About This Section

In this section of the Annual Report, we summarise the basis of preparation of the Group's financial statements and set out other information (such as non-accounting performance indicators and off-balance sheet information) that are considered useful for users to assess the financial performance and financial position of the Group.

Target Readers

This section is written primarily for institutional investors, shareholders, bankers and other stakeholders who are interested in doing business with us.

Non-accounting performance indicators

In addition to accounting information, the Group also discloses non-accounting performance indicators to help readers understand the key drivers of our operating results.

Examples of key non-accounting performance indicators relevant to the Group's hotel business include:

Average Room Rate (HK$)

$$\frac{\text{Total rooms revenue}}{\text{Rooms occupied}}$$

Rooms Revenue per Available Room ("RevPAR") (HK$)

$$\frac{\text{Total rooms revenue}}{\text{Rooms available}}$$

Occupancy Rate

$$\frac{\text{Rooms occupied}}{\text{Rooms available}} \times 100\%$$

Financial Statements and their Key Components

The objective of the Financial Statements is to set out the historic financial performance and financial position of the Group. The key components of the Financial Statements are the income statement, the statement of financial position and the statement of cash flows, all of which are inter-related. The information presented in the income statement, the statement of financial position and the statement of cash flows is described separately in this Financial Review. The Group's summarised Financial Statements are set out in the Financial Review Summary on pages 32 and 33.

Basis of Preparation of the Financial Statements

The Group's Financial Statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRS"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards and interpretations. HKFRS are issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") designed for general purpose financial statements. Whilst certain management judgements may be applied when preparing the Financial Statements, the Group is obliged to follow the framework of HKFRS and a set of prescriptive standards under the HKFRS to measure, recognise and record its transactions; and to present and disclose the resultant accounting effects in its Financial Statements without any departures.

During 2012, the HKICPA has issued several amendments ("Revised HKFRS"). The Group has adopted all Revised HKFRS which are effective for the year ended 31 December 2012 and the adoption of the same has not resulted in any significant impact on the Group's results of operations and financial position.

Non-accounting Performance Indicators and Operational Statistics

To enable users of the Financial Statements to assess the Group's operating performance in a more comprehensive manner, operating and non-accounting financial performance indicators are included in this Financial Review to supplement the information presented in the Financial Statements.
A summary of the key operational statistics of the Group's individual hotels and commercial properties is set out in the Ten Year Operating Summary on pages 143 to 145.

The Group's Adjusted Net Asset Value

For the purpose of financial statements presentation, the Group has selected the cost model instead of fair value model under HKFRS as its accounting policy to account for its hotels (other than shopping arcades and offices within the hotels) and golf courses. Under the cost model, hotels and golf courses are measured at depreciated cost less accumulated impairment losses, if any. The fair value model has not been selected in order to avoid the inclusion of unnecessary short term fair value movements in respect of hotels and golf courses in the income statement, which are considered irrelevant to the underlying economic performance of the hotel and golf course operations. However, in order to provide users of the Financial Statements with additional information on the value of the Group's net assets, the Directors have commissioned an independent third party fair market valuation of the Group's hotels and golf courses as at 31 December 2012, the details of which are set out on page 51. If these assets were to be stated at fair market value instead of at cost less depreciation and any provision for impairment, the Group's net assets attributable to shareholders would increase by HK$3,246 million or 10% from the reported net assets attributable to shareholders of HK$33,144 million.

In the light of the above, the Directors have provided the users of the Financial Statements with a calculation of the Group's adjusted net asset value as at 31 December 2012 on the basis set out below.

HK$m		**2012**		2011
Net assets attributable to shareholders per audited statement of financial postion		**33,144**		31,455
Adjusting the value of hotels and golf courses to fair market value	**3,619**		3,641	
Less: Related deferred tax and non-controlling interests	**(373)**		(393)	
		3,246		3,248
Adjusted net assets attributable to shareholders		**36,390**		34,703
Audited net assets per share (HK$)		**22.07**		21.11
Adjusted net assets per share (HK$)		**24.23**		23.29

Adjusted NAV

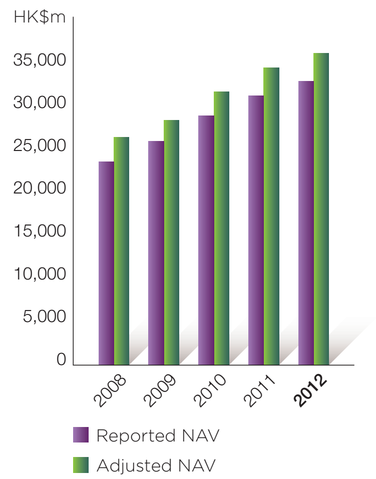
+4%

HK$24.23
for 2011 (HK$23.29)

The net asset value ("NAV") per book is not a fair representation of the Group's underlying value as its hotels and golf courses are stated at cost less depreciation rather than their fair value. In order to provide users of the Financial Statements with additional information on the Group's net assets, the Group presents adjusted NAV by adjusting its hotels and golf courses to fair market value based on the valuation conducted by independent third party valuers.

The following chart summarises the movement of the Group's adjusted NAV over the last five years.

NAV



Underlying EPS

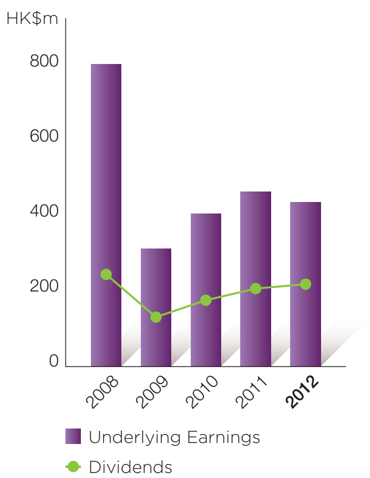
-6%

HK$0.29
for 2011 (HK$0.31)

In order to provide additional insight into the performance of its business operations, the Group presents underlying earnings by excluding non-operating and non-recurring items that are considered irrelevant to the underlying operating performance of the Group.

The following chart summarises the Group's underlying earnings for 2008–2012.

Underlying Earnings



The Group's Underlying Earnings

The Group's operating results are mainly derived from the operation of hotels and letting of commercial properties. However, to comply with HKFRS, the Group is required to include non-operating and non-recurring items, such as any changes in fair value of investment properties and impairment provision adjustments for certain assets, in its income statement. As the Group continues to be managed with principal reference to its underlying operating cash flows and recurring earnings, the Directors have provided for the users of its Financial Statements calculations of the Group's underlying profit attributable to shareholders and underlying earnings per share, which are determined by excluding the post-tax effects of the property revaluation movements and other non-operating items, as set out below.

The decrease in the Group's underlying earnings was mainly due to the renovations at The Peninsula Hong Kong and the de Ricou serviced apartment tower at The Repulse Bay which started in January 2012 and February 2012 respectively. Further details of the financial impacts of the renovations of these two key assets on the Group's results are set out on pages 39 and 43.

