Management Discussion & Analysis

1. Operations Review

The Group's business is organised into three main segments:

Hotel operation	–	Hotel ownership and operation
Hotel management	–	Provision of hotel management and related services to Group-owned hotels and to hotels owned by third parties
Property rentals	–	Ownership and leasing of office properties, commercial properties and serviced apartments

The Group's turnover from operations is derived principally from its hotels. The hotel businesses in the Group's core Asia Pacific region recovered quickly in the second half of 2003 following the June 2003 lifting of World Health Organization and government travel advisories concerning SARS (severe acute respiratory syndrome). The continued turnaround of these businesses in 2004 exceeded expectations, with both room and food and beverage revenues improving significantly. Overall weighted average annual occupancy of Group-owned hotels climbed to 71% compared to 55% for 2003, while weighted average room yield ("RevPAR") registered a 40% year-on-year increase.

The performance of the Group's investment properties generally showed improvement with the exception of serviced apartments in Beijing; commercial properties in Changchun, Singapore and Malaysia; and office properties in Malaysia.

Revenue

For the year ended 31 December

	Combined Revenue by Trade				
	2004		2003		%
	US$ million	%	*US$ million*	%	*Change*
Hotel Operation	970.0	81%	696.3	77%	39%
Hotel Management	12.4	1%	8.3	1%	49%
Property Rentals	215.0	18%	196.9	22%	9%
Total	1,197.4	100%	901.5	100%	33%

Breakdown of Turnover

For the year ended 31 December

	Subsidiaries			Associated Companies		
	2004 *US$ Million*	2003 *US$ Million*	% *Change*	2004 *US$ Million*	2003 *US$ Million*	% *Change*
Hotel Operation						
The People's Republic of China						
Hong Kong	155.0	105.5	47%	–	–	N/A
Mainland China	208.0	149.6	39%	211.5	132.7	59%
Singapore	93.1	69.2	35%	20.8	15.2	36%
The Philippines	88.2	70.9	24%	–	–	N/A
Malaysia	78.6	63.2	24%	18.0	10.0	80%
Thailand	46.0	32.7	41%	–	–	N/A
Fiji	20.0	20.0	0%	–	–	N/A
Indonesia	–	–	N/A	24.7	22.4	10%
Myanmar	6.1	4.9	25%	–	–	N/A
	695.0	516.0	35%	275.0	180.3	52%
Hotel Management	12.4	8.3	49%	–	–	N/A
Hotels Sub-total:	707.4	524.3	35%	275.0	180.3	52%
Property Rentals						
The People's Republic of China						
Mainland China	5.8	5.1	12%	183.6	168.9	9%
Singapore	8.1	6.9	17%	8.4	8.1	4%
Malaysia	3.4	3.5	(3%)	4.9	3.8	30%
Thailand	0.8	0.6	38%	–	–	N/A
Properties Sub-total:	18.1	16.1	12%	196.9	180.8	9%
Total	725.5	540.4	34%	471.9	361.1	31%

Note: Revenue of the hotel management group is stated after elimination of revenue earned from fellow subsidiaries.

N/A Not Applicable

(a) Revenue

Hotel Operations

As at 31 December 2004, the Group has equity interest in 37 operating hotels, including the Portman Ritz-Carlton Hotel, Shanghai and the Shangri-La Hotel, Surabaya (in which the Group has only 10% interest).

The key performance indicators of the Group's hotels on a combined basis are as follows:

Country	2004 Weighted Average			2003 Weighted Average		
	Occupancy (%)	Transient Room Rate (US$)	RevPAR (US$)	Occupancy (%)	Transient Room Rate (US$)	RevPAR (US$)
The People's Republic of China						
Hong Kong	71	207	157	45	188	113
Mainland China	72	99	72	56	86	49
Singapore	77	111	84	56	105	63
The Philippines	71	101	70	59	92	57
Malaysia	73	64	46	58	59	36
Thailand	81	111	87	57	103	55
Fiji	65	97	80	63	92	60
Indonesia	47	94	40	39	92	32
Myanmar	48	33	15	37	34	12

Notes: (i) The RevPAR of hotels under renovation have been computed by excluding the number of rooms under renovation.

(ii) Performance indicators for hotels in Malaysia has included Shangri-La's Rasa Sayang Resort, Penang while the performance of the Shangri-La Hotel, Surabaya has not been included in these indicators.

(iii) Combined revenues are the aggregate of turnover of all operating subsidiaries and associated companies while consolidated revenues relate to operating subsidiaries only.

China World Hotel, Beijing – Horizon Club Lounge

Overall combined room rentals increased by 48% to US$521.9 million. Correspondingly, combined food and beverage revenue increased by 31%.

The People's Republic of China

Hong Kong

The Group's Hong Kong hotels experienced a strong recovery in 2004 supported by a growth in arrivals into Hong Kong. Arrivals increased by 40.4% year-on-year to a record 21.8 million. Mainland China continued to be Hong Kong's largest source market, with over 12.2 million arrivals. Major long-haul markets rebounded to pre-SARS levels. With accelerated integration with the mainland economy following the establishment of the Closer Economic Partnership Arrangement, or CEPA, growing confidence in the local economy, and the opening of Hong Kong Disneyland in September 2005, the outlook for the corporate and leisure travel markets in Hong Kong is expected to remain positive.

The Kowloon Shangri-La, Hong Kong ("KSL"), which completed major renovations in October 2003, benefited from the improved market conditions. The Island Shangri-La, Hong Kong ("ISL") has been undergoing a phased renovation of its facilities since mid 2003. Completion of the renovation is expected by April 2005. Consolidated revenues of the two hotels increased by 47% in 2004 largely due to the growth in RevPAR and food and beverage revenues. Combined room rentals increased by 77% while combined food and beverage revenues increased by 27%. The average room rates of ISL and KSL for the year reached US$238 and US$183, respectively. The Group expects to maintain this growth momentum throughout 2005.

Mainland China

In 2004, the Group's Mainland hotels recorded impressive growth in their business, reflecting both improved domestic travel in China and significant growth in international arrivals. Combined revenues of the hotels increased by 49%. Weighted average annual occupancies of all hotels increased by 16 percentage points to 72%, and weighted average room rates increased by 15% to US$99. All the hotels recorded increases in RevPAR, ranging from 12% to 151%. With the exception of the Traders Hotel, Shenyang, which faces an oversupply situation in its market, all hotels recorded positive growth rates in occupancy and room rates. The Group's flagship properties, the China World Hotel, Beijing (which completed major renovations in mid 2003) and the Pudong Shangri-La, Shanghai ("SLPU") recorded increases in RevPAR of 96% and 44%, and increases in room rates of 18% and 21%, respectively. The Shangri-La Hotel, Zhongshan, which opened for business in January 2004, achieved an average annual occupancy rate of 70%.

The Shangri-La Hotel, Fuzhou (wholly owned by the Group) soft-opened for business on 25 January 2005. The hotel is expected to have all its 414 rooms available for sale by mid April 2005. Phase 2 of SLPU which comprises 375 guest rooms and complementary facilities, will open for business in the third quarter of 2005. The Group is optimistic on the overall prospects of its hotel business in Mainland China for the foreseeable future.

Singapore

Business at all three Singapore hotels improved substantially with combined revenues increasing by 35%. RevPAR increases ranged from 24% for the Traders Hotel, Singapore to 36% for the Shangri-La Hotel, Singapore. With visitor arrivals improving, the outlook for the Group's hotels remains very positive.

The Philippines

The Group's Philippines hotels also recovered from their lacklustre performance of the previous two years. RevPAR increases ranged from 7% at the Edsa Shangri-La, Manila to 37% at the Makati Shangri-La, Manila. With the exception of Shangri-La's Mactan Island Resort, Cebu, which achieved a 14% increase in average room rates in 2004, the hotels in Manila posted a moderate average rate increase of 6%, indicating some rate resistance. The overall outlook for the Group's Philippines hotels is positive.

Malaysia

The strong performance of the hotels in 2004 was mainly attributable to significant improvements in occupancy levels. The combined revenues of all the hotels increased by 32% despite the closure of Shangri-La's Rasa Sayang Resort, Penang from 1 December 2004 for redevelopment. The Shangri-La Hotel, Kuala Lumpur achieved another year of solid growth, reflecting the on-going benefits of an extensive renovation programme completed in May 2003. This hotel recorded total revenue growth of 20% in 2004, with the occupancy rate increasing to 74% from 65% in 2003.

