Chairman's Statement

Dr. Lee Shau Kee *Chairman and Managing Director*

Dear Shareholders,

On behalf of your Board, I am pleased to present my report on the operations of the Group for the year ended 30 June 2006.

Profit and Net Assets Attributable to Shareholders

The Group's consolidated profit after taxation and minority interests for the year ended 30 June 2006 amounted to HK$3,667.2 million, an increase of HK$159.5 million or 4.5% over the re-stated profit for the previous year. Earnings per share were HK$1.28 (2005 re-stated: HK$1.25).

The underlying profit for the year, excluding the revaluation surplus of investment properties, was HK$2,066.1 million, or a decrease of HK$154.3 million or 6.9%. Based on the underlying profit, earnings per share were HK$0.72 (2005 re-stated: HK$0.79).

At 30 June 2006, the consolidated net asset value attributable to equity shareholders was HK$27,652.6 million, 28.5% higher than the re-stated amount of HK$21,516.5 million a year earlier. At the year end, the Group was in a net cash position of HK$5,063.1 million (2005: HK$2,537.6 million).

Dividends

Your Board recommends the payment of a final dividend of HK$0.15 per share to shareholders whose names appear on the Register of Members of the Company on 12 December 2006. The total distribution per share of HK$0.28 for the full year, including the interim dividend of HK$0.13 per share already paid, is the same as the total distribution per share in the previous year. Warrants for the final dividend will be sent to shareholders on or before 13 December 2006.

Business Review

Property Investment

The Group currently has nine major investment properties. Together with the investment properties held by its listed associates, the Group has a vast portfolio with a total attributable gross floor area of 2.0 million square feet. For the year under review, the Group's gross rental income remained stable at HK$613.8 million, with average occupancy maintained at a high 95% at the year end.

In terms of the office portfolio, Kowloon Building, benefiting from the prevailing shortage of quality office space in core business areas and the trend of decentralization, was 98% let at the year end.

Meanwhile, continued improvement in domestic consumption and tourist arrivals boosted the retail sector. As a result, the Group's network of shopping malls in the new towns, including City Landmark II in Tsuen Wan, Trend Plaza in Tuen Mun, Shatin Centre and Fanling Centre, performed well with occupancy rates ranging from 90% to 99% at the year end. Eva Court, a luxury residential property nestled within Mid-Levels, enjoyed 92% occupancy at the year end.

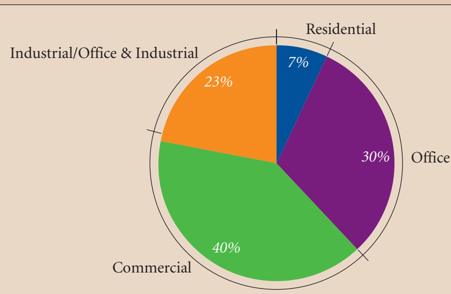
Hotel

Driven by the continued economic growth in this region, coupled with the expansion of the Individual Visit Scheme for mainlanders coming to Hong Kong, the number of tourist arrivals to Hong Kong has shown a steady rise. Newton Hotel Hong Kong and Newton Hotel Kowloon, with average occupancy increased to 83% and average room rate growth of 9.7%, recorded marked increase in room revenue for the year, with double-digit growth in business.

Infrastructural Projects

The Group holds 64% of China Investment Group Limited, which is engaged in the toll-bridge and toll-road joint venture operations in Mainland China. Owing to the repair work undertaken for the Hangzhou Qianjiang Third Bridge, profit for the infrastructural segment dropped by 46.2% to HK$81.8 million. During the year, the Group's interests in Province Expressway 34, Ningbo Fenghua, Zhejiang Province together with its ancillary facilities from Jiangkou to Sanheng and to Daqiao, and from Sanheng to Xiachen, as well as Province Expressway 36 together with its ancillary facilities from Jiangkou to Xikou, were disposed of as they suffered declining traffic flows resulting from keen competition from the newly-completed highways and toll-roads nearby.

