BEA securities

EAST ASIA SECURITIES COMPANY LIMITED
8/F, 10 Des Voeux Road Central, Hong Kong.
Dealing: 3608 8000 Research: 3608 8096 Facsimile: 3608 6132

HONG KONG RESEARCH
8th August 2008

Analyst: Sabina Cheng

SWIRE PACIFIC LIMITED (太古股份公司)

Sector	:	Conglomerates	Chairman	:	Christopher Pratt
HKSE Code	:	00019			
Market Price	:	HK$79.00 (7/08/2008)	Finance Director	:	Martin Cubbon
HSI	:	HK$22,104.199 (7/08/2008)			
Shares Issued	:	915.5645 million ('A' share)			
Market Cap	:	HK$72,329.59 million			
52-week Hi / Lo	:	HK$116.00 / HK$73.00			

SUMMARY OF INTERIM RESULTS FOR THE SIX MONTHS ENDED 30TH JUNE 2008

Interim Results Highlights

	1H2008 HK$ million	1H2007 HK$ million	*Change*
● Turnover	11,782	10,338	*14.0%*
● Change in fair value of investment properties	10,023	8,895	*12.7%*
● Operating profit	13,587	12,844	*5.8%*
● Net finance charges	-341	-187	*82.4%*
● Share of results of jointly-controlled companies	380	276	*37.7%*
● Share of results of associated companies	227	1,462	*-84.5%*
● Profit before tax	13,853	14,395	*-3.8%*
● **Profit attributable to shareholders**	**12,380**	**12,493**	***-0.9%***
Excluding the impact of investment property revaluation:			
● **Underlying attributable profit**	**3,265**	**5,255**	***-37.9%***
● EPS (HK$) – 'A' share	8.17	8.18	*-0.1%*
● Interim DPS (HK$) – 'A' share	0.90	0.90	*Unchanged*

- Swire Pacific ("Swire") announced a 37.% drop in its 1H08 underlying profit attributable to shareholders, which excludes net property valuation gains to HK$3.265 billion- the first decline in its first-half earnings since 2003 due to weakness in Cathay Pacific earnings and a reduction in asset realisations.

- Attributable earnings of HK$12.380 billion include net property valuation gains of HK$8.172 billion and a HK$949 million write-back of deferred tax on brought forward property valuation gains.

- Turnover rose by 14.0% y-o-y to HK$11.78 billion, mainly due to strong growth in property trading and marine services.

- EPS ('A' share) fall slightly by 0.1% y-o-y to HK$8.17. An interim DPS ('A' share) for 1H 2008 was maintained at HK$0.90. DPS for its B shares in 1H08 was also maintained at HK$0.18 each.

- Net debt increased by HK$6.658 billion over the six months to HK$29.150 billion as a result of continued investments in property projects and new vessels. Gearing ratio rose in the period by 3.3 percentage points to 19.8%. Cash and cash equivalent was HK$4.516 billion as of 30 June 2008 compared with HK$3.648 billion at 31 Dec 2007.

- **Turnover breakdown by business lines**:

HK$ million	1H08	%	1H07	%	Change
Property					
- *Property investment*	3,291	27.9%	2,692	26.0%	22.3%
- *Property trading*	477	4.0%	8	0.1%	5,862.5%
- *Sales of investment properties*	0	0.0%	280	2.7%	NA
- *Hotels*	78	0.7%	65	0.6%	20.0%
Beverages	3,626	30.8%	3,329	32.2%	8.9%
Marine Services	1,849	15.7%	1,332	12.9%	38.8%
Trading & Industrial	2,511	21.3%	2,681	25.9%	-6.3%
Head Office/Inter-segment elimination	-50	-0.4%	(49)	-0.5%	2.0%
Total	**11,782**	**100.0%**	**10,338**	**100.0%**	**14.0%**

- **Attributable profit by divisions**:

HK$ million	1H08	%	1H07	%	Change
Property	10,948	88.4%	8,981	71.9%	21.9%
Aviation	10	0.1%	1,283	10.3%	-99.2%
Beverages	196	1.6%	219	1.8%	-10.5%
Marine Services	878	7.1%	1,739	13.9%	-49.5%
Trading & Industrial	234	1.9%	209	1.7%	12.0%
Head Office	114	0.9%	62	0.5%	83.9%
Total	**12,380**	**100.0%**	**12,493**	**100.0%**	**-0.9%**

- Attributable profit from the **Property Division** rose by 21.9% y-o-y to HK$10.948 billion, which includes a net property valuation gain of HK$8.092 billion (HK$7.313 billion for the same period in 2007). Underlying profit in the Property Division increased by 8% to HK$1.915 billion, with gross rental income rising 23% to HK$3.257 billion, reflecting continued strong demand for office and retail space. Office occupancy rate was close to 100%, except One Island East which is now 91% leased. The Village at Sanlitun retail development in Beijing was opened in July 08. Major tenants include Adidas, Esprit, IT and Apple.

- The **Aviation Division**'s results for the period suffered from exceptionally high oil prices, with attributable profit falling to HK$10 million from HK$1.283 billion in the first half of 2007. Passenger demand at both Cathay Pacific and Dragonair remained robust. However, strong revenue growth could not outweigh a very significant increase in fuel costs. Cathay Pacific's results also include a provision of HK$468 million relating to the settlement of the antitrust investigations into its cargo business in the United States. The HAECO Group recorded a higher profit of HK$591 million during the period, an increase of 8% over the comparative period in 2007, in line with expectations, as strong demand for aircraft maintenance services continued.

- The **Beverages Division** reported a 10.5% y-o-y drop in attributable profit to HK$196 million. Total sales volume grew 11% y-o-y while turnover grew 8.9% y-o-y. In Mainland China, despite the severe snow storms in early Feb 08 and poor weather in June 08, sales volume increased by 14% over the comparative period. Persistent high material and fuel costs continued to squeeze margins but were partially countered by increase in selling price early in the year. Growth prospects for the second-half are uncertain with weakening economic conditions offsetting the positive impact expected from marketing campaigns linked to the Beijing Olympics.

- Attributable profit from the **Marine Services Division** rose by 33% y-o-y to HK$878 million, excluding the HK$1.078 billion profit on sale of Shekou Container Terminals in Feb 2007. Swire Pacific Offshore (SPO) reported an attributable profit of HK$834 million for 1H2008, an increase of 33% over 1H2007. High oil prices had driven increase demand for offshore support services, with charter rates for SPO's vessels up by an average of 23% over 1H2007. SPO performed strongly in all geographical markets. Fleet utilisation reached a record high of 94% on continued high demand as several dry dockings were deferred to the second half of 2008 to suit charter hire timings.

- The **Trading & Industrial Division** reported an attributable profit of HK$234 million in 1H2008, a 12% increase over 1H2007, as strong growth at Swire Resources in particular, and improved results across the division in general were partially offset by the effects of a further decline in the Taiwanese vehicle market. The Taikoo Motors Group reported an attributable profit of HK$8 million, falling from HK$60 million in the same period last year, as market sentiment remained weak.

Outlook & Prospect

- **Low vacancy rates for office** The Grade A office rents climbed to as high as HK$200 per sq ft in Central, largely driven by low vacancy rate which stood at 1.1% there. Meanwhile, for Swire, the occupancy was close to 100% excluding One Island East (91% let). Management guidance showed that spot rental office was- HK$100/sq ft at One and Two Pacific Place, HK$80 at Three Pacific Place, low-HK$30 at Island East, and almost HK$50 at One Island East. Given that the office vacancy rates remain low, there should not be a significant downward adjustment for spot rents. Accordingly, it is expected that Swire can continue to enjoy its pricing power for its Hong Kong office and retail properties.

