

Chairman's Letter to Shareholders



Our businesses are strong, and sound and I believe we have the necessary mechanisms and structures in place to manage risks and maximise returns for our shareholders.

2009 First Half Results

CITIC Pacific recorded a profit attributable to shareholders of HK\$2,468 million in the first six months of 2009 compared to HK\$4,360 million for the same period in 2008.

We should remember that economic conditions in key markets were buoyant in the first half of 2008, and the subsequent rapid deterioration resulted in a most challenging operating environment for business. Beginning in the second quarter of 2009, we have seen encouraging signs of recovery, and this is reflected in the mixed results of our businesses.

In the first half of the year, the special steel business faced weaker demand for its products, in particular in overseas markets, but remained profitable. Property sales in many of our developments in mainland China have shown encouraging signs of recovery, in particular in the second quarter. Our power business did better than last year as the coal price dropped. Other businesses such as tunnels in Hong Kong, CITIC 1616 and Dah Chong Hong continue to provide us with stable profits and cash flow.

At the Annual General Meeting, I said that paying a dividend again would be considered once our company returned to profitability. The Board recommends paying an interim dividend of HK\$0.15 per share. When making this decision, we not only took into consideration the expectations of our investors, but also our company's need for capital to further develop our business, and our obligation to repay maturing debts.

Improving Corporate Governance

After I became Chairman in April, I identified the three things that impressed me the most about CITIC Pacific, and which I believe are central to the success of this company: the quality of our businesses and assets; the international standard of our management and employees; and the strong commitment to leadership in our approach to governance.

Looking at what this company has achieved since its formation has given me, and all of us at CITIC Pacific, the confidence and determination to work hard, and to return this company to strong and prosperous growth.

Besides running businesses and ensuring they generate profit and returns for our shareholders, we clearly recognise the importance of managing risks and strengthening our controls and central management. A lot has been achieved in this area.

We now have a much more formalised decision-making process, which greatly facilitates our ability to manage the diverse nature of our company's activities, and effectively monitor their associated risks.

I chair a re-defined and re-invigorated executive committee, which serves as a medium for communicating our direction and priorities, and for sharing information about key developments and issues affecting our various businesses. This committee now includes the leaders of most of our businesses, with the participation of the heads of major functional departments in the head office.

Our newly established investment committee's role is to consider the strategy and planning of the company, and to review investment proposals. The committee consists of four executive directors, including myself, and one non-executive director. Meetings are held regularly. Since its formation in April, we have reviewed and made decisions on a number of proposed investments and disposals.

The asset and liability management committee ('ALCO'), set up late last year, continues its important work. Chaired by the finance director and with representatives of different disciplines in the company, ALCO meets monthly to review the asset and liability balance of the company. It monitors and sets limits to our exposure in relation to asset and liability mismatches, counter parties, currencies, interest rates, commitments and commodities. It also establishes hedging policies, reviews and approves financing plans, and controls the use of any new financial products.

Throughout my career, I have learned and felt deeply that the running of a company depends very much on a well-established system and process and, most of all, on a cohesive management team. Like all organisations, having highly qualified people is essential to our operations. One of the central jobs of my chairmanship will be to ensure the recruitment of additional high quality and experienced personnel to our company. One example is the appointment of a new financial controller to further strengthen the effectiveness of financial controls throughout the company. Having spent 17 years with CITIC Group in various capacities in China and most recently in the United States, he brings to CITIC Pacific a wealth of knowledge and experience, not only in accounting and financial management, but also in his understanding of CITIC Group. We have also recruited a very experienced new treasurer, who will be joining us in the near future.

Businesses

Facing the challenging operating environment, our businesses, from special steel, to iron ore, to property, to tunnels, to power, and Dah Chong Hong and CITIC 1616, have proven that they are fundamentally strong.

Development of each of our businesses will be based on an assessment of its market position, competitiveness, future prospects, and the extent of our ability to influence its management. We are also studying and exploring potential opportunities and synergies between CITIC Pacific and CITIC Group. Our goal and responsibility is to increase investment returns for our shareholders, and we will achieve this by way of good management, co-operation, and, where needed, by the sale and restructuring of assets.

We intend to sell businesses over which CITIC Pacific is unable to exercise management control, which are not significant to the company's future or do not generate sufficient profit or cash. Examples are the disposals of our 20% interest in North United Power and our interests in Kaifeng Power and Weihai Power. These disposals do not indicate a disinterest in the power sector but a rationalisation to concentrate on the important components such as Ligang Power Station.

