A Conversation with the Managing Director

John CHAN Cho Chak Managing Director

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Steering **Forward**

At KMB, we are constantly exploring stakeholder expectations of our business. In a conversation with the Managing Director, Mr John Chan Cho Chak, writer Glynis Green explores key issues that have been commonly raised by stakeholders – investors, financial analysts, business partners and community groups.

Q: How would you describe the operating environments of Hong Kong and the Chinese Mainland in the context of the Group's business aspirations?

A: Both operating environments are very challenging, but in different ways. In Hong Kong we have had several years of deflation in the overall economy, but continuously rising costs — mainly wages and fuel — for the bus industry. This has created a dichotomy in which the community perceives an increasing gap between public transport fares and general consumer prices. Given that bus fares are controlled by the Government, this perception has meant that, politically, it has become increasingly difficult for the bus industry to be allowed to recover its rising costs from fares. The Group's fares have not increased since December 1997. In fact, they have been reduced as a result of various fare concessions that we have introduced, either through Bus-bus Interchange Schemes or by way of direct reductions of certain fares. At the same time, the successive opening of new railways, at a time when the population has remained relatively stable, has created a situation of significant over-supply in public transport services. This has resulted in more intense competition among different public transport modes. All these factors have combined to squeeze the profit margin of the Hong Kong franchised bus operation that still accounts for over 90% of the Group's top-line revenue.

Whilst the public transport market in Hong Kong is essentially a mature market with passenger growth generally in line with the relatively slow population growth, and while Hong Kong can boast one of the best public transport systems in the world, the situation on the Chinese Mainland is quite different. Public transport services on the Mainland are still in the developing phase and dominated by state-owned enterprises. The Central People's Government has now firmly embarked on a process of privatisation aimed at uplifting the quantity and quality of public transport services and reducing, if not eliminating, the heavy burden of Government subsidies. With strong economic growth and rising incomes in many provinces and cities, the potential growth in demand for public transport services is huge. With its wealth of operational experience, strong management and internationally recognised brand name, the Group is well placed to tap this potential and to contribute to the development of public transport services on the Mainland. The main challenges on the Chinese Mainland revolve around the need to learn to adapt to the local regulatory environment, to select the most promising projects from a myriad of possibilities and to identify joint venture partners with whom we can establish mutual rapport and respect.

Q: What are your investment priorities in terms of the allocation of capital resources and what is the rationale behind these priorities?

A: Over the next few years, apart from the redevelopment of the former Lai Chi Kok Bus Depot into a commercial and residential complex, the main engine for growth in the Group's business is going to be on the Mainland market. We shall continue to explore business opportunities on the Mainland and to invest in suitable projects that can be expected to contribute to the Group's profit. But while this may be the priority area in relative terms, we are mindful of our obligations and commitment, as Hong Kong's largest public transport provider operating under a Government franchise, to make continuous improvement to our franchised public bus services in Hong Kong. This has to be done also for a practical commercial reason, namely to maintain our competitive edge over other modes and against the background of the ever-rising expectations of our customers. We shall continue to invest in updating and upgrading our fleet of buses in Hong Kong, in minimising the impact of our operations on the environment and in training and developing our human resources.

Q: With increasingly competitive transport operations in Hong Kong and global uncertainties such as the weak US dollar and fluctuating oil prices, what can be done operationally and strategically to moderate impacts on the Group?

A: Our focus for the near term will be on controlling costs and improving productivity in areas that are within our own control. Fluctuations in exchange rates and oil prices are totally outside our control, but even there we shall be on the lookout for opportunities to gain some protection from hedging arrangements. Improving the internal productivity of our network, through realigning and rationalising our routes and redeploying our resources from catchments that have experienced reduced demand for our services to catchments where there is still unsatisfied demand, will be an important part of the strategy. On this, however, we shall need to work hard to gain the support of Government and of the community at large, as without such support the process of rationalisation will be extremely difficult to implement. We shall have to try to convince the community that the maintenance of excess capacity is wasteful and will eventually work against the interests of commuters at large.

At the same time, and as I have said before, the Group will keep on trying to sharpen its competitive edge in the Hong Kong market by continuously improving services and by seeking new opportunities for business growth on the Mainland.

Q: What business profile do you visualise for the Group in 10 years?

A: Our business strategy is to anchor our business activities firmly in our core competency — providing world-class public transport services to the communities that we serve. At the same time we will also seek business growth in related businesses. As well as further development of our Mainland operations, we shall continue to explore new business opportunities. Our successful launch of the highly innovative concept of RoadShow is an excellent example of what could be done.

I am sure that, in 10 years' time, KMB will still be a key player in the Hong Kong public transport scene, and a recognised leader and standard setter in the international bus industry. But the Group's business in other areas will have grown substantially and will, I believe, be making a contribution to the Group's profit that will at least equal that from the Hong Kong franchised bus operation.

Q: Corporate social responsibility is now on the agenda of companies across the globe. To what extent does KMB address environmental, social and economic issues as integral aspects of its business strategy?

A: We recognise that active corporate citizenship requires us to look at sustainability practices across our business – in business planning, day to day operations, staffing policies and long-term investment strategies. Additionally, we are in the transportation industry and that brings with it a serious level of responsibility towards the environment. The Group has never shirked this responsibility and continues to work on proactive policies and measures aimed at improved environmental performance. As a Group, we were particularly pleased that in 2004 our commitment to corporate social responsibility was recognised globally when we were invited to become a constituent member of the FTSE4Good Global Index.