How to Invest HK$100 Billion
for Our Future

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(3.1) "Gateway to the World" HK$22bn

- An 11m sf "Destination" commercial complex at the airport. Gateway to the World will provide the highest levels of convenience and services possible in the world by making them available to our Global Customers as they step off the plane or arrive by land. The Greenest new town in the world, "Flying Dragon" with capacity of 700,000, will be built in Tung Chung. In the future, most residents will leave zero carbon footprint when they go to work at GTTW. Minimal commuting also makes more time for family life

(3.2) "Sub-Culture" HK$10bn

- A 2m sf underground mall "Sub-Culture" at the 8m sf West Kowloon Cultural District will bring Significant Patronage to Art offerings. Net profits, at an initial HK$1bn, will add 35-40% to annual public art and culture budget, opening myriad possibilities for our Cultural Repertoire including contracting series of world-class performers as regulars and Redefining Art Skyline for the World City of Hong Kong

21st April, 2012

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(4.3) Adopt an Accretive Population Policy to attract Global Talents and the Well-to-do's & improve Capabilities, Connectivity & Diversity of this World City

(4.4) HK$40bn in Expanding Medical Capacity and Capability to keep our People Healthy & Active

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P. 105 (2) Invest HK$10bn in a 2m sf "Sub-Culture" underground mall in the West Kowloon Cultural District to (1) enhance TST's retail quantum and range of experience so as to reinforce the area as the top-grossing global shoppers' paradise and (2) generate recurrent income to support the development of arts and culture in Hong Kong

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How to Transform Hong Kong into a World City

HK'S DEVELOPMENTAL BOTTLENECKS	HK$100 Billion Investments	Hong Kong the World City
SHORTAGE OF LIVING SPACE	Develop **Tung Chung** into the most desirable (**green** & **high growth**) **New Town** in the world	Greenest World City
SHORTAGE OF COMMERCIAL SPACE	Build "**Gateway to the World**", an **11m sf** service complex at Hong Kong International Airport	No. 1 IFC - Vibrant Economy
	Build "**Sub-Culture**", a **2m sf** underground mall at the 8m sf West Kowloon Cultural District	Cultural & Value Exporter
IMPENDING LABOUR SHORTAGE & RETIREMENT BOOM	Add **10,000** publicly-subsidised **University Places**	
	Expand **VTC & ERB Retraining Capacity** to accommodate **40,000** more trainees per year	Service Paradise
	Attract **200,000 Global Talents** over the next 10-15 years	
AGEING POPULATION & MEDICAL CRISIS	Hire **4,000 New Doctors** over the next 10-15 years	Prosperity for All
	Build **New Hospitals** to add **7,000 New Beds** to the medical system	
POOR AIR QUALITY	Replace **4,000 Euro-I & II old Buses** by cleaner new models	Compassionate & Harmonious Society
CULTURAL DESERT	Kick-start construction of **West Kowloon Cultural District** and Open **25%** of the area by 2018	

HKGolden 50

How to Invest HK$100bn for Our Future

Hong Kong is a small city with big energy, colours and imagination. Our short history is marked by dramatic disruptions and challenges that could have easily sidelined Hong Kong. What has enabled Hong Kong to defy that fate and bounce back stronger is the abundance of good sense, dare, hard work and the big heart of our people. There were moments of weakness but there was never danger of a “death of Hong Kong”.

When hubris has turned into humility 15 years after the return to motherland, we are ready to take our first step forward, to writing the first page of what history will describe as Hong Kong’s Golden 50 Years. Success is all the sweeter and more meaningful after painful struggle, wracking of brains, self-doubt, toil and sweat, agony, debate and introspection transform into a community consensus to reach up, invest and re-invent Hong Kong into a World City alongside London and New York.

This is not a stating of vision but reporting of facts and trends that were conclusions from our previous two reports. In stepping up to this new future, we should not repeat the “tinkering” approach of the past, adding a bit here, taking a bit off there. The starting point should be, after establishing what The World City of Hong Kong requires in functionality and in spirit, we will proceed to procure using the many policy tools at hand, including fiscal incentives and immigration measures or to build them ourselves, removing bottlenecks in our current unhappy system along the way.

The designing of the end-product to this transformation, the World City of Hong Kong, must fully reflect the value system and soaring aspirations of our community which often requires best-in-class performance, and the potential of our economy. And all the three pre-conditions for this take-off are already present and in abundance, except the heart to make that change: (1) the demand / market – the need for commercial and community spaces are clearly present, as reflected by high rents and prices (2) capital – there is abundant cash in private and public sectors to finance the upgrade in capacity and capabilities (3) value system – the imperatives for green living and a compassionate and harmonious society are clearly understood. As the material aspects of transformation are already present, the change can be made in a proverbial heartbeat, as and when our community delivers the greenlight by forming the consensus to move forward.

The diagram on the previous spread outlines this process and the table below summarises the investments we must start to make.

Proposed Investment

HK$ bn	HK$ bn	Proposed Investment
22		Destination Commercial Complex "Gateway to the World" (GTTW) • 4m sf mall, 10,000 car park slots, 6-8 hotels with GFA 3m sf (3,000 rooms) & 1m sf office for credibility industries & NGOs; Community New Town "Flying Dragon" for 700,000 people in 20-30 years
10		WKCD Underground Mall "Sub-Culture" • 2m sf shopping space
	32	**Sub-total: Hardware**
6		Replace all old buses (70% of bus fleet) by incentivising bus companies to reduce roadside emission by 40%
3		Expanding current retraining facilities by 20% to help alleviate annual 0.4-0.8% drop in workforce
0		Adopt accretive population policy to attract talents and entrepreneurs that can improve Hong Kong business connectivity with China and the world - these will create jobs and income opportunities to Hong Kong. Target some 200,000 overseas and mainland talents over 10-15 years
40		Build more hospitals to expand capacity of public medical system by one-third
15		Add 10,000 (67%) university places to seed quality workforce we will need and to export values of this World City
4		Adequate funding to open 25% of WKCD by 2018 and supporting local art and culture institutions
	68	**Sub-total: Software**
100	**100**	

Source: Government Budget 2011/12, HKGolden50

1: Summary: Hong Kong has a destiny to fulfil – to become a World City. It is high time our whole community awoke our "can-do" spirit and started building that future by investing our private and public capital from today

(1) Opportunities in the "Golden 5 Years" of 2010-14 will likely "Gift" us more than HK$350bn in Fiscal Surpluses[1]

"How to Invest HK$100bn for Our Future" aims to provide concrete proposals on what investments our community and government should make in order to direct Hong Kong from the decade of 2000-2009 which was "lost" to anaemic growth, self-doubt, own-goals, missed-opportunities and self-pity back to its "natural" destiny of becoming a World City alongside London and New York City[2].

Our second report has already outlined the essential initiatives that Hong Kong urgently needs to take, and now this report transforms those initiatives into actionable public investments and policies to enhance the capacity and capabilities of our world-class service sector which provides over 90% of our jobs and incomes.

We have clear and present need for a bigger, better and more compassionate Hong Kong

Inflow of plentiful opportunities, talents and capital in the immediate few years have blessed us with windfall fiscal surpluses that set records - more than enough to make good deficiencies and mistakes of the past decade and re-equip Hong Kong for a far brighter future

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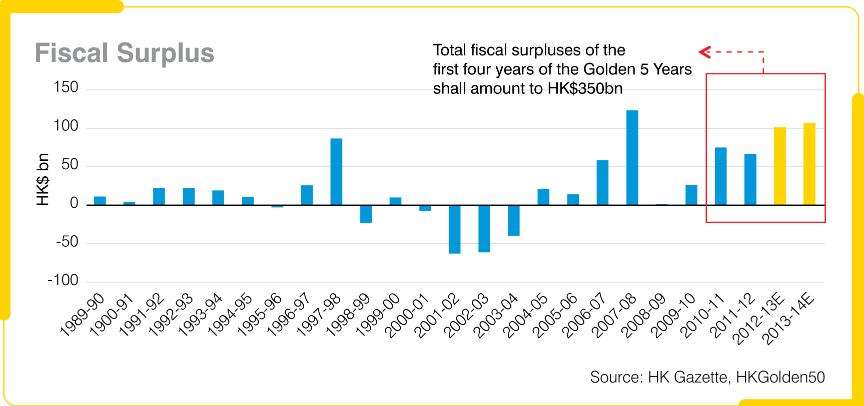
1 Please refer to our first report, "Hong Kong - The Golden 5 Years (2010-2014) and the Decline that may follow...?", Sep 2011
2 Please refer to our second report, "How to become a World City: Lessons from London", P. 8-84, Dec 2011

HKGolden50 is an independent, non-political and non-profit research organization whose mission is to illustrate through hard facts and figures the significant tasks the community and the government must undertake in order to convert the tremendous inflows of business opportunities, talents and capital during 2010 to 2014, "the Golden 5 Years" as we term it, into foundation for a more prosperous, vibrant and compassionate society for the next generation. HKGolden50 has two core beliefs: (1) the best 50 years of Hong Kong are ahead of us, and not behind us (2) taking over the baton to make Hong Kong a better place is the responsibility of the post-80's, our best-educated generation.



The report starts with illustrating our fiscal health. We estimate that following the large surpluses already recorded during the previous two fiscal years (2010/11 and 2011/12), Hong Kong will continue to enjoy remarkable surpluses of more than HK$100bn, or 4-5% of the territory's GDP, in the coming two fiscal years (2012/13 and 2013/14). The recurrence of significant fiscal surpluses is a direct product of strong structural demand for Hong Kong services during the Golden 5 Years and these provide the wherewithal to support our proposal to invest HK$100bn in Hong Kong.

Public capital is abundant for Hong Kong – amounting to 4-5% of GDP each year and an estimated HK$350bn in the first four years of the Golden 5 Years

This sum is transformative in scale, enough to make good a significant part of our previous underinvestment in hard and soft infrastructure of this service capital of the world. For instance, HK$100bn can fund the construction of more than ten Hong Kong University of Science and Technology (HKUST). Yet this sum represents only slightly over one year's expected fiscal surplus or 28% of our forecast fiscal surpluses over the first four of the Golden 5 Years totalling HK$350bn.

HK$100bn public sector investment plan will transform Hong Kong but is highly affordable as it represents only 28% of forecast fiscal surpluses (HK$350bn) over the first four of the Golden 5 Years

Furthermore, the HK$350bn surplus will come on top of the HK$600bn already held in reserves that academics have argued to be deployable by the government without impairing the health of our currency peg system. While we must never be complacent about our privileged fiscal fortunes, and indeed the ill winds from the European debt crisis may blow over our shores and sap our economic vigour, we are nevertheless well fortified to exploit any softness in prices of building materials and labour market to execute our investment plans. This will not only safeguard our jobs but also enable us to lock in building costs at cyclical low levels.

The HK$350bn forecast surplus will add to the HK$600bn deployable fiscal reserves. Total thus accumulated of HK$950bn amounts to some 50% of GDP and three years of public expenditure – more than enough to fund new infrastructure for Hong Kong and (1) insulate our jobs against any threats from crises overseas while (2) enabling us to bargain hunt for low building costs

For a fuller context of what size of a shock our forecast cumulated fiscal reserve of HK$950bn can buffer our economy against, we can refer to the HK$165bn total fiscal deficit from 2001/02 to 2003/04. This was the biggest deficit period in our history and represents the biggest stress-test to our system, brought on by a collapse in home prices (70% down from 1997 peak), an over-leveraged private sector, discontent over a number of public policies, deflation of 6%, unemployment at 8% and SARS. It is absolutely necessary for us to prepare for rainy days, but we should question the need to stock up for a biblical flood.

"Stress test", anyone? Forecast cumulated surplus of HK$950bn is almost six times the cumulated deficits of 2001/04, the most stressed period of our recent financial history

We highlighted in our first report[3] why the good fortunes during the Golden 5 Years may not run any longer. Though demand for services in Hong Kong should be robust over the five years, the growth in our ability to keep the quality of our services at high levels will be choked off by the twin shortages of hardware (hotels, shopping centres, offices, housing, hospitals, universities etc) and software (the expected retirement of some 300,000 workers, or over 8% of total, from our workforce in the coming decade).

There may not be a Golden 6th Year as acute shortage of most types of property and workers will send inflation and costs beyond the acceptance of Hong Kong's customers, our citizens and businesses

The unprecedented strength of demand in the first two years of the Golden 5 Years (2010 and 2011) has already completely removed any slack in our service capacity so much so that rentals and wages stood at or very near their all-time-highs at the end of 2011, triggering core inflation of 6.4% as compared to the average CPI of 0% in the first 14 years of the handover. We expect inflation to stay in the 5-8% range for the remainder of these five years which will undermine our cost competitiveness and chase customers away from Hong Kong, potentially bringing about a "growth recession" beyond this period.

3 Please refer to our first report, "Hong Kong - The Golden 5 Years (2010-2014) and the Decline that may follow...?", P.8-11, Sep 2011

(2) Four important Considerations behind our Call to Invest HK$100bn and Build a Bigger, Better and more Compassionate Hong Kong:

Before delving into the details of our forecast fiscal windfall, it is important to appreciate the context of the Hong Kong economy in the Golden 5 Years which forms the basis of our call to tackle our two growth bottlenecks.

(2.1) A "Demand Surplus" Hong Kong stands out in a sickly "Demand Deficit" World in which Governments are Willing but financially Unable to help; but is an Able but Unwilling Hong Kong Community better off?

Debt/deflation spiral has incapacitated most western government's wish to create more demand and jobs

While much of the western world is struggling to create demand and employment growth, most governments have found it uphill struggle to help in the healing process against a mountain of private and public sector debts and an de-leveraging/asset deflation spiral. Extreme measure after extreme measures have been administered but there does not seem to be any end to QE's and similar stimulative programmes.

Uniquely, Hong Kong should be snug as a bug but instead it feels stuck in a hole

On the diametrically opposite end of the misery scale sits fortunate Hong Kong which uniquely faces a "demand surplus" problem. In a normal situation, this is a "happy" problem as excess demand means more profits to be made which in turn incentivise the investment in more supply capacity to the point that this excess demand is met. Yet, this problem is not a happy one in the case of Hong Kong as the limiting factors to meeting excess demand are more land and labour – both of these cannot be "created" by the private sector. However, our government does hold sway in both. Unlike most western governments that have their fiscal hands tied, ours is brimming with surpluses and more than able to create needed hardware and productive workers to hold down the incoming opportunities for our current and next generations. It is high time Hong Kong summonsed our legendary "can-do" spirit to re-invigorate our entire society and take our city to a much higher level.

We believe it is the responsibility of both the private and the public sectors to face up to the potential of our community and make up for the underinvestment in our city over the past decade. We already have the means, all we need is the will. A surplus of HK$75bn was registered in the 2010/11, marking the start of the Golden 5 Years, which has continued to bless us with another HK$67bn recorded last fiscal year (2011/12). Taking the forecast surpluses for the next two fiscal years together with the previous two, the first four year of the Golden 5 Years should see cumulated surplus of HK$350bn and set new record for serial surpluses in Hong Kong:

Abundant fiscal surpluses in the Golden 5 Years to fund "remedial & essential" investments to secure Hong Kong's future as a World City

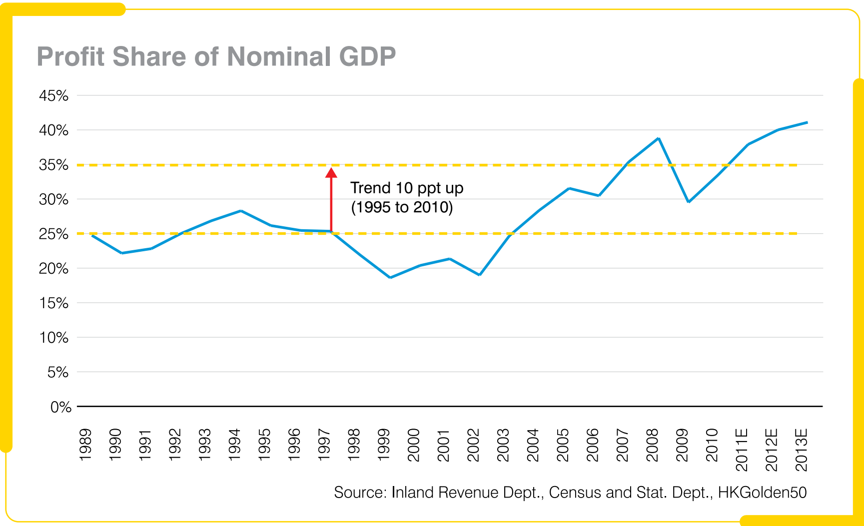
Fiscal Surpluses and Projections

(HK$ bn)	2010/11	2011/12	2012/13E	2013/14E	First 4 years of the Golden 5 Years
Profits Tax	93	119	133	148	493
Salaries Tax	47	56	63	68	234
Stamp Duties	51	43	51	57	202
Investment and others	125	132	162	186	605
Revenue before land	316	350	409	459	1,534
Expenditure	(303)	(366)	(398)	(442)	(1,509)
Surplus/(Deficit) before land	13	(16)	11	17	25
Land Premium	62	83	90	90	325
Surplus	75	67	101	107	350
Nominal GDP	1,742	1,894	2,099	2,338	8,074
Surplus % of GDP	4.3%	3.5%	4.8%	4.6%	4.3%

Source: Government Budget, HKGolden50

We expect profits to increase at a double-digit rate and above the rate of GDP growth. This reflects the strength of business opportunities in the Golden 5 Years. In 2007/08, profit share of nominal GDP reached 38% which is 10 percentage points higher than the previous peak over 1994/97. The ratio dipped to c.30% after the 2008 global financial turmoil, but quickly returned to the higher trend level of 34-38% after just one year. We expect this ratio to continue climbing as demand conditions remain robust which will drive up profit tax revenues in the next few years until surging business costs of rents and wages have started to scare customers away, causing revenues to slow and margins to erode towards 2015.

Strong influx of business opportunities likely to re-set records for profit and salary taxes



That said, one man's poison is another man's meat – while a business moans about exorbitant rents and wages, the landlord books obscene revenue and the workers pocket fatter pay cheques – contributing higher profit and salary taxes to the Inland Revenue just the same. Hence, insofar as Hong Kong receives more payment for our services, the taxman will always take a higher toll even though the taxpayer may vary along the value-adding chain.

As documented in the latest Hudson Report which studies the employment expectations of firms, hiring intentions of the economy have remained robust despite a crippled external goods trading sector, with the bright spots being consumer goods, IT, manufacturing/industrial and media – all having 20%+ net increase in hirings and next to zero intentions to retrench in the second quarter of 2012. When people employed are standing at an all-time-high, companies will have to pay up to retain talents in 2012.

Contrary to general belief, hiring intentions and by implication, expectations to make more profit with additional staffing, have remained robust despite more troubles on the western front

Permanent Hiring Expectations 2012Q2

	Increase	Steady	Decrease	Net Increase
Banking and Financial Services	38%	52%	10%	28%
Consumer	48%	51%	1%	47%
IT & T	49%	48%	3%	46%
Manufacturing & Industrial	44%	55%	1%	43%
Media/PR/Advertising	26%	74%	0%	26%
All Industries	41%	53%	6%	35%

Source: Hudson Report

Stamp duties for 2011/12 have fallen to HK$43bn. Reflecting lower property transactions after the imposition of tougher stamp duty rules and tighter mortgage criteria the previous year. "Investment and other income" of the government was affected by volatile capital markets and has therefore only managed to register modest increase compared with 2010/11. Looking to 2012/13, we expect a more favourable market consequent to a strong job market and prospect of a prolonged period of negative real interest rates and a more favourable domestic investment environment to benefit both stamp duties and investment income to benefit both stamp duties and investment income and this source of income should increase to HK$162bn this year.

Land premium has contributed HK$83bn to the coffers in 2011/12. We expect to see higher levels of land premium in the coming fiscal year as developers may well react to surprisingly strong space demand and re-stock buildable sites after achieving healthy sales in 2011.

The highest land premium in the history is recorded in 2011/12

On the expenditure side, total government expenditure was HK$366bn in 2011/12, up 21% yoy. We project this to grow 9% to HK$398bn in 2012/13. Taking expenditure against revenues, fiscal surpluses of HK$67bn resulted last year and HK$101bn should arise for 2012/13, representing 3.5% and 4.8% of GDP in their respective years

(2.2) Retail/tourism - the First in a Stream of Opportunities that will arrive in Hong Kong when "One country, one market"[4] unfurls in the Golden 5 Years and which has clearly Demonstrated its potency in Creating job/income/fiscal receipts

When man-made barriers in the mainland to the natural flow of customers, talents and capital are lowered, Hong Kong services will enjoy a long period of structural growth

Retail and hospitality sectors provide some 30% of our jobs. These sectors are critical to the new economy Hong Kong is building in this coming decade for two reasons.

Firstly, they are amongst the first in a stream of service industries in Hong Kong to benefit from the growing opportunities of "One country, one market" when man-made administrative barriers that have hindered the voluntary movement of capital, talents and customers to come to Hong Kong are gradually lowered.

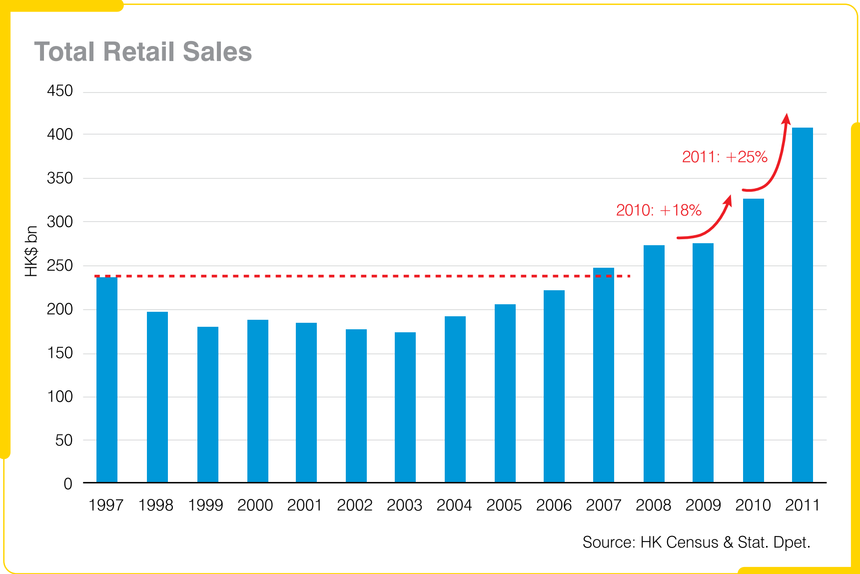
This process will create a rapid rise in customers across a range of industries ("J-Curves"[5], as we described this phenomenon in our first report), quickly straining capacity and clipping our ability to serve. The timing of the arrival of such demand will differ from industry to industry. Retail and hotel sectors are at the forefront of this structural increase in demand for Hong Kong services.

4 Please refer to our first report, "Hong Kong - The Golden 5 Years (2010-2014) and the Decline that may follow...?", P.8-12, Sep 2011

5 Please refer to our first report, "Hong Kong - The Golden 5 Years (2010-2014) and the Decline that may follow...?", P.16-21, Sep 2011

Retail takes the lion's share of our family purse, thus forms one of the biggest sectors in our economy. This sector took a hit from the Asian financial crisis in 1998 which also brought on a collapse in our home prices. It was not until 2007 that retail spending recaptured its 1997 level. There was some growth in 2008 and 2009 but in 2010, retail took off, rising 18% and marking the start of the Golden 5 Years. The next year, when global demand sagged which brought our export sector down with it and when the Hang Seng Index fell through the 20% correction territory, officially marking a "bear market" for out stocks, a defying retail sector accelerated, and posted a 25% rise. It does seem, therefore, that a strong structural uptrend in demand is happening in Hong Kong which has more than offset global cyclical recessive factors.

Retail sales defied weakness in exports and a bear market in stocks to surge a further 25% in 2011, marking a c.50% growth in just two years – evidencing the arrival of the Golden 5 Years



We have argued that the most important economic policy for Hong Kong for the next decade should not be the dollar-peg, Rmb policy or global financial performance, but rather, how to promote the freedom for mainland customers, talents and capital to choose and use Hong Kong services. The irony is that while Hong Kong enjoys almost complete porosity of two-way movement in these categories with most of our trading partners, it is with our motherland that two-way porosity, in particular, the inflow to Hong Kong, that has been obstructed for well over a decade.

With familiarity, comes fondness. The more times a person visits Hong Kong the more knowledge the person will know about our city. Some may acquire a liking to our system of values, efficiency, openness, soft infrastructure etc and may want to work or live in Hong Kong. Hence, a jump in visitor numbers presages inflow of talents and residents and at some stage perhaps, the setting up of businesses in Hong Kong for the efficiency of Hong Kong to conduct "head office" functions including treasury operations.

Some visitors may get to know and like Hong Kong, and may stay or even bring their businesses to be managed from this city

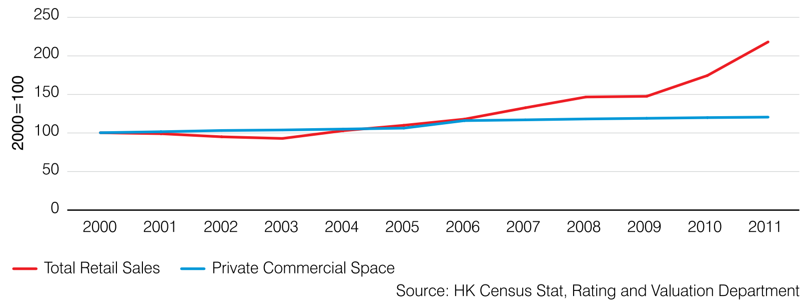
Thus, demand for retail spaces should, in time, lead to demand in office/hospitals and housing spaces. It is logical that, with the structural uplift of demand for our services, starting from hotels/retail, and migrating to financial/professional/administrative and educational/medical offerings, more opportunities for income growth will open to our people. The proviso is that more property to cater for this inflow, across retail/hotel/office and hospitals/universities/schools etc have to be produced in order to house these opportunities.

As a sequence of demand types arrive at Hong Kong, a sequence of worker and property shortages will appear, starting with hotels and retail

We have argued that in the past decade or so, our competitors north and south of Hong Kong may have taken over 300,000 finance and business service jobs (half the current size of this sector) from us as we simply have not produced enough hardware and skilled talents to capture these opportunities. Just as before, opportunities wait for no one – if we want our post-80's generation to have a wide and varied jobs platform to parade their skills, we must seize these few years to build it.

We may have already lost over 300,000 high-pay, high-skilled jobs (half the current size of this sector) to competitors in the past decade, and will lose more if we do nothing to lock these opportunities down today

Supply of Retail Property Has Not Responded to Doubling Retail Demand (Sales) Over Last Decade



Source: HK Census Stat, Rating and Valuation Department

"Too much of a good thing" can be a very good thing if we build more shopping centres and hotels; otherwise (1) surging retail rents will pass on to local customers, entrenching inflation while (2) visitors will be appalled by long lines, packed shops and tiny but expensive hotel rooms and stop coming to Hong Kong

Faced with a rising wall of demand, government and developers have somehow failed to react with new supply

The way Hong Kong has reacted to the surge in demand for retail and hospitality services is worrying – in response to the 48% jump in retail sales over 2010 and 2011, for instance, the increase in retail spaces was only 1%, and with no noticeable pick up in supply in the pipeline. Similar situation is observed in the hotel sector. While government should shoulder some of the blame for not providing enough land for such projects or not inducing their production through faster premium negotiations and redevelopment approvals, it must take the bulk of the blame for putting society's priorities wrong.

The government and developers must get the priorities right – more hotels, shopping centres, offices, homes, in that order please?

For instance, an objective measure of relative shortages of types of property is the extent to which rents have risen and independently produced data show that hotel rates rose some 40% in 2011, retail spaces 20-35%, office spaces around 20% and residential homes 6%. Indeed, measuring such rises from the previous peak of the property market, office and retail rents are more than twice their levels in 1997 while hotel rates have risen even more than that, with residential rents barely reaching their old highs. Yet, the October 2011 Policy Address did not mention the need for more hotels and retail spaces. There was some focus on producing more office in Kowloon East but these initiatives will not yield new spaces in another five to eight years and should have been undertaken a few years ago to allow for the delivery lag but the bulk of the policy limelight was put on producing Home Ownership Scheme units.

