Chairman's Statement

The performance of the Group's gas business in Hong Kong **remained steady** in 2010. The Group's mainland businesses **progressed well** in 2010.

The Year's Results

The performance of the Group's gas business in Hong Kong remained steady in 2010. 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 proactively developed.

Profit after taxation attributable to shareholders of the Group for the year amounted to HK$5,584.8 million, an increase of HK$309.7 million compared to the restated profit of 2009. Earnings per share for the year amounted to HK 77.8 cents, an increase of 6.6 per cent over 2009. Profit growth in 2010 was mainly due to growth in profit of mainland businesses.

During the year under review, the Group invested HK$4,277.5 million in production facilities, pipelines, plants and other fixed assets for the sustainable development of its various businesses in Hong Kong and the mainland.

Gas Business in Hong Kong

The local economy continued to recover in 2010. An increase in the number of inbound tourists, prosperous tourism, restaurant and hotel sectors and lower average temperatures than 2009 helped the total volume of gas sales in Hong Kong to rise by 1.1 per cent compared to 2009. Total number of appliances sold in 2010 was 233,313 units, an increase of 6.1 per cent over 2009. This was due to the Company's launch of more new products, expansion of sales channels and strengthening of market promotions.

As at the end of 2010, the number of customers was 1,724,316, an increase of 25,593 compared to 2009.

Business Development in Mainland China

The Group's mainland businesses progressed well in 2010.

The mainland economy maintained strong momentum in 2010 benefiting the Group's city-gas and natural gas businesses which recorded continuous growth in the year under review. 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 also progressing well. ECO is currently at a stage of developing projects for investment. Construction work for some of its projects has already begun. In the long run, both city-gas and emerging environmentally-friendly energy businesses on the mainland have good prospects and investment value.

Overall, as at the end of 2010, inclusive of projects of the Group's subsidiary, Towngas China Company Limited ("Towngas China"; stock code: 1083.HK), the Group had 120 projects spread across 20 provinces/ autonomous regions/municipalities, encompassing upstream, midstream and downstream natural gas sectors, the water supply and wastewater treatment sectors, natural gas filling stations and emerging environmentally-friendly energy and energy resources projects.

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

Utility Businesses in Mainland China

The Group's city-gas businesses progressed well in 2010, with a further new project successfully established in Yonganzhou Industrial Park, Taizhou, Jiangsu province. Inclusive of eight new projects established by Towngas China in 2010, the Group had 93 city-gas projects in mainland cities spread across 17 provinces/autonomous regions/municipalities as at the end of 2010. During the year under review, the number of gas customers on the mainland reached 11.88 million and total volume of gas sales was 8,540 million cubic metres. The Group has now become the largest city-gas enterprise on the mainland.

In the coming years, with completion of large-scale natural gas projects, including the transmission pipelines from Sichuan province to eastern and southern China and phase two of the West-to-East pipeline, and an increase in the quantity of imported liquefied natural gas, together with national sources, the current shortfall in natural gas supply will be mitigated. The Group therefore anticipates its mainland projects will have access to sufficient gas sources to enable them to 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, Hebei province and Hangzhou, Zhejiang province; a joint venture that invests in the construction of natural gas pipelines and the exploitation of gas fields in Jilin province; the Guangdong Liquefied Natural Gas Receiving Terminal project; and a natural gas valve station project in Suzhou Industrial Park, Suzhou, Jiangsu province. These kinds of high-pressure, natural gas pipeline joint ventures generate good returns and help the Group develop and strengthen its downstream city-gas market interests.

The Group also operates water supply projects in Wujiang, Jiangsu province and in Wuhu, Anhui province, and manages an integrated water supply and wastewater joint venture in Suzhou Industrial Park, Suzhou, Jiangsu province. These projects are progressing well.

The Group will keep on looking for opportunities to invest in high-quality utility projects on the mainland.

Emerging Environmentally-friendly Energy Businesses

Coalbed Methane and Non-conventional Methane Utilisation Businesses

ECO's coalbed methane and non-conventional methane utilisation businesses have been developed based on the technology and operational experience gained from its landfill gas utilisation project which has been successfully operating in Hong Kong for several years. The North East New Territories landfill gas treatment facility contributes to improving air quality, minimising the use of fossil fuels and reducing greenhouse gas emissions. Since 2008, ECO has been developing similar clean and environmentally-friendly energy projects on the mainland with an extended scope of application, the first being a phase-one coalbed methane liquefaction facility located in Jincheng, Shanxi province which was commissioned in late 2008. Construction of a phase-two facility was successfully completed during the year under review, and is expected to be commissioned in the first quarter of 2011. Annual production capacity of the whole facility, the largest liquefaction and utilisation project of its kind on the mainland, will then increase to approximately 250 million standard cubic metres of liquefied coalbed methane which will be subsequently transported by road tankers to downstream markets.

