CHAIRMAN'S STATEMENT

The Year's Results

The performance of the Group's gas business in Hong Kong remained steady in 2012. In comparison, the Group's city-gas businesses in mainland China thrived, continuing to record good profit growth; concurrently emerging environmentally-friendly energy businesses are being developed at a fast pace. As anticipated, the combined results of the Group's emerging environmentally-friendly energy and mainland utility businesses were higher than those of its Hong Kong gas business for the year 2012.

Profit after taxation attributable to shareholders of the Group for the year amounted to HK$7,727.9 million, an increase of HK$1,578.3 million compared to 2011. Earnings per share for the year amounted to HK88.9 cents, an increase of 25.7 per cent over 2011. Profit growth in 2012 was mainly due to growth in profit of mainland businesses, a revaluation surplus from the International Finance Centre ("IFC") complex and a one-off net gain. Profit after taxation attributable to shareholders of the Group, excluding revaluation surplus from the investment property, amounted to HK$6,333.4 million.

During the year under review, the Group invested HK$5,905.5 million in production facilities, pipelines, plants and other fixed and intangible assets for the sustainable development of its various businesses in Hong Kong and mainland China.

Gas Business in Hong Kong

Local economic growth slowed down in 2012 compared to 2011 under the impact of a weak global economy and low demand from European and United States markets. Despite this, tourism, restaurant and hotel sectors, still benefiting from an increase in the number of inbound tourists, continued to prosper. However, as the average temperature for 2012 in Hong Kong was slightly higher than 2011, overall gas sales were affected as a result, and total volume of gas sales in Hong Kong for the year increased only slightly by 0.8 per cent compared to 2011. Appliance sales for the year 2012 increased by 6.1 per cent compared to 2011.

As at the end of 2012, the number of customers was 1,776,360, an increase of 25,807, as forecasted, compared to 2011.

The Company's operating costs have been increasing over the past few years. Although the Company has been implementing cost saving and process re-engineering measures, such initiatives are no longer offsetting additional costs. Therefore the Company will raise its standard gas tariff by HK1 cent per megajoule with effect from 1st April 2013, which represents 4.6 per cent of the standard gas tariff, with a commitment to no further increase for this tariff in the coming two years.

Business Development in Mainland China

The Group's mainland businesses progressed well in 2012 in respect of the number of projects and profit.

The mainland economy continued to grow steadily during 2012 though the pace was slower compared with 2011 owing to the weak global economy and a downturn in domestic exports. The Group's city-gas and natural gas businesses, benefiting from both an increase in upstream natural gas supply and on-going economic advancement in certain regions on the mainland, recorded continuous growth during 2012. The Group's development of emerging environmentally-friendly energy projects, through its wholly-owned subsidiary ECO Environmental Investments Limited and the latter's subsidiaries (together known as "ECO"), is progressing well with ECO now at various stages of project investment, construction and gradual commissioning.

Mainland China's sustainable economic development is leading to a rise in internal demand for consumer goods, progressive urbanisation and an increasing demand for clean energy. These factors, coupled with improving upstream natural gas supplies, are creating good prospects and investment value for both city-gas and emerging environmentally-friendly energy businesses on the mainland in the long run. Furthermore, the Group's establishment of several data centre and telecommunications conduit system project companies, following the development of telecommunications businesses in both Hong Kong and the mainland over the last few years, is also contributing to diversification of the Group's businesses.

Overall, inclusive of projects of the Group's subsidiary, Towngas China Company Limited ("Towngas China"; stock code: 1083.HK), the Group had 150 projects on the mainland, as at the end of 2012, 12 more than at the end of 2011, spread across 22 provinces, municipalities and autonomous regions. These projects encompass upstream, midstream and downstream natural gas sectors, water supply and wastewater treatment sectors, natural gas vehicular filling stations, environmentally-friendly energy applications, energy resources, logistics businesses and telecommunications.

Diversification and an increase in the number of projects are rapidly transforming the Group from a locally-based company centred on city-gas businesses into a sizable, nation-wide, multi-business corporation with a focus on environmental protection, energy ventures and utility sectors.