When occupancy of all types of commercial spaces is at or near all-time-high and supply is near all-time-low, our community should equate lack of new spaces with loss of job/income opportunities. When there are no new hotels, there is no point for graduating in hotel management. When there are no new office spaces for top quality asset management firms, there is no prospect for an MBA finance student in considering a career in fund management. When there are no new hospitals, there are no spaces for doctors and nurses to practise their skills.

Efforts to produce our best-educated generation are in vain, when graduates of hotel management cannot find a hotel to manage, fund managers cannot find an office to work from and doctors fail to find new hospitals to join

Perhaps epitomising the underinvestment in hardware, Hong Kong built no new hospitals in the past ten years when eight were completed a decade before that. Does it make sense that while we had 11% more people and we had older people compared with the previous decade, our hospital needs should be less?

Secondly, the retail and hospitality industry provides a lot of jobs for low- and semi-skilled workers.

This is especially important for us because we have received some 700,000 migrants under the 150-a-day quota from the mainland who added 11% to our population at handover. Only 8% of them had received post-secondary education and significantly below the average level for Hong Kong. Of late there has been a lot of public discussion about income inequality (Gini Coefficient), social mobility and the plight of the 1m people (14% of our population) below the poverty line.

In our second report we pointed out that the income disparity that we face has a successful side with Hong Kong managing to increase the number of people in high income brackets significantly over the past decade. What makes our inequality unusual in a global context, is that few countries, if any, would at the same time admit immigration with significantly less skill. It does not require much imagination to link the 700,000 new immigrants with our 1m poor people. Adding to the rich and the poor at the same time does not make for a pretty Gini Coefficient.

Perhaps unique in the world, Hong Kong has added to the rich and the poor at the same time – thus inducing our own inequality discontent

We also argued in our second report that there is no point in discussing income equalisation since our nominal per capita income had only moved at an adjusted rate of around 1% per annum for the past decade, despite our having the fortune of having a fast-growing (10% per annum) China as parent. Our "pie" so to speak has hardly grown so, if a person wants a bigger share, it will have to be taken from another person and society will not be happier for it. Priority for our community therefore, is to shun this futile zero-sum game and be proactive in seizing the opportunities we can all enjoy as "One country, one market" unfurls further, and grow our service income pie and create real growth in incomes for ourselves.

Income-equalisation debate is futile as someone's gain is another's loss - our nominal per capital income hardly grew in the past ten years, making it a zero-sum pie to divide; a practical way to help the poor is to grow the Hong Kong service income pie – not difficult when "One country, one market" is happening

We have only one class of Hong Kong citizens and we must do our utmost and take affirmative action to help the low-skilled. While office work generally requires computer literacy, most retail and hotel jobs have much lower demands. Thus, the current boom in tourism trade offers a golden opportunity for us to add significantly to hotels and shopping spaces and create tens of thousands of jobs and income opportunities for the new members of our society.

We have only one class of citizenship in Hong Kong and we must empower our new members with the opportunities to better themselves – retail and hotel sector is one golden opportunity

Having taken into consideration the following, we propose two complementing sets of commercial and community hardware for immediate implementation:

(1) acute undersupply situation in retail, hotel, hospital and office spaces and the lack of any meaningful relief in the next six to eight years.

(2) the structural nature of demand growth in this sector (discussed under the concept "One-Country, One-Market" in our previous reports).

16+ reasons to invest HK$22bn to build a 11m sf multi-use commercial complex to showcase our services at the airport for first-phase completion in 2016, in time for the opening of the Hong Kong-Zhuhai-Macau Bridge the same year which will bring us many visitors. We will build the most environmentally friendly new town in the world where Tung Chung is, enabling its future residents to leave behind zero carbon footprint when they go to work, a stone's throw away

(3) the potency of these opportunities in helping our new citizens by (a) creating new jobs and (b) retaining existing jobs within Hong Kong. We estimate 162,000 jobs can arise in the new Tung Chung which will comprise an 11m sf commercial complex (temporarily called “Gateway to the World” or “GTTW” for short) to offer the best services of Hong Kong (medical, retail, finance, NGO, education, credibility services, art and culture, galleries, hotels, offices etc) at the point of arrival of our customers either by air or by land. This will mark a first in the world whereby customers are served “at the gate”, dispensing with the trouble with spending more time and cost to travel to urban areas in order to receive Hong Kong’s world-class services. These opportunities and the new runway plus the extension of Tung Chung towns can support a population of over 486,000. GTTW is approximately twice the size of Harbour City and will be a “destination facility” (ie worthy of making a special trip to see and use) by virtue of its scale and diversity of offerings.

(4) the importance of creating new “content” in Hong Kong in order to attract more visitors to use our airport, especially when we are about to commit HK$86bn present value or HK$136bn (money of the day) to add a third runway.

(5) the need to transform the “forgotten” under-sized backwater Tung Chung into a purposeful community and an desirable place to live. As things stand, the 82,000 residents fall well short of the 200,000 threshold for a public library and the 240,000 for a general hospital and other public amenities. Private facilities and job offerings for its residents are also few

(6) Government forecasts that the Hong Kong population will grow 1.9m, or 27%, from the current level to 8.9m by 2039.

(7) our citizens aspire to building a most environmentally friendly town that befits the World City of Hong Kong. We have the population and commercial needs for a new town and the means to create a most desirable environment to live, work and play in. The new and significantly enlarged Tung Chung (temporarily called “Flying Dragon”) gives us the opportunity to focus our development experience over the past decades and the latest technology and design considerations to craft a new town that fully reflects our aspiration to be the greenest World City. Hence, we should insist that the best applicable green standards are adopted. In future, when residents of Flying Dragon go to work, they will leave zero carbon footprint and can just walk across to GTTW.

(8) the general public’s desire for a home located alongside existing arteries of public transport. For instance, few would want to live in a district when rail links are pending or bus services infrequent.

(9) the completion of the Hong Kong-Zhuhai-Macau Bridge 2016 which enters our territory near the airport, will put Tung Chung within the direct reach of 70m people who live in the affluent Pearl River Delta. GTTW will provide parking facilities initially for 10,000 vehicles (five times the capacity of that at Harbour City) to allow visitors to "park and shop/bank/get surgical help/get educated/watch a show or see an exhibition at AsiaWorld-Expo etc", "park and ride to urban areas", "park and fly".

(10) the fact that the site has received town planning and other land use approvals means that construction can start once the go ahead is given to GTTW.

(11) there is no need for land premium payment – thus the only new investment required for GTTW is planning and construction. In a city where 70-80% of total development cost is often attributable to land, GTTW is a very rare opportunity - effectively having done without the cost of land means a low investment hurdle. With total cost at around HK$1,600psf, even renting of its 1m sf office spaces at HK$10psf a month will yield a 7.5% on investment.

(12) liberate the full potential of AsiaWorld-Expo by providing fully-fledged service and accommodation facilities to attract more usage of the exhibition site.

Being our second convention centre, the government-owned AsiaWorld-Expo suffers from a low utilisation as users complain there is little for them, and their families if they come along, to do and nowhere to go after attending a conference or an exhibition.

(13) our public funds have tended to earn low and unstable returns and investments in US 10-year treasuries can only produce c.2% incomes, which will likely undershoot Hong Kong inflation. Against the trending demand for services and spaces in Hong Kong, and the HK$160bn investment by the government in new infrastructure around GTTW, the project will likely generate a risk-adjusted return far superior than that of the traditional public portfolio. We estimate that GTTW should fully pay off its cost in around six years and carry an ultra-high ungeared Internal Rate of Return (IRR) of 13.8%.

(14) GTTW provides huge scope for externalities. Further to the highly attractive financial returns, including a positive Net Present Value of an estimated HK$41bn, which can cover almost half the negative present value arising from the third runway, the commercial complex should promise substantial externalities, including morale of our citizens, and other non-direct benefits to Hong Kong.

(15) GTTW and Flying Dragon have limited downside. Hong Kong has never invested as much in infrastructure in a single location as we are doing in Tung Chung. If GTTW fails totally, the loss of HK$22bn will represent 14% of the other investments of HK$160bn being added to the district and should it fail, more pertinent questions should be raised as to whether the HK$160bn could be justified in the first place. A more reasonable way to look at GTTW should be, since we are committed to some HK$160bn in putting up infrastructure for a better future, we should, using the same positive assumptions about our future, invest a further 14% in new commercial facilities to make it doubly sure that these preceding investments work, by attracting more users and customers to these investments.

(16) importance of re-enforcing Hong Kong's "First mover advantage" in service sector by adding scale and diversity. The robust visitor arrivals and the influx of overseas companies, talents and capital into Hong Kong in the Golden 5 Years clearly evidence the quality and attractiveness of our services. GTTW can be a powerful contributor to building up Hong Kong's first mover advantage.

To reinforce the pre-eminence and enrich the shopping experience of the already overcrowded TST, the top-grossing shopping district of the world, and to cater for the opening of the HK$62bn Guangzhou-Shenzhen-Hong Kong Express Rail Link in early 2016 which will bring another 50,000 visitors into the district each day, we propose the construction of “Sub-culture”. This is a 2m sf shopping centre that parades 600+ shops and ancillary food and beverage points and built underground to the 8m sf West Kowloon Cultural District (WKCD) along the concepts suggested by Professor Kwok-pun Cheung of the University of Hong Kong Faculty of Architecture in his report to the Legislative Council in March 2011. The Express Rail Link will put 30m+ population from the affluent Guangdong cities of Guangzhou, Dongguan and Shenzhen within 48 minutes’ reach of the TST terminus and this extra traffic will likely be the straw that breaks the camel’s back as existing foot traffic through the major malls in the Tsimshatsui (TST) area today is already at or near capacity eg. 150,000 at Harbour City and 100,000 at The Elements. In the next four years, arrivals at TST should grow at a compound rate of 10-15% a year, adding 50-80% to current flows. If nothing is started today, there may be a need to pedestrianize Canton Road before the Link is opened.

Build a 2m sf underground mall (“Sub-Culture”) to reinforce global pre-eminence of TST as the world’s most popular shopping district and stimulate patronage to the 8m sf Cultural District. Net profit of HK$1bn a year will boost annual public art-spend by 35-40% initially, creating huge scope for transformative cultural repertoire including contracting series of world-class performers as regulars and redefine art skyline for World City of Hong Kong

We will apply all the annual net profit from Sub-Culture to augment the government's budget on Arts and Culture. The first full year's contribution of some HK$1bn will add around 35-40% to the government's spending, benefiting all the existing recipients of the subsidies and providing significant upside to improve the range of artistic performance available in Hong Kong. For instance, we can consider contracting Mr Yo-Yo Ma, Mr Lang Lang and other top musicians on a periodic basis so that our citizens and visitors can expect world-class performances as a regular feature of the Hong Kong art scene, just as Celine Dion is a performance fixture of Las Vegas. As the net profits from Sub-Culture will grow with shoppers, it is ultimately the market, which will continue to benefit from the "One-Country, One-Market" dynamics over the long run, that drives public sector art spending. As art and culture offerings increase and improve, more visitors and local users will patron our facilities and generate more revenues for art and culture development, thereby setting about a virtuous cycle. When our general facilities are well used and performances are fully attended, critics may not be able to call Hong Kong a cultural desert anymore.

HK$1bn annual net profit from Sub-Culture will be applied back to art and culture, boosting public spending by 35-40% initially, leaving generous room for major enhancement of our art scene, including contracting world-class performers like Mr Yo-Yo Ma and Mr Lang Lang and more on a periodic basis, to create a permanent repertoire for Hong Kong

(2.3) Masterplan to the Prospect of becoming a World City - we Have the Know-how to do it: (2.3.1) Scale (2.3.2) Build it and they will come (2.3.3) Be friendly to the Environment

In directing the course of the development of Hong Kong back to its original path of becoming a World City, we need a clearly annunciated masterplan. We have argued that since it is a natural development for Hong Kong to be the next World City and already endorsed by Time Magazine and other independent authorities, we only need a detailed game plan to take us there.

Hong Kong should approach this holistically rather than the piecemeal manner in the past. For instance, immigration policies and taxation rules are means to a policy end. Hence, we should provide incentives to businesses that are considered essential to our move to becoming a World City and talents that can catalyse the transformation. Most countries have such schemes and Hong Kong should not lose out in the global fight for entrepreneurship and talents which can bring long-term benefits to our people.

Our community have learned precious lessons from 50 years of building up new towns and world class infrastructure. We should have no problem in putting up efficient and user-friendly new spaces to contain our new businesses and expanded population:

(2.3.1) Scale: One such lesson is the need for scale. A new town needs to have over 240,000 residents to warrant a public hospital and has to enjoy existing link to mass transport in order to attract people to move in.

(2.3.2) Build it, and they will come: A number of initiatives failed initially but they all came right within three to five years as the economy has performed well and more space was demanded. The most recent example of this is Kowloon East. This was started a piecemeal selling of government sites for low rent (started as low as HK$5-8 psf a month) and a rezoning of previous industrial uses into office functions. After a few years, the spillage of high grade tenants from traditional locations has turned this to become one of the two largest office clusters in the territory with spaces almost fully occupied and rents upped to HK$20-30psf, all over a period of three to five years. This lesson, that when we have good growth opportunities, as is the case in these few years, the case for “build it, and they will come” is valid.

(2.3.3) Be friendly to the Environment: A long-term problem when we developed new towns is that they fail to be self-contained, and most residents will have to travel outside their district to find work. In planning for the better Hong Kong, we should actively consider bringing work to residents and this should reduce carbon emissions. We will apply all these three lessons from the past in the crafting of our proposed investments. Our proposal to build up Tung Chung and creating new commercial spaces at the airport should meet this desirable criterion. For instance, we should consider building new hotels in Tin Shui Wai – an area of low incomes and skills. For packaged tourists, it matters little where the hotel is located as most of the day they will be out sight-seeing or shopping. A bus ride from popular Canton Road to Tin Shui Wai is around half an hour and new hotels there should be attractive proposition in view of the low cost of land there. Such an initiative can create a lot of jobs for residents there.

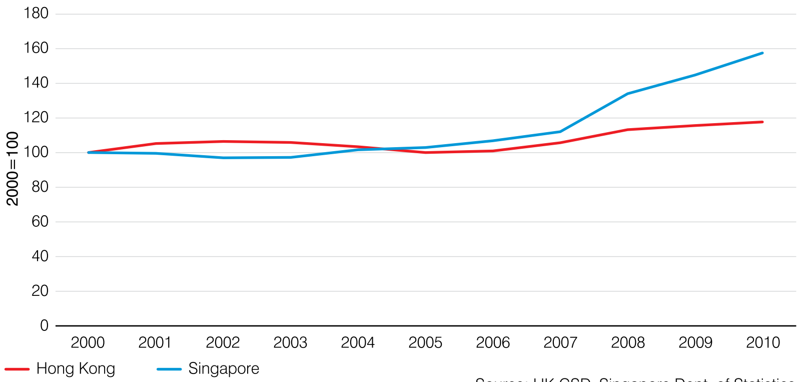
(2.4) "Big Market, Small Government" philosophy is neither the best nor the only way

An economic performance that has significantly underperformed Hong Kong's potential and our peers' and an unenthusiastic reception of our social policies over the last decade do not support the case for an inflexible fiscal formula

Every now and then, the government emphasises the principle of "Big Market, Small Government" and keeping public expenditure within 20% of GDP. Yet, the anaemic growth we recorded over the past decade and our significant underperformance vis-à-vis our key Asian peers, in particular Singapore, which faces far less favourable circumstances than we do (for instance, we have a fast growing China as our motherland), and a less-than-contented citizenry, do not suggest such a fiscal rule is producing a desirable outcome.

In this respect, we agree with Professor Wilson Wong (Government and Public Administration, Chinese University of Hong Kong), a veteran scholar in public finance. He remarked in a public forum a few months ago that there was no proven rule that determines the optimal size of government spending and that public expenditure should adjust according to the development needs of the economy.

Public Expenditure Growth (local currency)

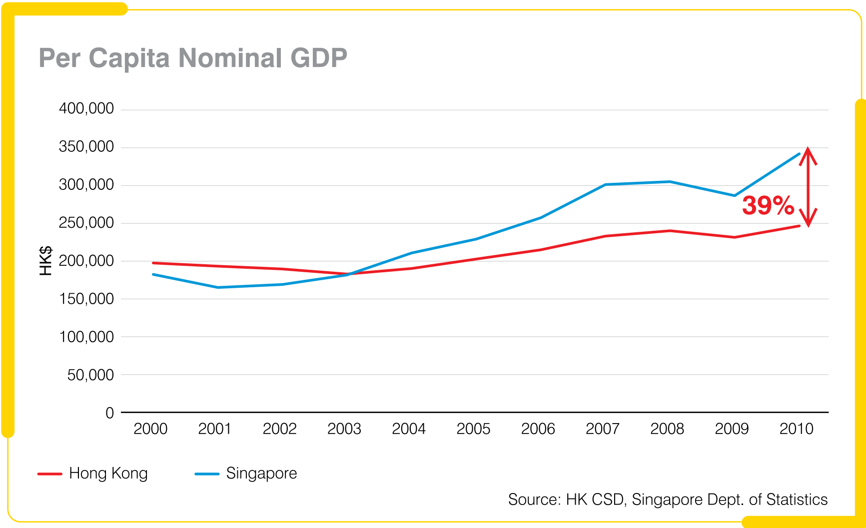


Source: HK CSD, Singapore Dept. of Statistics

Spending when it is appropriate – tried and tested by Singapore

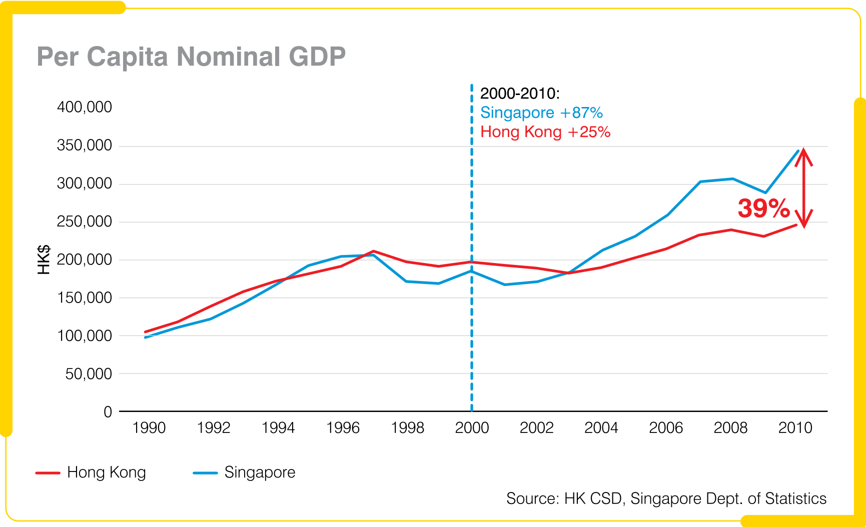
We show above, the movement of fiscal outlays of Hong Kong and Singapore over 2000-2010, referenced to their 2000 levels. When our economy flat-lined this period, our fiscal expenditure followed the same pattern. However, Singapore's public spending rocketed from 2006 and recorded a 57% rise over the same period. We should put our focus on 2002-2003 when Singapore's public expenditure and GDP reached their troughs in the decade. What indeed did the Singapore government see at that time that warranted a drastic "spending spree" from 2007? The answer is "Remaking Singapore" – an initiative that was announced in February 2003 after a fundamental re-examination of the country's situation. Singapore saw lots of challenges but devised decisive strategies, fiscal spending included, to execute a comprehensive "remaking" of the country.

Below, we show the performance of the movement of nominal per capita income of the two cities. While Hong Kong's posted little uptick over this period, Singapore's raced ahead, pulling further and further away from Hong Kong's in 2010.



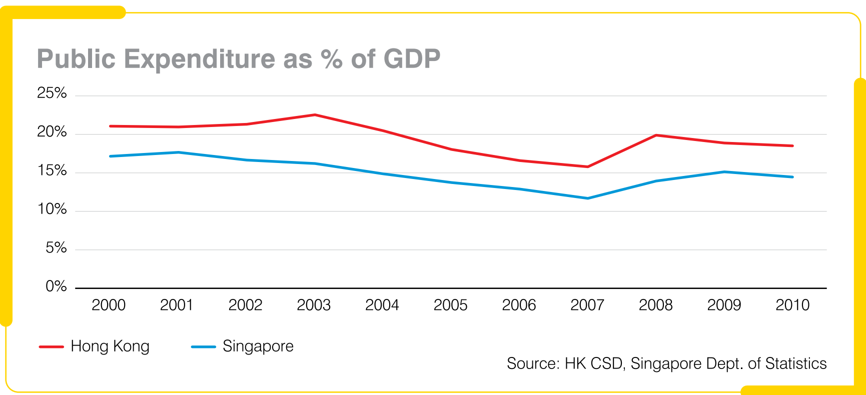
There is a very important lesson for us here. Over this decade, Hong Kong's nominal income per capita grew only tepid 25%, against London's 53% (as a peer IFC to Hong Kong), Singapore's 87% and China's 278%.

Extending our comparison with Singapore back another ten years shows that Hong Kong had outperformed almost the entire period from 1990 to 2003, but has lagged behind ever since. A pro-change fiscal policy that complements the structural changes in the economy has clearly worked in Singapore's favour.



An honest level of foresight attained after a thorough collective introspection has produced a result the small country should be proud of and which offers us a precedence for a more proactive approach to managing our citizens' money. As to the worry that the surge in public expenditure might have blown a hole in Singapore's GDP, our last chart on this subject is highly assuring – despite the sharp rise in public spending from 2001, Singapore's GDP has risen more than the pick-up in government expenditure, and the public sector's share of GDP has not risen but has indeed fallen, over this period. It seems that a fiscal strategy to spend when appropriate has worked out well. One may say that Hong Kong's ratio has not moved much either, but this could not be something that comforts us – our incomes have stagnated.

"To Spend when Appropriate" has resulted in a shrinkage of Singapore's public sector as a percentage of GDP, even though the city-state pumped up its fiscal spending by c.60% from 2004 to 2010



Since all the evidence (record employment, inflation, record arrivals of overseas talents and customers, fiscal surpluses etc) for the two structural trends of (1) a West-to-East shift of economic momentum which will continue to usher into Asia more investments and inflow of overseas companies and talents and (2) “One country, one market” are present, we should not hesitate and start reacting to these opportunities with “Investing HK$100bn for Our Future”.

While it may have become customary for the government to devise a tax/rate rebate or a cash hand out to the public, we question the logic for doing this again this or next year. A tax refund and similar schemes represent a stimulus to the economy to (1) encourage employment and (2) prevent deflation of general prices. We face the opposite to both today. Latest official figures show that total employment stand at record high and even job vacancies, or positions waiting for job applicants to fill, are also at their pinnacle. Income security is anything but frail and deflation risks are remote.

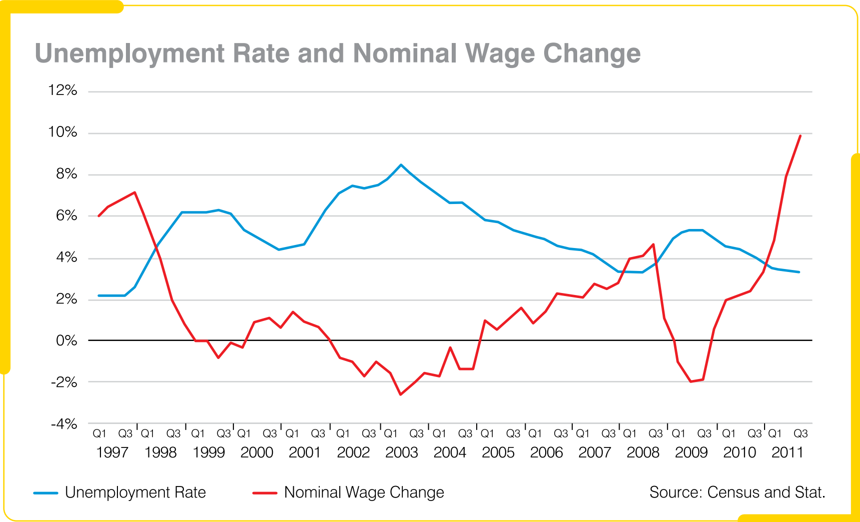
Number of Employed Persons and Vacancies

Faced with effective full employment and an average wage growth of 9.9%, the highest in 17 years, individuals and businesses are doing very well and do not need relief from the government. What they should require, we argue, is to trade whatever refunds for a commitment from government to invest in more public goods – those infrastructure items including university places, more border crossing staff (to help reduce long queues of visitors), training programmes, medical care, more new land etc. - facilities that private individuals cannot procure themselves but require the government to produce. Shortages in these will aggravate inflation and the government is at the centre of its resolution.

We do not need tax rebates nor cash hand outs, we need a commitment to help solve our persistent inflation caused by shortages of hardware and software

The question is whether a citizen is willing to pay the government any rebate in return for a commitment from the government to (1) invest that sum in new hospitals so that when that person falls ill, he or she will not sleep in a corridor alongside crying babies and moaning patients, (2) to produce new land so that a private or corporate tenant may not need to get an anxiety attack every two years when the new rent is announced and (3) add more university places and step up on-the-job training so that the imminent shrinkage of our workforce can be countered by a rise in productivity rather than triggering a bun fight for staff and an upward wage spiral. The writing is on the wall and the seeds of discontent are already sown – much that the average inflation in the first 14 years of the handover was 0%, wages did rise at their fastest rate of 11% in 2011.

Will you trade your rebate/ hand out for a commitment by government to step up supply and alleviate shortages?



In 2008, unemployment rate was 3.6% and nominal wage rose 4.5%. When unemployment returned to 3.3% last year after the Global Financial Crisis in 2008/09, nominal wage registered a 11% growth. Considering the 1.8% growth in labour force last year with tens of thousands of middle-aged population re-joining the labour market, it is fair to deduce that we are "emptying" the reserves of our labour force. While more than half of our inflation is driven by residential and commercial rents (i.e. shortage of hardware), the highest average wage growth in 17 years recorded in 2011 is indicative that Hong Kong will likely enter into a wage-price spiral as an ageing population contributes to a shrinking workforce against the expansion of retail, hotel, tourism and catering industries and it will add to inflationary pressure in the Golden 5 Years.

Wage inflation will start to add to rent inflation

One of the most important responsibilities of the government is the provision of "public goods", i.e. goods or services that the private sector does not (or cannot) produce on its own yet are beneficial to the society as a whole, e.g. free education, public medical services and other infrastructures. This is precisely the case of Hong Kong: our university places are insufficient, hospitals are packed and land is scarce. But the general public cannot raise funds on their own and build hospitals and universities, nor can they alter the population policy of Hong Kong. We are not advocating planned economy or extravagant public spending, but are only calling for the government to fulfil its basic responsibility to supply the public goods that it has been underinvesting in the past decade.

The government must fulfil its basic responsibility to supply public goods

Hong Kong does not only benefit from the eastward shift of economic centre of gravity, but it also enjoys the countless opportunities brought by "One Country, One Market" – an advantage that Singapore can only dream about. If Hong Kong still loses out in the critical battle for the emergence of the next World City, there is truly no one else to blame but ourselves.