HK$m	**2012**	2011	2012 vs 2011
Profit attributable to shareholders	**1,555**	2,259	(31%)
Increase in fair value of investment properties	**(1,073)**	(1,841)	
Provision for impairment losses	**–**	20	
Share of property revaluation loss of The Peninsula Shanghai, net of tax	**14**	–	
Gain on disposal of Inncom International, Inc., an unlisted equity investment	**(46)**	–	
Tax and non-controlling interests attributable to non-operating items	**(11)**	26	
Underlying profit attributable to shareholders	**439**	464	(5%)
Underlying earnings per share (HK$)	**0.29**	0.31	(6%)

Income statement analyses the Group's financial performance for the year, showing profitability and comparatives.

Income Statement

The company is an investment holding company, whilst its subsidiary companies, associated companies and jointly controlled entity are engaged in the ownership, management and operation of hotels, commercial properties and clubs and services.

The Group's summary results for the year ended are set out in the table on the next page and its consolidated income statement is set out on page 148.

A detailed discussion of the performance of the Group is set out on pages 37 to 50 of this Financial Review.

HK$m	2012	2011	2012 vs 2011
Turnover	**5,178**	5,009	3%
Operating costs	**(3,977)**	(3,798)	5%
EBITDA	**1,201**	1,211	(1%)
Depreciation	**(384)**	(377)	2%
Net financing charges	**(85)**	(88)	(3%)
Share of results of The Peninsula Shanghai	**(125)**	(85)	47%
Non-operating items	**1,119**	1,821	(39%)
Taxation	**(170)**	(203)	(16%)
Profit for the year	**1,556**	2,279	(32%)
Non-controlling interests	**(1)**	(20)	(95%)
Profit attributable to shareholders	**1,555**	2,259	(31%)

Turnover
HK$5,178m +3%

Hotels
HK$3,885m +3%

Commercial Properties
HK$733m -1%

Clubs & Services
HK$560m +12%

Turnover represents the gross amount invoiced for services, goods and facilities including management fees and rental income.

The turnover by activity of the Group for 2008-2012 are presented in the chart below.

Turnover

The Group's turnover in 2012 was HK$169 million or 3% above 2011.

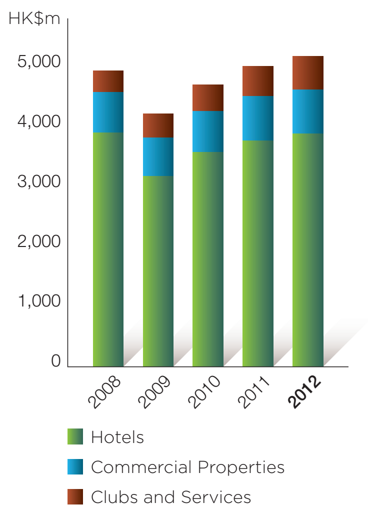
The Hotels Division is the main contributor to the Group's revenue, accounting for 75% of the total revenue. Despite the renovations of the guestrooms and The Verandah restaurant at The Peninsula Hong Kong which negatively impacted the hotel's business operation, the Hotels Division achieved a revenue growth of 3% in 2012.

For the Commercial Properties Division, although the residential leasing market in Hong Kong remained strong in 2012, the Division recorded a decline in revenue by 1% due to the closure of the de Ricou tower at The Repulse Bay for major renovation.

For the Clubs and Services Division, the 12% revenue growth was principally attributable to the increased business achieved by Peninsula Merchandising.

The table on the next page sets out the breakdown of consolidated revenues by business segment and by geographical segment.

Turnover by Activity



Consolidated revenue by business segment HK$m	2012		2011		2012 vs 2011
Hotels					
Rooms	**1,637**	**32%**	1,642	33%	(0%)
Food and beverage	**1,232**	**24%**	1,175	23%	5%
Commercial	**639**	**12%**	597	12%	7%
Others	**377**	**7%**	352	7%	7%
Total hotel revenue	**3,885**	**75%**	3,766	75%	3%
Commercial Properties	**733**	**14%**	743	15%	(1%)
Clubs and Services	**560**	**11%**	500	10%	12%
	5,178	**100%**	5,009	100%	3%

Consolidated revenue by geographical location HK$m	2012		2011		2012 vs 2011
Arising in					
Hong Kong	**2,224**	**43%**	2,314	46%	(4%)
Other Asia	**1,864**	**36%**	1,650	33%	13%
United States of America	**1,090**	**21%**	1,045	21%	4%
	5,178	**100%**	5,009	100%	3%

The portfolio of the Group's Hotels Division comprises The Peninsula hotels in Hong Kong, Shanghai, Beijing, New York, Chicago, Beverley Hills, Tokyo, Bangkok, Manila and Paris (under construction).

With the exception of The Peninsula Hong Kong, which was affected by the renovation, all Peninsula hotels achieved revenue growth over 2011.

Hotels Division

Revenue from our Hotels Division was negatively impacted by the guestroom renovation at The Peninsula Hong Kong. Nevertheless, the Hotels Division generated a total revenue of HK$3,885 million, representing an increase of HK$119 million (3%) over 2011, with revenue growth at all hotels except The Peninsula Hong Kong.

The RevPAR for all our hotels, apart from The Peninsula Shanghai, increased by up to 25% in 2012 as compared with 2011, with the biggest increases being in the Peninsula hotels in Tokyo, Hong Kong and Bangkok. The increased RevPAR resulted predominantly from higher occupancy apart from The Peninsula Hong Kong, where the increase was mostly due to the higher average room rate. In other locations, the growth in average room rate was limited due to keen competition in these markets.

Set out below is a breakdown of revenue by hotels:

HK$m	2012 Rooms	2012 F&B	2012 Commercial	2012 Others	2012 Total	2011 Rooms	2011 F&B	2011 Commercial	2011 Others	2011 Total	2012 vs 2011
Consolidated hotels											
The Peninsula Hong Kong	231	321	421	52	1,025	366	336	393	61	1,156	(11%)
The Peninsula Bejing	166	84	148	19	417	159	75	133	19	386	8%
The Peninsula New York	367	117	34	48	566	363	109	34	46	552	3%
The Peninsula Chicago	254	157	–	58	469	236	152	–	58	446	5%
The Peninsula Tokyo	344	348	31	91	814	275	323	31	70	699	16%
The Peninsula Bangkok	119	84	3	19	225	101	72	3	17	193	17%
The Peninsula Manila	156	121	2	23	302	142	108	3	20	273	11%
Management fees income	–	–	–	67	67	–	–	–	61	61	10%
	1,637	1,232	639	377	3,885	1,642	1,175	597	352	3,766	3%
Non-consolidated hotels											
The Peninsula Shanghai	184	173	103	32	492	188	160	83	30	461	7%
The Peninsula Beverly Hills	323	105	3	50	481	284	94	2	41	421	14%
	507	278	106	82	973	472	254	85	71	882	10%

The Peninsula Hong Kong: Total revenue was HK$131 million (11%) lower than 2011, being impacted by the renovation works which resulted in a significant portion of the room inventory being unavailable for sale during the year. The first phase of the renovation for 135 rooms commenced in January 2012 and was completed in September 2012. The second phase for the 165 rooms in the Original Building began in September 2012 and is scheduled for completion in mid 2013. In addition, The Verandah restaurant and The Bar were closed for renovation for two and a half months during the year, while a new Conference Centre and Wedding Salon have been added in place of offices on the 6th floor of the hotel.

