

# Chairman's Report



Dear shareholders,

I am pleased to present the Annual Report of the Company for the year ended 31st December, 2006.

## **FINANCIAL RESULTS**

For the year ended 31st December, 2006, the Group achieved a consolidated profit attributable to shareholders of HK\$300.1 million, as compared with the profit of HK\$517.4 million (as restated) attained for the financial year in 2005.

The overall net profit achieved was relatively lower than that in the preceding year due primarily to the fact that the share of profits contributed by the Group's associates during the year under review, including that from Regal Hotels International Holdings Limited, were lower than those recorded in 2005. However, at the operational level, the core hotel businesses of Regal have continued to perform satisfactorily and a more detailed account of the financial results and operational performance of Regal in the year under review is contained in the relevant sections below.

Furthermore, shareholders would have noted that Regal, in which the Group presently holds a 45.3% shareholding interest, has successfully completed the spin-off and separate listing of Regal Real Estate Investment Trust on The Stock Exchange of Hong Kong Limited in March 2007. Under the spin-off transaction, Regal has disposed of its interests in the five Regal Hotels in Hong Kong to Regal REIT at a gross sale consideration of HK\$12,500 million. Regal has derived from the transaction a gain of not less than HK\$2,000 million, which is attributable to its initial disposal of 28% interest in Regal REIT and before taking into account further gains that may arise from any exercise of the over-allotment option. The share of profit thus attributable to the Paliburg Group will correspondingly be reflected in the results of the Group in the current financial year of 2007.

### **DIVIDEND**

The Directors have resolved to recommend the payment of a final dividend of HK0.3 cent per ordinary share for the year ended 31st December, 2006 (2005 - HK0.2 cent), absorbing an amount of approximately HK\$21.6 million (2005 - HK\$14.4 million), payable to holders of ordinary shares on the Register of Ordinary Shareholders on 12th June, 2007. Together with the interim dividend of HK0.15 cent per ordinary share paid in November 2006 (2005 - Nil), total dividends per ordinary share for the year ended 31st December, 2006 will amount to HK0.45 cent (2005 - HK0.2 cent), representing an increase of 125% over the total dividends paid for the 2005 financial year.

### **CLOSURE OF REGISTER**

The Register of Ordinary Shareholders will be closed from Friday, 8th June, 2007 to Tuesday, 12th June, 2007, both days inclusive, during which period no transfers of shares will be effected. In order to qualify for the proposed final dividend, all transfers of ordinary shares, duly accompanied by the relevant certificates, must be lodged with the Company's branch registrar in Hong Kong, Tengis Limited, no later than 4:00 p.m. on Thursday, 7th June, 2007. The relevant dividend warrants are expected to be despatched on or about 29th June, 2007.

### REVIEW OF OPERATIONS

#### PROPERTIES

##### Hong Kong

##### **Ap Lei Chau Inland Lot No. 129, Ap Lei Chau East**

This development project, in which the Group has a 30% interest, entails primarily residential accommodation comprising luxury apartments together with ancillary retail areas, which has total gross floor area of about 913,000 square feet and complemented with recreational and car parking facilities. The site formation works are progressing and foundation works have also been commenced.

##### **211 Johnston Road, Wanchai**

As reported in the Interim Report 2006, the Group has decided to retain for rental income purpose the unsold portions in this commercial building, comprising all the office floors with total gross floor area of about 60,900 square feet and certain ground floor shops with total gross floor area of about 2,200 square feet. Consequently, this property has been reclassified from property held for sale to investment property. Based on an independent professional market valuation as at 31st December, 2006, a fair value gain on this property in the amount of HK\$80 million (in addition to a fair value gain of approximately HK\$70 million upon accounting reclassification of the property to investment property during the year) has been reflected in the financial results for the year under review. Due to the increased demand for office accommodation, the rental rates achieved have also increased progressively and, at present, virtually all of the units are leased.

