Financial Review

Adjusted NAV per share

HK$26.04

+2%

The Group's Adjusted Net Asset Value

In the Financial Statements, the Group's hotels (other than shopping arcades and offices within the hotels) and golf courses are stated at depreciated cost less accumulated impairment losses, if any, and not at fair value.

Accordingly, we have commissioned an independent third-party fair valuation of the Group's hotels and golf courses as at 31 December 2014, the details of which are set out on page 51. If these assets were to be stated at fair value, the Group's net assets attributable to shareholders would increase by 10% to HK$39,496 million as indicated in the table below.

HK$m	2014	2014	2013	2013
Net assets attributable to shareholders per the audited statement of financial position		**35,901**		35,105
Adjusting the value of hotels and golf courses to fair market value	**4,378**		4,103	
Less: Related deferred tax and non-controlling interests	**(783)**		(722)	
		3,595		3,381
Adjusted net assets attributable to shareholders		**39,496**		38,486
Audited net assets per share (HK$)		**23.67**		23.37
Adjusted net assets per share (HK$)		**26.04**		25.62

Underlying EPS

HK$0.53

+56%

The Group's Underlying Earnings

Our operating results are mainly derived from the operation of hotels and letting of commercial properties. We manage the Group's operations with principal reference to their underlying operating cash flows and recurring earnings. However, to comply with the applicable accounting standards, we are required to include non-operating and non-recurring items, such as any changes in fair value of investment properties, in our income statement. In order to provide a better reflection of the performance of the Group, we have provided 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 and non-recurring items on the next page.

The Group's underlying profit attributable to shareholders for the year ended 31 December 2014 increased by 57% to HK$804 million.

HK$m	2014	2013	2014 vs 2013
Profit attributable to shareholders	**1,146**	1,712	
Increase in fair value of investment properties	**(496)**	(1,403)	
Share of property revaluation (gain)/loss of The Peninsula Shanghai, net of tax	**(6)**	178	
Provision for impairment loss in respect of The Peninsula Beijing and The Peninsula Manila	**132**	–	
Other non-operating and non-recurring items	**22**	(3)	
Tax and non-controlling interests attributable to non-operating items	**6**	27	
Underlying profit attributable to shareholders	**804**	511	57%
Underlying earnings per share (HK$)	**0.53**	0.34	56%

Income Statement

The Group's consolidated income statement for the year ended 2014 is set out on page 192. The following table summarises the key components of the Group's profit attributable to shareholders. This table should be read in tandem with the commentaries set out on pages 46 to 49 of this Financial Review.

HK$m	2014	2013	2014 vs 2013
Turnover	**5,838**	5,508	6%
Operating costs	**(4,310)**	(4,202)	3%
EBITDA	**1,528**	1,306	17%
Depreciation and amortisation	**(423)**	(395)	7%
Net financing charges	**(66)**	(94)	(30%)
Share of result of The Peninsula Shanghai	**(6)**	(280)	(98%)
Share of results of The Peninsula Beverly Hills and The Peninsula Paris	**(35)**	–	n/a
Non-operating items	**364**	1,406	(74%)
Taxation	**(231)**	(231)	–
Profit for the year	**1,131**	1,712	(34%)
Non-controlling interests	**15**	–	n/a
Profit attributable to shareholders	**1,146**	1,712	(33%)

Turnover

HK$5,838m

+6%

Hotel
HK$4,260m

+5%

Commercial Properties
HK$901m

+12%

Clubs and Services
HK$677m

+3%

Turnover

The Group's turnover in 2014 increased by 6% to HK$5,838 million. A breakdown of this by business segment and geographical segment is set out in the following table.