The room rate for the renovated rooms has surpassed expectations, resulting in the hotel achieving a record average rate in the market. The hotel's RevPAR in 2012 was 22% higher than 2011 (based on the reduced room inventory), with higher occupancy and a 14% higher average room rate. Corporate business from the United States of America showed strong signs of recovery and the hotel's top three markets remained Japan, mainland China and the United States of America. Food and beverage business volumes were impacted by the partial closures of guestrooms and The Verandah for renovation; however, the average spending increased over 2011.

Rental income from the Peninsula Arcade increased by 8% over 2011. The Arcade continues to be fully let and there has been a 7% increase in the average rent. The high quality tenant mix was further enhanced by the refurbishment of prominent store fronts. Office revenue was 2% higher than 2011 despite the conversion of the 6th floor into a Conference Centre and Wedding Salon.

The Peninsula Hong Kong

Revenue HK$1,025m -11%

Occupancy +5pp

Average Room Rate +14%

RevPAR +22%

There was 11% ($131m) less Complex revenue as a result of 21% ($159m) less hotel revenue; but increased by 7% ($28m) commercial revenue.

Occupancy and RevPAR during renovation are based on the number rooms not being renovated, which amounted to 52% of the room inventory in 2012. The higher rate was mostly achieved from the renovated room product.

The Peninsula Beijing

Revenue HK$417m	+8%
Occupancy	+4pp
Average Room Rate	-3%
RevPAR	+4%

The Peninsula Beijing: Total revenue was HK$31 million (8%) above 2011, with higher occupancy, food and beverage revenue and increased Arcade revenue. The competition amongst luxury hotels in Beijing remains intense resulting in limited opportunity for room rate growth. The hotel achieved improved occupancy from 49% in 2011 to 53% in 2012, though at a lower average room rate, resulting in RevPAR being 4% higher than 2011.

The Arcade remains fully let. The Arcade occupancy reflects an increase from 92% in 2011 to 99% in 2012 because there was preparation work for various tenant movements in the first half of 2011. One of the anchor tenants in the Arcade has completed the remodelling of its store into a three-storey flagship boutique. Meanwhile, another anchor tenant is also constructing a triplex store. The completion of these flagship stores will help to further enhance the pre-eminent status of The Peninsula Arcade in mainland China.

The Peninsula New York

Revenue HK$566m	+3%
Occupancy	+2pp
Average Room Rate	-1%
RevPAR	+1%

The Peninsula New York: Total revenue was HK$14 million (3%) higher than 2011, with slightly higher revenue throughout the hotel. Room revenue was higher than 2011 due to higher occupancy, despite the lower average room rate. The reduction in Group business, especially from the Middle East, was replaced by transient growth, primarily from on-line travel agents, wholesalers and consortia. There was a noticeable return of business from the key feeder markets of France, Germany and the UK.

The hotel's two-year guestroom renovation programme was completed in September 2012 with the reintroduction of the Peninsula Suite. The new Sun Terrace offers guests an outdoor dining opportunity with Central Park views and is also well utilized for private events.

The Peninsula Chicago

Revenue HK$469m	+5%
Occupancy	+3pp
Average Room Rate	+2%
RevPAR	+7%

The Peninsula Chicago: Total revenue was HK$23 million (5%) above 2011, with improved revenue across all areas. The hotel relies almost entirely on domestic business from within North America and it continued to be the leader in Chicago in terms of room rate. The hotel achieved the second highest RevPAR in its competitor set in 2012, with a 7% increase in RevPAR as compared with 2011.

The Avenues restaurant conversion into a junior ballroom was completed in November 2012. This has significantly improved the financial yield from this area and provides a welcome addition to the hotel's range of meeting venues.

The Peninsula Tokyo: Total revenue was HK$115 million (16%) higher than 2011, with significantly improved revenue in all areas, including a 25% increase in RevPAR. Whilst corporate business has returned to pre-earthquake occupancy levels, the long-haul leisure travel has taken longer to return. Official delegations to Japan from the Asia region as well as from the Middle East have had a positive impact on average rates. The territorial dispute between China and Japan continues to strain relations and hampers efforts to grow business from Greater China.

The hotel celebrated its 5th anniversary in September 2012 and benefited from the International Monetary Fund-World Bank meeting in October. Wedding business continues to be strong, with the 1,000th couple getting married in the hotel in September.

The Peninsula Tokyo

Revenue HK$814m	+16%
Occupancy	+11pp
Average Room Rate	+5%
RevPAR	+25%

The Peninsula Bangkok: Total revenue was HK$32 million (17%) higher than 2011. The political situation has remained stable and business levels and tourist arrivals have shown significant improvement over 2011 with a record number of international arrivals in 2012. Nevertheless, room rates remain subdued in a competitive environment.

There has been a gradual strengthening in the market and it is expected that room rates will improve significantly in the coming year.

The Peninsula Bangkok

Revenue HK$225m	+17%
Occupancy	+13pp
Average Room Rate	-8%
RevPAR	+17%

The Peninsula Manila: Total revenue was HK$29 million (11%) higher than 2011, which resulted in the hotel having another record year. The Philippines' economy was strong throughout 2012 and remained resilient in the face of continuing global economic uncertainty.

A stable government and an expanding middle class provided strong private and public consumption. International visitor arrivals also enjoyed a significant increase. Both rooms and food and beverage have focused on improving the volume of business, which has raised revenue levels throughout the hotel.

The Peninsula Manila

Revenue HK$302m	+11%
Occupancy	+3pp
Average Room Rate	+5%
RevPAR	+9%

The operating performances of The Peninsula Shanghai and The Peninsula Beverly Hills are provided below, even though these operations are not consolidated as they are not subsidiaries of the Group.

The Peninsula Shanghai

Revenue HK$492m	+7%
Occupancy	+0pp
Average Room Rate	-3%
RevPAR	-2%

The Peninsula Shanghai: Total revenue was HK$31 million (7%) above 2011, as a result of increased revenue in food and beverage and the commercial areas comprising the Arcade, Bund 33 and The Peninsula Residences.

Despite intense competition in the city, the hotel was able to capture high yield domestic travellers which, in addition to giving further growth in the number of US and European visitors into the hotel, helped it to maintain its leadership position in terms of RevPAR. Catering business was also strong, with a 17% increase in revenue over 2011. The Rose Ballroom has become a very popular and desirable wedding venue. During the year, the hotel entered into exclusive partnerships with selected luxury brands in the Arcade to create unique customer experiences.

The Peninsula Beverly Hills

Revenue HK$481m	+14%
Occupancy	+5pp
Average Room Rate	+6%
RevPAR	+14%

The Peninsula Beverly Hills: Total revenue was HK$60 million (14%) above 2011, resulting in 2012 being an exceptional year for the hotel with the highest revenue, the highest number of days with full occupancy and the highest average room rate.

General business conditions in Los Angeles were excellent in 2012 due to healthy growth in international tourist arrivals, particularly from the Middle East and Australia and the easing of visa restrictions. Domestically, the luxury market continued to show signs of recovery.