##### **Rainbow Lodge 9 Ping Shan Lane, Yuen Long, New Territories**

This residential project was developed by the Group and completed in 2004. The development has a total of 16 duplex units with aggregate gross area of approximately 30,800 square feet with ancillary car parking facilities. Up to the balance sheet date, 6 duplex units have been sold and the Group retained within the development 10 duplex units with aggregate gross area of approximately 19,720 square feet and 14 car parks.

In January 2007, the Group entered into a sale and purchase agreement with Cosmopolitan International Holdings Limited, a listed company in Hong Kong, for the sale of the entire equity interests held by the Group in its wholly-owned subsidiary that beneficially owns the 10 retained units and unsold car parks in this completed development.

Under the terms of the sale and purchase agreement, the consideration was agreed at HK\$70 million, HK\$14 million of which was paid in cash and the balance of HK\$56 million was to be satisfied by the issue to the Group of convertible bonds in a principal amount of HK\$56 million, which will be convertible into 800 million new ordinary shares of Cosmopolitan at an initial conversion price of HK\$0.07 per share (subject to adjustments) and, if not converted, will be redeemable on the 2nd anniversary of the date of issue at a yield to maturity of 3.5% per annum. The Group would also grant to Cosmopolitan certain placement rights, exercisable within 12 months of the date of issue of the convertible bonds, for Cosmopolitan to procure potential investors to purchase part or all of the convertible bonds to be held by the Group. In the case where the Group disposes of the convertible bonds pursuant to such placement rights, the Group would account to Cosmopolitan 70% of the profits arising from the sale of such convertible bonds.

The sale and purchase agreement has subsequently been duly completed in March 2007 and the profit of approximately HK\$37 million derived from this transaction will be reflected in the results of the Group in the current financial year of 2007.

## **The People's Republic of China**

### **Development Project in the Central Business District of Beijing**

As reported in the Interim Report 2006, the Group and Regal each beneficially owns a 50% equity interest in a company which, in turn, holds a 59% interest in an investee company established in the PRC, the remaining 41% interest of which is held by a local joint venture partner. The investee company has fully settled the land premium payable under the Land Grant Contracts for the Phase I land in April 2006 and is seeking to obtain the relevant Land Use Right Certificate. In the meanwhile, the investee company is actively working to secure its rights to the remaining Phase II land site comprised in the overall development project. The overall development project, comprising both Phase I and Phase II, is expected to have total permissible gross floor area of about 4,630,000 square feet encompassing office, hotel, commercial, residential and car parking accommodations. Due to the longer time anticipated to be needed to obtain relevant planning approvals and to secure the development rights to the Phase II land site, it is expected that there will be a delay in the overall development timetable for this project.

### **Other Investments**

As reported before, the Group has substantially resolved most of the outstanding issues with the purchaser who has defaulted on the agreement previously entered into by the Group in 2003 with respect to the sale of the Group's entire joint venture interest in the development project at Gong Ren Ti Yu Chang Street East, Chao Yang District, Beijing. The sale transaction will be formally completed once the remaining outstanding issues have also been resolved.

### **CONSTRUCTION AND BUILDING RELATED BUSINESSES**

#### **Construction Business**

The construction business of Chatwin Engineering Limited continued to progress steadily. Apart from new jobs secured from the private sector, including part of the works associated with the asset enhancement programme at the Regal Hotels in Hong Kong, Chatwin has also been awarded the construction contract for the Redevelopment of Sau Mau Ping Estate Phases 13 & 16 from the Housing Authority in August 2006.

#### **Building Related Businesses**

A comprehensive range of building related businesses, including development consultancy comprising architectural, engineering and interior design services, project management, building services and estate management, are being operated by the Group. These business operations, together with the technology-based businesses undertaken by the Leading Technology group, have all performed satisfactorily during the year under review. While these operating divisions have been offering professional services and support to most of the in-group projects as well as to third parties, they will also be important for any new projects planned to be undertaken by the Group in the expansion of its property portfolio.

