnover of jointly controlled entities for the year ended 31st December, 2003 was HK\$1,334 million (nine months ended 31st December, 2002: HK\$1,164 million) generating an audited consolidated profit for the year of HK\$124 million (nine months ended 31st December, 2002: HK\$87 million).

At the forthcoming Annual General Meeting to be held on 12th May, 2004, the Board will recommend the payment of a final dividend of HK5 cents (nine months ended 31st December, 2002: HK2 cents) and a special dividend of HK15 cents (nine months ended 31st December, 2002: Nil) per share.

BUSINESS REVIEW

Highway and Expressway

Road King Infrastructure Limited ("Road King"), an associate of the Group, contributed profit of HK\$103 million to the Group for the year ended 31st December, 2003 (for the nine months ended 31st December, 2002: HK\$86 million). The contribution for the year was stated after deduction of the Group's finance costs related to the highway and expressway division, the net loss on deemed disposal of partial interest in Road King and income released from negative goodwill arising from acquisition of additional interest in Road King.

Road King recorded an audited profit after taxation of HK\$318 million for the year ended 31st December, 2003 representing an increase of 1.8% as compared with that of year 2002. Following the persistent economic growth in China, car ownership in China is at a fast growing stage and traffic volume increased tremendously. The increase of traffic volume recorded in the second half of year 2003 not only compensated the revenue loss due to Severe Acute Respiratory Syndrome in the first half of the year but also exceeded Road King's annual forecast.



Highway



BUSINESS REVIEW (Cont'd)

Highway and Expressway (Cont'd)

During the year, the issued share capital of Road King increased by more than 10% because of the following new issues:

- (a) Stagecoach Asia Limited, one of Road King's substantial shareholders, converted mandatorily all its 418,380 preference shares of Road King to 48,876,168 ordinary shares of Road King ("Road King Shares") at a conversion price of HK\$8.56;
- (b) Options to subscribe for a total 10,625,000 Road King Shares were exercised by Road King's employees at the weighted average price of HK\$3.21 per share;
- (c) Warrants for 6,534,189 Road King Shares were exercised at HK\$5 per share; and
- (d) A placement of 2,500,000 Road King Shares at HK\$4.8 per share.

Therefore, despite that the Group purchased 1,552,000 Road King Shares at the weighted average price of HK\$5.56 per share throughout the year, the Group's overall interest in Road King was effectively reduced from 49.1% as at 31st December, 2002 to 43.6% as at 31st December, 2003. As the overall weighted average price of the above movements of Road King Shares was lower than the carrying value of Road King in the Group, which was about HK\$8 per Road King Share, the Group recognized a net loss of HK\$23 million from the overall reduction of interest in Road King.

Road King continues to expand its portfolio of highway projects. In September 2003, Road King completed the acquisition of 40% interest in toll collection and operation rights of Baoding-Tianjin Expressway project in Hebei Province.

In addition, Road King also signed a conditional agreement in March 2004 with a PRC partner to acquire 45% in toll collection and operation rights in Tangshan to Tianjin Expressway in Hebei Province. The transfer application was already submitted to relevant government authorities for approval.

On the financial front, Road King's cash and bank balances at the end of the year maintained at HK\$488 million, after capital investments on new highway projects of over HK\$900 million during the year.

Construction

The turnover and share of turnover of jointly controlled entities of construction division was HK\$1,207 million for the year ended 31st December, 2003 (nine months ended 31st December, 2002: HK\$1,047 million). The construction division recorded profit from operations of HK\$63 million (nine months ended 31st December, 2002: HK\$15 million) and contributed net profit of HK\$40 million (nine months ended 31st December, 2002: HK\$19 million) to the Group for the year.



Construction



BUSINESS REVIEW (Cont'd)

Construction (Cont'd)

In the Company's Interim Report 2003, we point out the fact that due to budget deficit, it is unlikely that the construction market will be able to recover in the near future and to date we still maintain this view. It is not in the interest of the shareholders to join the battle of cutthroat competition and so far we have been able to avoid such action. As a result, we have to be prepared for a lower turnover in the coming years.

The current government procurement policy (since November 2002) in awarding contracts to contractors on a combination of contractors' past performance and financial offer is a welcome signal. Our strategy in improving all current project performance is paying off as we have been awarded few contracts even though we were not the lowest tenderer. It is our long term commitment to provide client with "value for money" and we are glad that government is taking the lead in the right direction.