The hotel completed its four signature Colour Suites during the year, with each suite featuring a dramatic yet tastefully styled colour palette in pink, white, blue and green. The hotel is building a new Deluxe Garden Suite. Food and beverage business was robust throughout the year.

The portfolio of the Group's Commercial Properties Division includes The Repulse Bay Complex, The Peak Tower, St. John's Building and The Landmark in Ho Chi Minh City, Vietnam.

Most properties within the Division remained fully occupied in 2012, although there was pressure from increased supply and/or reduced demand. The renovations at The Repulse Bay had a negative impact on this Division's revenue.

Commercial Properties Division

The total revenue from the Commercial Properties Division was HK$10 million (1%) below 2011 mainly due to the renovation of de Ricou apartments in The Repulse Bay Complex, despite increased revenue from the other apartments and from The Peak Tower.

Set out below is a breakdown of revenue by individual properties:

	2012				2011				
HK$m	Residential properties	Office	Shopping Arcade	Total	Residential properties	Office	Shopping Arcade	Total	2012 vs 2011
The Repulse Bay Complex, Hong Kong	378	–	140	518	400	–	138	538	(4%)
The Peak Tower, Hong Kong	–	–	131	131	–	–	121	121	8%
St. John's Building, Hong Kong	–	45	–	45	–	45	–	45	–
The Landmark, Ho Chi Minh City, Vietnam	12	22	5	39	10	26	3	39	–
	390	67	276	733	410	71	262	743	(1%)

The Repulse Bay Complex, Hong Kong: Total revenue was HK$20 million (4%) below 2011, due to the renovation of the de Ricou serviced apartments, where revenue was HK$38 million below 2011. The ongoing improvement work in the public areas has further enhanced the appeal of The Repulse Bay Complex as a premier residential property, with continued high occupancy and rental rates despite cautious sentiments in the market.

The Repulse Bay Complex, Hong Kong

Revenue HK$518m -4%

Occupancy +0pp

Average monthly yield per suquare foot +8%

The Peak Tower, Hong Kong: Total revenue was HK$10 million (8%) above 2011. There was higher rental revenue from retail tenants and more visitors to Sky Terrace 428 as compared with 2011. The retail spaces in the Tower remained fully let during 2011, with the majority of existing tenants renewing their leases upon expiry.

The Peak Tower, Hong Kong

Revenue HK$131m +8%

Occupancy -1pp

Average monthly yield per suquare foot +13%

Sky terrace visitors increased by 3% to just under 2 million visitors in 2012, with 4% more revenue. Revenue from the the Sky Terrace increased to HK$43 million in 2012.

St. John's Building,
Hong Kong

Revenue
HK$45m +0%

Occupancy -9pp

Average monthly yield per suquare foot +0%

St. John's Building, Hong Kong: Revenue was in line with 2011. Although rental rates were higher in 2012, there was less occupancy due to the vacant periods between tenants.

The Landmark,
Ho Chi Minh City, Vietnam

Revenue
HK$39m -0%

Occupancy -11pp (Office)
+11pp (Residential)

Average monthly yield per suquare foot -17% (Office)
+12% (Residential)

The Landmark, Ho Chi Minh City, Vietnam: Total revenue was in line with 2011, with higher residential occupancy though less office occupancy and stable rental rates. The competition amongst serviced apartment buildings and office space remains intense, with many new buildings opening up, which limits the opportunity for rate growth.

Clubs and Services businesses of the Group include management and consultancy services, wholesaling and retailing of merchandise, operating of the Peak tram, operation of golf clubs and provision of dry cleaning and laundry services.

The Division recorded encouraging growth in revenue in 2012.

Clubs and Services Division

Businesses within this Division achieved higher revenue as compared to 2011. The combined revenue was HK$60 million (12%) above 2011.

Set out below is a breakdown of revenue by individual operations:

HK$m	2012	2011	2012 vs 2011
Clubs and Consultancy Services	**154**	131	18%
Peninsula Merchandising	**126**	116	9%
Peak Tram	**114**	108	6%
Thai Country Club	**66**	60	10%
Quail Lodge & Golf Club	**56**	47	19%
Tai Pan Laundry	**44**	38	16%
	560	500	12%

Clubs and Consultancy Services: Management fees from the clubs that the Group manages were 8% higher than 2011, with positive growth in business levels. Revenue from the operation of the Cathay Pacific Airways' first and business class lounges, where the revenue is based on the number of passengers utilising the lounges, also increased in line with the growth in passenger volumes, which were 9% higher than 2011.

Under Peninsula Clubs & Consultancy, the Group manages the prestigious Hong Kong Club, The Hong Kong Bankers Club and Butterfield's in Hong Kong and operates Cathay Pacific Airway's first and business class lounges at the Hong Kong International Airport.

Peninsula Merchandising: Revenue was HK$10 million (9%) above 2011, with another record year for the sale of the division's signature mooncakes during the Mid Autumn Festival period, with revenue of HK$53 million in 2012.

The Peak Tram: Revenue was HK$6 million (6%) above 2011. The Peak Tram's patronage rose 2% as compared with 2011 to 5.9 million passengers, marking an all-time record.

Thai Country Club: Revenue was HK$6 million (10%) higher than 2011, with 8% more golf rounds and increased spend per round.

Quail Lodge & Golf Club: Revenue was HK$9 million (19%) above 2011 due to increased revenue from The Quail, A Motorsports Gathering event.

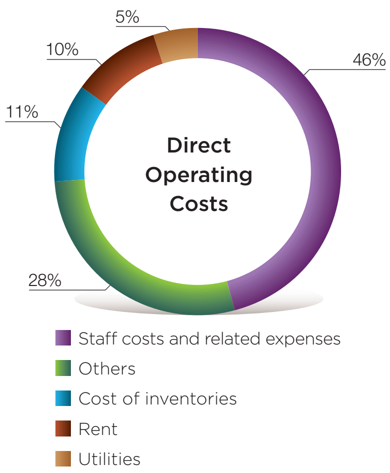
From September 2012, KemperSports Management is managing the golf clubhouse operations including golf, membership, food and beverage outlets, and banquet operations.

The Lodge remains closed and is currently undergoing renovation. The new design by Bob Barry Design Associates will reflect California Ranch and Spanish Colonial designs giving the hotel a fresh new look that is comfortable, appealing and distinctly Californian. The renovated lodge is expected to open at the end of March 2013.

Tai Pan Laundry: Total revenue in Tai Pan Laundry was HK$6 million (16%) higher than 2011, as a result of the increased business from airport lounges and one new hotel account.

Direct Operating Costs
HK$3,977m

+5%



Operating Costs

All business operations have exercised cost control measures to maintain or improve profit margins.

Excluding depreciation and amortisation, direct operating costs of the Group for the year amounted to HK$3,977 million, which was only 5% higher than 2011 despite pressure on the cost base from rising staffing levels and remuneration rates as well as other cost increases.

The majority of the increase was due to the increased staff costs and related expenses which accounted for 46% (2011: 45%) of the Group's direct operating costs. As business levels returned in 2012, the Group's operations gradually filled vacant positions to cope with staffing needs. The breakdown of the Group's full-time headcount as at 31 December is set out in the table on the next page.

