

**For discussion on
25 January 2010**

**Legislative Council Panel on Economic Development
Update on Hong Kong Disneyland**

Purpose

This paper updates Members on the operation of the Hong Kong Disneyland (HKD).

Fiscal Year 2008-09 (FY09) Performance Overview

Attendance

2. Opened on 12 September 2005, HKD has just completed its fourth full year of operation. As of the end of December 2009, it has received over 19 million visitors since its opening. In FY09¹, HKD's attendance grew by 2% year-on-year, with robust double-digit growth in the first half of the year partially offset by the adverse impact of the H1N1 influenza after confirmation of the first case in Hong Kong in May 2009 and continuing through the rest of FY09. Despite such challenges, HKD continued to capture a diverse mix of guests from local market and the rest of the world. The guest mix in FY09 is 41% local, 36% Mainland and 23% international. Compared to the previous year, local and Mainland attendance increased by 4% and 10% respectively, while international attendance dropped by 9%.

3. During the year, HKD continued its partnership with the travel trade to increase sales penetration and product awareness in the Mainland, and targeted emerging markets (such as Taiwan, Philippines and India) in promoting Hong Kong as a premier family vacation destination through advertising and joint promotions with trade partners, as well as participating in trade missions organised by the Hong Kong Tourism Board (HKTB). Arrivals from India recorded double-digit growth.

¹ According to the internal financial arrangement of HKD, the fiscal year ends on the Saturday closest to 30 September. FY09 covers the period from 28 September 2008 to 3 October 2009.

4. HKD continued to maintain high service standard as evidenced by positive results in guest surveys conducted by the management company. In FY09, guests stayed an average of more than six hours in the park, and majority of them intended to re-visit HKD in the future and would recommend the park to others. 91% of theme park visitors and 97% of hotel guests rated their overall experience as “good” or above. The “Star Guest Programme”, which was introduced from March to May 2009, had received 43 000 guest compliments as well as a number of international and local awards.

5. The two hotels at HKD recorded a combined occupancy rate of 70% in FY09, representing a drop of eight percentage points from the previous year. This was mainly due to the unfavourable impacts of H1N1 and the macro-economic environment.

Special events and programmes

6. To broaden HKD’s appeal to various customer segments, a variety of theme-based events have been launched in different seasonal periods in FY09. These include “Disney’s Haunted Halloween” event with exciting entertainment elements; “Sparkling Christmas - Royal Kingdom”; “Mickey Celebrates the Year of the Ox” combining Chinese traditions with Disney creative elements; and “Celebration of Love” during Valentine. In addition, there was the “Star Guest Programme” with new products including “Star Pass”, “Star Finale” and “Star Tour” which continued throughout the spring season; and “Stitch’s Summer Dance Bash” themed on the popular character Stitch from the Disney / Pixar film “Lilo & Stitch” during the summer school-break period. These events achieved encouraging results and high guest satisfaction, showing that they were appealing to different target customer segments. “Disney’s Haunted Halloween” and “Celebration of Love” were in particular appealing to young adults, while the Christmas and Summer events catered for both family and non-family segments.

Marketing and Promotion

7. Since launching of the annual pass programme in September 2006, some 350 000 passes had been sold. HKD has also been widely recognised for its performance in the MICE (Meetings, Incentive travels, Conventions and Exhibitions) business. In FY09, HKD was granted the award of “Top 10 Best Theme Hotel of China” of the “2008 China Hotel Starlight Award” and Gold Award in the Hotels, Restaurants and Catering

Companies sector under the Hong Kong Awards for Environmental Excellence.

8. In FY09, HKD extended its sales network in the Mainland. From its existing sales offices in Beijing, Shanghai and Guangzhou, HKD reached out to neighbouring secondary cities (such as Tianjin, Shenyang, Nanjing, Hangzhou, Zhongshan, Dongguan, and Jiangmen, etc), and will set up its fourth sales office in Chengdu in the first quarter of 2010. HKD also appointed a sales representative in India to develop this potential market for the resort. Besides, HKD formed a strategic partnership with Cathay Pacific and Dragon Air to run joint promotions during slow periods. In an effort to further integrate with the travel industry, HKD waived entrance fees to registered Hong Kong tourist guides for one year starting from 1 June 2009.

