

OPERATIONAL REVIEW – CONTAINER LEASING, MANAGEMENT AND SALE

In the face of intense competition in the market and the global economic slowdown, the Group continued to expand its container fleet in a steady pace through an asset light business model, thus further solidified its leading position in the industry. In 2008, Florens, a wholly-owned subsidiary of COSCO Pacific, continued to rank as the world's second largest container leasing company. With a fleet size of 1,621,222 TEUs (2007: 1,519,671 TEUs), Florens captured approximately 13.6% (2007: approximately 13.2%) of the global container leasing market. During the year, the profit contribution from container leasing, management and sale businesses rose 19.5% year-on-year to US\$141,055,000 (2007: US\$117,994,000).

Moving into 2009, the global economic downturn is expected to further exacerbate. Confronted with a very difficult business environment, the Group will take a prudent yet proactive approach in handling upcoming challenges. It will come up with appropriate measures to effectively control risks and plan ahead for the recovery of the economy.



MARKET REVIEW

Given the increasing demands by shipping companies, the container leasing market was generally active from January to September 2008. Starting from mid-October 2008, the overall demand for leased containers plunged dramatically as a result of the financial tsunami and the global economic slowdown.

According to the February 2009 issue of Containerisation International, the new vessels deliveries in 2008 totalled 1,503,000 TEUs (2007: 1,300,000 TEUs), which led to an increase in demand by shipping companies for containers. However, the price of new containers was generally high in 2008 given the increasing price in raw materials, energy and rising labour costs. The ex-factory price of a new 20-foot dry container soared up to US\$2,600 in August 2008. Shipping companies therefore cut back on their purchase of new containers and instead leased containers from leasing companies in the first half of 2008. In the third quarter of 2008, the financial tsunami triggered by the US subprime mortgage crisis swept across the world. Signs of depression emerged in the developed economies and the financial crisis made a quick intrusion into the emerging economies as well. In the wake of this, tightening of capital flow was seen in the global capital markets and tightening of credits by banks resulted in high financing costs for businesses. All these contributed to a plunge in exports and imports. To control costs, shipping companies adjusted their capacities, which led to a drastic drop in the demand for leased containers.

The world's top 10 container leasing companies in 2008

Fleet size (TEUs)
and market share

Textainer Group	2,050,000 (17.1%)
COSCO Pacific (Florens)	1,621,222* (13.6%)
Triton Container	1,500,000 (12.5%)
TAL International	1,060,000 (8.8%)
Seacastle Container	980,000 (8.2%)
GE SeaCo	950,000 (7.9%)
CAI	780,000 (6.5%)
UES International (HK)	500,000 (4.2%)
Gold Container	480,000 (4.0%)
Cronos Group	460,000 (3.8%)

Source: World Cargo News (August 2008)

*The container fleet size of Florens as at 31st December 2008

The world's top 10 container lines in 2008

Fleet capacity (TEUs)
and market share

Maersk Line	1,865,603 (13.1%)
MSC	1,468,713 (10.3%)
CMA CGM	1,001,386 (7.0%)
Evergreen	629,312 (4.4%)
Hapag-Lloyd	496,724 (3.5%)
COSCON	496,000* (3.5%)
APL	474,453 (3.3%)
CSCL	420,562 (2.9%)
NYK	407,208 (2.9%)
Mitsui O.S.K. Lines	374,059 (2.6%)

Source: CI Online (February 2009)

*The fleet capacity of COSCON as at 31st December 2008

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BUSINESS REVIEW

COSCO Pacific's container leasing, management and sale businesses are operated and managed by its wholly-owned subsidiary, Florens. In the face of intense competition in the market and the global economic slowdown, Florens further streamlined its asset light business model, which comprises owned, managed and sale-and-leaseback containers. Florens steadily expanded its container fleet, and further strengthened its leading position in the industry. During the year, Florens remained the world's second largest container leasing company, accounting for approximately 13.6% (2007: approximately 13.2%) of the global container leasing market and continued to provide quality container leasing services for international container lines.