Consolidated revenue by business segment

HK$m	2014	2013	2014 vs 2013
Hotels	4,260	4,044	5%
Commercial Properties	901	806	12%
Clubs and Services	677	658	3%
	5,838	5,508	6%

Consolidated revenue by geographic location

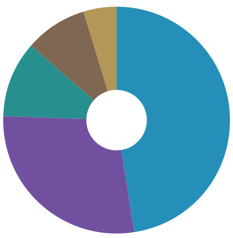
HK$m	2014	2013	2014 vs 2013
Arising in			
Hong Kong	2,775	2,505	11%
Other Asia	1,718	1,786	(4%)
United States of America	1,290	1,190	8%
Europe	55	27	104%
	5,838	5,508	6%

Our hotels division is the main contributor to the Group's revenue, accounting for 73% (2013: 73%) of total revenue. Within the other Asia revenues are the two Thai properties, namely The Peninsula Bangkok and the Thai Country Club, which have both been significantly affected by political events. A further analysis of the revenues and operating performance of individual operating entities are set out in the Business Review section on pages 24 to 41.

Operating Cost

HK$4,310m

+3%



Staff costs and related expenses
Others
Cost of inventories
Rent
Utilities

Operating Costs

In 2014, our operating costs (excluding depreciation and amortisation) increased by 3% to HK$4,310 million due to higher business levels attained by most of our operations.

Given the nature of operating high-end luxury hotels, staff costs continued to be the largest portion of operating costs. Staff costs and related expenses for the year increased by 5% to HK$2,052 million, representing 48% (2013: 46%) of the Group's operating costs and 35% (2013: 35%) of the Group's revenue.

EBITDA and EBITDA Margin

EBITDA (earnings before interest, taxation, depreciation and amortisation) of the Group increased by HK$222 million or 17% to HK$1,528 million in 2014. Compared to an increase of HK$330 million or 6% in consolidated revenue, the increase in EBITDA represented a flow-through of 67%. Our successful efforts to control costs have resulted in an increase of two percentage points in the Group's overall EBITDA margin to 26%.

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

EBITDA (HK$m)	Hong Kong	Other Asia	United States of America	Europe	Total
2014					
Hotels	**565**	**209**	**44**	**–**	**818**
Commercial Properties	**524**	**16**	**–**	**42**	**582**
Clubs and Services	**130**	**9**	**(11)**	**–**	**128**
	1,219	**234**	**33**	**42**	**1,528**
	80%	**15%**	**2%**	**3%**	**100%**
2013					
Hotels	452	189	8	–	649
Commercial Properties	484	16	–	21	521
Clubs and Services	144	15	(23)	–	136
	1,080	220	(15)	21	1,306
	83%	17%	(1%)	1%	100%
Change					
2014 vs 2013	13%	6%	320%	100%	17%

EBITDA margin	**2014**	2013
Hotels	**19%**	16%
Commercial Properties	**65%**	65%
Clubs and Services	**19%**	21%
Overall EBITDA margin	**26%**	24%
Arising in:		
Hong Kong	**44%**	43%
Other Asia	**14%**	12%
United States of America	**3%**	(1%)
Europe	**76%**	78%

The luxury hotel business is a labour-intensive industry, which also requires a relatively high cost of inventories to maintain the quality of service and food and beverage. Despite this, we are pleased to have been able to improve our hotels division's EBITDA margin by three percentage points to 19% in 2014.

The EBITDA margin of the commercial properties division in 2014 remained stable as a result of our efforts to control increases in costs within a soft residential market. However, the clubs and services division's EBITDA margin decreased by two percentage points to 19%, mainly due to the higher licence fee charged by the Hong Kong government to The Peak Tram for the two-year extension of its operating right to the end of 2015, and the revenue shortfall suffered by the Thai Country Club as a result of the political situation in Thailand.

Depreciation and Amortisation

The depreciation and amortisation charge of HK$423 million (2013: HK$395 million) largely relates to the hotels. The increase in depreciation and amortisation in 2014 was mainly due to the full year depreciation impact following the completion of the renovation project at The Peninsula Hong Kong in April 2013. Depreciation charges are substantial and as such the Group adopts a rolling 5-year capital expenditure plan that is reviewed regularly to monitor planned replacement of furniture, fixtures and equipment, purchase of new items and major upgrade or enhancement projects.

