

Chairman's Statement

Dear Shareholders:

When I was appointed Executive Chairman in June 2003, I was not unfamiliar with the Company as I had served on its Board as an Independent Director. I was fully aware that the Company was beleaguered with financial, business and legal tribulations.

At its peak, Yongnam was a sterling Company riding high in the latter half of the 1990s despite the devastating 1997 Asian Financial Crisis. During this period, we successfully completed a number of landmark projects including the Singapore Post Center, Kranji Racecourse, and Capital Tower. It was this confidence that saw Yongnam commit to a 7-hectare factory at its current premises in Tuas, Singapore. We also invested heavily in the modular strutting system for the deep excavations required in the construction of MRT stations and Expressway tunnels.

Since 1997, the economy has gone in a downwards spiral, resulting in the inevitable contraction of the entire construction industry. Particularly badly affected was infrastructure development (MRT and Expressways). This in turn burdened the Company with increased capacity and excessive inventory of steel struts. We had no choice but to seek and commit to jobs with lower margins in a shrinking market.

To add to our woes, we were also hit during this period by a series of project difficulties and financial control issues. In order to finance our new factory and ongoing projects, we had to approach banks for new credit and borrowing. Though our bankers have been supportive and understanding, these loans nevertheless resulted in a high liability status for Yongnam. This, in all honesty of disclosure, continues to exert an impact on our finances today.

In particular, one name, *Springleaf Tower*, remains our highest priority for settlement. In 1999, Yongnam entered into an agreement whereby it agreed to receive the 23rd floor of the building in payment of what it was owed for its construction work. Yongnam completed the project in 2001 with funds borrowed from a finance company but Yongnam has not yet received the 23rd floor (Please refer to Investment Property on page 30 - Notes to the Financial Statements - for more details). This evolved into a legal tussle which is now before the Court of Appeal. This, together with

bad debts and un-claimable variation works, has adversely affected Yongnam's financial position.

It was a critical period. The Board realized it must make radical changes to overcome the multitude of challenges faced by the Group. We began by re-examining ourselves. Speed, Simplicity and Self-confidence became the motto for all staff. Troubleshooting, critical analysis and improvement were daily routines. Our Finance Department had since been restructured, enhancing its ability to provide management with faster and better financial information for decision-making. We have also revamped our Project Management team, as part of our efforts to better control costs and expenditures.

In addition, Yongnam implemented other cost-savings and cash-flow improvement programmes, including the employment of a Legal Officer to better manage the rampant disregard for proper payment within the construction industry. Improvements in communication between project managers, QS and finance officers had also resulted in more efficient collection of certified works.

In June 2003, the Company undertook a capital reduction exercise whereby the par value of its shares was reduced from \$0.20 each to \$0.01 each. Three months later in September 2003, the Company implemented the Scheme of Arrangement pursuant to Section 210 of the Companies Act (Cap. 50) between the Company, Yongnam Engineering & Construction (Private) Limited (YNEC) and the unsecured creditors of YNEC. To date, a total of 254,763,540 Scheme shares had been issued. Upon the completion of the allotment and issue of all the Scheme shares, approximately \$25.5 million of the YNEC debts was fully settled.

After almost a year of relentless hard work, the business transformation and debt restructuring plan were partially accomplished at year end. With the effects of wage reductions, and further bolstered by support from our suppliers, sub-contractors, bankers and service providers, end results had been encouraging. Nonetheless, we acknowledge more work needs to be done.

The Group's results for FY2003 were as follows: Group revenue increased by 6% from last year to \$65.3 million. The moderate growth in 2003 over

2002 was attributed largely to the contract for the Second Bangkok International Airport. We also significantly reduced our loss to \$15.5 million for 2003 from a net loss of \$29.9 million in 2002. The improvement was largely due to better operating margins and reduction of Finance Cost. Despite strenuous efforts to trim cost, total general and administrative expenses remained high and unchanged at \$13.8 million. As wages form a large component of our overheads, a flexible wage system will be implemented to control our manpower cost. Though we recorded an exceptional gain of \$13.7 million from the Scheme of Arrangement, the Board decided to offset this gain by making a full provision of \$12.2 million for Springleaf Tower. Overall, the balance sheet remained weak at year end.