We have no one to blame but ourselves if Hong Kong fails to fulfil its destiny of becoming a World City

In summary, here are the remedial and essential investments for Hong Kong that we propose:

Proposed Investment

HK$ bn	HK$ bn	Proposed Investment
22		Destination Commercial Complex "Gateway to the World" (GTTW) • 4m sf mall, 10,000 car park slots, 6-8 hotels with GFA 3m sf (3,000 rooms) & 1m sf office for credibility industries & NGOs; Community New Town "Flying Dragon" for 700,000 people in 20-30 years
10		WKCD Underground Mall "Sub-Culture" • 2m sf shopping space
	32	**Sub-total: Hardware**
6		Replace all old buses (70% of bus fleet) by incentivising bus companies to reduce roadside emission by 40%
3		Expanding current retraining facilities by 20% to help alleviate annual 0.4-0.8% drop in workforce
0		Adopt accretive population policy to attract talents and entrepreneurs that can improve Hong Kong business connectivity with China and the world - these will create jobs and income opportunities to Hong Kong. Target some 200,000 overseas and mainland talents over 10-15 years
40		Build more hospitals to expand capacity of public medical system by one-third
15		Add 10,000 (67%) university places to seed quality workforce we will need and to export values of this World City
4		Adequate funding to open 25% of WKCD by 2018 and supporting local art and culture institutions
	68	**Sub-total: Software**
100	**100**	

Source: Government Budget 2011/12, HKGolden50

(3) Invest to Improve in our Service Capacity and Capabilities – Build World-class Hardware:

Please refer to Section 2 for full details on

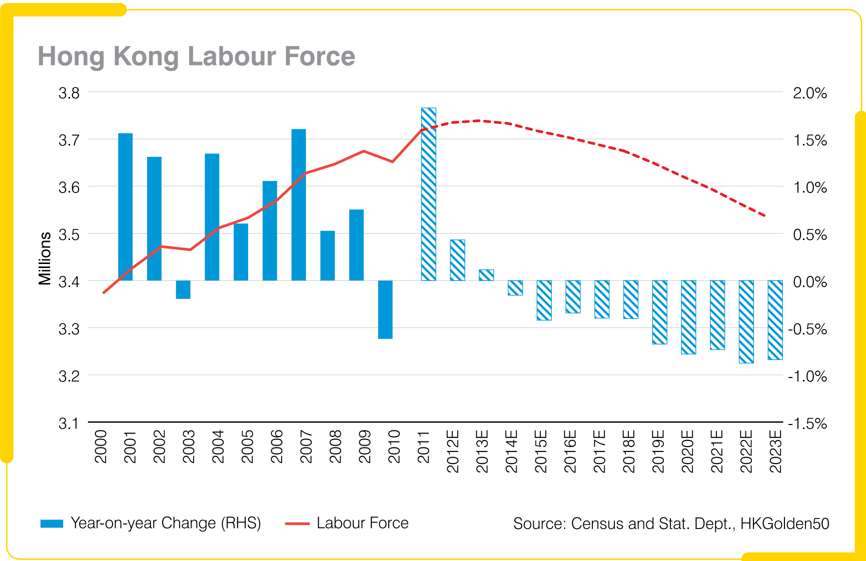
(3.1) "Gateway to the World" HK$22bn

(3.2) "Sub-Culture" HK$10bn

(4) Invest to Improve in our Service Capacity and Capabilities – Build World-class Software:

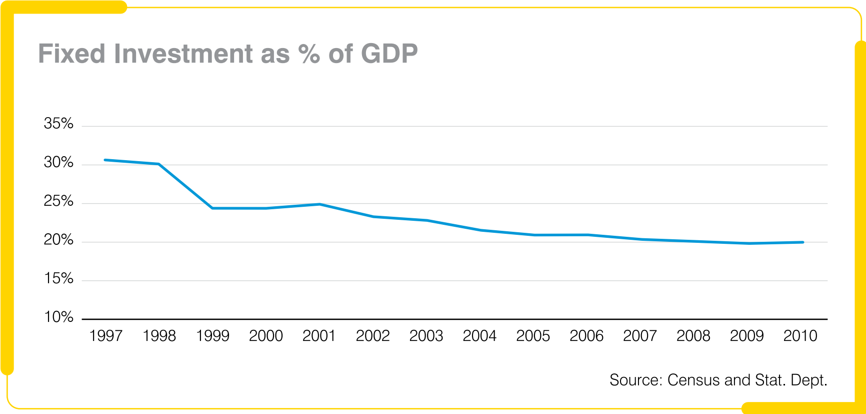
The provision of world-class services does not only need hardware (hotels, shops, offices, hospitals, schools etc.) but also software (professionals, salespersons, teachers, doctors etc.). In addition to sufficient commercial spaces, Hong Kong also needs a high quality workforce to ensure the city can maintain the quality of services that it provides.

Besides increasing supply of commercial spaces, Hong Kong also needs a high quality workforce to maintain our service quality



Unfortunately, shortage of labour as a result of ageing population and a prolonged period of low birth rates will likely curb Hong Kong's potential to sustain growth. Hong Kong is going to lose 20,000 to 40,000 workers, or 0.4-0.8% of our workforce, every year starting around 2012. Given the shrinking pool of labour, it takes an average of some 6% increase in labour productivity per annum when demand for our service is expected to grow at 5-6% per year – which is virtually impossible when we consider the fixed investment as % of GDP in Hong Kong has been falling for more than a decade.

Reversing the gain of some 400,000 workers in the past decade, we will lose 300,000 pairs of hands from our workforce in the coming 10 years. This decline will severely undermine the quality of our services unless productivity picks up rapidly



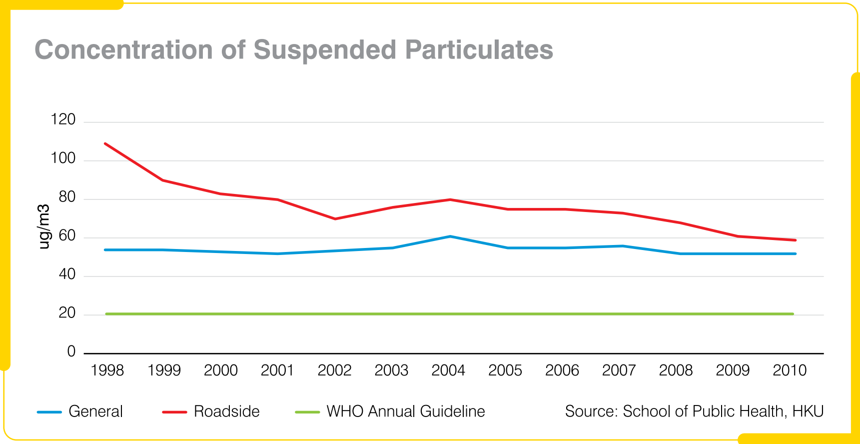
(4.1) HK$6bn to Freshen our Air

Air quality is often a critical factor for multinationals and expatriates when they make decisions of where to locate their regional offices/headquarters and which city to work in. Hong Kong must add to the positive momentum it has built up in environmental issues. We propose the government should set aside HK$10bn to subsidise bus companies to replace their old buses to improve air quality. The government also needs to update its Air Quality Objectives (AQO) to completely meet the standards set by World Health Organization (WHO).

Businesses and investors, local and overseas talents, are often driven away by poor air quality

According to the revised (Jan 2011) Hedley Environmental Index compiled by the School of Public Health of HKU, over the last five years Hong Kong has incurred an average HK$8bn of tangible economic loss and more than 600 premature deaths per year due to air pollution.

On average, Hong Kong has incurred tangible economic loss of HK$8bn and 600 premature deaths per year due to air pollution over the last five years



The effort paid by the government in improving air quality is clearly insufficient. Although there has been a decreasing trend in a number of pollutants like nitrogen dioxide (NO2) and respirable suspended particulates (RSP) over the past years, the roadside emission of NO_2 and RSP still exceed the WHO guideline by 195%.

Roadside emission of NO_2 and RSP still exceed the WHO guideline by 195%

Concentration of PM2.5 Suspended Particulates Among Various Cities

Ranking	City	Annual Mean Concentration (ug/m3)
92	Sydney	7.0
447	New York	12.7
461	London	13.5
520	Singapore	19
541	Paris	22.9
559	**Hong Kong**	**36.0**

Note: Data for China and Taiwan not available
Source: Friends of the Earth, WHO

The poor air quality in Hong Kong is driving foreign enterprises and expatriates away. A recent survey conducted by Regus indicates that 75% of corporate leaders believe air quality is hindering Hong Kong's ability to attract and retain talents.

Poor air in Hong Kong is driving foreign companies and expatriates away

Sources of Pollutants

Pollutant Source Categories (2007)	NOx	RSP	CO	SO2
Road Transport	22%	30%	82%	1%
Public Electricity Generation	46%	28%	5%	89%
Navigation	16%	7%	3%	5%
Civil Aviation	6%	0.4%	3%	0.5%
Other Fuel Combustion	11%	21%	7%	5%
Non-combustion	NA	13%	NA	NA
Total	100%	100%	100%	100%

Source: HKEPD

Reducing emission of public buses is essential to improving air quality of Hong Kong

Figures from the Hong Kong Environmental Protection Department (HKEPD) show that road transport is the most important source of RSP and carbon monoxide, and the second most important source of nitrogen oxides. By vehicle types, franchised buses account for 40% of the total roadside emission. It is therefore of paramount importance to reduce the emission from franchised buses in order to improve effectively the air quality of Hong Kong.

Composition of Buses by European Emission Standards

	Hong Kong		Singapore	
	# of Buses	Expected Year of Retirement	# of Buses	Replacement Deadline
Pre-Euro	456	2012	0	
Euro I	1338	2015	2700	2011
Euro II	2688	2019	586	
Euro III	1233	2026	207	
Euro IV	53		506	
Euro V			357	
Total	5768		4353	

Source: Civic Exchange

As at 2009, almost 80% of Hong Kong's public buses are of Euro II standards or below, whereas Singapore has upgraded all Euro I buses to Euro V

Compared to Singapore, Hong Kong lags behind in upgrading franchised buses. As at 2009, almost 80% of Hong Kong's public buses are of Euro II standards or below, while Singapore has already upgraded its Euro I public buses to Euro V. Also, only 0.9% of public buses are equipped with engines that meet Euro IV standards, while in Singapore, 20% of public buses have met standards of Euro IV or above.

A comparison of buses of different generations shows that upgrading public buses can drastically reduce emission of pollutants. For example, by upgrading from Euro II to Euro IV, emission of nitrogen oxides and particulate matters are cut down by 50% and 92% respectively.

	Capital Expenditure HK$bn	Return
Incentivise franchised bus companies to replace all Euro I and II public buses to Euro IV standards	6	Avoid 200 premature deaths per year Avoid tangible economic loss of HK$2bn per year

We propose the government to set aside HK$6bn as to incentivise franchised bus companies to replace all Euro I and II public buses (70% of our bus fleet) to Euro IV or higher standard models. Special preference is for electric buses when technology has become effective.

We propose the government to set aside HK$6bn to incentivise franchised bus companies to replace all Euro I and II public buses to Euro IV and higher standards, including electric buses

While the exact amount of subsidies and the details mechanism (e.g. linking the amount of subsidies with the net book value of the replaced buses) should be subject to further public discussion, we believe earmarking HK$6bn (which is enough to cover up to 60% of the total cost of replacement) is sufficient to provide enough incentives for franchised bus companies to replace their buses under the current profit control scheme in which profits of bus companies are based on average fixed assets value.

In fact, providing subsidies with a view to improving air quality is not unprecedented. For example, the Hong Kong government has been providing subsidies (a total subsidies of HK$4bn has been provided by now) to encourage replacement of old diesel commercial vehicles. From an international perspective, Seoul, for example, has provided subsidies of HK$1bn (25% of cost) to bus operators to replace diesel buses to compressed natural gas (CNG) buses.

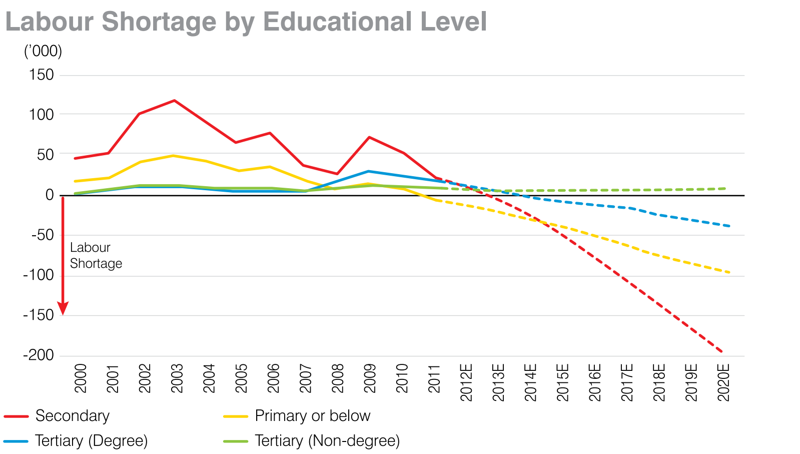
Most importantly, with reference to the model developed by the School of Public Health of HKU, our conservative estimate is that by replacing these old buses we can reduce overall roadside emission of NO_2 and particulate matters by 25%, and thus avoiding air pollution-related premature deaths by 200 per year, and tangible economic loss of HK$2bn per year.

Replacing old buses can reduce emission of NO_2 and particulate matters by 25%, and thus avoiding air-pollution-related premature deaths by 200 per year, and tangible economic loss of HK$2bn per year

(4.2) HK$3bn to Train and Increase Productivity of our Workers to ensure we Improve the Quality of our Services and Global Competitiveness despite the Rapid Shrinkage of our Workforce

We expect that by 2014, Hong Kong will be lacking workers in almost every level of education with the sharpest shortage in workers without tertiary education (red and yellow lines in chart), with the deficiency up to 70,000, roughly 3% shortfall in labour in this category. And this situation will get worse with every passing year adding some 1.5% to the shortage.

By 2014, there will be shortage of labour in almost every level of education, with the sharpest shortage in workers without tertiary education



Source: Census and Stat. Dept., HK Universities Grants Committee, HKGolden50

When our present education system mandated attendance up to secondary school diploma, the supply of workers with sub-secondary schooling (yellow line) will dwindle with the retirement of the existing workforce. Shifting up one rung of education, those with secondary schooling (red line) will experience an even sharper fall off of workers. This reflects the significant stepping up of tertiary education in the past two decades which has equipped a high proportion of secondary school leavers with further qualifications leaving not so many students with only their secondary diplomas. The retirement of this latter group will quickly create shortages.

Demand for sub-tertiary workers, on the other hand, is expected to rise as service sector will grow at 5-6% p.a., spurred by opportunities entering Hong Kong during the Golden 5 Years. Hot spots in the job market should include shop assistants, waiters and tour guides - often positions that do not require a high level of formal education.

The Golden 5 Years bring tremendous demand for all kinds of services, which derives demand for labour with relatively lower educational level

	Capital expenditure to increase training capacity HK$bn	Operating cost to train 40,000 extra workers per year HK$bn	Return per year (Income loss avoided by having more productive staff working for 10 years) HK$bn
Increase the current retraining capacity by 20%	3	1.2	1.8 (18)

To counter the effect of the looming labour shortage, we call for a 20% increase in the capacity of the current retraining programmes (mainly offered by the Vocational Training Council (VTC) and the Employees Retraining Bureau (ERB)). Re-training programmes of this nature (lasting six to nine months) are effective in raising labour productivity. We expect HK$3bn is required to expand and upgrade the current facilities for 40,000 more trainees each year and an extra operating cost of HK$1.2bn will be needed every year. This is small cost when compared with the income loss of HK$18bn that can be avoided by having properly trained, productive staff working for ten years.

To cope with the problem of labour shortage, we propose to expand the current retraining programmes by 20%

Long-series academic studies in Europe have reported that for every 1% of workforce receiving retraining, labour productivity can be increased by 0.4%, with minor limitations. Taking a “deprival” approach to work out the potential loss of earned income as businesses fail to fill vacancies, we have computed that without such an expansion in retraining programmes, Hong Kong will lose HK$1.8bn each year, or a total of HK$18bn over a course of ten years.

Without such an expansion, Hong Kong will lose HK$1.8bn per year, or HK$180bn over a course of ten years

Our economy is undergoing another major “restructuring”: “One-Country, One-Market” has led to boom in “credibility services”, e.g. retail, restaurants, tourism, MICE, finance and other personal services including beauty care and medical services. On the contrary, some large industries like import/export may be stagnant or even on the decline. We believe such an expansion in retraining programmes can help those who are structurally unemployed or who are currently out of the labour force (e.g. 54% of the new immigrants are economically inactive) by equipping them with skills that our economy currently needs.

Expansion of retraining programmes can help the structurally unemployed or who are currently out of the labour force

(4.3) Adopt an Accretive Population Policy to attract Global Talents and the Well-to-do's & improve Capability, Connectivity & Diversity of this World City

Hong Kong does not seem to realise there are many, many policy schemes and instruments for the crafting of public policies to facilitate the attainment of social and economically desirable goals, including the making of a World City. Our policy to attract global talents appears stark naked when compared against Singapore's, for instance

Most countries actively partake in immigration policies to attract talents and well-to-dos, yet Hong Kong's case is exceptionally rare. Our current intake of global talents is heavily biased towards admitting mainland talents in non-business related disciplines: 55% work visas granted through the Admission Scheme for Mainland Talents and Professionals (ASMTP) are issued by the academia and the arts and culture sector. While these talents are important in adding diversity and knowledge to their fields, over 53% of all admittances earn less than HK$20,000. These talents are clearly not the crème de la crème when it comes to adding value to our economy and creating jobs for our people.

In contrast, Singapore's accretive immigration policy not only attracts more talents with sharp business acumen to compound their economic growth, the government's competence in retaining these talents makes us pale in comparison. Each year, Singapore successfully channels 75,000 foreign talents to become permanent residents (PRs) and equivalent each year by granting instant permanent residencies to targeted talents, whereas our ineffective population policy only manages to retain a couple thousand.

We have clearly lost out in the fight to attract global talents – this must change

In the face of an increasingly competitive quest to attract global talents and the, we propose to (1) embark on a talent and connection accretive population policy that attracts some 200,000 talented individuals of all sectors who can prosper from Hong Kong's global service platform and bring connectivity, jobs, and business opportunities over the next ten to 15 years; (2) loosen the PR requirement by shortening the minimum period of stay from seven years to two years for selected applicants considering that many countries do grant PRs outright or within two years; and (3) Create a panel of business representatives from relevant sectors to help civil servants exercise discretion in granting PR to talented applicants who may otherwise be overlooked on the count of low education attainment. All of the above measures can attract talents who can fill the places of the 300,000 decline of workforce in the upcoming decade when baby boomers retire.

(4.4) HK$40bn in Expanding Medical Capacity and Capability to keep our People Healthy & Active

Hong Kong's medical system has been one of the world's best with one of the lowest infant mortality rates and remarkably higher cancer survival rates than the West, but the quality is unlikely to sustain as both hardware (e.g. hospitals and equipment) and software (e.g. doctors and nurses) of the medical system is severely stressed.

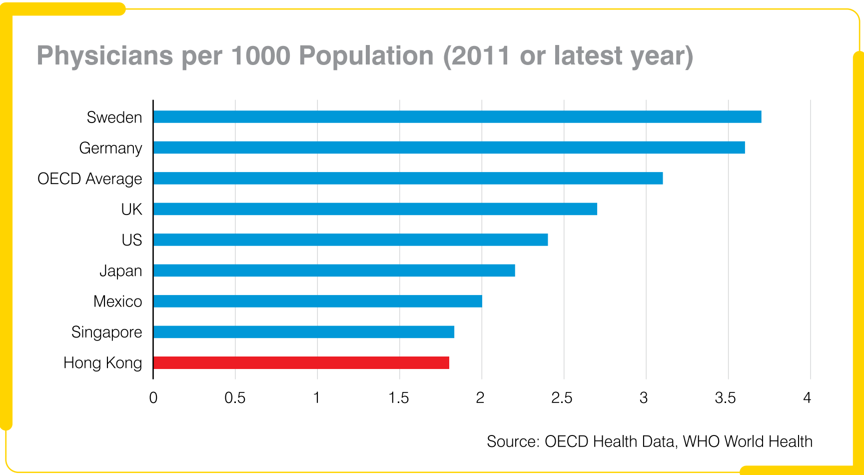
Both hardware and software in our medical system are heavily stressed

We have characterised, in our previous report, the last ten years of Hong Kong as the "Lost Decade": although our population has been growing and ageing, in the 2000s, not even one new hospital was established and operational, whereas eight hospitals were constructed during the 1990s.

Eight new hospitals were opened in the 90's yet zero hospital was established in 2000s, despite a growing and ageing population

In addition, old equipment may jeopardise our ability to respond effectively in case of an epidemic like SARS.

As Dr. Ho Pak-leung, President of the Centre for Infection of HKU, pointed out in September last year, 90% of the apparatus at the Centre for Infection are at least 20 years old, he described the current situation as "driving an antique car and you never know when it will break down" and Hong Kong will be under great threat in the case of an outbreak of infectious diseases.

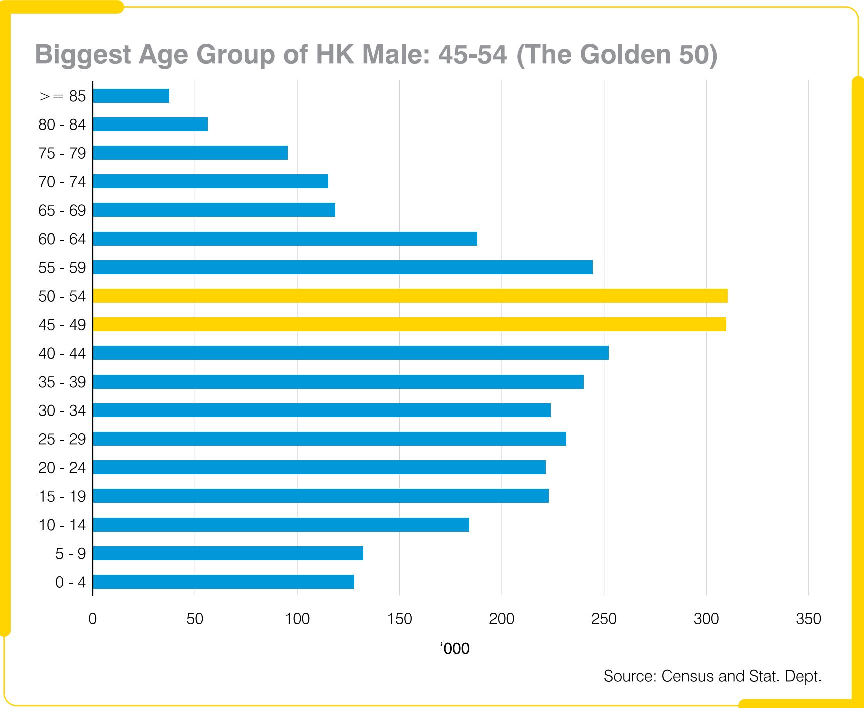


As far as software is concerned, the number of doctors per 1,000 population is 1.8 in Hong Kong, far lower than the average of 3.1 in OECD countries. Insufficient supply of medical staff has led to a significant one-third jump in number of reported medical negligence in hospitals. In fact, as Dr. W.L. Cheung, Director of Cluster Service Division of HKHA has remarked that the public medical system is in acute shortage of doctors and importing overseas doctors would certainly help alleviate the problem.

Number of doctors per 1,000 population is 1.8 in Hong Kong, shortage of medical staff has caused the number of medical negligence to increase by one-third

To make matters worse, the current age distribution of the Hong Kong population brings two important implications: (1) demand for medical services, especially geriatric medical services, will at least triple in 15 years' time and (2) supply of medical staffs will contract significantly as a result of the waves of retirement of baby-boomers in the coming decade.

(1) Demand for medical services will triple in 20 years; (2) supply of medical staff will contract as baby boomers retire



The current age distribution suggests that existing capacity of the medical system caters for about 200,000 men aged 65-74 (similar pattern for women), but 20 years from now when the two yellow bars in the population pyramid shift up, the medical system has to support over 600,000 men in the same age group. On the other hand, our medical system will lose a large number of veteran doctors and nurses as the baby-boomers retire in the coming decade. Given an already overstretched medical system, an expected jump in demand and drop in supply of medical manpower, we must take action now to invest in increasing medical capacity by at least one-third.

We have to act now: invest to expand our medical system by one-third

	Capital expenditure HK$bn	Operating cost per year HK$bn
Increase hospital capacity by one-third • Expansion of 6,600 hospital beds • Replace and upgrade old equipment for hospitals and research centres • Corresponding increase in operating expenses (staff, drugs, medical supplies etc.)	40	13

We call for an expansion of hospital capacity of 6,600 beds and funding hospitals and research centres (e.g. Centre for Infection) to replace and upgrade their equipment. This involves capital expenditure of HK$40bn and a recurrent expenditure of HK$13bn per year for the cost of additional medical staff, drug and other medical supplies for operation.

Here we highlight two points in carrying out such an expansion: (1) The expansion should correspond to the relative shortage of medical services across districts. For example, the Kowloon East Cluster should be considered first, given the highest proportion of population aged 65+ and only three public hospitals in the area. (2) There are actually potential land resources that we may utilise for hospital expansion in the urban area. Just to give an example, relocating the barracks near the Baptist Hospital can vacate a site that measures up to 10 ha (c.1m sf). While this is just one of the many suggestions to consider, the general direction is that we need to have more proactive and creative ways to find land for expansion of medical facilities.

To alleviate the acute shortage in medical staffs, we believe the strategy should include importing overseas doctors to meet immediate demand and expanding medical schools to increase supply in the longer term as the current rate of expansion of medical schools is too slow compared to the increase in medical demand. We certainly need some more radical reform if we do not want to fall even more behind our peers.

We shall address these issues in greater details in our fourth report, “How to Build a World-class Medical System”, coming out in May.

(4.5) HK$15bn to Expand our Universities and Improve Quality of our Economy's New Blood

	Capital expenditure HK$ bn	Operating subsidy per year (per 4-year degree for 10,000 students) HK$ bnHK$ bn	Return per year (extra income of 10,000 students earned over 35-year work life) HK$ bn
Add 10,000 university places	15	2 (8)	3.2 (112)

We propose to invest HK$15bn to add 10,000 university places and admitting more non-local students

We therefore propose to invest HK$15bn in expanding our universities by 10,000 places, or 67%, and admitting more non-local students, due to the following three reasons:

(1) To produce more university graduates to meet labour demand;

(2) To attract more talented students from the mainland and the rest of the world to establish Hong Kong as a regional education hub;

(3) To extend the channels through which the value system and excellence of this World City can be exported to the world, increasing its global influence. London universities do not cater only for students in London or the United Kingdom, but the world. By absorbing such a wide range of talents, the perspectives of both local and overseas student are greatly shared and extended.

The total extra income gained by 10,000 students completing a four-year degree programme amounts to HK$3.2bn per year, and is significantly higher than the additional operating subsidy of HK$2bn per year.

Prof. Francis Lui of the Hong Kong University of Science and Technology has calculated that one year of university education could increase income by 15-18%. We estimate that aggregating the extra income gained by the 10,000 students after completing a four-year degree programme would amount to some HK$3.2bn per year, or HK$112bn over the course of a 35-year working life. This income gain represents the gain by society and which significantly exceeds the additional education subsidy to run such a course of HK$2bn a year, or HK$8bn over the four-year programme.

Hong Kong has all the makings of a recognised regional education hub and the quality of our universities reflects well in global rankings: four out of the eight UGC-funded institutions in Hong Kong are ranked top 20 in Asia while only three mainland universities are so ranked despite the vastly bigger student catchment.

"Hong Kong has all the makings of a recognised regional education hub: four of our UGC-funded universities are ranked top 20 in Asia"

Global Ranking of Universities

Rankings	Asia	Worldwide
University of Hong Kong	**2**	**34**
Peking University	4	49
Hong Kong University of Science and Technology	**7**	**62**
Tsinghua University	8	71
The Chinese University of Hong Kong	**15**	**151**
University of Science and Technology of China	19	192
City University of Hong Kong	**20**	**193**

Source: Times Higher Education 2011-2012

In other words, students from the mainland and the rest of Asia find universities in Hong Kong desirable institutions for their education. This is especially true for students in southern China due to geographical proximity. The first survey on mainland graduates at the University of Hong Kong (HKU) conducted by HKGolden50 has confirmed this view, with 88% of the respondents saying their education at HKU had given them an advantage over mainland degrees.

Students from the mainland and the whole of Asia would find Hong Kong attractive as a place to pursue university education

We have identified three possible methods to accommodate the HK$15bn expansion of universities: (1) reclamation for universities with a water frontage (2) a re-configuration of land usage and density to make for more buildable space for campuses which are located in urban areas and (3) making use of the Lok Ma Chau (LMC) Loop to develop "second campus" and new high technology research centres.

(1) Reclamation for universities with a water frontage, (2) Re-zoning and changing density for universities in the urban area and (3)development of the LMC Loop are possible options to accommodate expansion of universities

(4.6) HK$4bn to Promote and Enrich Art & Culture for a Vibrant, Upbeat & Cultural World City

Hong Kong has to foster its art and culture sector through more active government support. A World City manifests its influence in the international arena not just through its "hard competence" like economic and brain power, but also its "soft competence", in its appreciation of the human experience and artistic expression. A hardworking population needs a good dose of art and culture to refresh the spirit and unwind stressed minds.