Non-Operating Items

The non-operating items are analysed as follows:

HK$m	2014	2013
Increase in fair value of investment properties	496	1,403
Provision for impairment loss	(132)	–
Gain on disposal of an unlisted equity instrument	–	3
	364	1,406

The increase in fair value of investment properties for the year was principally attributable to the increase in the appraised market value of the shopping arcade at The Peninsula Hong Kong and The Repulse Bay Complex. In 2013, The Peninsula New York also recorded an increase of HK$523 million in fair value in respect of its shopping arcade due to the successful restructuring of the retail leases.

The Directors considered that the book values of The Peninsula Beijing, pending major renovation, and The Peninsula Manila as at 31 December 2014 were higher than their respective recoverable amounts. On this basis, the book values of these hotels were written down by HK$132 million.

Result of The Peninsula Shanghai

The Group, through its joint venture The Peninsula Shanghai Waitan Hotel Company Limited ("PSW"), owns a 50% interest in The Peninsula Shanghai Complex which comprises a hotel, a shopping arcade and a residential tower of 39 apartments. In order to reduce financing charges, PSW resolved in July 2013 to sell 19 apartment units in the market. Accordingly, these apartment units were reclassified from "investment properties" to "assets held for sale" during 2013. Following this reclassification, these apartment units are stated at their fair value net of the estimated selling costs to be incurred as required by the applicable accounting standard, whereas the remaining 20 apartment units, which are available for lease, continue to be stated at fair value.

During 2014, The Peninsula Shanghai remained as the market leader in terms of average room rate and RevPAR in its competitive set, generating an EBITDA of HK$247 million (2013: HK$92 million), of which HK$129 million was derived from the sale of 11 apartment units (2013: HK$nil). In addition, The Peninsula Shanghai Complex recorded a net unrealised gain of HK$12 million on revaluation of the hotel arcade and remaining apartments (2013: a net loss of HK$355 million, mainly due to the unrealised loss incurred for the reclassification of the 19 apartment units from "investment properties" to "assets held for sale" as noted in the previous paragraph).

As PSW has been mainly debt financed and the hotel building is subject to a high depreciation charge given the remaining lease term, PSW made a net loss of HK$12 million after accounting for depreciation and net financing charges. The Group's share thereof amounted to HK$6 million (2013: HK$280 million).

Details of the operating performance of The Peninsula Shanghai are set out in the Business Review section on page 29.

Results of The Peninsula Beverly Hills and The Peninsula Paris

The Group has a 20% interest in each of The Peninsula Beverly Hills and The Peninsula Paris. The Group's share of net loss of these two hotels for 2014 amounted to HK$35 million (2013: HK$nil), of which HK$22 million related to the share of pre-opening expenses incurred by The Peninsula Paris which opened for business on 1 August 2014.

Details of the operating performances of The Peninsula Beverly Hills and The Peninsula Paris are set out in the Business Review section on pages 34 and 35.

Balance Sheet

The Group's financial position as at 31 December 2014 remained strong, with a year-on-year increase in shareholders' funds of 2% to HK$35,901 million, representing a per share value of HK$23.67 compared to HK$23.37 in 2013. The consolidated balance sheet of the Group as at 31 December 2014 is presented on page 194 and the key components of the Group's assets and liabilities are set out in the table below.

HK$m	2014	2013	2014 vs 2013
Fixed assets	**38,168**	38,187	(0%)
Other long-term assets	**2,474**	2,596	(5%)
Cash at banks and in hand	**2,477**	1,494	66%
Other assets	**863**	867	(0%)
	43,982	43,144	2%
Interest-bearing borrowings	**(5,481)**	(5,486)	(0%)
Other liabilities	**(2,350)**	(2,284)	3%
	(7,831)	(7,770)	1%
Net assets	**36,151**	35,374	2%
Represented by			
Shareholders' funds	**35,901**	35,105	2%
Non-controlling interests	**250**	269	(7%)
Total equity	**36,151**	35,374	2%

Fixed Assets

The Group has interests in ten operating hotels in Asia, the USA and Europe. In addition to hotel properties, the Group owns residential apartments, office towers and commercial buildings for rental purposes.

Our hotel properties and investment properties are accounted for in different ways. The 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. Therefore, independent valuers have been engaged to conduct a fair valuation of these properties as at 31 December 2014, and a summary of the Group's hotel, commercial and other properties showing both the book value and the fair value as at 31 December 2014 is set out in the table on the following page.

