

## **HONGKONG ELECTRIC HOLDINGS LIMITED**

### **OPERATIONS REVIEW**

Sales of electricity rose by 3.2% in 2001 to 10,311 million kWh. Maximum demand reached another record high, rising 4.1% to 2,516 MW. Demand was led by the commercial sector, which saw a 4.4% increase. With this sector accounting for more than 70% of total sales, it demonstrates the resilience of demand to economic weakness, supporting our long-term forecasts. Customer numbers rose 1.9% to 535,549.

#### ***Generation***

The Generation Division again exceeded performance targets while increasing productivity and taking further measures to improve operations from an environmental perspective.

The Lamma Power Station continued to perform well. The availability of coal fired generating units increased as we reduced the number and length of planned outages for upgrading work.

Work continued on the conversion of two existing gas turbines to a combined cycle unit. This will generate an additional 115MW of power with the same fuel input through recovering waste heat energy. This project is on target for completion in September 2002.

The coal jetty extension at Lamma Power Station was completed, further improving our coal handling facilities. Control systems were upgraded.

Consumption of low sulphur coal, our main fuel source, grew to over four million tonnes. With coal a major cost to the Group, we devoted considerable effort to finding ways to achieve savings. Higher oil prices led to increased global demand for coal and rising prices. We sought to counter this through wider diversification and the use for the first time of more cost effective sub-bituminous coal. The results have been satisfactory and we plan to use more of this fuel in future.

The Environmental Management System has allowed us to prioritise our efforts to protect the environment. The progress to retrofit a submerged scraper conveyor system neared completion, in line with our goal of minimising effluent discharge. We also increased our recycling of wastewater and rainwater.

Work on the Lamma Power Station extension began in March and solid progress was made. Dredging was completed and construction began on the seawall. The 300MW gas-fired generating unit of Phase I is targeted for completion by mid 2004.

### ***Transmission and Distribution (T & D)***

In 2001, the T&D Division continued to exceed targets for customer services and supply reliability while its productivity was further improved.

All 18 pledged service standards were met or surpassed and 851 commendations were received from our customers. We continued to make use of the latest technologies to improve our customer services. In 2001, HEC expanded and upgraded its remote meter reading system for its maximum demand customers. Aside from basic meter reading functions, the system provides continuous monitoring of meter integrity and on-line acquisition of load profiles for the customers. In addition, the WAP (Wireless Application Protocol) service was extended to all mobile phone users so that customers can freely access their electricity account and obtain other useful information and services with a WAP phone anywhere and anytime.

The supply reliability achieved was 99.999% - an exceptional rating achieved now for six consecutive years. To maintain this level of reliability and to meet the increase in electricity demand, a total of 53 new distribution substations were commissioned and 286km of distribution cables laid.

To provide supply to the MTR Tseung Kwan O Line, a new 2x60MVA infeed substation at Quarry Bay was commissioned.

The Group also completed preparatory work for the new 22kV distribution voltage system to be introduced to the Cyberport and Central area in year 2002, followed in year 2003 by the Southern District.

The 22kV voltage has the same cable size and hence capacity is twice that of 11kV cables. It will require less underground space and since most underground spaces in Hong Kong are already congested, 22kV distribution is the most effective means of expanding our electricity distribution network to meet increased demand. The 22kV voltage has been adopted by other major cities with a similar underground congestion situation and high load density and is the first of its kind to be introduced in the Hong Kong SAR.

## *International*

### ETSA Utilities, Australia

ETSA Utilities, the electricity distribution business for the State of South Australia jointly owned by the Group and Cheung Kong Infrastructure, performed well during 2001. Sales revenue for the year of 2001 was higher than expected due to a record number of new customer connections and strong sales during a hotter than expected summer, together with a buoyant economy driven by a thriving building industry. Indeed, the severe weather conditions including major storms and the hottest summer of 93 years put great strain on the distribution network. In response, additional capital was invested to ensure a continued high level of system reliability. In addition, significant efficiency gains were achieved across the organization during the year, through improved work practices, increased automation and greater utilization of information technology.

### Powercor Australia

Powercor Australia, also jointly owned by the Group and Cheung Kong Infrastructure, is Victoria's largest electricity distributor, with a network covering about 64% of the State. This business performed strongly in 2001, achieving higher than budget electricity sales gross margin in servicing Melbourne's rapidly expanding western suburbs and the State's key regional and rural growth centres. During 2001, attention was also focused on productivity improvements and cost savings without adversely affecting system reliability or customer service, and significant progress was made in this area. In June, and in keeping with the Group's policies on risk management, the energy trading retail division of Powercor was disposed of for A\$315 million, with the proceeds being used to reduce gearing. This transaction gave rise to a profit on disposal attributable to the Group of HK\$344 million.

