

Group Managing Director's Report

‘Today and into the future, our customers can count on us for a reliable and stable power supply.’



Tso Kai-sum
Group Managing Director



In the past year, we have experienced both change and continuity. Natural gas and coal prices showed extreme volatility, while environmental issues remained a focus for us. In January 2008 we signed the new Scheme of Control Agreement (SCA) with the HKSAR Government that runs from 2009 to 2018. Effective 1st January 2009, the SCA provides a 9.99% rate of permitted return on assets other than renewable energy facilities and 11% on renewable energy facilities, down from the 13.5% under the previous SCA which expired in December 2008.

What remains unchanged is our way – **consistency, commitment, growth and recognition** – which are distinct hallmarks of our company. Strong market value, impressive customer services records, technological progress and dedicated community service all reflect the steady and dynamic nature of our company.

Today and into the future, our customers can count on us for a reliable and stable power supply. They can be confident that HK Electric is a trusted partner in their every success.

Consistency

Since 1889, HK Electric has been providing Hong Kong with efficient and affordable electricity. With world class reliability, we have contributed to the development of Hong Kong and its role as a financial centre.





We have met or exceeded all pledged customer services standards in 2008.



Our shareholders benefit from the Group's strong financial position.



HK Electric achieves outstanding electricity supply reliability.





Five Customer Relationship Excellence Awards are given to outstanding employees at HK Electric.



The Marsh Road Station Building adopts a green building concept.



CitiPower and Powercor reach important milestone of one million customers.

...in providing reliable electricity

Generation

HK Electric's Lamma Power Station has a total installed capacity of 3,735 MW, which includes both coal-fired and gas-fired generating units. In 2008, the power station's coal-fired units generated approximately 83% of the electricity sent out while the gas-fired units generated approximately 17%.

Overall availability and reliability of all the generating units was higher in 2008. Unit 9, HK Electric's first gas-fired combined cycle generating unit performed satisfactorily in 2008. To increase the power station's gas-fired generating capacity, the conversion of GT57 from an oil-fired combined cycle unit to a gas-fired unit was completed in 2008.

Emission reduction works continued at the Lamma Power Station in 2008 with the installation of flue gas desulphurisation (FGD) plants and low nitrogen oxide system retrofit works for Units 4 and 5 and Unit 2 FGD retrofit works. By the end of 2010, it is expected that over 95% of the electricity generated at the Lamma Power Station will be generated by both gas-fired and coal-fired units with FGD and low nitrogen oxide burners resulting in lower emission levels.

Coal prices increased substantially in 2008 and, while moderating toward the end of the year and into 2009, they remain high by historic standards. The impact of the higher coal costs was mitigated in part through the sourcing and use of a variety of coal during the year.

Transmission and Distribution

Unit sales of electricity in 2008 were 10,865 million kWh compared with 10,891 million kWh in 2007. The slightly lower sales were due to the cooler and wetter weather

during the summer and to the effect of various energy saving initiatives. System maximum demand increased from 2,552 MW in 2007 to 2,589 MW in 2008 due to the exceptionally warm weather in late September.

HK Electric continued to maintain world class supply reliability with a rating of over 99.999% in 2008, the high level of supply reliability has been consistently maintained since 1997.

Supply reliability was supported through investment in our transmission and distribution system. Major transmission projects completed in 2008 included substations and transmission circuits at Marsh Road, Morrison Hill, Apleichau, Tamar and Cyberport. The Marsh Road substation commissioned in 2008 is an energy efficient building with renewable energy installations serving the financial and commercial districts on Hong Kong Island.

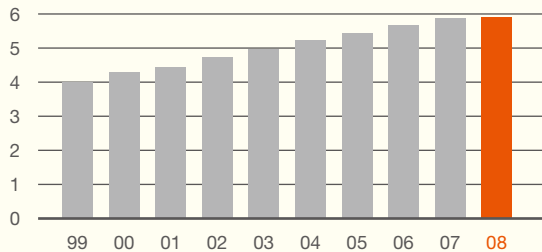
We upgraded major computer application systems such as the Energy Management System and Distribution Management System, which were completed in November for enhanced reliability and performance in system control and monitoring.

...in providing a high standard of customer service

Professionalism

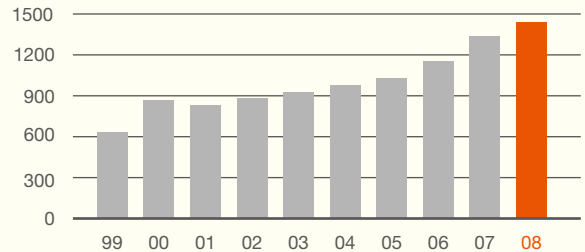
We are pleased that all of our pledged customer services standards in the past year were either achieved or surpassed. The number of commendations received from customers reached a record high of 1,443. This reflected a high level of customer satisfaction with our services, which was due in no small part to the considerable effort of each of our employees.