Operating and Financial Performance

9. In FY09, HKD welcomed 4.6 million guests, generating revenues of \$2.541 billion which was 1% slightly lower than prior year. There was however a \$91 million improvement in loss before interest, taxes, depreciation and amortisation from \$161 million in FY08 to \$70 million in FY09. This was mainly due to continued cost containment efforts and growth in attendance despite the unfavourable impact of H1N1 outbreak on HKD. Net finance costs decreased by 36% from \$605 million to \$387 million due to lower interest rates, as well as the conversion of loans from shareholders to ordinary shares. This resulted in a \$259 million improvement in net loss from \$1.574 billion to \$1.315 billion. Following the capital realignment of Government and The Walt Disney Company (TWDC), shareholders' equity increased from \$4.606 billion to \$9.442 billion in the year.

10. To improve the financial stability of Hongkong International Theme Parks Limited (HKITP), at Government's request, TWDC waived the management fees and deferred the receipt of royalties for FY09. According to the agreement reached between Government and TWDC in July 2009, the formula for calculating the base management fee payable to the management company was revised so as to link it to park performance directly, i.e. to replace the current formula of 2% of gross revenue with 6.5% of earnings before interest, taxes, depreciation and amortisation (EBITDA). A mechanism has also been agreed that payment of royalties by HKITP would be deferred in the event that HKD's financial performance is hampered by adversity.

11. In addition, according to the aforementioned agreement reached by both parties, key operating and financial results of HKD will be disclosed annually starting with FY09, with a view to enhancing the transparency of HKD's operation. The annual business review for FY09 is at the Annex.

12. We would like to point out that HKD is a long-term asset that grows over time and it is still in its early years of development. Over the past four years, under close scrutiny of the board of directors on operating strategy and daily operations, the management company has been investing in building brand awareness and park image, and focusing on maintaining high quality services and guest satisfaction. Since its opening, HKD has received 76 awards, of which 28 were won in FY09 from local and international industry associations and publications in recognition of its world-class assets, design and technical achievements, distinctive guest services, and appeal to families.

Economic Benefits

13. HKD has generated substantial economic benefits for Hong Kong. According to survey statistics and other data from HKTb, visitors to HKD have generated an additional cumulative spending of \$24.2 billion in Hong Kong in the past four operating years, over and above what would have been spent without the park. Taking into account both the direct and indirect value added generated from these additional spending, HKD has brought about \$10.3 billion of value added to the Hong Kong economy in the first three years. This has raised GDP by an average of about 0.2% each year. For FY09, the additional value added amounted to over \$4.4 billion, raising its contribution to GDP to about 0.3%. In terms of visitors, the park managed to attract many induced tourists (i.e. tourists whose main purpose of coming to Hong Kong is to visit HKD) with the novelty effect in its first year of operation. The number of induced tourists decreased in the ensuing two years. However, with further development of the park, it has gradually built up its image and brand in the market. FY09 performed better than the last two years, with double-digit growth in induced tourists, as well as substantial growth in the average spending of base tourists (i.e. who would have visited Hong Kong even without the HKD project but will spend additional time in Hong Kong to visit HKD). The additional spending of visitors to HKD has created more than 10 000 jobs (in terms of man-years) in each of the past four years, providing considerable job opportunities for grass-roots workers and the travel industry.

Expansion Plan

14. To enhance its long-term attraction and sustainably broaden its penetration to different visitor segments especially teenagers and young adults, Government and TWDC reached an agreement in July 2009 for the expansion of HKD and the related financial arrangements. Under HKD's expansion plan, three brand new themed areas will be developed in phases by mid-2014. Of these, two of the themed areas will be the first to be launched amongst Disney theme parks worldwide, and the other one will also be the first amongst Disney theme parks within Asia. The expansion will enlarge the existing theme park by about 23% and add more than 30 new attractions, entertainment and interactive experiences (including "thrill" rides popular among youngsters), bringing the total number of attractions in HKD to over 100.

