

Group Risk Committee Report



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ROLE AND COMPOSITION

I was appointed as Chairman of the Group Risk Committee when I joined the Company as its Chief Financial Officer in March 2014. The Group Risk Committee (“GRC”) is a sub-committee of the Group Management Board, formed to enhance our focus on existing and potential risks of the Group. This report provides an overview of what the Committee has done during the year.

Chairman: Mr Alan Clark (Chief Financial Officer)

Members: Group General Manager, Audit and Risk Management
Selected members of senior management and corporate Group General Manager

In 2014, the GRC met four times to provide oversight of principal business risks to which the Group is subject. The GRC also issued two updates to the Group Management Board (“GMB”) in 2014 on key risks, incidents and mitigating actions, and overall plans, trends and analyses, and shared updates with responsible management.

GROUP RISK COMMITTEE CHARTER

The GRC developed and adopted the Group Risk Committee Charter (“Charter”) as its governing instrument. This document outlines the membership, meeting format and frequency, responsibilities for risk oversight and reporting, implementation of the Group Risk Register (“Register”), and the reporting line that applies to the Committee.

The main responsibilities of the GRC under the Charter include:

- Evaluating the Group’s principal risks through review and challenge, where necessary, of information received
- Monitoring exposure to risk types in a sufficiently accurate and timely manner, and the available mitigating actions
- Evaluating the risk profile of the Group, and subsequently recommending to the GMB an appropriate level of risk for the Group
- Developing and updating risk management procedures including overseeing and advising GMB on the embedding and maintenance of a supportive risk management culture throughout the Group, to ensure effective delegation of risk management responsibilities, identification of key risks, implementation of action plans and remedy of incidents
- Coordinating and compiling the Register with on-going maintenance, and preparing summaries of top tier risks and related contingency plans to Audit Committee and the Board
- Implementing the Register including establishing clear roles and responsibilities for risk oversight, risk reporting and escalation, risk ownership, and communicating across the Group
- Approving policies, procedures and instructions relating to the Register

MAIN ACTIVITIES IN 2014

In 2014, the main focus of the year was an overall review of our existing risk management structure and processes. We introduced certain initiatives to enhance our system. Such initiatives included establishing a clear risk management process as described under the “Risk Management Functions – second line of defence” on page 168.

To enhance the usefulness and relevance of operational risk registers, a formalised and coordinated procedure for semi-annual updating and reporting was adopted in

2014 for implementation since January 2015. The meeting schedule of the GRC was also revamped, with two of the four regular meetings dedicated to discussing emerging and risk mitigation issues, while the remaining two regular meetings to focus on discussion of semi-annual Group Risk Management Reports.

We also continued to monitor all incidents reported through the Incident Reporting Policy as described in Risk Management Functions on page 168 and the actions taken and best practices shared. There was no incident of a material nature in 2014 which needed to be brought to the attention of the shareholders.

Other various activities of the GRC in 2014 include:

- ✔ Reviewed Group Risk Management Reports prepared by ARM including the Group’s Risk Profile Report, for submission to GMB, then Audit Committee and the Board for approval
- ✔ Nine new local operations risk registers were successfully established and in active use, including The Peninsula Paris which opened in August 2014. By end of 2014, a total of 21 local risk registers has been put in place
- ✔ Since early 2014, the Company commenced the implementation of a single central enterprise risk management system to automate the Group’s risk management process and to assist operations in capturing, managing and reporting key risks and incidents. The online incidents management module was deployed in December 2014 across all Hong Kong operations of the Group, while the risk register module is expected to be launched in 2015
- ✔ In response to the civil protests in Hong Kong, a comprehensive response protocol was successfully prepared and utilised in response to the crisis at corporate office and for Hong Kong operations
- ✔ Reviewed Ebola virus threat risk assessment. Group-wide response directives released by corporate office
- ✔ Reviewed the progress of follow-up actions on recommendations in integrated property, safety and security risk reports of external third party specialists on all Asian operations
- ✔ Engaged external third party specialists to conduct integrated property, safety and security risk reviews of our US operations in New York, Chicago and at Monterey Peninsula, California
- ✔ Reviewed security procedures for protecting the Group information technology infrastructure
- ✔ Reviewed alternative insurance strategies including feasibility of captive insurance vehicles

PRINCIPAL RISKS

A summary of the Group's principal risks is presented below. This summary is compiled through aggregation, filtering and prioritisation of the risks from a Group's perspective, taking into account each of the Group's operation's detailed risk registers. The process for compiling the principal risks faced by each operation includes multiple interviews and validations with risk owners of the operation concerned. In addition, in 2014, all members of senior management were interviewed to review the principal risks profile of the Group.

