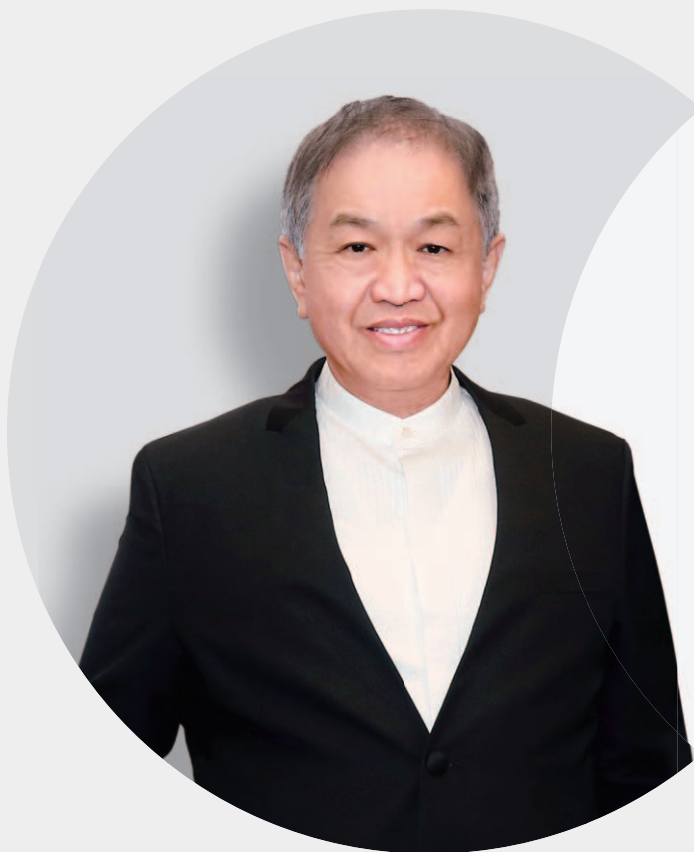


# CHAIRMAN'S STATEMENT



**In the longer term, we envisage an investment pipeline which includes the further replacement of coal-fired generating units by gas-fired units and other supporting infrastructure.**

## PREPARING FOR A GREEN ENERGY FUTURE

It gives me great pleasure to present the financial and operating results for HKEI in 2016.

This year we continued to achieve a balance between shareholder and customer value, with stable distribution to holders of our Share Stapled Units (SSU), while reducing our tariffs across the board. Following the 2016 tariff reduction we have announced further cuts for 2017, delivering savings of over 17% on average for all customers, thanks to lower-than-expected fuel costs. These cuts follow a two-year tariff freeze and have enabled us to go over and above our 2013 pledge to keep tariffs unchanged for five years till end 2018.

Over the years, it is clear that the world's energy needs have evolved: the need is now for reliable and accessible energy that is also environmentally friendly. One of our key strategies to achieve this in the immediate term is through a significant increase in the use of natural gas for generation. In 2015, we had begun the work of increasing gas-firing

generation capacity with the construction of a new gas-fired generating unit, L10 at Lamma Power Station (LPS). In September 2016, we secured Government approval for another such unit, L11, and have already commenced with preparation works for its construction.

In the longer term, more efforts would be required to support the Government's Climate Action Plan 2030+ which sets out an aggressive target to reduce Hong Kong's carbon intensity by 65-70% in 2030 compared to the 2005 level. We envisage an investment pipeline which includes the further replacement of coal-fired generating units by gas-fired units and other supporting infrastructure.

## FINANCIAL RESULTS AND DISTRIBUTIONS

For the year ended 31 December 2016, HKEI's EBITDA was HK\$8,034 million (2015: HK\$8,035 million) and audited profits attributable to SSU holders was HK\$3,599 million (2015: HK\$3,591 million).

## CHAIRMAN'S STATEMENT

The Board of the Trustee-Manager has declared a final distribution by the Trust of HK20.12 cents (2015: HK20.12 cents) per SSU, payable on 19 April 2017 to SSU holders whose names appear on the Share Stapled Units Register on 6 April 2017. This, together with the interim distribution of HK19.92 cents (2015: HK19.92 cents) per SSU, amounts to a total distribution of HK40.04 cents (2015: HK40.04 cents) per SSU for the year.

### INFRASTRUCTURE FOR INCREASED GAS-FIRED GENERATION TO COMBAT CLIMATE CHANGE

In 2015, following an extensive public consultation exercise, the Hong Kong Government released its fuel mix strategy for the energy sector. It mandated an increase in local gas-fired generation to about 50% of total output in 2020 which we fully support. In 2016, we progressed with several key initiatives to reach this target.

We will consecutively install two new gas-fired combined cycle generating units, L10 and L11, at LPS, our primary generating facility, to replace retiring coal-fired and gas-fired units. Construction of the L10 unit is progressing well with the superstructure construction set to commence on schedule for commissioning of the unit in 2020. Preparations for the newly approved L11 unit are underway with piling work having commenced at end 2016. When L11 is commissioned in 2022, our gas-firing generation capacity will rise to about 55% of total output which will help reduce emissions further. We are excited about these projects and are confident that they will be completed on time and within budget. Other coal-fired units at LPS are coming to the end of their useful lives and need to be replaced by gas-fired units before the end of the next decade.

