

# CHAIRMAN'S REPORT

The global economy is in the midst of a deep downturn caused by an unprecedented financial tsunami in 2008. The precipitous decline in trade activities across the globe is consequently damaging the international shipping industry. Responding to this dramatic worsening market, COSCO Pacific is maintaining its prudent business strategy in order to meet challenges ahead and is pleased to announce that it has achieved a stable financial performance in the difficult year of 2008. During the year, the Group expanded its global terminal network and increased the controlling right in its terminal portfolio. Meanwhile, the Group further optimised the capital structure of its container leasing division by an asset light strategy. These achievements have further strengthened the Group's leading positions in the industries in which it is engaged.

Looking ahead, 2009 is expected to be a year with unprecedented challenges. The global recession has generated historic decline in trade volumes which has inevitably resulted in a further decline in container terminal throughput. During the first two months of 2009, China trade volume and China major ports throughput declined by 27.2% and 15.0% respectively, compared with the same period in 2008, resulting in a substantial impact on the Group's core businesses. The terminal and container leasing industries are facing relatively a sharp market contraction of which is highly likely to last for the year of 2009.

With our expertise in the shipping and port industries and the capital market, we are well equipped to meet challenges ahead. COSCO Pacific is maintaining its prudent financial policy with risk management playing an important part of its long term planning. Moreover, with the strong support from COSCO, China COSCO's shipping fleet and COSCO Pacific will fully leverage their business synergy so as to strengthen their core competence. The Group will also further strengthen its cooperation with terminal business partners so as to overcome difficulties arising from the volatile markets. COSCO Pacific makes its dedicated efforts to provide the most efficient container terminal handling and container leasing services to our customers. The Company believes that it is well positioned to benefit immediately from the recovery of market and to make solid progress towards its long-term development targets.

**COSCO Pacific is confident that its long range planning will steer it through the current financial storm and should be beneficial to its long term stability and lead to a solid profitability for its shareholders.**



Dear Shareholders,

I am pleased to report that despite the difficult global economic and market situation, COSCO Pacific continued to achieve a stable business performance in 2008. On behalf of the Board of Directors, I would like to take this opportunity to thank all of you and our business partners for your unfailing support, as well as all of our staff for their untiring efforts and valuable contributions to the accomplishment of our goals and targets.

## 2008: AN EVENTFUL YEAR

In 2008, the most severe financial crisis in the past fifty years resulted in a global credit crunch which substantially impacted the economy. During the year, the global economic growth slowed down to 3.4% from 5.2% in 2007.

China economic growth also slowed down to 9.0% in 2008 from 13.0% in 2007. What caused concerns was that the growth rate slowed down to just 6.8% in the fourth quarter, the slowest quarterly growth in the past seven years. This slowing trend extended to the first quarter of 2009. The contraction in economic activities around the world resulted in a slowdown in growth of China's external trade. Total China trade amounted to US\$2,561.6 billion for the full year of 2008, with growth rate slowed down by 5.7 percentage points year-on-year to 17.8%. The total throughput of China major ports reached 126 million TEUs while the growth rate slowed down by 9 percentage points year-on-year to 12.2% in 2008.

Growth of the global container shipping volume also decelerated in 2008. According to estimates from Drewry Shipping Consultants Limited, the global container traffic rose 7.2% to 153 million TEUs in 2008, 4.8 percentage points slower than that in 2007. Due to the plunge in the demand for container shipping services, shipping companies had to reduce shipping capacity in the fourth quarter of 2008 so as to curtail operating costs on this front. The Group's terminal and container leasing businesses are under considerable pressure. The situation is expected to become more critical in 2009.

## STABLE PERFORMANCE IN 2008

Since the fourth quarter of 2008, COSCO Pacific's terminal and container leasing businesses have been affected by the slow down of the global economy and shipping industry. As a result, the growth of the Group's terminal throughput and the expansion of container fleet slowed down. Throughput for 2008 recorded a year-on-year increase of 17.7% (2007: 20.4%) to 45,878,875 TEUs (2007: 38,982,605 TEUs). The container

fleet size increased by 101,551 TEUs to 1,621,222 TEUs, representing a year-on-year increase of 6.7% (2007: 21.5%). The utilisation rate remained at 94.6% (2007: 94.5%). COSCO Pacific maintained its ranking as the fifth largest container terminal operator and the second largest container leasing company in the world.