In Penang, occupancy at Shangri-La's Golden Sands Resort rose from 58% in 2003 to 79%, supported by a rebound in leisure arrivals from key regional and long-haul markets. Helped by a strong pick-up in business travel, occupancy of the Shangri-La Hotel, Penang increased to 70% from 55% in 2003. Both RevPAR and total revenues increased by 22%. Shangri-La's Rasa Sayang Resort achieved an average occupancy of 59% for its eleven months of operation. After careful consideration, the Group concluded that a major redevelopment of the resort is critical to re-establishing its position as one of the region's premier resorts. Accordingly, the resort ceased operations effective 1 December 2004. The Group has recognised a net loss of US$7.3 million in its accounts towards the retrenchment compensation paid to staff and discarding of fixed assets pursuant to the redevelopment which is scheduled for completion by end of 2006.

The Group's two resorts in Kota Kinabalu enjoyed buoyant leisure demand, particularly from Australia as well as the domestic market, achieving an annual average occupancy rate of 79%. The RevPAR of Shangri-La's Tanjung Aru Resort, Kota Kinabalu and Shangri-La's Rasa Ria Resort, Sabah increased by 38% and 67%, supported by 27% and 25% increases in room rates, respectively. The Group's Malaysia hotels and resorts are expected to further improve their performance in 2005.

Shangri-La Hotel, Bangkok – Swimming Pool

Thailand

Shangri-La Hotel, Bangkok completed a three-year major renovation programme and benefited from the recovery of the country's tourism industry. The hotel is home to the Group's very first CHI spa, which opened in July 2004, setting new regional standards of luxury and service for hotel spas. Hotel occupancy increased to 81% from 57% while room rates increased by 8%. The hotel also benefited from the conversion of three floors to serviced apartments in the Krungthep Wing, which enjoyed an average occupancy of 71%. The outlook in 2005 for the hotel remains very favourable.

Fiji

Renovation of the Lagoon Wing guest rooms at Shangri-La's Fijian Resort, Yanuca Island was substantially completed at the end of 2004. As a result, occupancy only increased marginally by 1% to 64%, while the average room rate rose by 7%.

Indonesia and Myanmar

The performance of the Shangri-La Hotel, Jakarta improved marginally with weighted average occupancy and weighted average room rates increasing by 8 percentage points and 3%, respectively. The performance of the Traders Hotel, Yangon continued to be adversely affected by Myanmar's problematic political and economic environment. Occupancy increased by 11 percentage points to 48% although room rates fell by 4%.

Hotel Management

The hotel management arm of the Group, SLIM International Limited and its subsidiaries (the "SLIM Group"), provides hotel management and/or technical consultation and project management services for hotels under development or renovation and hotel management and marketing services for operating hotels. The SLIM Group has hotel management and/or technical consultation and project management services contracts in respect of all the Group's hotels with the exception of the Portman Ritz-Carlton Hotel, Shanghai. As at 31 December 2004, it also had hotel management contracts in respect of 8 operating hotels owned by third parties.

Aided by the strong recovery of the hotels' business and successful signing of new contracts, the SLIM Group recorded a 49% increase in revenues. However, profit before tax and consolidation adjustments only increased to US$2.7 million from last year's US$0.7 million due to several cost factors, namely:

– the establishment of a hotel training centre, the Shangri-La Academy, in Beijing
– an increase in headcount required by the large number of new hotels and projects under development
– the launch of new central reservation and information management systems, and
– the continued expansion of regional sales offices to strengthen the Group's marketing network.

The Group believes that these expenditures will make significant contributions to future earnings.

In 2004, the Group signed seven new hotel management contracts:

- Traders Hotel, Chennai, India (opening in April 2005)
- Shangri-La Hotel, Suzhou, Mainland China (opening in late 2005)
- Traders Hotel, Media City, Dubai (opening in late 2006)
- Shangri-La Hotel, Palm Island, Dubai (opening in mid 2007)
- Shangri-La Hotel, Dongguan, Mainland China (opening in mid 2007)
- Traders Hotel, Urumqi, Mainland China (opening in early 2007)
- Shangri-La Hotel, Vancouver, Canada (opening in early 2008)

In August 2004 the Group assumed the management of the former Radisson Plaza at the Pier, in Cairns, north Queensland, Australia, and has successfully rebranded it as Shangri-La Hotel, the Marina, Cairns. The 256-room five-star hotel underwent extensive refurbishment, including the addition of 36 new rooms, which was completed in early 2005. The hotel is located in the new centre of the city, adjoining the popular Pier Shopping Centre, and is an ideal base for visits to the Great Barrier Reef and Daintree Rainforest.

In March 2004, the Group terminated its management contract for a hotel project in Zhengzhou, Mainland China due to inordinate delays in project implementation.

The 374-room Traders Fudu Hotel, Changzhou, Mainland China opened for business on 3 January 2005.

In March 2005, the Group signed three new hotel management contracts for the development of two Shangri-La hotels and one Traders hotel in Bangalore, the technology capital of India.

Property Rentals

The Group's investment properties are located principally in Shanghai and Beijing and are owned by associated companies. The average yields of the office space in the China World Trade Center ("CWTC") in Beijing, the Beijing Kerry Centre ("BKC"), the Shanghai Kerry Centre ("SKC") and the Shanghai Centre ("SC") recorded increases of 6%, 5%, 5% and 22%, respectively. These four centres also recorded an increase in yields of the commercial space ranging from 5% to 8%. The average occupancy rate for both the office and commercial spaces in these centres was above 90%. The SKC and SC serviced apartments recorded increases in yields of 8% and 15%, respectively. However, the yields of the serviced apartments in Beijing continue to suffer due to over supply. Yields of the serviced apartments in the BKC recorded a decline of 16% while the apartments in the CWTC registered a decline of 10%. The Century Towers Apartments in Beijing, and the serviced apartments in the Century Tower Apartments, Dalian both recorded a 5% increase in yields.

In Singapore, the average yields of serviced apartments increased by 18% and the commercial space registered a weighted average occupancy rates of 99%. Yields of the Singapore office space, however, registered a decline of 6%.

In Bangkok, yields of the office space registered a substantial increase of 77%, supported by an increase in the occupancy rate, from 58% to 88%.

In Kuala Lumpur, yields of the office space decreased by 4%, albeit yields of the serviced apartments increased by 19%. In Johor Bahru, yields of the commercial space increased by 13% while those of the office space remained unchanged.

(b) Consolidated Profits

Consolidated profits attributable to shareholders for 2004 increased to US$141.5 million from US$72.7 million in 2003. The financial performance reflected the combined effects of the 34% increase in consolidated turnover and one percentage point increase in the gross profit ratio.

The detailed breakdown of the profit is as follows:

Consolidated Profit Attributable to Shareholders

For the year ended 31 December

	2004 US$ Million	2003 US$ Million	% Change
Company & Subsidiaries			
Hotel Operation			
The People's Republic of China			
Hong Kong	32.8	12.5	164%
Mainland China	47.1	28.8	64%
Singapore	26.1	9.8	165%
The Philippines	13.1	9.8	34%
Malaysia	6.8	2.6	163%
Thailand	8.3	4.9	67%
Fiji	3.0	0.7	314%
Myanmar	(1.1)	(1.2)	7%
	136.1	67.9	100%
Property Rentals			
Mainland China	1.2	1.6	(24%)
Singapore	2.9	1.3	116%
Malaysia	0.8	0.4	92%
Thailand	0.2	0.1	67%
	5.1	3.4	47%
Hotel Management	0.6	(0.2)	NM
Associated Companies			
Hotel Operation			
Mainland China	12.5	4.7	169%
Singapore	0.6	–	NM
Malaysia	2.2	0.3	562%
Indonesia	0.2	(0.3)	NM
	15.5	4.7	232%
Property Rentals			
Mainland China	23.3	18.5	26%
Singapore	0.7	0.5	45%
Malaysia	0.5	0.4	40%
	24.5	19.4	26%
Operating Profit After Tax	181.8	95.2	91%
Less:			
– Corporate expenses net	(6.6)	(3.7)	(78%)
– Pre-opening expenses of projects	(3.8)	(0.8)	(354%)
– Net interest expenses on corporate borrowings	(31.9)	(40.2)	21%
– Net interest expenses on convertible bonds	(4.8)	–	NM
Profit before Non-Operating Items	134.7	50.5	167%