At the end of 2012, the Group had 5,484 full-time employees for its direct operations around the world. Staff costs include HK$19 million which was invested in the learning and development programmes of our employees. Attracting the right talents and developing them are keys to ensure that we continue to provide the highest standard of luxury and quality to our customers. In 2012, the Group was able to keep its annual staff turnover rate at 19%, whilst that for our Hotels Division was 18%, which compares favourably with the industry average. The level of turnover has an impact on the costs of employee recruitment and training.

In addition, the Group managed to reduce staff injury and occupational disease rates significantly through a more robust health and safety management system and enhanced staff training and awareness programmes. This has a positive impact on the Group's staff insurance costs and productivity. For more information on how we manage employee health and safety, please refer to the Sustainability Review section.

The Group is cognizant of the importance of protecting our environment. In 2012, the average per unit cost for energy and water inflated by 4% and 8% respectively across the cities in which our operations are based. Our environmental programme for driving efficient use of energy and water not only helped the Group to reduce our impact on the environment but also enabled us to control the overall utility cost to a net increase of 3%. For example, by investing in the on-going re-lamping exercise and a new building automation system, The Peninsula hotels in New York and Chicago generated an overall savings of HK$1.4 million utility charges in 2012 despite the effects of increased business levels and inflation. Further details of our environmental programme are outlined in the Sustainability Review section.

Full time headcount at year end	2012			2011			
	Direct operations	Managed operations	Total	Direct operations	Managed operations	Total	2012 vs 2011
By division:							
Hotels	**4,354**	**1,258**	**5,612**	4,349	1,126	5,475	3%
Commercial Properties	**314**	**–**	**314**	323	–	323	(3%)
Clubs and Services	**816**	**427**	**1,243**	808	416	1,224	2%
	5,484	**1,685**	**7,169**	5,480	1,542	7,022	2%
By geographical location:							
Hong Kong	**1,778**	**427**	**2,205**	1,772	416	2,188	1%
Other Asia	**2,701**	**847**	**3,548**	2,742	723	3,465	2%
United States of America	**1,005**	**411**	**1,416**	966	403	1,369	3%
	5,484	**1,685**	**7,169**	5,480	1,542	7,022	2%

EBITDA and EBITDA Margin

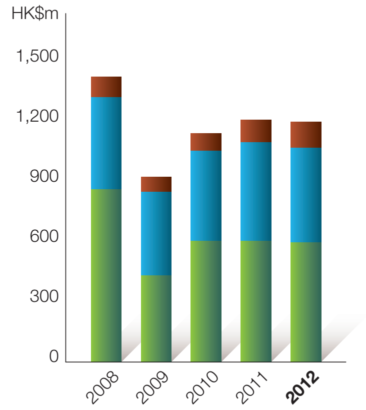
EBITDA (earnings before interest, taxation, depreciation and amortisation) decreased by 1% to HK$1,201 million.

The EBITDA margin of the Group remained flat in 2012 due to the impact of the renovations at The Peninsula Hong Kong and The Repulse Bay Complex which limited the revenue growth of the Hotels and Commercial Properties Divisions.

The table on the next page sets out the breakdown of the Group's EBITDA by business segment and by geographical segment.

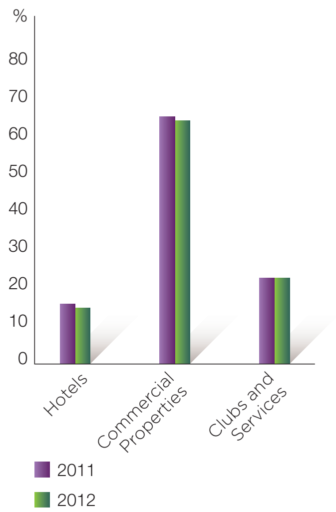
EBITDA	HK$1,201m	-1%
Hotels	HK$596m	-1%
Commerical Properties	HK$474m	-4%
Clubs and Services	HK$131m	+16%

EBITDA by Activity



EBITDA (HK$m)	Hong Kong	Other Asia	United States of America	Total
2012				
Hotels	**384**	**181**	**31**	**596**
Commercial Properties	**453**	**21**	**–**	**474**
Clubs and Services	**135**	**18**	**(22)**	**131**
	972	**220**	**9**	**1,201**
	81%	**18%**	**1%**	**100%**
2011				
Hotels	503	71	31	605
Commercial Properties	471	22	–	493
Clubs and Services	125	15	(27)	113
	1,099	108	4	1,211
	91%	9%	0%	100%
Change				
2012 vs 2011	(12%)	104%	125%	(1%)

EBITDA Margin



The EBITDA margin of the Hotels Division in 2012 was 1% lower than 2011 because of the impact of the renovation of The Peninsula Hong Kong, despite the gains in other locations. There was a 1% decrease in the EBITDA margin of the Commercial Properties Division due to the renovation of the de Ricou serviced apartment tower in The Repulse Bay Complex. The EBITDA margin of the Clubs and Services Division was stable.

The breakdown of EBITDA margins by business segment and geographical segment are set out below.

EBITDA margin	2012	2011
Hotels	**15%**	16%
Commercial Properties	**65%**	66%
Clubs and Services	**23%**	23%
Overall EBITDA margin	**23%**	24%
Arising in:		
Hong Kong	**44%**	47%
Other Asia	**12%**	7%
United States of America	**1%**	0%

Depreciation and amortisation

The depreciation and amortisation charge of HK$384 million (2011: HK$377 million) largely relates to the hotels. The Group has a 5-year capital expenditure plan that is reviewed annually. This includes planned replacement of fully depreciated furniture, fixtures and equipment, purchase of new items and major upgrade projects such as The Peninsula Hong Kong rooms enhancement project and reconfiguration of the de Ricou serviced apartment tower at The Repulse Bay Complex.

The Group has selected the cost model instead of the fair value model under the HKFRS to account for its hotels. Accordingly, the Group's hotels are subject to depreciation.

Non-operating items

During the year, the Group disposed of its interest in Inncom International, Inc., an unlisted equity investment, and recognised a non-operating gain of HK$46 million.

In 2011, the provision for impairment loss of HK$20 million was in relation to Quail Lodge Golf Club. Given the adverse operating environment faced by the club during 2011, the Directors considered its carrying amount should be written down by HK$20 million to its recoverable amount based on its fair value determined by an independent professional valuer with reference to the discounted cash flow valuation model of the assets.

The non-operating items are analysed below:

HK$m	2012	2011
Increase in fair value of investment properties	1,073	1,841
Gain on disposal of an unlisted equity instrument	46	–
Provision for impairment loss	–	(20)
	1,119	1,821

Non-operating items are gains or losses from sources unrelated to the normal operating activities of the business. These include gains or losses from investments and property revaluation.

The increase in fair value of investment properties for the year was principally attributable to the increase in the appraised market value for The Repulse Bay Complex and the shopping arcade at The Peninsula Hong Kong. Such increase was a reflection of the continued strong demand for luxury residential and high-end commercial properties in Hong Kong.

