Chief Executive Officer's Report

2007 was a buoyant year for the economies and travel demand in our key markets. Operating from the strength of our brand and their well-established market positions, our hotels and other properties and businesses achieved pleasing results, with this year's profit before non-operating items of HK$1,088 million representing an increase of 20% from last year.

HSH was thus able to continue the sustained recovery which it has enjoyed since coming out of the Asian financial crisis which occurred in the late 1990s, with our EBITDA having improved consistently every year from its low of HK$698 million in 2001 to HK$1,510 million in 2007. Our balance sheet has continued to strengthen, with our gearing decreasing to 7% during the year despite the significant spend on the Peninsula Tokyo project during its final stages of construction.

Hotels

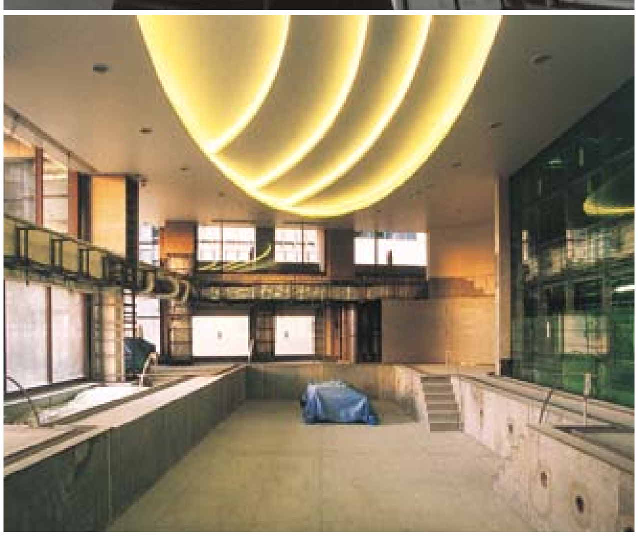
The highlight of the year for our Company was undoubtedly the opening of the new Peninsula Tokyo hotel. Situated in a most prime location in the Marunouchi business district of Tokyo, within a short walk to the heart of Ginza and overlooking the Imperial Palace and Gardens, this project was conceived, designed and constructed in partnership with Mitsubishi Estate Company. With meticulous attention to detail, no effort was spared in creating the 314 guestrooms and suites, the four different and strongly themed restaurants, the lobby, ballroom and other public areas, the dramatic swimming pool and spa and the artwork in the hotel. The philosophy of our

Group is to focus on a small number of hotel projects at any one time and thus, this was our first new hotel opening since 2001. From the reaction of hotel guests and the market generally since its soft opening in September 2007, I believe that this focus and attention to detail has paid off, with a hotel that is already proving to be a strong addition to our brand, as well as gaining worldwide recognition in its own right.

Our seven existing Peninsula Hotels generally had a strong year, continuing in their positions as being either top or amongst the leaders in room rate and revenue per available room (RevPAR) in their respective cities. In particular, The Peninsula Hong Kong had a record year in terms of RevPAR, which at HK$2,892 (US$371) represented an increase of 12% from the previous year. This, our flagship hotel, is truly standing proud as it enters its 80th anniversary year.

Elsewhere in Asia, business conditions for the year were somewhat mixed. The Peninsula Beijing faced intense competition from the large number of new luxury hotel openings ahead of the Beijing Olympics and its RevPAR increased by 9% to HK$1,048 (US$134). The Peninsula Bangkok lived through a period of relative political uncertainty in Thailand from the ousting of the former Prime Minister in October 2006 until elections were held in December 2007. In the circumstances, the hotel did well to achieve a RevPAR of HK$1,201 (US$154), up 19% from last year.

The Peninsula Manila enjoyed its first full year following the extensive renovation of the Makati Tower, lobby and ballroom, with room rates in the newly renovated rooms achieving a premium of well over 60% above the similar unrenovated rooms. The RevPAR of the hotel ended at HK$752 (US$96) for the year, an increase of 55% as compared to the previous year when it was under renovation for part of the year. Unfortunately, the hotel gained world-wide media attention in November 2007 when it was seized by anti-government rebels and the ensuing attack by government troops significantly damaged the lobby and some other areas of the hotel. Through the outstanding hard work of our staff, the hotel was re-opened for business just four days after this event, although disruption to the business of the hotel continued for a period of time.



