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## INDUSTRY OVERVIEW

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*The information presented in this section has been derived from various official Government sources. None of the information and statistics from the above sources is commissioned by our Group nor the Sponsor. Our Directors believe that the sources of this information are appropriate sources for such information and have taken reasonable care in extracting and reproducing such information. Our Directors have no reason to believe that such information is false or misleading in any material respects or that any fact has been omitted that would render such information false or misleading in any material respects. The information has not been independently verified by our Company, the Vendors, the Sponsor, the Lead Manager, the Underwriters, their respective advisers or affiliates or any other party involved in the [REDACTED] and no representation is given as to its accuracy, and accordingly, the information contained herein may not be consistent with information from other sources and should not be unduly relied upon.*

### SOURCES AND RELIABILITY OF INFORMATION

Certain information provided in this section is derived from various official or publicly available sources including the following:

**WSD** is a government sector of the Government, which is responsible for sourcing and maintaining the city’s supplies of fresh and salt water.

**The Government Budgets** are official publications issued by the Government each year.

**DSD** is a government sector of the Government, which is responsible for providing world-class wastewater and stormwater drainage services enabling the sustainable development of Hong Kong.

**CEDD** is a government sector of the Government and a leading organisation engineering the development of Hong Kong.

**CSD** is a government sector of the Government, which aims to provide statistics covering various social and economic aspects of Hong Kong.

**WBDB** is a government sector of the Government, which is responsible for planning, management and implementation of public sector infrastructure development.

The information presented in this document from the above official authorities is freely accessible by the public. We are of the view that sources of information used in this section, which are derived from above official authorities of the Government, are reliable and not misleading.

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### MARKET OVERVIEW

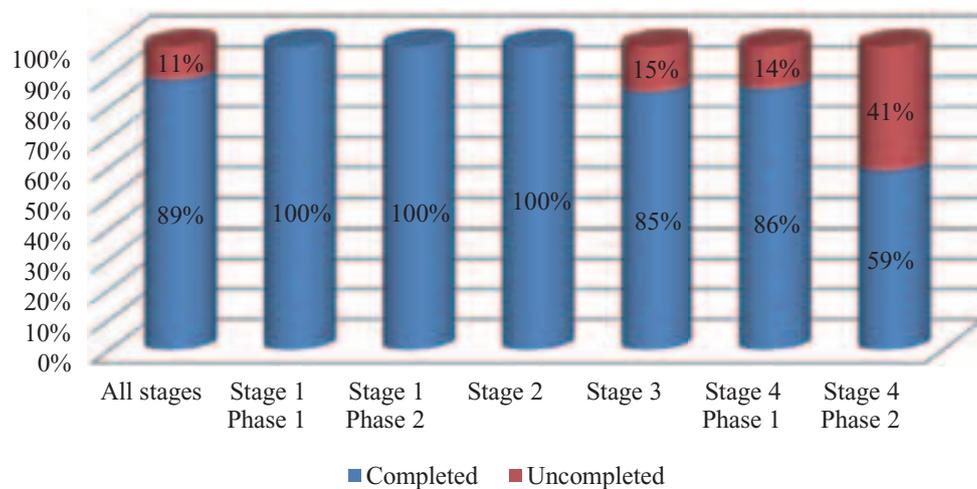
#### Water works improvement in Hong Kong

The fresh water and sea water supplies of Hong Kong are provided through a network of approximately 8,307 km of water mains. Most of these water mains are underground and were laid more than 30 years. These water mains are progressively approaching the end of their service life and have become increasingly difficult and costly to maintain. Ageing water mains are prone to bursts and leaks, resulting in water loss, disrupting water supply and causing inconvenience to the public.

In order to reduce supply interruptions arising from the leakages at and bursts of aged water mains, WSD has launched the Replacement and Rehabilitation of Water Mains Programme ("R&R Programme") since 2000 to replace and rehabilitate approximately 3,000 km of aged water mains within 15 years in four stages. The Government estimated the total cost for the replacement and rehabilitation of the aged water mains under the R&R Programme would be approximately HK\$23.6 billion.

The chart below illustrates the progress of works in respect of different stages under the R&R Programme as at 31 December 2014:

**Percentage of completion of works under the R&R Programme at different stages as at December 2014**



Source: Website of WSD ([www.wsd.gov.hk](http://www.wsd.gov.hk))

The Government will commission a review to appraise the condition of the remaining water mains which are not subject to the current R&R Programme. Subject to the review findings, the Government expects that the whole project will be completed by 2015.