Utility Businesses in Mainland China

The Group's city-gas businesses are progressing well, with seven new projects successfully established by Towngas China in 2012. As at the end of 2012, the Group had 107 city-gas projects in mainland cities spread across 20 provinces, municipalities and autonomous regions. The total volume of gas sales of these projects for 2012 was approximately 11,900 million cubic metres, an increase of 15 per cent over 2011, and at the end of the year the Group's gas customers on the mainland stood at approximately 14.82 million. The Group continues to be a large-scale city-gas enterprise with outstanding performance on the mainland.

With on-going completion of large-scale natural gas projects, including transmission pipelines from Sichuan province to eastern and southern China and phase two of the West-to-East pipeline, and an increase in the sources and quantity of imported and domestic liquefied natural gas, the shortfall in the mainland's natural gas supply in the past few years is now gradually being mitigated. Thus, with sufficient sources of gas supply, expanding pipeline networks and the public's aspiration for greater environmental protection, the Group anticipates its mainland city-gas businesses will continue to thrive in the future.

The Group's midstream natural gas projects are making good progress. These include high-pressure natural gas pipeline joint ventures in Anhui province, in Hebei province, in Hangzhou city, Zhejiang province and in Jilin province; the Guangdong Liquefied Natural Gas Receiving Terminal project; a natural gas valve station project in Suzhou Industrial Park, Suzhou city, Jiangsu province; and a new pipeline project in Henan province. Towngas China, the Group's subsidiary, also added a midstream pipeline project located in Wafangdian, Dalian city, Liaoning province to its portfolio in 2012. These kinds of high-pressure, natural gas pipeline projects generate good returns and help the Group develop and strengthen its downstream city-gas markets.

As at the end of 2012, the Group had invested in and was operating four water projects, all of which are progressing well. These include water supply projects in Wujiang district, Suzhou city, Jiangsu province and in Wuhu city, Anhui province; and an integrated water supply and wastewater joint venture project, together with an integrated wastewater treatment project for a special industry, in Suzhou Industrial Park, Suzhou city, Jiangsu province. During the first quarter of 2013, the Group successfully added a water supply project in Zhengpugang Xin Qu, Maanshan city, Anhui province to its portfolio, making a total of five water projects in hand.

Operation and management of businesses encompassing city-gas, city-water and midstream natural gas projects create positive synergy and mutual advantages. Furthermore, these businesses generate stable income and high environmental benefits, with room for expansion. The Group will therefore keep on looking for opportunities to invest in high-quality utility projects on the mainland.

Emerging Environmentally-friendly Energy Businesses

ECO's two major businesses in Hong Kong – an aviation fuel facility, servicing Hong Kong International Airport, and dedicated liquefied petroleum gas ("LPG") vehicular filling stations – are operating smoothly. Total turnover for the aviation fuel facility for 2012 was 5.56 million tonnes of aviation fuel, providing a safe and reliable fuel supply for Hong Kong International Airport. In comparison, the profit margin for ECO's filling station business for 2012 was lower than in 2011 due to the impact of rising petroleum gas prices.

ECO's vehicular clean energy business on the mainland mainly focuses on the use of compressed or liquefied natural gas to replace diesel in order to conserve energy, reduce emissions and create economic benefits by saving on fuel costs. After several years of development, a network of filling stations established by ECO is gradually taking shape in Shaanxi, Shanxi, Shandong, Henan and Liaoning provinces mainly servicing heavy-duty trucks. As at the end of 2012, nine filling stations were in operation and another five under construction. Further expansion of this business into other provinces is expected. By increasing the number of filling stations, the brand name of ECO will gradually become more well-known in the market.

Construction of a logistics port in Jining city, Shandong province, to link an upstream dedicated coal transportation railway with a nearby downstream canal connecting Beijing and Hangzhou, part of ECO's new "Energy Logistics" business sector, is nearly complete. The pilot run for bulk cargo transportation has commenced. The logistics port is expected to be fully commissioned during the fourth quarter of 2013. ECO is also planning to provide liquefied natural gas filling facilities for incoming and outgoing heavy-duty trucks and river transport vessels at the pier so they may progressively replace their use of diesel.