Productivity 1999 - 2008 (millions of kWh)



Units sold per employee

Written Commendation Statistics 1999 - 2008



In the past year, individual employees at HK Electric took home five 2007 Customer Relationship Excellence Awards for the following honours: Customer Services Manager of the Year, Customer Services Team Leader of the Year, Customer Services Professional of the Year, and two Merit awards for Customer Services Team Leader of the Year and Customer Services Professional of the Year.

Government electricity charge subsidy

In February 2008, the Government announced that an Electricity Charge Subsidy Scheme would be launched to ease inflationary pressure. We offered full support to the Scheme and worked closely with the Government to devise the implementation details. The Scheme was successfully launched on 1st September 2008. Under the Scheme, a monthly electricity charge subsidy of \$300 is allocated to each residential electricity account for 12 consecutive months. The subsidy can be used for paying electricity charges until 31st August 2014 or the closure of the account, whichever is earlier.

Convenient billing

Our customers now have a network of options for settling their electricity bills. The electricity bill payment service via VanGO convenience stores was introduced in December 2008. In addition to Circle K and 7-Eleven convenience stores, customers can settle electricity bills of up to \$5,000 per transaction by cash at any VanGO store.

The Enterprise Advisor Service was introduced in 2008 at the Customer Centre, providing our commercial customers and their electrical contractors with one-stop advisory services on application for new or additional supply, energy efficiency, electricity safety, power quality and account matters.

To enhance our services to the Maximum Demand customers, the provision of automatic meter reading for the Maximum Demand customers was practically completed in 2008.

Communicating with our customers

To enhance communication with our customers, a new bulletin “HK Electric On-line” was introduced in June for distribution to all customers on a quarterly basis. The bulletin features company updates, green initiatives and community work.

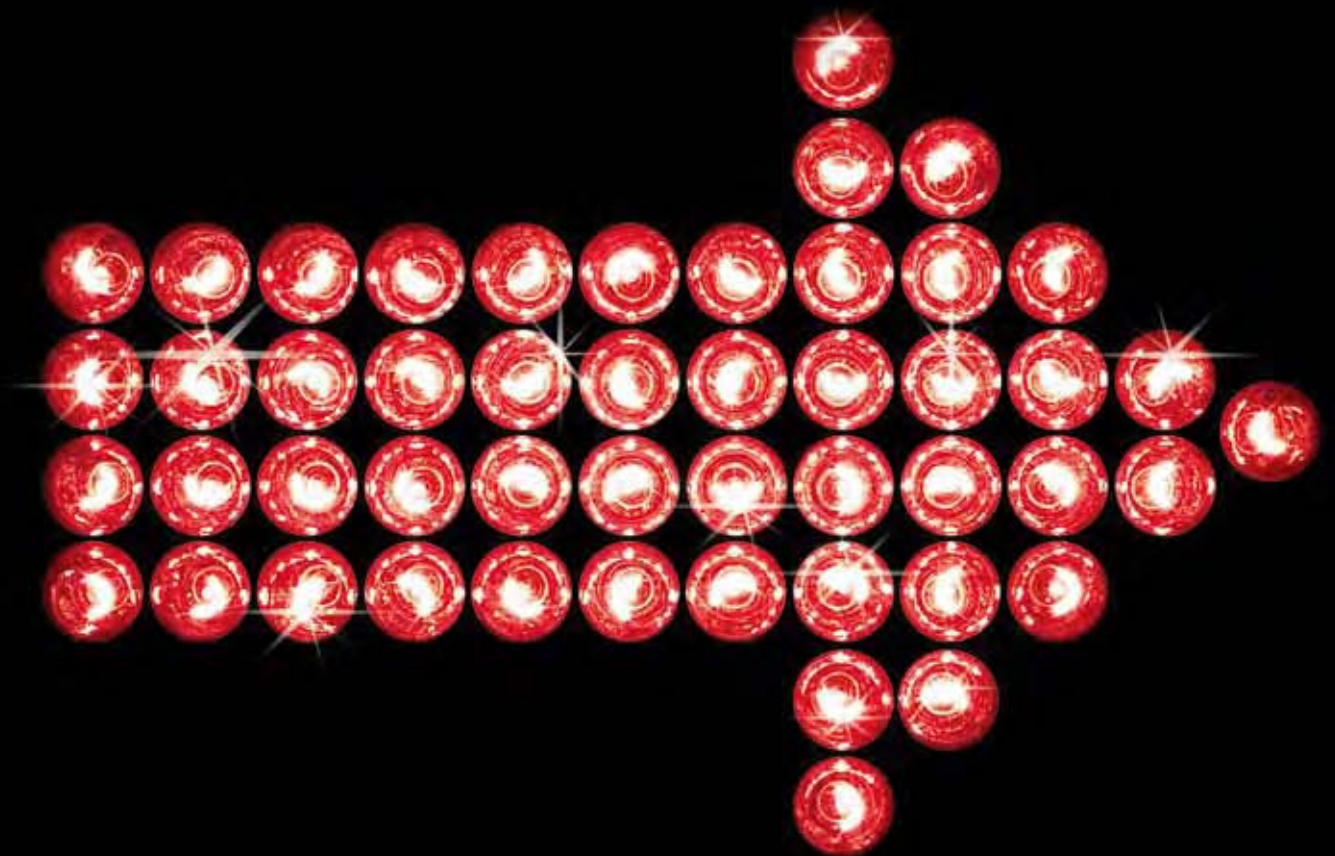
The annual Customer Liaison Group (CLG) Meeting was held on 12th January, where the Company’s major milestones in 2007 and a number of topical issues related to the Company’s latest developments were shared with members. In return, members offered their views and feedback on our services for continuous improvements. This was followed by another meeting of the CLG Committee on 27th September.