As at the Latest Practicable Date, all waterworks contracts under the R&R Programme had been tendered and awarded by WSD.

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The following table illustrates the Government’s expenditure on the water supply projects under construction in Hong Kong for each of the fiscal years from 2010 to 2014:

	2010	2011	2012	2013	2014
	(Actual)	(Actual)	(Actual)	(Actual)	(Estimated)
Expenditure of works under construction (HK\$ million)	3,387.7	3,311.2	3,519.0	3,951.1	4,499.5

Source: The Government Budgets for the fiscal years from 2011-12 to 2014-15 (www.budget.gov.hk)

As shown above, the annual expenditure of the projects under construction of water supply increased from HK\$3,387.7 million in fiscal year 2010 to HK\$3,951.1 million in fiscal year 2013.

Given that the R&R Programme will complete in 2015, our Group intend to diversify its source of income by tendering more contracts originated from other departments of the Government, in particular, CEDD and DSD to sustain the Group’s business growth and ensure future profitability. Kwan On was upgraded to Group C Contractor (confirmed) and Group B Contractor (confirmed) under the “Roads and Drainage” category and “Site Formation” category on 26 February 2013 and 19 June 2013 respectively which will enable it to tender any number of contracts under the two categories with larger contract sum. Please refer to the paragraphs headed “Drainage service in Hong Kong” and “Slope works in Hong Kong” under this section for the details of the works and opportunities under the aforesaid two categories.

### Drainage services and roads works in Hong Kong

DSD is responsible for providing wastewater and stormwater drainage services in Hong Kong. North New Territories and North West New Territories are the major flood-prone areas in Hong Kong. The low-lying topography, inadequate drainage capacity of the natural watercourse and heavy rainstorms have been the principal causes of flooding in these areas. In addition, the existing drainage system in some old urbanised areas such as Mongkok and Sheung Wan, are becoming inadequate to meet the current flood protection standards due to the aging of the drainage system and flooding occurs frequently during the heavy rainstorms. To mitigate the flooding problem, DSD has implemented a series of major flood control projects to tackle the flooding problem since 1990’s.

Long term improvement measures implemented or being considered by DSD involves the following major works:

1. expansion and improvement of existing drainage system to increase the flow capacity and facilitate more effective collection of surface runoff;
2. river training works for effective discharge of storm flow;
3. tunneling works for interception and diversion of storm flow from upland catchment for direct discharge into the sea, thus avoiding the storm flow from overloading the downstream drainage system;

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4. flood storage facilities to temporarily retain storm flow from upland catchment in order to attenuate the peak runoff loading for the downstream drainage system;
5. stormwater pumping scheme to remove directly storm flow at flood prone areas; and
6. village flood protection scheme comprising a protective bund to stop storm flow from entering into a low-lying village and a stormwater pumping station to pump away storm flow collected within the village.

The following table illustrates the expenditure on capital projects, the length of stormwater drains and watercourse under management and inspected for each of the fiscal years from 2010 to 2014 in Hong Kong:

	2010 <i>(Actual)</i>	2011 <i>(Actual)</i>	2012 <i>(Actual)</i>	2013 <i>(Actual)</i>	2014 <i>(Estimated)</i>
Expenditure on capital projects (HK\$m)	1,976.7	1,926.1	1,987.8	1,263.8	858.3
Length of stormwater drains and watercourses under management (km)	2,689	2,707	2,718	2,723	2,733
Length of stormwater drains and watercourses inspected (km)	1,987	2,290	2,221	2,250	2,243

*Source:* The Government Budgets for the fiscal years from 2011-12 to 2014-15 ([www.budget.gov.hk](http://www.budget.gov.hk))

The annual expenditure decreased from approximately HK\$1,976.7 million in fiscal year 2010 to approximately HK\$1,263.8 million in fiscal year 2013. It is expected that the expenditure on capital projects of stormwater drainage will be approximately HK\$858.3 million in fiscal year 2014. The length of stormwater drains and watercourses under management of the DSD showed an increasing trend during the last 5 years. The length of stormwater drains and watercourses under management increased from a total of 2,689 km in fiscal year 2010 to 2,723 km in fiscal year 2013 and is expected to increase to a total of 2,733 km in fiscal year 2014. Meanwhile, the length of stormwater drains and watercourses being inspected each fiscal year ranged from 1,987 km in fiscal year 2010 to 2,250 km in fiscal year 2013 and is expected to increase to 2,243 km in fiscal year 2014.

In addition, according to the information published on the website of HyD, HyD had granted 11 roads and drainage work contracts to contractors between January 2014 and December 2014, the contract values of which range from approximately HK\$32.7 million to approximately HK\$8,399.9 million.