With gradual depletion of global petroleum resources and associated price increases, the mainland is proactively developing alternative substitutes to meet its growth in demand for energy. To this end, ECO's coalbed methane liquefaction facility located in Jincheng city, Shanxi province is operating smoothly; production increased by 36 per cent in 2012 compared with the same period for 2011, generating good profits for the Group. ECO's methanol production plant in Erdos city, Inner Mongolia, which converts coal into methanol and has an annual production capacity of 200,000 tonnes, is now running smoothly at the pilot stage of production. To further enhance the economic benefits of this project, ECO plans to also convert the methanol into high value-added energy products.

In addition, ECO's new-energy research and development centre, which possesses a strong and growing technical force, is also working proactively on technologies to convert resources of low value into high value-added energy. Industrial tests on a medium scale, focused on converting coal tar oil of medium to low temperature into petrol or diesel, were successfully completed in 2012 and planning is now in place to apply this technology to commercial projects in 2013. Furthermore, ECO is also developing its interests in methanol processing and in conversion prospects for coke oven gas, tar oil and biomass energy. ECO will continue to work proactively to apply these technologies to industrial use; these kinds of investments are expected to play an increasingly important part in ECO's new energy businesses.

ECO also made a new investment in the upstream sector of its new energy businesses in mid-2012 by acquiring a 60 per cent effective stake in the development of onshore oilfield blocks in central Thailand; ECO has already smoothly taken over the operational management of the oilfields and organised a professional team to formulate a plan for their comprehensive development. In addition, in Guizhou province, ECO has conducted an innovative test with promising results on surface extraction of coalbed methane for coal mines of low permeability. In Inner Mongolia, ECO's Xiaoyugou coal mine, with an annual production capacity of 1.2 million tonnes, is now at the pilot stage of production and is expected to be fully commissioned during the first quarter of 2013 while its open-pit Kejian coal mine has been operating normally as planned.

Towngas China Company Limited

(Stock Code: 1083.HK)

Towngas China, a subsidiary of the Group, continued to record good growth in profit after taxation attributable to its shareholders, amounting to HK$841 million in 2012, an increase of approximately 19 per cent over 2011. As at the end of December 2012, the Group had an approximately 66.18 per cent interest in Towngas China.

In 2012, Towngas China acquired seven new piped-gas projects located in Wafangdian, Dalian city and Xinqiu district, Fuxin city, Liaoning province; in Binhai Science and Technology Industrial Park, Zhaoyuan city and Pingyin county, Jinan city, Shandong province; in Yifeng county, Yichun city, Jiangxi province; in Lingang Industrial Park, Shanhaiguan district, Qinhuangdao city, Hebei province; and in Changting county, Longyan city, the Group's first in Fujian province. Towngas China also added a new midstream pipeline project in Wafangdian, Dalian city, Liaoning province to its portfolio in 2012. Towngas China is focused on developing city-gas businesses in cities with a high proportion of industrial gas consumption. To capture investment opportunities resulting from the country's commitment to promote the utilisation of natural gas during the period of the Twelfth Five-Year Plan (2011-2015), Towngas China will continue to strive for rapid expansion through mergers and acquisitions.

In January 2013, Towngas China issued and sold 150 million new ordinary shares by placement (the "Placing") at a price of HK$6.31 per share. Net proceeds from the Placing after deducting related commission and other expenses were HK$930 million. The Placing was over-subscribed more than 20 times within a very short period of time, demonstrating a very good response. All new shares were finally subscribed by a number of investors. The Group's interest in Towngas China was slightly diluted from 66.18 per cent to 62.37 per cent after the Placing. The Placing helps Towngas China to strengthen its funding structure, lower its future financing costs and increase its public float.

Development of Town Gas Network and Facilities in Hong Kong

The network supply capability of the Company is expanding at a good pace in line with market growth. Several network development projects are in progress to meet long-term demand.