Usage of Investment Properties



Others

Megastrength Security Services Company Limited, a wholly-owned subsidiary of the Group, provides a wide range of professional security services, which are complementary to the Group's property management operation. In recognition of its commitment to providing quality service and enhancing customer satisfaction, this company has won a good reputation in the industry.

Associated Companies

The Hong Kong and China Gas Company Limited

38.46% owned by the Group, Hong Kong and China Gas reported an unaudited consolidated profit after taxation of HK$2,509.5 million for the six months ended 30 June 2006, which comprised HK$1,803.6 million arising from its gas business and property rental income (an increase of HK$38.7 million as compared with the corresponding period in 2005) and HK$705.9 million from the sale of properties and a revaluation surplus on an investment property.

- **Gas business in Hong Kong**

  A slower pace of completion and occupancy of new residential units, compounded by the warmer weather during the first half of 2006, has led to a slight decrease of 1.5% in the total volume of gas sales in Hong Kong compared with the same period last year. At 30 June 2006, the number of customers was 1,606,841, an increase of 32,328 from the end of June 2005.

- **Introduction of natural gas to Hong Kong**

  By the fourth quarter of this year, Hong Kong and China Gas will introduce natural gas from the Guangdong Liquefied Natural Gas (LNG) Terminal to Hong Kong to partially replace naphtha as feedstock for the production of town gas. Tai Po gas production plant is now undertaking trial runs of the production of town gas using a dual naphtha and natural gas feedstock mix. Full implementation is scheduled to start in October 2006. As Hong Kong and China Gas has a contract for natural gas to be supplied at a price currently lower than naphtha, savings in production cost will be shared with customers through the existing fuel cost adjustment mechanism, thereby enhancing the competitiveness of the gas tariff. In addition, the introduction of natural gas will also help to protect the environment.

- **Business development in Mainland China**
  Hong Kong and China Gas currently has a total of 43 projects spread across 36 cities in nine provinces and an area of Beijing. Hong Kong and China Gas's mainland city-gas joint ventures have built up an excellent brand reputation across all cities where they are located. Diversification is rapidly transforming Hong Kong and China Gas into a sizable, nation-wide, multi-business corporation from its origins as a local company focused on a single business.

  Hong Kong and China Gas now has city piped gas joint venture projects in 34 mainland cities across Guangdong province, eastern China, Shandong province, central China, northern China, northeastern China and western China. Following the arrival of natural gas in some regions in recent years, Hong Kong and China Gas's joint ventures there converted to natural gas. After the Guangdong LNG Terminal is formally commissioned in the fourth quarter of 2006, its joint ventures in Guangdong province will also convert to natural gas.

  Besides, Hong Kong and China Gas now operates a water supply project in Wujiang, Jiangsu province and in Wuhu, Anhui province, and manages an integrated water supply and wastewater joint venture in Suzhou Industrial Park, Suzhou, Jiangsu province. To cope with the rising need for clean water sources, the central government is opening up the water utility market, which provides enormous opportunities for Hong Kong and China Gas to expand in this sector.

- **Environmentally-friendly energy businesses**
  Liquefied petroleum gas (LPG) filling station business, run by its wholly-owned subsidiary company, ECO Energy Company Limited (ECO), continues to achieve business growth. Following the implementation of a new pricing mechanism in March 2006, ECO filling stations have been able to adjust their LPG selling prices every month. This will improve business prospects as prices can now be more directly linked to the cost of LPG. Meanwhile, ECO's landfill gas project at the North East New Territories landfill site is progressing well and its operational tests will be conducted within this year. Construction work of a 19 km pipeline to Tai Po gas production plant is also nearly completed. The plant would start using the treated landfill gas to partially replace naphtha as a fuel for town gas production by the end of this year. Using landfill gas will effectively limit depletion of underground oil resources and reduce air pollution, thereby further contributing to the Group's commitment to protect the environment.