	Group's Interest	100% Value: Fair Value based on Independent Valuation (HK$m)	100% Value: Book Value (HK$m)
Hotels			
The Peninsula Hong Kong	**100%**	12,172	10,038
The Peninsula New York	**100%**	2,413	1,764
The Peninsula Beijing	**76.6%***	1,493	1,244
The Peninsula Chicago	**100%**	1,342	1,146
The Peninsula Tokyo	**100%**	1,178	711
The Peninsula Bangkok	**75%**	741	751
The Peninsula Manila	**77.4%**	182	182
		19,521	15,836
Commercial Properties			
The Repulse Bay Complex	**100%**	16,566	16,566
The Peak Tower	**100%**	1,331	1,331
St. John's Building	**100%**	919	919
21 avenue Kléber	**100%**	548	548
1-5 Grosvenor Place	**50%**	3,447	3,447
The Landmark	**70%****	88	88
		22,899	22,899
Other Properties			
Thai Country Club golf course	**75%**	232	252
Quail Lodge resort, golf course and vacant land	**100%**	304	264
Vacant land near Bangkok	**75%**	330	330
Others	**100%**	207	92
		1,073	938
Total market/book value		43,493	39,673
Hotel and investment property held by a joint venture			
The Peninsula Shanghai Complex***	**50%**	5,341	5,019
Hotel property held by associates			
The Peninsula Paris	**20%**	6,622	6,169
The Peninsula Beverly Hills	**20%**	2,533	428

* The Group owns 100% economic interest of The Peninsula Beijing with a reversionary interest to the PRC partner in 2033 upon expiry of the co-operative joint venture period.

** The Group owns 50% economic interest of The Landmark with a reversionary interest to the Vietnamese partner in 2026 upon expiry of the joint venture period.

*** Excluding the remaining 8 apartment units held for sale.

Other Long-Term Assets

The other long-term assets as at 31 December 2014 of HK$2,474 million (2013: HK$2,596 million) principally comprise the Group's 50% interest in The Peninsula Shanghai, the Group's 20% interest in The Peninsula Paris and the hotel operating rights in respect of The Peninsula Paris. The decrease in balance was mainly due to the exchange difference on translation of the Group's investment in The Peninsula Paris resulting from the weakening of the Euro exchange rate. The exchange differences were accounted for as other comprehensive income in 2014.

Cash At Banks and in Hand and Interest-Bearing Borrowings

As at 31 December 2014, the Group's cash at banks and in hand increased to HK$2,477 million (2013: HK$1,494 million), partly due to delayed operating and project expenditures, whilst interest-bearing borrowings decreased to HK$5,481 million (2013: HK$5,486 million). The net cashflow from operations was therefore sufficient to cover capital expenditure on existing assets for the year. A breakdown of the Group's capital expenditure for the year ended 31 December 2014 is set out on page 53.

Cash Flows

The consolidated statement of cash flows of the Group for the year ended 31 December 2014 is set out on page 197. The following table summarises the key cash movements leading to the increase in cash at banks and in hand of the Group as at 31 December 2014.

HK$m	**2014**	2013
EBITDA	**1,528**	1,306
Net change in debtors/creditors	**61**	95
Tax payment	**(157)**	(93)
Net cash generated from operating activities	**1,432**	1,308
Capital expenditure on existing assets	**(409)**	(928)
Net cash inflow after normal capital expenditure	**1,023**	380
Acquisition of new properties	**–**	(2,293)
Net cash inflow/(outflow) before dividends and other payments	**1,023**	(1,913)

The tax payment in 2014 was higher due to the non-recurrence of 2013 depreciation allowances in respect of the renovations of The Peninsula Hong Kong and The Repulse Bay Complex.

The after-tax net cash generated from operating activities for the year amounted to HK$1,432 million (2013: HK$1,308 million), of which HK$409 million (2013: HK$928 million) was applied to fund capital expenditure on existing assets.