Profit attributable to the equity holders of the Company for the year was US\$274,725,000 (2007: US\$427,768,000). If the non-recurring gain of financial gain of US\$55,181,000 in relation to the put options of CIMC and the profit of US\$90,742,000 from disposal of our equity interest in Chong Hong Bank in 2007 are excluded, the profit attributable to the equity holders of the Company in 2008 should have declined only slightly by 2.5% year-on-year.

## DIVIDEND DISTRIBUTION

The Company has always been committed to enhancing shareholders' returns. Since becoming a constituent stock of the Hang Seng Index in 2003, it has maintained a dividend payout ratio of about 56%. While making a decision on the payout of dividends, the Board of Directors took into account the supply of capital required for the Company's development. In view of the economic downturn in 2008 generating uncertainties for the economic and capital market outlook in 2009, we expect the financial sector to remain under heavy strain making the funding of capital to be difficult and the cost of capital to be likely increased.

Very careful consideration has been given to the persistent illiquidity of the financial market, resulting in the Board of Directors' decision to moderately adjust the dividend payout ratio to 40.0% (2007: 56.6%) so as to retain more cash for the Company. The Board has proposed a final dividend of HK10.7 cents per share for the fiscal year 2008. Together with the interim dividend of HK27.4 cents per share paid on 19th September 2008, the full-year dividend for 2008 will be HK38.1 cents per share, down by 48.1% from the prior year.

In addition, the Company is providing a scrip dividend alternative so that our shareholders may have a choice of reinvesting their cash into our Company. This is the first time the Company will provide its shareholders with a scrip dividend alternative. In addition to preserving cash for the Company, this arrangement provides long-term shareholders a chance to reinvest in the Company. Management of the Company is confident that the dividend payout ratio is still relatively high among peer companies following the adjustment and we will consider increasing the ratio when the market recovers.

### REINFORCING CORPORATE DEVELOPMENT STRATEGY

In June 2008, Dr. Wei Jiafu resigned as Chairman of the Board and a non-executive director of the Company in order to have more time to pursue his duty as the president and CEO of COSCO and the chairman and CEO of China COSCO. With great honour, I was appointed by the Board to take over Dr. Wei's role as Chairman of the Board, fully aware of what a Herculean task I have been entrusted with.

Since June 2000, Dr. Wei dedicated his efforts in optimising the Group's asset structure as well as its business model and placed great emphasis on corporate governance and management, through which he built a solid foundation for the Company's business development, leading the COSCO Pacific team from one achievement to another and generating good returns for shareholders. During his tenure, Dr. Wei also substantially strengthened the Company's leading position in terminal and container leasing industries. In 2003, COSCO Pacific became a constituent stock of the Hang Seng Index. From 2000 to 2007, the Company's profit attributable to equity holders grew at a compound annual growth rate of 17.3%.

I, on behalf of the Board of COSCO Pacific and its staff, would like to take this opportunity to extend our heartfelt thanks and sincere tributes to Dr. Wei for his achievements over the past eight years.

Going forward, I will continue to reinforce COSCO Pacific's stated strategy. Whilst further strengthening the leading position of the Group's core businesses, I will also endeavour to develop the terminal business to be our principle earnings driver and further enhance our global terminal network so as to provide efficient terminal services to shipping companies.

### TERMINAL BUSINESS: SOLIDLY MOVING FORWARD

In 2008, COSCO Pacific continued to implement its transformation strategy for the development of the terminal business. The four key components of this strategy included the increase in controlling rights in terminals, expansion of the global terminal network, further diversification of the terminal portfolio and enhancement of value of its terminal business. However, the world economy started slowing down dramatically in the fourth quarter of 2008. In response to such a rapid change in the market, the Group has adjusted its pace of investments in new terminals in 2009.

### Four key components of the transformation strategy

#### Control - Increasing the controlling rights in terminals:

The Group has transformed its terminal development strategy from an investment-based model to a control-based model by obtaining controlling stakes in new terminal investments. In 2008, the Group successfully bid for a concession to operate and develop Piers 2 and 3 of the Piraeus Port in Greece. This brings the total number of terminals in which the Group holds controlling stakes to six.