As at 31st December 2008, the fleet size of the Group's owned, managed and sale-and-leaseback containers reached 1,621,222 TEUs (2007: 1,519,671 TEUs), representing a year-on-year increase of 6.7%. The fleet size of the owned containers was 747,202 TEUs (2007: 757,053 TEUs), accounting for 46.1% (2007: 49.8%) of the total container fleet. The size of the managed container fleet reached 755,926 TEUs (2007: 762,618 TEUs), or 46.6% (2007: 50.2%) of the total fleet. The size of the sale-and-leaseback container fleet reached 118,094 TEUs (2007: nil), or 7.3% (2007: nil) of the total fleet.

As at 31st December 2008, 551,219 TEUs (2007: 517,311 TEUs) of containers were made available to COSCON, among which 433,125 TEUs (2007: 517,311 TEUs) were owned containers and 118,094 TEUs (2007: nil) were sold and leased back by the Group. Containers made available to international customers amounted to 1,070,003 TEUs (2007: 1,002,360 TEUs), among which owned containers were 314,077 TEUs (2007: 239,742 TEUs) and the managed containers were 755,926 TEUs (2007: 762,618 TEUs).

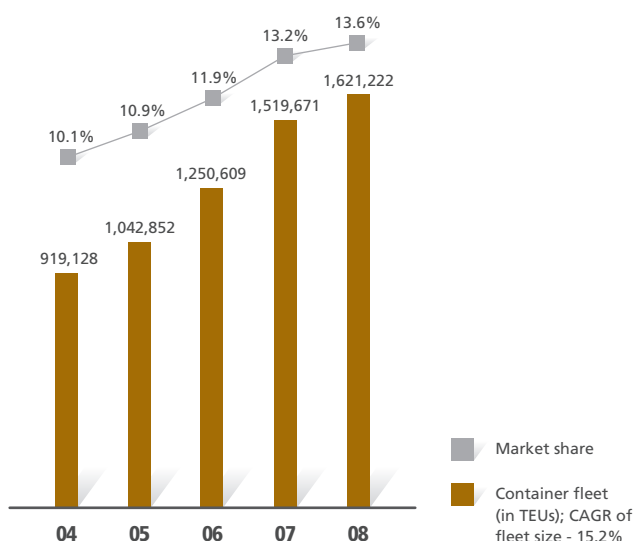
Whilst expanding its business in the sale-and-manage-back model, the Group kept abreast of the market developments and continued to develop its owned container fleet. During the year, the Group purchased 152,752 TEUs (2007: 326,715 TEUs) of new containers, of which 64,802 TEUs (2007: 112,754 TEUs) were ordered for COSCON, accounting for 42.4% (2007: 34.5%) of the Group's total new purchase of the year. The remaining 57.6% (2007: 65.5%) or 87,950 TEUs (2007: 213,961 TEUs), were for international customers.

As at 31st December 2008, the Group had a customer base of 300 companies (2007: 280). In 2008, the overall average utilisation rate was 94.6% (2007: 94.5%). The average fleet age was 4.15 years (2007: 3.75 years).

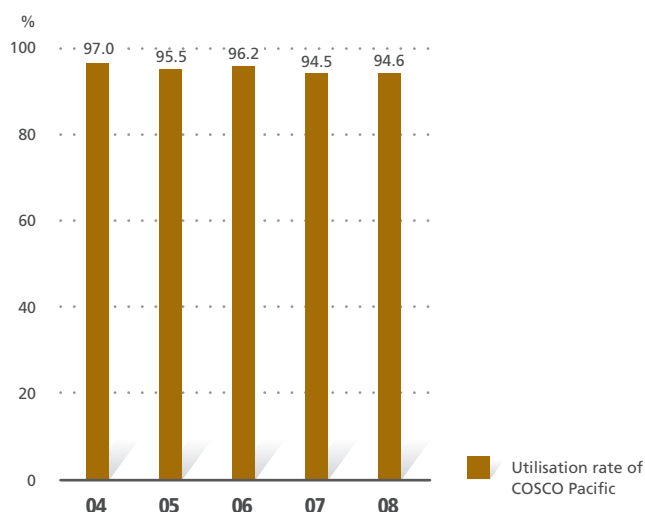
Breakdown of owned, managed and sale-and-leaseback containers (in TEUs)

