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Plaza 66, Shanghai

CHAIRMAN'S LETTER TO SHAREHOLDERS

Ronnie C. Chan
Chairman

Results and Dividend

Revenue decreased 6% to HK$9,435 million for the year ended December 31, 2019. Net profit attributable to shareholders jumped 29% to HK$6,816 million. Earnings per share rose likewise to HK$5.01.

Underlying net profit attributable to shareholders leaped 44% to HK$3,796 million when excluding all the effects of property revaluation gain. Underlying earnings per share increased similarly to HK$2.79.

In the past year, we sold an older building in Hong Kong at a good profit. In light of our strong financial position, your Board proposes to pay a special dividend.

The Board declares a special dividend and recommends a final dividend of HK26 cents and HK63 cents per share respectively. If the final dividend is approved by shareholders, total dividends per share for the year ended December 31, 2019 will be HK108 cents. Both the special and final dividends are payable on May 20, 2020 to shareholders of record on May 7, 2020.

Business Review

This year Hang Lung Group (HLG) celebrates its 60th anniversary. On September 13, 1960, the late Mr. T.H. Chan founded Hang Lung Development Co. Ltd. Prior to that, he co-founded another real estate concern in 1955 with a partner and earned his initial capital to start the present company. The only other equity shareholder of Hang Lung at the time was Mrs. T.H. Chan who, as a nurse, had good savings. Mr. Chan's younger brother, Mr. Thomas T.T. Chen, was invited to join as the first colleague.

Upon the death of Mr. T.H. Chan in 1986, Mr. Chen became the company chair. Five years later, I assumed that position. Throughout the 60 years, we only have had five Managing Directors, now called CEOs, before Mr. Weber Lo, our present CEO, took up the post in July 2018. We are indeed blessed with very stable leadership. Weber was 47 years old when he joined us. Together with our Executive Director Mr. Adriel Chan, who is now 37, the pair should ensure management continuity for at least another 20 to 30 years.

In the past, I have managed to convince the Board as well as the individuals concerned to have our former CEOs stay on as non-executive directors. While always giving younger leaders a free hand, they nevertheless provide critical experience at the board level. Ours is an experience-intensive industry with long market cycles, each lasting many years. Unless someone has gone through two or three such cycles, it is easy to repeat the same mistakes.

That said, your Board is also cognizant of the need to invite people of younger age to join as directors. At least two facts dictate this: everywhere around the world, the average age of shoppers of luxury items has gone down significantly. This is particularly true on mainland China, our primary growth market. Second, the use of technology in our business is becoming critical and will remain so in the foreseeable future. In fact, retailing itself is undergoing revolutionary changes. I want to make sure that the Company is guided by a combination of older people with experience and younger ones with ideas.

To the Chinese, 60 years completes a sexagenary cycle and bears a special meaning. So perhaps it is right that at this point, I should provide a brief history of the Company. As the Chinese say, reviewing the past can illuminate the path to the future. Inevitably, I will touch upon the social surroundings to which we are constantly adapting, and in which we find business opportunities.

After World War II (WWII), China was embroiled in chaos for another 30-some years, until 1978 when it embarked on the Reform and Opening-up Policy. During that time, the little British colony called Hong Kong, or Fragrant Harbor, quietly thrived. When China was closed off to most of the world, it needed Hong Kong. For decades, we were the country's primary, and certainly the most convenient, window to the outside. And when China opened up, it needed us just as much. We provided much needed capital, expertise, and information, as well as adequate air and sea links. Being right next to the Mainland, none was better positioned to help, as well as to benefit therefrom.

The timing and geographic location provided Hong Kong with the first reason for its success. We should also thank the British for their contributions. The use of English was one of them; others included maintaining a relatively peaceful society, an efficient government, and a reasonable judicial system. Corruption was rife until the mid-1970's when the Independent Commission Against Corruption (ICAC) was formed. Things then got a lot better.

An unusual policy however was put in place by the British, at the latest, in the early 1970's. Since land was the only natural resource that the territory possessed, and there was not a lot of it to go round, it must be preserved. Like all colonialists, the main objective was to maximize economic benefits for the home country. After all, Hong Kong was the last major colony still in British hands. But unlike the Spanish, the French, the Portuguese, or the Belgians, the British were always in it for the long haul. They did things in order to keep the colony economically useful for as long as possible. By limiting Hong Kong's developed area to under 25% of its total landmass, it conserved this natural resource longer. I know of no other major metropolises in the world like this. In so doing, the city had to develop vertically. This drove land value up, which suited the colonial master well. They made the same amount of money by selling less, with more to sell for a longer time to come. Brilliant!

Eventually, Hong Kong became known as having the world's most expensive land and buildings. This kept the public coffers full. Land sales and real estate-related revenue such as transaction tax often accounted for over 40% of the annual government income. It enabled Hong Kong to have one of the lowest personal and corporate income taxes in the world. British companies, which dominated our economy for decades, could repatriate most of their profits. As little as possible should be left in the colony. Low taxes also attracted many foreign companies to set up businesses here and, in the process, helped energize our economy.

This was the primary reason real estate became one of the most profitable businesses in this town. Yet the British did not want to tie down their own capital in hard assets in a colony. They preferred other more respectable industries such as trading, shipping, banking, and utilities. This was why only one of the four major British "Hongs", i.e. big British corporates, had a sizable property portfolio in the city. The others usually only kept on their books their headquarters building and staff housing.

This gave the local Chinese an opportunity to dominate in residential real estate. Major commercial properties were still mainly controlled by British companies. To the extent that local family businesses owned any, they were mainly used as their own head offices. It was not until the 1970's that the local Chinese property groups ventured into the commercial sphere. We were, in fact, among the first. While we made money, in hindsight, it was a wrong decision as I will explain later.

Here is an interesting sidebar. The only British "Hong" that had a big commercial property portfolio was also the one most suspicious of Beijing and the future after 1997. They were the first to relocate their company registration from Hong Kong, and also moved their public listing elsewhere. They did not expand here, nor did they enter the mainland China market in any significant way, even to this day. On the other hand, in the late 1970's, another major "Hong" saw the opportunities enjoyed by the local Chinese and jumped

Mr. and Mrs. T.H. Chan (1st from right and 2nd from left), with their two sons Mr. Ronnie C. Chan (2nd from right) and Mr. Gerald L. Chan (1st from left)

in. They have since performed superbly in Hong Kong commercial and residential real estate, and later entered the Mainland market with equal success. Over the decades, Hang Lung had business dealings with all of them and so we knew some of the stories. Fortunate for the first "Hong" mentioned above, they have done spectacularly well outside Hong Kong and mainland China.