The other five are the 51% interest in Zhangjiagang Win Hanverky Terminal, the 55.59% interest in Yangzhou Yuanyang Terminal, the 71.43% interest in Quan Zhou Pacific Terminal, the 80% interest in Jinjiang Pacific Terminal, and the 70% interest in Xiamen Ocean Gate Terminal. Two berths under construction at Xiamen Ocean Gate Terminal are expected to be in trial operation by 2011.

As at 31st December 2008, the Group held various equity interests in 28 terminal companies, among which 22 were operating. Based on the Group's equity interest in each terminal company, its equity throughput reached 9,973,805 TEUs in 2008, up 22.8% year-on-year, which represents 21.7% of the Group's overall total throughput, up 0.9 percentage point year-on-year.

## **Globalise - Expanding global terminal network:**

The Group has adjusted its investment targets from solely focusing on China's terminals market to being a global player with the China market as its core and has committed to further expanding its global terminal network. In June 2008, the Group won the privatisation tender for Piers 2 and 3 of the Piraeus Port in Greece, and received a 35-year concession to operate and develop these two piers from 1st October 2009.

Following COSCO-PSA Terminal, Antwerp Terminal and Suez Canal Terminal, Piraeus Terminal became the fourth overseas terminal invested in and operated by the Group. The three overseas terminals handled a combined throughput of 4,731,456 TEUs in 2008, up 143.2% year-on-year, accounting for 10.3% of the Group's overall total throughput, an increase of 5.3 percentage points from 2007.

## **Diversify - Further diversifying terminal portfolio:**

The Group has diversified its terminal portfolio from investing solely in container berths to a portfolio with investments in break-bulk cargo or multi-purpose berths. This diversification serves to lower the Group's investment risks and to expand its sources of income. During the year, one break-bulk cargo berth at Jinjiang Pacific Terminal commenced operation. The Group continues to study the investment opportunities in some ports and terminals with great potential to enhance the profitability of its terminal division.

## **Enhancement - Maximising value of terminal business:**

The Group attaches great importance to mid to long-term development in its terminal portfolio. In order to enhance the enterprise value of COSCO Pacific, we move from a profit-centric strategy, to value-maximising strategy. The entry barrier of investment in terminal is relatively high. Terminal investment requires certain amount of committed capital and the construction of a new terminal takes a longer time. However, after the ramp-up period of operation, a terminal will be capable to generate stable cash flow with an attractive investment return. Therefore, the Group evaluates the return of terminal investment with a mid to long-term perspective.

Besides, geographical location is a critical success factor of a terminal operation. Prime locations are considered as scarce resources. The Group will continue its efforts on studying investments in quality ports and terminal assets. However, the current global economic downturn has exposed terminals investment to more uncertainties that will likely induce certain investment risks and higher cost of capital. Therefore, the Group has deferred new terminal investments since the fourth quarter of 2008 and is taking substantial review on modifying its existing terminal investment plan and the valuation of related projects.

### **STRENGTHENING RISK MANAGEMENT**

While dedicating its efforts in developing core businesses, the Group also attaches great importance to risk management. In the first half of 2008, with the emergence of the US sub-prime mortgage crisis, many financial institutions became saddled with huge losses, which led to a problematic US economy. The Group has always kept on monitoring the potential impact of the global economy and market conditions on the operational performance of its businesses and has instructed all senior management team to be fully aware of the importance of risk management. Furthermore, the Group studies intensively the measures of how to monitor investment risks, operational risks and financial risks by consulting the Investment and Strategic Planning Committee, Risk Management Committee and Audit Committee of the Board.

Whilst exercising prudence in relation to financial planning, COSCO Pacific's senior management team also closely monitors the Company's gearing ratio, interest cover ratio, debt structure, financial risks, dividend policy and financing strategy, so as to provide a strong financial position for the future development of the Company.

### **ATTACHING GREAT IMPORTANCE TO CORPORATE GOVERNANCE**

COSCO Pacific has always been striving for practicing good corporate governance to protect the long term interests of the Company and its shareholders. Meanwhile, the Company strongly believes that a successful and well respected company should make its utmost effort to be a good corporate citizen. The Company has been continually strengthening

the supervising function of the Board of Directors, and is committed to improving its corporate governance structure so as to take all necessary steps to prevent any possible fraud and other irregularities.