...in providing a steady return for our shareholders

HK Electric shareholders have benefited from the Group’s strong financial position and conservative investment profile with the Company shares being one of the best performing shares in the Hang Seng Index in 2008. Going forward, the Company and its businesses both in Hong Kong and internationally are well placed to withstand the current worldwide economic uncertainties, and we expect to see continued growth in the proportion of our earnings arising from our activities outside Hong Kong.

Commitment

HK Electric has shown its continuing commitment to Hong Kong through its substantial investment over the years in Hong Kong's electricity infrastructure and environmental management, employee safety and development as well as public education and enrichment.





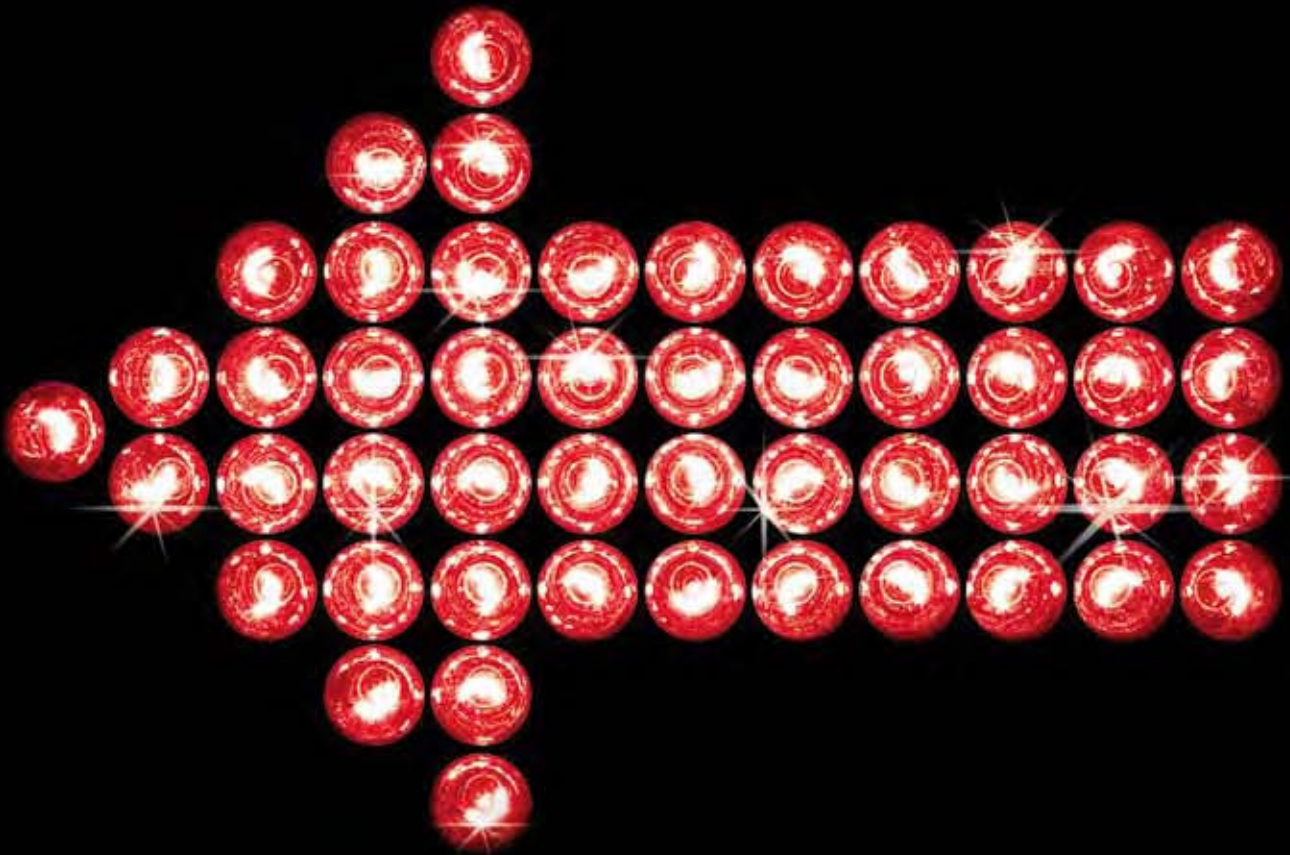
The "Cruise and Learn" programme continues to benefit underprivileged children.