Starting in the mid-1950s, local Chinese residential developers began to emerge. Our founder, Mr. T.H. Chan, was one of them. Hang Lung quickly became quite a force in this new field. By some accounts, in the mid-1960's we were already one of the biggest real estate concerns in terms of total assets, next only to the British "Hong" mentioned above with many commercial properties. At the time of our public listing in 1972, we had one of the largest market capitalizations. There was another company which was marginally bigger because it was a merger of five or six families. Our growth in the 1960's was indeed phenomenal.

But that was the end of our glory. In the 1970's, we made several strategic mistakes that greatly slowed down our progress. First, having made money early, we became conservative. We bought commercial real estate for long-term hold and did not build much housing for sale. Some investment properties which we owned in the early 1970's are still in our portfolio today.

Second, our management at that time did not trust the future of Hong Kong, and so altogether underestimated the residential boom of the 1970's and 1980's. For the same reason, we did not believe in the potential of the New Territories, which was leased by China's Qing Dynasty in 1898 to the British for 99 years, hence the 1997 timeline. We had very few development projects throughout the 1970's, and the ones that we had did not make much money.

When we awakened in the early 1980's and jumped into the market, we were caught in the Sino-British negotiations in 1982 over the future fate of the territory. The market tanked, and we were lucky to have survived, thanks to the investment properties we had, which provided steady streams of rents. Even then, we still needed help from the banks to stay afloat. One might say that venturing into commercial property was part of our mistake, but the rents therefrom eventually helped to bail us out. It was only by 1986 to 1987 were we out of the woods, and it took us many more years to nurture ourselves back to financial health.

History showed that Hong Kong's residential boom of the 1970's, all the way to the end of the colonial era and beyond, was one of the biggest business opportunities that the city has ever seen. We entered the right industry but did not perform well at that time. We totally missed it. Instead, we tied down our capital in commercial real estate.

Here are the reasons why the residential sector fared better then. First, housing prices rose far more than those of commercial properties. The 1970's was a time of fast economic growth. Hong Kong's population ballooned, as many from the Mainland moved here to escape the Cultural Revolution. The U.S., Japan, and Europe were growing fast, and Hong Kong as an entrepôt benefited greatly. The rapid rise in salaries had also enabled our citizens to buy private housing. Together with the land policy described above, home prices and land prices both climbed briskly.

Something else happened that added impetus. By the early 1980's, London knew that it had no choice but to return Hong Kong to China in 1997. To the British, two conditions were high on their consideration in the Sino-British negotiations. The same was always true when they had to forgo any colony. Namely, they wanted an honorable retreat (not that there is anything honorable about colonialism), and they wanted to preserve their economic interests for as long as possible. One way to accomplish the former was to ensure high residential prices up until June 30, 1997. Anything happening thereafter would not be their business. So they did everything possible to keep the prices up.

Beijing was aware of this and so stipulated in their negotiations that only a defined amount of land could be sold annually before 1997. China was afraid that by selling too much at exorbitant prices and sending the money away, it would use up the land resource and leave the coffers of the Hong Kong Special Administration Region (HKSAR) government, come July 1, 1997, empty. Nevertheless, limiting the land supply must have helped prices remain high, something that the British had also wanted.

But the British had another reason to keep real estate prices up. They wanted to create an atmosphere of prosperity at the time of their departure. Having very high housing prices was one excellent way. The wealth effect thus produced among the locals would be powerful.

What then should be done with the huge sums of money from land sales? Increase social welfare spending! It jumped significantly in the last few years before the British had to leave. For decades, Hong Kong was known to be a model of laissez-faire government. Conservative Nobel Prize economist, Milton Friedman, thought that it was paradise on earth. The government did the minimal and let the people fend for themselves. So why, in the early 1990's, did London reverse this policy?

The combination of the wealth effect from high housing prices and the increase in social spending was to ensure that the Hong Kong people appreciated the British. If the territory continued to thrive after the return to Chinese rule, Britain would at least have retreated "honorably," having left the former colony in great shape. But if Hong Kong flopped, so much the more our citizens would appreciate the former colonial master as they reminisced about the good old days. Of late, we have seen this on our streets. I witnessed with my own eyes an elderly woman waving a big Union Jack in front of an HKSAR government building. There were also students doing the same, but they were probably unaware of the history.

Interestingly, June 30, 1997 indeed saw the peak in Hong Kong real estate prices, both for residential and commercial. In fact, we were competing for an office building whose bidding process closed that day. In hindsight, we are so pleased that we did not win. On July 2, the Asian Financial Crisis (AFC) hit and prices started to plummet in December that year. It took many years for the market to recover. Thankfully, because Hong Kong's return to China was successful for some time, real estate prices eventually recovered and in fact reached new heights.

If we had won the bid on June 30, 1997, it would have drastically changed our financial position for the worse. I doubt if we would have been prepared to buy all the residential land on the cheap during the AFC in 1999 and 2000, which eventually made us some HK$30 billion in profit. This in turn enabled us to buy Mainland commercial land outside Shanghai beginning in 2005. It extended our winning streak, the financial benefits of which we are just beginning to reap. This shows how treacherous the industry is. A single wrong move can send us back a decade or more.

There is another reason that holding commercial real estate would underperform those who churn their capital by building and selling residential properties. The boom-bust cycle in housing is usually shorter than that in commercial. Those who caught each cycle correctly, say from 1971 to 1997, would have benefited far more than those who, like us, held the property for the whole period. Even if commercial prices moved up in tandem with home prices, the summation of all the cycles from the bottom to the peak is far greater than the simple price differential between 1971 and 1997.

To be sure, not many caught those cycles perfectly, but a few came close. They are, today, the biggest players. Several others made one or more mistakes, with a few of those almost went bankrupt. But as long as they survived, they are still doing well today. In general terms, our overall performance in that period was among the second group. We were partly helped by having capitalized on the opportunities provided by China's opening-up policy. If we had not, we might well not be in this league today.

How did we catch up to the extent we did? After missing the bull market in the 1970's and 1980's, I took over the chairmanship in January 1991. A year later, I asked Mr. Nelson Yuen, now still an Independent Non-Executive Director of Hang Lung Properties (HLP), to become Managing Director. By then, our finances had already recovered but were not strong. Worse was our market positioning. We did not have any cheap land bank like many others, so we had to be extra careful when buying land. We had nothing with which to average down prices if we bought expensive. We had to make every decision correctly. Fortunately, we did.

By the mid-1990's, we were financially quite healthy and were ready for the big break. We strengthened our balance sheet greatly starting around 1995 and waited. To do nothing was not easy. The opportunity arrived in 1997 in the form of the AFC. We had prepared ourselves well, we bought land well, and eventually we sold the residential units well.