Share of result of a jointly controlled entity

The Group, through its jointly controlled entity, The Peninsula Shanghai Waitan Hotel Company Limited ("PSW"), owns a 50% interest in The Peninsula Shanghai Complex. The complex comprises a hotel, a shopping arcade and a hotel apartment tower of 39 units. In addition to operation of the hotel and leasing of the shopping arcade and apartments, PSW also sublet No. 1 Waitanyuan which is adjacent to the complex.

The Peninsula Shanghai remained the market leader in terms of RevPAR and generated an EBITDA of HK$68 million (2011: HK$68 million). However, due to the increase in borrowings to fund the payment of contractors' costs for the development of the hotel and apartments and the inclusion of a post-tax non-operating loss arising from property revaluation, the Group's share of loss increased to HK$125 million in 2012 (2011: HK$85 million).

The Group accounts for its jointly controlled entity under the equity method and recognises its share of the jointly controlled entity's post-acquisition post tax results, including non-operating items, in its consolidated Income Statement.

Set out below is an extract of the income statement of PSW:

HK$m	2012	2011	2012 vs 2011
Income	**492**	461	7%
Operating expenses	**(424)**	(393)	8%
EBITDA	**68**	68	–
Depreciation	**(102)**	(105)	(3%)
Net financing charges	**(188)**	(125)	50%
Loss before non-operating item	**(222)**	(162)	37%
Non-operating item, net of tax	**(28)**	(8)	250%
Loss for the year	**(250)**	(170)	47%

The Statement of Financial Position summarises the Group's assets and liabilities as at the end of the reporting period and how the net assets were funded.

According to the Group's accounting policies, hotel properties (other than shopping arcades and offices within the hotels) and golf courses are stated at cost less accumulated depreciation and any provision for impairment losses, while investment properties are stated at fair value. In order to provide users of the Financial Statements with additional information on the current market value of our hotels and golf courses, the Directors have commissioned independent valuers to perform a fair valuation of these properties (except for The Peninsula Beverly Hills which is 20% owned by the Group) as at 31 December 2012.

Statement of Financial Position

The Consolidated Statement of Financial Position of the Group as at 31 December 2012 is presented on page 150 and the following is a summary of its key components.

Fixed assets

The Group has interests in and manages nine operating hotels in Asia and the USA and is developing a hotel in Paris, in which the Group has a 20% interest.

In addition to hotel properties, the Group owns residential apartments, office towers and shopping arcades for rental purposes.

A summary of the Group's hotel, investment and other properties showing both the book value and the market value as at 31 December 2012 is set out in the table on the next page.

	Group's Interest	100% value Market Value (HK$m)	Book Value (HK$m)
Hotels			
The Peninsula Hong Kong	100%	11,276	9,407
The Peninsula Beijing	76.6%*	1,896	1,413
The Peninsula New York	100%	1,710	1,186
The Peninsula Chicago	100%	1,313	1,152
The Peninsula Tokyo	100%	1,468	1,059
The Peninsula Bangkok	75%	852	848
The Peninsula Manila	77.4%	307	291
		18,822	15,356
Investment properties			
The Repulse Bay Complex	100%	15,577	15,577
The Peak Tower	100%	1,234	1,234
St. John's Building	100%	861	861
The Landmark	70%	88	88
		17,760	17,760
Other properties			
Thai Country Club golf course	75%	262	257
Quail Lodge resort, golf course and vacant land	100%	168	159
Vacant land near Bangkok	75%	340	340
Others	100%	173	105
		943	861
Total market / book value		37,525	33,977
Hotel and investment property held by a jointly controlled entity			
The Peninsula Shanghai Complex	50%	6,747	6,468

* Despite its 76.6% legal interest in The Peninsula Beijing, the Group owns 100% economic interest in the hotel with a reversionary interest to the PRC partner at the end of the co-operative joint venture period.

According to the Group's accounting policy, its investment in jointly controlled entity is accounted for under the equity method and is initially stated at cost, adjusted for the Group's share of post-tax results.

Interest in a jointly controlled entity

The balance of HK$1,229 million as at 31 December 2012 (2011: HK$1,340 million) represented the Group's 50% indirect interest in The Peninsula Shanghai Waitan Hotel Company Limited, an enterprise incorporated in the People's Republic of China which owns 100% of The Peninsula Shanghai Complex. The decrease in balance was mainly due to the Group's share of loss amounting to HK$125 million (2011: HK$85 million) for the year, which included a post-tax non-operating loss arising from property revaluation.

Similar to the accounting treatment of interest in a jointly controlled entity, the Group accounts for its associates under the equity method.

Interest in associates

The balance of HK$572 million as at 31 December 2012 (2011: HK$562 million) represented the Group's 20% equity interest in and 20% share of the shareholder's loan to Al Maha Majestic S.à r.l., a company incorporated in Luxembourg which indirectly owns a 100% interest in a property in Paris to be redeveloped into The Peninsula Paris.

The Groups states its investment in hotel management contracts at cost less accumulated amortisation and impairment losses.

Investment in hotel management contracts

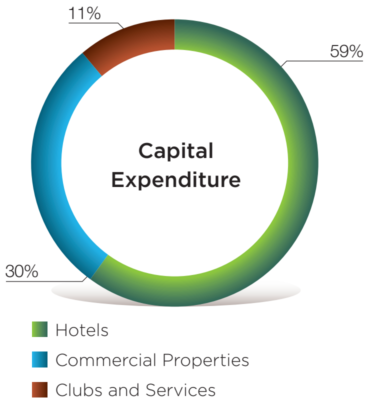
As at 31 December 2012, investment in hotel management contracts amounted to HK$670 million (2011: HK$662 million). The balance included an attributed consideration of EUR57.7 million in respect of the right acquired to manage The Peninsula Paris to be developed jointly by the Group and its associate, Al Maha Majestic S.à r.l.. The increase in the balance was mainly due to exchange rate adjustment on retranslating the Euro currency at the year end.

Statement of Cash Flows

The consolidated statement of cash flows of the Group for the year ended 31 December 2012 is set out on page 153 and the table below summarises the key cash inflows and outflows.

HK$m	Year ended 31 December 2012	2011
EBITDA	**1,201**	1,211
Changes in working capital and other adjustments	**(67)**	(65)
Net tax paid	**(169)**	(146)
Purchase of fixed assets	**(875)**	(312)
Payment for the acquisition of additional interest in a subsidiary	**–**	(578)
Proceeds for disposal of an equity instrument	**46**	–
Repayment from / (loans to) an associate and a jointly controlled entity	**181**	(580)
Net financing charges and dividends paid	**(171)**	(144)
Net increase / (decrease) in bank borrowings	**48**	(88)
Net (placement) / withdrawal of interest-bearing bank deposits with maturity of more than three months	**(487)**	990
Net cash (outflow) / inflow for the year	**(293)**	288
Cash and cash equivalents at 1 January	**1,963**	1,644
Effect of changes in foreign exchange rates	**12**	31
Cash and cash equivalents at 31 December	**1,682**	1,963

The Statement of Cash Flows provides information about the Group's change in financial position, reconciles the Group's reported income to operating cash flows and analyses how cash generated from operations was applied in investing and financing activities during the year.