According to DSD's website, DSD announced on 26 March 2013 that the Kai Tak River improvement works is one of DSD's major flood prevention works and DSD plans to eliminate most of the remaining flooding blackspots in 5 to 6 years. DSD also keeps on conducting review studies for the drainage master plans for different districts with a view to reviewing the adequacy of the existing drainage system, updating and establishing flood

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prevention plans having regard to the latest land development and land use proposals. In addition, DSD also announced public tenders for several drainage projects in the second half of 2014.

### **Slope works in Hong Kong**

The Landscape of Hong Kong is fairly hilly to mountainous with steep slopes, heavy rain and dense development are prone to the risk from landslide. The Geotechnical Engineering Office (the “**GEO**”) of CEDD is responsible for setting safety standards and developing new technology, exercising geographical control, upgrading substandard Government slopes, mitigating natural terrain hazard and promoting slope maintenance and public awareness in slope safety. There are approximately 60,000 sizeable man-made slopes in Hong Kong, two thirds of which, or approximately 40,000 slopes, are government slopes. The Government spends approximately HK\$1 billion in upgrading and HK\$800 million in maintaining government slopes each year.

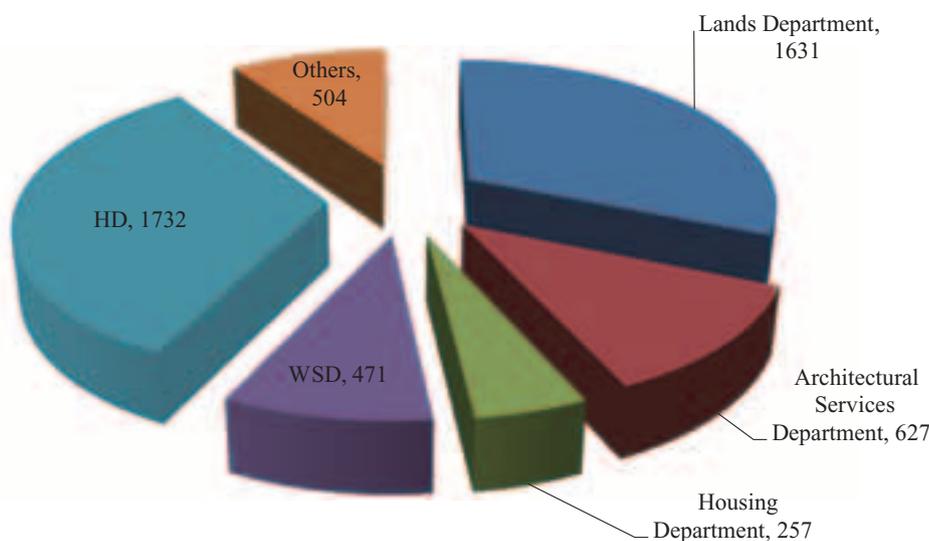
The studies and works under the Landslip Preventive Measures Programme (the “**LPMP**”) were completed in 2010. A long-term Landslip Prevention and Mitigation Programme (the “**LPMitP**”) has been launched to dovetail with the LPMP to deal with the remaining landslide risks associated with both man-made slopes and natural hillside. Under the LPMitP, the most deserving man-made slopes and natural hillside catchments are selected for studies each year in accordance with a risk based priority ranking system. The necessary landslip prevention and mitigation works, as identified by the studies, for man-made slopes and natural hillside catchments under the Government’s maintenance responsibility are implemented under the LPMitP. For private slopes found to be liable to become dangerous, statutory actions are taken against the responsible private owners by BD through the Buildings Ordinance to ensure its rectification. Apart from in-house resources, GEO also engages consultants in landslip prevention and mitigation studies and the letting and administration of contracts for the subsequent works. GEO awarded an average of about 10 consultancy agreements and 13 works contracts on landslip prevention and mitigation works each year.

It is the Government’s policy to improve the environment and to make slopes look as natural as possible in their surroundings. Hence, apart from maintaining the highest standard of slope safety, GEO is committed to ensure that landscape treatments to all man-made slopes are upgraded and natural hillside mitigation measures are implemented under the LPMitP.

