

Management Discussion and Analysis – Business Review



Helping customers at our new Customer Service Centre in Tsimshatsui

This business review outlines the major activities of the various business streams within the CLP Group during the first half of 2002.

Hong Kong Electricity Business

The Group's core Hong Kong electricity operations, carried out by CLP Power, supply electricity to more than two million customers, representing a population of approximately 5.4 million in Kowloon, the New Territories, Lantau and a number of outlying islands. In the first half of 2002, local unit sales of electricity increased by 3.6% over the same period last year. The commercial sector registered a modest increase of 3%. Sales to the manufacturing sector were down by 6.3%, reflecting the continuing contraction of Hong Kong's manufacturing base. Higher than normal temperatures during the period pushed up the sales to the residential sector by 7.3%. The Government and others sector maintained a steady sales growth of 6.6%. Completion of new sewage

treatment projects, extension of education institutions, improvement to public facilities and railway expansions were among the prominent key drivers. Electricity sales to Guangdong Guang-Dian Power Grid Group Company Limited remained at a high level. Total unit sales, including sales to the Chinese mainland, rose 7.6%.

CLP Power maintains its efforts towards improving productivity and keeping operating costs to a minimum. Customers are already benefiting from these productivity drives through an average net tariff that is the lowest in Hong Kong. In January 2002, CLP Power gave a package of rebates and fuel clause reductions to all its customers, totalling about \$560 million. This represents an average tariff reduction of 2.2%. CLP Power's basic tariff has also remained unchanged for the fourth consecutive year.

CLP Power continues to enhance its supply quality and reliability, as well as provide for demand created by new towns and infrastructure development projects in our supply area. Capital expenditure in the transmission and distribution networks during the period amounted to HK\$1,704 million. Major projects included the Tseung Kwan O – Tai Wan 400kV circuit, Sham Tseng substation, Ma On Shan B substation, Sai Kung and Yau Tong Bay substations. In addition, CLP Power also invested HK\$153 million in customer services and other supporting facilities.

After winning the prestigious "2001 Hong Kong Award for Services – Customer Service" last December, CLP Power has again won four awards in the "Hong Kong Association for Customer Service Excellence Award 2001". These awards include Overall Champion of Customer Service Excellence Function Award as well as other awards for customer service, hotline service and field service.

CLP has an absolute commitment to safety. CLP Power and a number of its operating units were awarded the Bunny Matthysen Trophy and the NOSCAR Award for 2001 for their excellence in occupational safety and health management in the past year. Locally, CLP Power received awards in the "Hong Kong Occupational Safety & Health

Awards" jointly organised by the Hong Kong Occupational Safety & Health Council and the Labour Department.

CLP Power's good financial standing was illustrated by the issue of a 10-year US\$300 million bond in May. The bond issue was priced at 105 basis points over the 10-year US Treasury Note. This is the lowest Hong Kong-based corporate coupon in the last 20 years. The transaction was nearly eight times over-subscribed with over US\$2.6 billion in orders from Asian and European investors.

Regional Electricity Businesses

CLP has been selectively pursuing business opportunities in the Chinese mainland and elsewhere in the Asia-Pacific region.

Chinese Mainland

The operation of the 3,000MW joint venture in Shandong Province, in which CLP Power China (CLP-PC) holds a 29.4% interest, has been satisfactory. Shiheng I (2x300MW) and II (2x300MW) Power Stations maintained their First Class Power Station title and were awarded the ISO 14001, ISO 9001 and Occupational Health and Safety Assessment Series 18000 Certification. This reflected their good performance in environmental protection, quality assurance and occupational health and safety. The construction of Heze II Power Station (2x300MW) and Liaocheng Power Station (2x600MW) is progressing well,

to budget and ahead of schedule. We anticipate that Heze II will start commercial operation this year.

