

# RISK FACTORS

Risks and uncertainties can affect the Group's businesses, financial conditions, operational results or growth prospects leading to a divergence from expected or historical results. Key risk factors affecting the Group are outlined below. In dealing with these risk factors, the Group remains in touch with our stakeholders with the aim of understanding and addressing their concerns.

These factors are not exhaustive or comprehensive, and there may be other risks in addition to those shown below which are not known to the Group or which may not be material now but could become material in the future.

## Global and Hong Kong Economic Environment

The global economic recovery has been weaker than expected with uneven recovery in advanced economies. In Hong Kong, the economy has slowed down as a result of a decline in tourist spending and modest growth in domestic demand.

The prevailing global uncertainty may materially and adversely affect the business of customers or potential customers, or cause a slowdown in economic activity in Hong Kong, which, in turn, may lead to a lower demand for electricity and related services in Hong Kong. This may adversely affect the Group's financial position, potential income, asset value and liabilities.

To address uncertainty in global and Hong Kong economies, the Group pursues prudent and pragmatic strategies in financial management and capital expenditure investment. The Group also strives for efficiency and cost effectiveness in all aspects of its operations to enhance financial performance.

## Currency Markets and Interest Rates

The Group's currency exposure mainly arises from the import of fuel and capital equipment, and from its debt issuances in capital markets.

The Group is also exposed to interest rate risk on its interest-bearing assets and liabilities. The Group's treasury policy guides the measures it undertakes to manage this exposure. Details of the Group's current practices to manage currency and interest rate risks are in the Financial Review on pages 48 to 50.

## Regulation, Government Policy and Market Reform

The operations of the Group's electricity business in Hong Kong are subject to a Scheme of Control Agreement (SCA) with the Government, which provides for a permitted level of earnings based principally on average net fixed assets for electricity generation, transmission and distribution.

The current SCA was renewed in 2008 for a term of ten years commencing 1 January 2009 with an option for the Government to extend it for a further term of five years. The implementation of the 2014-2018 Development Plan, the extension of SCA beyond 2018, the structure and regulation of the power industry in Hong Kong, and the Government's policies on air quality and fuel mix for the medium to long term (including possible direct import of electricity from southern China) are all factors affecting the Group's results and growth. The Group has established a mechanism to review these factors on a regular basis and proactively engages with various stakeholders, including the Government, on electricity market and regulatory issues.

## Health and Safety

The nature of the Group's operations exposes it to a range of significant health and safety risks.

An accident or the outbreak of a communicable disease resulting in fatalities or injuries to members of the public or to employees could have significant consequences. These may include widespread distress and harm or significant disruption to the Group's operations, and could result in regulatory action, legal liability, material costs and damage to the Group's reputation.

The Group has in place Health and Safety Management Systems to manage its exposure and protect its employees, customers, contractors and the public by conducting its business in a safe and socially responsible manner.



## Reliability of Supply

The Group can be exposed to supply interruptions. A severe earthquake, storm, lightning, flood, landslide, fire, sabotage, terrorist attack, failure of critical information and control systems that support the power system, or any other unplanned event could lead to a prolonged and extensive power outage.

The loss of cash flow resulting from such interruption, and the cost of recovery from network damage could be considerable. Such an incident could damage customer goodwill and lead to claims and litigation. Substantial increases in the number or duration of supply interruptions could result in increases in the costs associated with the operation of the Group's supply networks, which could have an adverse effect on the businesses, financial conditions and results of operations as well as the reputation of the Group.

The Group conducts regular maintenance and upgrades of its power supply equipment, undertakes reliability reviews, provides comprehensive training to operational staff and operates with sophisticated information technology control and asset management systems. It also has fully tested contingency plans to ensure supply reliability standards are maintained.

## Fuel Supply

Our generating units in Lamma Power Station mainly rely on coal and natural gas as a fuel source. Any interruptions or shortages in the supply of coal or natural gas or substandard fuel quality may result in significant disruption to the operations of our generating units. This could have an adverse effect on the reliability of supply, businesses, financial conditions as well as the reputation of the Group.

The Group has a fuel supply strategy and fuel quality control system in place to maintain sufficient reliable supplies and quality stock to meet its generation requirements.

## Environmental Regulations

In 2008, the Government stipulated the emission allowances for the power sector for 2010 and beyond through the Technical Memorandum for Allocation of Emission Allowances in respect of Specified Licences under the Air Pollution Control Ordinance. Subsequently, three more Technical Memoranda issued in 2010, 2012 and 2014 have further tightened the emission allowances starting from 2015, 2017 and 2019 respectively. The Government will also review emission allowances for 2020 and beyond when there is a policy decision from an earlier public consultation on the future fuel mix for electricity generation for Hong Kong.

In addition, the Government currently links the rate of return to the compliance with the emission allowance requirements. Failure to comply with these emission allowance requirements could result in financial penalties and other legal actions against the Group.

The Group has Environmental Management Systems and a dedicated team to ensure compliance with relevant environmental regulations and to formulate action plans in various aspects to closely monitor and control the emissions from the power plant.