	2004 US$ Million	2003 US$ Million	% Change
Non-Operating Items:			
– Net realised and unrealised gains on other investments and provision for long-term investments	19.3	17.1	13%
– Discarding of fixed assets due to property renovations	(18.4)	(13.9)	(33%)
– Provision for impairment losses on other land	–	(9.5)	NM
– Surplus on valuation of investment properties	–	22.6	NM
– Amortisation of negative goodwill	5.5	5.9	(7%)
– Loss on disposal of 1.59% interest in a subsidiary	(1.2)	–	NM
– Retrenchment payout and discarding of fixed assets due to redevelopment of a resort	(7.3)	–	NM
– Reversal of deferred provision for taxation on possible future distribution of retained profits of a subsidiary after group reorganisation	8.9	–	NM
	6.8	22.2	(69%)
Profit attributable to shareholders of the Group	141.5	72.7	95%

Notes:

1. Interest expenses of operating units' bank borrowings and deferred tax provision are included in operating results.
2. All balances stated are net of share of minority interests.
3. Profit of the hotel management group is stated before elimination of revenue earned from fellow subsidiaries and operating results of the subsidiaries are stated before elimination of management fees charged by the hotel management group.

NM: Not Meaningful

(c) Consolidated Net Asset Value and Gearing Ratio

The substantial improvement of the operating results of the hotel business also enhanced the fair value of the hotel properties; this, together with the issuance of 183,832,000 new shares at HK$7.4 per share in February 2004 under an arrangement involving placement of existing shares and subscription top-up for new shares to certain companies within the Kuok Group, led to the substantial increment of the Group's net asset value. In addition, a total of 11,173,000 shares, 2,726,543 shares, 6,003,664 shares and 2,850,932 shares at exercise prices per share of HK$6.81, HK$8.18, HK$8.26 and HK$8.82, respectively under two option schemes of the Company were allotted to the option holders in 2004 upon their exercise of rights and the net proceeds from such issue were approximately US$22.2 million. The Group's net asset value increased by 18% to US$3,109 million as at 31 December 2004 from last year's US$2,624 million while the net borrowings to shareholders' equity ratio decreased substantially to 28.6% from 40.6%.

The currency mix of the Group's total tangible assets and total liabilities as at 31 December 2004 is as follows:

	Total Tangible Assets	Total Liabilities
In Hong Kong dollars	17%	45%
In Renminbi	42%	17%
In Singapore dollars	14%	2%
In Philippines Pesos	10%	7%
In Malaysian Ringgit	8%	11%
In Thai Baht	4%	5%
In US dollars	3%	12%
In Fiji dollars	2%	1%
	100%	100%

Note: Total tangible assets included all non-current and current assets with the exception of negative goodwill while total liabilities included balances of minority interests and loans from them.

2. Corporate Debt and Financial Conditions

Taking advantage of the liquidity in the financial market and the favourable conditions in the stock market, the Group issued zero coupon guaranteed convertible bonds due March 2009 in the aggregate principal amount of US$200 million with an initial conversion price of HK$9.25 per share of the Company (subject to adjustment) in March 2004 with net proceeds of approximately US$196.4 million immediately following the issuance of new shares in February 2004 which generated proceeds of approximately HK$1,360 million. Unless previously redeemed, converted or purchased and cancelled, these bonds will be redeemed at 114.633 percent of their principal amount on the maturity date. These proceeds provided funding for financing the development of new hotels for the next 3 years.

The Group has also successfully negotiated the reduction of the interest margin for some of its unsecured bilateral Hong Kong dollar loan agreements with individual banks.

Also taking advantage of the current liquidity and strong competitive environment in the banking system, and with a view to addressing its capital commitment requirements for a number of new projects, the Group executed 5 unsecured bilateral dual-currency loan agreements with individual banks in March 2005 in a total amount equivalent to US$524.1 million. These loans have a maturity of 5 years and their all-inclusive cost is 37 basis points over LIBOR or HIBOR at the option of the Group. This gives the Group the flexibility for shifting the denominated currency from time to time considering financial market conditions. These new loans have also served to push out loan maturities and reduced the loan interest margin.

The Group has satisfactorily complied with all covenants under its borrowing agreements.

The analysis of borrowings outstanding as at 31 December 2004 is as follows:

Maturities of Bank Loans, Overdrafts and Convertible Bonds Contracted as at 31 December 2004

	Repayment				
(US$ Million)	Within 1 year	In the 2nd year	In the 3rd to 5th year	After 5 years	Total
Borrowings					
Corporate bank loans	76.9	202.6	467.9	–	747.4
Project bank loans and overdrafts	27.0	19.4	39.9	38.7	125.0
Convertible bonds	–	–	204.4	–	204.4
Total	103.9	222.0	712.2	38.7	1,076.8
Undrawn but Committed facilities					
Bank loans and overdrafts	470.3	25.0	74.3	14.8	584.4

As at 31 December 2004, all the above borrowings were unsecured except the bank loans of a subsidiary amounting to US$68,000 which were secured by charges over certain motor vehicles of the subsidiary with net book values totaling US$112,000.

The currency-mix of the borrowings and cash and bank balances as at 31 December 2004 is as follows:

(US$ Million)	Borrowings	Cash and Bank Balances
In Hong Kong dollars	800.5	29.7
In Singapore dollars	–	3.9
In Malaysian Ringgit	42.5	1.8
In Renminbi	24.4	49.3
In US dollars	209.4	64.0
In Thai Baht	–	24.3
In Philippine Pesos	–	8.3
In Fiji dollars	–	4.8
In other currencies	–	0.8
	1,076.8	186.9

The borrowings in Hong Kong dollars, Malaysian Ringgit and US dollars (with the exception of the convertible bonds) are at variable rates of interest at spreads over HIBOR, Cost of Funds and SIBOR, respectively. The loans in Renminbi are at rates specified by The People's Bank of China from time to time.

As at 31 December 2004, of the Group's cash and bank balances, US$111.3 million (2003: US$63.8 million) were kept in Mainland China, Malaysia, Thailand, the Philippines and Myanmar. The remittance of funds out of these countries is subject to rules and regulations of foreign exchange control promulgated by the governments of the respective countries.

The Group also executed guarantees in favour of banks for securing banking facilities granted to certain associated companies. The utilised amount of such facilities covered by the Group's guarantees for these associated companies as at 31 December 2004 amounted to US$25.3 million (2003: US$10.0 million).

3. Treasury Policies

The treasury policies followed by the Group aim to:

(a) Minimise Interest Risk

This is accomplished in the loan re-financing and loan negotiation process, and in ensuring that surplus funds from operations are made available to the corporate treasury to reduce the debt exposure. The proceeds from the issue of new shares in February 2004 and the convertible bonds (which carried a fixed yield to maturity of 2.75% per annum) in March 2004 have also been temporarily used principally to reduce the borrowings or placed in short term deposits to minimise interest costs pending use for financing the development of new hotels.

The Pudong Shangri-La, Shanghai repaid bank loans amounting to RMB200 million financed by the US dollar shareholder loans provided by the Group and surplus cash directly from fellow subsidiaries in Mainland China. The Shangri-La Hotel, Qingdao has also repaid RMB10 million to the bank. The Group repaid all the Singapore dollar borrowings in 2004 that carried higher interest rates.

From time to time, the Group closely monitors its loan portfolio and compares the interest margin under existing agreements against new offers. The Group has also sought to hedge its medium term interest rate risk by entering into HIBOR interest rate swap contracts. As at 31 December 2004, the Group had outstanding contracts for an aggregate principal amount of HK$2,716 million at fixed interest rates ranging between 4.69% and 5.74% per annum. The interest cover continues through December 2006.

In March 2005, the Group contracted for additional forward cover for an aggregate principal amount of HK$1,300 million for a period of 5 years at fixed interest rates ranging from 4.335% to 4.345% per annum.