Hong Kong has to foster its art and culture sector through more active government support

We propose two policies: (1) allocating the extra HK$4bn necessary to start constructing the West Kowloon Cultural District (WKCD) immediately and (2) re-work the delivery programme so that facilities will not be opened until 2018 when 25% of the entire project is complete, as opposed to the current plan of opening in 2015 with phase 1 which involves only 9% of the complex and measures a Lilliputian 700,000 sf. The size of phase 1 is not enough to justify a special trip (not a destination) and in its attempt to suit many tastes and biases, it contains too many of everything. Hence, it runs a real danger, in our view, of pleasing no one. Public interests in the project will quickly wane and support to finish the remaining 91% will be jeopardised.

(1) Allocate an extra HK$4bn to start construction of WKCD immediately; (2) re-work the district's delivery programme

We sincerely hope that you find this report informative and useful and has helped you to understand better both the huge potential open to Hong Kong in the coming 50 years and the challenges and opportunities that we face, as a community, in these pivotal Golden 5 Years. We are eager to know any comments or suggestions that you may have about our report. Please let us know your thoughts by emailing friends@hkgolden50.org and please stay in touch through our website www.hkgolden50.org.

There is a lot about Hong Kong's future that all of our citizens should understand, reflect on and take positive action about. HKGolden50 encourages discussion and ownership of these immediate issues

2: Invest to Improve in our Service Capacity and Capabilities – Build World-class Hardware

In directing the development of Hong Kong back to its original path of becoming a World City, we need a clearly annunciated masterplan. Hong Kong should approach this holistically, putting up new hardware and software capabilities as are necessary for the full and effective performance of this World City instead of the piecemeal, haphazard approach of devising standalone solutions that target only one aspect of the economy/society as has been the practice for the past decade or so.

A holistic approach involving building hardware and software capabilities, a masterplan, is a "must" to steer Hong Kong towards its destiny of becoming a World City

For instance, immigration policies and taxation rules are means to a policy end and are not an end by themselves. Yet, none of these tools have been deployed as instruments to a policy as there has not been an immigration policy nor a scheme to foster any capabilities. Henceforth, we should provide incentives to businesses that are considered essential to our move to becoming a World City and talents that can catalyse the transformation. Most countries have such schemes and Hong Kong should not lose out in the global fight for entrepreneurship and talents which can bring long-term benefits to our people.

Many of the diverse tool-set of public policy instruments are yet to be deployed in Hong Kong

Another example is that scant, if any, mention was made in the approval of the HK$62bn Guanghou-Shenzhen-Hong Kong Express Rail Link and the 50-km HK$47bn Zhuhai-Macau-Hong Kong Bridge as to how the customer and vehicular traffic these infrastructure projects will bring to Hong Kong could be accommodated or serviced.

Some of our mega projects do not seem to dovetail with other public considerations – for instance, can the traffic from the HK$47bn Zhuhai-Macau-Hong Kong Bridge go all over the territory?

In addition, our community has learned precious lessons from some 50 years of building new towns and world-class infrastructure. We should not have much problem devising, when taking our first shot for the future, efficient and user-friendly new spaces to house our new businesses and future population. It pays, however, before we set out the details of the two significant pieces of hardware Hong Kong should start investing in during the Golden 5 Years, that we refresh our memories of three key lessons in building hardware from over the past half-century:

Armed with 50 years of hard earned lessons in building new towns and infrastructure, Hong Kong should be able to plan and execute our new hardware investment programme perfectly

(a) Scale – with scale, come choices, convenience and better living environment

The first lesson is the need for scale. Hong Kong puts a rich premium on convenience. While greenery is top priority to most residents in other countries, the Hong Kong populace most likely place convenience to work place and shopping spaces as equals to greenery, if not as a higher preference. Convenience is often a function of scale. For instance, a new town needs to have over 240,000 residents to justify a public hospital and scale is essential for mass transit facilities to be built nearby. And of course, with scale, comes large shopping centres, libraries, cinemas, sports grounds, art facilities, schools and frequent public transport – offering residents plenty of choices and quality of life.

Lesson 1: Scale is everything for a convenience-centric Hong Kong populace

A lesson we learned to our cost is that almost every new town we built in the past 50 years has a bus terminal as its centre point. If Shatin, our first and largest new town north of Lion Rock, were to be re-designed, chances are that we would put more recreational space at its heart with New Town Plaza by its side so that the town's c.650,000 residents can have greenery and convenience in equal measures.

In our next new town, we will have green, open, community space at its centre, and not another bus terminus!

Furthermore, in our next new town to come out of reclamation, all the land-filling will have been completed by the time people start moving in. This will get round all the nuisance current residents of Tseung Kwan O are putting up with as reclamation comes in protracted phases, causing dust, odours and traffic over many years.

Our next new town to rise from reclamation will have all its land formed, when the first residents move in

Our history of building new towns for private, public housing and community needs is littered with examples of undersupply. For instance, the first development plan for Shatin in 1961 foresaw a population of 360,000. In 1972, new plans were drafted and reclamation in Tolo Harbour was undertaken to increase the township's capacity to 500,000. Another ten years later, traffic capacity for Shatin and Ma On Shan was increased to 704,000 and in 1986, another government review raised the district's planned population to 750,000. In all, Shatin grew from a village of 30,000 in the early 70's to a 3,591 ha new town of 630,000 people today.

Noting we have consistently underestimated Hong Kong's needs for community and commercial spaces, we must put right our past wrongs and build suitable land reserves that cater for our future needs, starting with "Project Flying Dragon" ("飛龍計劃"), provisional name for a re-planning of our backwater town of Tung Chung into our most significant and most environmentally friendly new city for 700,000

In our proposal to build the "under-provided" township of Tung Chung (current population: 82,000) into the world's most environmentally-friendly new town which we have provisionally named "Project Flying Dragon" ("飛龍計劃") which will be discussed in the next section, we will recommend reclaiming land and building public facilities sufficient for a community the size of Shatin (700,000) to arise over two to three decades.

Over HK$160bn worth of new infrastructure or HK$2m per resident in its neighbourhood within the next ten years will enable centre-of-delta town of Tung Chung to "take to the sky" in the coming two to three decades

Just as the name "Shanghai" ("上海") summons up the aspiration of a city to "reach out to the four seas", "Flying Dragon" ("飛龍") symbolises Hong Kong people's cosmopolitan ambition. Fuelling the growth of this new city at a rate similar to that of Shatin's is its situation at the gateway to all the mainland provinces west of Hong Kong. If the evolution of Shatin, our first new town north of Lion Rock, benefitted from the growth of China from a very low income base in the past 30 or so years, Flying Dragon should experience a faster rate of growth, spurred by the sustained development of China on a significantly higher income level and the much improved porosity for people and business opportunities to flow into Hong Kong.

Looking at the physical means for inflows from neighbouring Guangdong province, for instance, we can expect significant improvements which will lead to growth opportunities in the neighbourhood of Flying Dragon. The HK$47bn Zhuhai-Macau-Hong Kong Bridge will open in 2016 and put Flying Dragon right at the centre of the 70m population Pearl River Delta with the best infrastructure which will cost some HK$160bn (or HK$2m per resident in Tung Chung) in the region radiating from it. These infrastructure projects will include the expected completion of our airport's HK$86bn third runway in 2023 and the proposed HK$23bn 9km Tuen Mun-Chek Lap Kok Link in 2017.

(b) "Build it, and they will come" – This is particularly true for the demand for commercial and community spaces given the "trending" or "structural" nature of demand for Hong Kong services in these few years

Lesson 2: There are no "white elephant" properties in Hong Kong

Any observer of Hong Kong property prices and rental trends over the long term cannot fail but notice that the pattern of movements has consistently been from the bottom left to the top right, despite the occasional gyrations. Somehow, a period or a district of high vacancies would turn into a subsequent period of shortage and price and rent hikes. Hence, while there can be some short-term pains and developer failures, there does not seem to be big danger for Hong Kong to build properties that will not be used and occupied. Build it, as the saying goes, and they (end-users) will come.

Kowloon Bay – the latest example of "rags turned riches"

The most recent example of this process of seeming overbuilding transforming into shortages is the office situation in Kowloon East. Briefly outlined, this district was started as a piecemeal selling of government sites for low rent (started as low as HK$5-8psf a month) and a rezoning of previous industrial uses into office functions. After a few years, the spillage of high grade tenants from traditional locations from 2007 has turned this to become one of the two largest office clusters in the territory with spaces almost fully occupied and rents shooting up to HK$20-30psf, over a period of three to five years.

There are many reasons for demand for commercial and housing spaces to be consistently strong in the territory but the sustained demand for Hong Kong services which form some 95% of our GDP and jobs by the rest of the world must lie at the centre of this property demand trend. Whenever demand for space is not matched by new supply, rents go up and businesses relocate to suit their own budgets – this takes place with a fluidity not often seen elsewhere in the world and this ensures that new and cheaper places get filled in rapidly. In most periods other than at the present, there were always office spaces going for less than HK$10psf, allowing room for start-ups and NGO's to survive.

Businesses fluidly move around the territory to fill spaces that suit their budgets – this lends significant support to any new district and enables it to attain critical mass quickly. The surge in rents in the first two years of the Golden 5 Years has removed the sub-HK$10psf option for start-ups and NGO's – not a healthy development for Hong Kong

In these few Golden Years, with "One-Country, One-Market" (eg. offshore Rmb, Mini-QFII and Individual Visits Scheme (IVS) etc.) continuing to fuel demand for more Hong Kong services and the freer movement of businesses, capital and people across our economic border with China, demand for all kinds of spaces in Hong Kong is stretched to unprecedented levels. The opening of new hard infrastructure (e.g. Zhuhai-Macau-Hong Kong Bridge and the Guangzhou-Shenzhen-Hong Kong Express Link etc.) will likely bring even more inflows and exacerbate this situation. The recent public attention to mainlanders becoming dominant users of certain local facilities is a reflection of the inability of the private and public sector to respond to the heightened demand for Hong Kong services. But it is the trending nature of this type of service demand that underwrites our investment in new hardware to support our economy and jobs for the younger generation.

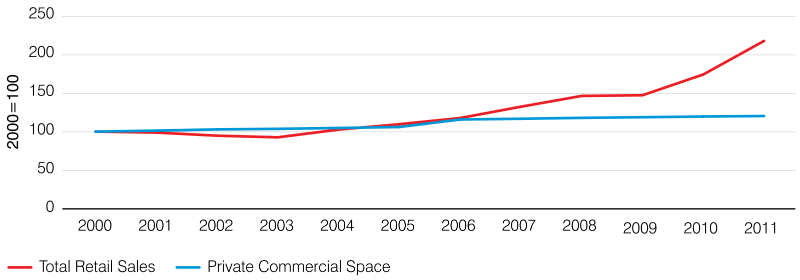
Demand has outstripped supply to result in unprecedented rentals – things will worsen as more inflows are on the cards

Demand has clearly surged but the supply needle has hardly moved – a market cum government failure?

One very troubling aspect of how our hardware has responded to the significant jump in demand for spaces in these few years is that it has not. Take retail spending for instance, during 2010 and 2011, the first two of the Golden 5 Years, total dollars spent surged almost 50% but retail space only increased by 1%. Taking total retail spending back a further three years, when total retail sales rose 85% from 2006 to 2011, total retail space only increased by little over 3%.

Retail sales surged almost 50% in the Golden Years 2010 to 2011, and 85% 2006 – 2011, but supply of shopping space barely nudged 1% and 3% over these periods! This suggests both market and government failure to facilitate supply – resulting in rent surges and inflation

Suggesting market/government failure, supply of retail space has not responded to sharp jump in retail spending in the past two-to-five years



Source: HK Census Stat. Dept., Rating and Valuation Dept.

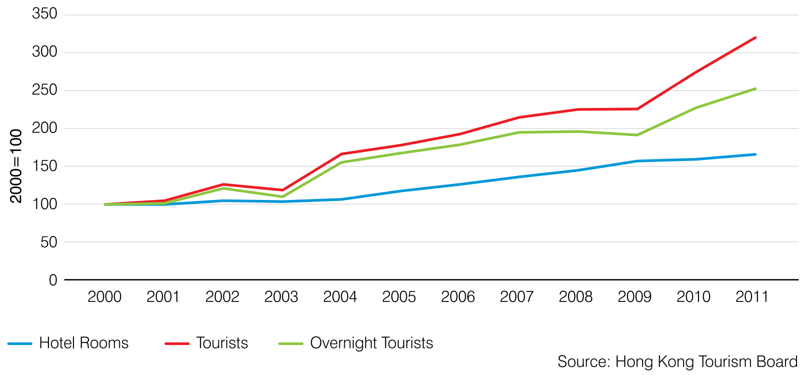
This absence of a supply response is particularly alarming as the cost of financing a build out of commercial space has fallen drastically to record or near-record low, thereby making it even more financially attractive to undertake a new shopping project. A contributing factor to the absence of new supply may well be that for a shopping centre to be viable, it has to be sizeable, probably above 400,000sf in scale. Such sites are hardly available in the urban areas when redevelopment projects have tended to be small and the government has not provided such sites at public auctions or land tenders. Unless the government realises that retail spaces support a lot of jobs and lessen the extent of our retail inflation and step up production of such projects, the community is likely to continue to suffer from rent-induced inflation in the next few years.

Big shopping spaces have to be produced by the government as developers are unlikely to be able to induce these through urban redevelopment or procurement of new town sites

The situation with our hotels is hardly better – while overnight visitors surged 32% in 2010 and 2011 (visitor arrivals actually spiked 42% but the unavailability of rooms probably forced many tourists to stay in Macau or Shenzhen), the first two of the Golden 5 Years, marking a sharp acceleration of arrivals from preceding years. The production of hotel rooms, on the other hand, only rose 6% and marked the first deceleration in supply over the past decade.

Visitors rose 42% in 2010 and 2011 but hotel rooms increased only 6%

Growth in Number of Hotel Rooms and Tourists

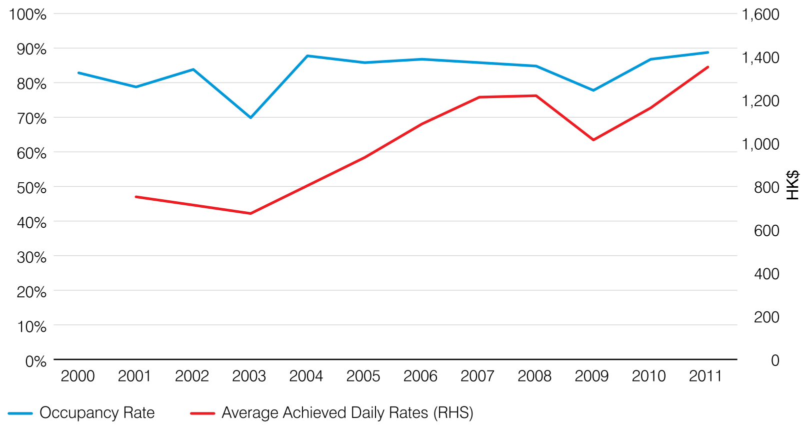


Source: Hong Kong Tourism Board

While overall hotel occupancy has remained at around 88% throughout the past decade, the relative absence of supply has translated to record all-grade blended daily rates of cHK$1,400 and represents c.45% jump from 2005 levels. It is likely that a shortage of hotel rooms and shopping spaces has conspired to compromise the quality of visitor experience in Hong Kong.

Lack of rooms and expensive charges, plus a shortage of shop spaces and pricey-goods, will form a deterrent to visitors – undermining growth of tourist industry, jobs and attractiveness of Hong Kong

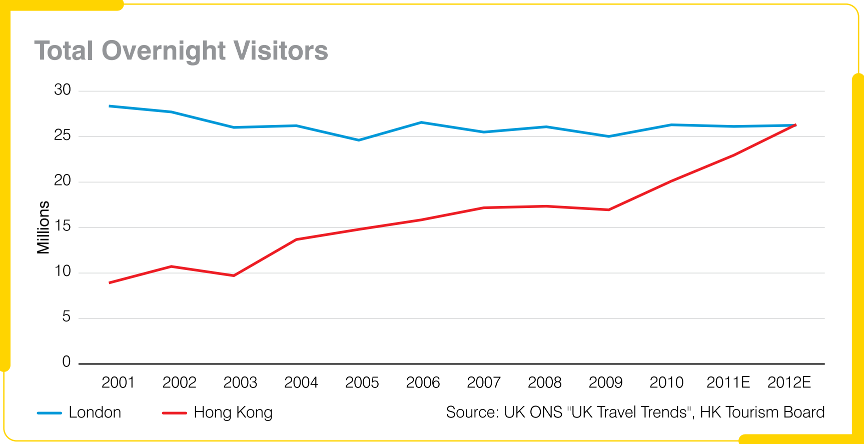
Hotel Rates and Occupancy Rate



Source: Hong Kong Tourism Board

Hong Kong is forecast to overtake London in terms of overnight visitors in 2012.

Even though overnight visitors to Hong Kong is expected to overtake London's this year 2012, London has 75% more rooms – clearly, lack of rooms and high rates in our city are chasing away customers



While London's overnight visitors fell from 2001 to 2012, Hong Kong equivalents have risen some 190% and on strong momentum. Overall room numbers on the other hand increased only some 65%.

Overnight visitors and Hotel rooms - Hong Kong vs London

	Hong Kong	London
Number of Hotel Rooms	62,660 (2011)	109,700 (2010)
Number of Overnight Visitors	26,321,000 (2012)	26,232,000 (2012)

Source: HK Tourism Board, UK ONS, HKGolden50

(c) We must be friendly to the environment

A perennial problem in our history of developing new towns is that they have all but failed to be self-contained, with most residents having to travel outside their districts to find work for instance. In planning for a better Hong Kong, we should actively consider bringing work to residents and this should reduce carbon footprint associated with employment.

By bringing workplaces and homes closer together, carbon footprint arising from commuting can be minimized

In addition, when we reclaim the sea for land, we must restrict our encroachment on marine life to "already disturbed" or "low environmental impact" areas and coastlines which support far fewer creatures. Hong Kong has more sea (1,650 sqkm) than land (1,104 sqkm). When our population is forecast by the government to grow 1.9m, or 27%, to 8.9m in the 27 years by 2039, given the public's preference for scale, it is likely that a significant part of the space has to come from reclamation. The government has indicated that every 1m population will require an extra 1% of Hong Kong's land to accommodate, implying Hong Kong needs roughly 22 sqkm of residential land by 2039. If this were all to be provided by reclamation, this would amount to some 1.3% of our sea. Given that we should still have 98.7% of our sea, it should not be difficult for us to devise a means to create marine reserves, artificial reefs or other means to enhance aquatic life to more than offset the quantum of creatures that have been affected by such disturbance. We must be able to increase the biomass or the "marine productivity" in the 98.7% of our unreclaimed sea by at least 1.3% to ensure we will not compromise the quality and quantity of our precious marine habitat. It goes without saying that studies on a development's impact on the environment must satisfy necessary standards before green light is given on its construction.

We must be able to increase the biomass or the "marine productivity" in the 98.7% of our unreclaimed sea by at least 1.3% to ensure we will not compromise the quality and quantity of our precious marine habitat

This viability of this pro-marine-life approach to development can be appreciated by noting that despite the reclamation in Victoria Harbour over the past decade or so, (1) the water quality has improved to such an extent that the Cross Harbour Swim restarted in October 2011, after a stoppage lasting 32 years when the harbour was deemed too contaminated and (2) the fish count has increased. There must be many ways we can be creative and improve the biomass and bio-diversity of our precious marine endowment while we carefully choose the least-impact way to develop and encroach on the environment.

We will apply all these three lessons from the past in the crafting of our proposed investments in new hardware.

2.1 Invest HK$22bn in an 11m sf "Gateway to the World" commercial complex to showcase Hong Kong's world-class services (retail, medical, hospitality, credibility, arts, NGO's and many others) and re-plan Tung Chung as befits its potential of becoming the gateway city of the affluent Pearl River Delta, home to 70m people

Recognising the community imperatives outlined below, we propose the construction in the district of Tung Chung, two sizeable projects – one for commercial use and the other for community purposes the final names for both will be determined by the public in due course. The first one is tentatively named "Gateway to the World" ("環球薈"). It is an 11m sf commercial facility (first phase opening 2016, last phase 2020) in the existing grounds of the airport. Abbreviated as "GTTW", the name signifies the project's significance as the gateway to the World City of Hong Kong – by air, via the airport and by land, via the Hong Kong-Zhuhai-Macau Bridge from the west and the likely Tuen Mun-Chek Lap Kok Link from the north.

Situated at the heart of the PRD and >HK$160bn of new infrastructure (HK$2m per resident), the humbly named Tung Chung (a tiny brook towards the east) has a far bigger destiny -- to become the most convenient and environmentally-friendly community in the World City of Hong Kong

The second project is the residential city of Flying Dragon ("飛龍"). It comprises the existing new town of Tung Chung (a tiny brook towards the east) and will be built mostly on reclaimed land over the coming 20-30 years. The new city, which will situate at the infrastructure centre of the Pearl River Delta with a population of 70m, will have a population capacity of 700,000, similar to that of Shatin, our first new town north of Lion Rock.

We propose two projects: (1) Gateway to the World ("GTTW") to offer the best services of our city to our customers arriving "at the gate" and (2) Flying Dragon to be our first fully-integrated environmentally friendly new town with zero-carbon footprint travel to employment provided at its doorsteps at GTTW

With at least HK$160bn worth of infrastructure spending completing in the area within the next ten years, all tapped into the richest region of China and approximately HK$2m for each of the 82,000 residents there - clearly a record for Hong Kong, the location's potential for economic and community development should far exceed that of all of our existing new towns. Just as Shanghai's name encapsulates the city's spirit to "take to the four seas", Flying Dragon symbolises our World City's cosmopolitan aspirations. Furthermore, by correcting the orientation of Tung Chung (which is actually on the west of our territory, not east (東), our city will have a rainbow (彩虹) to the east, and a flying dragon (飛龍) to our west. (東有彩虹， 西有飛龍).

Flying Dragon and GTTW will provide the opportunity for us to (1) put to action all the positive lessons we have learned from and (2) correct all previous design or operating "wrongs" in the building of new towns over the past 50 years. Hence we should be confident that we can now, with the tailwinds of rich opportunities of the Golden 5 Years behind us, craft our most convenient and environmentally friendly new town for the next 50 years.

Our hard-earned know-how of building new towns should ensure we "get it right first time" with our best-endowed new town yet

Having taken into consideration the below and other good reasons, we recommend the construction, under the auspices of Hong Kong Airport Authority (HKAA), a multi-use commercial complex GTTW and directly by the government, the new city of Flying Dragon:

16+ reasons to invest HK$22bn in a 11m sf multi-use commercial complex to showcase our services at the airport for first-phase opening in 2016, in time for the opening of the HK$47bn Hong Kong-Zhuhai-Macau Bridge that year

(1) The acute undersupply situation in retail, hotel and office spaces currently and the lack of any meaningful relief in the next five to six years.

Acute shortage in commercial spaces to persist in the next five to six years

(2) The structural nature of demand growth in this sector (discussed under the concept "One-Country, One-Market" in our previous research reports).

Demand is likely to remain robust for quite some time

(3) The potency of these opportunities in helping our new citizens by (a)creating new jobs and (b) retaining existing jobs within Hong Kong. We estimate that GTTW can support 36,000 jobs on site upon completion of its first phase consisting of the facilities discussed here. The land grant for the site allows another 10-11m sf of mostly logistics use. It is likely that a phase 2 can be built, depending on demand and is to be considered after phase 1 has been in operation for a decade. The construction of phase 2 or any logistic facilities should create a further 36,000 jobs, resulting in a GTTW direct workforce of 72,000. This compares with the 62,000 workers directly employed at the airport recently. Assuming a 4% servicing staff for the facilities at Flying Dragon, a further 28,000 jobs should arise when the city reaches a capacity of 700,000. Together with the current on-site workers numbering 62,000, the above should already provide jobs for 162,000. If the staffers represent the only person working in a family and assuming a household size of three, then direct employment in GTTW and Flying Dragon can already support a 486,000 population.

An estimated 162,000 jobs may arise on site at the airport, GTTW and Flying Dragon - can already support a population of 486,000. Perhaps employment / population double that size can also be supported off site. Furthermore, the third runway will create 141,000 jobs. With such potent job creators embedded in these facilities nearby and the adoption of the best town-planning standards, Flying Dragon should be a desirable place to live for many.

The Airport Authority has estimated 141,000 jobs to arise from the construction of the third-runway and this should support a further 423,000 population even though this may not be on a permanent basis. In addition, the Airport Authority 2008 estimates show that indirect/induced employment created by airport operations amounted to 124,000 jobs, double that of direct employment. Hence, it is easy to appreciate that airport and other commercial functions at centres of infrastructure are very potent in creating both low-skilled and high-skilled jobs and GTTW and Flying Dragon should not be difficult in creating enough jobs for a busy community.

Of course, the extent of how many families that rely on the many jobs created on site and offsite will choose to live at Flying Dragon cannot be determined with certainty. That said, if all the mod-cons and environmental features are designed into crafting a most convenient and green new city, compared with the rest of the territory which contains mostly older housing stock, it should not be difficult for Flying Dragon to become a popular option for families.

(4) The importance of creating new "content" in Hong Kong in order to attract more visitors to use our airport, especially when we are about to commit HK$86bn now or HK$136bn "money of the day" to add a third runway. With Hong Kong residents accounting for only around 30% of the users of our airport, the potential for growth from this source is not likely to be enough to justify a third runway. Growth from the use of our airport by (1) transit and (2)other passenger sources eg. travellers using land transport to come to Hong Kong from Shenzhen and the rest of Guangdong, will be imperative to Chek Lap Kok's growth.

By conveniently putting Hong Kong world-class services at the gates of our airport we will have created a content-rich "one-stop shop" for our customers in the PRD and help ensure viability of our third runway

Thus, Hong Kong needs to ensure that the building of further airport capacity and international routes at Guangzhou and Shenzhen will not undermine the demand for our airport. One effective way of achieving this is to ensure there are many more reasons and experiences for people to come to Hong Kong. Creating a significant hub for Hong Kong's world-class services in credibility businesses, retail, medical care, education conveniently situated at the gates of our airport will create a "destination draw" for our runway capacity.

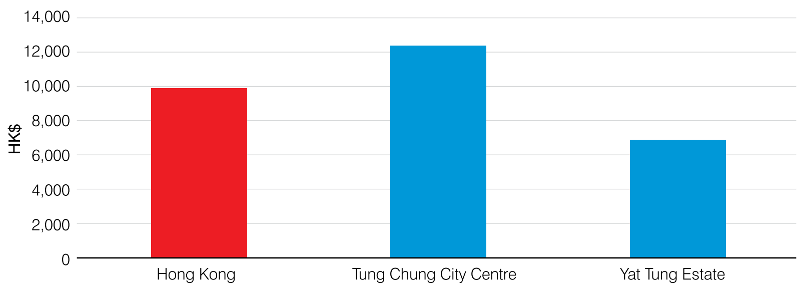
The Airport Authority invests HK$136bn to build the third runway for our airport, which needs 28 years of construction in three phases. However, its future utilisation is uncertain - 70% of all users of our airport are non-Hong Kong residents, and many of them for stopovers may use the nearby new second runway of Shenzhen Bao'an International Airport (completed in 2011) and the new third runway of Guangzhou Baiyun International Airport (expected to be completed in 2015). By complementing the third runway investment for our airport with the profit of nearly HK$3bn from GTTW rentals every year starting from its full opening in 2018, GTTW serves as a good hedge for the uncertain future profit from the third runway which opens after 2030.

GTTW, with cHK$3bn first annual profit from 2018, serves as a good hedge for the uncertain future profit from the third runway which opens after 2030

(5) The need to transform the "forgotten" under-sized backwater Tung Chung into a purposeful community and an desirable place to live. As things stand, the 82,000 residents fall well short of the 200,000 threshold for a public library and the 240,000 for a general hospital and other public and private amenities and job offerings for its residents are few and narrow.