Our attempt to enter into markets outside Hong Kong is still an uphill battle. Our medium term objective is to have one third of our turnover outside Hong Kong by year 2008. The figure for year 2003 is 8%, so we need to step up our effort. In China we wish to focus on environmental projects, and we are also actively looking at opportunities elsewhere in places like Dubai, where entry barrier is not high and procurement system is transparent and fair.

The award on arbitration with Housing Authority ("HA") was handed down in September 2003. Subsequent to the award, Zen Pacific Civil Contractors Limited ("ZPCCL") signed an agreement with HA to settle the whole issue by ZPCCL paying HK\$80 million to HA for a full and final settlement. With this problem behind us, we can fully concentrate on looking forward through the windshield rather than looking in our rear mirror.

We are not pessimistic about the future of our construction sector. We strongly believe that there is always a need for good quality construction work. The challenge is to identify clients who have the same philosophy on value for money and then deliver our best service possible.

As of the date of this report, the construction division had contracts on hand of about HK\$7,652 million of which HK\$965 million has yet to be completed.

Quarrying

The turnover of quarrying division was HK\$128 million for the year ended 31st December, 2003 (nine months ended 31st December, 2002: HK\$122 million). The quarrying division recorded profit from operations and contributed net profit to the Group of HK\$9 million for the year ended 31st December, 2003 (nine months ended 31st December, 2002: HK\$21 million).

The production and sale of quarry products in Hong Kong in year 2003 was 1.9 million ton, and we believe there will not be any increase in volume in the coming year. Competition is still very keen, but with concrete market recovering in the last six months, hopefully this will have some positive impact on our sales price. However, quarrying is a mature business in Hong Kong and the best one can hope in the near future is to maintain our position.



Quarry



BUSINESS REVIEW (Cont'd)

Quarrying (Cont'd)

Our operation so far in Shanghai is not a success and in fact last year the Group recorded a loss for the pure quarrying business there. Although the need for high quality aggregate is well recognized, yet the sales price does not reflect the same. As a result in the near future, we do not intend to invest more into quarrying business in China, except when good opportunities come knocking at our door.

Bio-technology

Wuhan Nature's Favour Bioengineering Company Limited ("Nature's Favour") has now obtained full production and distribution licenses for five bio-pesticide products. We expect that full licenses will be granted to another three new products shortly. With these, Nature's Favour is actively producing and promoting its own developed products. Production is now in full swing. With experience gained in year 2003 and the expansion of product lines, the sales team is well positioned to market our own products through established distribution network in over twenty provinces/cities in China and is actively soliciting overseas sales orders. It is anticipated that the results of Nature's Favour in year 2004 will be satisfactory.

The research and development ("R&D") team of Nature's Favour is now forty-five people strong. With the dedicated guidance and invaluable experience of the technical advisory committee consisting of two academics from the Chinese Academy of Science and five doctoral study supervisors, the R&D team is committed to develop at least three new products a year, enriching the product lines of Nature's Favour.

Property Development Projects with Government

The Group had interests in two property development projects with government, one in Kwai Shing Circuit and another in Hung Hom Bay. Property construction for both projects were completed in year 2002. As a result of post development costs, the Group shared a net loss of HK\$9 million from its interests in these property development projects for the year ended 31st December, 2003 (nine months ended 31st December, 2002: HK\$28 million).

With the change of government policy in respect of home ownership scheme projects, the property development project in Kwai Shing Circuit was converted to public rental housing and the government purchased the residential area and the car parking spaces thereof in April 2003.

In January 2004, the government offered an opportunity to change the property development project in Hung Hom Bay to a private sector project. As the Group is not a private property developer and has no expertise in the development, sales and marketing of private property development, the Group disposed of its interest in this property development project to a subsidiary of Sun Hung Kai Property Limited in February 2004 for an aggregate consideration of HK\$597 million. In view of the cash generated and the fact that minimum dividends were paid out in the last few years, the Board recommends to pay a special dividend of HK15 cents per share.



Bio-Technology



FINANCIAL REVIEW

Liquidity and Financial Resources

During the year, the Group managed to reduce its total borrowings significantly from HK\$248 million to HK\$184 million with the maturity profile summarised as follows:

	As at 31st December,	
	2003	2002
	HK\$' million	HK\$' million
Within one year	104	173
In the second year	40	50
In the third to fifth year inclusive	40	25
	<u>184</u>	<u>248</u>

Major reduction of the total borrowings during the year was related to the settlement of financial obligations associated with the Group's interests in the two property development projects. As at 31st December, 2002, the total outstanding liabilities of such financial obligations were HK\$72 million. The amount was fully settled by internal resources and bank financing during the year.