(b) Minimise Currency Risk

The Group has an economic hedge in terms of currency risk to the extent that all the properties in Hong Kong, Mainland China, Singapore and Malaysia derive their revenue (and most of the expenses associated therewith) in local currencies. In addition, a substantial portion of the hotels' room revenues in the Philippines, Thailand and Indonesia are priced in United States dollars. Revenues in Indonesia are also immediately converted into United States dollars upon realisation, to the maximum extent possible.

The Group attempts to align the currencies of its loan portfolio with the currency mix of the Group's investments and revenues in various countries. Given the general expectations about the strengthening of the Renminbi and in compliance with directives issued by the foreign exchange regulatory authorities, subsidiaries in Mainland China have contracted bank loan facilities partly in Renminbi and partly in Hong Kong dollars. During the year, the Group's wholly owned subsidiary in Fuzhou obtained new bank loan facilities in an aggregate amount of HK$218 million to finance the hotel's development cost. A subsidiary in Malaysia has obtained a new bank loan facility of RM90 million to finance the redevelopment project of Shangri-La's Rasa Sayang Resort, Penang. As mentioned earlier, the Group has secured new corporate bank loans in dual-currencies to provide flexibility in view of the continuing depreciation of the US dollar. The

Group has also repaid all its borrowings in Singapore dollars in view of the general appreciation of that currency against the US dollar. Moving forward, the Group plans to selectively increase the funding assistance provided to its subsidiaries in Mainland China in order to reduce their Renminbi borrowings.

The Group has not felt it appropriate to substantially hedge against currency risks through forward exchange contracts upon consideration of the currency risks involved and the cost of obtaining such cover.

4. Fixed Asset Valuations

(a) Fixed Assets Values* – by Geographical Area

	2004 US$ Million	%	2003 US$ Million	%
The People's Republic of China				
Hong Kong	787	15%	715	15%
Mainland China	2,384	46%	2,123	44%
Singapore	762	15%	721	15%
The Philippines	486	9%	478	10%
Malaysia	421	8%	425	9%
Thailand	182	4%	168	4%
Fiji	81	1%	73	1%
Indonesia	33	1%	33	1%
Myanmar	37	1%	37	1%
Total	5,173	100%	4,773	100%

* Including total fixed assets value owned by subsidiaries and the effective interest share of fixed assets value owned by associated companies.

(b) Independent Valuation of Properties

Based on an interpretation note issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), hotel properties have been accounted for under the Statement of Standard Accounting Practice 13 "Investment Property" as at 31 December 2004 and 2003. With the exception of properties held on leases of which the unexpired term is 20 years or less, all investment properties including hotels are stated at professional valuations carried out by the following independent firms of professional valuers as at 31 December 2004:

CB Richard Ellis Limited, DTZ Debenham Tie Leung Limited and Chesterton Petty Limited	:	For properties in Mainland China
CB Richard Ellis Limited	:	For properties in Hong Kong, the Philippines, Indonesia, Myanmar, Fiji and Thailand
Colliers International Consultancy & Valuation (Singapore) Pte Ltd and DTZ DebenhamTie Leung (SEA) Pte Limited	:	For properties in Singapore
W.M. Malik & Kamaruzaman and CH Williams Talhar & Wong Sdn Bhd	:	For properties in Malaysia

Changes in the value of these properties are dealt with as movements in the investment properties revaluation reserves on a portfolio basis. The valuations of all the investment properties (including hotel properties) made in the current year end resulted in a net increase in revaluation reserves of US$155.0 million after adjustment of minority interests and additional provision for deferred tax relating to the full effect of temporary differences arising from revaluation of the properties. This increase was partly offset by the release of reserve balances for the properties in Malaysia due to the disposal of 1.59% interest in Shangri-La Hotels (Malaysia) Berhad, Malaysia in order to comply with the local public float requirements.

The HKICPA has issued a number of new and revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards ("new HKFRSs") that are effective for accounting periods beginning on or after 1 January 2005. The Group has not been an early adopter of the new HKFRSs in the financial statements for the year ended 31 December 2004. As announced on 17 December 2004, the Group is in the process of making an assessment of the impact of these new HKFRSs and has so far concluded that the adoption of HKAS 17 "Leases" and HKAS 40 "Investment Property" will have the following significant effects:

I. The Group's hotel properties will no longer be accounted for as investment properties. Accordingly, for the accounting year beginning on 1 January 2005, instead of stating the hotel properties at fair value, the Group will adopt the following accounting policies retroactively:

(1) The underlying buildings and integral plant and machinery will be stated at cost less accumulated depreciation and impairment, if any, under HKAS 16 "Property, Plant and Equipment";

(2) The underlying freehold land will be stated at cost less impairment, if any, under HKAS 16 "Property, Plant and Equipment"; and

(3) The underlying leasehold land will be stated at cost and subject to annual operating lease rental charge (amortisation of land cost) as required by HKAS 17 "Leases".

Adoption of these new accounting policies will have the following significant consequences:

(a) The net book value of fixed assets, the overall provision for deferred tax liabilities and the net asset value of the Group will be reduced.

(b) The annual depreciation and lease rental charges will increase and this will reduce the profit after tax attributable to the shareholders ("PAT") and the earnings per share ("EPS") of the Group.

II. For the accounting year beginning on 1 January 2005, the Group will adopt the following accounting policy retroactively for its investment properties:

- The Group's investment properties will continue to be stated at fair value. All changes in the fair value of investment properties from one balance sheet date to the next will be reported in the income statement. Previously, such changes were taken directly to the investment property revaluation reserve account on a portfolio basis to the extent that the reserve remained in surplus.

Adoption of this new policy will affect the PAT and the EPS of the Group depending on the results of the annual revaluation.

However, the above changes will have no impact on the cash generated from operations of the Group or the estimated market values of its fixed asset portfolio that are largely influenced by their ability to generate operating cash flows. In addition, these changes are not expected to adversely affect the financial viability of the Group's operations or to jeopardise its financial position.

The Group will be continuing with the assessment of the impact of the other new HKFRSs and other significant changes may be identified as a result.

The Group's first results prepared under these new and revised accounting standards will be published in its interim report for the six months ended 30 June 2005 together with the 2004 restated comparatives.

5. Other Investments

Given favourable market conditions, the Group continued to gradually dispose of its investment portfolio in marketable securities to realise cash for its project developments. In 2004, this disposal of US$33.1 million recorded realised gains of US$8.9 million before adjustment for minority interests (US$8.8 million after minority interests). Dividend income from marketable securities of US$1.4 million before adjustment of minority interests (US$1.3 million after minority interests) was recorded in 2004.

As at 31 December 2004, the market value of the Group's investment portfolio was US$37.1 million which included an unrealised gain of US$12.0 million before adjustment of minority interests (US$10.5 million after minority interests). The investment portfolio included 11,805,055 ordinary shares in the Company ("such SA shares") with a market value of US$16.9 million held by a wholly owned subsidiary of Shangri-La Hotel Public Company Limited, Thailand ("SHPCL"), one of the principal subsidiaries of the Group which is listed on the Stock Exchange of Thailand. Such SA shares were held by the wholly owned subsidiary of SHPCL before the Company acquired a controlling interest in it in late 1999. The Company had undertaken, subject to market conditions, to use its reasonable endeavours to procure SHPCL to dispose of all such SA shares to parties independent of the Kuok Group. 1,390,000 of SA

China World Hotel, Beijing – Lobby Lounge Mural

shares were disposed of on The Stock Exchange of Hong Kong Limited in 2004 by that subsidiary. The investment portfolio also included 7,643,968 ordinary shares in Kerry Properties Limited ("KPL") with a market value of US$16.3 million as at 31 December 2004. Subsequent to the year end and up to the date of this report, the Group further disposed of part of its investment portfolio for US$1 million and recorded realised gains of US$0.1 million (both before and after adjustment of minority interests).

6. Management Strategies

General

The Asia-Pacific region, and in particular Mainland China, which clearly presents tremendous opportunities for continuing growth, continue to be the Group's main sources of business and the focus of its capital investments. The Group is able to sustain a rapid pace of expansion on the Mainland China by entering into management contracts for third-party-owned hotels that do not require a commitment of equity, as well as directly investing in project development.

Mainland China's economic fundamentals continue to be sound, and progressive relaxation of travel restrictions coupled with rising urban incomes is helping to create a boom in domestic and outbound travel.