There is great need to turn an "underperforming" Tung Chung into a vibrant and desirable place to live

Even though the latest available income data show that the median incomes in Tung Chung are similar to that of Hong Kong as a whole, those living in Yat Tung Estate (which comprises half of the new town's population) have a significantly lower income at only HK$6,000-7,900. Low-income residents (defined as 50% lower than median income of Hong Kong) comprise close to 50% of Yat Tung Estate. This level of poverty is reflected by the fact that almost half of households living in Yat Tung Estate are on Comprehensive Social Security Assistance (CSSA) - the fourth highest among all housing estates in Hong Kong, after Sau Mou Ping Estate (Kwun Tong), Kwai Chung Estate (Kwai Chung) and Pak Tin Estate (Shek Kip Mei) all of which are "very old districts". These statistics suggest that while the new and modern township of Tung Chung has managed to attract above-average income households, most likely due to the opportunities provided within Lantau, there is a large segment of under-performing families. The provision of significant non-office-based service opportunities within their neighbourhood in GTTW should not only enable this group to better their lot, but also improve the attractiveness of the district as a source of private and public housing alike.



Reports on the plight of Tung Chung residents by a multiple non-governmental organisations such as the Hong Kong Outlying Islands Women's Association and the Hong Kong Chinese Civil Servants' Association often cite the long distance and high commute expenses as problem areas. As a result, apart from a small number of Tung Chung residents who work at the nearby airport, most are stuck without much opportunity to improve their situation, effectively creating chronic low employment and thus poor living standards.

Tung Chung residents have to travel a long way to find work

The small population in Tung Chung also results in limited retail choices, which ironically translates into high prices that cannot be afforded by the low-income residents in the community. In various price-checks conducted by CSSA Alliance, Community Development Alliance and Hong Kong Federation of Trade Unions in 2011, prices of daily food and necessities are 10%+ higher in Tung Chung when compared to that found in Hong Kong's richest district, Wan Chai.

Prices of daily food and necessities are 10%+ higher in Tung Chung than the richest district in Hong Kong

(6) The government forecasts that the Hong Kong population will grow 1.9m (up 27% from the current 7m) to 8.9m by 2039. This suggests a 27% increase over the next 27 years or roughly 1% or 70,400 persons a year. Simplistically put, a total of at least three Shatins will have to be built in 27 years, or approximately one Shatin every nine years but there is nothing available for the production of anything remotely near the capacity of Shatin within the next nine years.

Hong Kong's population will grow 27% in the next 27 years, adding 1.9m over this period – this suggests we have to find space to house one Shatin's worth of residents every nine years. There is no obvious way to produce the first of our three Shatins

(7) Our citizens aspire to building a most environmentally friendly town that befits the World City of Hong Kong. We have the population and commercial needs for a new town and the means to create a most desirable environment to live, work and play in. Flying Dragon and GTTW give us the opportunity to focus all our development experience over the past decades and the latest technology and design considerations to craft a new town that is consistent with our aspiration to be the greenest World City.

Flying Dragon and GTTW will be the world's most environmentally friendly community adopting the world's best sustainability standards

Hence, we should insist that the best applicable green standards are adopted in creating Flying Dragon and GTTW. Even though all green standards (counting BEAM, LEED and China's Three-star) apply only to buildings and not high-density communities, we must still aspire to be creative in devising the highest sustainability solutions in the building of this new community. The adoption of central water-based air-conditioning system that saves significant energy and facilities that treat food wastes may be considered.

The pairing of jobs with residence saves commuting time and minimises carbon footprint. Reclamation in the shallow and already disturbed coastline at Tung Chung and north Lantau makes relatively low-impact to marine life and reparatory measures will be undertaken in other parts of our waters to more than offset the biomass affected

We recommend that the zoning and building plans for the North Lantau district be overhauled to reflect the new reality of it becoming the centre of the Pearl River Delta (PRD) infrastructure network and our community's desire to have the most environmentally friendly community there. This should free our town planners and professionals from the shackles of an old plan which could not have taken these new priorities into account.

Flying Dragon should be a custom-designed town with the best environmental designs – existing Outline Zoning Plans and other planning constraints would have been superseded by the subsequent new infrastructure links and technology

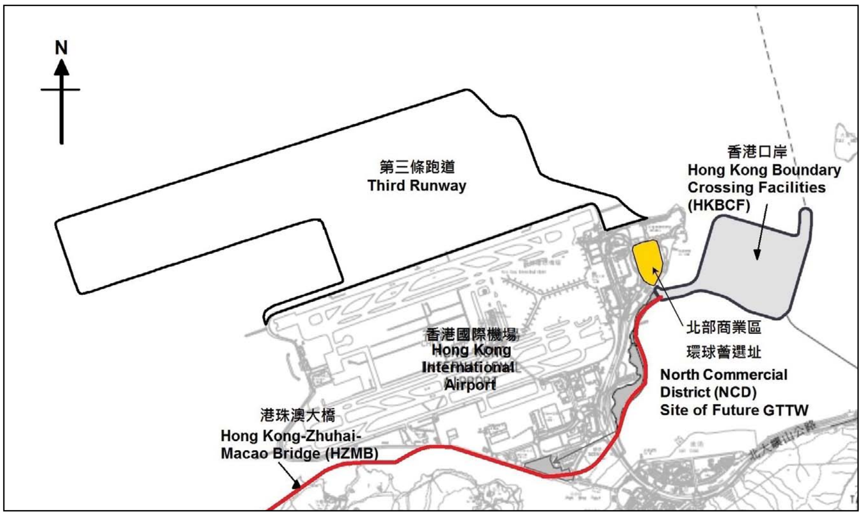
In the comprehensive review on development potential of North Lantau, all pre-existing prescriptive limits including noise zoning should be re-optimised in light of new technology and other planning possibilities.

The pairing of jobs with residence saves commute, leaving more time for family, leisure and exercise, and minimises carbon footprint. Reclamation in the shallow and already disturbed coastline at Tung Chung and north Lantau, fringed by an expressway and train tracks to the airport, makes relatively low-impact to marine life compared with formation of land in pristine districts. Full reparatory measures will be undertaken in other parts of our waters to offset more than the biomass affected by the reclamation.

It is inevitable that building a new town the size of Flying Dragon will take up to some two decades. If the reclamation work has to be phased, even though it is desirable to have disturbance over and done with over a short period, then such nuisance to early-phased residents should be minimised. For instance, consideration should be given to patterns of prevailing winds and ways of providing green cover on newly formed land so that dust and odours can be minimised. Studies should also be conducted to establish if there is economy of scale and impact on the environment for the reclamation to take place alongside the land formation for the third runway.

If phasing of reclamation is inevitable then steps should be taken at the design stage to minimise dust and odour. There may also be economy of scale in terms of impact on the environment and cost to overlap the landfilling for the third runway and Flying Dragon

(8) The general public's desire for a home located alongside existing arteries of public transport. For instance, few would want to live in a district when rail links are pending or bus services infrequent.



(9) The completion of the Hong Kong-Zhuhai-Macau Bridge 2016 which enters our territory near the airport, will put Tung Chung within the direct reach of 70m people who live in the affluent Pearl River Delta. GTTW will provide parking facilities initially for 10,000 vehicles (five times the capacity of that at Harbour City), with a capacity option for double that amount in future. This facility can alternatively situate in the Hong Kong Boundary Crossing Facilities (HKBCF) run by the government and which primarily handles Immigration and Customs matters.

The HK$47bn Hong Kong-Zhuhai-Macau Bridge will open in 2016, bringing land traffic directly to Tung Chung which will become an Immigration stopover – naturally creating a hub for "Park and One-stop Shop", "Park and Ride (to the rest of Lantau tourist spots or the urban areas" or "Park and Fly", adding patronage to our airport

Whether the current public concern that allowing left-hand-drive vehicles enter Hong Kong from the mainland will cause accidents on Hong Kong roads is justified is a matter to be debated. Notwithstanding, it is unlikely that our roads will have the capacity to carry thousands of vehicles from Guangdong. Hence, a facility that allows travellers to park their cars at GTTW or HKBCF and take public or private land transport to the tourist destinations (Park and Ride) in the rest of Lantau or travel to the urban areas must be useful. Of course, such a holding facility can support the usage of our airport as visitors can Park and Fly. For those visitors that simply want to patron the world-class services of Hong Kong, including watching performance/show/exhibition at the AsiaWorld-Expo, they need go no further than GTTW (Park and One-stop Shop).

(10) The fact that the site has received town planning and other land use approvals means that construction can start once the go ahead is given to GTTW.

GTTW site has received all planning approvals and requires no new land premium to be paid – thus is an effective "turn key" project which can completed three to five years from the start of a phase

(11) There is no need for new land premium payment – thus the only new investment required for GTTW is planning and construction. In a city where 70-80% of total development cost is often attributable to land, GTTW is a very rare opportunity - effectively having done without the cost of land means a low investment hurdle. With total cost at around HK$1,600psf, even renting of its 1m sf office spaces (two phases) at HK$10psf a month will yield a 7.5% on investment.

With no new cost to pay for land, the only investment hurdle for GTTW to clear is the investment in construction. Such low cost allows room for charging low rents for the earlier leases which will provide greatly needed relief for rent refugees including NGO's, start-ups, SME's and artists who will otherwise need to close down as rents in traditional districts have soared

(12) Liberate the full potential of AsiaWorld-Expo by providing fully-fledged service and accommodation facilities to attract more usage of the exhibition site. Being our second convention centre, the government-owned AsiaWorld-Expo suffers from a low utilisation as users complain there is little for them, and their families if they come along, to do and nowhere to go after attending a conference or an exhibition. This convention centre is one of the best equipped in Asia and Hong Kong can greatly improve its MICE market share and its World City reputation as a conference centre/meeting place/gateway when capacity, quality, enriched user experience, convenience and competitive prices are offered in one comprehensive package at the airport under GTTW and AsiaWorld-Expo. The need to make additional investment for Wanchai's Convention Centre should be delayed until we can observe the potential of the synergies GTTW can deliver to improve utilisation of AsiaWorld-Expo.

By providing a very sizeable and interesting "habitat" for conference and exhibition goers to "keep themselves occupied" after attending their functions, GTTW will greatly improve usage of government-owned AsiaWorld-Expo next door

(13) Our public funds have tended to earn low and unstable returns and investments in US 10-year treasuries can only produce c.2% incomes, which will likely undershoot Hong Kong inflation. Against the trending demand for services and spaces in Hong Kong, and the HK$160bn investment by the government in new infrastructure around GTTW, the project will likely generate a risk-adjusted return far superior than that of the traditional public portfolio and offers a means for our government to add diversity to its holdings.

Investment in US 10-year treasuries only produces c.2% return which undershoots Hong Kong inflation (latest core rate 6%) – adding GTTW should provide far superior risk-adjusted returns to our public portfolio. We estimate GTTW to "payback" in as short as six years of full operation and carries an ultra-high ungeared Internal Rate of Return of 13.8%

Our workings are shown in later paragraphs and they show that GTTW should fully pay off its cost in as short a period as within six years of full operation and it carries an ultra-high ungeared Internal Rate of Return (IRR) of 13.8%. The latter suggests that an investor's cost of funds has to be as high as 13.8% in order to nullify a proposed project's Net Present Value (NPV), or the time-discounted net returns to a project. Financially, since the government is the sole owner of our airport, it does not matter if the government directly undertakes GTTW or delegates the task to the Airport Authority directly.

(14) GTTW provides huge scope for externalities. Further to the highly attractive financial returns that should arise from this project, as discussion later in this section will show that GTTW will generate a NPV of an estimated HK$41bn, the commercial complex should open up substantial externalities and non-direct returns to Hong Kong.

In addition to producing a NPV of HK$41bn, which should be able to offset close to 50% of the Present Value cost of building our third runway of HK$86bn, GTTW provides huge scope for non-financial returns to society and the reputation of Hong Kong as a World City

In the global competition for talents and investors, it is imperative that a city projects a positive image and it is difficult to achieve that if our citizens do not think highly of our administration nor of the direction our economy is heading. GTTW and Flying Dragon are projects with a clear purpose, and they answer the demands already indicated by the market. Their acceptance by the public will rekindle the "Can-do" spirit and remind our citizens what Hong Kong stands for and what made our city great. They will show the world that Hong Kong is taking its future in its own hands again. This positive momentum will draw talents, more credibility businesses and investors from around the world and feed further to the making of Hong Kong's Golden 50 Years.

To the world, GTTW and Flying Dragon are unmistakable signals that the community of Hong Kong has found its purpose and "Can-do" again

(15) GTTW and Flying Dragon have limited downside. Hong Kong has never invested as much in infrastructure in a single location as we are doing in Tung Chung. If GTTW fails totally, the loss of HK$22bn will represent 14% of the other investments of HK$160bn being made to the district and should it fail, more pertinent questions should be raised as to whether the HK$160bn could be justified in the first place. A more reasonable way to look at GTTW should be, since we are committed to some HK$160bn in putting up infrastructure for a better future, we should, using the same positive assumptions about our future, invest a further 14% in new commercial facilities to make it doubly sure that these preceding investments work, by attracting more users and customers to these investments. In this way, GTTW is an insurance premium to underwrite the success of the HK$160bn preceding investments.

GTTW and Flying Dragon have limited downside. If GTTW completely fails, it would represent 14% of total preceding investments in infrastructure and would question the logic of these bigger investments. In a positive way, undertaking GTTW will underwrite the success of these preceding investments of HK$160bn

We should also remember the second lesson learned from 50 years of developing up Hong Kong – there are no property white elephants! Somehow, when we build a property, it gets filled - perhaps not always immediately, but nothing is left vacant and rents somehow, have found their way northwards.

Remember lesson number 2 – there are no property white elephants in Hong Kong. Nestled in so much infrastructure and locational convenience, GTTW is unlikely to become the exception

Flying Dragon is an extremely low risk investment as it mostly involves reclamation which costs HK$250-450psf and should have little trouble from the sale of development land at over HK$2,000psf in gross floor area terms. Against the government's projection of population growth and medium-term growth expectations of Hong Kong, property demand should much more than finance the building out of Flying Dragon. Hence we have not sought to model how positive the NPV of such a process can be.

(16) The importance of re-enforcing Hong Kong's "First mover advantage" in service sector by adding scale and diversity. The robust visitor arrivals and the influx of overseas companies, talents and capital into Hong Kong in the Golden 5 Years clearly evidence the quality and attractiveness of our services. When the gap between our immediate hinterland, the PRD and our city narrows over time, Hong Kong's advantage of being the service hub for the entire region can be made unassailable when we add significantly to scale and diversity when the difference in standards is still great as is the case today. GTTW can be a powerful contributor to building up Hong Kong's first mover advantage.

Flying Dragon involves mostly reclamation which costs HK$250-450psf. Against population growth and medium-term economic prospects, new land should sell above HK$2,000psf and easily justifies the project. Hence no modelling is considered necessary here.

By adding scale and diversity to the city's service provision, GTTW can re-enforce Hong Kong's "First mover advantage" in the PRD

A. What are we investing in?

- An 11m sf world-class commercial complex, roughly twice the square footage of the Harbour City complex in Tsimshatsui, to situate at the North Commercial District in the airport, to showcase Hong Kong's excellent services to the world, featuring:

a) A 4m sf destination mall with 600+ shops (mostly outlet format) and restaurants. These should add around 4% to Hong Kong total retail spaces.

b) A 1m sf medical service centre with 400+ beds and surgical facilities so that patients from around the world can fly or driven in for treatment. Visiting relatives can stay in the hotels and can occupy themselves with the many facilities within GTTW and Lantau during non-visiting hours.

c) A 1m sf office which initially will provide low-rent spaces to tenants from outside districts and will also support the airport and providing other credibility and accreditation services that are drawn to the district's location at the heart of the PRD. The high ceilings can also cater for art studios and galleries.

d) A 1m sf car park with 10,000 spaces.

e) Six to eight mostly two to five-star hotels with a total of 3,000 rooms totaling 3m sf which can add around 5% to our inventory of hotel rooms.

The complex will be completed in two phases with the first section to open in 2016, in time for the operation of the Hong Kong-Zhuhai-Macau Bridge, and the second and final phase by 2020.

	Service Complex			**Car Park**	**Hotel**
	Destination Mall	Medical Service Centre	Office		
2012 **2013** **2014** **2015**	First Phase construction	First Phase construction	First Phase construction	First Phase construction	First Phase construction
2016	First Phase opening of 3m sf	First Phase opening of 0.5m sf	First Phase opening of 0.5m sf	Full opening of 1m sf	First Phase opening of 3m sf (4 to 5 hotels)
2017 **2018** **2019**	Second Phase construction	Second Phase construction	Second Phase construction	Second Phase construction	Second Phase construction
2020	Second Phase opening of 1m sf	Second Phase opening of 0.5m sf	Second Phase opening of 0.5m sf	To be determined	Second Phase opening of 1m sf (2 to 3 hotels)

- The financial parameters: If considered as a standalone and un-levered (ie all equity financed) project, the HK$22bn investment should produce a Net Present Value (NPV) of HK$41bn and achieve a full payback within six years of full operation from 2020. The latter compares with payback periods of 36+ and 40-50 years for the Hong Kong-Zhuhai-Macau Bridge and Guangzhou-Shenzhen-Hong Kong Express Rail Link, respectively.

In the project's first full-year's operation upon completion of the entire project, a net profit of some HK$2.9bn should arise, implying a 13% return on total investment of HK$22bn. This suggests that if the entire project is funded 60-70% by debt and the remainder by equity - a typical financing structure, the return to equity would be in the region of 40%.

- The absence of a hefty upfront cost for land has also greatly lessened the sensitivity of its time-adjusted cash value to the rate of discount. Hence, GTTW carries a very high IRR of 13.8%. In other words, the discount rate one has to adopt in order to nullify the project's NPV is 13.8%. This means that the lower one's cost of fund is, the higher will the project's NPV be. In comparison, the yield on US 10-year treasuries is around 2% and in our computation, we have adopted the discount rate of 4% as used by the government for the Guangzhou-Shenzhen-HK Express Rail Link and by the Airport Authority in its assessment of the third runway.

An Ungeared Internal Rate of Return of 13.8% is exceptional in the property world

To better appreciate the reasons for GTTW and Flying Dragon, four overlays are set out below to provide further context to the two projects:

1. The case for a showcase for Hong Kong's best service offerings
2. The geographical advantage of Hong Kong within the PRD
3. Tung Chung – a town that is stuck on drawing board for 30 years – It is high time Flying Dragon defied the gravity of bureaucracy and GTTW opened for business
4. MICE is very important to a World City – Hong Kong must re-double its efforts to re-establish its commanding lead in the region

1. The case for a showcase for Hong Kong's best service offerings

Huge demand exists for Hong Kong's services, especially from the mainland.

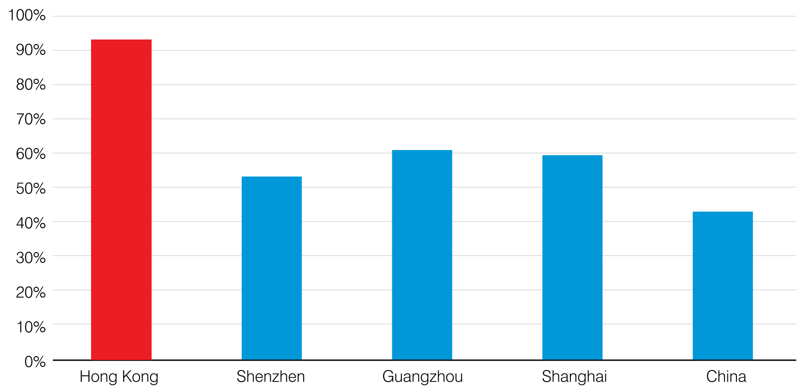
With services accounting for 93% of our GDP, Hong Kong is a centre of service excellence - this has been illustrated in our second report, “How to Become a World City: Lessons from London”.

Hong Kong’s immediate customer catchment of Guangdong Province is the most populous and richest region of China. However, it has a rather low service intensity and quality compared with Hong Kong. Less than an hour away from Central, Shenzhen, despite having the highest per-capita income in China (at RMB¥95,000 in 2010, some three times the national average), has a service sector that only accounts for 53% of its GDP. Around two hours away from Hong Kong by train, the provincial capital, Guangzhou, has a higher service intensity of 60%, similar to China’s commercial powerhouse, Shanghai.

Hong Kong is a centre of service excellence with this sector accounting for 93% of our GDP; the bigger this sector becomes, the more competitive and better quality it will be

Even though Shenzhen has the highest per-capita income in China, its service sector contributes only 53% to the city’s GDP

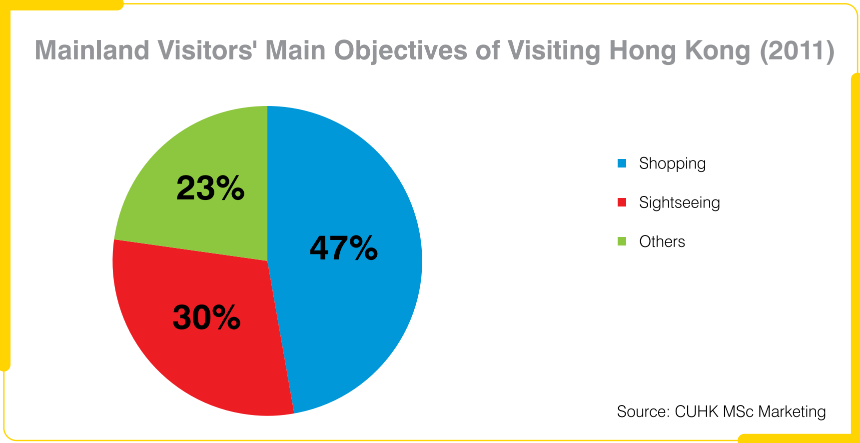
Service Sector Output as A Percentage of City GDP for 2009



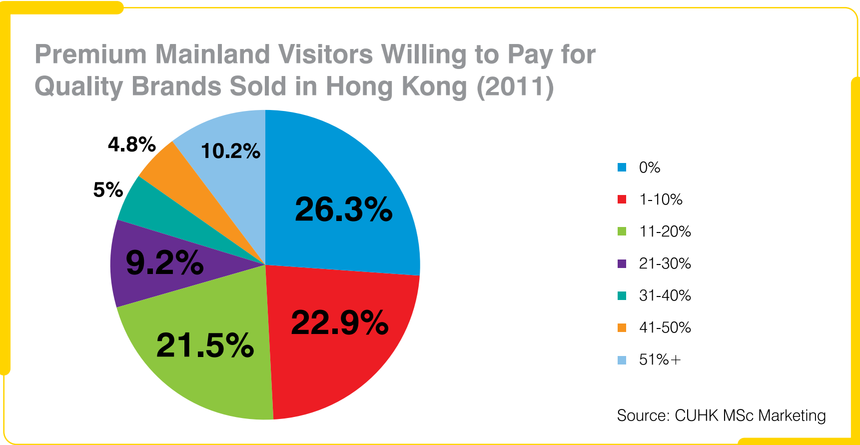
Source: HK Census & Stat. Dept., China Statistical Yearbook 2010, 2010 Guangdong Statistical Yearbook, Release from the Statistical Departments of Shanghai

Discrepancy in service intensity and quality has meant that many mainlanders will come to Hong Kong for the world-class services they would like to enjoy. In a survey conducted by the Chinese University of Hong Kong (CUHK) in the second-half of 2011, 47% of all the mainland respondents cited shopping as the main objective of coming to Hong Kong. What is most important is that some 74% of respondents would pay a premium for quality brands sold in Hong Kong compared with the same on offer in the mainland.

Discrepancy in service intensity and reliability has meant a lot of high-income mainlanders are happy to pay a rich premium to enjoy Hong Kong’s world-class services – survey suggests 30% of mainland visitors would pay >20% premium



Furthermore and reflecting their trust in Hong Kong quality, 30% of respondents indicated that they were willing to pay more than 20% premium for quality brands sold in Hong Kong compared with the same being offered in the mainland, 20% would pay over 30% premium and a staggering 10% willing to pay over 50% premium.



It stands to reason that if mainland customers are willing to pay a premium for impersonal products, they are even more willing to pay a premium for "credibility" goods and services that are likely to involve more valuable considerations eg. health and medical products, financial assets and academic qualifications etc. Take medical services, for instance, the Chinese Minister of Health, Mr Zhu Chen, in a conference in June 2011 in Hong Kong admitted widespread problems with mainland medical quality and practice. He further suggested the Chinese system should be improved through modelling on Hong Kong's. Media have also reported that more and more mainlanders are coming to private hospitals and clinics in Hong Kong in addition to their demand for maternity services. The number of non-maternity foreign patients admitted to Hong Kong hospitals, comprising of mostly mainlanders, has increased by 50% to some 20,000 patients from 2007 to 2011, a sharp increase compared to our local growth of 24% only over the course of four years.

Mainlanders trust our medical service - more and more mainlanders will come to private hospitals and clinics in Hong Kong for non-maternity services

Mainlanders are also keen to send their children to Hong Kong to study, from kindergarten to tertiary levels. For instance, university enrollment doubled from school year 2005/06 to 2010/11 and in 2011, all four Beijing students who achieved highest scores in the 2011 mainland university entrance examination chose to come to Hong Kong despite offers from prestigious mainland universities, including Peking University and Tsinghua University.

Mainlanders trust our education service - coming to Hong Kong not only for universities, but also primary schools and even kindergartens

Turning to kindergartens and primary schools, those located in North District have become favourites due to their proximity to the mainland. For instance, many kindergartens in Sheung Shui have achieved full admission a year before semester began and before the 2012 Hong Kong primary school central allocation, the Hong Kong Education Bureau had sent letters to eligible mainland children's parents urging them to send their children to places further away from North District in order to alleviate the admission pressure of the schools there. It has been estimated that over 10,000 students cross the border every day for school.

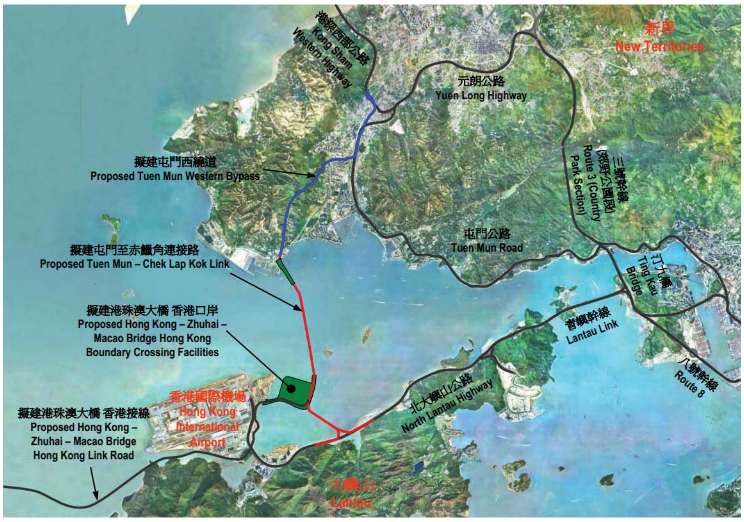
As the discussion above has outlined, it appears obvious that demand for Hong Kong services, from retail to education, medical, financial and other businesses where "credibility" matters, is strong and rising, as the mainland becomes more affluent and as the difficulties in coming to Hong Kong are lessened. A research conducted by the Hong Kong Tourism Board, Hong Kong Polytechnic University and Savills Research and Consultancy in 2010 projected tourist arrivals to grow at 14% per year in the next few years. In order to meet this rising trend, it makes sense to have our services lined up at the aerial and land gateways to the mainland and prevent excessive crowdedness and rental pressure in our existing facilities.

2. The rising geographical advantage of Hong Kong within Pearl River Delta (PRD)

The growth in demand for Hong Kong services can accelerate when the 70m+ population in the Greater PRD can more easily come to Hong Kong when new infrastructure comes on stream from 2016.

Work on the Hong Kong-end of the Hong Kong-Zhuhai-Macau Bridge commenced in December 2011 and the entire bridge shall be completed in 2016. Construction of the Tuen Mun-Chek Lap Kok Link has also commenced after detailed design and funding approval from the Legislative Council Financial Committee on 18th November, 2011, and it shall be complete in 2017. A further rail link to Tuen Mun is being considered and should facilitate flows to and from Shenzhen further.