### **REGAL HOTELS INTERNATIONAL HOLDINGS LIMITED**

For the year ended 31st December, 2006, Regal achieved a consolidated profit attributable to shareholders of HK\$331.3 million, as compared with the profit of HK\$528.4 million attained for the financial year in 2005. The overall net profit achieved was relatively lower than that in the preceding year due primarily to the fact that during the year under review, while general interest costs have increased and much less profit contribution has been attributed from associates, there was also a deferred tax charge as compared to the recognition of substantial deferred tax income last year.

At the operational level, total operating profits (including hotel net rental income) of the Regal group generated by its five hotels in Hong Kong and from its hotel management business amounted to HK\$570.5 million in the year under review, which represented an increase of 13.8% over the HK\$501.3 million attained in 2005.

In March 2007, Regal has successfully completed the spin-off and separate listing of Regal Real Estate Investment Trust on the Stock Exchange. Under the spin-off transaction, the Regal group has disposed of its interests in the five Regal Hotels in Hong Kong to Regal REIT at a gross sale consideration of HK\$12,500 million and, at the same time, has entered into leases with Regal REIT for the leasing of the five hotels for a term until 31st December, 2015. The Regal group has derived from the transaction a gain of not less than HK\$2,000 million, which is attributable to its initial disposal of 28% interest in Regal REIT and before taking into account further gains that may arise from any exercise of the over-allotment option, and the profit thus derived by Regal will be reflected in its results for the current financial year of 2007.

After the spin-off transaction, the operational model of the Regal group will be substantially different from that undertaken in the year under review, as it will no longer own the five Regal Hotels in Hong Kong directly, but will however continue to be the hotel operator pursuant to the leases with Regal REIT as the new hotel owner.

### **HOTELS**

#### **Hong Kong**

Total revenue from the hotel operations (including rental income) and management business of the Regal group increased by approximately 11.1% from HK\$1,082.7 million for the year ended 31st December, 2005 to HK\$1,202.5 million in 2006. The increased revenue was mainly attributable to the increase in the average room rates achieved by the five Regal Hotels in Hong Kong and an improvement in the mix of business and leisure travelers. Compared on a year-on-year basis, the combined average room rate of the five hotels in 2006 enhanced by approximately 11.5% in 2006. While Regal Airport Hotel is still working to catch up on its room occupancy, the other four Regal Hotels in Hong Kong were steadily operating at an average occupancy level of about 90%. Overall for the five hotels, the combined average room occupancy in 2006 was maintained at about 81%, approximately the same level as that recorded in 2005. Taking into account the intermittent disruptions on the business operations caused by the asset enhancement programme and renovation works, the operating results achieved by the Regal Hotels in Hong Kong in the year under review should be considered as satisfactory.

A major part of the asset enhancement programme planned for four of the Regal Hotels in Hong Kong is scheduled to be completed before the end of the third quarter in 2007. The remaining phase relates to the addition of three stories, comprising 274 additional rooms, on top of the existing hotel building at the Regal Riverside Hotel in Shatin, the construction works for which will soon commence and are targeted to be completed before the end of 2008.

By the end of the third quarter this year, the total hotel room stock of the five Regal Hotels in Hong Kong will increase from the present number of 3,348 to 3,542 and when the asset enhancement programme is fully completed, will boost the aggregate number of hotel rooms to 3,816.

#### **The People's Republic of China**

Benefiting from the buoyant economy in China, the two managed hotels in Shanghai continued to perform satisfactorily. The Regal group has been managing successfully these two hotels in Shanghai since 1997 with high repute and this is exemplary of the quality and dedication of professional services that Regal commits to its hotel management business.

To enhance the image and recognition of the Regal brand, the Regal group is planning to strengthen and expand its footholds in China, through development of new hotel projects and the provision of management services, with initial focus on major cities.

In January 2007, the Regal group entered into a letter of intent with Cosmopolitan to participate in a large scale development project in Shenyang City, Liaoning Province, the subject of an overall development cooperation framework agreement between Cosmopolitan and the Shenyang Menrong Economic District.