Construction of ECO's coal-mine methane liquefaction project in Chongqing is progressing well; commissioning is expected in the first quarter of 2012. Coal-mine gas, which typically contains about 40 per cent of methane, will be used to produce liquefied methane deploying coal-mine gas deoxidisation and coalbed methane cryogenic liquefaction technologies. Other than in-situ power generation plants, this project, with an estimated annual production capacity of 91 million standard cubic metres, is slated to become the world's first large-scale coal-mine gas utilisation facility to convert otherwise wasteful resources to fuel of high value. ECO has also confirmed its investment in a second coal-mine methane deoxidisation and liquefaction project located in Yangquan mining district, Shanxi province to expand this business and provide the Group's city-gas projects with more environmentally-friendly gas sources to help conserve energy and reduce gas emissions.

Coal Resources and Coal Chemical Processing

ECO started to develop coal resources and coal chemical processing businesses in 2009, focusing mainly on more environmentally-friendly and cleaner technologies for coal resources utilisation. To this end, ECO's construction of a methanol production plant and development of a coal mine in Junger, Erdos, Inner Mongolia are progressing well; both are expected to be commissioned in 2011. With an annual production capacity of 200,000 tonnes, the methanol production plant has already entered the commissioning stage. ECO's coking coal mining and plant project in Fengcheng, Jiangxi province, is also on schedule; commissioning is expected in 2012. This project will provide an additional gas source for the Group's Fengcheng city-gas project. ECO will continue to expand its resources reserves of both thermal coal and prime coking coal and endeavour to develop more far-sighted clean coal utilisation techniques.

Energy-related Logistics and Facilities Businesses

ECO's energy-related logistics and facilities businesses originated from its five dedicated liquefied petroleum gas filling stations in Hong Kong which have been operating steadily for several years servicing taxis and minibuses. ECO started to develop its gas filling station business on the mainland in 2008. Since then, ECO has been gradually establishing a network of compressed and liquefied natural gas filling stations used by heavy-duty trucks in Shaanxi, Shandong, Liaoning, Henan and Anhui provinces.

ECO's aviation fuel facility in Area 38, Tuen Mun, to service Hong Kong International Airport, was completed and commissioned in November 2010. Jetties and facilities are available for berthing tankers of 80,000 tonnes and 50,000 tonnes and unloading their aviation fuel into eight large tanks with a total capacity of 264,000 cubic metres. After re-certification, the fuel is then transported to the airport via submarine pipelines.

The facility has now become a major logistics base for supply of aviation fuel in Hong Kong.

Establishment of Chinese Holding Company

In tandem with the rapid development of its emerging environmentally-friendly energy businesses on the mainland, ECO established a Chinese holding company in Erdos, Inner Mongolia at the end of 2009 to increase management effectiveness and financing channels.

The energy market on the mainland has great potential to expand. ECO's development of emerging environmentally-friendly energy businesses and its conclusion of related agreements are expected to bring good economic benefits and business prospects to the Group.

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

Towngas China, a subsidiary of the Group, continued to record good profit after taxation attributable to its shareholders, amounting to HK$436 million in 2010, an increase of approximately 64.4 per cent over 2009.

In mid-July 2010, the Group completed the injection of its entire equity interests in six piped city-gas project companies in Liaoning and Zhejiang provinces into Towngas China in exchange for the allotment and issue of 485 million new shares by Towngas China. The transaction raised the Group's shareholding in Towngas China from approximately 45.5 per cent to approximately 56.3 per cent. As such, Towngas China has become a majority-owned subsidiary of the Group, and its position as a leading operator of piped-gas businesses on the mainland has been enhanced. Standard & Poor's Ratings Services, an international rating agency, has raised its long-term corporate credit rating on Towngas China to BBB with a stable rating outlook, demonstrating the agency's positive evaluation of Towngas China's closer integration with the Group.

In mid-November 2010, the Group took 250 million Towngas China shares placed by a subsidiary of Enerchina Holdings Limited (stock code: 622.HK), the second largest shareholder of Towngas China, for an aggregate consideration of HK$907.5 million. As a result, the Group's interests in Towngas China were further increased to approximately 66.5 per cent.

In 2010, Towngas China acquired eight new projects located in the New Industrial District of Anshan, Dalian Lvshun Economic Development Zone, Kazuo county of Chaoyang in Liaoning province; in the Lingui New District of Guilin in Guangxi Zhuang Autonomous Region; in the Nanhai New District of Laiyang and Linqu county of Weifang in Shandong province; and in the Chengdong Harbour District of Jiujiang and the Fubei Industrial Park of Fuzhou in Jiangxi province. The project in the Lingui New District of Guilin, the Group's first in Guangxi, is a stepping stone to acquiring more projects in this region in future. Towngas China is focused on developing city-gas businesses in small to medium-sized cities and will continue to strive for rapid expansion through mergers and acquisitions.

Pipelaying Projects

In order to cope with growth in future demand and enhance reliability of gas supply in Hong Kong, several pipelaying projects are currently underway. 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 progressing well. Construction of a 9 km pipeline in the western New Territories to strengthen supply 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 regions are underway. Route planning for a new submarine pipeline from Ma Tau Kok to North Point is progressing well.