The operation of CLP Guohua Power Company Limited, which owns three operating power stations with a total installed capacity of 2,100MW in the Beijing-Tianjin-Tangshan area and in which CLP-PC holds a 49% interest, has been satisfactory. New tariffs for these power stations have been implemented, effective January 2002.

The Guangdong Daya Bay Nuclear Power Station, in which Hong Kong Nuclear Investment Company Limited owns a 25% interest, continued to maintain international performance levels with ISO 14001 re-accreditation in 2002. Regular exchanges continue with international bodies including the International Atomic Energy Agency and the World Association of Nuclear Operators.

Good progress has been made in plant construction in the Huaiji Power Project, in which CLP-PC owns a 41.5% equity interest. Five out of the nine hydro power stations are already in operation. The 110kV transmission line connecting the 98MW joint venture hydro power stations at Huaiji County, Guangdong Province, to the Zhaoqing power grid has successfully been put into operation. Generating units at Yutiao and Gaotang Power Stations are being commissioned. This renewable energy project utilises the abundant water resources in the Huaiji County and generates and supplies electricity to this remote county in the north-western border of Guangdong Province and the nearby areas.

Shareholders may recall that, in consortium with ExxonMobil, CLP Enterprises had submitted a bid to participate in the West-East Gas Pipeline project in the Mainland. The exploitation of the gas reserve in Western China is a massive endeavour in which CLP is keen to participate. After careful consideration, we decided not to pursue a shareholding in the pipeline itself. We believe that involvement in future downstream gas-fired power stations represents a route that will make better use of CLP's skills and experience.



Heze II Power Station, Shandong Province, China



Ho-Ping Power Station, Taiwan

Asia-Pacific Region

During the first half of 2002, CLP Power International (CLP-PI) has made significant progress in implementing its joint venture with Powergen in Australia, India and Thailand, and in the commissioning of Ho-Ping Power Station in Taiwan.

Through the CLP-Powergen joint venture which is 80% owned by CLP-PI and 20% by Powergen UK plc, CLP-PI has acquired an effective equity interest of 73.6% in Yallourn Energy, which owns and operates a 1,450MW coal-fired power station and a dedicated coal mine in Australia. In December 2001 industrial action was taken by employees in the mine maintenance area with the result that Yallourn Energy did not achieve its revenue targets for the year ending 31 December 2001. However, Management was able to resolve the issues under dispute and establish new workplace arrangements that now cover all employees at the site. This has enabled Yallourn Energy to move forward in its objective to introduce new technologies and flexible working practices that will improve efficiency and productivity.

In February 2002, the CLP-Powergen joint venture completed the acquisition of an 88% interest in Gujarat Powergen Energy Corporation (now renamed Gujarat Paguthan Energy Corporation Private Limited – GPEC), in which CLP-PI has an effective equity interest of 70.4%.

GPEC owns and operates a 655MW combined cycle power station in India. Efforts continue to obtain the consents from relevant lenders and regulatory authorities for the acquisition by the joint venture of the remaining 12% stake in GPEC, which is expected to be completed by the end of 2002.

In June 2002, Powergen notified CLP-PI of the exercise of a put option under the joint venture agreement to sell to CLP-PI 50% of Powergen's interest in the joint ventures. The joint venture agreement provides for the price payable by CLP to be decided by an independent expert, in the absence of agreement by the parties.

At the end of last year, CLP-PI completed the acquisition of an effective 40% equity interest in BLCP, which is developing a 1,434MW coal-fired power project at Map Ta Phut, Thailand.

The first 660MW coal-fired unit of Ho-Ping Power Station in Taiwan, in which CLP-PI holds a 40% stake, has been successfully commissioned and started commercial operation on 1 June 2002. Unit 2 is also making good progress and will commence commercial operation in the second half of this year. The power station will improve the security of electricity supply in Taiwan, because of its geographical location near the load centre, and is expected to make a significant contribution to the earnings of CLP-PI.

