CHAIRMAN'S STATEMENT

The Year's Results

The performance of the Group's gas business in Hong Kong remained steady in 2014. In comparison, the Group's city-gas businesses in mainland China thrived, bringing stable growth; concurrently emerging environmentally-friendly energy businesses are continuously developing. The Group's overall recurrent businesses recorded good results in 2014.

Profit after taxation attributable to shareholders of the Group for the year amounted to HK$7,109 million, an increase of HK$255 million compared to 2013. Earnings per share for the year amounted to HK67.6 cents. Exclusive of the Group's share of a revaluation surplus from investment properties and unrealised exchange differences on the renminbi, the Group's profit after taxation for the year increased by approximately HK$640 million to approximately HK$7 billion, an increase of 10 per cent compared to 2013 mainly attributable to a rise in profit from the Group's local businesses and mainland utility businesses.

During the year under review, the Group invested HK$6,365 million in production facilities, pipelines, plants and other fixed assets for the sustainable development of its various existing and new businesses in Hong Kong and mainland China.

Gas Business in Hong Kong

The local economy sustained moderate growth in 2014 with favourable overall local employment conditions. Despite a slowdown in local consumer spending, restaurant and hotel sectors, benefiting from continuous growth in the number of inbound tourists, continued to progress well during the year. As a result, commercial and industrial gas sales increased in 2014. However, growth was weakened due to a slightly higher annual average temperature in 2014 than 2013. Overall, total volume of gas sales in Hong Kong for the year increased slightly by 1 per cent to 28,835 million MJ whereas appliance sales revenue increased by 6.1 per cent with a total of 252,135 sets sold, both compared to 2013.

As at the end of 2014, the number of customers was 1,819,935, an increase of 21,204 compared to 2013, slightly up by 1.2 per cent.

Business Development in Mainland China

The Group's mainland businesses continued to progress well in 2014 in respect of the number of projects and profit.

Overall, inclusive of projects of the Group's subsidiary, Towngas China Company Limited ("Towngas China"; stock code: 1083.HK), the Group had 202 projects on the mainland, as at the end of 2014, 29 more than at the end of 2013, spread across 24 provinces, autonomous regions and municipalities. These projects encompass upstream, midstream and downstream natural gas sectors, water sectors, environmentally-friendly energy applications, energy resources' exploration and utilisation, as well as telecommunications.

Diversification and an increase in the number of projects are gradually transforming the Group from a locally-based company in Hong Kong centred on a single business into a sizable, nation-wide, multi-business corporation with a focus on environmentally-friendly energy ventures and utility sectors.

The Group's development of emerging environmentally-friendly energy businesses and related research and development of new technologies, through its wholly-owned subsidiary ECO Environmental Investments Limited and the latter's subsidiaries (collectively, "ECO"), are progressing well. With a number of environmentally-friendly and energy conservation projects already commissioned or under construction, and new projects under development, the foundation for long-term growth of the Group's businesses is being continually reinforced.

Utility Businesses in Mainland China

The Group's city-gas businesses are progressing well with a total of eight new projects added to its portfolio in 2014. As at the end of 2014, inclusive of Towngas China, the Group had a total of 127 city-gas projects in mainland cities spread across 23 provinces, autonomous regions and municipalities. The total volume of gas sales for these projects in 2014 was approximately 15.2 billion cubic metres, an increase of 14 per cent over 2013. As at the end of 2014, the Group's mainland gas customers stood at approximately 18.98 million, an increase of 10 per cent over 2013. The Group continues to be honoured with a good reputation for being a large-scale city-gas enterprise with outstanding performance on the mainland.

Despite the impact of a slow recovery in the global economy and weak demand for commodities, the mainland economy continued to grow steadily though the pace was slower in 2014 compared to 2013. The demand for energy remains strong across the country. A long-term steady supply of natural gas, the major clean energy resource on the mainland, is particularly essential. In May 2014, a 30-year gas supply purchase and sales contract was signed between mainland China and Russia. Under this contract, Russia will start transmitting natural gas to the northeastern region of mainland China via a pipeline from 2018, an important move in guaranteeing sufficient gas resources. Inclusive of a framework agreement signed in November 2014, Russia will supply a total of 68 billion cubic metres of piped natural gas annually to mainland China. The mainland government has also formulated a natural gas utilisation policy to strengthen preventative measures to combat air pollution and to minimise the formation of haze. This momentum is benefiting the Group's city-gas and natural gas businesses and helping to create continuous growth.