Going forward, we need to think out of the box for strategies to deal with our difficulties. On the issue of modular strutting systems in our inventory, we view it as a new edge to our competitiveness in the Specialist Civil Engineering business. Our modular system of components is fabricated in the factory under stringent quality control and accuracy so as to ensure the overall safety of the strutting system and to provide an effective restraint and limit soil movement in deep excavations. In Singapore, we have successfully designed and constructed the strutting system in six contracts along the MRT North East Line. With such ready stock in hand, we can cater to projects faster, more efficiently with greater safety, and at better pricing than our competitors as a result of the increased steel prices.

During the year, Samsung Corporation Engineering & Construction Group and Taisei Corporation awarded us major contracts, namely the Kallang/Paya Lebar Expressway (KPE) C423 and the KPE C424, both of which are currently in progress. Together with KPE C421 which we secured in FY2002, almost 80% of the subcontract for 9-km long KPE tunnel section is undertaken by Yongnam. As for the Circle Line (CCL) stage 1 contract, we are currently installing the strutting system for C825. We will also be commencing work soon for CCL stage 3 C853a Bishan station. To cater to these deep excavation projects, Yongnam has its own team of experienced consultants and staff, who are both familiar with the soft and difficult marine clay environment, working depths of 30m and spans of 80m.

Yongnam is also currently collaborating with the key main tenderers for the MRT Circle Line stage 4 and 5 projects. These projects which require deep excavations are scheduled to start in the third quarter of 2004, with completion targeted to be in 2010. The timing is ideal for Yongnam as the KPE project is scheduled for completion in 2007.

As for our Structural Steelworks business, we have identified a plethora of opportunities in the overseas market, particularly China, Malaysia and the Middle East. The regional engineering & construction sector is experiencing a bullish upswing with rising spending and an increasing number of new major projects. The 2008 Beijing Olympics is also initiating many new projects including a sports stadium, toll roads, bridges and other support infrastructure. These are structural steel engineering jobs that Yongnam will focus on. Yongnam has been working on the new Second Bangkok International Airport and sections of the Hong Kong MTRC tunnel system. These opportunities, and in turn the entire market, would come to fruition in the near future with the establishment of the ASEAN Free Trade Area.

Yongnam has always been one of the leaders in the Mechanical & Engineering sector. To better capitalize on our legacy in this area, we are switching to a project-based employment system to trim expenditures for new projects. We have recently signed a MOU with Ishikawajima-Harima Heavy Industries Co. Ltd (IHI) and Alstom K.K. (Japan) for the supply and fabrication of steel for the electrostatic precipitator & fuel desulphurization, boiler and ducting structure in the 3 X 700MW coal fire power plant for the Tanjong Bin project in Malaysia. Subject to final project negotiations, this contract is valued at approximately US\$11 million. We expect to commence work on the project in the later part of the year.

In order to build upon our capabilities and strength in mechanical engineering, Yongnam is pursuing projects for the decommissioning and removal of offshore Oil & Gas facilities in Malaysia and Indonesia. We are also looking at the possibilities involving the installation and commissioning of the Wind Power Plants in China. Preliminary studies/discussions have been held with relevant parties, and we believe that these two new areas of business will bring major growth and technology opportunities to Yongnam if current discussions are successful.


The planned initiatives to be implemented in the coming months include the capitalization of approximately S\$10 million in debts and a rights issue, which would bring in additional working capital (Please refer to Additional measures to further improve the Group's financial position on page 16 - Notes to Financial Statements - for more details). When these measures are implemented successfully, the Group's financial position would be improved. We will continue to explore opportunities with our bankers and potential investors to quickly and significantly reduce our debts. Our marketing capabilities for winning new jobs are at the moment still restrained by our weak financial situation.

At this point I wish to extend my gratitude to our staff, who have continued to believe in Yongnam and were both enthusiastic and receptive towards our new measures. I am equally grateful to our bankers and suppliers, who have continued to support Yongnam in our operations, giving us the strength and capability to continue the battle.

In particular, I would also wish to acknowledge Mr. Tan Tin Nam, our founder and previous Chairman. His steady resolve, acumen, and integrity, has not only made my job as Chairman easier, it has also made this turnaround process much more bearable.

It is still a long journey from this day on. However, we know that the storm has passed. Though the challenges ahead continue to be daunting, I have no doubt that with the strong support of management, staff, bankers, suppliers and shareholders, Yongnam will emerge stronger from the doldrums and eventually regain our position as the leader for structural steelworks and specialist civil engineering.

Sincerely,



Kevin Yap Foo Seong
Executive Chairman
12 May 2004