The Group has been committed to the Mainland China market since opening its first hotel there, the Shangri-La Hotel, Hangzhou, in 1984. The Group subsequently opened three hotels in Beijing between 1986 and 1990. Dramatic expansion occurred in the second half of the 1990s, when the Group opened nine hotels on the Mainland China. The Group's growth in Mainland China has closely followed the country's economic development, with many of the Group's properties built in or near Mainland China's designated economic development zones, including Shenzhen, Pudong, Qingdao and Dalian. The Group will continue to expand the number of properties that it owns and operates in Mainland China and is targeting key provincial cities for new hotels. Today, some 8,000 of approximately 21,000 rooms in 19 of 46 properties managed by the Group are situated in Mainland China. The Group is the leading luxury hotel operator in the country, and its plans for expansion are timed to capitalise fully on Mainland China's economic advancement as well as specific developments including the country's entry into the World Trade Organization, Beijing's role as host of the 2008 Olympics and Shanghai as host of the World Expo 2010.

With a view to further diversifying its portfolio, heightening global awareness of the Group's brand name and, not least, improving returns to shareholders, the Group is also steadily expanding in its youngest markets, South Asia and the Middle East, and is firmly intending to plant the Shangri-La flag in key European and North American gateway cities.

The Group has set up development offices in Beijing and Dubai to facilitate execution of the development strategy in Mainland China and the Middle East.

The Group is also extending the unique Shangri-La brand to new product lines. This past year saw the successful debut of the Group's spa concept, CHI, in one of the most competitive of spa markets, Thailand, and the coming years will see the rollout of more than ten new CHI spas around the world.

Investment in customer relationship management, data warehousing and revenue management are key priorities of the Group with the object of improving the competitive position and profitability of the Group's hotels.

Finally, and most importantly, the Group views the development and retention of the best and brightest talent in our industry as a strategic imperative.

Intended Sale of Non-core Assets

The Group intends to sell all those assets that it considers "non-core" at favourable prices as and when suitable opportunities arise. Funds released from such sales will be used to finance the Group's capital expenditure commitments, reducing reliance on debt finance. To this end, the Group's subsidiaries entered into a conditional sale and purchase agreement in May 2004 to dispose their entire shareholding in Johdaya Karya Sdn Bhd ("Johdaya"), which owns a commercial and office complex in Johor Bahru, Malaysia. As at the date of this annual report, the Group's effective interest in Johdaya is 35.83%. The proposed disposal of 27 million shares of Johdaya, at a price of RM2.43 per share, is expected to be completed in the second quarter of 2005, subject to the receipt of regulatory approvals.

Development Programmes

In 2004, the Group broke ground for the construction of the following hotels in Mainland China:

- Shangri-La Hotel, Ningbo — 550 rooms
- Shangri-La Hotel, Futian — 596 rooms
- Extension to the Shangri-La Hotel, Qingdao — 190 rooms
- Shangri-La Hotel, Chengdu — 580 rooms
- Shangri-La Hotel, Xian — 400 rooms

Work is progressing satisfactorily at the Group's projects in Pazhou, Guangzhou (Mainland China) and Chiangmai, Thailand which are expected to open in 2006 and early 2007, respectively. On 22 March 2005, the Group broke ground for construction of a hotel project in Wenzhou, Mainland China.

The hotel project in Guilin is in the conceptual design stage. The Group has also acquired land in Huhhot and Baotou, Inner Mongolia (Mainland China), and in Boracay, the Philippines for future hotel developments. It also entered into a joint venture agreement in January 2005 to develop a 180 room hotel as part of a mixed-use complex in Ulaanbaatar, Republic of Mongolia.

The current estimated funding required directly from the corporate for the above projects is US$453 million and will be mainly financed by the existing surplus cash on hand, operating fund flows and available borrowing facilities. Joint venture partners and locally contracted project loans will provide the balance of funds required for these developments.

Renovations

Over the past three years, nearly all of the Group's flagship hotels have been fully renovated and are positioned to benefit from the upturn in business. Major renovations are ongoing at the Island Shangri-La, Hong Kong, Shangri-La's Fijian Resort, Yanuca Island and the Shangri-La Hotel, Jakarta. In December 2004, the Shangri-La's Rasa Sayang Resort in Penang was closed for renovations and redevelopment with the intention to reposition this resort and secure its long term profitability. The expenditure by all subsidiaries on renovations, amounting to an estimated US$84 million, will be financed mainly from operating cash flows of the individual hotels, supplemented by locally contracted short-term bank loans where appropriate.

CHI Spa

Management Contracts

In addition to the 8 hotels under operation which the Group manages for third party developers/investors, it has contracts on hand for development of 16 new hotels as at 31 December 2004. These represent an inventory of 8,540 rooms. The development projects are located in Muscat, Dubai (2 hotels), Doha (Qatar), Maldives, Kuala Lumpur, Vancouver, Chennai and New Delhi (India), Suzhou, Dongguan, Sunny Bay – Sanya, Haikou, Kunshan, Changzhou, Urumqi (all in Mainland China).

Among the 16 projects, the Traders Fudu Hotel, Changzhou (374 rooms) opened for business on 3 January 2005.

On 19 March 2005, the Group signed management contracts to manage two Shangri-La hotels (938 rooms) and a Traders hotel (250 rooms) in Bangalore, the technology capital of India. These hotels are expected to open for business in late 2007/ early 2008.

The Group continues to review proposals it receives for management opportunities in the Australia, Middle East region and intends to secure contracts in locations/cities which it considers to be of long-term strategic interest.

Lease

In February 2005, the Group entered into an operating lease agreement for a Shangri-La hotel at London Bridge Tower, scheduled to open in late 2009. This marks the Group's foray into the European market. The hotel will be the first new-build five-star hotel to open in the Central London area in over a decade. Designed by the acclaimed architect Renzo Piano, the iconic, 70-storey London Bridge Tower is situated on the South Bank of the Thames River, minutes from the City of London, easily accessible to Canary Wharf and close to key tourist attractions, making it an ideal location ideal both for business and leisure travellers. The deluxe, 195-room, 18-floor Shangri-La will occupy floors 34 to 52 of the Tower. The Tower will have direct access to a key transport interchange providing extensive mainline railway, bus and underground stations. The hotel will also be home to Europe's first CHI spa. The Group's investment for fit-out costs and pre-opening expenses is estimated at US$40 million and will be largely incurred in 2009.

Spas

The Group's first 'CHI' spa opened at the Shangri-La Hotel, Bangkok in July 2004. Designed to create a sanctuary of tranquility inspired by the legend of "Shangri-La", the CHI spa features some of the largest and most luxurious private suites and villas in the hotel sector. CHI spas offer a range of specialised therapies based on Chinese and Himalayan healing traditions, philosophies and rituals. The essence of 'chi' symbolises Shangri-La's definition of a complete wellbeing concept within an Asian context.

There are at present plans for more than ten CHI spas to be introduced in various Group hotel and resort locations over the next few years. CHI spas are scheduled to open in 2005 at Shangri-La's Mactan Island Resort, Cebu, Shangri-La's Fijian Resort, Yanuca Island, the Pudong Shangri-La, Shanghai, and Shangri-La's Barr Al Jissah Resort & Spa, Muscat, Oman.

Connected Transaction – Jingan District, Shanghai

In June 2004, the independent shareholders of the Company and KPL approved at their respective special general meetings, the entering into of the discloseable and connected transactions relating to the joint acquisition, ownership and development of sites in Jingan District, Shanghai in which the Group will have 48.5% interest. It is intended to develop a high-end composite development consisting of office, residential, serviced apartments, retail and a Shangri-La hotel. Each of the Group and KPL own a piece of land in the area. Development would commence once the joint acquisition of the remaining parcels of land and all local registrations and approvals are obtained. The maximum total investment in the entire project is not expected to exceed US$700 million.

7. Marketing*

Market Overview

Following the SARS crisis of 2003, the Group saw a very strong return of business in 2004 from all major source markets, with a year-on-year increase of 31.8% in total room nights for all its managed hotels; this was, very notably, an 11.6% improvement on the previous strongest year, 2000.