Laying of a 15 km pipeline to bring natural gas from Tai Po to Ma Tau Kok gas production plant, to partially replace naphtha as feedstock for the production of town gas, is near completion with commissioning expected this year. Construction of a 9 km pipeline in the western New Territories to strengthen supply capability and reliability is also in progress. In tandem with the government's development of West Kowloon, South East Kowloon and a cruise terminal, network planning, design and construction in these locations are underway. Construction of a new submarine pipeline from Ma Tau Kok to North Point commenced in 2012. Meanwhile, the gas main extension to Lei Yue Mun is substantially complete and some of the restaurants situated along the South East Kowloon seashore have already converted to the use of town gas.

The Group will constantly allocate resources towards renovating Hong Kong's town gas network to ensure safety of gas supply.

Property Developments

Leasing of the commercial area of the Grand Waterfront property development project located at Ma Tau Kok is good. The Group also has an approximately 15.8 per cent interest in the IFC complex. Rental demand for the shopping mall and office towers of IFC continues to be robust. The occupancy rate of the project's hotel complex, comprising the Four Seasons Hotel and rental serviced apartments, remains high.

Financing Programmes

In line with the Group's long-term business investments, the Group continued issuing medium term notes, for a total amount equivalent to HK$4.4 billion, during the year 2012 under its medium term note programme (the "Programme") established through HKCG (Finance) Limited, a wholly-owned subsidiary of the Group. Inclusive of the Group's first renminbi-denominated notes in Hong Kong issued in late March 2011 for a total amount of RMB1 billion over a term of five years, the Group had issued, as at the end of December 2012, medium term notes of an aggregate amount equivalent to HK$10.2 billion under the Programme with tenors ranging from 5 to 40 years.

Commemorative Activities for the Company's 150th Anniversary

The Company celebrated its 150th Anniversary in 2012. To reward our shareholders, the Company distributed a one-off special dividend of HK17.5 cents per share to shareholders in mid-2012; including interim and final dividends, the total dividend paid out represented 150 per cent of that originally recommended for the whole year. The Company also held a series of commemorative activities, including a 150th Anniversary cocktail reception on 15th October 2012 for several hundred guests representing political, commercial and other sectors; Mrs. Carrie Lam, Chief Secretary for Administration of the Hong Kong Special Administrative Region ("HKSAR"), was Guest of Honour. All were there to celebrate the Company serving the local community in Hong Kong for over one and a half centuries during which unremitting efforts have been made to contribute to the prosperous development of the territory.

Company Awards

The Company gained a number of awards and recognitions in Hong Kong and overseas during its 150th Anniversary year, and for the first time reached the British newspaper Financial Times' "Global 500 List", with a ranking of 443rd, the only Asian company in the "Gas, water and multi-utilities" sector; market capitalisation of companies is a major criterion for ranking.

The Company has gained "The Excellence of Listed Enterprise Awards" from Capital Weekly for two consecutive years, in recognition of the Company's excellent corporate governance, investor relations, corporate strategy, corporate social responsibility performance and business growth. The Company was also once again listed by Yazhou Zhoukan in 2012 in its "Global Chinese Business 1000" with sixth ranking for Hong Kong.

By virtue of their outstanding performance in corporate sustainability, both the Company and Towngas China have been selected as constituent companies of the Hang Seng Corporate Sustainability Index Series for the last two consecutive years, indicating the Group's high standard of performance in environmental, social and corporate governance aspects as well as workplace practices.

With good business results and comprehensive strengths in its business operations, the Company also reached the "Top 100 – Comprehensive Strength", the main ranking of the "Top 100 Hong Kong Listed Companies" jointly organised by Finet Group Limited and Tencent in 2012. Towngas China also made its way into the sub-ranking "Top 10 Stock Price Gainers".

A new series of appliances launched to commemorate the Company's 150th Anniversary was selected for the "2012 Hong Kong Awards for Industries: Consumer Product Design Category", in recognition that the Company's products are meeting the demands of the consumer market.

