Operations Review

OUR BUSINESS

Hysan is principally engaged, together with its subsidiaries and joint ventures, in investment, development and management of quality properties. As at 31 December 2006, Hysan's investment property interests totalled some 3.8 million gross square feet of high-quality office, retail and residential space in Hong Kong. The redevelopment of the Hennessy Centre commenced in the fourth quarter of 2006 accounted for the year-on-year reduction of gross floor area.

Michael T.H. Lee, Managing Director

2006 PERFORMANCE

The Group's turnover was HK$1,268 million, up 1.4% (2005: HK$1,250 million). If the element of the Entertainment Building (disposed of at the end of 2005) is excluded, the turnover increase would be 8.3%.

Profit excluding asset value changes and prior year tax provision was HK$755 million, 17.8% up from last year (2005: HK$ 641 million). Underlying profit, excluding unrealised revaluation changes on investment properties and related items, amounted to HK$1,012 million (2005: HK$1,005 million). Profit for the year was down by HK$1,022 million (24.8%), to HK$3,099 million (2005: HK$4,121 million), mainly due to HK$1,650 million less fair value changes on the Group's investment properties taken to the income statement, reflecting a rise in asset value at a more moderate rate.

PERFORMANCE INDICATORS

Although many factors contributed to the results of the Group's businesses, some of the key drivers for assessment of our performance included those set out below. Performance is measured by these and other financial indicators as further analysed below.

Key Indicators	
Operations	1. Occupancy rate 2. Rental income growth 3. Property expenses and as a percentage of turnover
Investments in listed securities	1. Total return – comprises dividends received and capital value growth
Financials	1. Average finance costs 2. Net debt to equity 3. Net interest coverage 4. Fixed/floating debt ratio 5. Average debt maturity 6. Ratio of bank facilities and capital market issuance – as a measure of diversity of funding sources

Condensed Consolidated Income Statement for the Year Ended 31 December	2006 HK$ million	2005 HK$ million	Change HK$ million	%
Turnover	1,268	1,250	18	1.4
Property expenses	(240)	(237)	(3)	(1.3)
Other income	147	38	109	286.8
Administrative expenses	(111)	(103)	(8)	(7.8)
Fair value changes on investment properties	2,576	4,226	(1,650)	(39.0)
Fair value changes on financial instruments	31	(25)	56	N/A
Net realised gain on disposal of available-for-sale investments	170	–	170	N/A
Share of results of associates	120	241	(121)	(50.2)
Finance costs	(163)	(214)	51	23.8
Taxation				
– current	(89)	(178)	89	50.0
– deferred	(469)	(678)	209	30.8
Minority interests	(141)	(199)	58	29.1
Profit for the year	3,099	4,121	(1,022)	(24.8)
Underlying profit	1,012	1,005	7	0.7
Profit excluding asset value changes and prior year tax provision	755	641	114	17.8

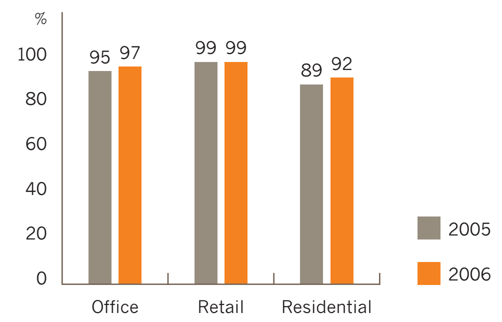
Turnover

Turnover comprised principally rental income derived from the Group's investment properties portfolio in Hong Kong.

The relevant occupancy rate, gross floor area and turnover of the Group's investment properties portfolio are as follows:

Key Indicator

Occupancy Rate



Gross Floor Area (million square feet)	Office	Retail	Residential	Total
At 1.1.2005	2.7	1.2	0.8	4.7
Property disposed of on 30.12.2005 (Note 1)	(0.1)	(0.1)	–	(0.2)
At 31.12.2005	2.6	1.1	0.8	4.5
Property under redevelopment vacated on 30.9.2006 (Note 2)	(0.5)	(0.2)	–	(0.7)
At 31.12.2006	2.1	0.9	0.8	3.8