Non-electricity Activities in Hong Kong and the Chinese Mainland

CLP is exploring opportunities to extend its non-electricity activities in Hong Kong and southern China by leveraging off our existing business, assets, skills and relationships.

2002 has been a difficult year for the telecommunications industry, and it is imperative for CLP TeleCom to position itself strategically to minimise the effect of adverse market conditions and to maximise return on investment.

With this objective in mind, CLP TeleCom has been reviewing its business model and direction to ensure they

are financially viable and reflect current market conditions, while exploring alternatives to maximise the competitive and strategic advantage for the company. For this reason, we have reached an agreement to partner with Cheung Kong Enterprises Limited (CKE) and Hongkong Electric Holdings Limited to launch a brand new broadband service, through a new technology called PowerCom Internet Access Technology. According to the agreement, CLP TeleCom will integrate its retail operations carried on under the Oxygen brand into PowerCom Network Hong Kong Limited, a joint venture between CKE and CLP TeleCom. We continue to own and operate "ChinaLink" which offers network service between Hong Kong and the Chinese mainland.

CLP Engineering is making steady progress in power engineering works for transmission and distribution projects. The success of these contracts will position CLP Engineering as a reliable, high quality and competitive contractor with capability in the full range of substation and cable projects including design, supply, installation, refurbishment and maintenance services. CLP Engineering also continued to provide contract engineering services for major Hong Kong enterprises such as the Mass Transit Railway Corporation, Kowloon-Canton Railway Corporation and the Hong Kong Airport Authority. CLP Engineering intends to build on this successful

performance by pursuing further work with these and other local clients.

Property Redevelopment in Hong Kong

CLP pursues the redevelopment of sites in Hong Kong which are no longer required for electricity purposes.

CLP's major current project is the residential redevelopment of the former power station at Hok Un, named Laguna Verde. This joint venture project, led by CLP Property and Cheung Kong, comprises 4,735 flats, 1,692 car parks and 270,000 sq. ft. of commercial space. Over 90% of the residential units in the redevelopment had been sold by the end of June 2002.

In June 2002, CLP Property obtained planning approval to develop a small decommissioned electricity substation site at Castle Peak Road in urban Kowloon. The envisaged redevelopment will have 65,000 sq. ft. of residential and retail space. CLP has no specific timetable yet for this project.

Research and Development Activities

In the first power project of its kind in Hong Kong, CLP Research Institute installed a renewable energy supply system on the island of Shek Kwu Chau. The innovative system comprises a wind turbine, a solar power system, a



Handover ceremony for the renewable energy supply system on Shek Kwu Chau



Team-building game at the Annual Reception of the 2002 CLP Internship Programme

solar hot water system, and a power house with a three-day battery supply system and standby generator. The system generates and stores sufficient electricity for an adjacent school and dormitory building. Meaningful data for important research into the use of renewable energy in Hong Kong is being captured. The system has been donated to the Society for the Aid and Rehabilitation of Drug Abusers on the island to help in the development of their drug abuse rehabilitation and community education work.

Our People

On 30 June 2002, the Group employed 4,205 staff (2001: 3,966), of whom 3,747 (2001: 3,596) were employed by CLP Power. Total remuneration for the six months ended 30 June 2002 was HK\$1,049 million (2001: HK\$1,070 million), including retirement benefit costs of HK\$67 million.

Talent acquisition is a key element in CLP's human resources strategy. This year, we have launched the CLP Executive Programme (CEP), which is designed to attract and develop future leaders through a structured programme of mentoring, job rotation, cross-functional project assignments and tailored career development. From over 870 applications, we have selected eight young

professionals, locally and overseas, as the first entrants to our CEP.

We have also continued the CLP Internship Programme (CIP) which encourages students to join CLP for a summer or 12-month secondment. The students are guided by a dedicated mentor and are given specific project assignments, deliverables and learning objectives. The CIP has an excellent reputation with local universities and students. In 2002, more than 50 interns have joined CLP on this Programme, a tenfold increase compared to five years ago.