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The chart below illustrates the total number of Government slopes being upgraded under the LPMitP as at 30 September 2014:

**Total number of government slope upgraded**



Source: Website of CEDD ([www.cedd.gov.hk](http://www.cedd.gov.hk))

The following table illustrates the expenditure for landslip prevention and mitigation works from fiscal years 2010 to 2014 in Hong Kong:

	2010 (Actual)	2011 (Actual)	2012 (Actual)	2013 (Actual)	2014 (Estimated)
Expenditure for landslip prevention and mitigation works (HK\$m)	1,262.3	997.0	1,038.0	1,029.0	1,000.0

Source: The Government Budgets for the fiscal years from 2011-12 to 2014-15 ([www.budget.gov.hk](http://www.budget.gov.hk))

The annual expenditure maintained at a relatively stable level during the last 5 fiscal years.

### Site formation works in Hong Kong

One of the major services of CEDD is to provide land and infrastructure. CEDD undertakes site formation and reclamation works to form land to meet different development needs.

For contractors who want to tender works projects in relation to landscaping or providing necessary utilities such as access roadways and drainage, it is required that the contractors must be listed in the Contractor List under the category of “Site formation” and CEDD is mainly responsible for servicing and monitoring the performance of all contractors within this category. In addition to that, all contractors must be registered to be an approved contractor for site formation works under Building Authority since 15 November 2004 (with

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grace period of 6 months to 17 May 2005) to tender projects of this category. According to the Contractor List published by WBDB as at the Latest Practicable Date, there were [79] approved contractors falling within this category, of which [56] were accredited with probationary status.

In the second half of 2014, CEDD plans to hold public tenders for LPMP, site formation and roads and drainage in different areas of HKSAR. Set out below are the tendering projects in the forecast of invitations to tender of CEDD for the period from March to June 2015 which Kwan On is eligible to tender for:

Contract No. & Title of contract	Probable date of inviting tenders	Works category & Lowest Group permitted to tender	Range of estimate of cost
NE/2014/02 Liantang/Heung Yuen Wai Boundary Control Point Site Formation and Infrastructure Works	Mar 2015	N/A	Exceeding HK\$300 million
NE/2014/03 Liantang/Heung Yuen Wai Boundary Control Point Site Formation and Infrastructure Works	Mar 2015	Roads and drainage Group C	Exceeding HK\$300 million
NE/2014/05 Ma On Shan Development – Roads, Drainage and Sewerage Works at Whitehead and Lok Wo Sha, Phase 2	Mar 2015	Roads and drainage Group B&C	From HK\$100 million, to HK\$200 million
GE/2014/04 Landslip Prevention and Mitigation Programme, 2011, Package F, Landslip Prevention and Mitigation Works in Kowloon and New Territories East	Mar 2015	Landslip preventive/ Remedial works to slopes/ Retaining walls	From HK\$100 million, to HK\$200 million
GE/2015/05 Landslip Prevention and Mitigation Programme, 2013, Package E – Ground Investigation for Landslip Prevention and Mitigation Works	Apr 2015	Ground Investigation Field Work	Up to HK\$100 million
GE/2014/02 Landslip Prevention and Mitigation Programme, 2010, Package I, Landslip Prevention and Mitigation Works in the New Territories	Apr 2015	Landslip preventive/ Remedial works to slopes/ Retaining walls	Up to HK\$100 million
Formation, Roads and Drains in Area 54, Tuen Mun – Phases 1 and 2	May 2015	Site Formation Group C	Exceeding HK\$300 million
Provision of Universal Access Facilities for Highway Structures – Package 1 Contract 2	May 2015	Roads and drainage Group C	From HK\$200 million, to HK\$300 million
GE/2015/06 Landslip Prevention and Mitigation Programme, 2013, Package D, Landslip Prevention and Mitigation Works	Jun 2015	Landslip preventive/ Remedial works to slopes/ Retaining walls	From HK\$100 million, to HK\$200 million

*Source:* Forecast report of invitations to tender of CEDD (07-12.2014)

Our Group has not submitted any tender in respect to the above forecast of invitations to tender of CEDD since most of the above forecast of invitations to tenders have not opened for tendering yet.

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### TENDERING FOR PUBLIC SECTOR PROJECTS IN HONG KONG

Public sector contracts in Hong Kong are normally awarded through open and competitive tendering procedures with a view to obtaining the best value for money. Tenders may be invited in the following ways:

**(i) Open tendering**

Tender invitations are published in the Government Gazette on every Friday, on the Internet, and if necessary, in the local press and selected overseas journals. All interested contractors are free to submit tenders.

**(ii) Selective tendering**

Tender invitations are published in the Government Gazette on every Friday, or are sent by letter to all contractors on the relevant lists of approved contractors for the purpose of selective tendering. Contractors not currently on the lists may also be considered provided that there is sufficient time to complete the qualification procedure.