Under the letter of intent, the Regal group will provide consultancy services to Cosmopolitan with respect to the hotel and related project, comprising hotels, service apartments, shopping, exhibition, entertainment and recreational facilities, to be included within the overall development project. The Regal group will also have the right of first refusal to invest in 55% interest (or such other percentage as may be mutually agreed) in the hotel and related project, subject to Cosmopolitan having entered into a legally binding agreement with the relevant government authorities.

In early April 2007, the Regal group together with other investors entered into a conditional subscription agreement with Cosmopolitan, pursuant to which the Regal group has agreed to subscribe for new convertible bonds in a principal amount of HK\$102.5 million proposed to be issued by Cosmopolitan group, which will be convertible into new ordinary shares of Cosmopolitan at an initial conversion price of HK\$0.205 per share and, if not converted, will be redeemable on the third anniversary of the date of issue of the convertible bonds at a yield to maturity of 5% per annum.

### **PROPERTIES**

#### **Hong Kong**

##### **Regalia Bay, Stanley**

For the year under review, the Regalia Bay, a project that is 70% owned by the Regal group, contributed a profit of approximately HK\$203.6 million to the Regal group mainly from a write back of provision. The Regal group is optimistic of the high-end luxury residential market and will continue to lease out the remaining houses for rental income unless the prices offered by prospective purchasers are attractive.

#### **The People's Republic of China**

##### **Development project in the Central Business District of Beijing**

As referred to above, the Regal group is a 50% joint venture partner of the Group with respect to the investment held in the investee company in the PRC.

### OUTLOOK

With the booming economy in China, the number of visitors from the Mainland will continue to increase in large numbers. To cater for the influx of visitors from Mainland as well as from overseas countries, Hong Kong is undertaking and planning a number of transport infrastructure projects, including additional land linkages between Hong Kong and Southern China, the enhancement of facilities at the Hong Kong International Airport and a new cruise terminal in South East Kowloon. In addition, Hong Kong is also embarking on the expansion of its various tourism and conference infrastructure, in order to secure the position of Hong Kong as a financial centre of global significance, an international conference and exhibition centre as well as a transport and aviation hub.

Over the next few years, there will be a number of new hotels scheduled for completion in Hong Kong, but a majority of these new hotels is located in non-traditional tourist areas. Moreover, based on the forecast growth in visitor arrivals, it is anticipated that the demand for hotel rooms in Hong Kong will continue to outstrip supply and while average room occupancy will be maintained at a high level, average room rate should be able to further improve.

The five Regal Hotels in Hong Kong continued to perform well during the first few months of 2007 in keeping with their forecast trend of growing profitability. Apart from the second phase works at the Regal Riverside Hotel, the asset enhancement programme is targeted to be completed before the end of the third quarter in 2007, which will bring into operation 194 additional new hotel rooms. Given the favourable operating environment presently prevailing, the directors of Regal are confident that the five Regal Hotels in Hong Kong will be able to generate in 2007 much enhanced operating profits than those attained in 2006.

Subsequent to the year end, Regal has successfully completed on 30th March, 2007 the spin-off of Regal REIT, which is now separately listed on the main board of the Stock Exchange.

Summarily, pursuant to the spin-off proposal, the Regal group sold its interests in the five Regal Hotels in Hong Kong to Regal REIT at a gross sale consideration of HK\$12,500 million. As part of the transaction, the Regal group leased from Regal REIT the five Regal Hotels with lease terms that continue until 31st December, 2015. The rents payable for the period from 30th March, 2007 to 31st December, 2010 consist of escalating base rents, starting from HK\$476 million for the period from the lease commencement date to 31st December, 2007 to HK\$780 million for 2010, plus variable rents. The rents payable for the term after 2010 will be determined by a jointly appointed independent professional property valuer, subject to a floor rent of HK\$400 million per annum. The Regal group has also been appointed as the hotel manager for the five Regal Hotels for a term of 20 years from 30th March, 2007. Regal REIT is managed by Regal Portfolio Management Limited, which is a wholly-owned subsidiary of Regal but functioning independently.