The breakdown of the Group's spending on its existing assets and the new acquisitions is analysed below.

HK$m	2014	2013
Properties upgrade		
Hotels		
The Peninsula Hong Kong		
(including guestroom renovation)	**56**	198
Other hotels	**201**	265
Commercial properties		
The Repulse Bay Complex		
(including de Ricou reconfiguration)	**56**	293
Other properties	**49**	50
Clubs and services	**47**	122
	409	928
New acquisitions		
1-5 Grosvenor Place	**–**	1,688
21 avenue Kléber	**–**	605
	–	2,293
	409	3,221

Treasury Management

The Group manages treasury activities centrally at our corporate office in Hong Kong. We are exposed to liquidity, foreign exchange, interest rate and credit risks in the normal course of business and have policies and procedures in place to manage such risks.

Liquidity/Financing

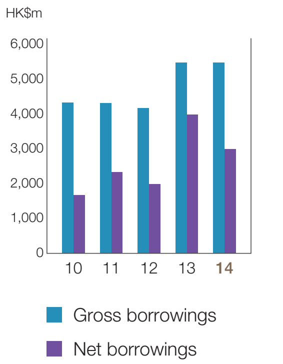
Our policy is to monitor current and expected liquidity requirements and to ensure that we maintain sufficient funds to meet short and longer-term obligations and commitments. The Group also constantly reviews its loan profile so as to manage its refinancing risks and extend its maturity profile.

In 2014, gross borrowings decreased to HK$5,481 million (2013: HK$5,486 million). Consolidated net debt decreased to HK$3,004 million as compared to HK$3,992 million in 2013, after taking into account cash of HK$2,477 million (2013: HK$1,494 million). Gearing, expressed as the percentage of net borrowings to the total of net borrowings and shareholders' funds, decreased from 10% to 8%, whilst the funds from operations (EBITDA less tax paid and less net interest paid) to net debt ratio increased from 28% to 44%. These ratios continue to reflect a healthy financial position for the Group.

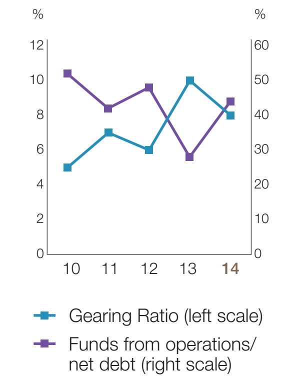
The average debt maturity decreased from 3.5 years to 3.1 years.

During the year, the Company arranged credit facilities of JPY2 billion and US$40 million respectively for two wholly owned subsidiaries and a credit facility of Baht800 million for a subsidiary to refinance their maturing term loans.

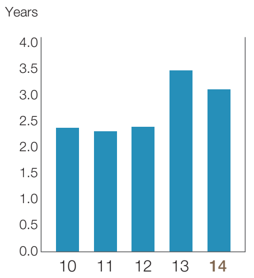
Gross and Net Borrowings



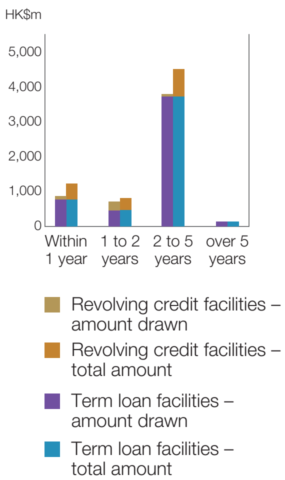
Gearing and Funds from Operations to Net Debt



Average Debt Maturity



Banking Facilities and Borrowings (by type and maturity)



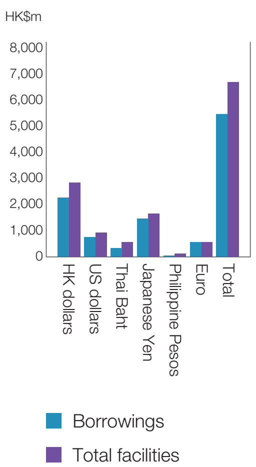
In addition to the Group's consolidated borrowings, The Peninsula Shanghai (50% owned), The Peninsula Beverly Hills (20% owned) and The Peninsula Paris (20% owned) have non-recourse bank borrowings which are not consolidated in the statement of financial position as the entities owning the assets are not subsidiaries of the Company.

