

# GROUP RISK COMMITTEE REPORT

 <b>Composition:</b>	<p>Chairman Mr Matthew Lawson, Chief Financial Officer</p> <p>Members Group General Manager, Audit &amp; Risk Management Select members of senior management Senior Vice President, Operations, The Peninsula Hotels</p>
 <b>Meeting Frequency:</b>	<ul style="list-style-type: none"> <li>Quarterly</li> <li>Four meetings in 2018</li> </ul>
 <b>Responsibilities:</b>	<ul style="list-style-type: none"> <li>To identify and assess the principal risks at group level and their corresponding mitigating treatments, as well as monitor the actions required for critical and major incidents within the group</li> <li>To facilitate the process whereby each operation and project defines its business objectives, addresses the risks identified, conducts self-assessment of internal control activities and tracks progress of mitigating plans</li> <li>To regularly review, assess and update the group risks and related contingency plans to Group Management Board (GMB) for further review by the Audit Committee and the Board</li> </ul>

The group's enhanced risk management process has formed a solid platform for us to focus on control effectiveness assessment and proactively address issues before they escalate.

A series of risk workshops were conducted in 2018, either in a face-to-face seminar or webinar format, with over 200 senior employees across all operations. Major topics of the workshops included an explanation of the group's risk management philosophy, an introduction of the enhanced risk management methodology and a brainstorming session on emerging risks arising from changes in internal and external environments.

In addition, we have improved the effectiveness of our controls in the following focus areas in 2018:

### Investment and project development risks

The Group Risk Committee (GRC) continued to monitor the risk governance process and review the key risks surrounding The Peninsula London, The Peninsula Istanbul, The Peninsula Yangon and The Peak Tram upgrade every quarter. Moreover, a project owner's risk register was set up during the year to facilitate the identification and management of risks that the group was facing as the owner of the three new hotels. Furthermore, pre-opening plans are being developed and implemented.

### Risk engineering survey

Our owner-operator business model is a capital intensive one and high attention is paid to protect and maintain our assets. To improve our assets' structural and engineering controls, our consultant has completed the second three-year cycle of risk engineering surveys in all our major properties during the year. Comparison of controls maturity across properties and sharing of best practices among the group will be conducted in 2019. Such comparison will assist us in formulating the next three-year plan by prioritising properties with a lower maturity to be inspected earlier in the upcoming cycle.

## 5-Step Risk Management Methodology



The 5-step risk management methodology continues to be applied across the group. Furthermore, in 2018, we enhanced our methodology with a focus on risk identification and analysis by finetuning our risk concepts, and further treatment by considering the effectiveness of the mitigating controls.



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Matthew Lawson  
Chairman of  
the Group Risk Committee  
14 March 2019

### Security and operational risk capability assessment

Guest safety is a priority for management. To provide the highest level of security in our operations and ensure consistency in execution, the Security & Operation Risk Department rolled out a new Group Security Policy Statement, Group Standard Operating Procedures and Group Crisis Management Plan to all hotel operations in 2018, with reference to ISO31000 Risk Management. Gap analyses between existing practices and the new standard were performed in nine hotels during the year. Recommendations to enhance security measures were communicated to management at the operations and undertaken where possible.

### Cybersecurity and data privacy

A variety of further improvements have been carried out by the Information Technology Department and Legal Department throughout the year to strengthen our controls over cybersecurity and data privacy. These included penetration testing, gap assessment on Payment Card Industry compliance, online security training and phishing awareness exercises. Furthermore, in response to the implementation of the General Data Protection Regulation (GDPR) in the European Union, a GDPR Info Hub has been launched in the group's intranet to provide information updates, recommended workflows and processes to ensure compliance across operations.

## Principal Risks

The Board, with support from the Audit Committee and the GRC, has assessed the principal risks facing the group, taking into account those that would impact its strategies, future performance and long-term objectives.

Our principal risks are compiled through prioritisation of risks from a total group perspective. This process includes an ongoing review by GMB of the most significant risks facing the group, and the identification and evaluation of potential new risks.

### Understanding why and how our principal risks change

The ongoing review of the most significant risks faced by the group focuses on how changes may arise and how our controls need to be adapted in response to changing business conditions and organisational changes.

