

Chairman's Statement

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Canning Fok Kin-ning
Chairman



The Group reported solid operating results for 2008 from both its Hong Kong and international operations. In 2008, our shareholders have benefited from the Group's strong financial position and conservative investment profile with the Company's shares being one of the best performing shares in the Hang Seng Index for 2008.

The year 2008 was the last year under the previous 15-year Scheme of Control Agreement (SCA) under which The Hongkong Electric Co., Ltd. (HEC) operated. As reported last year, a new SCA was signed with the Hong Kong Government for ten years commencing 1st January 2009 at the lower rate of permitted return on average net fixed assets of 9.99%. The Government has an option to extend the SCA for a further term of five years. Shareholders will benefit over the next ten years from the certainty and stability of a long term regulatory framework for HEC that the new SCA provides; however, the lower rate of permitted return will impact the level of HEC's earnings.

We have sought to increase the proportion of the Group's earnings derived from its activities outside Hong Kong and good progress was made in this regard in 2008. In July 2008, we acquired a 50% interest in the Wellington electricity distribution network in New Zealand. In November 2008 we increased our interest in Northern Gas Networks in the United Kingdom (U.K.) from 19.9% to 35.1%. The increased interest has allowed us to increase our investment in one of our existing businesses which has performed well at a valuation that met our investment return parameters. A significant step was taken in February 2009 when we announced that we had agreed to purchase 45% equity interests in three joint ventures owning power plants in China, two of which are located in Zhuhai in Guangdong province adjacent to Hong Kong. The transaction, upon completion, will allow us to take a strategic stake in the electricity generation business in China at an attractive return and will enhance the earnings from the Group's international operations. Shareholders approved the acquisition of the power station interests at an extraordinary general meeting held on 16th March 2009.

Results

The Group's audited consolidated net profit after tax for the year ended 31st December 2008 was HK\$8,029 million (2007:HK\$7,448 million), an increase of 7.8%. Earnings from the Group's Hong Kong operations were HK\$7,008 million (2007:HK\$6,727 million). Higher HEC sales revenue, lower depreciation due to extension of useful lives of certain categories of fixed assets and a deferred tax adjustment due to a change in the Hong Kong profits tax rate contributed to the higher earnings from the Group's Hong Kong operations. Earnings from the Group's international operations were HK\$1,021 million (2007:HK\$721 million). The higher international operations earnings in 2008 were primarily due to the inclusion of earnings from the Thai power plant business which commenced full operations in June 2008 and from the Canadian and New Zealand businesses.

Final Dividend

The Directors will recommend a final dividend of HK\$1.49 per share, payable on 15th May 2009 to those persons registered as shareholders on 14th May 2009. This, together with the interim dividend of HK\$0.62 per share, will give a total dividend of HK\$2.11 per share for the year (2007: HK\$2.01 per share).

Hong Kong Operations

Unit sales of electricity for 2008 were 0.2% lower than that for 2007. The lower unit sales were primarily due to the wetter and cooler summer in 2008 and to the effect of various energy saving initiatives. The number of domestic customers in 2008 recorded a slight increase and the number of commercial customers a slight decrease while the number of industrial sector customers continued their declining trend. Maximum Demand in 2008 was 2,589 MW compared with 2,552 MW in 2007.

During 2008, the Lamma Power Station's coal-fired units generated approximately 83% of the electricity sent out while the gas-fired units generated approximately 17%. Both the coal-fired and gas-fired generating plants at Lamma performed satisfactorily in 2008 with no significant operational issues.

Lamma Winds, the 800 kW wind turbine on Lamma Island with its associated exhibition centre on renewable energy continued to attract public interest in renewable energy.

High coal prices continued to put pressure on fuel costs in 2008. Coal costs moderated somewhat toward the end of 2008 and into 2009 though they still remain high by historic standards. In order to mitigate in part the impact of higher coal costs we continued to source and use a variety of coal during the year.