The performance of the three Peninsula Hotels in North America has been very strong during the year. The Peninsula New York had a record year, increasing its RevPAR by 17% to HK$4,771 (US$612). The Peninsula Chicago maintained its position as the top hotel in the city and, in a relatively weak year for conventions in the city, increased its RevPAR by 8% to HK$2,638 (US$338). The Peninsula Beverly Hills continued to achieve rate increases, resulting in a RevPAR of HK$4,242 (US$544), up 12% from the previous year.

Quail Lodge, under Peninsula management since April 2006, continued to improve its service standards and offerings but still faces the challenge of filling in the off-peak periods during the year. Quail's RevPAR was up 2% to HK$1,462 (US$187).

We continue to focus on seeking projects to enhance our brand and our services, as well as to improve the return on our hotel assets. The focus on the development of our own exclusive line of Peninsula Spas continued. Following the successful openings of the new Peninsula Spas in our hotels in Hong Kong, Bangkok and Chicago, we have now started the construction of new Peninsula Spas in The Peninsula Beijing, due to be completed in May 2008 prior to the Olympics, and in The Peninsula New York, due to be completed in September 2008. At the same time, the rooftop facilities at The Peninsula New York are being renovated with a new design theme for the popular rooftop bar.

Following the successful outcome of the phase one renovation of The Peninsula Manila, which included all the guestrooms in the Makati Tower, the lobby, the ballroom and some back of house areas, we have

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decided to proceed with phase two of the renovation in 2008, which will include a renovation of all of the guestrooms in the Ayala Tower.

With generally high levels of inflation in the key economies in which we operate, it continues to be a significant challenge to manage costs while maintaining and improving the level of service provided to guests. Through our efforts to control our operating costs, the EBITDA margin on our hotel businesses, excluding the pre-opening expenses of HK$83 million and the initial operating results of the new Peninsula Tokyo, has increased from 30% last year to 32% in 2007.

The retail arcades in The Peninsula Hong Kong and The Peninsula Beijing continue to be most sought after by top level brands, achieving amongst the highest rentals per square foot in their respective cities and enjoying effective full occupancy. We have been pleased to welcome brands like Harry Winston, Chopard, Goyard, Graff and de Grisogono to our arcades. For the year, The Peninsula Hong Kong arcade achieved 96% occupancy at an average rent of HK$314 per square foot per month and The Peninsula Beijing arcade achieved 98% occupancy at an average rent of HK$95 per square foot per month.

During the year Peninsula Merchandising opened four Peninsula Boutiques in China and Japan, bringing the total number of shops to 18 around the world.

Overall, the hotel division's revenue and EBITDA for the year were HK$3,550 million and HK$991 million, an increase of 22% and 15% respectively as compared to 2006.

Non-hotel properties and operations

During the year, the market remained buoyant in Hong Kong for both residential and office lettings and this was reflected in the performance of our properties. The average occupancy at The Repulse Bay was maintained at 92% whilst the rental per square foot of the unfurnished apartments increased to HK$36 per square foot per month, as compared to HK$34 per square foot in 2006. St. John's Building maintained an occupancy of 99% at HK$25 per square foot per month.

The Repulse Bay Arcade, which is architecturally a replica of the famous old Repulse Bay Hotel, is a centre for dining and shopping in the Southside, as well as being one of Hong Kong's leading wedding venues. During the year, we have obtained the approval of the Town Planning Board to proceed with a scheme which would enlarge the retail floor area and enhance the mix of shops and restaurants of the Complex. During 2007, the Arcade was fully let at an average rental of HK$69 per square foot, although lettings will be disrupted for the expected duration of the renovation project from mid 2008 to end 2009.