The Yunnan Dali Wind Project is one of two wind power projects in mainland China.



Northern Gas Networks distributes gas to 2.6 million homes and businesses.





HK Electric is recognised for outstanding environmental achievement.

Three Lamma units are being retrofitted with Flue Gas Desulphurisation plants.

Young designers capture the spotlight at our "Go Green Fashion Design Competition".

...to reducing emissions

Emissions reduction programme

HK Electric's emissions reduction programme at the Lamma Power Station progressed well in 2008. We continued to move toward achieving the Hong Kong Government's 2010 emission targets.

A number of retrofit projects progressed at different stages in 2008, including the completion of all piling and civil works for the retrofit of the Flue Gas Desulphurisation (FGD) plants at Units 4 and 5, and most civil works for the Unit 2 FGD retrofit at the Lamma Power Station. Installation of the Unit 5 FGD plant, including the absorber tower, associated gas ductwork and common facilities started in 2008 and are in reasonable progress targeting for commissioning by mid 2009. Installation of the Unit 4 and Unit 2 FGD plants also commenced in 2008.

For Units 4 and 5 Low Nitrogen Oxides System, retrofit work is currently underway. Site retrofit work at the L5 boiler began in October 2008 and was completed before the end of January 2009, targeting for commissioning in April 2009. Finally, retrofit work for L4 boiler is scheduled for commencement in September 2009, for commissioning by March 2010.

Harnessing wind energy

Following the completion of a Comprehensive Site Selection Study in April 2008, detailed Environmental Impact Assessment (EIA) studies for both the Southwest Lamma Site and Eastern Offshore Site for

the development of a 100MW Offshore Wind Farm commenced in August 2008. Marine mammal and avifauna surveys for both sites are in progress, and a draft EIA Report will be ready in mid 2009.

Meanwhile at Lamma Winds, our demonstration wind turbine project on Lamma Island, over 800,000 kWh of electricity was generated in 2008 which saved over 600 metric tons of carbon dioxide emissions.

By visiting the wind power station, people of all ages can gain an appreciation of renewable energy and its environmental benefits. In 2008, a total of 70 visits for professional institutes and schools to Lamma Winds and Lamma Power Station were organised to enhance public understanding of our operation.

Environmental management

Our Environmental Management System at Lamma Power Station (LEMS) was certified to have met the requirements of ISO 14001:2004 by the HKQAA. The certification recognises LEMS's conformance to internationally acclaimed standards in dealing with potential environmental impacts generated during electricity production.

In the Lamma Power Station, wastewater and rainwater collected for reuse made up 9% of our raw water consumption. Besides, 85,000 metric tons of ash were harvested from the Ash Lagoon and used for reclamation and land formation at our Lamma Extension site. In addition to paper and batteries, we began collecting spent fluorescent tubes and energy-saving lamps for recycling.

Students gain practical insights and learn about applications of renewable energy for sustainable development with the support of the HK Electric Clean Energy Fund.



The Clean Energy Fund supports the use of renewable energy on school campus.

Our commitment to environmental protection and continuous improvement in environmental performance continued to be recognised in 2008. We won the Environmental Performance Award of the 2008 Hong Kong Award for Industries organised by the Business Environment Council, the 2008 Prime Award for Eco-Business, Hang Seng Pearl River Delta Environmental Awards and the 2008 Hong Kong Enterprise Environmental Achievement Award.

