CHAIRMAN'S STATEMENT

"The performance of the Group's gas business in Hong Kong remained steady in 2007... The Group predicts good prospects for its mainland businesses will continue."

The Year's Results

The performance of the Group's gas business in Hong Kong remained steady in 2007 and related profit was stable. The local gas market is maturing in the face of keen competition from other residential, commercial and industrial energy suppliers. The Group has endeavoured to enhance its operational efficiency, given increasing operating costs associated with an inflationary local economy. The Group expects performance of its gas business to continue to remain stable in future.

Profit after taxation attributable to shareholders of the Group for the year amounted to HK$9,269.6 million. The increase in profits was mainly due to a one-off gain, profit from the sale of properties and a revaluation surplus from investment properties, totalling HK$6,471.1 million in all. This comprised a HK$2,235.7 million one-off gain resulting from the acquisition of shares in Panva Gas Holdings Limited by way of asset injection, HK$2,775.0 million from the Group's share of profits arising from the sale of units at Grand Promenade, Grand Waterfront and King's Park Hill property development projects, HK$1,269.4 million from the Group's share of a revaluation surplus from an investment property, the International Finance Centre complex, and HK$191.0 million from a revaluation surplus from another investment property, Grand Waterfront. In comparison, in 2006, the Group's share of profits from the sale of properties was HK$1,779.4 million and its share of a revaluation surplus from an investment property was HK$858.8 million. The substantial one-off gain will not be repeated in 2008 and profit from sale of properties will reduce in the coming year.

Earnings per share relating to the Group's profit after taxation for principal businesses for the year amounted to HK 53.1 cents, an increase of 3.2 per cent over 2006.

During the year under review, the Group invested HK$1,595.2 million in pipelines and facilities in Hong Kong and the mainland.

Gas Business in Hong Kong

The Company's gas sales did not keep pace with economic growth in Hong Kong during 2007. As a result of higher temperatures and an extremely hot summer, compounded by keen competition in the energy sector, the volume of residential gas sales decreased slightly by 1.6 per cent compared with 2006, a continuing downward trend. At the same time, despite thriving hotel and restaurant sectors, the volume of commercial and industrial gas sales increased slightly by 2.1 per cent in comparison to the previous year. Overall, total volume of gas sales in Hong Kong for 2007 remained at a similar level to 2006. As at the end of 2007, the number of customers was 1,646,492, an increase of 23,844 over 2006.

Towngas China Company Limited (Stock Code: 1083)

The Group has an approximately 45.4 per cent interest in Panva Gas Holdings Limited ("Panva Gas") which was renamed as Towngas China Company Limited ("Towngas China") on 23rd May 2007. The well-recognised and reputable brand name "Towngas" in Chinese has been adopted by the Group for its mainland city-gas businesses. In acquiring Panva Gas, the Group extended the geographical reach of its piped city-gas projects on the mainland.

In mid 2007, Towngas China raised approximately HK$700 million by way of an open offer of one offer share for every ten shares. This increased the number of Towngas China shares held by the Group to approximately 850 million shares and provided an additional capital injection of approximately HK$300 million to Towngas China. Following a further acquisition of approximately 37 million shares, the Group currently holds approximately 890 million Towngas China shares.

Business Development in Mainland China

The Group's mainland businesses are progressing well. The acquisition of Panva Gas in March 2007 injected an additional 25 piped city-gas projects into the Group and extended the Group's footprint in north-eastern and south-western China. With the re-structuring at state level of the country's energy mix and the possibility of on-going high international oil prices, the Group, besides investing in piped city-gas projects, is also endeavouring to develop emerging energy projects, including the exploitation and utilisation of coalbed gas and natural gas and projects involving coal-based energy, the chemical industry and environmentally-friendly vehicle fuels. These endeavours are progressing well. The exploitation and utilisation of emerging energies, which can be used as substitutes for petroleum products, are expected to have good prospects, creating more investment opportunities in the energy sector for the Group.

CHAIRMAN'S STATEMENT

The Group's first coalbed gas liquefaction joint venture project started in early July 2007 in Jincheng, Shanxi province; commissioning is anticipated by mid 2008. As the components of coalbed gas are similar to those of natural gas, coalbed gas has the potential to become an important environmentally-friendly energy fuel. In September 2007, a further joint venture agreement relating to the second phase of this project was concluded to increase the production capacity of liquefied coalbed gas.

The Group established its first energy exploitation joint venture in early 2007 in Jilin province. By participating in the exploitation and sale of petroleum and natural gas, the Group will be able to provide additional gas sources for downstream gas projects. Experience gained from this project will help the Group to develop other similar upstream energy projects in the mainland.

