

# financial review

## Capital Expenditure, Liquidity, Financial Resources and Gearing Ratio

Capital expenditure during the year amounted to HK\$3,005 million, which was primarily funded by cash from operations. Total external borrowings outstanding at year-end were HK\$10,645 million (2004 : HK\$12,997 million), comprising unsecured bank loans, unsecured deferred creditors and debt securities in issue. In addition, the Group has undrawn committed bank facilities of HK\$3,465 million (2004 : HK\$5,376 million) and available liquid funds of HK\$4,561 million (2004 : HK\$1,426 million). Gearing ratio (net debt/shareholders' funds) at 31st December 2005 was 15% (2004 : 31%).

## Treasury Policies, Financing Activities and Capital Structure

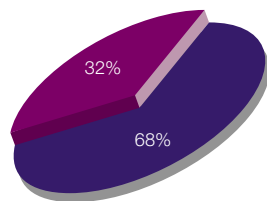
We finance our operations and business expansion by a combination of internal resources, bank borrowings and debt issuance. We manage our financing activities to ensure that committed facilities are available for refinancing and business growth.

Capitalising on the liquidity in debt markets and the low interest rate environment, Hongkong Electric, through its subsidiary Hongkong Electric Finance Limited, issued HK\$500 million 4.15% p.a. fixed rate notes due 2015 in May 2005. The issue was made out of the Medium Term Note Programme established in 2002.

In December 2005, the Group disposed of a 22.07% attributable interest in its Australian electricity distribution business. The disposal generated a A\$948 million (HK\$5,405 million) cash inflow for the Group, A\$488 million (HK\$2,781 million) of which was utilised to reduce borrowings associated with the investment in the distribution business.

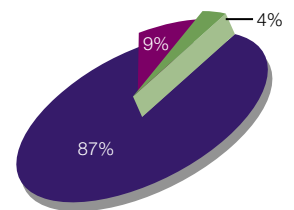
At 31st December 2005, the profile of our external borrowings after taking into account currency and interest rate swaps was as follows:

68% ● Hong Kong Dollars  
32% ● Australian Dollars



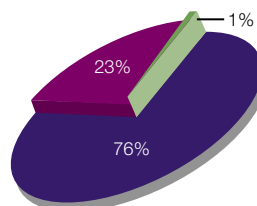
### By Currency

4% ● Within 1 Year  
87% ● Between 2 to 5 Years  
9% ● Beyond 5 Years



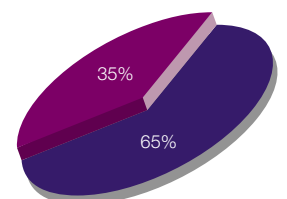
### By Maturity

76% ● Bank Loans  
23% ● Capital Market Instruments  
1% ● Suppliers' Credits



### By Structure

65% ● Fixed or Capped Rate  
35% ● Floating Rate

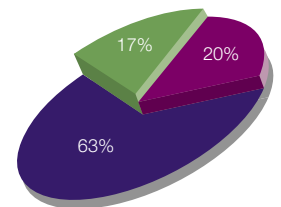


### By Interest Rate Structure

Currency and interest rate risks are actively managed in accordance with our treasury policy. We use derivative financial instruments primarily for managing interest rate and foreign currency risks and do not engage in speculative transactions. Treasury transactions are only executed with counterparties with acceptable credit ratings to control credit risk exposure. Foreign currency transaction exposure is managed, utilising forward contracts and interest rate and currency swaps. As at 31st December 2005, approximately 80% of the Group's transaction exposure was either denominated in US dollars or hedged into Hong Kong or US dollars. Currency exposure arising from overseas investments is mitigated by financing those investments with local currency borrowings.

The Group's policy is to maintain a substantial portion of its debt in fixed or capped rate. Interest rate risk is managed by either securing fixed or floating rate borrowings or by using interest rate swaps and caps. The contractual notional amounts of derivative instruments outstanding at 31st December 2005 amounted to HK\$10,210 million (2004 : HK\$20,598 million).

20% ● Cross Currency Swaps  
 63% ● Interest Rate Swaps & Caps  
 17% ● Foreign Exchange Forward Contracts



## Derivative Financial Instruments

### Contingent Liabilities

As at 31st December 2005, the Company has issued guarantees in respect of development security of an associate amounting to HK\$33 million (2004 : HK\$35 million).

The Company has given guarantees and indemnities in respect of bank and other borrowing facilities available to subsidiaries and financial commitments of subsidiaries totalling HK\$5,002 million (2004 : HK\$11,136 million). Out of this amount, HK\$4,781 million (2004 : HK\$9,238 million), while being a contingent liability of the Company, is reflected in the Consolidated Balance Sheet of the Group.

A wholly-owned subsidiary of the Company, The Hongkong Electric Company, Limited, has given guarantees to third parties in respect of the value of leased equipment of HK\$210 million (2004 : HK\$210 million) at expiry of the lease.

### Employees

The Group continues its policy of pay by performance and market pay rates are monitored to ensure competitiveness is maintained. The Group's total remuneration costs for the year ended 31st December 2005, excluding directors' emoluments, amounted to HK\$889 million (2004: HK\$945 million). As at 31st December 2005, the Group employed 1,987 (2004 : 2,045) permanent staff. No share option scheme is in operation.

Apart from well-established training schemes for university graduates, trainee technicians and apprentices, the Group also provides training for employees in language, computer knowledge and technology relevant to our industry. As well there are job-related courses to enhance the general skills and knowledge of our employees.