The risk review process provides an opportunity to highlight emerging risks and/or include new risks to the risk registers. The risk registers also track movements of risks and their specific ratings across the Group, contributing to ensuring their proactive management.

PRINCIPAL RISKS	KEY CONTROLS AND MITIGATING FACTORS
<p>ACQUISITIONS, INVESTMENTS AND DEVELOPMENTS⁽¹⁾</p> <p>Acquisitions, investments and developments of properties carry inherent risks. These are often pursued in partnership with third parties. Risks related to meeting budgets, incurring debt, missing targets, partnership relationships and competition for resources will need to be managed. Challenges may arise in relation to obtaining planning or other consents and compliance with different jurisdictions' design and construction standards</p>	<ul style="list-style-type: none"> • Engagement with experienced and reputable local partners, and familiarisation with local authorities • Adequate due diligence to be conducted for each project • Developing complete and detailed integration plans and business strategies • Continuous monitoring and review of all aspects of developments, planning and construction progress • Involvement of Legal and Audit & Risk Management Departments to monitor legal, regulatory and internal policy compliance of our projects and developments assisted by external professionals
<p>BRAND AND REPUTATION⁽¹⁾</p> <p>Failure to protect the Group's brand and reputation from significant adverse publicity in media, social media or elsewhere could result in a loss of confidence in our brand, a decline in guest, tenant and/or customer base, and affect our business and our ability to recruit and retain good people</p>	<ul style="list-style-type: none"> • Care in staff recruitment and training to bring forth the level of service that is befitting of our brand • Our Code of Conduct and behavioural standards regulate staff conduct • Supplier Code of Conduct implemented to mitigate risks relating to labour standards and product integrity • Clear guidelines on incident communication and crisis management process by Crisis Management team • Implementation of Group-wide social media usage guidelines
<p>COMPETITION⁽¹⁾</p> <p>Increased competition, cyclical over-supply of luxury hotels in some markets could also harm our business</p>	<ul style="list-style-type: none"> • Continuously monitor and analyse competitive and market information in order to anticipate unfavourable changes • Brand and communication initiatives to drive revenue growth and strengthen our brand's market position • Reinvestments into our properties to ensure competitiveness

PRINCIPAL RISKS

KEY CONTROLS AND MITIGATING FACTORS

BUSINESS PORTFOLIO/ CONCENTRATION⁽¹⁾

A significant portion of our Group revenues is derived from our operations in Hong Kong. Unfavourable events in the city could disrupt our overall business, lower our revenues, and impact the valuation of our assets

- Focus on increase of overseas revenue, including entering new markets
- Continuous monitoring of the operating and political environment of Hong Kong to anticipate issues for possible adjustment of any business activities promptly

DISASTER EVENTS⁽²⁾

A major disaster event, such as an incident, "Act of God," natural disaster, terrorist activity, war or contagious diseases such as Avian Flu, SARS and Ebola could impact on our assets, business levels, level of travel activity, and therefore our ability to conduct business, and reduce earnings

- Comprehensive insurance coverage for properties and businesses
- Multiple risk inspections by external risk consultant on selected properties focusing on insurable risks
- Crisis Response Plan rolled out across all operations to ensure business continuity

MACROECONOMIC AND POLITICAL⁽²⁾

Changes and volatility in general economic conditions, including the severity and duration of any downturn in the USA, Europe or global economy and financial markets, decreased corporate budgets and spending could impact our business

Political instability and uncertainties, including actions or interventions impacting hospitality and travel related activities, could impact travel patterns and guest spend

- Focus on spreading business area, including entering new markets
- Continuous monitoring of the macroeconomic, political and regulatory landscape in all our key markets to anticipate issues for possible adjustment of any business activities promptly
- Crisis Response Plan rolled out across all operations to ensure business continuity

DATA PRIVACY⁽³⁾

Given our wide guest base and global operations, we are regulated by privacy laws and regulations of many jurisdictions, compliance with which could increase our operating costs and impact our direct marketing abilities. Breaches could result in fines and lawsuits and may adversely affect our brand and business

- Implementation of Group-wide data privacy manual and training (classroom and online formats)
- Implementation of a process for escalation and management of data breaches
- Investment in information technology infrastructure, application and staff training to protect personal data
- Management of risks via e-Commerce functions at operational level