Environmental education

The Smart Power Campaign 2007/08 was launched in November 2007, focusing on promoting energy sustainability in everyday lives, while continuing with its conservation messages.

Under the campaign, around 1,000 students from local schools took an educational and fun-packed journey to the Lamma Power Station and Lamma Winds in April 2008. Eco-tours on Lamma Island, conducted by HK Electric volunteers, were incorporated into the four-hour programme to inspire young students to love and care for the environment.

In addition to a cooking competition and a series of radio programmes, we also held a “Go Green Fashion Design Competition” in June 2008. An array of innovative designs captured the spotlight during the show, which was attended by more than 200 young fashion designers and their supporters. Designers recycled used clothing and newspapers, discarded compact discs, and even mosaic tiles to convey sustainability and energy conservation messages.

Another 12 schools were awarded funding to implement renewable energy projects on their campus. The projects range from an aquatic system energised by PV panels and wind turbines to a stepping generator for powering gardening devices. Students gained practical insights and learnt about applications of renewable energy for sustainable development with the support of the HK Electric Clean Energy Fund.

...to employee well-being

Health & safety education

To ensure that health and safety issues are paramount in HK Electric, leading indicators on health and safety were introduced in respect of hazard identification, risk assessment and risk control. The indicators include site safety inspections, pre-job risk assessment, job safety analysis, manual handling risk assessments and display screen equipment risk assessments, and safety audits.

An annual audit of HK Electric’s Health & Safety Management System carried out in November 2008 confirmed that the present Corporate Health and Safety Management System was properly developed, implemented, and is in compliance with the statutory requirements on health and safety.



The “Cooking in Harmony” programme helps new arrivals integrate into the community.



HK Electric introduces leading Key Performance Indicators on health and safety.



Over 1,000 senior citizens play and learn at our “CAREnival for the Elderly”.

Training and development

During the year, 18,425 participants joined in various types of training activities and 64,945 training hours were recorded. Apart from well-established training schemes for university graduates, trainee technicians and apprentices, we provided training for employees in management and functional skills, language skills, computer knowledge and technology relevant to our industry by both classroom training and e-learning platforms. Job-related programmes to develop and enhance the general skills and knowledge of employees were also provided. In addition, various talks were held regularly for all levels to widen the knowledge base and perspective of employees catering for their intellectual, social, emotional and physical wellness.

...to community investment

Volunteering for a caring community

We are very proud of the HK Electric Volunteers Team which boasts a membership of 843, about 44% of our employees. Our volunteers continued to extend the Company’s care to the needy in 2008, organising 68 voluntary services, with the total service hours exceeding 3,860.

Our volunteers left their mark with three new eco-trails that were developed to encourage the public to explore and appreciate Lamma Island’s ecological resources as well as cultural and historical relics, allowing more

people to understand and enjoy Lamma in a green way. To facilitate understanding, 20 educational panels were installed en route, while an eco-tour map was published and 60 eco-leaders, including Lamma residents, HK Electric volunteers, and secondary school students, were trained as we marked the completion of the three-year Green Lamma Green project.

CAREnival for the elderly

To ensure that our elderly customers are kept informed of the Hong Kong Government’s provision of an electricity charge subsidy for all domestic customers commencing 1st September 2008, HK Electric partnered with three local community groups to organise a new community programme named “CAREnival for the Elderly” for the Company’s elderly customers who currently enjoy its concessionary tariff. Over 1,000 senior citizens attended the carnivals held between August 2008 and February 2009, and learnt about the safe use of electricity and energy efficiency through fun and games.

Supporting elderly education

Also centering on the elderly, the U3A (University of 3rd Age) network, which is funded by the HK Electric Centenary Trust, was expanded to include 19 social service agencies. Six more organisations were selected to run U3A courses in 2008, which is designed to support lifelong learning and volunteerism among the retired population in Hong Kong. Over the past three years, more than 550 courses have been organised,

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The Smart Power Open Day provides a fun, educational journey to the Lamma Power Station and Lamma Winds for 1,000 students.

benefitting over 8,000 U3A students. Participants were recognised for their achievements at a ceremony in March 2008.

To build on the success of the programme, we rolled out the "Outstanding Third Age Citizens Award" in November 2008 to recognise retirees with exceptional achievements in promoting lifelong learning and dedicated community service. It is hoped that the award scheme will encourage more third age citizens to fully apply their knowledge and experience and thereby continue contributing to our society.