In the past two years, the non-residential sector has been impacted by a rise in the gate price of natural gas in July 2013 and a rise in the gate price of natural gas stock in September 2014. This rising cost of natural gas is having a short-term adverse impact on commercial and industrial gas market demand with certain sectors unable to withstand high energy prices, thus slowing growth of gas sales. However, in the medium to long term, natural gas is still projected to be the clean energy of choice on the mainland for reducing pollutant emissions to improve hazy atmospheric conditions. With gradual commissioning of the country's large-scale natural gas projects all coming on stream, including transmission pipelines from Sichuan province to eastern and southern China and the West-to-East pipeline, and pipeline projects for importing natural gas from Central Asia and Myanmar, together with the signing of piped natural gas supply contracts with Russia, as well as a rise in the quantity of imported liquefied natural gas ("LNG"), supply of natural gas on the mainland will increase substantially in the next few years. Thus, with increasing 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 future.

The Group's midstream natural gas projects are operating smoothly. These include natural gas pipeline projects in Anhui and Hebei provinces; natural gas extension projects in Jilin and Henan provinces; the Guangdong LNG Receiving Terminal project; and Towngas China's midstream pipeline project located in Wafangdian, Dalian city, Liaoning province. Construction of the Group's gas storage facility in underground salt caverns in Jintan city, Jiangsu province commenced in November 2014. Upon completion, this facility will be the first of its kind developed by any city-gas enterprise on the mainland. Phase one of this project, with a total storage capacity of 110 million standard cubic metres, is expected to be commissioned in mid-2016 and will help the Group to supplement and regulate gas supplies during the peak winter period in eastern China. This project is also in line with the Chinese government's policy advocating the development of gas storage capacity at a faster pace. These kinds of midstream projects generate good returns and support the Group's development of its downstream city-gas markets.

The upstream natural gas supply market is also facing reform. In January 2015, Shanghai municipal government announced that a petroleum and natural gas trading centre will be set up in Shanghai city which is anticipated to further promote marketisation of natural gas prices. These kinds of reforms impacting both the natural gas supply mechanism and prices will be conducive to the healthy development of downstream city-gas businesses.

The Group has so far invested in, and operates, six water projects, including water supply joint venture projects in Wujiang district, Suzhou city, Jiangsu province and in Wuhu city, Anhui province; wholly-owned water supply projects in Zhengpugang Xin Qu, Maanshan city and in the starting area of Jiangbei Concentration Zone, Wuhu city, both in Anhui province; and an integrated water supply and wastewater treatment joint venture project, together with an integrated wastewater treatment project for a special industry, both in Suzhou Industrial Park, Suzhou city, Jiangsu province. With increasing demand for clean water resources across the country, the Group's water projects are progressing well, with steady growth in volume of water sales. To achieve a healthier development in the water sector, these project companies are now striving for a reasonable increase in the selling price of water.

Operation and management of businesses encompassing city-gas, midstream natural gas and city-water projects create positive synergy and mutual advantages. Furthermore, these businesses generate stable income and provide good 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 major businesses in Hong Kong – an aviation fuel facility, dedicated liquefied petroleum gas ("LPG") vehicular refilling stations and landfill gas utilisation projects – are all operating smoothly. Total turnover for ECO's aviation fuel facility for 2014 was 5.8 million tonnes. The facility provides a safe and reliable fuel supply to Hong Kong International Airport and contributes to ECO's steady profit growth. The LPG refilling station business achieved good results in 2014. ECO's landfill gas project in the North East New Territories, after operating for several years, is generating noticeable environmental benefits. On this basis, ECO has recently concluded an agreement for the development of a South East New Territories landfill gas utilisation project, which will make a further contribution to energy conservation and emission reduction in Hong Kong.

As haze and air pollution on the mainland are now a growing concern, the Chinese government is increasing its efforts to promote the development of refilling station networks supplying LNG as a fuel for vehicles and vessels. The use of LNG as a gradual replacement for diesel for heavy-duty trucks is an especially important and effective anti-pollution measure. In response to this opportunity, ECO has been reinforcing its production of LNG by using raw materials such as coalbed gas, coke oven gas, agricultural and forestry waste. ECO is also studying innovative resource conversion technologies for the production of high value-added environmentally-friendly energy. Related research and development has shown promising results, demonstrating noticeable economic and environmental benefits, especially in the areas of methanol upgrading and utilisation of agricultural waste which should help strengthen ECO's competitive edge in this new energy sector in future.

ECO's coalbed methane liquefaction facility, located in Jincheng city, Shanxi province, is operating smoothly, with an annual production volume of 250 million cubic metres in 2014. ECO is now seeking more natural gas and coalbed gas supply sources at different strategic locations in order to expand its production capacity and distribution networks.