The other big break was our entering the Mainland market in 1992. Our timing was auspicious, the chosen location (Shanghai) was correct, and the strategy was sound. Together with the huge profits made from selling Hong Kong housing units, we were able to move to Phase 2 of our Mainland business – buying land outside Shanghai – beginning in 2005.

The opening ceremony of Grand Gateway 66 in Shanghai held in December 1999

Plaza 66, Shanghai

Palace 66, Shenyang

Eighteen years into my chairmanship, I wrote in January 2008 to the shareholders of HLP that we could roughly divide my tenure into three stages of seven years each — the Preparatory Phase, the Catch Up Phase, and the Take Off Phase. Between 1991 and 1997, we strengthened our financial position and waited for the big opportunity. From 1998 to 2004, we took advantage of the aftermath of the AFC to catch up. We made good money in Hong Kong residential and were encouraged by the initial successes in Shanghai. From 2005 to 2011, our two Shanghai properties roared ahead and we bought much land on the cheap in several Mainland cities for future growth. Then I concluded my presentation by speculating that what followed might be a golden era for reaping the benefits of previous decisions.

Well, it did not arrive – at least not in the time frame that I had hoped for. In 2008, I could not have foreseen the bear market that descended upon us in 2011, one which lasted until the end of 2017 or the beginning of 2018. In July 2011, I first noticed the chill and notified our shareholders. The golden era that I was hoping for turned out to be a long, harsh Winter. In the interim, we had to greatly upgrade our management team. This we have done.

Because our strategy was sound, Summer might be delayed but it would sooner or later come. In 2018, it arrived, six or seven years late! The harvest phase has now been with us for two years, and should last for many more years to come. Shanghai is still carrying the weight for us. Our six complexes elsewhere that opened between 2010 and 2016 are now performing well. One after another, they begin to blossom. Our pipeline of projects to be completed in the seven years from 2019 to 2025 is very strong. In the coming few years, we should enjoy much organic growth in the form of improving net profit, while newly added space will provide top-line increase that will later translate to bottom-line rise.

Our performance in 2019 bears out that point. Our Mainland properties in Shanghai and elsewhere both performed well, some very well. I will single out Plaza 66 in Shanghai, Palace 66 in Shenyang, Center 66 in Wuxi, and Olympia 66 in Dalian. Grand Gateway 66 in Shanghai is still undergoing Asset Enhancement Initiative (AEI), but even so, it has performed strongly. Parc 66 in Jinan is a solid development which has always contributed steadily. Even the two weaker properties, Forum 66 in Shenyang and Riverside 66 in Tianjin, are improving, albeit slowly. Spring City 66 in Kunming which opened last August has been well received by the public. For a fuller discussion of our performance, I refer readers to my Letter to Shareholders of HLP. It can be found online at http://www.hanglung.com/en-US/media-center/publications/chairmans-letter-toshareholders.

Our Hong Kong investment properties were doing well until the street riots broke out in June last year. Gains made in the first half were partially given back in the second. An assessment of the cause, the impact, and the long term future of Hong Kong can also be found in my HLP letter.

There are two particular events in 2019 that affected our results. First, we sold two mature properties and pocketed very rewarding profit. On the other hand, we parted with (through HLP) far fewer residential units in Hong Kong than in the year before.

Olympia 66, Dalian


Center 66, Wuxi

Prospects

Looking ahead, I see a divergence of the two main portfolios of our business – Mainland rental and Hong Kong rental. The latter operates in a rather mature market, and so we expect around 3% annual growth if the market conditions remain approximately the same as the past two to three years. However, the social unrest may change this, at least for as long as trouble lasts.

What is more worrisome is the long-term future of our city. For the past two decades, the primary cause for the success of our economy in general, and the retail business in particular, was the increased interactions with the Mainland. Theirs is the world's second largest economy, and is over 35 times that of ours. (Interestingly, in 1997 their GDP was only about five times ours.) They have been growing at more than 6% per annum for decades, whereas ours has been less than 3% in recent years. Alienating the citizens therefrom is definitely not a good idea. It is like a shopkeeper, or someone by his door, hitting at every other potential customer who walks in. Bankruptcy will be his or her fate.

As such, some retail outlets in Hong Kong will close down. What is amazing is that many of these shop owners participated in the recent riots themselves. If so, they deserve to lose their customers. But what about the many innocent retailers? They will become collateral damage.

I fear that the long-held positive sentiments which many Mainlanders had for Hong Kong had disappeared. In the future, only those who need to be here will come. Once their business, whatever it may be, is done, they will leave, instead of spending say a weekend here to shop and dine. For why should they?! Such an attitude, once formed, will not be easily dispelled. I do not know what can be done to reverse the damage, nor do I know how long their apprehension will last.

Another concern of mine is that the social schism in Hong Kong has been greatly accentuated by the recent turmoil. The pro-Beijing and anti-Beijing camps will further divide our community. This is what the latter group has always wanted to do since our return to China. Their decade-long efforts have scored a great success of late. This is very bad for our economy.

Before 1997, Hong Kong, as primarily a commercial city, concentrated on business with little distractions. This created much wealth for our citizens. The livelihood of the average person was greatly enhanced in the post-WWII decades. Of course, we were not perfect but things were overall moving in the right direction. For example, the 1953 great fire in a district called Shek Kip Mei forced the then government to build public housing, which basically addressed the housing problem. The riots in 1967 ushered in more socialistic policies to improve the living standards of the less privileged. The shocking corruption cases relating to the police force in the 1950's to the 1970's prompted the establishment of the ICAC in 1974.

All these changes occurred in the absence of so-called democracy. This shows that a particular form of government is not a prerequisite for social progress. Neither did we have to pay the hefty price associated with democracy. In those years, Hong Kong was consistently lauded as having one of the cleanest and most efficient governments. Even today, Singapore does not have the Western notion of democracy, yet it is praised as one of the best success stories of governance. Some people, primarily because of a deep-seated mistrust for Beijing, have decided to fight the Central Government. They want to alter our relationship with Beijing, as governed by the Basic Law, our mini constitution, which was extolled and accepted by all countries in the world when it was first promulgated. Such people think that election democracy is the panacea, but look at Taiwan. The island went through the same process in the past three decades, and its economy has gone from being very vibrant before to an economic nonentity today, with no good prospects in sight.

For Hang Lung, over half of our business is now on the Mainland, whose society is certainly not a utopia but may well remain as one of the world's most stable places in the coming decades. Their economy will likely grow at twice the rate of the West. They have the two most important qualities that make a country a good place to do business: stability and growth. As long as Beijing can avoid social unrest, the Mainland will remain an auspicious place to make money for shareholders.