Capital expenditure incurred by the Group on upgrading its properties during 2012 amounted to HK$875 million (2011: HK$312 million) and the breakdown of this sum is as follows:

HK$m	2012	2011
Hotels		
The Peninsula Hong Kong (including guestroom renovation)	336	36
Others	183	178
Commercial Properties		
The Repulse Bay Complex (including de Ricou service apartment tower reconfiguration)	220	56
Others	42	26
Clubs and Services	94	16
	875	312

After accounting for investing and financing activities and excluding bank deposits maturing after more than three months amounting to HK$494 million (2011: HK$7 million), cash and cash equivalents as at 31 December 2012 amounted to HK$1,682 million (2011: HK$1,963 million).

Off Balance Sheet Information

The following transactions and events are not reflected in the Group's income statement, statement of financial position and statement of cash flows but are considered relevant to the users of the Financial Statements.

Capital commitments

Capital commitments represent the amounts of funds planned to be spent on capital expenditure in the near future.

The Group is committed to enhancing the asset value of its hotel and investment properties and improving the service quality of these assets. As at 31 December 2012, the Group's capital commitments amounted to HK$1,520 million (2011: HK$1,818 million) and the breakdown is set out on the next page.

HK$m	2012 Contracted for	2012 Authorised but not contracted for	2012 Total	2011 Contracted for	2011 Authorised but not contracted for	2011 Total
Capital expenditure						
The Peninsula Hong Kong	**173**	**143**	**316**	236	328	564
The Repulse Bay Complex	**225**	**208**	**433**	88	623	711
Others	**53**	**718**	**771**	36	507	543
	451	**1,069**	**1,520**	360	1,458	1,818
The Group's share of capital commitments of						
– A jointly controlled entity	**3**	**19**	**22**	–	13	13
– Associates	**227**	**160**	**387**	195	215	410

Contingent liabilities

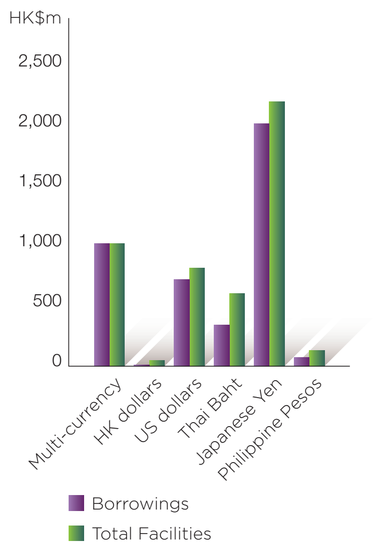
Contingent liabilities as at 31 December 2012 for the Group and the Company are analysed in the table below. The Directors consider that the below contingent liabilities are unlikely to materialise. Therefore, no provision was made in the Financial Statements.

HK$m	Group 2012	Group 2011	Company 2012	Company 2011
Guarantees given in respect of borrowings and other banking facilities for subsidiaries	**–**	–	**4,239**	4,393
Other guarantees	**1**	1	**1**	1
	1	1	**4,240**	4,394

Contingent liabilities are potential obligations that may or may not be incurred by the Group depending on the outcome of a future event such as a lawsuit. Contingent liabilities are not booked in the Group's Statement of Financial Position as it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably.

Non-adjusting post reporting events are those not related to any situations that existed on the balance sheet date. Rather, they provide evidence of conditions that arose after the balance sheet date which should be accounted for in the next financial period.

Banking Facilities and Borrowings (by Currency)



The long term financial obligations of the Group's entities are normally arranged in currencies in which they have substantial positive operational cash flows, thereby establishing natural currency hedges.

Non-adjusting post reporting period events

After the end of the reporting period, the Directors proposed a final dividend of 10 HK cents per share in respect of the year ended 31 December 2012, which will be payable on 20 May 2013. The final dividend is subject to the approval by shareholders at the forthcoming Annual General Meeting to be held on 3 May 2013 and no provision has been made in the Financial Statements.

Treasury Management

Borrowings

In 2012, gross borrowings decreased to HK$4,174 million (2011: HK$4,319 million).

In addition to the Group's consolidated borrowings, The Peninsula Shanghai (50% owned), The Peninsula Beverly Hills (20% owned) and The Peninsula Paris (20% owned) have non-recourse bank borrowings, which are not consolidated in the statement of financial position as the entities owning the assets are not subsidiaries of the Company. During the year, The Peninsula Shanghai Waitan Hotel Company Limited entered into a 15-year RMB2.5 billion term loan agreement with Agricultural Bank of China to refinance its maturing facilities and to provide additional financing.

The consolidated and non-consolidated borrowings as at 31 December 2012 are summarised as follows:

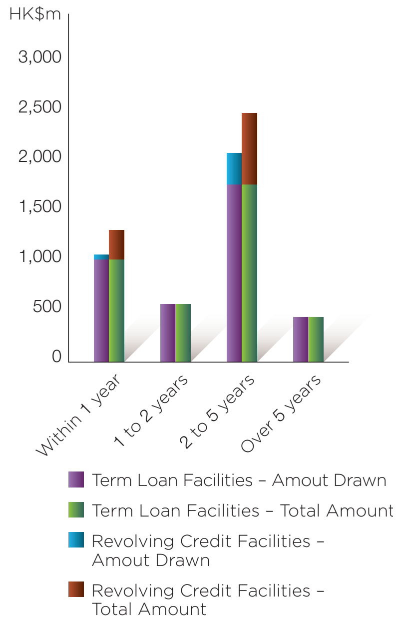
HK$m	2012 Hong Kong	2012 Other Asia	2012 United States of America	2012 Europe	2012 Total	2011 Total
Consolidated gross borrowings	1,031	2,427	716	–	4,174	4,319
Non-consolidated gross borrowings attributable to the Group*:						
The Peninsula Shanghai (50%)	–	1,425	–	–	1,425	1,176
The Peninsula Beverly Hills (20%)	–	–	218	–	218	218
The Peninsula Paris (20%)	–	–	–	215	215	42
Non-consolidated borrowings	–	1,425	218	215	1,858	1,436
Consolidated and non-consolidated gross borrowings	1,031	3,852	934	215	6,032	5,755

* Represented HSH's attributable share of borrowings.

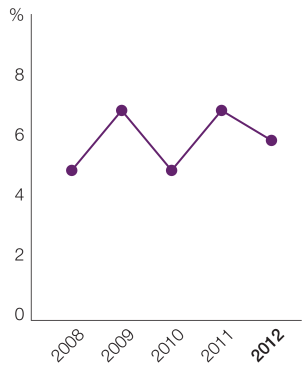
Consolidated net debt decreased to HK$1,989 million as compared to HK$2,335 million in 2011 taking into account cash of HK$2,185 million (2011: HK$1,984 million). The increase in cash was mainly due to partial repayment of an entrustment loan of HK$373 million (RMB 300 million) from The Peninsula Shanghai which is 50% owned. Hence, gearing decreased from 7% to 6%.

Also, in August 2012, the Group through its wholly owned subsidiary, HSH Financial Services Limited, entered into a six-year JPY5 billion fixed rate term loan agreement with Development Bank of Japan Inc.. This is to prepay part of its existing debts maturing in 2014 and to extend the maturity profile of its borrowings to 2018. The average debt maturity of the Group borrowings has increased from 2.3 years to 2.4 years.