Our emission reduction programme at the Lamma Power Station progressed well during 2008. Civil construction work is progressing on schedule for the flue gas desulphurisation (FGD) plant and low nitrogen oxide system retrofit works for the coal-fired Units 4 and 5. Engineering design has been substantially completed and construction work commenced for the coal-fired Unit 2 FGD retrofit work. Conversion of GT57 from an oil-fired combined cycle unit to a gas-fired unit has been completed and the unit commissioned. By the end of 2010, it is expected that over 95% of the electricity generated at the Lamma Power Station will be generated by gas and by coal-fired units fitted with FGDs and low nitrogen oxide burners resulting in lower emission levels.

In December, the Hong Kong Government approved HEC's Development Plan for the period 2009-2013 which provided for HK\$12.3 billion in capital expenditure over that period. This investment will be focused on additions

to and maintaining the reliability of our transmission and distribution network and in furthering our emission reduction programme at the Lamma Power Station. We are continuing with our evaluation work for a 100 MW offshore wind farm with detailed environmental impact assessment studies in progress.

Supply reliability was maintained at over 99.999% in 2008 surpassing our pledged customer service standards. This world class supply reliability has been consistently maintained since 1997. Supply reliability was supported by the improvement and maintenance work carried out on the transmission and distribution network in 2008.

During 2008, we continued with our participation in environmental and community activities. A total of 70 visits from professional institutes and schools to the Lamma Power Station and Lamma Winds were organised in 2008. The HK Electric Clean Energy Fund continued its efforts in 2008 in promoting renewable energy. The HK Electric Volunteers which now has a membership of over 840 employees focuses its activities on care for the elderly and those in the community in need. During 2008, the volunteers undertook 68 service activities with a total of over 3,800 service hours. The HK Electric Centenary Trust continued to provide scholarships for secondary students and funding for self learning centres for senior citizens. The trust also funds the U3A (University of 3rd Age) network which now includes 19 social services agencies. U3A courses promote lifelong learning and volunteerism among the retired.

International Operations

In Thailand, construction of the 1,400 MW gas-fired Ratchaburi Power Station was completed in 2008 with the first unit being commissioned in March and the second unit in June. Electricity generated is sold to the Electricity Generating Authority of Thailand under a long term power purchase agreement. The power plant has achieved an availability factor of over 90% since commissioning.

In Canada, the Group benefited from the first full year of operations of Stanley Power Inc. Stanley Power Inc. has interests in six power plants, five of which are gas-fired and one coal-fired. Higher gross margins were recorded in 2008.

In the U.K., Northern Gas Networks (NGN) which operates a gas distribution network in the north of England recorded results ahead of those for the previous year. NGN has been benchmarked by its regulator as the most efficient network in the U.K. gas industry.

In New Zealand, the Group benefited from six months of operations from its interest in the Wellington electricity distribution network which was acquired in July 2008. The network serves the Wellington, Porirua and Hutt Valley regions.

In Australia, both ETSA in South Australia and Powercor and CitiPower in Victoria performed satisfactorily with both businesses recording a strong financial performance with higher distribution revenue. Customer service and reliability targets for 2008 were exceeded.

In mainland China, construction of the 48 MW wind farm in Dali, Yunnan province was completed in December and began full commercial operation in January 2009. Construction work for the 49.5 MW wind farm in Leting, Hebei province is substantially complete and commissioning is underway.

Outlook

The year 2009 is expected to be a challenging year with the impact of the current worldwide economic and financial uncertainty continuing to be felt. However, with its strong financial position and conservative investment profile the Group is well placed to face this uncertain operating environment. In Hong Kong, HEC will continue with its focus on the environment through its emission reduction programmes. Internationally, we will continue to look for new investment opportunities.

I would like to thank the directors for their continued support during the year and the management and staff for their loyalty and hard work in 2008.

Canning Fok Kin-ning

Chairman
Hong Kong, 17th March 2009