Notes: (1) Entertainment Building
(2) Hennessy Centre

Key Indicator

Turnover

	2006	2005			Year-on-year Change			
	From Property Held at year end (1) HK$ million	From Property Held at year end (1) HK$ million	Disposed(2) HK$ million	Total HK$ million	From Property Held at year end (1) HK$ million	%	Total HK$ million	%
Office	509	462	39	501	47	10.2	8	1.6
Retail	491	463	40	503	28	6.0	(12)	(2.4)
Residential	232	209	–	209	23	11.0	23	11.0
Others	36	37	–	37	(1)	(2.7)	(1)	(2.7)
	1,268	1,171	79	1,250	97	8.3	18	1.4

Notes: (1) Hennessy Centre was vacant as at 30 September 2006 in preparation for redevelopment
(2) Entertainment Building was disposed of on 30 December 2005

Office Sector

Positive rental reversion, which began in the second half of 2005, continued into 2006. The Group was successful in concluding renewals and new leases during the year with strong growth in rental rates. Such positive reversion, together with full year contribution of renewals and new leases concluded in 2005, brought a 10.2% like-for-like office revenue growth to HK$509 million. Overall office sector revenue, reflecting the impact of the disposal of the Entertainment Building on 30 December 2005, increased by 1.6%.

Retail Sector

Although tourist spending continued to be a significant source of retail consumption, strong domestic demand on the back of favourable employment conditions and financial market performance became the key driver of rental growth in the retail sector. The Group's retail properties remained virtually fully let as at 31 December 2006. Renewals and new leases were successfully concluded with satisfactory rental rates growth during the year. A 6.0% like-for-like rental growth was recorded, since most of these renewals and new leases were completed during the second half of the year. Such rental rate increases will be translated into a full year contribution in 2007. Overall retail sector revenue, however, decreased slightly by 2.4% in light of the disposal of the Entertainment Building as at the end of 2005.

Residential Sector

There was a sustained demand for luxury residential properties from expatriates with more flexible housing budgets. Year-on-year growth was HK$23 million, up 11.0% from last year. This was mainly due to higher occupancy (2006: 92%; 2005: 89%) and to increased rental levels achieved for our residential units.

Property Expenses

Property expenses are the costs of providing property services directly associated with the daily operations of our investment properties, being primarily related to utilities costs, building operations, front-line staff wages, repairs and maintenance.

Property expenses amounted to HK$240 million (overall: up 1.3%; excluding the Entertainment Building: up 6.7%). This was mainly attributable to the increase in utilities costs and government rates, and higher direct costs incurred in revenue generation including agency costs, repairs and maintenance and building refurbishment.

Overall the property expenses were maintained at 19% of turnover.

Key Indicators		
	2006	2005
Property expenses (HK$ million)	240	237
Percentage on turnover	19%	19%

Other Income

Other income mainly comprised dividend, interest and other receivables, which amounted to HK$147 million (2005: HK$38 million). The increase was attributable to the recognition of a recovery item, higher dividend income from the Group's listed securities investment and additional interest income derived by depositing surplus cash proceeds of the Entertainment Building received at the end of 2005.

Administrative Expenses
Administrative expenses increased by HK$8 million (7.8%) over the 2005 level. This included higher employee share option costs, which since 2005 are required to be recognised in the income statement on a cumulative basis under the applicable accounting standards, despite the fact that no cash outlay was involved. Other reasons included increased managerial staff costs and pay rises in line with the market.

Fair Value Changes on Investment Properties
The Group has elected the fair value model for investment properties under the Hong Kong Accounting Standard ("HKAS") 40. As at 31 December 2006, the investment properties of the Group were revalued at HK$32,473 million (2005: HK$29,815 million), by an independent professional valuer, being 8.9% higher than the corresponding value for last year. This reflected further increase in rentals of the Group's existing investment properties portfolio and the redevelopment of the Hennessy Centre.

Excluding additions, adjustments and disposals, fair value gain on investment properties of HK$2,576 million (2005: HK$4,226 million) were recognised in the consolidated income statement during the year.

Investment Properties	Fair Value HK$ million
As at 31 December 2005	29,815
Additions and adjustments	84
Fair value gain	2,576
Disposals	(2)
As at 31 December 2006	32,473

Fair Value Changes on Financial Instruments
The Group enters into hedging arrangements from time to time to hedge volatilities and pricing risks of its treasury assets and liabilities. Positive fair value changes of HK$31 million recognised in the income statement mainly represented the aggregate of the marked-to-market fair value movements of these financial instruments.

Net Realised Gain on Disposal of Available-For-Sale Investments
The Group has been managing its treasury assets held as long-term investments with the aim of balancing the anticipated liquidity position, funding needs and capital gains. For this reason, certain available-for-sale investments were disposed of during the year resulting in a net realised gain of HK$170 million (2005: Nil). The remaining available-for-sale investment portfolio will continue to be held as the Group's long-term investments.