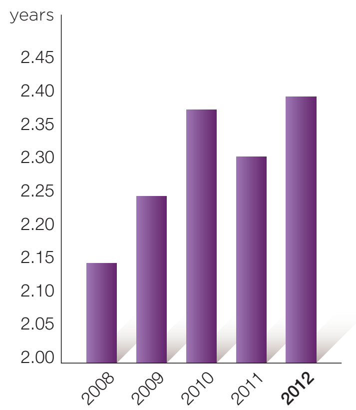
Banking Facilities and Borrowings (by type and maturity)



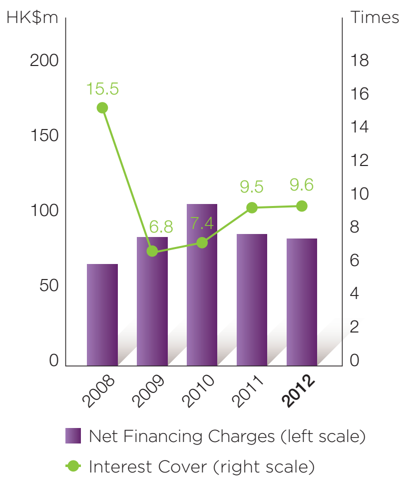
Gearing



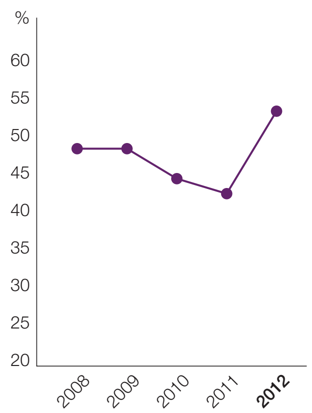
Average Debt Maturity

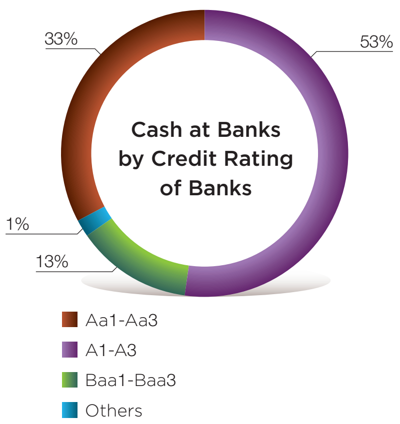


Net Financing Charges and Interest Cover



Long Term Fixed-to-Total Borrowings (Adjusted for the hedging effect)





Interest rate risk

Financing charges on borrowings in 2012 amounted to HK$141 million (2011: HK$137 million). After netting off interest income of HK$56 million (2011: HK$49 million), a net charge of HK$85 million (2011: HK$88 million) was recognised in the income statement.

The weighted average gross interest rate for the year increased slightly to 3.2% (2011: 3.1%) after accounting for all hedging activities and interest cover (operating profit divided by net financing charges) increased to 9.6 times (2011: 9.5 times) in 2012.

The Group seeks to minimise net financing charges by investing its surplus cash in low-risk high-yield structured deposits. The Group also makes use of interest rate swaps and cross currency interest rate swaps to hedge its interest rate risk.

As at 31 December 2012, the Group's fixed to floating interest rate ratio was at 54% (2011: 43%).

The Group's interest rate risk management policy focuses on reducing the Group's exposure to changes in interest rates.

In addition to raising funds directly on a fixed rate basis, the Group may use interest rate swaps or cross currency interest rate swaps in managing its long term interest rate exposure.

Credit risk

As at 31 December 2012, over 90% of cash at banks and 100% of the derivatives were placed with financial institutions with credit ratings of at least an investment grade.

The Group manages its exposure to non-performance of counterparties by transacting with counterparties which have a credit rating of at least an investment grade when depositing surplus funds. However, in developing countries, it may be necessary to deal with banks of lower credit ratings.

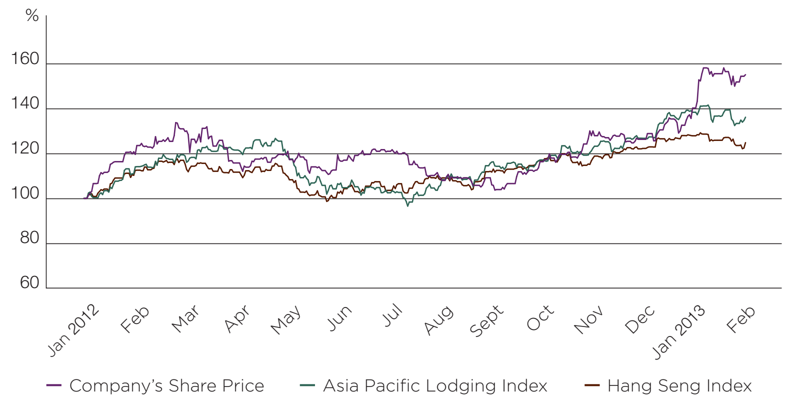
Derivatives are used solely for hedging purposes and not for speculation and the Group only enters into derivative transactions with counterparties which have credit ratings of at least investment grades, even in developing countries, because of the longer term effect.

Share Information

The Company's share price closed on 13 March 2013 at HK$13.50, giving a market capitalisation of HK$20.3 billion (US$2.6 billion). This reflects a discount of 39% to net assets attributable to shareholders of the Company, or a discount of 44% to the adjusted net assets (see page 35).

The average closing price during 2012 was HK$10.16, with the highest price of HK$11.92 achieved on 29 February 2012 and the lowest price of HK$8.63 recorded on 3 January 2012.

Share Price and Indices

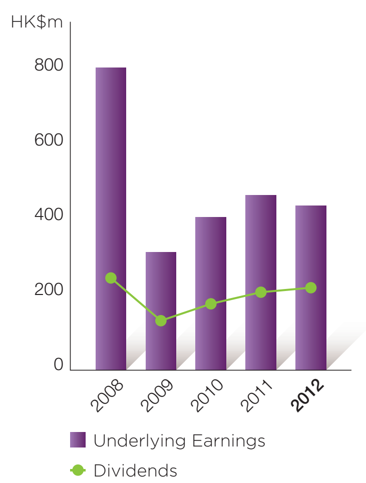


Dividends

In addition to capital appreciation (in the form of our share price performance over time), the Company seeks to provide its shareholders with investment return through the payment of dividends. Over the past five years, the Company's dividend payout rates have been approximately 40% of underlying earnings.

As the operating results remain flat, the Board has recommended a final dividend payable on 20 May 2013 of 10 HK cents per share. Together with the 2012 interim dividend of 4 HK cents per share paid on 28 September 2012, the total dividend in respect of the 2012 financial year will be 14 HK cents per share.

Underlying Earnings



Total Shareholder Return

Total shareholder return ("TSR") is calculated based on the capital gains and dividends of the stock. HSH had a TSR of 27.51% for 2012. During the period 2007 to 2012, the Company provided an annualised TSR of -3.31%, versus -0.83% and 6.21% for the Hang Seng Index and the Asia Pacific Lodging Index respectively.

Returns of Company's Shares and Indices