Corporate travel accounted for 43.8% of Group business, an increase of 18.4%, while the fastest-growing segment was leisure travel, up 36.5%, fuelled by the emergence of a number of low-cost intra-regional airlines in Asia.

In terms of source markets, the Asia-Pacific region posted an 18.9% increase in room nights. Mainland China, the top-producing market in the region, enjoyed a 12% increase in room nights. Japan saw a sharp increase of 43.1% in room nights, while Hong Kong reported a 30.8% increase in room nights. Singapore was up 19%, Thailand up 54.5%, Indonesia up 14.4%, Taiwan up 14.4% and Korea was up 27.5%. Although coming from a low base, an important emerging market within the region is India, with a 77.1% increase in room-night production and with the corporate travel market segment growing by 59.8%.

Australia production grew by 40.6%, proof that the establishment of a hotel in a market can have a substantial brand-building effect and drive new business to Group hotels overseas. The outbound market from Australia increased by 35.8%.

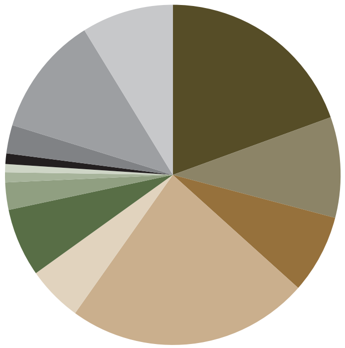
The European market returned in strength, with a 43.2% increase in room nights. The United Kingdom (UK) saw a 37.7% increase in room nights led mainly by leisure travel, which increased by 37.3%, supported by the strength of the Pound. Germany reported a 49.2% increase in room nights led largely by the corporate segment which increased by 49.8%. France saw an increase in room nights of 54.7%, followed by Italy at 69.2%. Russia, an emerging market, reported a 90.4% increase.

North America saw a 47.7% increase in room-night production. The US corporate travel segment was the key driver, producing 63.6% of all US business, an increase of 41.3%. The corporate meetings market posted a strong increase of 76.4%.

* *Note:* The term "Group" used in the Marketing, Food and Beverage Operations, Human Resources and Information Technology sections refers to all hotels managed by the Group.

The Middle East recorded a 136.8% increase in roomnights with the outbound market to Asia registering a strong increase of 64.9%.

Sources of Business in 2004



Marketing Communications

Brand Differentiation

The Group's city hotels comprise two distinct brands viz the upscale Shangri-La and the Asian business-class Traders.

Shangri-La hotels epitomise the brand's promise of traditional Asian values delivered in a contemporary manner. They live up to the standards expected of the best 5-star hotels and are always 'best in class' in their competitive set, noted for generous lobby areas, large guestrooms and grand ballrooms. The Asian heritage of Shangri-La distinguishes it from most of its competitors and the exclusiveness of the brand sets it apart from larger competitive 'chain hotels'. Service levels are consistently high and local and regional influences are reflected in architecture, service and cuisine.

Traders caters to mid-market business and leisure travellers looking for modern, functional accommodation. Traders hotels are established predominantly in locations that do not yet warrant a five-star hotel, or where they complement an existing Shangri-La hotel or hotels. Whilst adhering to the distinctive Asian values of Shangri-La, Traders has a more contemporary design and a less formal feel.

Advertising and Public Relations

A new television advertising campaign made its debut in June 2004 on the regional television stations CNN, Discovery and ESPN, followed by local television stations in Mainland China and Hong Kong. This was complemented by a comprehensive schedule of in-flight presentations on the Group's global airline partner network.

A new global print advertising campaign was launched in the fourth quarter of 2004. The campaign will run in key business, news, lifestyle and travel publications in Asia, Europe, the Middle East and North America through 2005.

Public relations has been substantially strengthened and broadened with the appointment of a Hong Kong-based Vice President-Public Relations and public relations agencies in Japan, France and Germany, the latter with responsibility for Austria and Switzerland. Shangri-La name recognition and visibility were significantly increased during the year through trade and consumer publicity channels.

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Customer Relations

"Golden Circle" Guest Recognition Programme

"Golden Circle", Shangri-La's guest recognition programme, was launched in 1997. "Golden Circle" is clearly differentiated in the market by the fact that it is not a typical bonus point programme – it emphasises customer individuality. It has been named Best Reward Programme and Best Reward Redemption Programme by readers of the international edition of Inside Flyer magazine. Enrolment is by invitation only to qualifying individuals. There are over 700,000 members worldwide.

Comprehensive "Golden Circle" member research was undertaken in 2004. The project provided an in-depth look into the expectations and satisfactions that members have towards the programme. The information provided the basis for revamped benefits and services, designed to maximise guest loyalty, introduced in the first quarter of 2005.

Frequent Flyer Programme Partnerships

The Group has well-established frequent flyer programme partnerships with 33 airlines worldwide.

These partnerships provide a significant incentive for frequent travellers to choose Shangri-La, provide exposure on and an endorsement from partner airlines, and stimulate brand awareness. Promotions targeting members of these programmes also provide a cost effective platform for advertising specific Group product developments such as new hotel openings.

Global Sales

The Group has a well-established global sales network, with offices and representatives in key markets including: Beijing, Hong Kong, Singapore, London, Los Angeles, Shanghai, Tokyo, Sydney, Cologne, New York, Guangzhou, Seoul, Melbourne and Dubai. This network also ensures effective support for roadshows, sales missions and representation at trade fairs.

In 2004, the Group maximised sales production and business opportunities for the global accounts through effective account strategies and action plans and more efficient responses to the diverse needs of its customers, resulting in greater revenues for all hotels through account penetration and profitable partnerships.

8. Food and Beverage Operations*

Around 43% of the combined hotel revenue was derived from food and beverage ("F&B") operations, the majority from banqueting sales, which contributed significantly to F&B profit, reflecting the effectiveness of large-capacity banqueting facilities. The Group's leadership in banqueting business has helped strengthen its hotels' positioning in their markets; local custom accounts for some 80% of F&B income.

The Group's strategy going forward is to retain its core family-oriented customer base, while attracting the growing, younger 'lifestyle' market segment. The Group has introduced a new café concept at a number of city properties, including the Café Too at the Island Shangri-La and Café Kool at the Kowloon Shangri-La in Hong Kong, Next 2 at the Shangri-La Hotel,

Kowloon Shangri-La, Hong Kong – Café Kool

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Shangri-La Hospitality

Bangkok, Café Plus at the Shangri-La Hotel, Qingdao, Café Cha at the Shangri-La Hotel, Beijing, the Lemon Garden at the Shangri-La Hotel, Kuala Lumpur, The Circle at the Makati Shangri-La, Manila, and more recently The Line at the Shangri-La Hotel, Singapore. The Group has also renovated its signature, formal European restaurants such as Petrus at the Island Shangri-La, Hong Kong and Lafite at the Shangri-La Hotel, Kuala Lumpur.

Management is also focused on the Group's resort hotels, given shifts in intra-regional tourism demographics, with plans to refit F&B outlets and offer guests a more casual ambience.

F&B outlets at Traders hotels, not yet a significant contributor to Group earnings, likewise will be given a clearer brand identity.

The Group's Food Safety Management System is deemed to be ahead of its peer group in the industry. Group F&B operations receive twice-yearly independent audits and deploy the best technology available. Local communities also benefit in that staff trained in the Group's safety culture transfer this knowledge to the home and community.

9. Human Resources*

As at 31 December 2004, the Company and its subsidiaries had approximately 18,100 employees. Headcount of all the Group's managed hotels totalled 24,700. Salaries and benefits including provident fund, insurance and medical cover, housing and share option schemes are maintained at competitive levels and bonuses are awarded based on individual performance as well as the financial performance of business units. The Board's Remuneration Committee reviews matters relating to the compensation and the incentives proposed for senior management and executive Directors.

The 6th Staff Opinion Survey was conducted in 10 different languages to gauge employees' opinions in 16 major categories. As in previous years, the survey saw virtually full participation among Shangri-La employees with 99.6% of staff responding. The results were encouraging. More than half of the participants responded favourably to 15 of the 16 categories surveyed, with Shangri-La employees outperforming the Global High Performance Norm in 6 of the 16 categories. The highest performances were recorded in two categories – Commitment to Quality Service and Receiving Feedback from Customers – showing that Shangri-La's Customer First Strategy is firmly entrenched across the rank and file.