Staffing

15. As of 3 October 2009, HKD's full time workforce stood at approximately 4 400, including one of the biggest teams of entertainment and performance talents in Hong Kong. Another 1 200 part-time staff were engaged to cope with the increased demand at Halloween, Christmas, Chinese New Year, summer holidays as well as other special occasions.

16. HKD maintains an explicit policy of providing equal opportunity for all employees and offers employment opportunities for disabled persons on equal and merit basis having regard to the job nature and safety. As of the end of December 2009, HKD had employed 300 disabled staff members.

Corporate Social Responsibility

17. To reinforce HKD's linkage with local community, HKD had actively engaged in community activities mostly for children and families. Since its opening in 2005, HKD has collaborated with over 500 local charities and non-profit organisations in sponsoring free visitations to the park and other activities, benefiting over 1 million underprivileged children and families. Two examples of such meaningful community relations programmes are –

- (a) Disney Children's Fund, which was sponsored by TWDC and managed by the management company, had granted \$2 million for 16 organisations to develop creative local community programmes for children within one year since its launch in 2008; and
- (b) The management company had also worked closely with local charities and non-profit organisations in their fundraising activities at the resort including the Inspiration Lake Recreation Centre, in which more than \$10 million had been raised for a wide spectrum of beneficiaries.

18. HKD also made in-kind donations, including equipment, merchandise and complimentary offers, to local charities and non-profit organisations in support of their children and youth development programmes. About 4 000 service hours were contributed by Disney volunteers throughout the year. The management company also made donations to local charities through its "Ears to You Programme" as well as support the rebuilding of Sichuan earthquake areas.

19. To contribute to the grooming of local entertainment and performance talents, HKD awarded 12 study scholarships to students of the Hong Kong Academy for Performing Arts in FY09. It also provided 211 internship placements for students, including 130 full-year internship programmes for students of the Hong Kong Institute of Vocational Education, as well as another 81 seasonal internship programmes for tertiary institutions and community colleges.

20. To promote environmental awareness among students and the general public, the management company had added two newly designed nature trails to the existing three trails in the park. A Nature Institute was also established to recruit and train students from the Institute of Vocational Education as nature tutors.

Work Plan for 2009-10

21. As a result of last summer's agreement between the Government and TWDC, work on the expansion project has already commenced and will be completed in phases before mid-2014, with the first themed area projected to open in about two years.

22. Prior to the opening of the first themed area, HKD will mark its 5th Anniversary with new product offerings to encourage visitation

during the celebration year. The celebration will include initiatives that will engage the community in new and exciting ways. HKD will fully engage the travel trade and media partners.

23. HKD will continue to provide diversified marketing and sales approaches that maximise partnerships with the travel trade and other strategic partners. HKD will also continue to capitalise on new consumer trends, such as social networking and interactive media, to engage guests and further increase awareness of the park's products, services and experiences. HKD will continue to partner with HKTB and others to identify and develop new markets as well as augment Hong Kong's reputation as one of the world's top cities for leisure tourists and business visitors.

24. Looking ahead, HKD will remain focused on being the premier vacation, entertainment and convention resort destination for Hong Kong. HKD will continue to focus on delivering great guest experiences and building up its brand and sales channels in target markets, using special events and seasonal promotional programmes to attract visitors, optimising operational effectiveness and cost efficiency, and enhancing the park's attractiveness to encourage repeat visitation.

Advice Sought

25. Members are invited to note the update on HKD's operation.

Tourism Commission
Commerce and Economic Development Bureau
January 2010

KEY HIGHLIGHTS

- Since its grand opening in 2005, HKDL remains focused on steadily growing its business and establishing its brand as the premier vacation, entertainment, and convention resort destination in the region
- For the year, total attendance grew 2% versus prior year
- Loss before interest, taxes, depreciation and amortisation decreased by 57% to HK\$70 million in fiscal 2009
- Agreed-upon capital realignment and expansion plan reduced HKDL's debt substantially, providing for significant attractions and entertainment asset growth as well as putting HKDL on a path for further long-term success

BUSINESS OVERVIEW

Hong Kong Disneyland ("HKDL") develops and operates the Disney-branded theme park, themed hotels and associated complex and infrastructure in Hong Kong on Lantau Island. HKDL is owned by Hongkong International Theme Parks Limited ("HKITP"), a joint venture between the Government of Hong Kong Special Administrative Region ("HKSAR") and The Walt Disney Company ("TWDC"), and is managed by Hong Kong Disneyland Management Limited, a wholly owned indirect subsidiary of TWDC.