Both the Hong Kong-Zhuhai-Macau Bridge and Tuen Mun-Chek Lap Kok Link will have been completed by 2017



According to 2010 Guangdong Statistical Yearbook, the PRD is home to 70m+ people. Once the 50km Hong Kong-Zhuhai-Macau Bridge is completed, the Hong Kong Airport and Tung Chung area will become vastly easier to access for the 30m population in the western banks of the PRD, reaching Tung Chung in some 40 minutes, representing a saving of almost four hours under the current road system. And when the 9km Tuen Mun-Chek Lap Kok Link is completed, the 40m population from Shenzhen, Dongguan, Huizhou and Guangzhou can also easily avoid the congested Luohu/Huanggang border crossings and access the Tung Chung area via the new facilities.

From 2016, the 70m+ population in the PRD can come to Tung Chung area far more easily than is currently the case eg. almost four hours saved on Zhuhai to Hong Kong trip

However, Hong Kong (and in particular Tung Chung) is vastly short of supply to cater for this exploding demand

Tung Chung, positioned at the centre of a web of new and existing infrastructure fanning out to the PRD, should benefit disproportionately from the region's growth in incomes and demand for services. Yet its offering, which comprises largely the Citygate Outlets, a shopping mall which offers mostly "outlet" type range of discounted branded goods and limited service range to residents in the district, is simply too small to meet the influx of retail and service demand. With only 0.4m sf in GFA, the Citygate Outlets has 78 shops, far fewer than other destination malls in Hong Kong such as the New Town Plaza (350+ shops) and Harbour City (700+ shops). Nevertheless, Citygate Outlets is popular with mainland visitors and local bargain hunters alike. It is busy with mainland shoppers even in non-holiday weekdays, and is full in the weekends.

Tung Chung should benefit most from future improvement in transportation, yet its present offering is too small to meet the influx of retail and service demand

Normally the outlets sell products from previous seasons, but some shops, because of robust sales, have to offer goods from the current season with little or no discount to satisfy demand. Cross border coaches travel from Huanggang, Shenzhen to Citygate Outlets from 8:30 a.m. till 10:15 p.m. with mostly half-hour frequency. Despite the direct bus service, travel time is still considerable. This goes to show that from this type of early success stories, the clear potential of Greater Tung Chung developing into a service-exporting centre, offering significantly more credibility services than mere retail and therefore creating more of a "destination" pull with consumers in PRD.

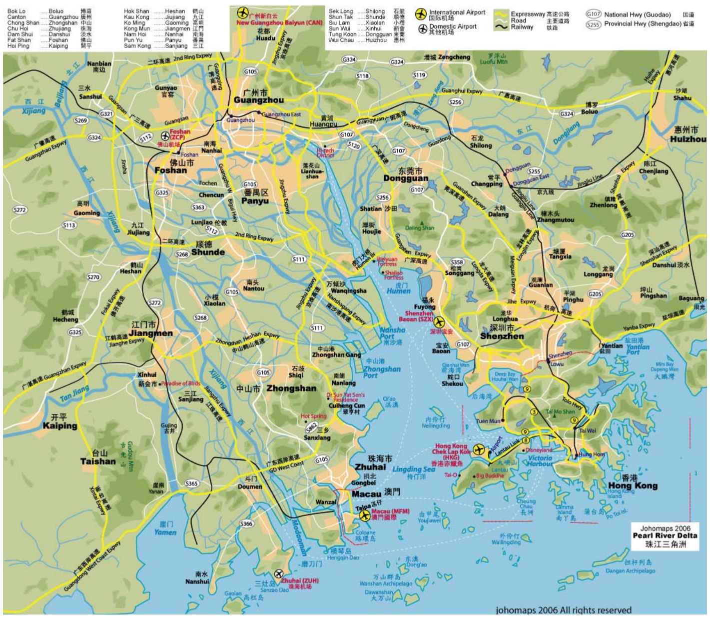
Shopping and F&B in Selected Major Shopping Malls in Hong Kong

	Shops	Restaurants	Total Area (m sf)
Harbour City	650	50	2
New Town Plaza	350+	50	1.5
Cityplaza	137	33	1.11
Pacific Place	115	18	1.1
MegaBox	108	37	1.1
Festival Walk	175	42	1
Elements	150+	70+	1
Times Square	230+	20	0.9
Citygate Outlets	78	15	0.5

Source: Harbour City, New Town Plaza, Cityplaza, Pacific Place, MegaBox, Festival Walk, Elements, Times Sqaure, Citygate Outlets

If Hong Kong does not seize on our "first mover" advantage to add capacity and capabilities to our service sector and to Tung Chung, competing Qianhai, Hengqin and the Shenzhen Bao'an International Airport, on the other end of major infrastructure links, will eventually rise and potentially eclipse Hong Kong. When the proposed Hong Kong-Shenzhen Western Express Line is eventually built, customers and opportunities could be drained away to the Qianhai Development Zone, which is now planning to be a financial and business centre, and the Shenzhen Bao'an International Airport, which is now developing its retail sectors. Moreover, competition does not come only from Shenzhen. We should bear in mind that within the narrow airspace in PRD there are more than five other airports; each of these airports is keen to extend its flight networks and retail sectors.

If Hong Kong does not seize on our "first mover" advantage to add capacity and capabilities to our service sector and in Tung Chung, competing Qianhai and the Shenzhen Bao'an International Airport will eventually rise and potentially eclipse Hong Kong



Despite the current situation, Tung Chung is set to fly high with improved transportation connections

As the PRD rapidly develops into the economic centre of Southern China, a golden opportunity lies ahead for Tung Chung, a small new town housing only 82,000. With the aid of new transport facilities including the Hong Kong-Zhuhai-Macau Bridge and Tuen Mun-Chek Lap Kok Link, Tung Chung will no longer be "out on a limb" of Hong Kong but becoming to be the centre of the PRD. If Greater Tung Chung manages to build up significant business mass, it is likely that more customers will fly in to use this service base from further afield in Asia and enable the Hong Kong Airport to surpass its passenger flows of 54m passenger in 2011.

With the aid of new transport facilities, Tung Chung will become Hong Kong's first and foremost gateway to receive the 70m tourists coming in from PRD

3. Tung Chung – a town that is stuck on drawing board for 30 years – It is high time Flying Dragon defied the gravity of bureaucracy and Gateway to the World opened for business

When one studies the history of Tung Chung's development, one would find that the present 82,000-population Tung Chung is not what the government envisioned for Lantau. The government used to have large-scale plan for Tung Chung, but somehow revised planning and reality fall well short of the original vision, resulting in persistent "under" population in Tung Chung which has created the social and economic problems we have discussed in earlier sections.

The present 82,000-population Tung Chung is less than a third of what the government envisioned some 30 years ago

The "Port and Airport Development Strategy" (PADS) in the late 1980s planned Tung Chung to be a supporting community for the airport, housing 260,000 residents after 2011. The subsequent "Comprehensive Feasibility Study for the Remaining Development in Tung Chung and Tai Ho" (CFS) in 1999 even scaled up Tung Chung as a part of the "North Lantau New Town" (Tung Chung and Tai Ho), which could accommodate 334,000 residents.

In 1999 the government planned Tung Chung as a part of the "North Lantau New Town", accommodating 334,000 residents

However, the "Revised Concept Plan for Lantau" in 2007, which is still in effect today, scaled down Tung Chung by a third to target only 220,000 residents, to reflect the low population level since the completion of Phase 3A in 1999.

The "Revised Concept Plan for Lantau" in 2007 revised down the scale of Tung Chung to accommodate only 220,000 residents

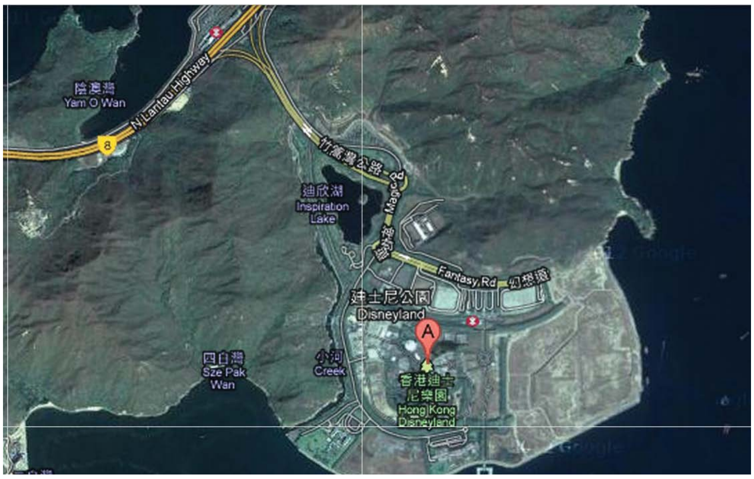
Distance to urban amenities and employment centres coupled with limited local job opportunities are the reasons behind Tung Chung's lack of popularity and there has yet been any noticeable effort to create in-town job opportunities by the government to bring the "new" town up to "critical mass". Moreover, hamstrung by the Hong Kong Planning Standards and Guidelines which prescribe users threshold to public facilities, the government made no noticeable effort to attract or retain citizens through providing basic civil facilities until 2010 - Tung Chung Municipal Services Building opened only in 2010, public swimming pool in 2011, and North Lantau Hospital in 2014.

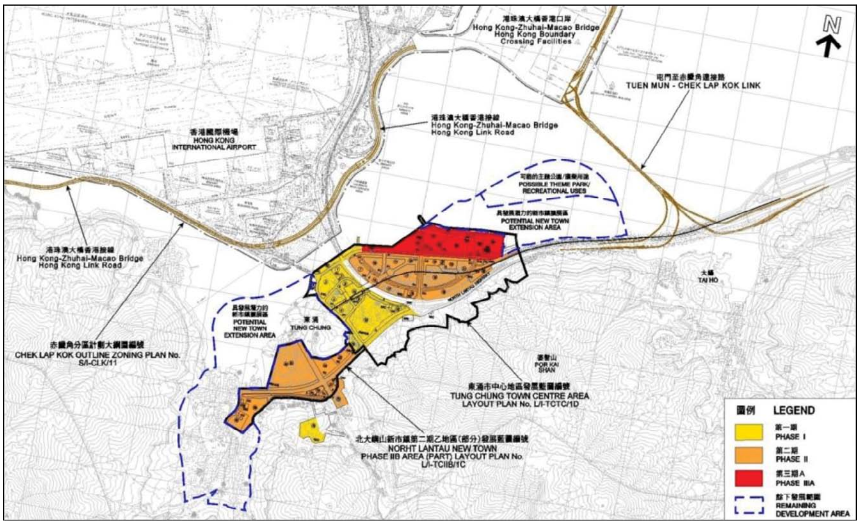
At the same time, the "Revised Concept Plan for Lantau" in 2007 initiated the project "Remaining Development in Tung Chung", investigating how Phases 3 and 4 of Tung Chung should be developed. Reclamation at Tung Chung East and Tung Chung West is one of the major areas being studied and the government's consultant, Arup, would finish the 30-month feasibility studies by 29th July, 2014, two years from now. As the district is not a greenfield site with no previous knowledge having been deposited, and existing and future infrastructure work (including additional highways to support the traffic to arrive from the Hong Kong-Zhuhai-Macau Bridge in 2016) would have created a wealth of relevant information, it really should not take 30 months to complete such a study. An important reference time frame is that it took only 2.5 years for the entire airport island to be reclaimed in open sea. We would argue that the length the government has prescribed for this study for Tung Chung reclamation is symptomatic of the "can always wait till another year / few years…" mentality with which the township has been dealt with or de-prioritised, without reflecting on the new dimensions that the HK$160bn+ new infrastructure and the environmental and economic opportunities will bring.

Reclamation studies on Tung Chung should not take 2.5 years – it is not a greenfield site and it must have been "raked over" by work done on other infrastructure projects. For comparison, it took only 2.5 years to reclaim the vast airport island. Such a "delay" is perhaps symptomatic of the "Tung Chung can always wait" mentality that has ignored the huge potential the HK$160bn new infrastructure and related economic linkages will bring

Since the vast majority of the northern Lantau is disturbed shoreline, we argue that a more comprehensive study be made to establish its full potential for development into the most environmentally friendly high density community in the world. In this new review, we should presume that the 40ha area allocated for possible theme park be dropped and deployed for community use. Some 300ha of land was created for Disneyland and only 22ha of that is built up theme park with another 102ha used for Inspiration Lake (30ha including surrounding grounds for leisure), parking and other facilities. There is scope for new theme parks in time but clearly these can be accommodated by tapping on the public infrastructure supporting Disneyland and new land should be formed as and when such need arises in the vicinity.

A comprehensive review should be commissioned to establish full potential of building the world's most environmentally friendly high-density community in North Lantau, completing in less than 12 months





To develop Tung Chung into a mostly-self-sufficient community reflective of the geographic-economic potential of its location at the heart of the PRD, we support reclamation significantly beyond the current plans for Tung Chung East and Tung Chung West. While the precise extent should result from the comprehensive study of Northern Lantau we discussed earlier, it is likely to encompass the areas north of existing trunk roads and railway line which represent already disturbed coastlines beyond Tai Ho and Siu Ho and the area between BCF and Tung Chung (chart above).

There is significant expanse of disturbed coastlines and areas of low wide life importance north and east of the existing reclamation districts being studied – these should provide significant potential for development

Turning to costing, recent reclamation benchmarks could be found from the Hong Kong-Zhuhai-Macau Bridge proceedings of 8th November, 2011 involving the Legislative Council Public Works Subcommittee of Finance Committee: reclamation of about 130ha for the artificial island (BCF) costs HK$244psf. The report also shows that the cost for reclaiming about 0.65m sf to the east of the Airport Island for the building of connecting roads to the Airport would cost HK$208psf. These suggest a range of HK$300-400psf would be sufficient for the reclamation at Tung Chung for the construction of Project Flying Dragon. Referencing the price of the most recent land sales of Tung Chung Town Lot 55B at HK$2,400psf in December 2011, reclamation costs should be easily recouped.

Reclamation and other development cost can be easily recouped by land sales

As the value-system of our people would demand that the World City of Hong Kong should have the most environmentally friendly high-density community in the world, we should not straightjacket the design of Flying Dragon into existing planning norms which are unlikely to satisfy our aspirations. Not only will the new township conform to the most rigorous environmentally-friendly building standards such as BEAM Plus and PNAP 152, its infrastructure design will also emphasise sustainability. Electric-based road-transport will be the norm serving its residential and commercial areas and water-cooling systems will reduce the use of electricity in air-conditioning. Central treatment of food waste and other best practice will also be adopted.

Environmentally-friendly measures will define Flying Dragon and demonstrate to the world that Hong Kong is not a concrete jungle which pays scant respect for the environment. It will be highly attractive to global talents and locals alike – combining high growth commercial district with a green and friendly neighbourhood which epitomises a value system that respects the environment and the individual. This concept was well implemented in a large-scale environmental project in Seoul a decade ago.

In designing the layout of the buildings, wind-tunnel simulations should be carried out to ensure the area's strong air flows are fully exploited so as to minimise the need for air-conditioning and maximise the field-of-view. While high rise will allow more open space and the tall hills fringing the new town can provide a to-scale backdrop to tall buildings, the average plot ratio of the district is unlikely to exceed six to seven.

In designing the most environmentally friendly high-density community in the world, we must not be encumbered by existing planning norms which will not be demanding enough to meet our people's aspirations for sustainability and a human-friendly neighbourhood

Just as the bulk of the development of Tung Chung never got off the drawing board, the majority of the commercial and logistic spaces embedded in the airport design have also been mired in seeming neglect and indifference by both the government and its wholly-owned Airport Authority. For instance, the North Commercial District (NCD) of the airport consists of some 22m sf of GFA designated roughly equally to commercial and logistic uses. This space was approved by the Town Planning Board 13 years ago.

The North Commercial District of the airport, with 22m sf GFA, is the largest ready-to-use land supply of Hong Kong – the territory-wide acute shortage of commercial space and future potential of the district must summon its immediate deployment

Land premium and Environmental Impact Assessment (EIA) had been exempted and all planning and construction permissions had been granted already without much restriction. Moreover, the Airport Authority could apply to the government to swap designated GFA within different commercial usage and from logistic/freight forwarding to commercial use, at no or minimal costs in both cases. The latter happened a few years ago when freight forwarding space was swapped to commercial use to support the building of AsiaWorld-Expo convention centre. The only real planning limit is, quite naturally, height restriction of 40-50m or around 7-8-levels. As discussed in this and previous reports, Hong Kong suffers from an acute shortage of retail/hotel/office/medical/parking space. This has translated into rapid escalation of rents which have not only undermined Hong Kong's competitiveness but also spilled over to drive general inflation. The urgency to keep this problem under control and the realization of the economic and social potential of this district warrant the immediate deployment of this fortuitous land reserve. Our proposal to build 11m sf Gateway to the World assumes the application of half of this land bank.

Gateway to the World will only tap half of this fortuitous landbank

The NCD currently consists of the SkyCity Nine Eagles Golf Course outside Terminal 2 building and a temporary car park adjacent to the golf course. The lease of both the golf course and car park shall expire in July 2013 and the land should be released for GTTW. Planning and preparation for tenders should commence immediately so that the project can be launched quickly and in time for the completion of the Hong Kong-Zhuhai-Macau Bridge in 2016.

This land reserve is currently a golf course and a temporary car park. The lease of both shall expire in July 2013. Hong Kong cannot afford anymore "waste of space" - planning and tendering for GTTW should commence immediately

This land reserve was originally designated as a potential airport city, termed "SkyCity", in the Hong Kong International Airport Master Plan 2020 published in 2001. More details were added in the Master Plan 2025 published in 2006. Despite this clearly spelt out earlier intention, in the assessment of the economic benefits in favour of building the third runway conducted a few months ago under "Master Plan 2030", there was no mention of the colossal employment and income potential the development of the commercial space would bring. In particular, we have argued in earlier sections that this huge commercial project can provide the "content" to justify overseas customers flying to Hong Kong and adds to the usage of our airport and supports the need for another runway. We have also estimated that GTTW should fetch a net present value of HK$41bn which can already cover almost half the cost of building the third runway which carries a negative present value of HK$86bn.

The once "SkyCity" has done a David Copperfield? HK$41bn and lots of externalities are not opportunities that Hong Kong can allow to vanish

Furthermore, the construction of GTTW will not hinder the construction of the third runway under “Master Plan 2030”. The planning of the third runway stipulates an underground automated people mover (APM) depot to accommodate maintenance, storage and other future needs at the NCD and 6,500 car parking spaces for airport users due to new capacity brought about by the third runway. Since the former is underground and the latter will not come out of the existing 11m sf GFA, both are consistent with the building of GTTW.

4. MICE is very important to a World City—Hong Kong must re-double its efforts to re-establish its commanding lead in the region

Meeting, incentives, conferencing and exhibition (MICE for short) are very important building blocks of a World City. These events bring visitors from overseas who will experience, first hand, the fun, culture and values of a place and increase the emotional and economic connections of the city with the rest of the world through these events. Many will return, bringing along their friends, family, business associates, as customers, tourists, investors and future citizens of the World City. A World City has a welcoming culture to visitors and Hong Kong should exude this openness and vibrancy of the city by hosting more events. The annual Rugby Sevens epitomizes how the spirit of our city connects deeply with the world through an event.

World City welcomes visitors and connects with them though MICE and events

Convention and exhibition are two major components of the MICE industry in Hong Kong. In 2011 Hong Kong ranks third (after China and Japan) in Asia exhibition market share, higher than Singapore and Macau. However, there are signs that Singapore and Macau are overtaking Hong Kong in hosting conventions: the former through the active promotion and incentives provided by the Singapore Exhibition and Convention Bureau and the latter due to the attraction offered by its casinos and relative facilities.

In 2011 Hong Kong ranks third (after China and Japan) in Asia exhibition market share; however, there are signs of Singapore and Macau overtaking Hong Kong in organising conventions

Singapore is very proactive in expanding the capabilities of its MICE industry and positioning itself as an Asian hub for business conventions and exhibitions. Three new exhibition centres, two of which are part of integrated resorts with large shopping and entertainment facilities, have been constructed within just five years. This has contributed to the rapid growth of business visitor arrivals in Singapore, which has increased 131% from 2001 and overtook Hong Kong in 2010.

Number of Business Visitors (including MICE)

Source: HK Tourism Board, Singapore Tourism Board

By 2011, Singapore has topped Asia's conventions for nine years, according to the International Congress and Convention Association.

Key advantages of Hong Kong as an exhibition venue are our airport, our city brand, and our city as a two-way springboard between China and the rest of the world

There are two main convention and exhibition venues in Hong Kong, namely the Hong Kong Convention and Exhibition Centre (HKCEC) and the AsiaWorld-Expo (AWE), currently having saleable exhibition space of 950,000 sf and 750,000 sf respectively. The three main exhibitions held in Hong Kong are electronics, gifts and jewellery - all are light industries. The advantages of Hong Kong as a venue for these events as cited by exhibitors and visitors include our airport (thus many buyers fly in from overseas), the brand of our city infers quality and the perception that our city is a two-way springboard between China and the rest of the world which is in part due to visa-free access granted by Hong Kong to the majority of countries. Mainlanders especially value and make good use of this connectivity advantage. For instance, in AWE, over 70% of all non-local exhibitors and 34% of all international visitors come from the mainland in 2010 and 2011.

The main organiser of exhibitions in Hong Kong is the Hong Kong Trade Development Council (HKTDC) which commanded around 45% of total market in 2008 and 2009. In contrast, the private sector is much smaller, with some 30 organisers like Global Sources etc sharing out what is left of the market, according to CUHK and BMT Asia Pacific's "Hong Kong Trade Exhibition - An Industry Review" in October 2009 and November 2011. Although there are no accurate published figures from 2010 onwards, The Concern Group for a Competitive Exhibition Industry has stated the market share level of HKTDC was retained in 2010 and 2011.

The Hong Kong Trade Development Council (HKTDC) commands 45% of total exhibition market in 2008 and 2009; the private sector is much smaller in size, with about 30 organisers sharing what remains of the market

Market share concentration in the public sector has led to two problems. First, it causes lack of variety of exhibition offerings as HKTDC does not need to venture beyond the "three main exhibitions" even though it is not entirely sure if all three light industries can remain crowd pullers in the long run. Private organisers are not in a position to enter and compete with the behemoth. For instance, Reed Exhibitions, a global leader in the industry and which organizes 500 events a year, only managed to do one or two in Hong Kong but nine to ten in Singapore. Second, HKTDC exhibitions have been concentrated in HKCEC and do not take advantage of the synergies and capacity which HKCEC and AWE together can create. This has led to public impression of exhibition space shortage at HKCEC while AWE has remained under-used. For instance, HKTDC held more than 90% of its exhibition events at HKCEC until 2010 (86% in 2011) even when AWE had become available.

Market share concentration on the public sector leads to lack of variety of exhibition offerings and upsets the intended synergy effect of HKCEC and AWE

Both HKCEC and AWE were initiated and funded by the government. The original intention of building AWE, as expressed by the Stephen Ip, then Secretary for Economic Development and Labour, in 2003, was to foster the MICE industry in Hong Kong such that both exhibition centres should develop in parallel. The first objective was fulfilled early on: the exhibition market in Hong Kong increased by around 50% in the first year after AWE commenced operations on 21st December, 2005. Though in absolute terms AWE has fallen well behind HKCEC even though given the 22-year history of HKCEC, it should have a more matured business profile and more limited potential for growth compared with the very young and modern AWE.

The original intention of building AWE was to foster the MICE industry in Hong Kong such that both exhibition venues will develop in parallel

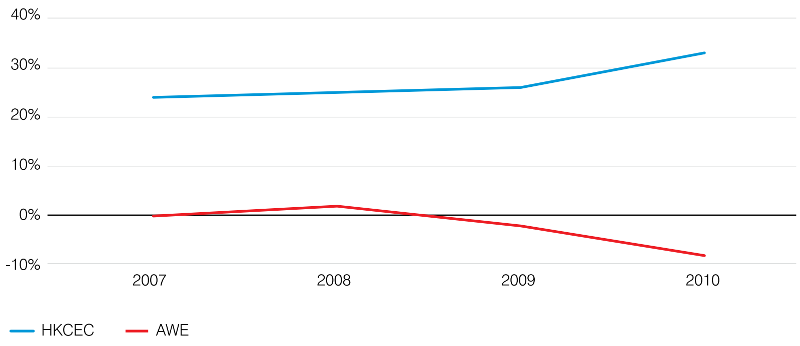
For the second objective, though the market share of AWE in Hong Kong international exhibition improved to 30% from 2005 to 2011, its growth was reversed in 2009 in the wake of the government-funded HKCEC Atrium Link Extension Project. The project added 210,000 sf (42%) of space to HKCEC. According to AWE Management Limited's "Written Submission to the Legislative Council (Panel on Commerce and Industry)" in April 2010, whereas the annual rented area (measuring how much area is cumulatively rented to conventions and exhibitions in one year) of AWE decreases by 8% from 2007 to 2010, that of HKCEC increases by 109%. The two events point to unproductive competition between HKCEC and AWE which are both government assets.

AWE's growth was reversed in 2009 following the opening of the HKCEC Atrium Link Extension Project, pointing to unproductive competition between the two government-owned venues. The two venues should be put under one management in future so that capacities and opportunities are optimized, to the benefit of Hong Kong

To optimize on the use of our exhibition resources and to encourage innovation, the management of the two venues should be merged and staff should be remunerated, amongst other KPI's, according to Hong Kong's (private and public sector) gain in the share in the region's exhibition market. The TDC, after all, has a mission to promote Hong Kong as whole, and not its market share therein.

There is clear scope for the two public sector players to work, as a corporate body, to optimize not only their combined business and utilize all the synergies in their facilities, but also the market share (including private operators) of Hong Kong in the regional market

Yoy Growth of Rented Area of Hong Kong Convention Centre (HKCEC) and AsiaWorld-Expo (AWE) (2007-2010)



Source: AsiaWorld-Expo Management Limited

The skewing of usage in favour of HKCEC has created impression of shortage in HKCEC exhibition space. This has fuelled recent discussions of building a HKCEC Phase III (already suggested in the 2008 Policy Address) by taking over the sites of the Wan Chai pier bus terminus and Wan Chai Sports Ground. As the HKCEC sits in the middle of a fully developed and busy commercial district with all its facilities and roadways further overladen with the arrival of the new government offices in 2011, any new exhibition capacity will only worsen the over-crowdedness. Since the law forbids reclamation of the Victoria Harbour, no new hotels, offices, shops and roads can be built to support the added facilities. A much more practical solution will be the upgrading of the support infrastructure at GTTW and create a top quality and fully supported exhibition capability at the gateway of Hong Kong. This can lessen the further over-burdening of already "overcrowded" facilities in the urban locations.

Such negative internal competition between the two venues creates public impression of HKCEC exhibition space shortage, in turn fueling recent discussions of HKCEC Phase III expansion

The question whether HKCEC needs to be expanded remains ambiguous. Although we could cite examples of HKCEC not having enough exhibition space, for instance, from 2008 onwards the annual Kenfair's Mega Show has to be divided into two phases because of space limitation of HKCEC, and some exhibitors of the 2011 Hong Kong International Art Fair needing to rent space for exhibitions in offices in Central, only for 26 days in 2008 and 15 days in 2009 did HKCEC managed to have 100% utilization, according to the CUHK and BMT Asia Pacific's reviews. For more recent data that are available publicly, 100% utilization happened in 22 days in October 2010.

HKCEC seemed to be able to achieve 100% utilization for less than a month each year from 2008 to 2010

"One Fair, Two Venues" could satisfy the supposed exhibition space shortage problem in HKCEC in the short term. The world's largest jewellery fair since 2009, The Hong Kong Jewellery and Gem Fair, became the world's largest fair of this nature since 2009. International visitors' and exhibitors' demand is greater than any one of the exhibition centre could provide by itself, and the deployment of both venues have been successful in meeting such demand since 2009. In 2011, a record 3,454 exhibitors from 46 countries attracted some 45,000 buyers from 135 countries and regions. All booths were sold out, and the fair expanded to occupy 1,400,000 sf of exhibition space.