**(iii) Prequalified tendering**

Prequalified contractors which are approved by the Permanent Secretary for Financial Services and the Treasury of Hong Kong will receive tender invitations. Invitations to apply for prequalification may take the form of open tendering or selective tendering and the respective procedures will apply.

**(iv) Single and restricted tendering**

Tender invitations are only sent to one or a limited number of contractors/suppliers approved by the Permanent Secretary for Financial Services and the Treasury or the Director of Government Logistics of Hong Kong. This tendering method is only used when the circumstances do not permit open tendering, for example, on grounds of extreme urgency or security, for proprietary products or for reasons of compatibility.

Individual works departments procure services at their discretion under the general supervision of WBDB. WSD, CEDD and DSD/HyD are the principal Government authorities that are responsible for procuring waterworks services, landslip prevention and roads and drainage works respectively for the public sector in Hong Kong. Generally, the procuring department is required to provide in the tender documents all the necessary information to assist the bidders to prepare their tenders, including standard contract forms covering the general aspects of tender and contract requirements, special conditions of contract, detailed price schedules, additional information and instructions applicable to a particular contract. Moreover, the procuring department is responsible for evaluating the tenders to determine whether they satisfy the conditions and specifications laid down in the tender documents.

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There are two common approaches to evaluate tenders, namely formula approach and marking scheme approach. These two methods evaluate the tenderers’ experience, past performance record and particular technical ability systemically. The formula approach is usually applied for general works projects, while the marking scheme approach is generally used for non-recurring and relatively complicated projects which require evaluation on the particular ability and past experience on the contractor candidate. Both approaches take into consideration the quality of work of the tenderers in addition to their financial bids.

Public sector projects in Hong Kong are sometimes contracted out by the main contractors to subcontractors and such subcontracts may also be awarded by way of tenders or upon private invitation. The selection criteria and process for subcontracting are determined by the main contractors.

### TENDERING FOR PRIVATE SECTORS PROJECTS IN HONG KONG

For private sector in Hong Kong, tenders are generally by invitation only and the contracts are awarded at the clients’ discretion. Usually, contractors for the private sector in Hong Kong are required to hold the relevant licences issued by BD, but need not be on the Contractor List and/or the Specialist List. Moreover, in addition to the competitiveness of the price quoted by the contractors, the job experience and track record of the contractors are also the determining factors to win a contract. When selecting subcontractors, the main contractors, regardless of whether it is a private or public project, may adopt similar selection processes. Hence, it is important for the subcontractors to establish good relationships with the customers and the main contractors as well as a good reputation in the market.

### COMPETITIVE LANDSCAPE

Contractors are eligible to tender for Government contracts provided that they are included in the Contractor List or the Specialist List under one or more of the work categories maintained by WBDB. In order to be listed as an approved contractor, the contractor has to apply for inclusion in the lists of particular work categories and/or groups and comply with the licencing requirements set forth in the ETWB Handbook. For details of the licencing requirements, the Contractor List and the Specialist List, please refer to the paragraphs headed “Contractor Licensing Regime”, “Contractor List” and “Specialist List” under the section headed “Regulatory Overview” in this document. According to the information published by WBDB, the number of approved contractors listed on the Contractor List for each work category as at the Latest Practicable Date was as follows:

Group	Building		Waterworks		Roads and Drainage		Site Formation	
	Confirmed	Probationary	Confirmed	Probationary	Confirmed	Probationary	Confirmed	Probationary
A	13	35	2	19	8	33	–	–
B	18	30	5	6	19	31	5	41
C	39	17	22	16	40	17	18	15

Source: Website of WBDB

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We compete primarily with those contractors who hold licences of the same status under the same categories on the Contractor List and the Specialist List as us. Our Directors consider that our main competitive strengths are: (i) our established operating history and proven track record; (ii) our diversified experience and capabilities; (iii) our experienced management team; and (iv) our stable relationships with our subcontractors and construction material suppliers. Further details of our competitive strengths are set out in the sub-section headed "Competitive strength" under the section headed "Business" in this document.

Based on the information contained in the above table, there were only 22 Group C contractors (confirmed) on the Contractor List under the category of "Waterworks". Kwan On, a member of our Group, is one of the Group C contractors (confirmed) under the category of "Waterworks". Kwan On is also one of the approved contractors among 40 Group C contractors (confirmed) under the category of "Roads and Drainage". Group C contractors are the highest ranking contractors in terms of tender limits, and can tender for public works with contracts sum of any value exceeding HK\$185 million. In addition, Kwan On is one of the Group A contractors (probationary) under the category of "Building" and one of the Group B contractors (confirmed) under the category of "Site Formation".