In 2004, the Group recorded the lowest staff turnover in its history, indicating a rising level of employee satisfaction and morale.

Launch of Shangri-La Academy, Beijing

December 2004 saw the launch of a centralised employee training centre at Oriental University City, Lang Fang Economic and Technology Development Zone near Beijing. The Shangri-La Academy will accelerate and intensify employee training in

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keeping with the Group's expansion in Mainland China and the critical need to attract and retain hospitality industry talent. By 2008, it is projected that the current Mainland China workforce of nearly 10,000 will virtually double to approximately 19,000. Its establishment is integral to the Group's push for standardisation in the delivery of its brand of service throughout its network of hotels.

With the Group's rapid expansion in Mainland China, the need to develop more staff to take up managerial positions grows more critical. Efforts to develop existing employees with high potential continue unabated under the Group's three core talent development programs – the 18-month Corporate Management Trainee Program (CMT), 12-month Corporate Executive Training (CET) and the 18-month Corporate Trainee (CT) Program.

Proprietary Service Culture Training Programme

The Group's training for all its staff members has resulted in a reputation for award-winning, highly personalised service. The Shangri-La Care service culture training programme's latest module, Shangri-La Care 3, rolled out at all the Group's managed hotels was completed by the end of 2004. All new staff undergo the three modules of the programme within six months of joining. The programme is designed to develop a consistent Shangri-La style of service that will deliver a superior guest experience and build brand loyalty.

10. Share Option Scheme

At the Special General Meeting of the Company held on 24 May 2002, the shareholders of the Company approved the adoption of a new share option scheme (the "New Option Scheme") and the termination of the operation of the executive share option scheme adopted by the shareholders of the Company on 16 December 1997 (the "Executive Option Scheme") (such that no further options shall thereafter be offered under the Executive Option Scheme but in all other respects the provisions of the Executive Option Scheme shall remain in full force and effect).

As of this date, options outstanding under the two schemes are as follows:

	Executive Option Scheme			New Option Scheme
Grant Date	1 May 1998	15 January 2000	15 January 2001	29 May 2002
Exercise price per option share	HK$8.26	HK$8.82	HK$8.18	HK$6.81
Balance as at 1 January 2004	12,278,861	7,859,463	4,589,521	16,400,000
Lapsed in 2004	(435,421)	(193,822)	(97,030)	(335,000)
Exercised in 2004	(6,003,664)	(2,850,932)	(2,726,543)	(11,173,000)
Balance as at 31 December 2004	5,839,776	4,814,709	1,765,948	4,892,000
Lapsed subsequent to 31 December 2004	–	(104,555)	–	–
Exercised subsequent to 31 December 2004	(359,308)	(465,171)	(203,763)	(1,816,000)
Balance as at 31 March 2005	5,480,468	4,244,983	1,562,185	3,076,000

The outstanding options have been treated as off-balance sheet items. Since the options were granted before 7 November 2002, the requirements under the new HKFRSs to recognise the fair value of these options in the financial statements will not be applicable and they will continue to be treated as off-balance sheet items in future.

11. Information Technology*

The Group is an industry leader in its use of information technology. It was the first hotel operator in the region to deploy a distributed reservation, trilingual point of sale and sophisticated yield management systems. In 2004, the Group moved forward in its three-year plan to upgrade its information technology infrastructure with the aim of maximising revenue potential, improving productivity and further strengthening customer relations.

Online Booking

With online booking now the fastest growing distribution channel, the Group has developed a proprietary web booking engine and upgraded its corporate website (http://www.shangri-la.com) to capitalise on this trend.

Built on the OPERA Web Suite platform, the web booking engine is fully integrated with the group's OPERA Central Reservations and Customer Information systems, allowing complete 2-way connectivity for all hotel rates availability, customer profiles and online reservations. Registered corporations are able to book at corporate rates on the website.

In a first for an Asia-based hotel company, a dynamically packaged "Shangri-La Vacations" portal allows online customers to customise and choose from travel services such as flights, car rentals, destination activities, and accommodation packages including a stay at a Shangri-La property – all in one convenient online location. This service is presently available to residents of the United States and United Kingdom.

Central Reservations Systems

MICROS-Fidelio's OPERA Central Reservations and Customer Information Systems were launched in the second quarter of 2004, at an investment of over US$3 million. With rapid expansion, these state-of-the-art systems ensure higher levels of guest recognition and customer service across all hotels as well as new properties as they open. Reservations can be made for any Shangri-La property using the Group's worldwide toll-free numbers, and callers are assured instant confirmation and best available rates.

With the central booking and profile management systems in place, the next phase involves migration of the local hotel Property Management Systems ("PMS") to the latest version of OPERA PMS. This will ensure seamless integration with the central platform and also achieve significantly higher system availability on the property level, due to new hardware technologies.

In addition to existing reservation centres in Hong Kong, Tokyo and London, a new call centre in Kuala Lumpur was opened. With this new call centre, the Group has established new toll-free numbers to service Indonesia, Malaysia, the Philippines, Singapore, Taiwan, Thailand, India, the Middle East and South Africa markets. For those calling from Mainland China there are now two toll-free reservations numbers for northern and southern Mainland China. Toll-free reservations numbers had already been established in Australia, New Zealand, Japan, South Korea, Europe and North America.

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Guest Broadband Access

The Group is gradually enabling its existing properties with wired and wireless broadband Internet access in public areas and guest rooms and all new properties are being designed with broadband capability.

Additional Management Systems

2005 will see the rollout of Group-wide Sales & Catering and Sales Force Automation Systems. These will enable the individual hotels and Regional Sales Offices to share sales leads, consolidate and track revenues and generally streamline the sales process. New software solutions in the areas of Materials Management and Human Resources and an upgraded Point-of-Sale System will also be rolled out in 2005.

12. Corporate Social Responsibility

Corporate Philanthropy

The Group is committed to supporting the communities in which it operates. This was evident in the immediate aftermath of the tsunami disaster that struck the Southeast Asia region in December 2004. At the corporate level, the Group contributed HK$5 million to the Red Cross and to various relief agencies. Individual hotels and staff contributed an additional sum of HK$2.3 million in cash, as well as in-kind donations of clothing, uniforms, bedding and other supplies. No Shangri-La employees or guests were harmed and no hotels or resorts were damaged by the tsunami.

Care for Children ("CFC"), a charity with its roots in the United Kingdom and registered in Mainland China, has been selected as the major beneficiary of the Group's ongoing social responsibility programme.

In Mainland China, CFC functions under the Ministry of Civil Affairs in Beijing, in cooperation with the China Social Work Association. CFC works at the national and local government levels on the Mainland China to introduce foster care and other strategic initiatives to relieve children's hardship, distress and sickness and to enrich the lives of orphans. Other respected global brands that have partnered with CFC include Virgin Atlantic, British Airways, BP, IBM, Credit Suisse, Carrefour, Rolls-Royce and Boeing.

Environmental Initiatives and Practices

The Group, a founding member of the Asia Pacific Hotels Environmental Initiative, has historically been an industry leader in environment-friendly initiatives and practices. In accordance with the Group's Environmental Policy, all Shangri-La and Traders hotels have "Green Programmes" to identify ways to reduce wastage and eradicate practices that could damage the environment. Recent Group initiatives include a switch from coal to diesel as boiler fuel at the Shangri-La Golden Flower Hotel, Xian. The Group is also switching from coal to gas at its Beijing properties and has changed to low sulphur diesel at the Island Shangri-La, Hong Kong.

The Group's commitment to environmental awareness has to date resulted in a total of 20 hotel properties receiving certification to ISO 14001, the international Environmental Management System standard. A number of Group hotels were the first to receive certification in their markets, and the Island Shangri-La, Hong Kong was the first to receive certification in the Asia Pacific region. Certification is only awarded to those organisations that are able to demonstrate the implementation of ISO 14001 throughout their operations.

The 20 hotels awarded ISO 14001 have also undertaken a number of environment-friendly measures benefiting their communities, including the installation of energy-saving light bulbs, sewage treatment facilities and the use of biodegradable cleaning materials and water restrictors.