"One Fair, Two Venues" is a half-way house to full rationalization of the public and private operators. Recent large scale fairs are successful examples

B. Operating Details and Financial Modelling

The world-class quality and world-topping-sized commercial complex Gateway to the World City (of Hong Kong), or GTTW, comprises GFA of 11m sf for the following uses:

Composition of GTTW

		First-phase GFA (m sf) completing 2016	Later-phase GFA (m sf)	GFA (m sf)
Service Complex	Destination Mall	3	1	4
	Medical Service Centre	0.5	0.5	1
	Office	0.5	0.5	1
Car Park		1	0	1
Hotels		3	1	4
GTTW (Total)		**8**	**3**	**11**

a) A 4m sf destination mall with 600+ shops and restaurants

The outlet format is a win-win for retailers, shoppers, airport usage, visitors, jobs and more

The 3m sf first-phase of the retail portion of GTTW will complete in 2016 and add around 3% to Hong Kong's total retail space – not a significant increase compared with the c.50% and c.90% surge in retail dollars over the past two and five years, respectively. Most of this new space will be in "outlet mall" format ie significantly larger shops compared with those in urban areas and which include a large storage area for ex-season stock gathered from the many outlets of a chain or a branded store all across the territory or even from across Asia. A typical shop will occupy 4,000 to 6,000sf as opposed to the 1,000 to 2,000sf stores that are typical of the usual mall in Hong Kong.

To the retailer, this low-rent (average rent at opening is HK$20psf), large-space but off-urban location enables it to centralize all the goods and lines that have gone ex-season in high-rent urban shops (for instance, estimated rents for Times Square are no less than HK$112psf and for Harbour City are around HK$153psf) for sale in one location so that all the bargain-minded shoppers can have wide choice and convenience otherwise not easily arranged in a one-stop-shop format. This also allows the retailer to put to the much more expensively-rented urban shops the new season's full-price offerings quickly after the lapsing of the old season, enabling a more profitable use of high-cost spaces.

To the shoppers, the scale and diversity of offerings of GTTW will make it a destination (ie. worth a special trip just to use the facilities at this location) on first opening. The wide choice and the convenience of being able to buy so many things and enjoy so many services (eg. convention, medical, education, entertainment, hotels etc in the non-mall portions of GTTW also) at one stop will make it the best offering in Greater China, if not Asia. The minimum customer catchment is the 70m population in the PRD who will arrive by land transport and a wider customer base from beyond Guangdong Province, by air.

With a first-phase 3m, GTTW mall compares with the world's biggest destination malls such as the 2.8m sf Mall of America and 3.8m sf West Edmonton Mall and will be the largest mall in Hong Kong, topping the current leader Harbour City which stands at 2m sf with 700+ shops and restaurants.

The first-phase retail space will be rented at an average of HK$20psf, which compares with the going rate of HK$30psf+ at Citygate Outlets near the airport. To ensure diversity and an interesting mix which are good for drawing in crowds, higher rents will be set for better-margin brands while lower rents could be set for galleries and studios etc.

Providing ability to cater for further demand and a change of mix, some 1m sf is reserved for the second phase.

b) A 1m sf medical service centre with 400+ beds

The medical service centre provides full-fledged, world-class medical services from acute and major surgeries to medical checkups. It is comparable to the scale of Union Hospital (390 beds) in Shatin. There are many options as to the running of this facility and it can cater for medical tourism and can have components to enable the training of doctors etc. Visitors and relatives to patients who are hospitalized can be conveniently accommodated in GTTW hotels.

To cater for the likelihood of a significant pick up in demand once potential customers realize that such services have become available, some 0.5m sf is reserved for the second phase.

c) A 1m sf office for accrediting, supporting, NGO and other "credibility" services

Office space in GTTW houses offices for shops in the destination mall, education centres, accrediting services, NGO's and other "flow" and "credibility" related businesses. Some 0.5m sf is reserved for further expansion.

a) to c) form GTTW's "Service Complex"

d) A 1m sf car park with 10,000 parking spaces

The car park caters for GTTW users which can include visitors from the Hong Kong-Zhuhai-Macau Bridge. Ideally this type of "holding" facility should be housed in the BCF and run by the government, leaving the valuable space in GTTW entirely for the performance of services as opposed to "storage". As yet the design of BCF is not available so we shall assume GTTW will have to take up the provision of "transit" point for arrivals at Hong Kong by land. From this entrance point, visitors can: (1) enjoy the best services and retail facilities Hong Kong can offer, "at the gate" of Hong Kong – noting again that a survey of mainland visitors showed that 47% of respondents indicated the main objective of coming to Hong Kong was "shopping" and if this primary purpose is met "at the gate", there is no need for further travel into the city where there is no or negligent hardware capacity left; (2) "park and ride" to urban locations or "park and fly" to other global locations.

Almost all Hong Kong services can be provided to our customers "at the gate" – possibly a world first and makes our city the most convenient service centre in the world

First phase of the car park will have 10,000 spaces, roughly five times the quanity at Harbour City. We expect this figure to be exceeded quickly as the vehicular population in Southern China is huge. For instance, in Guangzhou one out of 13 persons had a car in 2008, and in Shenzhen the figure was one out of every six persons in 2010. It is likely that the land-route will bring in a lot of customers for "health and nutritional necessities" eg. formula powder, who can load up a car or "bulk buy" for themselves or relatives. Further holding capacity should be provided by the government in BCF which has a land area of 130 ha, almost the size of seven Victoria Parks.

Some 47% of mainland visitors have indicated that their primary purpose for coming to Hong Kong is shopping – this could be satisfied "at the gate" and this can alleviate the "overcrowding" of our urban facilities, rent rise and inflation

e) Six to eight two- to five-star hotels with a total of 3,000 rooms

The 3m sf 3,000-roomed full price-range offerings will cater for visitors that encompass concert- and performance-goers at AWE who want to a no-frills hotel for overnight stay to full-price business and holiday people who come for meetings and tourist facilities in southern China. Together, these new hotels will add around 5% to territory-wide capacity and help alleviate the acute shortage of accommodation. The context being that while visitor number went up over 40% in the past two years, rooms only increased by 6%.

Each hotel will have 400-600 rooms, with around half of them in the format in terms of scale and quality comparable to the Regal Airport Hotel (which has won a number of prizes) and the nearby Novotel Citygate Hotel. Unlike standalone hotels in city centre, hotels in GTTW do not need to reserve large space for convention facilities since AWE is just next door. The natural synergy is clearly observed with the Grand Hyatt Hong Kong and the Renaissance Harbour View Hotel linking up with the Hong Kong Convention and Exhibition Centre Complex.

Another 1m sf is reserved for future expansion or for alternative use.

Mode of operation

We would advise that the government allocate HK$22bn to the Airport Authority to fund the construction of the GTTW, payable in phases. The Airport Authority shall own the entire GTTW and be responsible for maintaining the entire infrastructure. Service and consultancy contracts could be tendered out to best-in-class operators at reasonable costs who will help run the components of GTTW.

Estimated construction timeframe

First Phase: Four years

Second Phase: Three years

Estimated investment

HK$22bn (two-stage: first phase: HK$ 14.1bn, second phase: HK$7.6bn)

Estimated payback period

Six years (after full opening in 2020)

Net present value

HK$41.1bn

(Timeframe: 30 years, 2012-2041; nominal discount rate: 4%)

Internal rate of return

13.8%

(Timeframe: 30 years, 2012-2041)

Financial model

1. Construction costs

Estimated GTTW Construction Costs

		Benchmark Unit Cost (HK$psf)*	Unit Cost in Our Estimation (HK$psf)	Phase 1 GFA (m sf)	Later phases GFA (m sf)	Total Cost for Phase 1 (HK$ bn)*	Total Cost for Later phases (HK$ bn)*
Service Complex	Destination Mall	1,625	1,600	3	1	5.2	2.2
	Medical Service Centre	2,600	2,600	0.5	0.5	1.4	1.8
	Office	1,625	1,600	0.5	0.5	0.9	1.1
Car Park		575-650	600	1	0	0.6	0
Hotels		2,100	1,900	3	1	6.0	2.5
GTTW (Total)				**8**	**3**	**14.1**	**7.6**

*Based on Quarterly Construction Cost Review Third Quarter 2011, Davis Langdon & Seah, except Medical Service Centre which used Union Hospital first phase,

2. Operating costs

Estimated GTTW Annual Operating Costs

	Benchmark (% of revenue)	Our Estimate (% of revenue)
Service Complex	Langham Place (2011): 21.1	20
Car Park	The Link (2011): 41.5	30
Hotel	Regal Hotels (2011): 51.5	35

Operating costs tend to fall with increasing scale of operation

3. Revenues

Estimated GTTW Annual Revenues

	Benchmark Unit Revenue (HK$psf)	Benchmark Occupancy Rate (%)	Estimated Unit Revenue to GTTW (HK$psf)	Estimated Occupancy Rate (%)
Service Complex	Citygate Outlets: $30+	Citygate Outlets: 99.4	$20	95
Car Park	Citygate (2012): $12 AsiaWorld-Expo (2012): $16 Hong Kong International Airport Terminal 1 (2012): $20 Terminal 2 (2012): $16 Terminal 4 (2012): $20	Rumsey Street (2009): 47 City Hall (2009): 23 Murray Road (2009): 47 Star Ferry (2009): 62 Middle Road (2009): 50 The Link (2011): 75	$9	40
Hotels	Regal Hotels (2010): $774 (Average Daily Rate)	Regal Hotels (2010): 85.8 Regal Hotels (2009): 74.2	$875-1,000 (Average Daily Rate)	70

*Benchmark and estimated unit revenue for car park in HK$ph

4. Timeline

	Service Complex			Car Park	Hotel
	Destination Mall	Medical Service Centre	Office		
2012 2013 2014 2015	First Phase construction	First Phase construction	First Phase construction	First Phase construction	First Phase construction
2016	First Phase opening of 3m sf	First Phase opening of 0.5m sf	First Phase opening of 0.5m sf	Full opening of 1m sf	First Phase opening of 3m sf
2017 2018 2019	Second Phase construction	Second Phase construction	Second Phase construction	Second Phase construction	Second Phase construction
2020	Second Phase opening of 1m sf	Second Phase opening of 0.5m sf	Second Phase opening of 0.5m sf		Second Phase opening of 1m sf

5. Assumptions

1. Nominal Discount Rate = 4%

Benchmarks: 4% (Guangzhou-Shenzhen-HK Express Rail Link)

5.3% (HK-Zhuhai-Macau Bridge)

6.1% (West Kowloon Cultural District)

2. Inflation = 5% (2012-2014), 3% (2015-2042)

Benchmarks: (HK Census & Stat. Dept.) 5% (2011)

3% (2008-2011)

2% (2004-2011)

3. Annual Escalations of Costs: 5%

4. Capital Expenditure Phasing

Capital Expenditure Phasing

	First Phase Construction	Second Phase Construction
Service Complex	2-2-3-3	3-3-4
Car Park	3-3-4	5-5
Hotel	3-3-4	5-5

Capital expenditure is phased. The phasing 2-2-2-3 of the Service Complex means that 20% of total capital expenditure of the whole project will be spent in each of the first and second years while 30% will be spent in each of the third and final years etc.

5. Financial Model Timeframe: 30 years (2012-2041)

6. Estimated Rent Growth (Yoy)

Estimated Rent Growth (Yoy)

	Benchmark Rent Growth (Yoy)	Estimated Rent Growth (Yoy)
Service Complex	6% (Savills Research & Consultancy, 1997-2011) 15% (Savills Research & Consultancy, 2004-2011)	6% (since opening)
Car Park	The Link (2007-2011): 4%	5%
Hotel	Regal Hotels: (2009-2010): 1.5% (2008-2009): -16.1% (2007-2008): 4.8% (2006-2007): 13.6%	6%

7. Practicality Assumptions

Practicality Assumptions

Service Complex	Lettable area = 70%
Hotel	Revenue distribution (Regal Hotels, 2011): 60% (room), 40% (dining, conference and others)

2.2 Invest HK$10bn in a 2m sf "Sub-Culture" underground mall in the West Kowloon Cultural District to (1) enhance TST's retail quantum and range of experience as a global shoppers' paradise and (2) generate recurrent income to support the development of arts and culture in Hong Kong

The theme of Hong Kong "bursting at the seams" in the Golden 5 Years cannot be clearer than when one stands in the middle of Tsimshatsui (TST), a global shoppers' paradise with its main streets reportedly grossing more sales than London's Oxford Street/Tottenham Court Road and New York's Fifth Avenue. With no new space in the pipeline, ever-rising rents and ticket prices, packed shops, overflowing pavements and jammed streets will conspire to chase customers away from Hong Kong.

Hong Kong is bursting at the seams with tourists and shoppers

We need to extend our edge as a shopping destination by adding capacity and capabilities to our city's favourite retail district without delay, or else the extra patronage from the opening of the Express Rail Link in 2015 which will put 30m+ population from the affluent Guangdong cities of Guangzhou, Dongguan and Shenzhen within 48 minutes' reach of the TST terminus, together with the "trend" growth of visitor arrivals, will crowd out the joys of shopping and eating in the World City of Hong Kong. We support Dr. Cheung Kwok Pun's concept of subterranean space in our district and propose adding square footage and service offerings in TST with a 2m sf underground mall, provisionally named "Sub-Culture". Sub-Culture's 1m sf first phase should open in 2017, its 0.5m sf second phase in 2019 and its 0.5m sf final phase in 2021.

To preserve and add to Hong Kong's reputation as shoppers' paradise, we must add square footage and service offerings in TST – a 2m sf underground mall, provisionally named "Sub-Culture" can be a highly useful solution

Providing real and powerful support to the development of art and culture enjoyment in Hong Kong, Sub-Culture should produce net profit of some HK$1bn in its first full year of complete operation. This income amounts to 35% of the spending on arts and culture by the Home Affairs Bureau in 2011/12.

Annual net profit from Sub-Culture can add some 35% to spending on arts and culture

A. What are we investing in?

- A 2m sf art-infused and culture-themed mall with 600+ shops and eateries under the West Kowloon Cultural District (WKCD) which we have provisionally named, "Sub-Culture".
- The financial parameters: If considered as a standalone and un-levered (ie all equity financed) project, the HK$10bn investment should produce a Net Present Value (NPV) of HK$11bn and achieve a full payback within eight years of full opening. The latter compares with payback periods of 36+ and 40-50 years for the Hong Kong-Zhuhai-Macau Bridge and Guangzhou-Shenzhen-Hong Kong Express Rail Link, respectively.

Sub-Culture will produce Net Present Value north of HK$11bn and a full payback within eight years of full opening

- In the project's first full-year's operation upon completion of the entire project, a net profit of some HK$1bn should arise, implying a 10% return on total investment of HK$10bn. To better appreciate why the financial attributes of Sub-Culture are so favourable, it is worth remembering that the cost of land normally accounts for 70-80% of the total development cost of a property project in Hong Kong. As the government already owns the land the main investment it needs making is the construction cost of around HK$4,000psf.

An Ungeared Internal Rate of Return of 11% is exceptional in the property world

- The absence of a hefty upfront cost for land has also greatly lessened the sensitivity of its time-adjusted cash value to the rate of discount. Hence, Sub-Culture carries a very high Internal Rate of Return (IRR) of 11%. In other words, the discount rate one has to adopt in order to nullify the project's NPV is 11%. This means that the lower one's cost of fund, the higher will the project's NPV. As comparison, the yield on US 10-year treasuries is around 2% and in our computation, we have adopted the discount rate of 4% as adopted by the government for the Guangzhou-Shenzhen-HK Express Rail Link which will situate next to Sub-Culture.

Art/Culture with Food/Goodies may pair like good food and wine

- The externalities: While there is no "magic formula" that guarantees success of any new undertaking, with 8m sf of space for performance and art appreciation above ground in WKCD, the 2m sf of retail area that lies below it does not appear excessive, especially when Hong Kong can easily absorb the additional capacity with the rising number of customers to our services. Just as Broadway in New York City is supported by shops and restaurants within walking distance, the pairing of the heart/vision/hearing Vs mind with stomach/eye/tactile experience of shopping may yet prove to be as enjoyable as good food and wine.

- Also, it should not take much to realize the possibility that what starts out as a shopping expedition for many in Sub-Culture may lead to a lifetime love affair with the arts when shoppers experiment with attending an exhibition or a performance above ground in WKCD.

A lifetime love affair with the arts may start with a handbag or an iPad

- The ownership structure: While making little or no difference to operations, the financing and ownership of Sub-Culture can be put under the government's Home Affairs Bureau or the West Kowloon Cultural District Authority (WKCDA). Legislation to set aside the funding is needed to be approved by the Legislative Council in either of the cases. There are pros and cons as to the level of private sector participation in the scheme but this decision can be delayed till the project is completed. Given the significant surpluses in our public coffers and the low returns they tend to generate, an investment in Sub-Culture should offer superior risk-adjusted returns.

Government should start the ball rolling immediately…

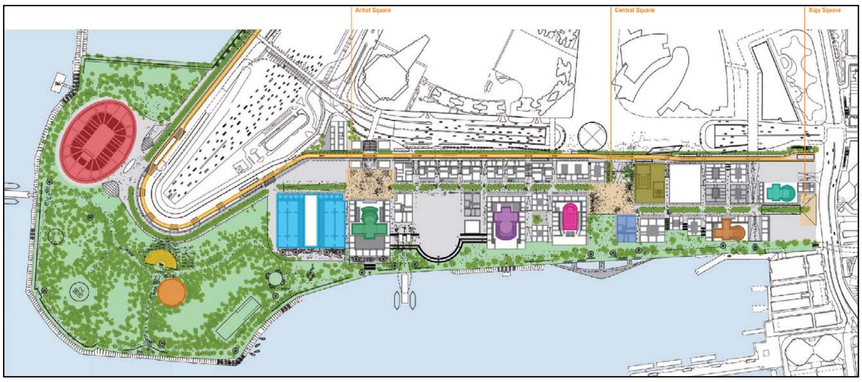
- The operational arrangement: There is no shortage of capable designers, builders and operators of great shopping centres around the world that can bring Sub-Culture to fruition. Through an open and fair process of competition and tenders, the right mix of expertise can be brought together speedily.

B. Why should we invest in Sub-Culture?

We believe there are two major reasons supporting the proposal of investing in Sub-Culture:

1. **Reinforce TST's prominent position as a shoppers' paradise and capitalise on the traffic brought by the HK$62bn Guangzhou-Shenzhen-Hong Kong Express Rail Link which should open in 2015.** (for a more detailed discussion please read on)

2. **Improve the quality and range of services offered by the HK$22bn WKCD by attracting more traffic and providing complementary enjoyment to patrons of art and performances.** Generate recurrent income to support the provision of arts and cultural activities. (for a more detailed discussion please read on)



1. Reinforce TST's prominent position as a shoppers' paradise and capitalise on the traffic brought by the HK$62bn Guangzhou-Shenzhen-Hong Kong Express Rail Link

As we have discussed earlier in section 2, Hong Kong is suffering from acute shortage of retail space, resulting in displacement of traditional retail offerings and soaring rentals which translate to general inflation.

Hong Kong's excellent service quality is highly appealing to tourists, yet the city is heavily constrained in retail space and this is especially true in urban areas. Canton Road, for instance, contributes 10% of Hong Kong total retail sales but only accounts for 2-3% of Hong Kong total shop spaces.

For instance, Canton Road contributes 10% of Hong Kong total retail sales but only accounts for 2-3% of total shop spaces

To safeguard the competitiveness of Hong Kong's flagship shopping district, we need to bulk up the spaces devoted to both tourists and local shopping needs and widen the range of service experience available. In the past few years, many retail offerings that support day-to-day needs of Hong Kong citizens (for instance, traditional restaurants, fast food shops and pharmacies) have been displaced by watch and jewellery and fashion outlets, many of which now dominate Canton Road and half of Queen's Road, Central. According to the Rating and Valuation Department, average high-street retail rentals of Mong Kok, Tsim Sha Tsui and Causeway Bay increased 20-30% in 2010 and 30%+ in 2011.

The lack of new retail space in urban areas has led to surging rentals that have priced out shops that cater for daily living: Rents rose 20-30% in 2010 and 30%+ in 2011

Once the Express Rail Link is completed, an additional 50,000 traffic will arrive per day in the TST area, potentially adding significantly to demand for shopping facilities

Once the Express Rail Link comes into operation in late 2015, 30m+ population of from the affluent Guangdong cities of Guangzhou, Dongguan and Shenzhen will only be a mere 48-minute train ride away from Hong Kong, a shorter travel time than the ferry ride from Hong Kong to Macau. In fact, the MTR Corporation forecasts that by the first full year of operation, in 2016, 99,000 passengers will travel between Hong Kong and mainland (both ways) by the Express Rail every day, i.e. around 50,000 passengers arrive at Hong Kong every day.

By 2016, around 50,000 passengers will arrive at Hong Kong by the Express Rail Link every day; It may take less time to travel to Hong Kong from Guangzhou than the ferry ride from Hong Kong to Macau

With Express Rail Link bringing some 50,000 arrivals every day, this traffic will add a significant burden to the foot traffic passing through the major malls in the TST area today: 150,000 at Harbour City and 100,000 at The Elements. In the next four years and before the Express Rail Link is opened, it is expected that arrivals at TST will grow at a compound rate of 10-15% a year, adding 50-80% to current flows. Let us not forget that the 50,000 Express Rail Link daily arrivals has not included the traffic drawn by WKCD, which could number 11,000 visitors per day according to the economic assessment conducted by the Financial Secretary's Office in 2007. These traffic numbers serve as a high-level indication that an additional mall in the TST area is justified. If nothing is started today, there may be a need to pedestrianise Canton Road within a few years.

In the next four years and before the Express Rail Link is opened, arrivals at TST may add 50-80% to current flows

2. Improve the quality and range of services offered by the HK$22bn WKCD by attracting more traffic and providing complementary enjoyment to patrons of art and performances

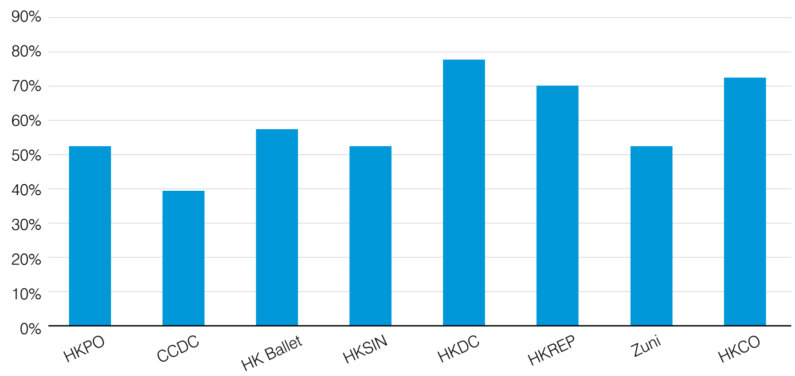
WKCD, at least in its early stages of operation, can rely on other facilities such as retail to help drive traffic

WKCD is the first large-scale art and cultural complex Hong Kong has ever planned and built, a right step for Hong Kong aspiring to be the next World City after London and New York.

An inconvenient truth is that most local arts and culture groups are not financially self-sustainable. Taking the example of the most heavily-subsidised "Big Nine" performing art groups (namely the Hong Kong Chinese Orchestra (HKCO), the Hong Kong Dance Company (HKDC), the Hong Kong Repertory Theatre (HKREP), the Hong Kong Philharmonic Orchestra (HKPO), the Hong Kong Sinfonietta (HKSIN), the Hong Kong Ballet (HK Ballet), City Contemporary Dance Company (CCDC), Chung Ying Theatre Company and Zuni Icosahedron (Zuni)), ticket sales can only generate an average of <40% to cover their operating expenses. One cause for the low profitability is Hong Kong people's lack of demonstrated interest in cultural activities. For instance, while 63% of Londoners and 33% of Singaporeans have seen a performance in the past 12 months, only 21% of Hong Kong citizens have done so. Therefore, other attractions, including retail, are helpful in generating traffic.

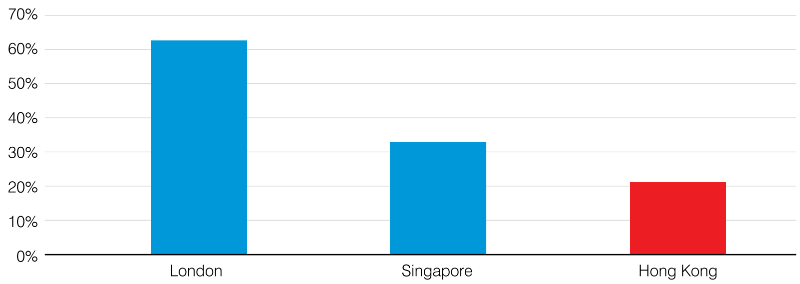
In Hong Kong, arts and cultural facilities unfortunately cannot attract enough patrons to sustain themselves financially and should require other attractions to help drive traffic

Government Grants as Percentage of Total Revenue



Source: Annual reports of HKPO, CCDC, HK Ballet, HKDIN, HKDC, HKREP, Zuni & HKCO

Percentage of local residents who have participated in at least 1 performing arts event in past 12 months



Source: London Cultural Audit 2008, DCMS UK, Singapore National Council of Arts, Leisure and Cultural Services

In fact, more and more cultural facilities around the world have started to co-locate with commercial offerings such as retail to drive patronage. A famous example is the Mori Art Museum, a contemporary art museum on the 53rd floor of the 54-level high Mori Tower in the Roppongi Hills area in Tokyo, Japan. The museum, despite having no permanent exhibitions of international acclaim, still attracts 1.5m traffic per year (the 24th most popular art museum in the world according to the Art Newspaper) - mostly leveraging the traffic to the sky-deck observatory and the 0.48m sf shopping mall at the Roppongi Hills.

More and more cultural facilities around the world have started to co-locate with mass offerings such as retail to drive patronage eg. Mori Art Museum in Roppongi Hills, Tokyo

The operational surplus from the extra mall can help finance capital shortage and subsidise more arts and cultural activities

As construction costs have risen 60% since the approval of the HK$21.6bn endowment to WKCDA in 2008, it is widely reported that the authority is in short of cash to finance the construction of all its originally planned arts and cultural facilities. The government should take advantage of the effort in assessing Sub-Culture to bring all costings of WKCD up to date and allow for extra costs in connecting the two facilities. With inflation not expected to abate anytime soon, the biggest disservice to Hong Kong is to procrastinate while costs escalate and art and tourist opportunities evaporate.

The biggest disservice to Hong Kong is to procrastinate while costs escalate and art and tourist opportunities evaporate

From WKCDA's latest Development Plan, it seems that the authority is planning to seek public-private partnership opportunities to help fund the construction and operation of certain facilities such as the Mega Performance Venue, yet whether this arrangement is commercially viable remains uncertain. However, Hong Kong people have already waited for 13 years since these facilities were promised back in 1998 and WKCD remains a barren piece of land. Therefore, we believe a possible way for WKCDA to overcome its financial burden is to obtain extra funding to complete its facilities as soon as possible and the government can rely on future incomes it derives from Sub-Culture to make good possible future shortfalls in WKCDA.

By obtaining extra funding to build Sub-Culture, WKCDA can fund its capital shortage and loss-generating cultural facilities by the HK$1bn annual income from Sub-Culture

Proposal

We propose building a 2m sf 600+-shop underground mall, Sub-Culture, in WKCD to cater for visitors and residents in TST as well as potential traffic brought by the Express Rail Link. The mall is comparable in size and number of shops as Harbour City (2m sf, 700+ shops), compared with the nearby The Elements which houses 220 shops in 1m sf of space. It should be noted that when The Elements opened for business, it added 1m sf or 50%, to the mall supply of Harbour City in a soft market and the subsequent prospering of both has illustrated the significant size of demand for shop space in the district, even before there was suggestion that a HK$62bn Express Link with Guangzhou would land in the middle of this market. Sub-Culture should provide, in addition to range of goods and services offered by shopping centres, spaces for galleries, auction houses and other art and design-related businesses. Unlike the arrival of The Elements, Sub-Culture's first phase of 1m sf in 2017 will only add 33% to the combined spaces of The Elements and Harbour City and in market conditions that will likely exceed the current ebullience as it opens one year after the opening of the Express Link. The addition of the two tranches of 0.5m sf of spaces will open with a two-year gap with the earlier phase, providing the flexibility to put right any problems with footfall and design before more capacity is introduced.

Mode of operation

The government or a public body should start the project and only consider its longer term future after running the completed projects for a few years. The subject property is a shopping centre and this requires top professional advice which does not come likely arise from public consultation.