Out of the gross proceeds received, approximately HK\$6,000 million was applied by the Regal group to subscribe initially for approximately 72% of the total outstanding units of Regal REIT. The Regal group has granted to the joint international underwriters under the initial public offering of Regal REIT an over-allotment option for up to approximately 4.2% of the total outstanding units of Regal REIT owned by the Regal group.

Another HK\$4,350 million of the proceeds received by the Regal group has been applied to repay all of its outstanding bank indebtedness. Consequently, the Regal group is now free of any bank debt and the remaining proceeds in the amount of approximately HK\$2,160 million have been retained for general working capital and for the funding of new acquisitions and investments.

In addition, the Regal group has derived from the transaction a gain of not less than HK\$2,000 million, which is attributable to its initial disposal of 28% interest in Regal REIT and before taking into account further gains that may arise if the over-allotment option is exercised.

Following the completion of the spin-off of Regal REIT, the Regal group plans to further expand its investments in the property and hotel development sectors. When suitable opportunities arise, the Regal group will also seek to diversify into other sectors that are complementary to its existing business base. Initial focus will be placed to secure appropriate hotel and other property development opportunities in major cities in Mainland China. The Regal group believes that the undertaking by the Regal group of new hotel developments will not only facilitate the planned expansion of its hotel management network, but potentially will also foster the parallel growth of Regal REIT through the right of first refusal granted by the Regal group to Regal REIT, as and when the Regal group should decide to dispose of any of its developed hotels after they have been completed and started to operate profitably. The Regal group is in the course of finalising a dynamic and sustainable Strategic Development Plan for the long term growth of the Regal group, which will take into consideration present and potential financial strength of the Regal group, its extensive experience, expertise and business network as well as its strong alliance with Century City International Holdings Limited, the Group and the newly listed Regal REIT.

As the gain realised on the spin-off of Regal REIT will be reflected in the current financial year, 2007 will undoubtedly be a very fruitful year for Regal. Given that the Regal group's financial position has now been substantially strengthened, the Regal group is now well poised to move forward with its expansion plan and the directors of Regal are confident that the Regal group will be able to grow from strength to strength and to generate to shareholders increasing returns.

The real estate values of all types of prime development properties in Beijing, from commercial, office, residential to hotel, have risen significantly over the last few years. Based on the prevailing market values, the land site beneficially owned by the investee company in the Central Business District in Beijing should now be worth far more than the carrying costs of the Group, as well as that of the Regal group, with respect to their investments in the project. The Group is strongly committed to this comprehensive development project and plans to develop it into one of the major landmarks in this capital city.

Moreover, with the ready resources and expertise presently available, the Group is well positioned to seek new projects to strengthen its portfolio in property development and investment, particularly in Mainland China where the economy is booming and business opportunities are relatively abundant.

The Ap Lei Chau project in the southern side of Hong Kong Island, comprising primarily luxury residential apartments, are expected to be in great demand, as supply of luxury apartments in Hong Kong within the next few years are limited. The Group anticipates that substantial profit will be generated from this project when it has been duly completed and sold.

Having regard to the prospects of the various business facets of the Group, the Directors are optimistic that the Group, as a whole, will continue to grow and prosper.

### **DIRECTORS AND STAFF**

First of all, I would like to express my personal gratitude to my fellow Directors and all management and staff members for their valuable support and dedicated efforts over the years.

Taking this opportunity, I would also like to thank Mrs. Kitty Lo Lee Kit Tai, who resigned as a Non-executive Director of the Company in January 2007, for her past contribution and to extend my warm welcome to Miss Lo Po Man and Mr. Kenneth Wong Po Man, who were both appointed as additional Executive Directors of the Company at that same time in January 2007, and I look forward to their continual efforts and contribution.

### **LO YUK SUI**

Chairman

Hong Kong  
19th April, 2007