The theme park consists of the following themed lands: Adventureland, Fantasyland, Main Street USA and Tomorrowland. These areas feature themed attractions, entertainment, and interactive experiences; restaurants; merchandise shops; and refreshment stands. Additionally, there are daily parades and a nighttime fireworks extravaganza.

HKDL has two themed hotels: the 400-room Hong Kong Disneyland Hotel and the 600-room Disney's Hollywood Hotel.

OPERATIONAL HIGHLIGHTS

- Having just completed its fourth full year of operations since its grand opening in 2005, HKDL remains focused on being the premier vacation, entertainment, and convention resort destination for Hong Kong and augmenting Hong Kong's position as one of the world's top cities for leisure tourists and business visitors. HKDL will continue to market its world-class attractions, entertainment, and interactive experiences as well as lodging, dining and shopping assets to grow its business. It will continue to refresh and expand upon these offerings in order to attract new guests and generate repeat visitation, recognizing an evolving marketplace and competitive environment.
- With an aim of driving visitation from local, mainland China and Southeast Asia regions and increasing guest experiences, HKDL launched the following key events and programmes in

different seasonal periods to generate guest excitement and ongoing interest in visiting throughout the fiscal year:

- offered a variety of haunted entertainment elements during “Disney’s Haunted Halloween” event at the beginning of fiscal 2009;
 - held “Sparkling Christmas – Royal Kingdom” during the winter holiday season;
 - launched “Mickey Celebrates the Year of the Ox” during the Chinese New Year period, combining Chinese traditions with Disney creative elements;
 - offered a Valentine-based “Celebration of Love” following the Chinese New Year celebration;
 - launched its “Star Guest Program” – with new products including the Star Pass, Star Finale and Star Tour – which continued throughout the spring season; and
 - held “Stitch’s Summer Dance Bash,” an event themed on the popular character Stitch from the Disney / Pixar film *Lilo & Stitch*, during the summer school-break period.
- In addition to its strategy to grow the business, HKDL is committed to contributing to Hong Kong and its community, with a focus on staff and community programmes such as underprivileged families, environmental awareness, and volunteerism. Key actions during fiscal 2009 included:
 - engaged in more than 100 local community activities and reached out to more than 100,000 children and families from among the underprivileged, senior, and other local community groups;
 - placed more than 200 students from local vocational institutions in internships and offered 12 study scholarships to students of the Hong Kong Academy for Performing Arts;
 - donated in-kind merchandise and equipment to underprivileged groups; and
 - provided trees and contributed horticultural advisory services in support of environmental protection and conservation.
 - HKDL employed more than 4,400 full-time staff and 1,200 part-time on average throughout the year and provided nearly a quarter million hours of professional and technical development, thus further strengthening the skill sets and quality of its workforce.
 - HKDL continues to generate exceptional guest satisfaction ratings. In fiscal 2009, 91% of theme park guests and 97% of hotel guests reported that their overall experience was “excellent,” “very good,” or “good.”
 - During fiscal 2009, HKDL received more than 25 awards from local and international industry associations and publications in recognition of its world-class assets, design and technical achievements, distinctive guest service, and appeal to families. Several of the specific awards are listed below:
 - Most Popular Resort Destination of Asia, awarded by Asia Hotel Forum;
 - The Most Influential Theme Park in China, awarded by The 5th Most Influential Brands in China Summit;
 - Top 10 Best Theme Hotel in China, awarded by 2008 China Hotel Starlight Award;
 - No. 1 – Best for Families (Asia), awarded by Trip Advisor Travelers’ Choice 2009; and
 - Top 10 Family Resorts – Asia, awarded by Holidays with Kids magazine.