2007 was the first full year of operations for The Peak Tower in Hong Kong after its extensive renovation and revitalisation which resulted in the creation of additional prime retail and restaurant spaces with superb views, as well as a lively new atrium and the spectacular Sky Terrace at the top of the Tower. The Peak Tower is now fully let at an average rent per square foot of approximately HK$56 and its total revenue for the year was HK$66 million, as compared to HK$23 million in its last full year of operations before the renovation.

"HSH was thus able to continue the sustained recovery which it has enjoyed since coming out of the Asian financial crisis which occurred in the late 1990s."

Amidst another record year for tourism in Hong Kong, patronage on the Peak Tram grew by 11% to 4.9 million passengers. To enhance this attraction for tourists, we created and opened during the year The Peak Tram Historical Gallery at the lower Peak Tram terminus.

Our other non-hotel operations, including the Thai Country Club, the Landmark office and serviced apartment complex in Vietnam, our club management operations and Tai Pan Laundry all performed positively. Booming air travel meant that we handled a record number of 1.2 million passengers at the Cathay Pacific first and business class lounges managed by us at Hong Kong International Airport.

Overall, the revenue and EBITDA from non-hotel properties and operations for the year were HK$992 million and HK$519 million, an increase of 22% and 25% respectively as compared to 2006.

Development and projects

Fundamental to the Group's business philosophy is our focus on the long-term ownership and management of a limited number of top quality hotels and other properties. We believe that by seeking prime locations and then committing significant human and financial resources to creating exceptional hotels, value will be created for our shareholders through both operating results and long-term asset value appreciation. This strategy means that we will focus our resources on a limited number of new hotel developments at any one time. The quality of the locations that we seek is exemplified by the Peninsula Tokyo and Peninsula Shanghai projects, which are both situated in exceptional prime locations.

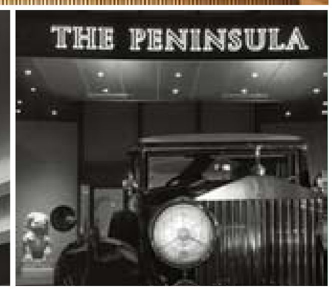
The Peninsula Shanghai will be the only new building to be constructed with a frontage onto the Bund, standing alongside the famous preserved buildings on this world-renowned promenade. The complex being developed will comprise a hotel which will include 235 rooms, five restaurants, a lobby, a ballroom, a swimming pool and spa and a 5,300 square metre high-end shopping arcade, as well as 15,600 square metres of hotel apartments.

Construction of the complex started in October 2006 and we have reached the topping-out of the 15 storey hotel tower. It is expected that topping-out of the entire complex will be achieved by June 2008. Designs of the interior spaces are well advanced and the interior fitting-out works have begun. The project is on schedule for the hotel to be completed by the summer of 2009 with a soft opening by the autumn of that year.

We continue to seek other opportunities for new hotel developments on a highly selective basis. We expect to commit to new projects on a measured basis to maintain the focus of our resources, as well as to ensure we only proceed with the most prime locations. A number of discussions are currently underway on potential projects.

Finance and results

I am pleased to report that the Company's profit before non-operating items increased by 20% to HK$1,088 million in 2007. After taking account of non-operating items, the most significant of which was the increase in fair value of investment properties (after providing for its related deferred tax and minority interest) of HK$2,710 million (2006: HK$1,189



million), the profit attributable to shareholders was HK$3,437 million, as compared to HK$2,094 million last year. The earnings per share for the year amounted to HK$2.40 (2006: HK$1.47). We have provided for shareholders' additional information a calculation of our earnings excluding non-operating items, which as set out on page 65 amounts to HK$901 million (2006: HK$761 million), representing earnings per share of HK$0.63 (2006: HK$0.54).