Having been in business for 40-some years, I have learned two things. The most critical factor for achieving sustainable success is not how smart, knowledgeable or well-connected one is. The number one factor is to find the right place in which to do business. We cannot fight the macro environment in which we operate. As an ethnic Chinese in the post-WWII decades, where was the best place to make money? With the benefit of hindsight, I would say Hong Kong until now, and thereafter perhaps mainland China.

Taiwan was not bad in the past, except that it has become politicized 20 years before us. As such, its successful economic streak was cut short by that much. It is also considerably more corrupt than Hong Kong, before or after it became democratic. Where should successful businesses go today as the island turned political is a big question. Mainland China welcomes them, but they have to be careful how the Taiwan government would view them. Nowadays, big businesses there can no longer stay out of politics.

Hang Lung's tradition from the beginning is to stay out of politics. One should understand it, but not get involved in it. Keep a distance! For the past 60 years, we have successfully stayed on this path. Even on the Mainland today, a sizable enterprise like us can stay out of politics and still succeed. Our experience in the past almost 30 years has amply proven that.

Singapore enjoys stability and good governance. The only problem there is that the public sector is too big. Government-Linked Companies are all too powerful, leaving little room for the private sector to expand. With the population comprising predominantly ethnic Chinese and Indian, both being very entrepreneurial, there is a myriad of vibrant small- to medium-sized enterprises. But to grow to a size matching Hong Kong's top 50 or even top 100 family-owned companies is very difficult. There, you do not want to cross hairs with the government or government-controlled entities.

The other major Southeast Asia nations all have a combination of several problems: racial strife, political instability, corruption, and poor governance with weak public finance. A few others are outright dictatorships or communistic, which make the survival of private enterprises impossible. Such places are usually among the poorest.

Of all the bigger ASEAN (Association of Southeast Asian Nations) countries, Thailand is, relatively speaking, better, but the corruption there is still serious. Periodic political upheavals are also a nuisance. Malaysia has racial and corruption problems. The Philippines, while the most democratic, is probably the most corrupt. By far the biggest, Indonesia can produce, and has produced, very large businesses, but again no one wants to deal with the corruption and racial issues there. The latter can get ugly.

In the end, all these countries have poor governance standards and weak public finance. After making a lot of money over decades, an event such as the AFC can set a business empire back by a decade or more. Currency devaluation alone is sufficient to destroy big and powerful enterprises. In fact, a number of my friends in Indonesia had to flee for their lives. Even those who eventually returned had settled their families in Singapore. This is a testament to their fear for their physical security. That is no way to live!

So all things considered, Hong Kong has been the best place to do business after WWII, especially if one is an ethnic Chinese. We had a good run of 70-some years of peace and stability for enterprises to thrive. But has it ended?

Besides choosing the right city or country, the next most important question, in my experience, is what business one should engage in. Some industries require much capital or very specific expertise. Others are government regulated and need special connections. Yet others are inherently too small, such that even if one becomes the biggest and the best, it is still not that significant in the community.

In this light, real estate is a very good choice. One may rightly say that the industry is capital intensive. True, but back in the 1950's and 1960's, regulations were not half as stringent as they are today. As long as one could muster up some capital through family, friends, or banks, one could start such a business. Before Mr. T.H. Chan founded Hang Lung, he used his family savings to start his first real estate company. Similar stories were probably true of the founders of many property concerns of that generation.

Why is Hong Kong real estate a particularly good business? I can think of several reasons. First, conceptually it is not a complicated industry. Anyone with an average intelligence can learn it. Second, it is potentially a big business. Experiences in the U.S. and Australia show that the biggest percentage of the 100 or 200 most substantive families made their money through real estate. Either in Hong Kong where the unit price is among the highest in the world, or in mainland China where the population and the landmass are for all practical purposes limitless, enterprises there can become world-class in size.

Third, as explained earlier, British companies did not want to be in it. Local developers faced no discrimination and had little interference. Fourth, also as mentioned above, the then colonial government wanted housing prices to remain high. As long as one did not get caught wrong-footed in reading market cycles, just by doing a few projects one could already make a lot of money. And for the dozen or so ambitious developers, half of them now rank among the world's wealthiest.

Fifth, demand so far has always outstripped supply. Before 1997, immigration from the Mainland never waned, so housing was always in shortage. After 1997, the same still holds, but there is one more unexpected booster to home prices. It is truly ironic. The anti-government camp always opposed any government proposal, including its various schemes to increase land supply. As a result, land prices kept going up and so did home prices. Inasmuch as this was not the wish of most of the socially conscientious developers like us, it was beyond our control. We were aware of this development several years ago, and so took our time to sell our completed apartments, leading to very satisfactory profits. The anti-government crowd was shuffling money into our pockets.

This narrative amply shows why our founder made the two most significant decisions correctly: choosing Hong Kong and real estate. He was an ambitious man who wanted to be successful in business. When he first arrived Hong Kong in 1949, it was not clear what the fate of the territory might be. In those years, many Chinese used this city as a stepping stone to go somewhere else. Our founder studied that possibility as well and even lived overseas for a year. It was fortunate that he decided to return to Hong Kong. He was welcomed back to the bank where he had worked before.

A few years later in August 1955, he and a friend, also from the Mainland, co-founded Tai Lung Construction & Investment Co. Ltd. Later they were joined by two other partners. It grew and did very well. It pioneered what was then considered high-rise residential with elevators – now considered at best mid-rise with around 10 stories. Their quality was among the best, and some of those buildings are still proudly standing today. Many longtime participants in or observers of the industry would know some of them.

Being the poorest of the four partners but the most hardworking, our founder saw no point in remaining there. In 1960, he set out on his own and, with the profits he made previously, founded Hang Lung Development Co. Ltd. (In 2001, the name was changed to the present one.) The rest is history, as one would say.

Inasmuch as Hong Kong was one of the best places in Asia to do business post-WWII, it was not without challenges. There were international events before 1997, like the stock market crashes in 1973, 1987, and 1994. There were also local and Mainland troubles that affected Hong Kong real estate: the bank run in 1964 to 1965, the decade-long Cultural Revolution which started in 1966, the Sino-British negotiations in the early 1980's, and the June 4, 1989 student movement on the Mainland.

Each of those incidents, whether international or local, saw property prices plummet and scared many to forsake Hong Kong, especially the wealthy. A good number of them simply sold their businesses and moved overseas. Yet our city recovered each time and went on to thrive even more. Almost all of those who left could only look back with envy and regret. Later some wanted to move back but could no longer afford our much more expensive housing prices.

The two biggest events in the past 60 years must be the Reform and Opening-up of China, and the return of Hong Kong to her Motherland. Both turned out to yield superb opportunities for our business, although at times it did not appear to be so.