	Owned Containers	Managed Containers	Sale-and-leaseback Containers	Total
As at 31st December 2008				
COSCON	433,125	-	118,094	551,219
International customers	314,077	755,926	-	1,070,003
Total	747,202	755,926	118,094	1,621,222
As at 31st December 2007				
COSCON	517,311	-	-	517,311
International customers	239,742	762,618	-	1,002,360
Total	757,053	762,618	-	1,519,671

Increasing market share and growing container fleet



Benefited from largely long-term leases, utilisation rates were kept high



Fleet age analysis (in TEUs)

Year	<1	1	2	3	4	5	6	7	8	9	10	>10	Total
Dry	142,987	337,061	258,977	165,991	145,510	145,824	111,335	89,565	60,634	33,469	18,834	60,275	1,570,462
Reefer	2,954	4,562	7,036	1,894	1,529	1,713	1,894	3,184	2,270	432	1,694	12,021	41,183
Special	780	600	199	-	-	-	10	-	-	932	2,011	5,045	9,577
Total	146,721	342,223	266,212	167,885	147,039	147,537	113,239	92,749	62,904	34,833	22,539	77,341	1,621,222

Fleet capacity breakdown by type of containers

		Owned Containers (COSCON)	Owned Containers (International customers)	Managed Containers (International customers)	Sale-and-leaseback Containers (COSCON)	Total
As at 31st December 2008						
Dry	%	95.5	97.7	97.8	94.1	96.9
Reefer	%	4.2	2.1	1.3	5.4	2.5
Special	%	0.3	0.2	0.9	0.5	0.6
Total number of containers	TEUs	433,125	314,077	755,926	118,094	1,621,222
Percentage of total	%	26.7	19.4	46.6	7.3	100.0
As at 31st December 2007						
Dry	%	94.8	98.7	97.5	-	96.8
Reefer	%	4.9	0.9	1.5	-	2.5
Special	%	0.3	0.4	1.0	-	0.7
Total number of containers	TEUs	517,311	239,742	762,618	-	1,519,671
Percentage of total	%	34.0	15.8	50.2	-	100.0

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Container Leasing, Management and Sale – Profit and Revenue

In 2008, the Group's container leasing, management and sale businesses grew steadily. The profit contribution from this division increased 19.5% year-on-year to US\$141,055,000 (2007: US\$117,994,000). Divisional total revenue totalled US\$252,620,000 (2007: US\$247,853,000), representing a year-on-year increase of 1.9%. Container leasing revenue accounted for 80.1% (2007: 73.2%) of the divisional total revenue. This increased 11.6% year-on-year to US\$202,437,000 (2007: US\$181,334,000), mainly due to increased on-hired units by international customers.

Disposal of Returned Containers upon Expiry of Leases

During the year, 28,770 TEUs (2007: 51,464 TEUs) of containers were returned by COSCON upon expiry of their 10-year leases. In 2008, the returned containers disposed of by the Group totalled 34,043 TEUs (2007: 56,759 TEUs), including disposal of 26,645 TEUs (2007: 51,365 TEUs) of containers returned by COSCON upon expiry of their 10-year leases in 2008 or before. The Group generated US\$39,352,000 (2007: US\$57,038,000) of sales proceeds from the disposal of returned containers, accounting for 15.6% (2007: 23.0%) of the divisional total revenue. Profit before tax from the disposal amounted to US\$7,094,000 (2007: US\$6,583,000).

Revenue analysis

	2008 (US\$'000)	2007 (US\$'000)	y-o-y change	2008 percentage of total	2007 percentage of total
Container leasing revenue	202,437	181,334	+11.6%	80.1%	73.2%
Management income	8,465	7,327	+15.5%	3.4%	3.0%
Sale of returned containers	39,352	57,038	-31.0%	15.6%	23.0%
Others	2,366	2,154	+9.8%	0.9%	0.8%
Total revenue	252,620	247,853	+1.9%	100.0%	100.0%

Focused on long-term leases to generate steady revenue stream from container leasing

Breakdown of long-term and master lease		2008	2007	2006	2005	2004
COSCON (long-term lease)	%	70.4	77.3	62.3	46.1	47.2
International customers (long-term lease)	%	21.8	18.0	27.8	37.9	34.4
International customers (master lease)	%	7.8	4.7	9.9	16.0	18.4
Total container leasing revenue	US\$'000	202,437	181,334	219,566	274,476	255,921



Further Streamlining of the Asset Light Business Model

To further optimise the container leasing business and lower operational risks, the Group further streamlined the asset light business model with the sale-and-manage-back business model getting more established. It completed a sale-and-manage-back transaction in March 2008 with containers amounting to 13,509 TEUs (2007: 135,956 TEUs), retrieving US\$22,421,000 in cash (2007: US\$238,802,000), and generating a pre-tax profit of US\$302,000 (2007: US\$25,975,000).