Share of Results of Associates
The Group has 23.7% and 25.0% ownership in the Shanghai Grand Gateway and the Singapore Amaryllis Ville projects respectively.


The Shanghai Grand Gateway development continued to deliver a good performance. The Group's share of results, excluding revaluation gains, recorded a 3.5% increase year-on-year. 100% occupancy was recorded for the retail and office properties. Satisfactory occupancy was achieved for the residential properties, including the luxury residential and serviced apartment development completed in 2006. Under HKAS 40, properties at Shanghai Grand Gateway have been revalued at market value by an independent professional valuer. The Group's share of the increase in valuation, less the corresponding deferred tax thereon, amounted to HK$57 million (2005: HK$182 million).

The Singapore Amaryllis Ville project continued to make a small positive contribution in 2006, reflecting the sale of additional units and increased rental income derived from the remaining units.

Finance Costs

During 2006, sales proceeds from the Entertainment Building (completed on 30 December 2005) were used to further reduce the Group's debt level. This led to a 23.8% reduction in finance costs to HK$163 million (2005: HK$214 million), despite the progressively increasing market interest rate. The Group also repurchased some of its fixed rate notes and progressively reduced the proportion of its fixed rate borrowing as part of its interest costs management programme. The Group's average finance costs rose to 4.9% in 2006 (2005: 3.6%). Further discussions on financial management, including financing policy and financial risk management are set out in the "Financial Policy" section.

Taxation

Tax provision was HK$558 million in 2006 (2005: HK$856 million) principally due to reduced deferred tax provision relating to lower revaluation gains on investment properties and the absence of prior year tax provision of HK$103 million.

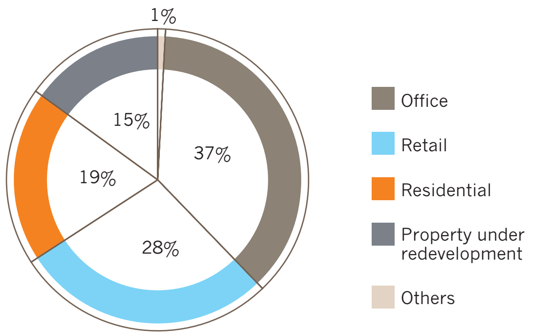
Condensed Consolidated Balance Sheet as at 31 December	2006 HK$ million	2005 HK$ million	Change HK$ million	% %
Investment properties	32,473	29,815	2,658	8.9
Available-for-sale investments – listed	1,678	1,170	508	43.4
Available-for-sale investments – unlisted	67	86	(19)	(22.1)
Interests in associates	1,272	1,147	125	10.9
Cash and bank balances	385	1,402	(1,017)	(72.5)
Other assets	378	371	7	1.9
Total assets	36,253	33,991	2,262	6.7
Borrowings	(2,821)	(4,301)	1,480	34.4
Taxation				
– current	(225)	(198)	(27)	(13.6)
– deferred	(3,349)	(2,879)	(470)	(16.3)
Other liabilities	(950)	(960)	10	1.0
Total assets less liabilities	28,908	25,653	3,255	12.7
Shareholders' funds	27,828	24,667	3,161	12.8
Minority interests	1,080	986	94	9.5
	28,908	25,653	3,255	12.7
Adjusted shareholders' funds	30,729	27,134	3,595	13.2

Investment Properties

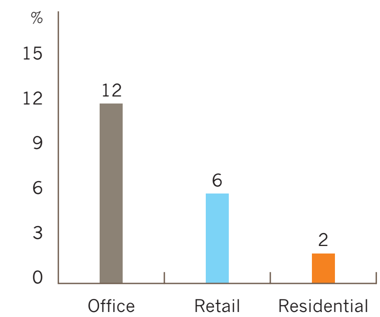
The investment properties were valued at HK$32,473 million, up by 8.9% (HK$2,658 million) from HK$29,815 million in 2005.

Breakdown of the Group's (i) investment properties value by sector as at year-end 2006 and (ii) year-on-year capital growth are as follows:

Capital Value by Sector



Capital Growth by Sector
(excluding property under redevelopment)



Available-For-Sale Investments

Available-for-sale investments comprised principally securities listed in Hong Kong.