The movement of our principal risks since the publication of our 2017 Annual Report are shown on the next page.

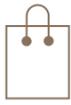
## Emerging Risks

The aggravation of income inequality in the cities we operate could impact economic growth, the desirability for people to work in the hospitality industry and society's perception of our brand. We will continue to monitor the latest development in our societies and ensure our labour practices are the best in class.

### 2019 Major Initiatives

In 2019, the GRC's main focus will continue to be on (i) enhancement of internal controls to manage the strategic risks of the group; (ii) further improvements to 5-step risk management methodology to other areas of the group such as the functional divisions and (iii) a focus on communication, awareness and ownership of risks and controls across the group.

# Group Risk Committee Report

Investment and Development Projects					
<p><b>1</b></p>  <p><b>INVESTMENT AND DEVELOPMENT PROJECTS</b></p>	<p><b>What is the risk?</b></p> <p>Investment and development of properties carries inherent risks. Risks relating to capital allocation, funding, meeting budgets, project milestones, partnership relationships and competition for resources need to be managed. Challenges may arise in relation to obtaining planning or other consents and compliance with different jurisdictions' design and construction standards. Post construction, pre-opening and opening challenges also exist when entering new markets.</p>	<p><b>What is the impact?</b></p> <p>May result in a major impact on our capital, partnership relationships and reputation.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>Enhanced due diligence and a transparent tendering process throughout the construction procurement phase so as to mitigate potential escalation of construction costs</li> <li>Partnerships with experienced and reputable local partners</li> <li>Individual and aggregated Investment/development-related risk levels and a robust risk management process with an oversight by GRC</li> <li>Continuous monitoring and review of all aspects of a development and reporting on potential project risks</li> <li>Business stress testing under various downside scenarios</li> <li>Development of pre-opening plans, hiring of dedicated resources, enhancing resources in our Operations Planning &amp; Support Department in advance of hotel openings</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Increased</p> <hr/> <p><b>Why?</b></p> <p>Continued investment in London, Istanbul and Yangon and The Peak Tram as these projects move into construction phases</p>	
Cybersecurity					
<p><b>2</b></p>  <p><b>CYBERSECURITY</b></p>	<p><b>What is the risk?</b></p> <p>Financial loss, business disruption, damage to reputation from failure of information technology systems due to internal or external circumstances, either malicious or unintentional.</p>	<p><b>What is the impact?</b></p> <p>Inability to operate effectively may result in a loss of information and unavailability of critical systems. Significant costs may be incurred for data recovery and system restoration, and/or possible financial or other regulatory penalties, and the need to maintain reputational risk.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>Increased resources deployed for information technology security and risk</li> <li>Roll out of a group-wide online security awareness training</li> <li>Ongoing review of business-critical applications for disaster recovery plan and regular vulnerability assessments and penetration tests</li> <li>Systematic due diligence for third party solution/service providers</li> <li>Strengthen account authentication and password management for all employees</li> <li>Continued to enhance security measures and adopt cyber insurance against potential loss</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Increased</p> <hr/> <p><b>Why?</b></p> <p>Number of cybersecurity incidents increased globally in 2018</p>	
Data Privacy					
<p><b>3</b></p>  <p><b>DATA PRIVACY</b></p>	<p><b>What is the risk?</b></p> <p>Our business involves handling a large amount of personal data and given the nature of our global operations, we are regulated by privacy laws and regulations in all jurisdictions. We are also at risk from breaches occurring within our vendor network.</p>	<p><b>What is the impact?</b></p> <p>Compliance could increase our operating costs and impact our ability to directly market. Breaches, either through deliberate targeted actions or inadvertent errors, may adversely affect our brand and business and may result in regulatory investigations and potential fines.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>Continuous monitoring of privacy laws and regulations to enhance our data privacy policies and practices</li> <li>Revamped data privacy compliance programme in light of GDPR and conducted training to the Board and senior management, data privacy teams at operations and selected employees</li> <li>Maintenance of a comprehensive data register across the group covering all applications which collect and store personal information</li> <li>Ongoing communication and risk assessments with Data Privacy teams across operations</li> <li>Promoting employees' overall awareness from data capture standards, reporting channels and workflows for data processing requests and data breaches</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Increased</p> <hr/> <p><b>Why?</b></p> <p>Global trend of tightening privacy laws such as GDPR has increased compliance obligations. The rise in cybercrime also exposes us to higher risk of data security breaches</p>	
Retail Tenants					
<p><b>4</b></p>  <p><b>RETAIL TENANTS</b></p>	<p><b>What is the risk?</b></p> <p>Retail letting has become more difficult due to factors such as the increased proliferation of e-commerce changing consumers' shopping habits from offline to online, general decline in spending in the luxury segment, shifts in consumer preferences, and increased competition.</p>	<p><b>What is the impact?</b></p> <p>Revenue from our retail arcades may be under pressure.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>Identification of exclusive niche retail brands and creation of exclusive VIP or concept stores that benefit from co-locating within a Peninsula hotel</li> <li>Proactively working with tenants to jointly develop marketing and incentive plans to drive traffic and repeat customers</li> <li>Improvements in the utilisation of floor space to allow flexible usage and conversion possibilities to accommodate tenants</li> <li>Seasonal and tactical campaigns held at the three properties across Greater China to stimulate spending</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Remains broadly the same</p> <hr/> <p><b>Why?</b></p> <p>Continuation of the mentioned challenges</p>	