To serve as a main contractor of landslip preventive and mitigative works to slopes and retaining walls services works, a contractor must be listed on the Specialist List under the category of "Landslip Preventive/Remedial Works to Slopes/Retaining Walls" category maintained by WBDB. To be admitted to this category, the contractor also has to be a Registered Specialist Contractor for site formation works of the BD. According to the information published by WBDB, there were only 23 approved contractors with confirmed status listed under the category of "Landslip Preventive/Remedial Works to Slopes/Retaining Walls" on the Specialist List as at the Latest Practicable Date. Kwan On has been one of the approved contractors with confirmed status under such category since 2000.

Based on the Government's expenditure of approximately HK\$3,951.1 million for the fiscal year 2013 and the estimated expenditure of approximately HK\$4,499.5 million for the fiscal year 2014 on the projects of water supply, our revenue generated from provision of waterworks engineering services for the public sector for each of the two years ended 31 March 2014 of approximately HK\$158.9 million and HK\$208.1 million represented approximately 4.0% and 4.6%, respectively, of the above expenditure.

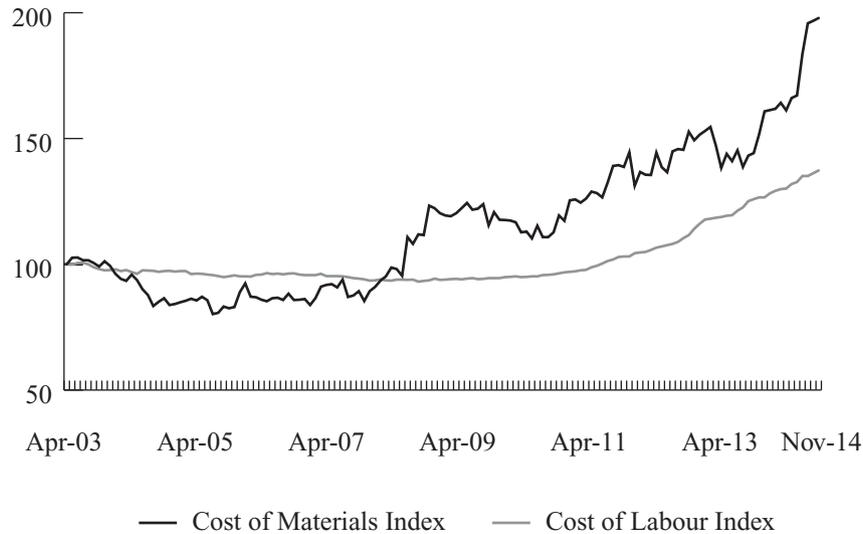
Based on the Government's expenditure of approximately HK\$1,263.8 million for the fiscal year 2013 and the estimated expenditure of approximately HK\$858.3 million for the fiscal year 2014 on capital projects of stormwater drainage, our revenue generated from provision of roads and drainage works for the public sector for each of the two years ended 31 March 2014 of approximately HK\$43.2 million and HK\$107.9 million represented approximately 3.4% and 12.6%, respectively, of the above expenditure.

Based on the Government's expenditure of approximately HK\$1,029.0 million for the fiscal year 2013 and the estimated expenditure of approximately HK\$1,000.0 million for the fiscal year 2014 on capital projects for landslip prevention and mitigation works, our revenue generated from provision of LPM Services for the public sector for each of the two years ended 31 March 2014 of approximately HK\$109.8 million and HK\$63.3 million represented approximately 10.7% and 6.3%, respectively, of the above expenditure.