### Union Power Development Company Limited, Thailand

During 2001, the Group added to our overseas portfolio with the acquisition of a 26% stake in Union Power Development Company Limited (UPDC), a consortium including leading Japanese energy concerns. UPDC has a license to develop one of the largest coal-fired power stations to be built in Thailand. The 1,400 MW facility in Hin Krut province will help prevent a looming energy deficit as power consumption continues to rise in the country. The project will benefit from a 25-year take-or-pay Power Purchase Agreement with the Government-owned Electricity Generating Authority of Thailand, at a tariff linked to the US dollar exchange rate. The Group has an option to increase its holding to 27.5% in the future.

Full environmental clearance has been granted, together with all other necessary licenses. Substantial commitments have been obtained for a non-recourse project financing. We are awaiting final approval from the Government of Thailand and aim to begin construction in late 2002, with the first 700MW phase to come on stream in 2006.

## **Associated Technical Services Limited (ATS)**

ATS continues to make useful contribution to the profit of the Group. In year 2001, ATS secured engineering service contracts in China, Taiwan and Thailand.

### **People**

#### ***Productivity***

Economic conditions brought a renewed emphasis on productivity. The Group's restriction on hiring remained in place and overall headcount fell, resulting in a rise of 5.4 % in output to 4.53 million kWh per employee.

#### ***Training***

We have achieved productivity gains not only through the application of technology but also by training people to work more flexibly and across a broader range of skills. This also increases job satisfaction. In 2001, Operations Division devoted a total of 101,000 man-hours to training.

#### ***Health and Safety***

The Group's longstanding "safety first" culture resulted in standards of health and safety classified as "excellent" internationally being achieved for 2001.

The T & D Safety Management System was accredited to OHSAS 18001 and HEC was the first local utility to acquire this prestigious certificate in health and safety management.

External recognition came when the division won the "Gold Award for Safety Management Systems" in the Occupational Health & Safety Enhancement Forum organised by Hong Kong's Occupational Health & Safety Council.

## **Corporate Citizenship**

The Group takes seriously its responsibilities to protect the environment and its contribution to the community.

### ***Environmental Care***

The adoption during 2001 of Environmental Management Systems by the Generation and T & D divisions demonstrates our continuing commitment to reducing the impact of our operations on the environment. The system has raised our environmental monitoring to the highest international standards and allowed us to prioritise our initiatives in this area more effectively.

No environmental incidents were recorded for the year. We increased our recycling of wastewater and rainwater. Ash disposal continued to decline towards zero, as the closed loop system diverted more to cement making.

As a step towards assessing the feasibility of renewable energy in Hong Kong, the Group in collaboration with Friends of the Earth has initiated a wind data survey study to ascertain the wind power potential in Hong Kong. After a careful site search, two wind monitoring stations on Po Toi Island and Lamma Island were set up in April and November 2001 respectively for collecting wind data over a period of 12 months.

The photovoltaic study by the University of Hong Kong which we are sponsoring has made good progress. Much valuable data was collected for analysis of the performance of photovoltaics under various weather conditions in Hong Kong.

### ***Community Outreach***

Safety is an important feature of our work with the community. Together with the Government's Electrical & Mechanical Services Department, we launched a Public Safety Education Campaign to heighten awareness of the need to use electrical appliances properly.

To enable visually impaired and elderly customers to receive the same messages, we converted printed safety and customer service information booklets to CD and audiocassette, supplementing the special page for the visually impaired on our website.

We also widened our concessionary tariff scheme that assists disadvantaged groups such as the disabled and the elderly, by extending it to single parent families. This helps to ensure that electricity is affordable across the community.

## **Corporate Governance**

The Company is committed to high standards of corporate governance and has complied throughout the year with the Code of Best Practice, as set out in Appendix 14 of the Rules Governing the Listing of Securities (“Listing Rules”) issued by The Stock Exchange of Hong Kong Limited.

The Board meets formally at least four times a year. The Executive Directors are responsible for the day-to-day management of the Company’s operations. In addition, there are regular meetings with the senior management of the Company’s subsidiary and associated companies, at which Group strategies and policies are formulated and communicated.

The Group views well developed reporting systems and internal controls as essential and the Board of Directors plays a key role in the implementation and monitoring of internal financial controls. Their responsibilities include :

- Regular board meetings focusing on business strategy, operational issues and financial performance.
- Active participation on the Boards of subsidiary and associated companies.
- Approval of annual budgets for each operating company covering strategy, financial and business performance, key risks and opportunities.
- Monitoring the quality, timeliness, relevance and reliability of internal and external reporting.

To enable the Company’s Directors to meet their obligations, an appropriate organizational structure is in place with clearly defined responsibilities and limits of authority.

The Company’s Audit Committee is composed of three independent Non-executive Directors and written terms of reference which describes the authority and duties of the Audit Committee are regularly reviewed and updated by the Board. The Audit Committee reports directly to the Board of Directors and reviews matters within the scope of audit, such as Financial Statements and internal controls, to protect the interests of the Company’s shareholders. The Audit Committee meets regularly with the Company’s external auditors to discuss the audit process and accounting issues, and review the effectiveness of internal controls and risk evaluation.