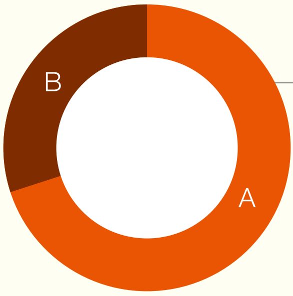
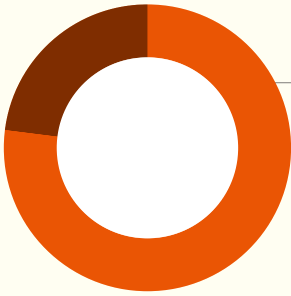
Financial Review





Capital Expenditure, Liquidity and Financial Resources

Capital expenditure during the year amounted to HK$2,084 million (2007 : HK$1,747 million), which was primarily funded by cash from operations. Total external borrowings outstanding at the year end were HK$10,667 million (31st December 2007 : HK$13,495 million), comprising unsecured bank loans and debt securities in issue. In addition, the Group had undrawn committed bank facilities of HK$7,450 million (31st December 2007 : HK$7,145 million) and bank deposits and cash of HK$8,962 million (31st December 2007 : HK$12,180 million).

Treasury Policies, Financing Activities and Capital Structure

The Group manages its financial risks in accordance with guidelines laid down in its treasury policy, which is approved by the Board. The treasury policy is designed to manage the Group's currency, interest rate and counterparty risks. The Group aims to ensure that adequate financial resources are available for refinancing and business growth.

The Group's financial profile remained strong during the year. Standard and Poor's affirmed the A+ long term credit ratings of Hongkong Electric Holdings Limited and The Hongkong Electric Company, Limited with a stable outlook in December 2008. As at 31st December 2008, the net debt of the Group was HK$1,705 million (31st December 2007 : HK$1,315 million) with a net debt-to-equity ratio of 4% (31st December 2007 : 3%).

The profile of the Group's external borrowings, after taking into account of interest rate swaps was as follows:-

(1) 70% was in Hong Kong dollars and 30% in Australian dollars;

(2) 77% was bank loans and 23% was capital market instruments;

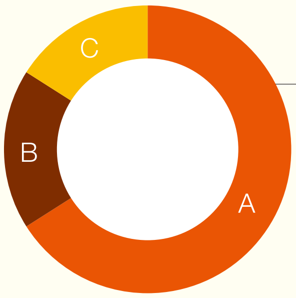
(3) 16% was repayable within 1 year, 66% was repayable between 2 and 5 years and 18% was repayable beyond 5 years;

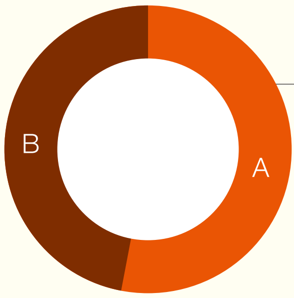
(4) 53% was at fixed rate and 47% was at floating rate.

Currency and interest rate risks are actively managed in accordance with the Group's treasury policy. Derivative financial instruments are used primarily for managing interest rate and foreign currency risks and not for speculative purposes. Treasury transactions are only executed with counterparties with acceptable credit ratings to control credit risk exposure.

The Group's policy is to maintain a portion of its debt at fixed interest rates. Interest rate risk is managed by either securing fixed or floating rate borrowings or by using interest rate derivatives. As at 31st December 2008, 53% of the Group's total borrowings were at fixed rates.

The Group's principal foreign currency exposures arise from its overseas investments and from the import of fuel and capital equipment. Foreign currency transaction exposure is managed mainly through forward contracts. As at 31st December 2008, over 95% of the Group's





transaction exposure was either denominated in US dollars or hedged into Hong Kong or US dollars. Where considered appropriate, currency exposure arising from overseas investments is mitigated by financing those investments in local currency borrowings. Foreign currency fluctuations will affect the translated value of the net assets of overseas investments and the resultant translation difference is included in the Group's reserve account. Income received from the Group's overseas investment which is not denominated in Hong Kong dollars is unless otherwise determined converted into Hong Kong dollars on receipt.

The contractual notional amounts of derivative financial instruments outstanding at 31st December 2008 amounted to HK$7,763 million (31st December 2007 : HK$9,576 million).

Charges on Group Assets

The shares of an associate were pledged as part of the security arrangements for project financing facilities for that associate. The carrying value of the associate as at 31st December 2008 was HK$552 million (31st December 2007 : HK$281 million).

Contingent Liabilities

As at 31st December 2008, the Group had given guarantees and indemnities totalling HK$1,262 million (31st December 2007 : HK$2,702 million).

The Company had given guarantees and indemnities in respect of bank and other borrowing facilities made available to and financial commitments of subsidiaries totalling HK$3,217 million (2007 : HK$5,286 million). Out of this amount, HK$3,207 million (2007 : HK$5,156 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, Hongkong Electric, has given guarantees to third parties in respect of the value of leased equipment of HK$210 million (2007 : HK$210 million) at the expiry of the lease.

Employees

The Group continues its policy of pay for performance and market pay levels are monitored to ensure competitiveness is maintained. The Group's total remuneration costs for the year ended 31st December 2008, excluding directors' emoluments, amounted to HK$877 million (2007 : HK$843 million). As at 31st December 2008, the Group employed 1,864 permanent staff (2007 : 1,879). No share option scheme is in operation.

Apart from well-established training schemes for university graduates, trainee technicians and apprentices, the Group provides training for employees in management and functional skills, language skills, computer knowledge and technology relevant to the Group's industry by both classroom training and e-learning platforms. Job-related programmes to develop and enhance the general skills and knowledge of employees are also provided.