- **Property developments**
  Hong Kong and China Gas has a 50% interest in the Grand Promenade property development project at Sai Wan Ho, whose significant returns contributed to its profitability. Following the success of Grand Promenade, the pre-sale of Grand Waterfront which is located at the Ma Tau Kok south plant site commenced in August 2006 and drew excellent response. Hong Kong and China Gas is entitled to 73% of the net sales proceeds of the residential portion, and has the full interest in the commercial portion of this project. Hong Kong and China Gas has an approximate 15.8% interest in the International Finance Centre (IFC). The shopping mall and office towers of IFC are almost fully let. Four Seasons Hotel and Four Seasons Place, which provide approximately 400 six-star hotel guest rooms and 520 hotel suites respectively, reported satisfactory results since their opening in September 2005.

Hong Kong and China Gas has not increased its basic gas tariff for the past eight years. Nevertheless it has made every effort to enhance its operational effectiveness, thus maintaining steady business performance. Full implementation of the production of town gas using a dual naphtha and natural gas feedstock mix is scheduled to start in October 2006. Since Hong Kong and China Gas contracted in 2002 to take natural gas at a comparatively low price, given the increasing competitiveness in the energy market, it now expects to lower its gas tariff to the benefit of both customers and future business development.

Hong Kong Ferry (Holdings) Company Limited

This associated company is 31.33% owned by the Group. The unaudited consolidated profit after taxation of Hong Kong Ferry for the six months ended 30 June 2006 amounted to HK$121.8 million, a decrease of HK$68.2 million or 35.9% over that for the same period last year. The sale of residential units of Metro Harbour View at 8 Fuk Lee Street, Tai Kok Tsui, Kowloon, continued to be the main profit driver for Hong Kong Ferry for the period under review, during which 95 units were sold.

Hong Kong Ferry plans to launch MetroRegalia at Tong Mi Road for sale in late 2006, in addition to selling the remaining unsold units of Metro Harbour View.

Besides, good progress has been made in the construction for the development site at 222 Tai Kok Tsui Road, which will be developed into a residential-cum-commercial property with a total gross floor area of approximately 320,000 square feet, comprising some 270,000 square feet of residential space and about 50,000 square feet of non-residential space. It is expected to be completed by late 2008.

The foundation and construction works for No.6 Cho Yuen Street, Yau Tong will commence in late 2006 and should be completed by early 2009. It will provide a total gross floor area of approximately 165,000 square feet, comprising some 140,000 square feet of residential space and 25,000 square feet of non-residential space.

Miramar Hotel and Investment Company, Limited

44.21% owned by the Group, Miramar reported a consolidated net profit after taxation of HK$1,169.4 million for the year ended 31 March 2006, an increase of 38.2% over the re-stated profit for the previous year. On a basis consistent with that for the previous year (before the re-statement of profit to comply with new accounting standards related to investment properties and hotel properties), the profit for the year including profit generated from land sales amounting to approximately HK$150 million would have been HK$448.0 million, an increase of 40.0% over the previous year. Increased tourist arrivals, improved employment levels and encouraging performance from property leasing activities have all contributed favourably to the company's results.

Miramar Hotel achieved healthy growth in its operating results with close to 90% average occupancy and an increase of 19% in average room rate. Performance in its food and beverage operation was steady. In the hotel management business, average room rate for the seven hotels under management recorded satisfactory growth with steady increases in average occupancy. Progress was made during the year to upgrade the client-mix and the overall image of the Miramar Shopping Centre, with its average occupancy reaching 91%.

During the year, Miramar sold approximately 60 acres (194 lots) of residential land and 20 acres of commercial land in Placer County, California, contributing HK$150 million in after-tax profit. At the end of the financial year, approximately 80 acres (290 lots) of residential land and 70 acres of commercial land remained available for sale. In Shanghai, almost all the office units at Shang-Mira Garden have been sold and its shopping arcade continued to achieve a high occupancy rate of 99%.

The overall results for Miramar Express improved slightly and the commercial travel sector increased its profit by more than 40%. Miramar Travel, its group tour business arm, joined forces with an industry veteran and Miramar reduced its shareholding to 54%. With a series of marketing activities under an innovative style of operation, marked improvement is expected for its travel business.