In October 2016, the Hong Kong Government's Sixth Technical Memorandum was published. The annual emission allowances of sulphur dioxide (SO<sub>2</sub>), nitrogen oxides (NO<sub>x</sub>) and respirable suspended particulates (RSP) are further tightened by 8%, 2% and 10% respectively for HK Electric from 2021 onwards. Our expanded gas-firing capacity as well as other emission control measures will enable us to meet these tightened allowances.

To maintain supply reliability while increasing gas-firing generation capacity, it is imperative to secure the supply chain. Hong Kong at present lacks storage facilities for

natural gas imported by sea, which also affects our negotiating power with international gas suppliers. To address this gap, we are, in partnership with CLP Power Hong Kong Limited, jointly exploring the feasibility of siting an offshore liquefied natural gas terminal using floating storage and regasification unit technology (FSRU). The terminal, if and when built, will serve the electricity sector as a whole. An Environmental Impact Assessment (EIA) began during the year. If the Government approves the EIA report and the project in time, the terminal is scheduled for commissioning in 2020.

### CONSISTENT PERFORMANCE ACROSS ALL PARAMETERS

While preparing for the future we continued to excel on all operating parameters in 2016.

Supply reliability was maintained at over 99.999% for the twentieth consecutive year and unplanned power interruption per customer was under one minute for the eighth consecutive year. I am gratified to note that we, once again, met or surpassed all eighteen customer service pledges, as we continue to offer customers reduced tariffs in response to softer fuel prices. Electricity sales in 2016 declined slightly by 0.8% as a result of conservation efforts across the community.

In preparation for the expansion of our gas-firing generation capacity, security and reliability enhancement works were carried out on the gas receiving station at LPS. On the transmission and distribution front, proactive network enhancement and improvement projects were implemented, to maintain high standards with respect to system reliability and power quality, and new equipment was commissioned for provision of new supply. Equally, we remained a prudent and mindful consumer of energy in our office buildings and across our fleet of company vehicles.

We believe that Electric Vehicles (EVs) have great potential to reduce roadside emissions. Our own fleet has over a hundred EVs. We were the official energy partner for the first Hong Kong ePrix held in October 2016, helping increase awareness that EVs are powerful enough to make it to the racing circuit. Other initiatives during the year included EV charging advisory services for buildings and the continued provision of free charging facilities in public carparks.

We once again outperformed all statutory emissions caps in 2016 and continued to encourage and educate the public on energy efficiency and environmental awareness through our community involvement programmes such as the Green Hong Kong Green and Smart Power Campaign. We offered energy audit advisory services for non-residential customers and funded energy improvement works at older residential blocks through the Smart Power Fund.

We remain an employer of choice, offering a healthy work-life balance, stimulating opportunities and planned career progression to employees from recruitment to retirement. I am honoured that we were ranked one of the Top 10 Most Attractive Employers in Hong Kong by Randstad.

Our involvement in the community remained unwavering, as our dedicated team of volunteers offered their time and expertise to the causes close to our hearts; such as supporting the vulnerable elderly, participating in community-wide initiatives and educating the public on conserving the environment. We pressed ahead with our efforts to minimise the amount of waste we produced and recycled unavoidable waste.

## REGULATORY FRAMEWORK FOR A STABLE SECTOR

One of the priorities for the Hong Kong Government during this period is to set the regulatory framework that will drive the sector upon the expiry of the current Scheme of Control Agreement (SCA). Responses to a public consultation on the future development of the electricity market conducted in 2015 indicated that the majority of the community felt the current arrangement should be maintained. We share this view.

The SCA framework has worked well and allowed the fulfillment of the Government's energy policy objectives of safety, reliability, affordability and environmental protection. It has been effective in balancing the interests of consumers and industry players, appropriately incentivising the long-term investments necessary to evolve Hong Kong's electricity infrastructure to meet the needs of the 21st century particularly in addressing climate change and air quality concerns.

On this note, we are encouraged by the reasonably good progress that has been made in our ongoing deliberations

with the Government over the future regulatory framework. The discussion is in an advanced stage now with both sides acknowledging the need for an early agreement with which HK Electric will be able to make timely investments to achieve the Government's energy and environmental objectives.

## OUTLOOK

With socio-economic uncertainties likely to prevail in Hong Kong and around the world, it is important to conclude the deliberations over the future shape of the regulatory framework for the power industry, as early as possible. A secure regulatory environment and a reasonable rate of return are crucial for industry players to make appropriate investments to maintain a high-quality, affordable and cleaner supply of electricity. This is particularly pertinent in the case of HK Electric with the impending retirement of many of our coal-fired units and the pressing need to reduce Hong Kong's air emission and improve its carbon footprint.

Another key priority will be the smooth construction and completion of the three large infrastructural projects for the two new gas-fired generating units and the FSRU which will contribute greatly to Hong Kong's green energy future.

Our expanded use of natural gas for power generation will increase our fuel costs from 2020, in turn exerting pressure on tariffs. We will plan appropriate measures to minimise the impact of these future increases on our customers.

To honour Hong Kong's commitments in the COP 21 agreement, the community as a whole needs to work to improve energy efficiency in both private and public life. We will work with the Government, and also intensify our community engagement efforts, adopting both best practice from overseas and developing our own measures applicable to the unique conditions of Hong Kong.

As always, I would like to thank our staff for their excellent service and the constant "can do" approach. Their skills, attitude and dedication are central to our continued success.

## Fok Kin Ning, Canning

Chairman

Hong Kong, 21 March 2017