The net asset value attributable to shareholders of the Company has increased significantly to HK$20,726 million (2006: HK$16,982 million), equivalent to HK$14.37 per share (2006: HK$11.89 per share), mainly due to the retained earnings generated by our businesses together with the revaluation of our investment properties. Our Financial Statements continue to be prepared on the basis that our hotels are recorded at cost less depreciation and any impairment provision. It should be noted that in many cases, the current market value of these hotel properties is significantly higher than book value and we have therefore provided an up to date assessment of their market values by independent appraisers as at 31 December 2007, as set out in the Financial Review section of this Annual Report. It should also be noted that the above net asset value figures have been arrived at after making a provision of HK$2,967 million in respect of deferred taxation on the revaluation surplus on investment properties in Hong Kong, which the Directors do not believe will materialise as capital gains on such properties are not taxable in Hong Kong. In the light of the above, the Directors have provided for shareholders' additional information a calculation of our adjusted net asset value, on the basis set out in the Financial Review section of this Annual Report, which amounts to HK$27,032 million (equivalent to HK$18.75 per share).




Net borrowings had decreased to HK$1,455 million by the year-end, thus maintaining a very comfortable net gearing ratio of 7% (11% last year). The Company has significant financial capacity to seek and pursue further new developments and asset enhancement projects.

Total capital expenditure during 2007, including investment into The Peninsula Tokyo project, amounted to HK$808 million, as compared to cash generated from operations of HK$1,616 million. Our net cash inflow for the year after payment of interest and dividends and before financing activities was HK$683 million.

The Directors are recommending to shareholders a final dividend for the year of 12 HK cents per share. Together with the interim dividend of 6 HK cents per share already paid, the total dividend for the year will be 18 HK cents per share, an increase of 13% over last year. Shareholders will continue to have the option to receive their dividends in either scrip or cash.

Strategy and outlook

We are truly a long-term looking business. Our philosophy is to seek assets of the highest quality, whether through green field development or renovation of existing buildings, and to operate them to the highest possible service quality levels. Returns to the Company and its shareholders are generated through the operating results achieved from the ability to charge premium room rates and prices in many of our locations, coupled with longer term asset value appreciation.

"It is worth remembering that our approach to handling any downturn is to look long-term and value the long-term relationship we have with our staff."

Within the overall philosophy set out above, our business strategy has remained largely unchanged during my tenure over the past few years. Once again I am able to confirm that our emphasis continues to be on enhancing our brand quality and image, improving service delivery through staff training, development and empowerment, seeking new hotel and hotel-related developments which are in the best locations and then designing and building those properties to a high quality standard, and continual enhancement of the value and functionality of all space within our existing assets.

In line with the above strategy, we have successfully opened the new Peninsula Tokyo, we are progressing on schedule with The Peninsula Shanghai project and we have been actively seeking other new hotel projects on a selective basis. Our efforts to enhance and improve the value of our existing assets have continued with many renovation and refurbishment projects which have either been completed or are underway.

The biggest operating challenge currently facing us is that our operating costs continue to rise, with continuing inflation and particularly wage and energy cost increases in our main business locations over the past few years. Whilst present business momentum continues to be positive, the outlook for our revenues has been clouded by the current uncertainties in the world economies and financial markets following the sub-prime crisis in the US. Amidst such uncertainties, it is worth remembering that our approach to handling any downturn that may result is for management to react quickly but always to look long-term and value the long-term relationship that we have with our staff.

Looking at the immediate business prospects of our operations, it appears that the hotel business in the US, particularly from the corporate sector, is showing signs of being negatively affected by the uncertainties in the economy and the financial markets. Such a slow down would inevitably also affect our Asian businesses, although presently demand is still good in Hong Kong both for the hotel and for residential lettings where demand mainly comes from the multi-national corporate sector. We are hoping that Thailand will remain stable after the recent elections and that our business in the Philippines will recover after the incursion by the rebels. In Beijing, we are gearing up for the Olympics in the summer but are concerned about possible over-supply of luxury hotels thereafter, resulting from the many new recent openings in anticipation of the Olympics.

Ultimately, the biggest protection we have against the ups and downs of the businesses we operate in is our genuine commitment to the long-term, through investing in our assets and our people and in adhering to the beliefs and values which have been proven through the long history of our Company. At the core of this is our commitment to our staff and it is once again fitting that I should end this message with my thanks and tribute to all the members of the Peninsula 'family' who have worked so hard, with flair as well as loyalty, to achieve these pleasing results.

Clement K.M. Kwok
19 March 2008