Privatisation Schemes

Henderson Cyber Limited

In August 2005, the Company, Henderson Land Development Company Limited ("Henderson Land"), Hong Kong and China Gas and Henderson Cyber jointly announced the privatisation proposal of Henderson Cyber by the Company and Hong Kong and China Gas by way of a scheme of arrangement involving the cancellation and extinguishment of the scheme shares in Henderson Cyber at the cancellation price of HK$0.42 in cash per scheme share. The scheme was approved by a majority of 99.96% of the independent shareholders present and voting at the Court Meeting. The scheme took effect in December 2005 and the listing of the shares in Henderson Cyber on the Growth Enterprise Market of the Stock Exchange of Hong Kong Limited was withdrawn. Upon completion of the privatisation, the Company's interest in Henderson Cyber was increased to approximately 78.69%, with the balance of 21.31% held by The Hong Kong and China Gas Company Limited. The aggregate amount of cancellation price paid by the Group was HK$252.53 million.

The Company

Henderson Land made a second attempt to privatise the Company in November 2005, following an unsuccessful privatisation effort in November 2002 ("the 2002 Exercise"). As announced in December 2005, the cancellation consideration was increased to one share in the Henderson Land in exchange for every 2.5 scheme shares in the Company. In order for the proposal to succeed, the scheme should not be disapproved by more than 10% in value of all the shares held by independent minority shareholders of the Company (the "10% Threshold").

At the Court Meeting held on 20 January 2006, a majority of up to 85.7% (as compared with 85.6% in the 2002 Exercise) of the independent minority shareholders of the Company present voted in favour of the privatisation proposal. However, since the votes that were cast against the scheme marginally exceeded the 10% Threshold — a repeat of the 2002 Exercise, the scheme could not take effect and hence lapsed. It is regrettable that, despite the majority support of independent minority shareholders of the Company on both occasions, the privatisation proposal on each occasion fell through by the narrowest of margin under the 10% Threshold.

Issue of New Shares

On 18 April 2006, pursuant to a placing agreement, a subsidiary of Henderson Land sold 230 million existing shares of the Company at the placing price of HK$13.55 per share. Pursuant to the placing agreement, the Company then issued 230 million new shares to Henderson Land at the placing price adjusted for this purpose by the expenses incurred in relation to the placing and the subscription. The new shares represented approximately 8.2% of the Company's then existing issued share capital and about 7.5% of its issued share capital as enlarged by the subscription.

Corporate Finance

The Group has always adhered to prudent financial management principles. At 30 June 2006, the cash holdings of the Group amounted to approximately HK$5,177.0 million (2005: HK$2,800.2 million). After netting off the total bank borrowings of HK$113.9 million (2005: HK$262.6 million), the Group was in a net cash position of HK$5,063.1 million (2005: HK$2,537.6 million).

All of the Group's bilateral banking facilities to fund the general operation are denominated in Hong Kong Dollars. For the Group's subsidiary, China Investment Group Limited, a portion of its borrowings to fund its toll road projects in Mainland China is denominated in Renminbi. Apart from its investments in China which are denominated in Renminbi and are not hedged, the Group had no other material open foreign exchange positions at the financial year end.

Prospects

Looking ahead, buoyant consumer confidence will continue to underpin retail spending and hence rental growth for shopping centres. The office market is expected to perform well on the back of tight supply being met by keen demand from companies looking for expansion opportunities. The continuing increase in expatriate inflow to Hong Kong will continue to fuel the hotel and residential market and sustain promising growth in rental rates. Rental income from both new lettings and renewals is expected to rise.

As such, both the Group's rental income, as well as recurring earnings from the Group's listed associates, will continue to grow steadily. With a strong cash position, the Group is well poised to capitalize on opportunities for quality asset expansion and business growth, generating higher returns for shareholders. In the absence of unforeseen circumstances, performance of the Group will show satisfactory growth in the coming financial year.

Appreciation

Executive Director Mr. Ho Wing Fun stepped down from the Board on retirement during the year. I would like to thank Mr. Ho most sincerely for his long years of loyal service and immense contributions to the Group.

I would also like to take this opportunity to thank the Directors for their wise counsel and support, and the management and staff at all levels for their dedication, hard work and contributions in the past year. I know I can continue to count on them in our quest to deliver value to our shareholders.

Lee Shau Kee
Chairman

Hong Kong, 21 September 2006