Meanwhile, construction of the gas supply trunk mains to Ocean Park Hong Kong to support new attractions, facilities and future extensions has been completed. As a result, tourists can now view spectacular fire effects fuelled by town gas at Ocean Park's Aqua City.

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

Property Developments

The entire residential floor area, consisting of approximately 1.22 million square feet, of the Grand Waterfront property development project located at Ma Tau Kok south plant site, had been sold by the end of December 2010. Leasing of the commercial area of the project is good.

The Group has a 50 per cent interest in the Grand Promenade property development project at Sai Wan Ho. Approximately 1.74 million square feet had been sold by the end of December 2010, representing over 99 per cent of the total residential floor area of the project.

The Group has an approximately 15.8 per cent interest in the International Finance Centre ("IFC") complex. Rental demand for the shopping mall and office towers of IFC continues to be good. The occupancy rate of the project's hotel complex, comprising the Four Seasons Hotel and Four Seasons Place, remains high.

Financing Programmes

In tandem with the Group's long-term investments on the mainland, HKCG (Finance) Limited, a wholly-owned subsidiary of the Group, successfully issued and sold US$1 billion of notes guaranteed by the Company (the "Notes"; stock code: 4303.HK) in August 2008 and further established a US$1 billion medium term note programme (the "MTN Programme") in May 2009. Since the establishment of the MTN Programme, the Group has issued medium term notes with, up to now, an aggregate amount of HK$3.01 billion at nominal interest rates ranging from 3.90 per cent to 5.00 per cent per annum and with a maturity of 10 to 40 years. These term notes have included the first ever issue of 30-year and 40-year notes, the longest term corporate papers ever issued, in the Hong Kong dollar bond market. The good reception to these corporate papers reflects investors' confidence towards the Group's very strong credit standing and long-term development.

In February 2011, the Group concluded a HK$3.8 billion 5-year syndicated term loan and revolving credit facility, the first syndicated financing transaction for the Group since 2006. The response to the syndication was overwhelming with an over-subscription of more than 70 per cent. This enabled the facility amount to be increased from an initial HK$3.0 billion to HK$3.8 billion backed by a total of 11 international and regional financial institutions including Japanese, American, Taiwanese, Spanish and Hong Kong banks. The success of this syndicated facility demonstrates the banking community's strong confidence in the Group's business development prospects.

Company Awards

In a survey conducted by The Wall Street Journal Asia, the Company was honoured to be positioned eighth in Hong Kong in Asia's 200 Most Admired Companies for the year 2010, which was the best ranking among energy utility companies in Hong Kong. Readers of the journal rated approximately 40 companies in each market for the year according to criteria such as innovation, long-term vision, quality, corporate reputation and financial reputation.

In addition, the Company once again gained the "Global Chinese Business 1000 – Outstanding Performance Award" for the year 2010 from Yazhou Zhoukan which ranks companies in Chinese-concentrated Asian districts such as mainland China, Hong Kong, Taiwan, Malaysia and Singapore according to market capitalisation. With a market capitalisation of US$17,860 million as at the end of July 2010, the Company's ranking in Hong Kong was raised from ninth in 2009 to sixth in 2010.

Towngas China also gained the Hong Kong Outstanding Enterprises Award 2010 from a locally-renowned financial magazine, "Economic Digest", in recognition of its rapid project development, continuous business growth and its overall good corporate strength.

Employees and Productivity

As at the end of 2010, the number of employees engaged in the town gas business in Hong Kong was 1,923, the number of customers had increased by 25,593 since 2009, and each employee served the equivalent of 897 customers, slightly up compared to each employee serving 890 customers as at the end of 2009. Total manpower costs for employees directly involved in the town gas business amounted to HK$660 million for 2010. In 2010, there was an approximately 3 per cent average increase in remuneration over 2009. 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 27th May 2011. The necessary resolution will be proposed at the forthcoming Annual General Meeting on 3rd June 2011, and if passed, share certificates will be posted on 7th June 2011.

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 27th May 2011. Including the interim dividend of HK 12 cents per share paid on 18th October 2010, the total dividend payout for the whole year shall be HK 35 cents per share.

Barring unforeseen circumstances, the forecast dividends per share for 2011 after bonus share issue shall not be less than that for 2010.

Business Outlook for 2011

The Company predicts steady growth and an increase of about 25,000 new customers in Hong Kong for 2011. Hong Kong's economy maintains momentum, with different business sectors including tourism, restaurant, and hotel sectors continuing to prosper. The Group expects commercial and industrial gas sales and appliance sales in Hong Kong will increase in 2011 compared to 2010.

In tandem with the gradual implementation of the Twelfth Five-Year Plan, the central government will advocate increasing urbanisation and domestic demand, more energy conservation and a reduction of gas emissions. With a blooming mainland economy, 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 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 anticipated that the combined results of the Group's emerging environmentally-friendly energy businesses and mainland utility businesses will reach the same level as that of its Hong Kong gas business in 2012, and will have faster growth momentum than the Hong Kong gas business thereafter.

LEE Shau Kee
Chairman
Hong Kong, 15th March 2011