The Group's midstream energy projects are also making good progress. These include high-pressure natural gas pipeline joint ventures in Anhui province, Hebei province and Hangzhou, Zhejiang province, and a new joint venture established in 2007 that invests in the construction of natural gas pipelines and the exploitation of oil resources in Jilin province. These kinds of midstream investments underpin downstream joint venture projects thus enabling the Group to strengthen its piped city-gas market interests in the regions concerned.

Following the acquisition of Panva Gas as an associated company in early March 2007, the Group's piped city-gas projects increased in number. In 2007, the Group further concluded joint venture agreements to invest in piped city-gas projects in Chaoan, Guangdong province and Fengcheng, Jiangxi province. The gas market is substantial in both cities because of their prosperous ceramic industries. New projects were also concluded by Towngas China during the year in Qijiang County in Chongqing, Mianyang in Sichuan province and Gongzhuling in Jilin province, bringing the Group's piped city-gas projects to 65 in mainland cities spread across 14 provinces/municipalities in eastern, central, northern, north-eastern, western and south-western China including Guangdong and Shandong provinces. The Group's investment in, and operation of, upstream coalbed gas and natural gas projects will help provide new gas sources for its piped city-gas projects. For example, the major gas source for the project in Chaoan, Guangdong province, will be liquefied coalbed gas from Shanxi province. With the implementation of a state plan for transmitting natural gas from Sichuan province to eastern and southern China, and a recent increase in the quantity of imported liquefied natural gas, the Group's mainland projects are projected to thrive during the next three years.

The Group is operating water supply projects in Wujiang, Jiangsu province and in Wuhu, Anhui province, and managing an integrated water supply and wastewater joint venture in Suzhou Industrial Park, Jiangsu province. The Group is able to capture synergies between these water projects and its gas joint ventures, thus achieving cost savings. Both the gas and water sector will gradually become market-based, in line with the opening up of the mainland's utility markets, creating more business opportunities for the Group.

Including Towngas China, the Group currently has a total of 77 projects spread across 16 provinces/municipalities, encompassing upstream, midstream and downstream natural gas sectors, the water supply and wastewater treatment sector and natural gas filling stations.

Diversification is rapidly transforming the Group into a sizable, nation-wide, multi-business corporation, with a focus on environmentally-friendly businesses and the energy sector, from a locally-based company centred on a single business.

Environmentally-friendly Energy Businesses of ECO

Since 2000, the Group has been proactively developing environmentally-friendly energy businesses in Hong Kong including dedicated liquefied petroleum gas ("LPG") filling stations, landfill gas projects and an aviation fuel facility. Starting in 2008, the Group will step up endeavours to develop clean, emerging energy projects and will enhance its monitoring of developments in the coal-based chemical industry and in new technology for the production of clean energies such as methanol and dimethyl ether, and of related market trends and potential investment opportunities associated with these alternative fuels. From January 2008, ECO Environmental Investments Limited and its subsidiaries (together known as "ECO") will spearhead the Group's business objectives to develop emerging energy and environmentally-friendly businesses in Hong Kong and the mainland.

Revenue from ECO's dedicated LPG filling stations in Hong Kong increased in 2007 compared to 2006 in line with the territory's continuing economic growth. ECO's landfill gas project also progressed well. Following several years of planning and construction, the North East New Territories ("NENT") landfill gas treatment facility was commissioned in early 2007. Treated landfill gas is transported to Tai Po gas production plant via a 19 km pipeline to partially substitute for naphtha as a fuel for town gas production. Given the success of the NENT project, ECO is now proactively looking for further opportunities to utilise landfill gas at other sites in order to help improve air quality by reducing flare-off of atmospheric-polluting gases.

In 2002, ECO signed a 40-year franchise agreement with the Hong Kong Airport Authority to design, construct and commission a permanent aviation fuel facility at Tuen Mun Area 38. This is an important infrastructure project that will supply aviation fuel directly to Hong Kong International Airport. The facility will consist of a large-scale tank farm for storage of aviation fuel and will be served by two jetties, one capable of berthing tankers up to 80,000 tonnes and the other tankers up to 40,000 tonnes. The project is on schedule and commissioning is expected in early 2010. The facility will become a major logistics base for supply of aviation fuel in Hong Kong.

On the mainland, ECO is now managing an experimental energy-saving and emission-minimising project in Shaanxi province involving the construction and operation of several compressed natural gas filling stations for heavy duty trucks. The stations are expected to be commissioned in mid 2008. Negotiations concerning several coal-based methanol and ether projects are also progressing well. ECO's emerging energy and environmentally-friendly businesses on the mainland are expected to bring economic benefits to the Group.

Pipelaying Projects

In order to cope with the demand arising from urban developments in Hong Kong, several substantial pipelaying projects are currently under way.