The financial tsunami has triggered collapses of various financial institutions. This had led to a plunge of investors' confidence in the market. Corporate governance and enhanced transparency have become particularly important to win their confidence. COSCO Pacific is very stringent in compliance with regulatory rules on the disclosure of Company's financials, results performance and particularly on the accuracy of information disclosed. It also takes the initiative of releasing the Company's quarterly results and updating terminals throughput on the corporate website on a monthly basis, in order to effectively communicate the latest information about the Company to its stakeholders. These initiatives have won wide acclaim from the market.

During the year, the Company received the Corporate Governance Asia Recognition Award from the Corporate Governance Asia magazine and one of the best companies in China in the Corporate Governance Award from The Asset magazine. The Company was also awarded the Hong Kong Outstanding Enterprise by the Economic Digest (Hong Kong) magazine. In addition, COSCO Pacific attaches great importance in enhancing shareholder returns. As a result, the Company became a constituent stock of the Dow Jones Global Select Dividend Index, Dow Jones EPAC Select Dividend Index, and Dow Jones Asia/Pacific Select Dividend 30 Index in November 2008.



## 2009 WILL BE A YEAR WITH UNPRECEDENTED CHALLENGES

Looking ahead, 2009 is expected to be a challenging year. According to the forecast by the International Monetary Fund, the global economy is expected to contract by 0.5% to 1.0% in 2009, the first decline in 60 years. The world trade volume (including goods and services) is also expected to slow down from 4.1% in 2008 to a negative growth of 2.8% in 2009. According to Drewry Shipping Consultants Limited, the global container traffic growth will drop to 2.8% in 2009, from 7.2% in 2008.

China's external trade has also deteriorated. During the first two months of 2009, China trade volume and China major ports throughput declined by 27.2% and 15.0% respectively in comparison with the same period in 2008, resulting in a substantial impact on the Group's core businesses that led to a 7.8% decline in the container terminal throughput. The terminal, container leasing and container manufacturing industries are in a difficult situation which is highly likely to last for the full year.

China plays a critical role in stimulating the global economy. Premier Wen Jiabao said in the Second Session of the 11th National People's Congress on 5th March 2009 that one of the major working plans of the government includes a substantial increase in government investment. A RMB 4 trillion investment plan will be implemented over two years, including RMB 1.18 trillion of structural tax reductions to boost domestic demand and consumption. Large scale stimulation plans for specific industries will also be implemented to enhance the overall competitiveness of the country. Premier Wen also stated clearly that China's GDP growth for 2009 is expected to be around 8%.

It remains uncertain on when the economy will start to recover. In order to deal with challenges ahead, COSCO Pacific maintains its prudent financial policy while risk management playing an important part of its long term planning.

COSCO, the ultimate parent company of COSCO Pacific, is the largest shipping enterprise in China and the second largest in the world. Of this giant's shipping fleet, China COSCO manages and operates its bulk and container shipping fleets as the largest bulk cargo shipping fleet and the sixth largest container shipping line in the world. With our expertise in the shipping and port industries and the capital market, we are well equipped to meet challenges ahead. Moreover, with the strong support from COSCO, our ultimate holding company, China COSCO's shipping fleet and COSCO Pacific will fully leverage their business synergy so as to strengthen their core competence.

The Group will also further strengthen its cooperation with terminal business partners so as to overcome difficulties which have arisen from the volatile markets. COSCO Pacific makes its dedicated efforts to provide the most efficient container terminal handling and container leasing services to our customers. Our senior management believes that it is well positioned to benefit immediately from the recovery of market and to make solid progress towards its long-term development targets.

COSCO Pacific is confident that its long range planning will steer it through the current financial storm and should be beneficial to its long term stability and lead to a solid profitability for its shareholders.

Last but not least, I would like to take this opportunity to show my deepest gratitude for the trust from shareholders and support from COSCO, China COSCO and affiliated companies, and business partners. My sincere thanks also goes to members of the Board and all staff at COSCO Pacific for their contribution to the Company's business development in 2008.



CHEN Hongsheng  
Chairman  
8th April 2009