There is substantial coke demand for steelmaking in the iron and steel industry in mainland China. During the industrial process to convert coking coal to coke, a large quantity of coke oven gas is generated. ECO is proactively investing in projects for the production of LNG by using coke oven gas to meet market demand. ECO has recently concluded agreements with two coking plants in Xuzhou city, Jiangsu province and in Heze city, Shandong province, to produce LNG by using coke oven gas from these plants; commissioning of both projects is expected in late 2015. As there are a large number of coking plants in mainland China, the utilisation of coke oven gas for environmental protection purposes has good prospects.

ECO's methanol production plant in Inner Mongolia Autonomous Region operated smoothly in 2014. On this basis, construction of a facility, which further upgrades methanol into natural gasoline (a gasoline substitute chemical product) using self-developed technology, was completed at the end of 2014, an important milestone for ECO's methanol upgrading business.

Mainland China, a sizeable agricultural country, generates a large quantity of agricultural waste. Apart from a small portion of this for use in fields or for power generation, the rest is incinerated and this inevitably pollutes the atmosphere. ECO is developing new technologies to convert agricultural and forestry waste into natural gas through gasification and methanation. Construction of a plant for this purpose is expected to commence in the second half of 2015, thus opening a new chapter in ECO's new energy businesses.

A network of ECO natural gas refilling stations is gradually taking shape in, amongst others, Shaanxi, Shandong, Shanxi, Henan and Liaoning provinces. All in all, ECO had 38 refilling stations in operation, under planning or construction as at the end of 2014, and further expansion into more provinces is in progress. The ECO brand name will gradually become more well-known in the market.

ECO's oilfield project in Thailand recorded good output in 2014. After conducting thorough research studying the geological structure of the oilfield, several high-yield wells were subsequently drilled producing a daily output of 6,000 barrels of oil by the end of 2014, four times that of earlier in the year. This high level of output is expected to be sustained in 2015.

Towngas China Company Limited
(Stock Code: 1083.HK)

Towngas China, a subsidiary of the Group, recorded good business growth in 2014. Exclusive of unrealised exchange losses on the renminbi, Towngas China recorded a net profit of HK$1,195 million, an increase of approximately 26 per cent compared to 2013. Inclusive of the losses from the exchange difference in the fair values due to the depreciation of the renminbi during the year, Towngas China's profit after taxation attributable to its shareholders was HK$1,054 million, a decrease of HK$52 million compared to 2013. As at the end of December 2014, the Group had an approximately 62.39 per cent interest in Towngas China.

Project development is also progressing well. Towngas China acquired eight new piped-gas projects in 2014 located in Xingyi city, Guizhou province; in Siping city, Jilin province; in Guyang county, Baotou city, Inner Mongolia Autonomous Region; in Jiajiang county, Leshan city, Sichuan province; in Songyang county, Lishui city, Zhejiang province;

in Tongshan district, Xuzhou city, Jiangsu province; in Luliang county, Qujing city, Yunnan province; and in Yangxin county, Binzhou city, Shandong province. In 2014, Towngas China also acquired a vehicular gas refilling station project in Qiqihar city, Heilongjiang province and a gas pipeline assembly project.

In May 2014, Standard & Poor's Ratings Services ("Standard & Poor's"), an international rating agency, upgraded its rating outlook on Towngas China to "positive" from "stable", and affirmed its "BBB" long-term corporate credit rating on the company. As a result of this revision, Standard & Poor's raised its long-term Greater China regional scale credit rating on Towngas China to "cnA+" from "cnA". In July 2014, Moody's Investors Service ("Moody's"), another international rating agency, also upgraded its rating outlook on Towngas China to "positive" from "stable", and affirmed its "Baa2" issuer rating on the company. Such ratings demonstrate Towngas China's increasing credit strength and the rating agencies' recognition of the company's growth momentum.

Financing Programmes

In order to tap funding in a timely and flexible manner, the Group established a medium term note programme in 2009 under HKCG (Finance) Limited, a wholly-owned subsidiary of the Group. In line with the Group's long-term business investments, the Group had issued, as at 31st December 2014, medium term notes of an aggregate amount equivalent to HK$10.4 billion with tenors ranging from 5 to 40 years under this programme.