On August 17, we agreed to sell 12.5% of Cathay Pacific to Air China and 2% to Swire Pacific. As a result, our interest in Cathay Pacific will be reduced to 3%. The sale will generate HK\$7.3 billion of cash, which will strengthen CITIC Pacific's financial position and direct resources to the development of our major businesses.

Restructuring of certain assets is another way to generate returns for our shareholders. CITIC Capital, 50% owned by CITIC Pacific, recently signed an agreement with China Investment Corporation ('CIC'), China's sovereign wealth fund, under which CIC will become a 40% shareholder through subscribing to new shares. After completion of this transaction, our interest in CITIC Capital will be reduced to 27.5%. Through this restructuring, not only will CITIC Capital's capital base be enlarged, it will also result in a material increase in funds under management.

We are increasing investment in our major businesses. At a time when most steel mills in China were incurring losses, our three special steel plants remained profitable, and CITIC Pacific Special Steel continues to be a leader in the special steel industry in China. We are committed to further developing and investing in special steel, a

major business of CITIC Pacific. This is reflected in the building of new production lines, as well as our purchase of the 20% interest in Jiangyin Xingcheng Special Steel currently held by its management, bringing CITIC Pacific's ownership in this steel mill to 100%.

Our iron ore mine in Australia continues to make progress. Given the complexity and the sheer size of this project, it is amazing to see how much has been accomplished, but there is still much to do to achieve production, and this is receiving the full attention of the management and our contracting partners.

Property development in mainland China is another major business. CITIC Pacific has signed a co-operation agreement with CITIC Real Estate Co. Ltd., a subsidiary of CITIC Group, and a well-known property developer in China with a significant land bank in many cities. Under the agreement, CITIC Real Estate will recommend projects to CITIC Pacific that it believes to have good potential. After its own evaluation, CITIC Pacific may take a 20% stake in these projects. The two companies will share knowledge, market information and other resources, and CITIC Pacific can also leverage off CITIC Real Estate's vast sales network. We are now evaluating several projects. At the same time, construction of CITIC Pacific's property developments in mainland China are progressing to plan, and sales of commercial and residential properties have picked up in recent months with an improvement in market sentiment. With hard work, many of our development projects will be ready for sale in the coming few years, and we expect they will bring significant profit contribution to CITIC Pacific.

When formulating CITIC Pacific's future development strategy, one thing is clear: having multiple businesses in diversified industries is beneficial to CITIC Pacific, in particular as our businesses are positioned to capture the fast growing demand of mainland China. As an example, special steel as a percentage of total steel produced in China is still quite low compared to that of industrialised countries. China's demand for special steel will continue to grow as the country becomes industrialised. For iron ore, our story is also very compelling. CITIC Pacific, will in due course, become Australia's largest exporter of magnetite concentrate. The concentrate we will be producing is of higher quality than most of China's imported ore. This high quality ore will not only satisfy the increasing need from Chinese steel mills, it will also serve Chinese society's demand for a greener approach to business.

Financial Position

At the end of the half year, shareholders' funds were HK\$55 billion, an increase of 11% compared with the end of 2008. Cash and available committed facilities stood at HK\$30 billion. We do recognise that we need to manage our on-going financing requirements and we have already begun to work on this. New loans of HK\$10 billion were signed or are in process in the last few months. Our mainland China property sales are expected to rise in 2010 and thereafter provide significant cash flow. In addition, sales of smaller or non-managed businesses will bring cash to the company.

I should mention that all of the Australian dollar leveraged foreign exchange contracts outstanding

at December 31, 2008, were restructured into plain forward contracts, which qualify for treatment as accounting hedges. As a result, volatility in the cost of the iron ore project due to exchange rate fluctuations will be reduced.

Conclusion

Challenged by the unprecedented global financial crisis, the Chinese government has taken proactive and timely measures, and implemented plans to stimulate its economy, which have brought initial success. As China's basic infrastructure and supporting pillar industries continue to improve, household income continues to grow, and the country continues to industrialise and urbanise, underlying consumption and demand will no doubt continue to grow. To be successful, the strategy we formulate, and the businesses and assets we invest in, should capture the growing demand in China.

CITIC Pacific's achievements in the last 20 years have been considerable. I have full confidence and resolve to take this company to greater success.

Let me take this opportunity to thank our Board and our employees for their continued support and their enormous hard work in a difficult period. I would also like to express my gratitude to our investors for standing by us and continuing to believe in CITIC Pacific.



Chang Zhenming

Chairman

Hong Kong, 26 August 2009