The Group has an extensive list of internally developed environmental "best practices" which hotels not yet certified as ISO14001 also follow. All properties use an Environmental Management System manual as a guideline. This helps to identify and address the immediate and long-term impact of every hotel's operations on its local environment and ensures on-going compliance with national and international requirements.

13. Corporate Governance

The Company has complied with the Code of Best Practice, as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "HK Listing Rules") (effective prior to 1 January 2005), throughout the year.

The Company has always recognised the importance of shareholders' transparency and accountability. The Board believes that shareholders can maximise their benefits from good corporate governance. Therefore, the Company continuously reviews its corporate governance framework to ensure that it aligns with generally acceptable practices and standards. The current governance framework of the Company is set out below. The Company is in the process of reviewing and realigning its governance framework to take into account of the new Code on Corporate Governance Practices as set out in Appendix 14 of the HK Listing Rules effective as at 1 January 2005.

The Board of Directors

The Board of Directors is accountable to the shareholders for leading the Group in a responsible and effective manner. The Company's Board of Directors comprises 5 Executive Directors, 5 Non-Executive Directors (including one Alternate Director) and 3 Independent Non-Executive Directors (with at least one of the Independent Non-Executive Directors having appropriate professional qualifications or accounting or related financial management expertise), whose biographical details are set out on pages 30 to 34. The Board has a majority of Non-Executive Directors, thereby improving management control and ensuring that the Board takes into account the interests of all shareholders.

The Board meets at least four times a year at quarterly intervals and meets more frequently as and when required. At the Board meetings, the Directors actively participate and hold informed discussions. The number of Board meetings held and meetings attended by each of the Directors during the year 2004 were as follows:

Executive Directors	Meetings attended	Meetings held during directorship
Mr Kuok Khoon Loong, Edward	4	4
Mr Ye Longfei	2	4
Mr Giovanni Angelini	4	4
Mr Lui Man Shing	3	4
Mr Ng Si Fong, Alan	3	4

Non-Executive Directors	Meetings attended	Meetings held during directorship
Madam Kuok Oon Kwong	4	4
Mr Ho Kian Guan	4	4
Mr Lee Yong Sun	4	4
Mr Roberto V. Ongpin	4	4
Mr Alexander Reid Hamilton	4	4
Mr Tow Heng Tan	4	4
Mr Timothy David Dattels	4	4

To facilitate the decision-making process, the Directors have unrestricted access to the management to make enquiries and obtain further information, when required. In addition, all Directors have unrestricted access to the advice and services of the Company Secretary to ensure that Board procedures and all applicable rules and regulations are followed. The Directors can seek independent professional advice at the Company's expense.

Board minutes kept by the Company Secretary are sent to the Directors for record and are open for inspection by the Directors.

The Company has arranged appropriate insurance cover for the Directors.

The Board has appointed Board committees to oversee particular aspects of the Company's affairs. Each Board committee is appointed with written terms of reference.

However, certain matters are reserved to the full Board for decision including matters relating to the following:

- corporate objectives
- interim and annual results
- interim and annual reports
- budgets
- significant investments
- major acquisitions and disposals
- major financings, borrowings and guarantees
- material contracts
- risk management
- any other significant matters that will affect the operations of the Group as a whole

Directors' Appointment, Re-election and Removal

The Company has not established a nomination committee. The Board as a whole is responsible for approving the appointment of its members and nominating them for election and re-election by the shareholders of the Company.

According to the current Bye-Laws of the Company, Directors appointed to fill a casual vacancy are subject to re-election at the next Annual General Meeting following their appointment. Besides, one-third of the Directors shall retire from office by rotation at each Annual General Meeting. The retiring Directors shall be eligible for re-election. The Board has proposed amendments to the Company's Bye-Laws which would require every Director to be subject to retirement once every three years. These proposed amendments will be presented for shareholders' approval at the Company's Annual General Meeting to be held in May 2005.

Shangri-La Hotel, Dubai – Lobby

Independence of Independent Non-Executive Directors

The Board has received from each of the Independent Non-Executive Directors confirmations of their independence according to the guidelines set out in Rule 3.13 of the HK Listing Rules. The Board is of the view that all Independent Non-Executive Directors of the Company are independent and is grateful for the contribution and independent advice and guidance that they have been giving to the Board and their participation in the Board committees.

Remuneration Committee

A Remuneration Committee of the Board of Directors was set up on 17 October 1997 to review matters relating to the compensation and the incentives proposed for senior management and Executive Directors of the Company. The Committee comprises three members including the Chairman and two Independent Non-Executive Directors. The current Committee members are Messrs Kuok Khoon Loong, Edward (who acts as chairman of the Committee), Alexander Reid Hamilton and Tow Heng Tan.

Audit Committee

The Company set up an Audit Committee of the Board of Directors on 25 August 1998. The Committee comprises three Non-Executive Directors, two of them being independent. The current Committee members are Messrs Alexander Reid Hamilton (who acts as chairman of the Committee), Ho Kian Guan and Tow Heng Tan. The Committee members have professional qualifications and experience in financial matters that enable the Committee to exercise its powers effectively and provide the Board with independent views and recommendations in relation to financial matters. The main duties of the Audit Committee includes, inter alia, reviewing the half-year and annual financial statements before they are submitted to the Board for approval. The Audit Committee met four times in 2004. Special meetings may be convened at the discretion of the chairman of the Committee to review significant control or financial issues.

The Audit Committee reviewed the financial statements of the Group for the year ended 31 December 2004 prior to recommending them to the Board for approval.

Internal Financial Controls

In performing its duties, the Board of Directors also acknowledges its responsibility for the Group's system of internal financial control. Internal financial systems have been designed to allow the Board to monitor the Group's overall financial position, to protect the Group's assets and to mitigate against material financial misstatement or loss.

Internal Audit

The Board also monitors its internal financial control systems through management reviews and a programme of internal audits. The internal audit team reviews the major operational and financial systems of the Group on a continuing basis and aims to cover all major operations within every division on a rotational basis. The scope of its review and the audit programme is determined and approved by the Audit Committee at the beginning of each financial year in conjunction with the external auditors. The internal audit function reports directly to the Audit Committee and submits regular reports for its review in accordance with the approved programme.

External Auditors

The Company's external auditors are PricewaterhouseCoopers, Hong Kong

During the year, PricewaterhouseCoopers, Hong Kong and its other member firms provided the following audit and non-audit services to the Group:

	US$'000
Audit services (including interim review)	365
Non-audit services	
– Tax services	39
– Other services	62

Total fees for audit services provided by other external auditors to the subsidiaries of the Group were approximately US$298,000.

PricewaterhouseCoopers, Hong Kong will retire and offer themselves for re-appointment at the Annual General Meeting of the Company to be held in May 2005.

Investor Relations

The Board and senior management recognise their responsibility to look after the interests of the shareholders of the Company.

With a view to developing and maintaining continuing good relations with the Group's shareholders and investors, various communication channels have been established.

The Company reports on its financial and operating performance to shareholders through interim and annual reports. At the Annual General Meeting, shareholders can raise any question relating to the performance and future direction of the Company with the Directors.

In addition, press conferences and analysts briefings are held at least twice a year subsequent to the interim and final results announcements at which the Executive Directors are available to answer queries on the Group. Shareholders and investors may visit the Group's website (www.shangri-la.com) for up-to-date financial and other information about the Group and its activities.

As at 31 December 2004, sufficient shares of the Company were on public float as required by the HK Listing Rules.

The Company made changes to its Bye-Laws during the year to comply with the amendments to the HK Listing Rules which came into effect on 31 March 2004.

Securities Transactions by Directors

The Board of Directors of the Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the HK Listing Rules as the Code for Securities Transactions by Directors of the Company (the "Securities Dealing Code").

The Directors who had securities transactions in the Company's shares during the year had informed the Chairman of their intention of dealing prior to the transactions and provided the Company with details of the transactions thereafter in compliance with the Securities Dealing Code. Interests in the Company's shares and share options held by the Directors as at 31 December 2004 are set out in the Report of the Directors section of this Annual Report on page 73.

All the Directors have confirmed compliance with the required standard set out in the Securities Dealing Code throughout the year.

Island Shangri-La, Hong Kong – Mural


Shangri-La's Tanjung Aru Resort, Kota Kinabalu – Tanjung Garden

China World Hotel, Beijing – Lobby