- **Satisfactory growth in retail rental** Swire recorded retail rental growth of 12% in 1H08, in line with Hong Kong retail sales growth. Nevertheless, growth is expected to slow on weakening consumption. Swire's plan to renovate its flagship Pacific Place shopping centre in Admiralty should help boost rental growth. Last month, the company said it would spend HK$1.5 billion to revamp Pacific Place to meet rapid changes in the retail market.

- **Loss-making carrier expected to drag performance of the Aviation Division** A return to satisfactory profitability for the Cathay Pacific group depends on the extent to which increased fuel costs can be recovered by higher fares and fuel surcharges. The positive driver for this business segment should be the firm demand for HAECO's services in second-half of 2008.

- **Further growth in earnings is expected from Swire Pacific Offshore** (SPO) SPO is expected to enjoy a good second-half earning this year on high charter rates and continued fleet expansion.

- **More China investment projects in the pipeline** Swire has received the first contribution from its mainland property developments, after the opening of the south site of the Village at Sanlitun in Beijing last month. Currently, Swire has 1 million sq ft of retail space and hotels in Beijing. It is also developing 6.85 million sq ft of commercial properties in Shanghai and Guangzhou. So far there are four new project developments, including, Beijing Sanlitun (North site to open in early 2009), Beijing Chaoyang, Guangzhou Taikoo Hui, and Shanghai Dazhongli.

- **Fair valuation** Swire's full-year profit for FY2008 would likely be dragged down further by the loss-making carrier. However, property earnings are expected to remain strong on continued high occupancy and strong demand. With a high-quality investment property portfolio including Pacific Place and Taikoo Place, Swire's long-term outlook remains promising despite volatile earnings in the short term. The counter is now trading at 32% discount to its 2009E NAV of HK$116.7 per share. Such discount is wider than long-term average of 24% but above trough discount of 40%-50%. Accordingly, we recommend to "Hold" the counter.

Recommendation: Hold

Important Disclosure / Analyst Certification / Disclaimer

This document is published by East Asia Securities Company Limited, a wholly-owned subsidiary of The Bank of East Asia, Limited (BEA).

The research analyst primarily responsible for the content of this report, in part or in whole certifies that the views on the companies and their securities mentioned in this report accurately reflect his/her personal views. The analyst also certifies that no part of his/her compensation was, is, or will be, directly, or indirectly, related to specific recommendations or views expressed in this report.

This report has been prepared solely for information purposes and has no intention whatsoever to solicit any action based upon it. Neither this report nor its contents shall be construed as an offer, invitation, advertisement, inducement or representation of any kind or form whatsoever. The information is based upon information, which East Asia Securities Company Limited considers reliable, but accuracy or completeness is not guaranteed. Information and opinions expressed herein reflect a judgment as of the date of this document and are subject to change without notice. Any recommendation contained in this report does not have regard to the specific investment objectives, financial situation and the particular needs of any specific addressee. This report is not to be taken in substitution for the exercise of judgment by respective readers of this report, who should obtain separate legal or financial advice. East Asia Securities Company Limited and / or The BEA Group accepts no liability whatsoever for any direct or consequential loss arising from any use of this report or further communication given in relation to this report.

At time of this report, East Asia Securities Company Limited has no position in securities of the company or companies mentioned herein the report, while BEA along with its affiliates and/or persons associated with any of them may from time to time have interests in the securities mentioned in this report. BEA and its associates, its directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein and may also perform or seek to perform broking, investment banking and other banking services for these companies.

BEA and/or any of its affiliates may beneficially own a total of 1% or more of any class of common equity securities of the subject company or companies mentioned in this report and may, within the past 12 months, have received compensation and/or within the next 3 months seek to obtain compensation for investment banking services from the subject company or companies mentioned in the report.

This document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of, or located in, any locality, state, country or other jurisdiction, publication, availability or use would be contrary to law and regulation.