Other community programmes

The popular "Cruise and Learn" programme continued in 2008 to benefit underprivileged children and their family members. Organised quarterly, a total of four educational boat trips were arranged in 2008 to visit the Lamma Power Station and cruise the Victoria Harbour. Participants were able to learn more about the power industry, environmental protection and the many historical and financial landmarks of Hong Kong. Over 400 participants from the YMCA, The Salvation Army, The Hong Kong Federation of Youth Groups, and the Hans Andersen Club took part in the cruises.

A special culinary programme "Cooking in Harmony" was organised in partnership with Christian Action in 2008 for ethnic minorities and new arrivals from mainland China. In an effort to help them better integrate into the Hong Kong community, the programme included a parent-child

workshop on festive customs and delicacies, as well as an 8-session workshop on dishes and drinks available in Hong Kong style cafés.

We continued to partner with the Housing Authority in conducting monthly electrical inspections for single elderly people living in public housing estates. Visits were paid to 70 senior citizens during the year and our volunteers helped inspect their electrical installations and replace any sub-standard plugs or adaptors to ensure safety.

HK Electric volunteers supported several green activities in the community throughout 2008, including "Clean up the World in Hong Kong", "No Hill Fire on Lamma Campaign", and "International Coastal Clean-up Action". They also helped raise funds by selling flags for four NGO's in 2008.

We are a generous supporter of charitable organisations and meaningful causes to help the needy. In 2008, millions of dollars were spent supporting a total of 86 community, environmental and professional projects.

Growth

HK Electric has continuously met the growth in electricity demand in Hong Kong while continuing to grow outside Hong Kong where we now have investments in Australia, New Zealand, Canada, Thailand, mainland China and the United Kingdom.



ETSA continues to deliver on key financial and non-financial targets during 2008.



We light up Wellington with our first entry into New Zealand through a joint acquisition.



Tamar is one of several major transmission projects completed in the past year.





The TransAlta Cogeneration L.P. has stakes in six Canadian generating plants.



Our Ratchaburi power plant in Thailand wins the 2008 Asian Power Award for Innovative Technology of the Year.



We demonstrate our commitment to renewable energy as we celebrate the commissioning of the Dali wind farm.

...by meeting future demand

Development plan

The HKSAR Government approved HK Electric's 2009-2013 Development Plan in December 2008. Over the next five years, we plan to invest HK\$12.3 billion in new and existing capital projects. Three generating units are being retrofitted each with a flue gas desulphurisation plant, two of which will also be retrofitted with low nitrogen oxides burners for reducing emissions. Reinforcement and expansion of our transmission and distribution system will continue to maintain the provision of a highly reliable electricity supply. Ongoing projects to develop the information and metering systems are undertaken with quality customer services as the objective.

...by developing our international markets

2008 was a very successful year for our international operations and overseas expansion through Hongkong Electric International Ltd. (HEI).

New Zealand

We made our first entry into New Zealand through the joint acquisition of the Wellington Electricity Network with Cheung Kong Infrastructure Holdings Limited (CKI).

The Wellington Electricity Network distributes electricity to more than 160,000 residential, commercial and industrial customers in the Wellington, Porirua and Hutt Valley regions.

China

We achieved a major milestone in 2008 with the successful development of our China renewable energy efforts whereby two joint ventures were established with China Huaneng Group for the development of two wind farms in China.

A subsidiary of HEI is co-developing these two wind farms – one 48MW in Dali, Yunnan province, and one 49.5MW in Leting, Hebei province. The Dali Wind Farm achieved Commercial Operation Date (COD) on 1st January 2009 and the Leting Wind Farm is planned to achieve full COD in mid 2009. Both projects qualify for the Clean Development Mechanism under the Kyoto Protocol.

In February 2009, we announced the acquisition of 45% equity interests in three power plants in mainland China – two in Zhuhai, Guangdong province, and one in Siping, Jilin province – with a total generating capacity of 2,800MW. The Zhuhai power plants are located in a growth centre in China adjacent to Hong Kong. The acquisition provides the Company with the opportunity to make a strategic entry into the power plant business in China at a secure and attractive rate of return.

Northern Gas Networks Limited is benchmarked as the most efficient network in the U.K. gas industry in 2008.



Northern Gas Networks records increased customer satisfaction in 2008.

Thailand

Another major milestone was reached this year by successfully commissioning our Thailand Independent Power Provider Project, Ratchaburi Power Company Limited, in two phases in March and June 2008, providing 1,400MW of installed capacity to the Electricity Generating Authority of Thailand. The Ratchaburi power plant went on to win the 2008 Asian Power Award for Innovative Technology of the Year.

Australia

ETSA Utilities operating in South Australia continued to deliver on key financial and non-financial targets during 2008. Strong economic and customer connections activity contributed to a strong year where the business exceeded its reliability and other customer service targets.