## Group Risk Committee Report

					Business Portfolio/Concentration	
<b>5</b>  <b>BUSINESS PORTFOLIO/ CONCENTRATION</b>	<b>What is the risk?</b> <p>Owing to the origin of the company, a significant portion of our group earnings is derived from our operations in Hong Kong.</p>	<b>What is the impact?</b> <p>Unfavourable events (e.g. pandemic, terrorism, natural disaster) in the city could severely disrupt our overall business, lower our revenues, and impact the valuation of our assets.</p>	<b>How do we manage it?</b> <ul style="list-style-type: none"> <li>• Focus on increasing overseas earnings contribution</li> <li>• Ongoing focus to strengthen our brand globally and in Hong Kong, being prepared to make prompt adjustment to our business strategies when necessary</li> <li>• Maintain comfortable level of gearing</li> </ul>	<b>Risk movement in 2018</b> <p>Remains broadly the same</p>	<b>Why?</b> <p>Group earnings still predominantly derive from Hong Kong operations despite increased contribution from the recently renovated The Peninsula Chicago and The Peninsula Beijing</p>	
					Competition	
<b>6</b>  <b>COMPETITION</b>	<b>What is the risk?</b> <p>Cyclical over-supply of luxury hotels and increased competition poses a significant competitive pressure to the business.</p>	<b>What is the impact?</b> <p>May result in a decline in market share, revenue and profit, and reduce partnership opportunities.</p>	<b>How do we manage it?</b> <ul style="list-style-type: none"> <li>• Drive revenue growth and strengthen our brand by continuously improving our product and developing unique guest experiences</li> <li>• Increased focus on digital marketing and e-commerce opportunities, recruitment of digital talent to contribute to the company's digital transformation</li> <li>• Continuously monitor and analyse competitive and market information in order to anticipate unfavourable changes</li> <li>• Increased focus on engaging directly with customers rather than through third party channels</li> <li>• Continue to focus on strengthening our people development platforms through training and cross exposure opportunities and promotions</li> </ul>	<b>Risk movement in 2018</b> <p>Remains broadly the same</p>	<b>Why?</b> <p>Competition level remained high during the year</p>	
					Disaster Events	
<b>7</b>  <b>DISASTER EVENTS</b>	<b>What is the risk?</b> <p>A major disaster, such as a natural catastrophe, extreme weather due to climate change impact, war or contagious diseases could impact our assets, business levels, level of travel activity, and therefore our ability to conduct business.</p>	<b>What is the impact?</b> <p>Major disaster events, although rare, may result in a severe impact on our customers, revenue and reputation.</p>	<b>How do we manage it?</b> <ul style="list-style-type: none"> <li>• Enhanced risk engineering control process by external risk engineering consultant and group engineering team on selected properties focusing on insurable risks</li> <li>• Launched Group Security Operational Risk Framework to standardise the group's approach to security and operational risks management in accordance with ISO31000</li> <li>• Performed gap analysis for all hotels to design a bespoke plan on how to align their current practice with the global framework and the timeline for implementation</li> <li>• Established a group level crisis command centre in Hong Kong to assist with global crisis</li> <li>• Deployed threat management platform collating and analysing security intelligence from both open and closed sources</li> <li>• Comprehensive property damage, business interruption and terrorism insurance scheme</li> </ul>	<b>Risk movement in 2018</b> <p>Slightly Increased</p>	<b>Why?</b> <p>Rising likelihood of occurrence of extreme weather conditions such as super typhoons in Hong Kong due to climate change</p>	