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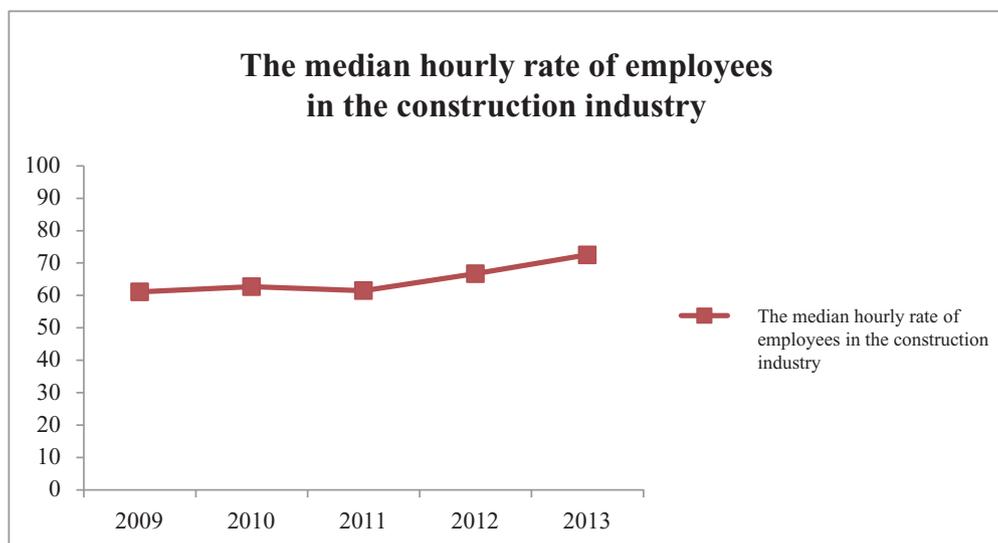
### HISTORICAL TREND OF CONSTRUCTION COSTS IN HONG KONG

**Index Numbers of the Costs of Labour and Materials Used in Public Sector Construction Projects (April 2003 = 100)**



Source: CSD – <http://www.censtatd.gov.hk/>

As shown in the graph above, the cost of materials used in public sector construction projects has been increasing since 2009. The cost of material index reached its peak to 197.9 in November 2014. The cost of labour index is quite stable comparing to the cost of materials index, it increased gradually since May 2009 from a level of 94.0 to the highest of 137.3 in November 2014. Both of the cost of materials and labour indexes showed an increasing trend over the past few years.



Source: CSD – <http://www.censtatd.gov.hk/>

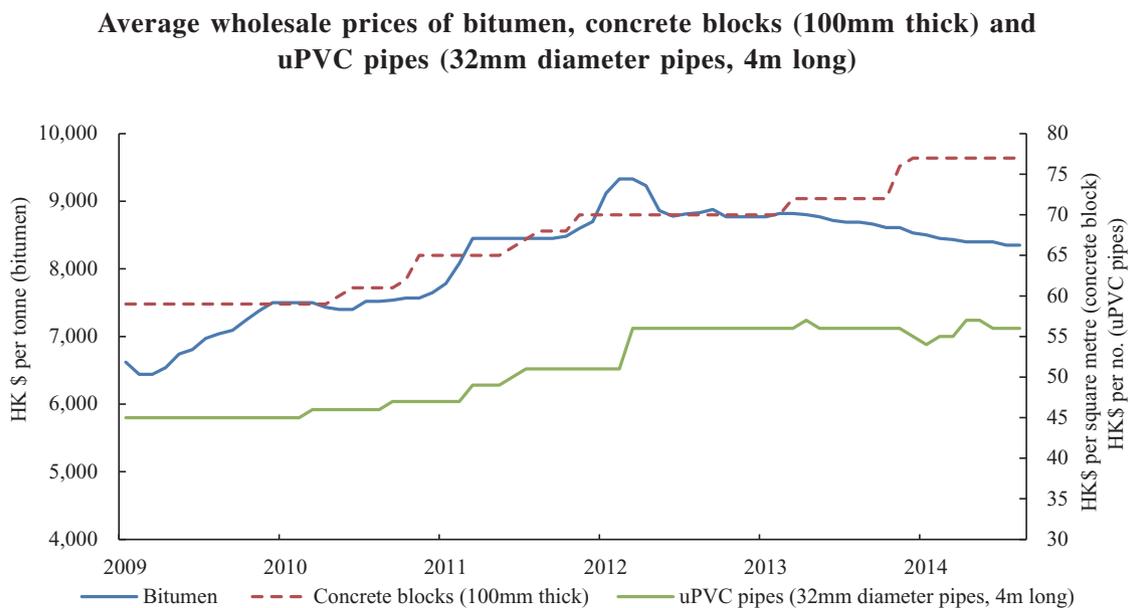
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As shown in the graph above, the median hourly rate of employees in the construction industry has remained at a relatively stable level from 2009 to 2011 and has been increasing gradually thereafter.

### *The prices of construction materials*

Construction companies make use of various construction materials in construction projects. The prices of construction materials are influenced by a number of factors including, but not limited to, the demand for construction materials, size and intensity of construction projects, prices of international commodities and foreign exchange rate fluctuation. The graphs below set out the average wholesale prices of construction materials commonly used in our construction projects as regarded by our Directors:

### *The average wholesale prices of bitumen, concrete blocks (100mm thick) and uPVC pipes (32mm diameter pipes, 4m long)*



Source: CSD – <http://www.censtatd.gov.hk>

### *Bitumen*

The average wholesale price of bitumen increased gradually from HK\$6,440 per tonne in May 2009 and reached its peak of HK\$9,330 per tonne in April 2012. After reaching its peak, the average wholesale price of bitumen moved within the range of HK\$9,330 per tonne and HK\$8,350 per tonne between May 2012 and October 2014.