The Hong Kong stock market reached a record high in 2006. Total returns from the Group's listed securities portfolio, including both dividend income and capital value growth, were 57.3% (2005: 31.6%). Total fair value of our listed securities portfolio as at 31 December 2006 was HK$1,678 million (2005: HK$1,170 million).

Interests in Associates

Interests in associates increased by HK$125 million (10.9%) over last year. This represented the Group's share of results in the Shanghai Grand Gateway and Singapore Amaryllis Ville projects.

Cash and Bank Balances

The cash and bank balances amounted to HK$385 million as at 2006 year-end (2005: HK$1,402 million), reflecting the application of funds for debt repayment during the year.

Borrowings

The carrying amount of the Group's gross debt stood at HK$2,821 million at 2006 year-end, a decrease of HK$1,480 million (34.4%) from HK$4,301 million as at 31 December 2005. This reflected the Group's debt reduction utilising cash flow from operations and the application of sales proceeds of the Entertainment Building and equity investment.

Taxation

Provision for current taxation and deferred taxation increased to HK$3,574 million in 2006 (2005: HK$3,077 million). The net increase was made up of a HK$110 million charge for the year, and HK$448 million related to additional deferred tax associated with investment properties revaluation gains, reduced by tax payments of HK$61 million.

Shareholders' Funds

Shareholders' funds increased by 12.8% from HK$24,667 million in 2005 to HK$27,828 million in 2006, mainly attributable to results for the year and revaluation gains associated with investment properties and listed securities portfolios. Adjusted shareholders' funds rose from HK$27,134 million in 2005 to HK$30,729 million in 2006.

Minority Interests

The increase of HK$94 million in minority interests was attributable to increased profit contribution as well as a revaluation surplus from Lee Gardens Two.

Contingent Liabilities

As of 31 December 2006, there were no guarantees granted to external parties, since all outstanding guarantees relating to associates and investee companies were released during the year.

The Group has underwritten to its associates on cash calls to finance working capital requirements. Based on currently available information, management does not anticipate any major call for cash contributions in the foreseeable future.

Critical Accounting Estimates

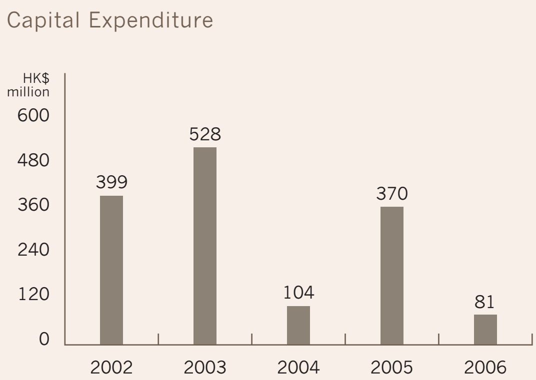
The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The most significant estimate relates to the valuation of the Group's property investments. For details, please refer to note 4 to the financial statements.

Capital Expenditure and Management

The Group is committed to enhancing the asset value of its investment properties portfolio through selective re-tenanting, refurbishment, repositioning and redevelopment.