In mid-2012, the Company gained the Gold Award under the category of "Public Organisation and Utilities" of the "2011 Hong Kong Awards for Environmental Excellence" jointly organised by 11 organisations including the Government of the HKSAR and the Environmental Campaign Committee. In the "Hong Kong Green Awards 2012" organised by the Green Council, the Company also won the "Corporate Green Governance Award – Grand Award", the "Corporate Green Governance Award – Corporate Leadership" and the "Green Management Award (Corporate) – Gold", in recognition of the Company's outstanding achievements in environmental protection, management and green corporate governance.

Hong Kong Employees and Productivity

As at the end of 2012, the number of employees engaged in the town gas business in Hong Kong was 1,943 (2011 year end: 1,938), the number of customers was 1,776,360, and each employee served the equivalent of 914 customers, slightly up compared to each employee serving 903 customers as at the end of 2011. Inclusive of employees engaged in local businesses such as telecommunications, LPG vehicular filling stations and engineering contractual works, the total number of the Group's employees engaged in businesses in Hong Kong was 2,282 as at the end of 2012 compared with 2,255 as at the end of 2011. Related manpower costs amounted to HK$829 million for 2012. In 2012, there was an approximately 5.5 per cent average increase in remuneration over 2011. The Group will continue to offer employees rewarding careers based on their capabilities and performance and arrange a variety of training programmes in order to constantly enhance the quality of the Group's customer services.

On behalf of the Board of Directors, I would like to thank all our employees for their dedication and hard work in creating value for shareholders and customers.

Bonus Issue of Shares

The Directors propose to make a bonus issue of one new share credited as fully paid for every ten shares held on the Register of Members on 14th June 2013.

The necessary resolution will be proposed at the forthcoming Annual General Meeting on 5th June 2013, and if passed, share certificates will be posted on 24th June 2013.

Final Dividend

The Directors are pleased to recommend a final dividend of HK23 cents per share payable to shareholders whose names are on the Register of Members as at 14th June 2013. Including the interim dividend of HK12 cents per share paid on 3rd October 2012, the total dividend payout for the whole year shall be HK35 cents per share.

Barring unforeseen circumstances, the forecast dividends per share for 2013 after bonus share issue shall not be less than the interim and final dividends for 2012.

Business Outlook for 2013

The Company predicts steady growth and an increase of about 25,000 new customers in Hong Kong during 2013. Restaurant, hotel and retail sectors are still benefiting from a prospering tourism industry in Hong Kong. However, the Government of the HKSAR anticipates that the global economy will continue to grow only modestly and downside risks still exist. In Hong Kong, operating costs for all business sectors are increasing. The Company's increase in the standard gas tariff with effect from 1st April 2013 will offset some of the pressure on its own rising operating costs. The Company will continue to enhance its operational efficiency so as to maintain stable revenue from its gas business in the territory.

In line with the gradual implementation of the Twelfth Five-Year Plan, the mainland government advocates increasing urbanisation, expanding domestic demand, more energy conservation and a reduction of gas emissions. As the mainland economy is sustaining good growth, it is anticipated that there will be rising demand for utility services and clean energy. The Group's city-gas and natural gas businesses on the mainland are therefore expected to continue to achieve good growth. Furthermore, following the mainland government's move towards a policy of energy diversification and environmental protection, the Group predicts good prospects for its emerging environmentally-friendly energy businesses, which will ignite a new light illuminating the way for the Group's long-term development and business growth.

It is projected that the Group's businesses will maintain good growth during 2013. The combined results of the Group's emerging environmentally-friendly energy and mainland utility businesses have already overtaken the results of its Hong Kong gas business, and, with the former's good prospects, are forecast to grow faster than the latter in the coming years.

With the Group's solid foundation in Hong Kong and its diverse business sectors spread across extensive areas on the mainland, together with its successful corporate brand names built up there over the last 20 years and an anticipated rising demand for clean energy, the Group predicts good prospects and an even better future for all its businesses in the years to come.

LEE Shau Kee
Chairman
Hong Kong, 18th March 2013