The first 30 years of China under the present ruling party was so horrific that many people did not believe in its eventual opening up, which began in December 1978. It took some 13 years before I was convinced, and only partially, that perhaps the reform was irreversible. It was good that we made the right decision.

Absence from the Mainland market in the past 20 to 30 years would mean that one has missed out on one of the greatest economic opportunities mankind has seen in close to a century. In modern history, there were only a few such cases. In the last few decades of the 19th century, the U.S. was fast developing its western territories which were gained not long before. Remember the Noon Day Gun where one could grab land for free and as much as one could take. Another big opportunity was the rebuilding after WWII, especially in the U.S., Western Europe, and Japan.

Then came the opening-up of China. Being an ethnic Chinese in Hong Kong, this was truly an opportunity of a lifetime. Having missed the residential price surge of the 1970's and the 1980's, we could not afford to miss this one as well. Not everyone is given two chances in life but we were. At least we took advantage of the second.

The other momentous event in the past 60 years must be Hong Kong's return to Chinese rule in 1997. The process was long and tortuous; it began around 1978 to 1979 and took almost 20 years. Many locals including ourselves were worried. Beginning in the fall of 1985, I had to confront the issue while working for our founder. Unfortunately, he died a few months later in March 1986 and I had to make the decision without him on whether to remain in Hong Kong. At that point, there was still time to plan for alternatives. Again fortunately, we made the decision to stay and, indeed a little later in 1992, to enter the Mainland market. This gave us the chance to completely reorient the Company to an area that bears great potential – commercial properties for investment.

In my 2004-2005 Annual Letter to Shareholders of HLP, I wrote extensively on why experienced and financially powerful Hong Kong developers had missed the huge Mainland residential market in the past 30 years. The conclusion was that even if they had tried, they might not have been able to compete with the locals. At the beginning, corruption was rife and building standards were very low, but the market was almost limitless. All this gave the Mainland developers the opportunity to grow quickly and, in some cases, wildly. Today, the market is totally dominated by Mainland entities, almost all of which are less than 30 years old.

The one Mainland market segment that Hong Kong developers could compete in successfully without being encumbered by corruption was high-end commercial properties. This was the field we chose. In some ways, we were a pioneer – back in the 1990's, we were probably the first to build large, truly five-star complexes for long-term hold. Such a strategy has served us well, and we are still expanding it.

In fact, I would argue that on the Mainland, the only property sector worth investing is ours and not residential. It does not mean that there are no more opportunities to make money in the latter, but on a risk-adjusted basis, we prefer commercial. China's economy is still projected to grow faster than most if not all Western countries. Increase in consumer spending should outstrip GDP rise, with the former growing perhaps close to 10% per annum for the coming many years. People's buying habits will continue to change, namely from quantity to quality. Owning something is no longer a major concern for the burgeoning middle-class; it is how well you own that matters. Quality goods will be in demand, such as branded items sold and bought at prestigious locations. This can only be good for our malls.

As I have written before, I believe that the best days for building and selling homes on the Mainland may be over. In the past 30 years, this sector has produced two to three dozen humongous companies that are among the biggest in the world. They are now well entrenched and powerful. If not careful, some of them may still fall, but otherwise the strong participants will become stronger. It will be difficult for new players to break in big time. They can only thrive in niche areas.

A similar situation exists in Hong Kong. In fact, it has been like that for the past few decades. The big boys of the 1970's and 1980's are still here. There has hardly been a new name in the major league since then. About 10 to 15 developers dominate the residential market. It is not a sector that is particularly growing, so I expect that this status quo will continue for the foreseeable future.

Will Hong Kong home prices increase going forward? This will mainly depend on land supply. Domestic housing demand has been steady, but thanks to the anti-government camp, land supply may remain tight. If it had not been for the recent riots and the animosity towards the Mainlanders, there would have been a good chance that, over time, more of them would come and buy homes. But now this is more unlikely. In fact, I will not be surprised if some Hong Kong citizens would decide to sell their homes and emigrate. Probably it will not be a huge exodus, so the impact may not be that significant.

There will always be a market for commercial properties. As rents come down, capital value may fall even more, given the uncertain future, and in turn the rise in capitalization rate. What exactly will happen is too early to tell, for no one knows if the street turmoil will resume or die down. There is no need to overreact at this stage. So far, transaction volume has fallen, and we will just have to wait and see. Suffice to say that it is hard to contemplate how the recent social unrest can be good for commercial real estate prices.

If my above analyses of the real estate industry on the Mainland and in Hong Kong are not too far from the truth, then we must have positioned ourselves well in the past. Two to three years ago, we had sold out almost all our Hong Kong inventory, with 10 units remaining at year-end 2019. The money received was ploughed back into our Mainland high-end commercial properties, which should do well for some time to come.

There are other reasons for retail to further boom on the Mainland. Amazingly, China with its huge population is now facing a shortage of labor, both blue-collar workers and the professional class. As the economy continues to enlarge and improve in quality, the need for a well-educated and well-trained workforce can only grow. This will put pressure on salaries. In the past two to three decades, income, especially of the professional class, has never stopped rising anyway, and this may continue for some time. These people are our potential customers. As they consume more, retailers will make more money and pay us higher rent. We are indeed in a sweet spot of the economy.

As I have explained in the past, high-end retail tenants are stickier and more inelastic than office tenants. If a neighboring building offers lower rent, the latter will easily be tempted to move. Much less so for the former. Once a mall has successfully gathered top fashion names, it is rather difficult for them to relocate. They like to flock together, for this gives every brand a better chance to sell more. As long as the landlord is reasonable and reasonably competent, these tenants will not easily move out. The steadily rising rent that follows will give the property a higher asset value. Such is the beauty of this real estate sub-segment that we have chosen.

There is another reason that quality commercial real estate will increase in value in the coming years. There is simply too much money in the world today. Funds everywhere chase after top assets in stable economies around the world. If the "deglobalization" I described six months ago does not happen, then good Chinese commercial properties will become very desirable. Companies from around the world will like to own a piece of it. And even if the world becomes somewhat bifurcated, such that Western corporates would not or could not own Chinese real estate, there will still be plenty of local commercial entities that would desire to have such assets on their books.

Today the globe is awash with cash. Since WWII ended, the world has been a relatively peaceful place. Wars have been basically limited to a few areas around the globe like the Middle East. The prolonged prosperity, first in the West and now even in the East, means a lot of accumulated wealth. This pool of money is mainly kept as cash savings or investments. The economic prosperity these owners help create is usually reflected in the stock and bond markets. In turn, people may invest in these instruments for further gains. The more successful an economy is, the bigger the investable pool of money. Consider the U.S., Japan, and Germany, etc. The numbers are big!