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### *Concrete blocks*

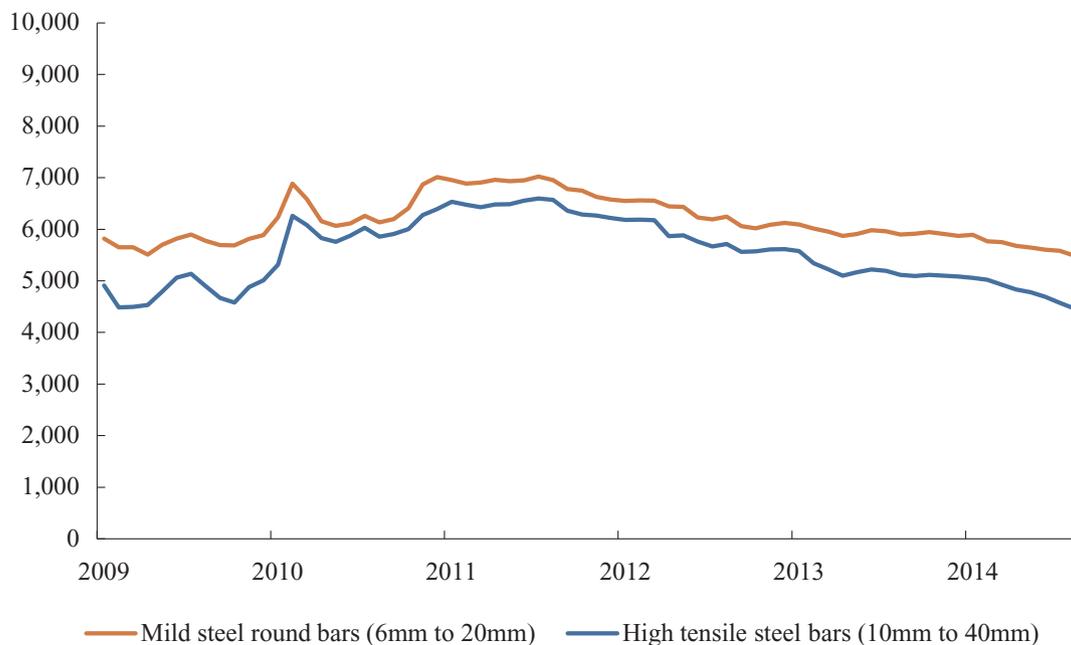
The average wholesale price of concrete blocks remained relatively stable at the range of HK\$59 per sq.m. to HK\$62 per sq.m. from 2009 to 2010. After that, it increased gradually to HK\$70 per sq.m. in January 2012 and remained stable until April 2013. In May 2013, the average wholesale price of concrete blocks increased slightly to HK\$72 per sq.m. and further increased to HK\$77 per sq.m. in October 2014.

### *uPVC pipes*

The average wholesale price of uPVC pipes increased gradually from HK\$42 per pipe in April 2008 to its peak of HK\$57 per pipe in June 2013. After that, the average wholesale price of uPVC pipes remained stable among HK\$56 per pipe.

*The average wholesale prices of mild steel round bars (6mm to 20mm) and high tensile steel bars (10mm to 40mm)*

**Average wholesale prices of mild steel round bars (6mm to 20mm) and high tensile steel bars (10mm to 40mm)**



Source: CSD – <http://www.censtatd.gov.hk>

### *High tensile steel bars and mild steel round bars*

The average wholesale prices of high tensile steel bars and mild steel round bars exhibited a similar pattern since 2009. Based on the average wholesale price statistic published by CSD, the average wholesale prices of high tensile steel bars and mild steel round bars increased from HK\$4,531 per tonne and HK\$5,510 per tonne in June 2009 respectively to HK\$6,595 per tonne and HK\$7,021 in September 2011 respectively and demonstrated a downward trend in 2012 subsequently. The average wholesale prices of high

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tensile steel bars and mild steel round bars remained relatively stable at the range of HK\$[4,462] per tonne to HK\$[5,118] per tonne and HK\$[5,490] per tonne to HK\$[5,945] per tonne respectively during the last twelve month period.