CKI/HEI Electricity Distributions Holdings (Australia) Pty Ltd operating in Victoria showcased considerable success in 2008's National Customer Service Business awards, winning the National Award for Best Customer Charter and the Victorian Award for the best large business.

Canada

HEI successfully acquired 50% shareholdings in Stanley Power Inc. in December 2007. Stanley Power Inc., a 50/50 joint venture with CKI acquired a 49.9% interest in TransAlta Cogeneration L.P. The TransAlta Cogeneration L.P. has stakes in six Canadian generating plants, including five gas-fired cogeneration plants in Alberta, Saskatchewan and Ontario, and a coal-fired generation plant in Alberta. The six plants add 202MW to HEI's portfolio.

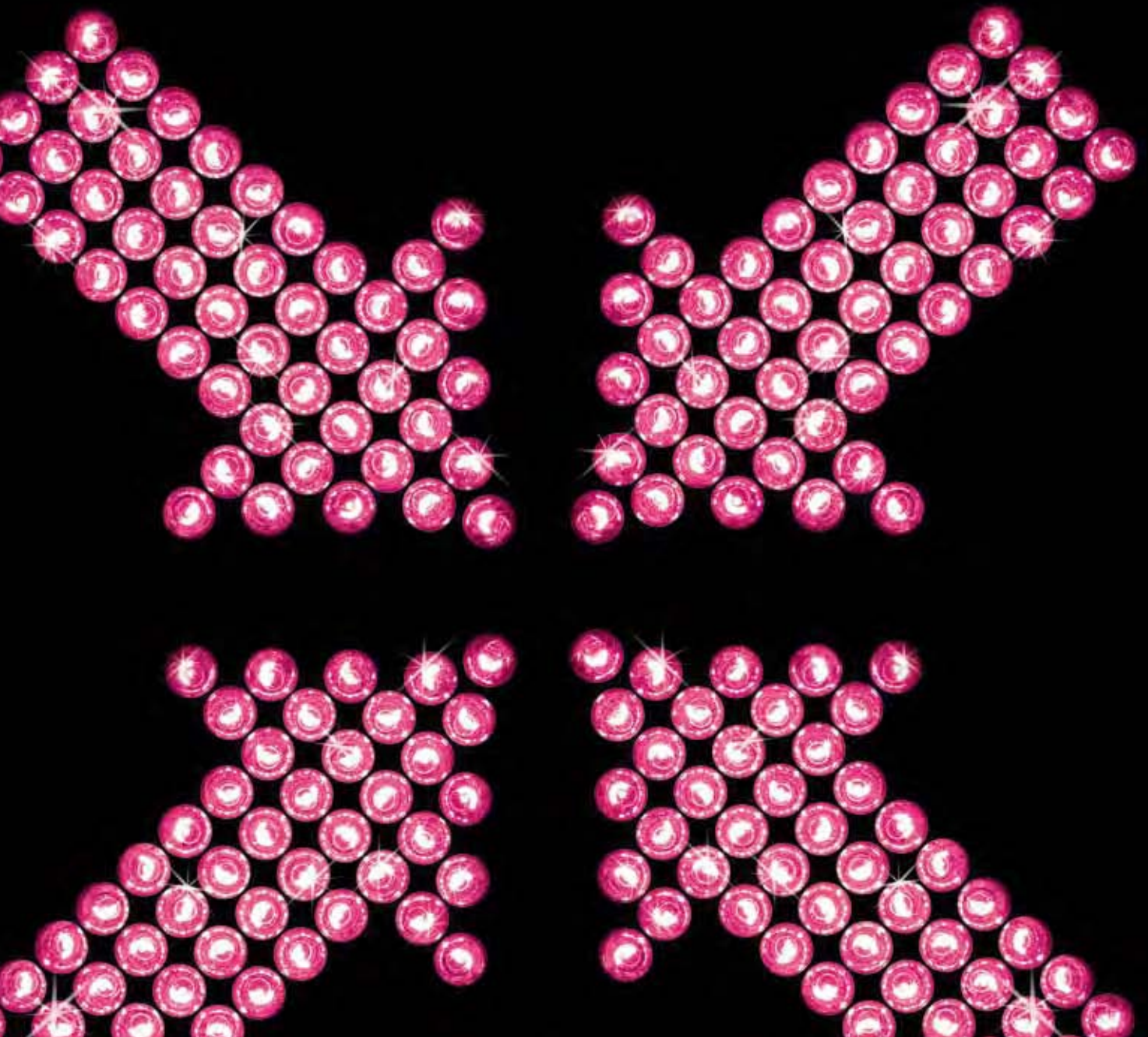
United Kingdom (U.K.)