Following the successful launch of the sale-and-manage-back business model, the Group sold 118,094 TEUs of containers to CBA USD Investments Pty Limited, a wholly-owned subsidiary of the Commonwealth Bank of Australia, in July 2008. Upon the completion of the transaction, the Group leased back these containers, which were continued to be leased to COSCON. The Group retrieved US\$250,000,000 in cash through the disposal and recorded a pre-tax profit of US\$3,928,000. This transaction increased the Group's cash flow and helped reduce its gearing ratio. In addition, the arrangement allows the Group to retain the commercial control over these containers, enabling the Group to lease them to customers and earn and retain the profit from these leases.

Risk Management

The Group has a comprehensive risk management system to enable it to evaluate and scrutinize its customers. An effective risk monitoring system is also in place to ensure the implementation of various risk management measures. The global economic downturn has led to an unfavourable business operating environment, in response to which, the Group further enhanced its risk management. It employed measures such as applying risk evaluation to strengthen customers' credit risk management, keeping a close eye on changes in customers' business operations and financial situation and strengthening analysis and monitoring of receivables, to improve the cash management of the Group.

Fleet capacity movement

	2008 (TEUs)	2007 (TEUs)	y-o-y change
Fleet capacity as at 1st January	1,519,671	1,250,609	+21.5%
New containers purchased	152,752	326,715	-53.2%
Managed containers deposited by a third party	-	10,778	-100.0%
Containers returned from COSCON upon expiry of leases			
Total	(28,770)	(51,464)	-44.1%
Re-leased	2,867	502	+471.1%
Disposed of and pending for disposal	(25,903)	(50,962)	-49.2%
Ownership transferred to customers upon expiry of finance leases	(828)	(469)	+76.5%
Defective containers written off	(230)	-	N/A
Total loss of containers declared and compensated by customers	(24,240)	(17,000)	+42.6%
Fleet capacity as at 31st December	1,621,222	1,519,671	+6.7%

The majority of the Group's customers are the world-class container lines, including the world's top 10 container lines. During the year, container leasing revenue from the world's top 10 container lines accounted for 80.7% (2007: 86.0%) of the Group's total container leasing revenue.

Leases of the Group's owned containers were mostly long term in nature in order to mitigate cyclical risks and warrant a high utilisation rate. During the year, long-term leases contributed 92.2% (2007: 95.3%) to the total container leasing revenue. Long-term leases by COSCON contributed 70.4% (2007: 77.3%) to the total container leasing revenue, while long-term leases by international customers contributed 21.8% (2007: 18.0%), and only 7.8% (2007: 4.7%) from master leases.

BUSINESS OUTLOOK

The global trading volume, along with the global economic growth, is expected to further slow down in 2009, given that the US and European economies are both in recession. Consequently, the growth rate of global container traffic will also plunge substantially. According to the estimation by Drewry Shipping Consultants Limited, the global container traffic is expected to grow by

just 2.8% in 2009, down from 7.2% in 2008. This would impose a heavy blow to the shipping industry and all foreign trade-related sectors.

The Group's container leasing, management and sale businesses will also be challenged by the very difficult business environment. Leasing revenue and utilisation rates are both anticipated to be under pressure. Despite all the uncertainties shrouding the global economy, the Group will continue to focus on the development of its long-term leasing business in 2009 to maintain a steady stream of leasing revenue. The Group will, in the coming year, continue to execute the asset light model for steady development of its container leasing, management and sale businesses and to exercise a strict control over capital expenditure and operating costs in order to maximise efficiency. The Group will closely monitor the global economy and market trends, and come up with appropriate measures to effectively control risks. It will take a prudent yet proactive approach in facing upcoming challenges and plan ahead for the recovery of the economy.