These astronomical sums are today lodged for the most part in banks, insurance companies, pension funds, investment houses, and the like. They have one thing in common: they all have huge liabilities, many of which with a reasonably long tenure. They need correspondingly longer-dated assets to match their books. Quality commercial buildings are one such type of asset class.

In the past, the West had a near monopoly on such huge pools of investable funds. After the oil shocks in 1973 and 1979, resource-rich countries in the Middle East joined them. For some time, only Japan in Asia had such big amounts. Singapore, although not as significant given its small population, nevertheless has concentrated its citizens' savings in a few sizeable government-managed entities. (Hong Kong's wealth is much more diversified in the hands of individuals, but there are nevertheless a few big pools.)

Then came the new boy on the block who became very big – China. Forty years of extraordinary economic climb has created much wealth. What is particularly impressive is not just its absolute size but also its speed of accumulation, which is still ongoing. It has been phenomenal. This is why even if the world becomes deglobalized and bifurcated, the domestic wealth in China is already big enough not to be taken lightly.

Then there are two other sources which indirectly contribute to enlarging the global pool of investible funds. First is quantitative easing or QE. In the past two decades or so, especially since the 2008 Global Financial Crisis, many countries have been printing money like mad. There may have been a legitimate reason in the beginning, such as to combat a financial crisis, but eventually governments have become addicted to it. It becomes a driver of GDP growth that is not accompanied by improvements in productivity. The biggest culprit here may be China, although certain Western countries may receive more headlines. Whatever the case, few major countries have proved the exception, so the world today is even more awash with money. People's wealth further ballooned and needs to be invested. Some of it will likely end up buying commercial properties.

The other source of new funds is what some call "funny money." These are financial instruments like derivatives which can give people a false sense of wealth. With the advancement of computers which are ever increasing in speed, all kinds of "funny money" is being "created." The huge velocity of money gives a false sense of having a lot of it. In 2008, it was precisely these purely financial instruments which helped wreak havoc on the world's financial system. It almost brought down the global economy, and was terrifying. Before the cataclysmic end arrived, some had benefitted greatly from such instruments. To them, it was real wealth – just as there must be corresponding real money losers – that needs to be further invested. Here again, commercial real estate may come into the picture.

It is possible that a day will come when Chinese companies, and possibly also international ones, will enter big time into the Mainland commercial property sector. Such a market is still nascent in China but can only expand over time. Of particular value to such investors will be high quality assets like ours. Whether or not we will sell is another thing. We will cross that bridge when we get there. As hard-core business people, conceptually, everything is for sale. It is just a matter of price. But for now, it is good to know that many suitors may one day knock on our doors.

In my Letter to Shareholders of HLP of even date, I wrote in considerable length about our semi-annual revaluation of assets. That is on a micro level. What I have written above presents a macro view, which also indicates that the value of our properties should only go up even if we hold all things else constant. Rising demand from the increased supply of money may by itself raise assets prices. Such is another beauty of our business. Nevertheless, for now Management does not count on such a factor in our decision-making. Instead, we will concentrate on making our properties more productive, as will be reflected in the sustained rent increase.

It is not in the genes of this Company to do much beyond what is necessary. As such, we seldom celebrate anniversaries as some others do. Ten years ago when we turned 50, we held a small closed-door event and invited former key staff from around the world to gather in Hong Kong for a day of fellowship. It was a meaningful and lovely time, but we may have to wait another 40 years from now to do it again. Until then, we will hunker down and do what we do best – create value for shareholders. We love doing that!

Nevertheless, we should take this somewhat auspicious 60th anniversary to affirm some of the values that our founder held dear. If alive today, he would turn 100 later this year. Since he is my father, I have some knowledge with which to speak.

Mr. T.H. Chan (4th from right), and his younger brother Mr. Thomas T. T. Chen (3rd from right), Mr. Ronnie C. Chan (2nd from right), and Mr. Nelson Yuen (3rd from left)

Over the years, I have only once spoken publicly about him. That was on May 27, 2015, at the portrait unveiling ceremony of the Harvard T.H. Chan School of Public Health in Cambridge, Massachusetts. I outlined the virtues of the man that he was. With the permission of my fellow directors, I have reprinted the short speech here (enclosed at the end of this letter). I think it is meaningful and serves as a reminder to Management of the values to which we should adhere.

A company is comprised of individuals. Only when each of us does our best to live and work in a virtuous manner will the corporate entity be honorable. Rules and regulations are necessary, but they will not work well without decent and honest people. The virtues detailed in my 2015 speech remain the guiding principles of Hang Lung today. Knowing my late father, he would have been most pleased to know that the Company he founded is not only financially successful today, but still cleaves to the values that he held dear and lived by so well.

I will conclude this discussion with an anecdote. It is a two-part story, of which the first was told to me by our founder, and the second was my personal experience.

In the early 1970's, Hang Lung was interested in a big piece of well-located land in Hong Kong that was being sold by a British company. My late father with a lawyer flew to London to negotiate. Everything was in order except that the counter-party privately asked for a bribe. My father refused and we lost that piece of land.

Almost exactly 20 years later, we were offered a beautiful piece of land in Beijing. The price was agreed upon. I even suggested to turn the road in front into a pedestrian street, and Hang Lung designed it with the help of an architect who was a schoolmate of mine. The scheme was accepted but there was a catch. I was asked to meet a government official at a hotel lobby and I dutifully did. It was an embarrassing meeting for I soon figured out what she wanted. I refused to open my mouth – like my father – and we eventually lost that piece of land. That woman later ended up in prison. Interestingly, the same company that beat my father also beat me.

Genes can hardly change, for better or worse. Ethics can be seen not only in what one does but also in what one does not do. A corporate culture must be built on proper values that are infused into every part of the organization.

At Hang Lung we have an unspoken policy of not hiring former government officials in order to avoid the appearance of impropriety. It is fairly safe to say that of all the similarly sized property companies in Hong Kong, we may be the only exception. We abide by this in Hong Kong and we do likewise on the Mainland.

Where does this come from? Our founder. I do not recall, throughout the years when he and I worked together, that he had any contact with Hong Kong government officials. He never hosted them nor was he hosted by them. Frankly he hardly knew them; he purposely stayed away from them. This was another reason we did not grow as fast as our peers, but we did fine. After all, being less successful in Hong Kong in the 1970's and 1980's might have made us more careful between 1986 and 1992 in evaluating the Mainland as a possible destination for investment. That opportunity served us well and will, I believe, serve us even better in the years to come.