CAPITAL REALIGNMENT AND EXPANSION PLAN

In July 2009, the shareholders of HKITP entered into a capital realignment agreement and expansion plan for HKDL. Under the agreement, TWDC converted its HK\$2,765 million loan and revolving credit facility to HKDL into ordinary shares and made a contribution of HK\$311 million in additional capital during fiscal 2009. This was accompanied by conversion of an equal amount of the HKSAR-provided loan to HKDL into ordinary shares, leaving a balance of HK\$4,063 million at the end of fiscal 2009. Over approximately the next five years, TWDC will make capital contributions in exchange for additional ordinary shares of HKITP to fund the expansion and other financial needs of the business. HKSAR will convert an additional amount of its loan into ordinary shares equal to the TWDC contributions, subject to a maximum conversion amount that would leave HK\$1 billion of the HKSAR loan outstanding by the end of the expansion. As a result of the above arrangements, TWDC's interest in HKDL increased from 43% to 47% during fiscal 2009 and is projected to increase to approximately 48%, although TWDC's ending ownership will depend on the aggregate amount of equity contributions made by TWDC pursuant to the expansion plan.

The expansion plan comprises three new themed areas with a total land-take of about 23% of the area of the existing theme park. There will be more than 30 new attractions, entertainment, and interactive experiences bringing the total at HKDL to over 100 such assets for guests to enjoy during their visits. The new themed areas will deliver one-of-a-kind experiences to guests, as "Grizzly Gulch" and "Mystic Point" will be exclusive on a worldwide basis for five years after opening and "Toy Story Land" (all working titles) will be exclusive in the Asia region for five years after opening. The new offerings are planned to be completed in phases through mid 2014. The expansion of HKDL is expected to not only contribute further to the significant appeal of HKDL as a tourist destination, but also bring direct economic benefits to Hong Kong by providing a substantial number of construction and related jobs in the near-term and additional resort-based employment positions once expansion is complete.

KEY BUSINESS DRIVERS AND FINANCIAL HIGHLIGHTS

For the fiscal year ended 3rd October, 2009, HKDL's loss before interest, taxes, depreciation and amortisation decreased 57% to HK\$70 million from HK\$161 million in fiscal 2008, mainly due to continued cost containment efforts and 2% year-on-year growth in attendance. Despite the global economic downturn, for the period from October to April of fiscal 2009, HKDL experienced double-digit growth in attendance over the same period in fiscal 2008. However, after the first confirmed H1N1 influenza case was reported in Hong Kong in May 2009, a significant reduction in leisure and business travel ensued, resulting in broadly reported impacts to hotels, resorts and tourist attractions. It is believed that the reduction in attendance during the remaining months of the fiscal year reflected the impact of H1N1 and reduced the full year's attendance growth to 2% compared to fiscal 2008.

Key revenue drivers for the fiscal year were as follows:

Key revenue drivers	2009	2008
Park attendance (in millions)	4.6	4.5
Hotel occupancy (percentage)	70%	78%
Year-on-year change for key revenue drivers	Percentage change from 2008 to 2009	
Park attendance	2%	
Per capita guest spending	(1%)	
Available room nights	2%	
Per room guest spending	8%	
Origin of visitors as a percentage of total attendance	2009	2008
Local	41%	40%
Mainland China	36%	34%
International	23%	26%

Key financial results for the fiscal year were as follows:

(in millions)	<u>2009</u>	<u>2008</u>	<u>Variance</u>
	HK\$	HK\$	HK\$
Revenues	2,541	2,568	(27)
Costs and expenses	2,611	2,729	(118)
Earnings / (Loss) before interest, taxes, depreciation and amortisation	(70)	(161)	91
Depreciation and amortisation	858	808	50
Net finance costs	387	605	(218)
NET PROFIT / (LOSS)	(1,315)	(1,574)	259
Non-current assets	13,937	14,475	(538)
Current assets	577	874	(297)
Current liabilities	(1,009)	(3,932)	2,923
Non-current liabilities	(4,063)	(6,811)	2,748
SHAREHOLDERS' EQUITY	9,442	4,606	4,836

With a year-end date on the Saturday closest to, if not on, 30th September, the fiscal year consists of 52 weeks with the exception that approximately every six years, the fiscal year comprises a 53-week period. Fiscal 2009 was a 53-week year ending on 3rd October 2009; fiscal 2008 was a 52-week year ending on 27th September 2008.