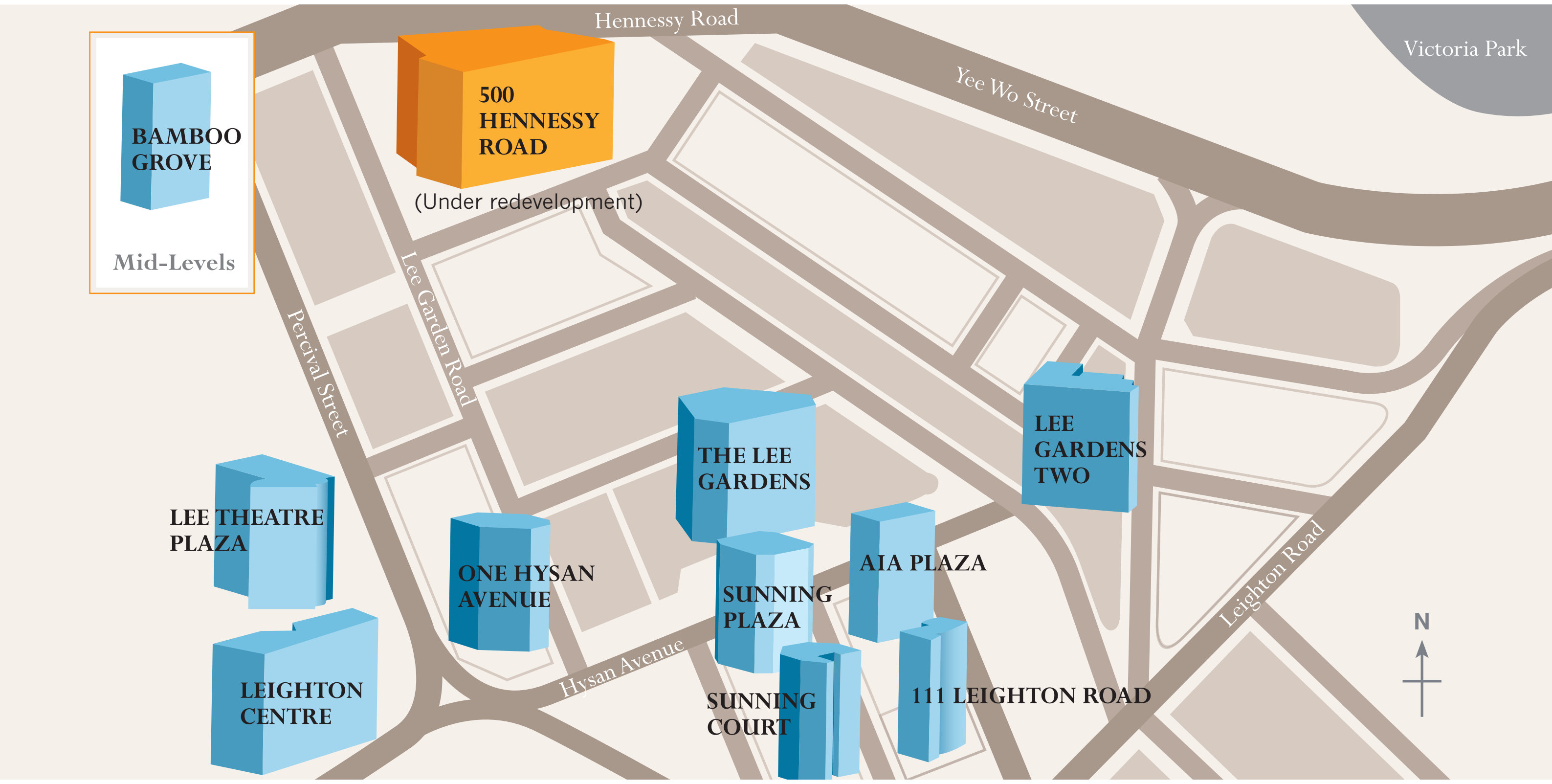
The Group also has in place a portfolio-wide whole-life cycle maintenance programme as part of its ongoing strategy to proactively review and implement maintenance activities. The redevelopment of Hennessy Centre, with demolition works commencing in the fourth quarter of 2006, is on schedule. This mixed office/retail complex has a projected gross floor area of approximately 710,000 square feet.

Total cash outlay of capital expenditure (excluding purchase of plant and equipment) during the review year was HK$81 million. The following graph illustrates capital expenditure patterns during the last five years:



The Group has an internal control system for scrutinising capital expenditure. Detailed analysis of expected risks and returns is submitted to division heads, executive Directors or the Board for consideration and approval, depending on strategic importance, cost/benefit and the size of the projects. The criteria for assessment of financial feasibility are generally based on net present value, pay back period and internal rate of return from projected cash flow.

At year end, the Group had HK$3.6 billion undrawn committed bank facilities. These facilities, together with the Medium Term Note Programme, available-for-sale investments and positive cash flows from local and overseas operations, provide adequate financial resources to fund the level of planned capital expenditure, including the Hennessy Centre redevelopment project, which the completion is expected by the end of 2009.



BAMBOO GROVE 74-86 Kennedy Road, Mid-Levels

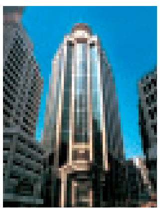
A luxury residential complex in the Mid-Levels, Bamboo Grove underwent major refurbishment in 2002 to enhance both the value and quality of the complex. The complex commands panoramic views of the harbour and the greenery of the Peak, and is well served by many different types of public transport. In addition to superb property management services and full club-house and sports facilities, tenants also enjoy personalised Resident Services that help ensure a comfortable stay.

Total Gross Floor Area:	691,546 sq.ft.	Parking Spaces:	436
Number of Units:	345	Year Completed/Renovated:	1985/2002

LEIGHTON CENTRE 77 Leighton Road, Causeway Bay

This office and retail complex enjoys close proximity to all forms of public transport. Its central location in the Causeway Bay area makes it a much sought-after location for many professional practices. Upgrading works on building facilities were completed in 2004.