In January 2014, the Group also issued its first perpetual subordinated guaranteed capital securities (the "Perpetual Capital Securities"), amounting to US$300 million, through Towngas (Finance) Limited, another wholly-owned subsidiary of the Group. These Perpetual Capital Securities have a nominal interest rate of 4.75 per cent per annum for the first five years, a record low for securities of the same kind issued by corporations in Asia at that time, and thereafter will have a floating interest rate. The Perpetual Capital Securities, guaranteed by the Company, were listed on The Stock Exchange of Hong Kong Limited on 29th January 2014 (stock code: 6018.HK) and rated "A3" and "A-" by international rating agencies Moody's and Standard & Poor's respectively. The issuance helps further strengthen the Group's balance sheet, improve its financing maturity profile, diversify funding sources and maintain solid investment grade ratings.

Hong Kong Employees and Productivity

As at the end of 2014, the number of employees engaged in the town gas business in Hong Kong was 1,972 (2013 year end: 1,966), the number of customers was 1,819,935, and each employee served the equivalent of 923 customers, slightly up compared to 2013. Inclusive of employees engaged in local businesses such as telecommunications, LPG vehicular refilling stations and engineering contractual works, the total number of the Group's employees engaged in businesses in Hong Kong was 2,331 as at the end of 2014 compared to 2,313 as at the end of 2013. Related manpower costs amounted to HK$917 million for 2014. In 2014, there was an approximately 4.7 per cent average increase in remuneration over 2013.

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 for every ten existing shares held by shareholders whose names are on the Register of Members on 9th June 2015. The necessary resolution will be proposed at the forthcoming Annual General Meeting on 1st June 2015, and if passed, share certificates will be posted on 17th June 2015.

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 9th June 2015. Including the interim dividend of HK12 cents per share paid on 3rd October 2014, the total dividend payout for the whole year shall be HK35 cents per share.

Barring unforeseen circumstances, the forecast dividends per share for 2015 after bonus share issue shall not be less than the interim and final dividends for 2014.

Business Outlook for 2015

The Company predicts steady growth in the number of customers in Hong Kong during 2015. Currently, favourable employment conditions and an increasing number of inbound tourists in Hong Kong are helping to stimulate internal demand and consumer spending. As the Government of the Hong Kong Special Administrative Region is also striving to increase land and housing supply, stable growth in gas customers and gas consumption are both anticipated. Expansion in the energy market is also benefiting from the competitiveness of town gas, an energy resource combining both environmental and economic benefits. As international oil prices have been decreasing substantially since the second half of 2014, charges for fuel cost adjustment of the gas tariff in Hong Kong have been reduced which is beneficial to customers and to further enhancement of the competitiveness of town gas. However, increasing local manpower costs and operating expenses have led to rising operating costs for businesses generally in Hong Kong. Nevertheless, the Company will continue to enhance its own operational efficiency so as to maintain stable development of its gas business in the territory.

In respect of city-gas businesses in mainland China, slowdown in the real estate market, resulting from related control policies, has impacted revenue from connection fees. In addition, growth of gas sales is declining due to an adverse impact on industrial production resulting from a sluggish global economic recovery, while growth of gas consumption in the commercial sector is also slowing due to the mainland government's more cautious approach to official spending. All these factors will create challenges to the overall profit growth of the Group's mainland businesses in 2015. Nevertheless, there will be a continuing rise in demand for utility services and energy in the long run resulting from the mainland government's drive to reduce emissions and utilise clean energy to combat air pollution, coupled with rapid urbanisation.

It is anticipated that natural gas price adjustment this year will lower upstream gas prices which would be favourable to the development of the downstream gas market and the healthy development of the natural gas business sector. In respect of emerging environmentally-friendly energy businesses, following the Chinese government's move towards greater energy diversification, environmental protection and the creation of a more circular economy, the Group is continuing to develop and apply new technologies for conserving energy and reducing pollutant emissions. There is also a growing trend for greater use of low-sulfur, high-quality oil and natural gas as fuels for vehicles and vessels to reduce atmospheric pollution. Despite the recent drastic fall in international oil prices, which will impact profit growth of emerging environmentally-friendly energy businesses in the short term, the Group will continue to select projects of high quality to invest in. In the long term, emerging environmentally-friendly energy businesses will ignite a new light illuminating the way for the Group's long-term development and business growth strategy.

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 technical experience, corporate brand names and sales channels built there over the last 20 years, and mainland society's rising concern over air quality, it is anticipated that there will be ever-rising demand for clean energy. In addition, given that the number of piped-gas customers in Hong Kong and mainland China is increasing, the Group, with a sizeable customer base, foresees a promising return from its diversified businesses which continue to expand.

Overall, the Group predicts good and broader prospects and an even better future for all its businesses in the years to come.

LEE Shau Kee
Chairman
Hong Kong, 18th March 2015