No one is perfect and neither are we, but we try very hard – in business and in ethics. We are not the most successful real estate company I know, but we are constantly improving. One thing however I am sure and am very proud of, is that for 60 years we have kept the tradition of being among the cleanest real estate companies in Hong Kong, and now on the Mainland as well. Our first generation of leaders, Mr. T.H. Chan and later his brother and my uncle, Mr. Thomas T.T. Chen, represent the highest standards of ethics in both their personal and business lives. So is the second generation. The two previous CEOs whom I appointed – Mr. Nelson Yuen from 1992 to 2010 and Mr. Philip Chen from 2010 to 2018 – are both upright and respectable. On the other hand, the senior executives that over the years I had to personally dismiss were all for ethical reasons. I know that the third-generation leaders under Mr. Weber Lo and Mr. Adriel Chan are equally honorable. They fully subscribe to the values practiced by their predecessors.

For now, we will keep working hard to make money for our shareholders. It is fun. In the process, we contribute to the economy and help make the society a better place.

In the coming 12 months, we should do well on the Mainland. The success of 2019 should continue. I would not be surprised if we perform even better than last year in Shanghai, partly due to Grand Gateway 66 completing its AEI, although its full effects will not be felt until 2021. Outside Shanghai, I anticipate more good news in the rise of tenant sales, rents received, and rental margin. Room for advancement in all these areas is plentiful.

How well our Hong Kong business will fare will depend to a great extent on how the social unrest will end. No one can predict the outcome at this time. But as I have written in my Letter to Shareholders of HLP, our dependence on Hong Kong rental has diminished a lot in the past decade. This trend will continue.

So to Hang Lung, Happy 60th Anniversary! I should also take this opportunity to thank all my colleagues, past and present, who have contributed to our success so far. Our past was not bad, and I am sure that even better days are ahead.

Ronnie C. Chan
Chairman
Hong Kong, January 21, 2020

In 2014, the Morningside Foundation, founded by the family of the late Mr. T.H. Chan, founder of the Hang Lung Group, donated US$350 million to support the research and teaching at the Harvard School of Public Health, which celebrated its 100th Anniversary that year. In recognition of this transformational gift, the School has been renamed the Harvard T.H. Chan School of Public Health. Mr. Ronnie C. Chan, the eldest son of Mr. T.H. Chan and the current Chairman of Hang Lung Group and Hang Lung Properties, attended the unveiling ceremony of Mr. T.H. Chan's portrait at the School in May 2015. He made the following remarks in memory of his father.

Speech by Mr. Ronnie C. Chan
at the
Harvard T.H. Chan Portrait Unveiling Ceremony
Krege Atrium, Harvard T.H. Chan School of Public Health
May 27, 2015

On behalf of my family, I want to thank you for attending this portrait unveiling ceremony. Some of you met my mother who was here last September 8 when we announced the gift. She was 94 then and is now 95. I want to report that she is doing very well, although she sends her regrets for not being with us today. The reason is that next week in Hong Kong, our company, Hang Lung, will celebrate the 50th anniversary of a joint venture with a Japanese enterprise called Hakuyosha. Over half a century ago, my mother indirectly introduced the Tokyo-based firm to my late father Mr. T.H. Chan. It resulted in a wonderful collaboration which saw the friendship between five generations of the Igarashi family and four of the Chan's. Although Hang Lung Hakuyosha today accounts for less than 0.03% of my company's total profit, we keep its operations going. My family values friendship, especially long standing ones.

From today onward, everyone entering this building will see the wonderful portrait of my late father, Mr. T.H. Chan. One may well ask: who is he? He was a very private man, and although well-known to the Hong Kong community, local newspapers were unable to find a photograph of him at the time of his untimely death in 1986. In that tradition, I have never spoken publicly about him. But now with his name on the School and on the wall, perhaps it is appropriate that I should say a word today. It will probably be the only time that you will hear about him.

Mr. T.H. Chan was a VIRTUOUS man. There are many in this world who have wealth and many others who have virtue. Usually those with the latter do not have much of the former; the reverse is also, sadly, more often than not, true. There are, however, a few who have both, and Mr. T.H. Chan was one of them.

One of his virtues was that he understood the value of money. Like all businessmen, he enjoyed making money, but seldom did he use it for self-aggrandizement or unnecessary personal pleasure. He lived a simple life and always knew that he would basically give all his money away. A few weeks before his death, he told me

Mr. Ronnie C. Chan (1st from left) and his younger brother Mr. Gerald L. Chan (1st from right), with Dr. Julio Frenk (2nd from right), the then Dean of the Harvard T. H. Chan School of Public Health that he would like to leave a small sum of money for each of his three sons. I was surprised, for I was brought up expecting nothing of that sort. I thanked him, but said that I did not need it. With him having given us a good academic education and, even more importantly, a strong moral education at home by words and deeds, I had what was necessary for whatever life might bring. But since I could not speak for my two brothers, I said I would check with them. Happily, they all shared my view. So, father and son together with my mother, we made the decision to, over time, give all his wealth away. This gift is just one gesture in that process.

I will mention several other virtues of my late father. There is nothing earth-shattering; I will use anecdotes to illustrate. I believe that every one of those virtues should be shared by all public health professionals.

Mr. T.H. Chan is an HONORABLE person. He has extraordinarily high integrity. I do not recall a single time that my father brought home or otherwise hosted a government official. When corruption was a common practice in those yesteryears, this was rare indeed for a significant business leader. He must have been one of the very few in that group who ran his business – Hang Lung – from day one basically in a clean way. As I drive around the city of Hong Kong today, I can point to buildings here and there which should have belonged to him. Because he was unwilling to pay bribes, he lost some deals. Losing good opportunities is never easy for a determined and ambitious businessman, but Mr. Chan kept a good conscience. He could sleep very well every night.

Mr. Chan was a COMPASSIONATE person. Looking at me, you may be surprised that Mr. T.H. Chan was a big man – he stood almost 6 feet tall and was strong. As a young man in China where buildings of four or five stories did not have elevators, he was known to have volunteered to carry, on his back, sick relatives and friends up many flights of stairs. He was always ready to help the needy.

Mr. Chan treated everyone with RESPECT. About a week before his death, my mother and I, early in the morning, took him to the hospital from where he never returned home. I was seated with the driver in front and my parents were at the back. After the car drove past the gate of the compound where we lived, my father said to me in a very weak voice, "Why did you not greet the doorman?" Thank God that my mother saw me wave at him and told my father so. What a strong and principled man, who while dying, was still concerned that his son should treat everyone with respect.