Total Gross Floor Area:	435,008 sq.ft.	Parking Spaces:	264
Number of Floors:	28	Year Completed/Renovated:	1977/2004



LEE THEATRE PLAZA 99 Percival Street, Causeway Bay

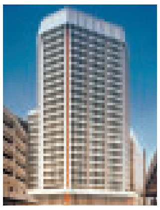
Like its predecessor, Lee Theatre, the Lee Theatre Plaza is a Hong Kong landmark, being one of the city's most popular shopping and dining complexes, and housing many of the world's most famous lifestyle brands and restaurants. The building provides access to various kinds of transport and the MTR Causeway Bay station.

Total Gross Floor Area:	317,160 sq.ft.	Year Completed:	1994
Number of Floors:	26		

500 Hennessy Road, Causeway Bay

Under redevelopment.

Estimated total Gross Floor Area:	Approx. 710,000 sq.ft.	Projected Year of Completion: End of 2009



ONE HYSAN AVENUE 1 Hysan Avenue, Causeway Bay

Located at the junction of three busy streets in the heart of Causeway Bay, this office and retail complex enjoys a prime location with a diversity of retail facilities in the surrounding area. The building underwent refurbishment of its external facade in 2002.

Total Gross Floor Area:	169,019 sq.ft.	Year Completed/Renovated:	1976/2002
Number of Floors:	26		

THE LEE GARDENS 33 Hysan Avenue, Causeway Bay

The Lee Gardens is the Group's flagship property comprising an office tower, Manulife Plaza, and a high-end shopping centre. The development, close to the MTR Causeway Bay station, enjoys spectacular views of the Harbour and Happy Valley and is home to many international corporations, luxury fashion brands and renowned restaurants.

Total Gross Floor Area:	902,797 sq.ft.	Parking Spaces:	200
Number of Floors:	53	Year Completed:	1997

LEE GARDENS TWO 28 Yun Ping Road, Causeway Bay

Lee Gardens Two is an office and retail complex. The retail podium underwent a comprehensive refurbishment in 2003 and was re-launched as Lee Gardens Two. The complex is conveniently linked to the neighbouring The Lee Gardens and is home to many international corporations, luxury fashion brands, renowned restaurants and a children's concept floor.

Total Gross Floor Area:	626,996 sq.ft.	Parking Spaces:	176
Number of Floors:	34	Year Completed/Renovated:	1992/renovation of retail podium in 2003

SUNNING PLAZA 10 Hysan Avenue, Causeway Bay

Designed by the renowned architect I.M. Pei, Sunning Plaza greets tenants and visitors with a spacious entrance and lift lobby. Among its retail tenants are popular food and beverage outlets, which have established the Plaza as a hub for relaxation and social recreation.

Total Gross Floor Area:	279,717 sq.ft.	Parking Spaces:	150 (jointly with Sunning Court)
Number of Floors:	30	Year Completed:	1982

SUNNING COURT 8 Hoi Ping Road, Causeway Bay

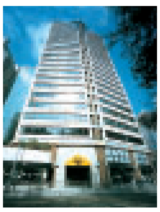
The 19-level Sunning Court is a unique residential tower in the dynamic Causeway Bay area. Located in a pleasant environment with tree-lined streets, and within easy reach of all forms of relaxation and entertainment in the surrounding district, the building provides maximum comfort for its tenants. The building underwent refurbishment of its external facade in 2003.

Total Gross Floor Area:	97,516 sq.ft.	Parking Spaces:	150 (jointly with Sunning Plaza)
Number of Units:	59	Year Completed/Renovated:	1982/2003

AIA PLAZA 18 Hysan Avenue, Causeway Bay

AIA Plaza is a 25-level office and retail complex at the corner of Hysan Avenue. The building boasts a bright and spacious lobby, and houses restaurants, specialty cafes and banking services.

Total Gross Floor Area:	139,119 sq.ft.	Year Completed:	1989
Number of Floors:	25		



111 LEIGHTON ROAD 111 Leighton Road, Causeway Bay

Located in a pleasant and quieter area in the heart of Causeway Bay, 111 Leighton Road is an ideal office location for professional and designer firms. The retail shops include a European kitchen concept store and fashion stores.

Total Gross Floor Area:	79,905 sq.ft.	Year Completed/Renovated:	1988/2004
Number of Floors:	24		