Construction of a 24 km transmission pipeline in the eastern New Territories to augment the capability and reliability of gas supply is at the completion stage. Meanwhile, a 19 km pipeline for the transport of landfill gas from the NENT landfill site to Tai Po gas production plant was completed and commissioned in early 2007. 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 has now started. Construction of a 9 km pipeline in the western New Territories to strengthen supply reliability is also under way.

Property Developments

Pre-sale of the Grand Waterfront property development project, located at the Ma Tau Kok south plant site, commenced in late August 2006. Take-up has been good. In late August 2007, newly completed flats were launched to promote further sales and on-site show flats were provided for viewing. The project consists of five apartment buildings, providing 1,782 units with a residential floor area of approximately 1.2 million square feet. Approximately 540,000 square feet were sold during the year, yielding substantial returns for the Group and bringing the total residential area sold by the end of December 2007 to approximately 1.17 million square feet. The Group is entitled to 73 per cent of the net sales proceeds of the residential portion of the project. Residential occupancy started in May 2007. The commercial area of the project is approximately 150,000 square feet. Rental of the commercial area started in the second half of 2007.

The Group has a 50 per cent interest in the Grand Promenade property development project at Sai Wan Ho. This project provides 2,020 units, with a total floor area of approximately 1.7 million square feet. Approximately 370,000 square feet were sold during the year. An overall total of approximately 1.67 million square feet had been sold by the end of December 2007. Residential occupancy started in early 2006.

The Group has an approximately 15.8 per cent interest in the International Finance Centre ("IFC"). The shopping mall and office towers of IFC are fully let. Given the increasing number of inbound visitors and continuing economic growth, the occupancy rate of the project's hotel complex, comprising the Four Seasons Hotel and Four Seasons Place, remains high and business overall is very successful.

Revaluation of Town Gas Network System

The Company's network system was revalued by American Appraisal China Limited, a wholly owned subsidiary of American Appraisal Associates Inc., a highly reputable international company experienced in asset valuation, at a fair market value of HK$25.8 billion as at 31st December 2007.

Company Award

The Group endeavours to protect the environment throughout its operations. The Group was awarded the "2007 Hong Kong Awards for Industries: Environmental Performance Grand Award" by the Business Environmental Council in recognition of the Group's commitment to environmental protection, improvement in environmental performance, and compliance with environmental legislation. The Group was also granted this award in 2004.

Employees and Productivity

The number of employees engaged in the town gas business was 1,919 at the end of 2007. During the year under review, the Company's customers increased by 23,844 with each employee serving 858 customers, compared to each employee serving 849 customers in 2006. Total remuneration for employees involved directly in the town gas business amounted to HK$632 million for 2007, an increase of HK$19 million in comparison with 2006. The Group offers employees rewarding careers based on their capabilities and performance and arranges a variety of training programmes in order to constantly enhance the quality of 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 of HK$0.25 credited as fully paid for every ten shares held on the Register of Members on 9th May 2008. The necessary resolution will be proposed at the forthcoming Annual General Meeting on 19th May 2008, and if passed, share certificates will be posted on 20th May 2008.

Dividend

The Directors are pleased to recommend a final dividend of HK 23 cents per share payable to shareholders whose names are on the Register of Members as at 9th May 2008. Including the interim dividend of HK 12 cents per share paid on 22nd October 2007, the total dividend payout for the whole year shall be HK 35 cents per share.

Barring unforeseen circumstances, the forecast dividends per share for 2008 after bonus share issue shall not be less than that for 2007.

Business Outlook for 2008

The Group's substantial profit for the year 2007 mainly resulted from profit from the sale of properties, a revaluation surplus from investment properties and a one-off book profit from the acquisition of Panva Gas. The substantial one-off gain will not be repeated in 2008 and profit from sale of properties will reduce in the coming year. As the local gas market is maturing, and operating costs are increasing due to rising remuneration and prices of commodities both associated with an inflationary local economy, the Group's gas business in Hong Kong is expected to come under pressure in 2008.

The Company has not increased its basic gas tariff for the past ten years. Nevertheless the Company has made every effort to enhance its operational efficiency while increasing the standard of services provided, maintaining steady performance of its gas business in Hong Kong. As a result of the implementation of a dual naphtha and natural gas feedstock mix in October 2006, feedstock costs have decreased to the benefit of customers. This has also helped the Company to off-set the economic impact resulting from the surge in international oil prices over the last year.

The Company anticipates an increase of about 25,000 new customers and a slight growth in gas sales volume in Hong Kong during 2008. The Group will endeavour to develop upstream, midstream, downstream and emerging energy markets at a faster rate. The Group predicts good prospects for its mainland businesses will continue.

LEE Shau Kee
Chairman
Hong Kong, 26th March 2008