As at the balance sheet date, there was a three years term secured bank loan of HK\$100 million, of which HK\$80 million is due after one year. However, the loan was subsequently settled in full with cash generated from the disposal of the property development project in Hung Hom Bay.

As at 31st December, 2003, the Group's cash and bank balances amounted to HK\$110 million, of which HK\$55 million bank deposits were pledged to secure bond and banking facilities granted to the Group and jointly controlled entities. Of the bank deposits pledged at the balance sheet date, an aggregate amount of HK\$18 million was subsequently released.

The Group's net finance costs for the year ended 31st December, 2003 was HK\$16 million (nine months ended 31st December, 2002: HK\$16 million).

The Group's borrowings and cash balances were principally denominated in Hong Kong dollars and Renminbi. Hence, there is no significant exposure to foreign exchange rate fluctuations. During the year, the Group had no borrowing at fixed interest rate and had no financial instrument for hedging purpose.

FINANCIAL REVIEW (Cont'd)**Capital Structure and Gearing Ratio**

The net gearing ratio, being the ratio of net borrowings (total borrowings less cash and bank balances) to shareholders' funds, was reduced from 6.4% to 3.6% during the year. As at 31st December, 2003, the shareholders' funds amounted to HK\$2,063 million (HK\$1,959 million as at 31st December, 2002), representing HK\$2.63 per share (HK\$2.52 per share as at 31st December, 2002). Increase in shareholders' funds was mainly attributable to profit retained after dividend paid and increase in share capital and share premium upon exercise of share options by employees. The financial position of the Group improved substantially upon disposal of the Group's interest in the property development project of Hung Hom Bay in February 2004.

Pledge of Assets

As at 31st December, 2003, apart from the bank deposits pledged to secure banking facilities granted to the Group, 46.5 million Road King Shares were pledged to secure counter indemnities and undertaking given by the Company to Chow Tai Fook Enterprises Limited ("CTF") for payment, discharge and performance of indebtedness, liabilities and obligations related to the Group's interests in two property development projects with government. In addition, a total of 180 million Road King Shares were pledged to banks to secure the three years term bank loan and other banking facilities granted to the Group and an associate. Subsequent to the balance sheet date, a total of 220 million Road King Shares were discharged and released from CTF and banks.

Contingent Liabilities

The Group had contingent liabilities amounting to HK\$1,623 million as at 31st December, 2003 (HK\$579 million as at 31st December, 2002) related to banking facilities granted to an associate and a jointly controlled entity as well as tender, performance and retention bonds issued to customers in respect of outstanding construction contracts. The substantial increase in contingent liabilities was mainly due to the guarantees with an aggregate amount of HK\$1,119 million given by the Company for a banking facility and performance bonds in respect of the Group's interests in the two property development projects with government. Of the total amount of contingent liabilities as at 31st December, 2003, an aggregate amount of HK\$1,293 million was released after the balance sheet date.

EMPLOYEES AND REMUNERATION POLICIES

As at 31st December, 2003, the Group had 1,032 employees (795 employees as at 31st December, 2002), of which 698 (615 as at 31st December, 2002) were located in Hong Kong, 311 (148 as at 31st December, 2002) were located in Mainland China and 23 (32 as at 31st December, 2002) were located in Taiwan.

Competitive remuneration packages are structured to commensurate with individual responsibilities, qualification, experience and performance.

FUTURE OUTLOOK

Car ownership in China has been growing rapidly, resulted in significant increase in traffic volume in highways. Road King is well positioned to reap the benefit therefrom. The Board has no reservation in Road King's approach in expanding its network of profitable highways.

The depressed economy and property market in Hong Kong have affected the performances of both the construction and quarrying divisions. Nevertheless, it is apparent that the steps taken by both divisions in the last two years to restructure and streamline their operations have taken effect, as both divisions have been making positive contributions to the Group despite the poor market conditions.

The Group is now in a cash surplus position and is free to make investments whenever appropriate opportunities arise. Nevertheless, management will still maintain a cautious approach in selecting appropriate investment targets within the Group's core and related businesses.

APPRECIATION

With our committed and diligent staff, the Board is optimistic on the Group's performance and future. The Board would like to take this opportunity to extend its heartiest thanks to the entire loyal and dedicated staff.

Zen Wei Pao, William
Chairman

26th March, 2004