HUMILITY was another virtue of his. He never considered himself superior to others. Perhaps two decades after his passing, I was invited one day to the private dining room of the chairman of the bank where Mr. Chan worked in the early 1950s. The head waiter greeted me warmly with a big smile. He told everyone present that he had known my late father since he himself joined the bank as a young waiter, when my father was a junior officer. No one at the bank, he said, treated him as well as Mr. Chan. One day, many years later, when my father was already wealthy and well-known, the waiter was walking on the streets of Hong Kong and heard someone loudly calling out his name with a warm greeting. My humble late father never forgot his humble friends.

Mr. Chan was a GENEROUS man. As my brother Gerald said at the announcement of this gift, he never turned away young people requesting help to further their education. I know of a story which took place during World War II. Upon noticing that a visiting friend did not have a watch on his wrist, he simply took off his own and gave it to him. Those were the years when everything was in shortage, not to mention that my father did like nice watches!

Mr. T.H. Chan was a SENSITIVE man. After his only visit in the 1970s to the Harvard School of Public Health which now bears his name, he flew to San Francisco and stayed with an old banker friend Mr. S.P. Wong. While obviously proud that his son was studying for a doctorate at Harvard, he told Mr. Wong that he was troubled. "Why should Gerald receive money from the University when we can afford it? It takes away opportunities from needy students!" We can forgive him for not knowing the difference between a fellowship and a scholarship but what a sensitive and caring person he was!

Finally, my late father was a very FOCUSED man. He focused on his business and on his family. He only had one wife and three sons and went home for dinner every day. He seldom entertained or agreed to be entertained. Trying not to be overweight – he was already a big man – he ate fish and vegetable every day and was only allowed a little red meat. Nevertheless, he had his vices – he liked cheese. My mother who, as a nurse, injected neighborhood kids with vaccines in our kitchen, also took care of my father's health. At home she would hide the cheese, so he kept it in his office. I was always delighted when he offered me a piece. Like father like son, I have the same vice today – I still like my cheese!

Today we gather here to unveil the portrait of the late Mr. T.H. Chan. I want to thank the wonderful painter Mr. Ray Kinstler for a job well done. There is a Chinese saying that one's countenance emanates from one's heart. There must be certain truths in that statement. On that count, Mr. Kinstler has done an excellent job portraying a man who is virtuous and kind at heart. Mr. Chan's many virtues came through well in this beautiful piece.

I also want to thank Dean Julio Frenk for organizing this wonderful portrait to be painted and now to be hung for posterity. Once again, I thank all of you for gracing us with your presence.

Addendum to Chairman's Letter to Shareholders

Our last Board meeting was held on January 21, which was also the date of my year-end letter to shareholders. I mentioned in my Hang Lung Properties (HLP) letter the new coronavirus disease or COVID-19 which has already been spreading in Wuhan. At that time, people did not fully recognize its seriousness. However, only a few days later, in fact right before Chinese New Year (January 25), China and indeed the world woke up to the severity of the epidemic. Since then, a lot of bad news has been reported, not just from the epicenter but also beyond. Doubtless, it will negatively impact our business, hence this Addendum.

My plan was to write this Addendum as late as possible, right before we have to go to print, with the hope that more information will be forthcoming. Unfortunately, there is still no end in sight to the problem. Perhaps the only good news is that some experts believe that the spread of the epidemic may be peaking. Whatever the case, being for long years associated with the field of public health, I have of late been in touch with many top experts from around the world and do my part to help, especially in the two places where we operate our business – mainland China and Hong Kong.

Wuhan, where Heartland 66 is being built, has for a while now been sealed off from the outside world. Most transport links between mainland China and other countries have also been cut, and that includes Hong Kong as a Special Administrative Region. Retail everywhere in China has fallen. A mall is considered lucky if footfall does not drop by 80% or more. Luxury sales on the Mainland tumbled in the past month. On January 25, we announced to our Mainland retail tenants an across-the-board cut of 50% base rent for three weeks. But the situation is still very fluid. We will work with our tenants to alleviate the potential impacts on both sides.

As mentioned in my HLP letter, since the fourth quarter of last year, in Hong Kong we had to give some rent relief on a case-by-case basis. This was due to retail slowdown brought on by the social unrest. Just as that trouble appeared to have moderated, we found ourselves hit with the novel coronavirus outbreak. The only positive outcome of the latter is that it would make large-scale street riots less likely. However, the impact of the invisible virus on retail is expected to be greater, although more short-lived, than the visible social turmoil.

In my letter to HLP shareholders, I presented a "somewhat harsh scenario where Hong Kong rents would fall by 5% per annum for the next two years." This was based on the assumption of prolonged social turmoil. If the epidemic is over by April, then I am hopeful that our Hong Kong rents for 2020 would not drop by that much, although it is not beyond the realms of possibility. As before, we will negotiate as needed with each tenant regarding rents. Past experiences here and elsewhere show that there should be a rebound once a public health threat is over. The negative effect also will not extend to a second year.

When the 2020 budget was formulated late last year, we were projecting a very good year on the Mainland. The performance in January was indeed strong until the last week of the month. Since no one knows when and how the epidemic will end, it is impossible, at this stage, to project full year results. It is possible that the anticipated rental growth in the high teen numbers may be halved or even more.

Construction projects everywhere will slow down, especially in Wuhan. At the media and analyst conferences right after announcing profit (on January 21), I commented that we needed to watch out if construction workers would return to Wuhan to work after Chinese New Year. Since then, Beijing has extended the holiday season for the entire country to February 16. Construction everywhere, however, has yet to resume work until the government gives its permission. In some cities like Wuxi and Tianjin, all malls (and other places where people congregate) were ordered to close. Only today will Center 66 in Wuxi reopen. We are currently applying for Riverside 66 in Tianjin to do business again.

Our hope is that, instead of the third quarter, Heartland 66 in Wuhan can still open before the end of the year. The Asset Enhancement Initiative (AEI) at Grand Gateway 66 in Shanghai may also be slightly delayed, as will other projects under construction, like our residential developments. As well, we will need to see how luxury brands will react after the COVID-19 epidemic is over. We hope that negotiations on new leases will not be too much affected.

I am gratified to report that under the capable leadership of our CEO, Mr. Weber Lo, the morale of our colleagues everywhere is high. Of our 200 or so staff in Wuhan, a little over two dozen are Hong Kong citizens. The leader in fact volunteered to stay there with his team. I salute all of them! Needless to say, we at the head office are in constant contact with them, and will do our utmost to support them.

Whilst the epidemic, which has brought with it tragic loss of life and a profound impact on business, is deeply regretful, nevertheless history tells us that the market will recover once it is over. We firmly believe that this short-term setback will not affect our longer-term prospects. Our future is still bright.

Ronnie C. Chan
Chairman
Hong Kong, February 21, 2020