The consolidated and non-consolidated borrowings as at 31 December 2014 are summarised as follows:

	2014					2013
HK$m	Hong Kong	Other Asia	United States of America	Europe	Total	Total
Consolidated gross borrowings	2,281	1,872	766	562	5,481	5,486
Non-consolidated gross borrowings attributable to the Group*						
The Peninsula Shanghai (50%)	–	1,183	–	–	1,183	1,412
The Peninsula Beverly Hills (20%)	–	–	224	–	224	218
The Peninsula Paris (20%)	–	–	–	409	409	446
Non-consolidated borrowings	–	1,183	224	409	1,816	2,076
Consolidated and non-consolidated gross borrowings	2,281	3,055	990	971	7,297	7,562

* Represents HSH's attributable share of borrowings

Banking Facilities and Borrowings (by currency)



Foreign Exchange

The Group reports its financial results in Hong Kong dollars and does not hedge US dollar exposures in the light of the HK-US dollar peg. It usually hedges most of the foreign exchange exposures arising from significant foreign currency monetary assets and liabilities, including foreign currency borrowings. The Group mostly uses cross currency swaps, foreign exchange swaps or forward exchange contracts to hedge exposures.

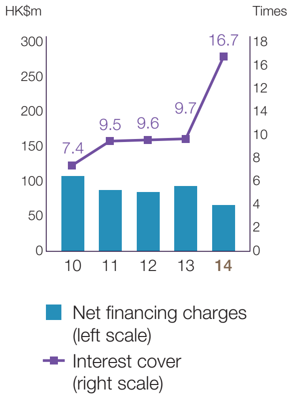
All of the Group's borrowings are denominated in the functional currency of the operations to which they relate. As at 31 December 2014, Hong Kong dollar borrowings represented 42% (2013: 37%) of total borrowings. Other balances were mainly in US dollars, Japanese yen and other local currencies of the Group's entities.

Interest Rate Risk

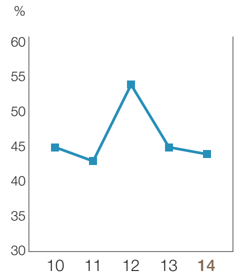
The Group has an interest rate risk management policy which focuses on reducing the Group's exposure to changes in interest rates by maintaining a prudent mix of fixed and floating rate liabilities. In addition to raising funds directly on a fixed rate basis, the Group also uses interest rate swaps or cross currency interest rate swaps in managing its long-term interest rate exposure.

Financing charges on borrowings in 2014 amounted to HK$131 million (2013: HK$140 million). After interest income of HK$65 million (2013: HK$46 million), a net charge of HK$66 million (2013: HK$94 million) was recognised in the income statement. Interest cover (operating profit divided by net financing charges) increased to 16.7 times (2013: 9.7 times) in 2014 due to the combination of improved operating profit and reduced net financing charges. As at 31 December 2014, the Group's fixed to floating interest rate ratio was at 44% (2013: 45%) and the weighted average gross interest rate for the year decreased to 2.3% (2013: 2.9%). The floating interest rate portfolio benefited from the current low interest rate environment.

Net Financing Charges and Interest Cover



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



Credit Risk

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

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 grade, even in developing countries, because of the longer term effect.

As at 31 December 2014, bank deposits of HK$2,463 million (2013: HK$1,471 million) and derivatives with notional amount of HK$1,788 million (2013: HK$2,090 million) were transacted with financial institutions with credit ratings of at least investment grade.

Share Information

At market close on 20 March 2015, the Company's share price stood at HK$11.16, giving a market capitalisation of HK$16.9 billion (US$2.2 billion). This reflects a discount of 53% to net assets attributable to shareholders of the Company, or a discount of 57% to the adjusted net assets (see page 44).

The average closing price during 2014 was HK$11.23, with the highest price of HK$12.60 achieved on 12 September 2014 and the lowest price of HK$10.08 recorded on 21 March 2014.