Data Privacy & Security has also been identified as a material sustainability issue of relatively high concern by external and internal stakeholders of the Company, as reported in our Sustainability Materiality Matrix (please refer to page 60 for further detail)

PRINCIPAL RISKS	KEY CONTROLS AND MITIGATING FACTORS
<p>RETAIL AND COMMERCIAL TENANTS⁽⁴⁾</p> <p>Commercial letting may become difficult due to factors such as decline in spend within the luxury industry, increased competition, or shifts of retail preferences leading to decrease in our arcade traffic</p>	<ul style="list-style-type: none"> • Improvements in design of commercial space to allow flexible usage and conversion possibilities to accommodate tenants • Commitment to maintain high quality properties • Active engagement with current and potential tenants • Diversification and maintenance of an appropriate mix of tenants
<p>PROPERTY/CAPITAL FUNDING⁽⁴⁾</p> <p>Failure to ensure the availability of funds to meet our capital expenditure requirements to develop, maintain and renovate our properties could limit our ability to remain competitive</p>	<ul style="list-style-type: none"> • On-going regular reviews of hardware standards • Continuous monitoring of furniture, fixture and equipment budget and spend by operations • Regular cash and treasury management and monitoring of allocation of funds and resources
<p>HEALTH AND SAFETY⁽⁴⁾</p> <p>Failure to timely address health and safety issues or comply with laws and regulations that regulate our operations, merchandise and the properties we own and manage could expose us to costs and liabilities and result in damaged trust in our business</p> <p><i>Food Safety & Hygiene, and Health & Safety of Employees and Guests have been identified as material sustainability issues of high concern by external and internal stakeholders of the Company, as reported in our Sustainability Materiality Matrix (please refer to page 60 for further detail)</i></p>	<ul style="list-style-type: none"> • Risks reviewed by management during monthly Safety Meetings and action plans are developed to address any areas of concern; measures deployed to prevent recurrence • Certification of the health and safety of our premises against relevant standards where possible and hiring or training staff with/for certification on health and safety • Policies and procedures on handling food, waste, and any hazardous materials • Supplier Code of Conduct to mitigate risks relating to product integrity • Continued improvements in Occupational Safety and Health programs
<p>LABOUR AND MATERIAL COST⁽⁴⁾</p> <p>Rising labour and material costs while we operate in a highly competitive environment will continue to be a major challenge for our business. Failure to manage our costs, such as payroll and benefits, new taxes and social insurance charges, could adversely affect our business</p>	<ul style="list-style-type: none"> • Close monitoring and management of operating costs, including payroll costs, new taxes and social insurance charges • Strategies to enhance our bargaining power with markets and suppliers • Professionals engaged to advise on labour related costs and liabilities

PRINCIPAL RISKS

KEY CONTROLS AND MITIGATING FACTORS

SECURITY AND INFORMATION TECHNOLOGY⁽⁴⁾

Our reputation and financial performance may be adversely affected if we fail to maintain appropriate security measures, including security over our information systems, to protect our guests, visitors and employees. The threat of terrorism, criminal acts, and fire incidents continue to be a significant concern for the hospitality industry

- Dedicated Security & Operational Risk teams work with local management to ensure there is adequate level of security in our operations
- Detailed threat and vulnerability assessments and tests are carried out at selected sites
- Crisis Response Plan rolled out across all operations to ensure business continuity
- Technical robustness of our information systems regularly reviewed by Information Technology Department, including engaging third parties to conduct independent tests

Notes:

Risk Category

(1) Strategic risks – risks relating to the Group's business model and strategy

(2) External risks – risks relating to external factors such as the economy, political developments and disaster events

(3) Compliance risks – relating to legal, regulatory and stakeholders considerations

(4) Operational risks – relating to operations, our properties, people and processes

EMERGING RISKS

In addition to addressing the principal risk categories faced by the Group, GRC also reviewed specific emerging risks. These emerging risks are normally results of changes in the economic, political, legal or technical environment, which may or may not be within an existing principal risk category. GRC recognises that the potential impact of such emerging risks may be significant and would monitor the potential impact to the Group, along with mitigating action plans.

In 2015, the GRC's main focus will be to ensure the smooth implementation and continued refinement of the improved Group-wide risk management process. We will also continue to monitor the status and progress of the action plan against each risk.

On behalf of Group Risk Committee



Alan Clark

Chairman of the Group Risk Committee

20 March 2015