# Group Risk Committee Report

Foreign Exchange, Interest Rate and Funding Risk				
<p><b>8</b></p>  <p><b>FOREIGN EXCHANGE, INTEREST RATE AND FUNDING RISK</b></p>	<p><b>What is the risk?</b></p> <p>Exchange rate fluctuations could result in significant foreign currency losses and affect our capital projects. Significant floating rate liabilities could result in higher cost of financing if current interest rates increase.</p>	<p><b>What is the impact?</b></p> <p>May impact our refinancing requirements and increase our cost of capital.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>• Operations predominantly charging in local currencies and expending in local currency to minimise currency mismatch</li> <li>• The majority of borrowings are typically denominated in the functional currency of the operations to which they relate</li> <li>• Regular stress testing (ad hoc for projects, and yearly for the group's financial reporting)</li> <li>• Actively managing fixed/floating interest rate exposure</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Slightly Increased</p> <hr/> <p><b>Why?</b></p> <p>Depreciation in RMB and rising interest rates</p>
Macroeconomic and Political				
<p><b>9</b></p>  <p><b>MACROECONOMIC AND POLITICAL</b></p>	<p><b>What is the risk?</b></p> <p>A global or regional economic downturn could lead to a reduction of global or country-specific travel activity, changes of travel patterns or business operating procedures.</p>	<p><b>What is the impact?</b></p> <p>May result in a decline in profit and cashflow, while inflation and currency fluctuation may increase operating costs. Changes to regulations may result in higher legal and compliance costs.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>• Diversification in terms of number and location of assets and target market segments we pursue</li> <li>• Continuous monitoring of macroeconomic, political and regulatory landscape</li> <li>• Close monitoring of operating costs and implementation of cost savings measures when required</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Remains broadly the same</p> <hr/> <p><b>Why?</b></p> <p>Macroeconomic and political risks in our operating locations remain at a similar level of uncertainty, particularly with the ongoing trade tensions between US and China</p>
Brand and Reputation				
<p><b>10</b></p>  <p><b>BRAND AND REPUTATION</b></p>	<p><b>What is the risk?</b></p> <p>Adverse publicity in traditional or social media, which may be frivolous or misconceived, but could still result in brand and reputational damage.</p>	<p><b>What is the impact?</b></p> <p>May lead to a decline in loyalty of existing guests, tenants and/or customers, and impairment of the ability to attract new customers. It may also result in a decline of ability to recruit and retain talent, and increased cost for crisis management and potential legal costs.</p>	<p><b>How do we manage it?</b></p> <ul style="list-style-type: none"> <li>• A continuous effort on corporate branding, both in traditional media and digital platforms</li> <li>• Clear guidelines on incident communication and crisis management processes by Crisis Management team with clear roles and responsibilities for each operation</li> <li>• Implementation of group-wide social media usage guidelines to ascertain appropriate behaviour online when representing the company or commenting on social media posts</li> <li>• Our Code of Conduct and behavioural standards and policies which regulate staff and guests conduct emphasises the zero-tolerance of abusive behaviour and misconduct by staff or guests, and provide clear guidelines on the escalation process</li> <li>• Increased focus on employer branding to ensure awareness of HSH being a reputable listed company and considerate employer</li> </ul>	<p><b>Risk movement in 2018</b></p> <p>Remains broadly the same</p> <hr/> <p><b>Why?</b></p> <p>Reputational risk still exists, as data privacy and sexual harassment remained topical throughout the year</p>