Revenues

HKDL generates revenues predominantly from the sale of admissions to the theme park; room nights at the hotels; and merchandise, food and beverage sales at the theme park and hotels. For fiscal 2009, total revenues decreased 1% or HK\$27 million to HK\$2,541 million, driven by the unfavorable impact of the H1N1 outbreak on attendance and hotel occupancy in the latter portion of the year. Prior to the outbreak in May 2009, revenues were trending high single digits above the comparable period in fiscal 2008.

Costs and expenses

Costs and expenses consist principally of labour, operating and support costs, costs of sales, and marketing and sales expenses. The decrease of 4% or HK\$118 million to HK\$2,611 million for fiscal 2009 was attributable to savings from cost mitigation activities which were implemented throughout the year and expanded further during the post-H1N1 period.

Net finance costs

Net finance costs consist of interest expenses and other borrowing costs, net of interest income. The decrease of 36% or HK\$218 million from fiscal 2008 to HK\$387 million in fiscal 2009 was attributable to lower effective interest rates applicable to the outstanding loan balances and the conversion of loans from shareholders to ordinary shares as a result of the capital realignment during the year (See FINANCIAL LIQUIDITY section for more details).

Net Profit / (Loss)

Net loss for the year decreased 16%, or HK\$259 million, to HK\$1,315 million. This was mainly attributable to savings in finance and operating costs.

Non-current assets

Non-current assets mainly include property, plant and equipment and the leasehold land. Non-current assets decreased 4%, or HK\$538 million, to HK\$13,937 million mainly due to depreciation and amortisation charges, partially offset by the addition of assets during the year.

Current liabilities

Included in current liabilities for fiscal 2008 was a short-term borrowing composed of a secured term loan and a revolving loan that matured on 30th September 2008. On 29th September 2008, HKDL entered into a loan facility agreement with TWDC (the "TWDC loan") to finance the repayment of the short-term borrowing and to provide working capital to meet HKDL's financial and operational needs. On 2nd October 2008, HKDL drew from the TWDC loan to repay the short-term borrowing in full. The decrease in current liabilities of 74%, or HK\$2,923 million, to HK\$1,009 million was mainly due to repayment of the short-term borrowing (See FINANCIAL LIQUIDITY section for more details).

Non-current liabilities

Non-current liabilities represent an unsecured long-term loan from HKSAR which is scheduled to mature on dates through 2030. The decrease of 40%, or HK\$2,748 million, to HK\$4,063 million was mainly attributable to the conversion of a portion of this loan into ordinary shares as part of the 2009 capital realignment (See FINANCIAL LIQUIDITY section for more details).

FINANCIAL LIQUIDITY

Summary of the changes in cash and cash equivalents was as follows:

(in millions)	2009 HK\$	2008 HK\$	Variance HK\$
Cash provided / (used) by:			
Operating activities	(58)	(262)	204
Investing activities	(316)	(344)	28
Financing activities	111	669	(558)
NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS	(263)	63	

HKDL's cash and cash equivalents as at the end of fiscal 2009 decreased by 40%, or HK\$263 million, from HK\$652 million in fiscal 2008 to HK\$389 million. The decrease was mainly related to the cash used in investing activities for capital spending, including those related to the expansion plan, partially offset by financing cash flow activities. The major financing activities included the full repayment of the short-term borrowing at the beginning of fiscal 2009, which was financed by the TWDC loans of HK\$2,963 million, a HK\$200 million repayment of the TWDC loans during the year, and TWDC's subsequent injection of HK\$311 million in additional capital in the fourth quarter of fiscal 2009 to start funding the expansion plan. The capital injection from TWDC was accompanied by a concurrent conversion of an equivalent amount of the HKSAR loan into ordinary shares.

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This Annual Business Review has been prepared for information purposes. The information presents a summary of certain operational and financial information relating to HKDL.