During 2008, Northern Gas Networks Limited was benchmarked as the most efficient network in the U.K. gas industry compared with our peers, setting the "efficiency frontier" for the industry.

As one of the top two gas distribution networks for the delivery of high standards of customer service, Northern Gas Networks Limited recorded increased customer satisfaction during the year.

Recognition

We have shown our commitment to the community by operating in a socially responsible manner and are encouraged to have been recognised by various organisations for quality and environmental management, occupational health and safety management as well as community service.





2008 HK Award for Industries; 8th China Golden Awards for Excellence in Public Relations; Gold Award in The HK Federation of Insurers Award for Excellence in Occupational Safety & Health; U3A programme named Outstanding Partnership Project; Caring Company Logo; 2008 HK Enterprise Environmental Achievement Award; 2008 Prime Awards for Eco-Business.

The U3A programme is named an Outstanding Partnership Project under the Caring Company Scheme. The project excels at encouraging local retirees to continue learning and contributing to society for life.

...for our efforts

Environmental awards

Among our honours in the past year was the Environmental Performance Award of the 2008 Hong Kong Award for Industries organised by the Business Environment Council.

We also received the Class of Excellence IAQWiSe Label for the Hongkong Electric Centre for our good indoor air quality under the 2008 Hong Kong Awards for Environmental Excellence organised by the Hong Kong Government and local trade associations.

Finally, we were proud to be awarded the Class of Excellence and the Class of Good EnergyWiSe Labels for electricity generation and delivery activities respectively, and the Class of Excellence of the WastewiSe Labels for both electricity generation and delivery activities, under the Hong Kong Awards for Environmental Excellence in its first year of implementation.

Integrated Management System

In December 2008, the HKQAA awarded the OHSAS 18001, ISO 14001 and the ISO 9001: 2008 as well as an IMS certificate embracing all operations of the Projects Division (PD). The PD successfully passed the HKQAA's surveillance audit on its existing Quality Management System in 2008 version and certification audits on the newly established Environmental Management System and Occupational Health & Safety Management System.

In 2008, our Transmission & Distribution (T&D) Asset Management System, which underpins the excellent reliability of our electricity supply, was certified by HKQAA for compliance with BSI PAS 55-1. We were the first company in Hong Kong to be awarded this certification by the HKQAA.

In November 2008, six ISO 9001 certificates from T&D were re-certified to meet the more stringent requirements of the upgraded ISO 9001: 2008 Standards after the surveillance audits by the HKQAA. The Environmental, Health and Safety Integrated Management System of the T&D Division comprising ISO 14001, OHSAS 18001 and ISO 9001 was well maintained and satisfactorily passed the HKQAA's surveillance audit.

Safety awards

Our focus on safety training continued to show good results. We won the Gold Award in The HK Federation of Insurers Award for Excellence in Occupational Safety & Health (OSH), the Silver Award in the OSH Annual Report Award and the Bronze Award in the Safety Enhancement Program Award at the 2008 Hong Kong Occupational Safety & Health Award Forum. As well, HK Electric was a Cup Champion in the Occupational Safety & Health Quiz 2008 that was organised by the Labour Department and Occupational Safety & Health Council.

Internationally, ETSA Utilities received a major award from SafeWork for Best Safety Management System in South Australia.

Among our honours in the past year is the Environmental Performance Award of the 2008 Hong Kong Award for Industries organised by the Business Environmental Council.

Community awards

In recognition of our contribution made to the Community Chest of Hong Kong through various fund-raising events during their campaign year of 2007/08, the Company was presented with the President's Award; the Gold Award for the Corporate and Employee Contribution Programme and the 8th Top Fund-raiser for the Employee Contribution Programme 2007/2008.

The Smart Power Campaign won the Silver Award in the Community Relations category at the 8th China Golden Awards for Excellence in Public Relations at a presentation ceremony held in Beijing on 14th November. Another programme, the opening of Lamma Winds, won a Nomination Award in the Environmental Protection category.

The Caring Company Logo was awarded to HK Electric for the 6th consecutive year in recognition of our efforts to build a caring community spirit by cultivating corporate citizenship among our various stakeholders, and for the strategic partnership between the business and social service sectors.

The U3A programme jointly organised with the Hong Kong Council of Social Service was named an Outstanding Partnership Project under the Caring Company Scheme. The project excels at encouraging local retirees to continue learning and contributing to society for life.

Tso Kai-sum

Group Managing Director
Hong Kong, 17th March 2009