Estimated construction timeframe

9 years

Estimated investment

HK$10bn

Estimated payback period

8 years (after full opening in 2021)

Net present value

HK$11.1bn

(Timeframe: 30 years, 2012-2041; nominal discount rate: 4%)

Internal rate of return

10.9%

(Timeframe: 30 years, 2012-2041)

Financial model

1. Construction costs

Estimated Sub-Culture Construction Costs

Benchmark Unit Cost (HK$ psf)*	Unit Cost in Our Estimation (HK$ psf)	GFA (m sf)	Total Cost (HK$ bn)
1,625+	4,000	2	10

*Taken from Quarterly Construction Cost Review Third Quarter 2011, Davis Langdon & Seah

2. Operating costs

Benchmark (% of revenue)	Our Estimate (% of revenue)
Langham Place (2011): 21.1	25

3. Revenues

Estimated Sub-Culture Annual Revenues

Benchmark Unit Revenue (HK$psf)	Benchmark Occupancy Rate (%)	Unit Revenue in Our Estimation (HK$psf)	Occupancy Rate in Our Estimation (%)
Habour City (2011): 130	Habour City (2010): 96	50	95

*Taken from Quarterly Construction Cost Review Third Quarter 2011, Davis Langdon & Seah

4. Timeline

2012	First Phase construction	
2013		
2014		
2015		
2016		
2017	Second Phase construction	First Phase opening of 1m sf
2018		
2019	Third Phase construction	Second Phase opening of 0.5m sf
2020		
2021		Third Phase opening of 0.5m sf

5. Assumptions

1. Nominal Discount Rate = 4%

   Benchmarks: 4% (Guangzhou-Shenzhen-HK Express Rail Link)

   5.3% (HK-Zhuhai-Macau Bridge)

   6.1% (WKCD)

2. Inflation = 5% (2012-2014), 3% (2015-2032)

   Benchmarks: (HK Census & Stat. Dept.) 5% (2011)

   3% (2008-2011)

   2% (2004-2011)

3. Escalations of costs: 5%
4. Capital Expenditure Phasing: 2-1-1-1-1-1-1-1-1
5. Financial Model Timeframe: 30 years (2012-2041)
6. Estimated Rent Growth (Yoy)

Estimated Rent Growth

Benchmark Rent Growth (Yoy)	Estimated Rent Growth (Yoy)
6% (Savills Research & Consultancy, 1997-2011) **15% (Savills Research & Consultancy, 2004-2011)**	6% (since opening)

7. Practicality Assumptions: Lettable area = 70%

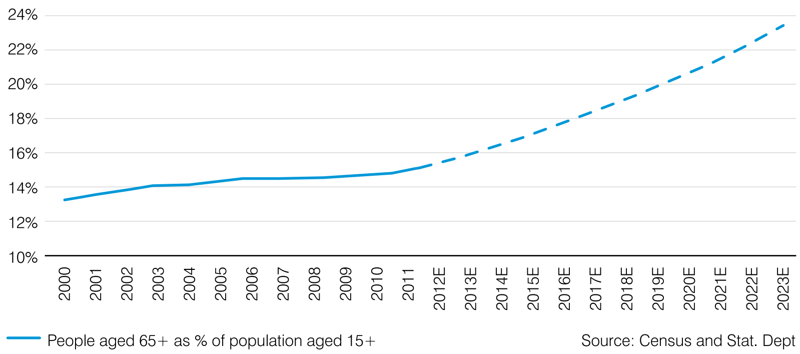
3: Invest to Improve in our Service Capacity and Capabilities – Build World-class Software

The provision of world-class services not only requires hardware (hotels, shops, offices, hospitals, schools etc.) but also software (professionals, salespersons, teachers, doctors etc.). In addition to sufficient commercial spaces, Hong Kong also needs a high quality workforce to ensure the city can maintain the quality of services that it provides.

Unfortunately, shortage of labour as a result of ageing population and a prolonged period of low birth rates will likely curb Hong Kong's potential to sustain growth.

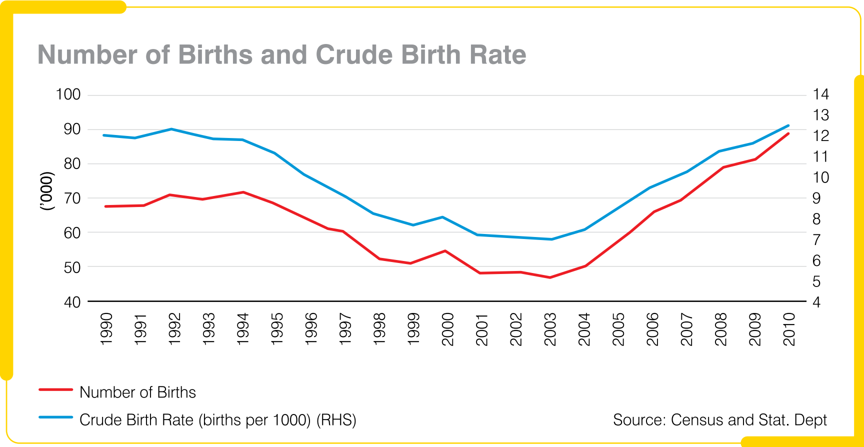
Ageing population and low birth rates contribute to a shrinking labour force

Proportion of Elderly People

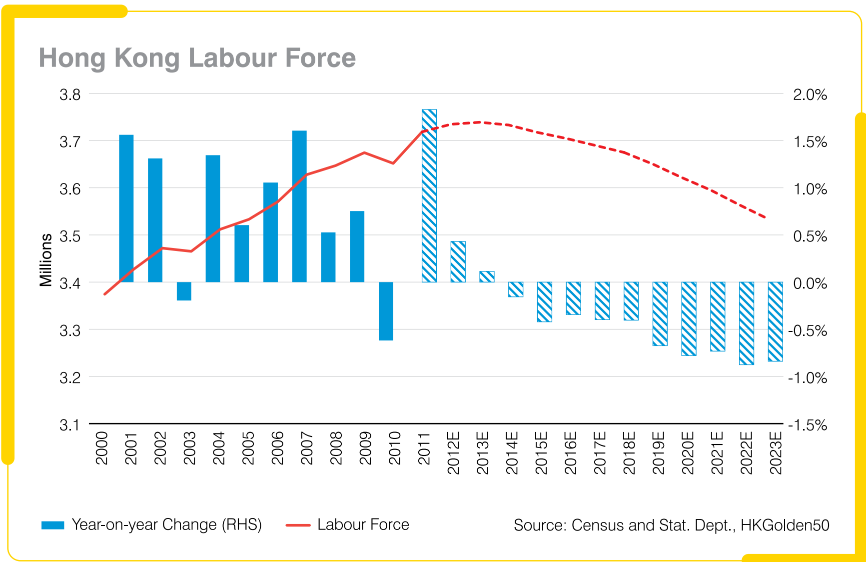


Source: Census and Stat. Dept

As at 2010, elderly people (aged 65+) accounts for 15% of the population aged 15+. This proportion is projected to increase rapidly starting 2013 and by 2023, almost one-quarter of our population aged 15+ will be at least 65 years old.

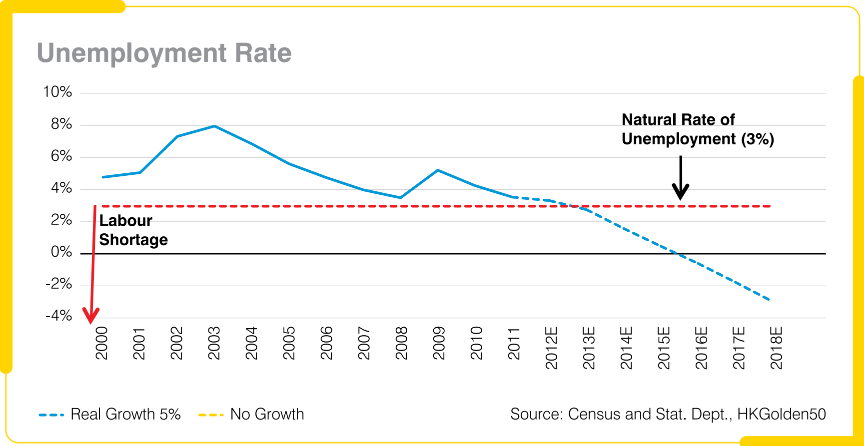


On top of our ageing population, birth rates in Hong Kong have been falling since the mid-1990s and have rebounded from the trough only after 2003. This phenomenon implies that the picking up of number of births will not be reflected in the labour force until mid-2020s. This period of low birth rates, together with the sharp increase in retirement-age population, in turn transforms into a shrinking labour force that we are going to witness next year.



Our labour force has grown by c.10%, gaining more than 300,000 workers in a decade, and is going to peak at 2013, reaching 3.74m. From then on it shall start to plummet at a rate of 0.4% to 0.8% (or 20,000 to 40,000 workers) per annum and in ten years' time, Hong Kong's labour force will contract by 6%, withdrawing more than two-thirds of the increase in number of workers in the last decade.

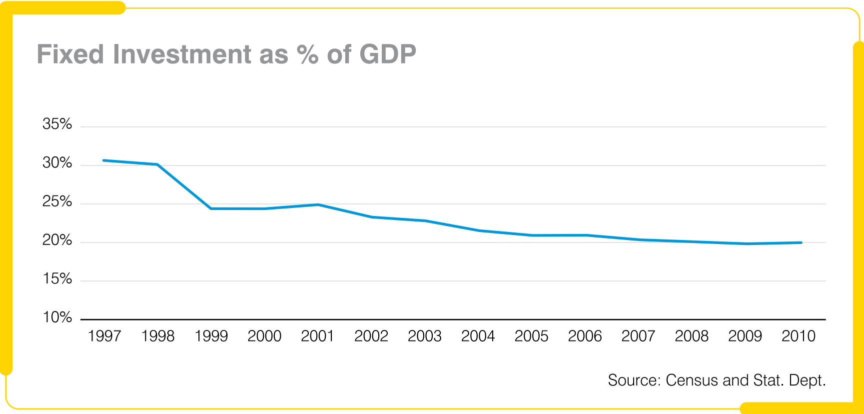
More than 200,000 workers will be withdrawn from our labour force in the coming decade as baby boomers retire



Given the shrinking pool of labour, a 5% increase in labour productivity p.a. is needed if our economy keeps growing

Hong Kong has nearly reached full employment with the unemployment rate staying at 3.3%, the lowest level in the past decade. We expect this trend to continue as the influx of business opportunities and service demand of all sorts derive even higher demand for labour.

Given that our labour force is declining by an average 0.6% per annum, if demand for our services expands at a rate of 5-6% so that GDP grows at 5% a year, then by 2014, the end of the Golden 5 Years, tightness of the labour market will be comparable to that in 1997 when unemployment rate was 2.2%. We estimate that it requires an average 6% increase in productivity per annum in order to maintain our servicing capacity.



A 6% productivity gain per annum is virtually impossible, given the low level of fixed investment in Hong Kong

However, even for advanced economies like the United States can only sustain a long term productivity growth of 2% per annum with an abundance of technological innovation and research and development. It is almost impossible for Hong Kong to gain 6% productivity a year, especially when fixed investment as % of GDP has been falling from 30% in 1997 to just 20% in 2010. Therefore, it is imperative for the government to invest heavily in education and training to improve the overall quality of our workforce.

3.1: Invest $6bn to Freshen Hong Kong's Air & keep our World City Refreshing & Clean for Better Quality of Life

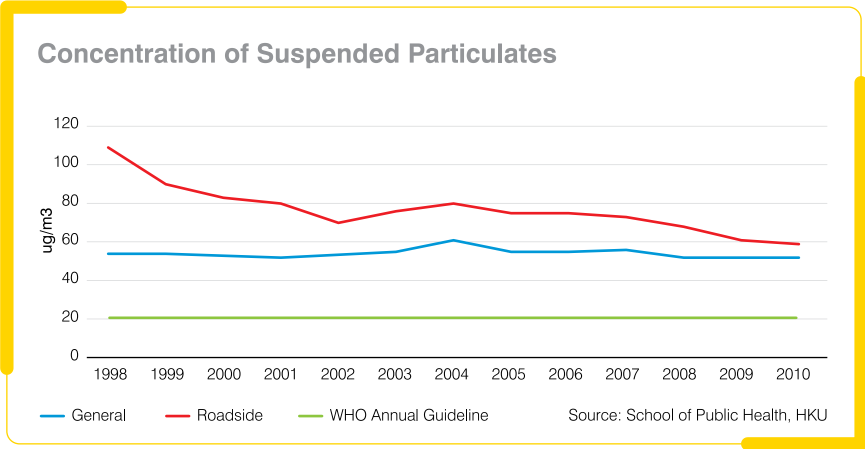
A. What are we investing in?

Invest HK$6bn to replace old polluting buses, the source of our pollution and health problems, by incentifying bus companies and updating our metrics completely in line with World Health Organization (WHO) in three years' time

B. Why should we invest in improving or air quality?

Bad air quality can shatter our dream of becoming a World City. According to the revised (Jan 2011) Hedley Environmental Index compiled by the School of Public Health of HKU, over the last five years Hong Kong has incurred an average HK$8bn of tangible economic loss and more than 600 premature deaths per year due to air pollution

Poor air quality is hindering Hong Kong from becoming a World City



The effort paid by the government in improving air quality is clearly insufficient. Although there has been a decreasing trend in a number of pollutants like nitrogen dioxide (NO_2) and respirable suspended particulates (RSP) over the past years, the roadside emission of NO_2 and RSP still exceed the WHO guideline by 195%.

Our Air Quality Objectives (AQO), despite the recent revision (Jan 2011) in the last two decades, still lag far behind the WHO standards. For example, our new emission target of sulphur dioxide (SO_2) (125 mg/m^3) is still 5x higher than what is suggested in the WHO guidelines (20 mg/m^3). Updating our AQO so that our metrics are completely in line with WHO standards is the first step to effectively freshen our air.

Hong Kong's metrics, though revised, are still not in line with WHO standards

Concentration of PM2.5 Suspended Particulates Among Various Cities

Ranking	City	Annual Mean Concentration (ug/m3)
92	Sydney	7.0
447	New York	12.7
461	London	13.5
520	Singapore	19
541	Paris	22.9
559	Hong Kong	36.0

Note: Data for China and Taiwan not available
Source: Friends of the Earth, WHO

The poor air quality in Hong Kong is also driving foreign enterprises and expatriates away. In August 2006, a study carried out by the American Chamber of Commerce indicates that 79% of respondents knew of professionals who have thought of leaving or have already left Hong Kong due to air pollution. A more recent survey conducted by Regus indicates that 75% of corporate leaders believe air quality is hindering Hong Kong's ability to attract and retain talents.

Foreign professionals find it difficult to settle in a place where they choke every day

Sources of Pollutants

Pollutant Source Categories (2007)	NOx	RSP	CO	SO2
Road Transport	22%	30%	82%	1%
Public Electricity Generation	46%	28%	5%	89%
Navigation	16%	7%	3%	5%
Civil Aviation	6%	0.4%	3%	0.5%
Other Fuel Combustion	11%	21%	7%	5%
Non-combustion	NA	13%	NA	NA
Total	100%	100%	100%	100%

Source: HKEPD

Figures from the Hong Kong Environmental Protection Department (HKEPD) show that road transport is the most important source of RSP and carbon monoxide, and the second most important source of nitrogen oxides. By vehicle types, franchised buses account for 40% of the total roadside emission despite that they only represent 5% of the total number of diesel commercial vehicles. It is therefore of paramount importance to reduce the emission from public buses in order to effectively improve the air quality of Hong Kong.

Road transport, or public buses in particular, is the major source of air pollutants

Composition of Buses by European Emission Standards

	Hong Kong		Singapore	
	# of Buses	Expected Year of Retirement	# of Buses	Replacement Deadline
Pre-Euro	456	2012	0	
Euro I	1338	2015	2700	2011
Euro II	2688	2019	586	
Euro III	1233	2026	207	
Euro IV	53		506	
Euro V			357	
Total	5768		4353	

Source: Civic Exchange

Compared to Singapore, Hong Kong lags behind in upgrading franchised buses. As at 2009, almost 80% of Hong Kong's public buses are of Euro II standards or below, while Singapore has already upgraded its Euro I public buses to Euro V. Also, only 0.9% of public buses are equipped with engines that meet Euro IV standards, while in Singapore, 20% of public buses have met standards of Euro IV or above.

Hong Kong has a much laggard bus fleet than Singapore

Emission Standards of Diesel Vehicles (g/KWh)

	Nitrogen Oxides	Particulate Matters
Euro I	8.0	0.36
Euro II	7.0	0.25
Euro III	5.0	0.10
Euro IV	3.5	0.02
Euro V	2.0	0.02

Source: Civic Exchange

A comparison of buses of different generations shows that upgrading public buses can drastically reduce emission of pollutants. For example, by upgrading from Euro II to Euro IV, emission of nitrogen oxides and particulate matters are cut down by 50% and 92% respectively.

	Capital Expenditure HK$ bn	Return
Incentivize franchised bus companies to replace all Euro I and II public buses to Euro IV standards	6	➢ Avoid 200 premature deaths per year ➢ Avoid tangible economic loss of HK$2bn per year

We propose the government to set aside HK$6bn as to incentify franchised bus companies to replace all Euro I and II public buses to Euro IV or higher standards once and for all.

Set aside HK$6bn to incentify franchised bus companies to replace old buses

While the exact amount of subsidies and the details mechanism (e.g. linking the amount of subsidies with the net book value of the replaced buses) should be subject to further public discussion, we believe earmarking HK$6bn (which could cover up to 60% of the total cost of replacement) is sufficient to provide enough incentives for franchised bus companies to replace their buses under the current profit control scheme in which profits of bus companies are based on average fixed assets value.

In fact, providing subsidies with a view to improving air quality is not unprecedented. For example, the Hong Kong government has been providing subsidies (a total subsidies of HK$4bn has been provided to date) to encourage replacement of old diesel commercial vehicles. From an international perspective, Seoul, for example, has provided subsidies of HK$1bn (25% of cost) to bus operators to replace diesel buses to compressed natural gas (CNG) buses.

With reference to the model developed by the School of Public Health of HKU, our conservative estimate is that by replacing these old buses we can reduce roadside emission of NO_2 and PM10 by 25%, and thus avoiding 200 air-pollution-related premature deaths, and tangible economic loss of HK$2bn per year.

200 premature deaths and HK$2bn tangible economic loss could be avoided by replacing old buses

Ultimately Hong Kong should possess a zero-emission public bus fleet as the technology gets more mature and prevalent. Therefore, the government needs to implement the pilot scheme for introducing zero-emission electric buses much more actively by scaling up the scheme as well as investing into the related logistics such as a large-scale installation of charging points. Looking ahead, the government can also include emission targets of bus fleet as one of the considerations upon renewal of public bus franchises.

It's time for action – at a greater scale, with a greater urgency

3.2: Invest HK$3bn in Training & Boosting Productivity of our Workers to ensure we Improve the Quality of our Services & Increase our Global Competitiveness despite the Rapid Shrinkage of our Workforce

A. What are we investing in?

Invest HK$3bn to increase the capacity of the current retraining programmes by the Vocational Training Council and the Employees Retraining Bureau to accommodate 40,000 more trainees per year in two years' time

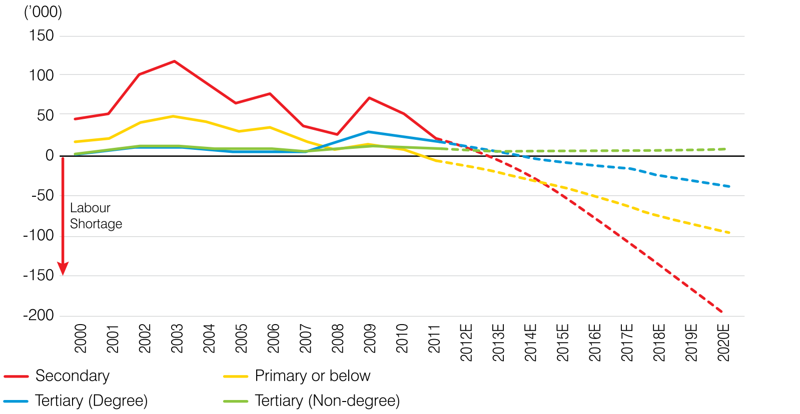
B. Why should we invest in expanding retraining facilities?

We need to urgently increase productivity of our workers so that service quality can be maintained in spite of a shrinking workforce

We need heads, and more so for workers with lower education (secondary or below)

While it is generally perceived that as Hong Kong is a developed knowledge-based economy and thus the severity of labour shortage should increase with level of education, we find that the opposite seems to be more likely: labour without tertiary education will be relatively scarcer than their higher-educated counterparts.

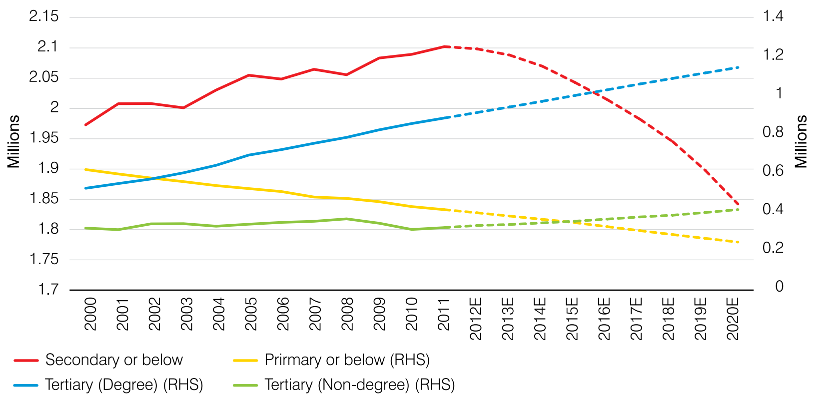
Labour Shortage by Educational Level



Source: Census and Stat. Dept., HK Universities Grants Committee, HKGolden50

Our simulation shows that (after allowing for the natural level of unemployment) by 2014, Hong Kong will be lacking workers in almost every level of education, with the sharpest shortage in workers without tertiary education (red and yellow lines in chart), with the deficiency up to 70,000, roughly 3% shortfall in labour in this category, while the corresponding figure for degree holders or above (blue line) shall be around 3,000.

Labour Supply by Educational Level



Source: Census and Stat. Dept., HKUGC, HKGolden50

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Our current education system does not produce workers with sub-secondary qualification

This is not difficult to understand: The 6-Year and 9-Year Compulsory Education were introduced in 1971 and 1978 respectively, rendering all new workers since 2000 to have at least completed junior secondary studies before joining the labour force. With the compulsory free education now extended to 12 years, our present education system basically does not produce any workers with qualifications lower than secondary school diploma. Also, the significant expansion of tertiary education since the early 1990s has led to a higher proportion of school leavers with tertiary qualifications before joining the labour force. Consequently, the imminent waves of retirement of baby boomers shall represent massive withdrawals of workers with sub-tertiary qualification.

Demand for these workers remains robust, leading to an acute shortage

Demand for these workers, on the contrary, is expected to grow with the economy, spurred by opportunities entering Hong Kong during the Golden 5 Years. Hot spots in the job market should include shop assistants, waiters and tour guides. Oftentimes these are positions that do not require a high level of formal education, leading to the expected sharp shortage in workers with lower education.

	Capital expenditure to increase training capacity HK$bn	Operating cost to train 40,000 extra workers per year HK$bn	Return per year (Income loss avoided by having more productive staff working for 10 years) HK$bn
Increase the current retraining capacity by 20%	3	1.2	1.8 (18)

To counter the effect of the looming labour shortage, we call a 20% increase in capacity of the current retraining programmes, mainly offered by the Vocational Training Council (VTC) and the Employees Retraining Bureau (ERB). Re-training programmes of this nature (lasting six to nine months) are effective in raising labour productivity. We expect that HK$3bn is required to expand and upgrade the current facilities to accommodate a total of 40,000 more trainees each year and an extra operating cost of HK$1.2bn will be needed every year. This is small cost when compared with the income loss of HK$18bn that can be avoided by having properly trained, productive staff working for ten years.

Long-series academic studies in Europe have reported that for every 1% increase in workers receiving training, labour productivity can be increased by 0.4%, with minor limitations. Taking a "deprival" approach to calculate the potential loss of earned income as businesses fail to fill vacancies, we have roughly computed that without such an expansion in retraining programmes, Hong Kong will lose HK$1.8bn per year, or a total of HK$18bn over a course of ten years.

Quarterly Business Receipt Indices (YoY change) on Selected Service Sectors

Service Sector	2011 Q1	2011 Q2	2011 Q3
Retail	21%	28.1%	27.5%
Accommodation	23.3%	20.8%	22%
Tourism and Exhibition	16.9%	23.6%	24.5%

Source: Census and Stat. Dept.

Our economy is undergoing another major "restructuring": "One country, one market" has led to boom in "credibility businesses", e.g. retail, restaurants, tourism, MICE and other personal services including beauty care and medical services. On the other hand, some large sectors like import/export may be stagnant or even declining. The retraining programmes should therefore focus on the aforementioned booming industries where labour is most needed. The government should continuously review the development of different sectors and accordingly tailor retraining facilities to equip our workforce with skills that the economy needs.

3.3: Adopt an Accretive Population Policy to attract Global Talents & the Well-to-do & improve Capabilities, Connectivity & Diversity of this World City

A. What are we implementing?

- Embark on a talent and connection accretive population policy that attracts some 200,000 talented individuals of all sectors who can prosper from Hong Kong's global service platform and bring connectivity, jobs, and business opportunities over the next 10 to 15 years
- Loosen the Permanent Residency (PR) requirement: shorten the minimum period of stay from seven years to two years for selected applicants—many countries do grant PRs out right or within 2 years; Hong Kong needs to get ahead of the race to attract global talents
- Create a panel of business representatives from relevant sectors to help civil servants exercise discretion in granting permanent residence (PR) to talented applicants who may otherwise be overlooked on the count of low education attainment

B. Why should we adopt an accretive population policy?

To attract global talents, especially those from the mainland, and thereby create jobs, business opportunities and connections for Hong Kong people and corporates

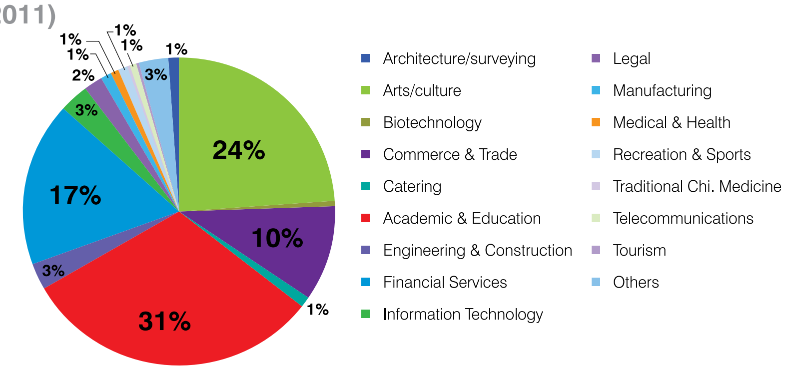
Building a World City depends much upon the talent pool of the city. Talents carry around capital, connections, skills and global perspectives, setting forth the congregation and exchange of the best ideas and practices in the world. Well-to-do immigrants, often entrepreneurial, bring with them jobs and a myriad of business customers and opportunities. Take the centre of the American melting pot for example. The 70,000 foreign-born entrepreneurs residing in New York City represent c. 50% of the World City's small business owners , creating c.30,000 jobs in the Big Apple last year.

Global talents congregate ideas and entrepreneurship, spinning off more jobs in World Cities

Unlike New York City's immigrants, the talents that we bring in are heavily skewed towards non-business related disciplines and individuals with relatively low income. Over 50% of mainland talents in the Admission Scheme for Mainland Talents and Professionals (ASMTP) obtain their work permit to contribute their expertise in Hong Kong's academia and the Arts & Culture field. These talents are important in adding diversity and knowledge to our city, yet with only 10% earning HK$40,000 or above among all ASMTP applicants, the vast majority of the talents we are bringing in with this supposedly targeted scheme are not individuals who have the economic and social capital to create jobs and bring connections that can enhance our global competitiveness and the income of our people.

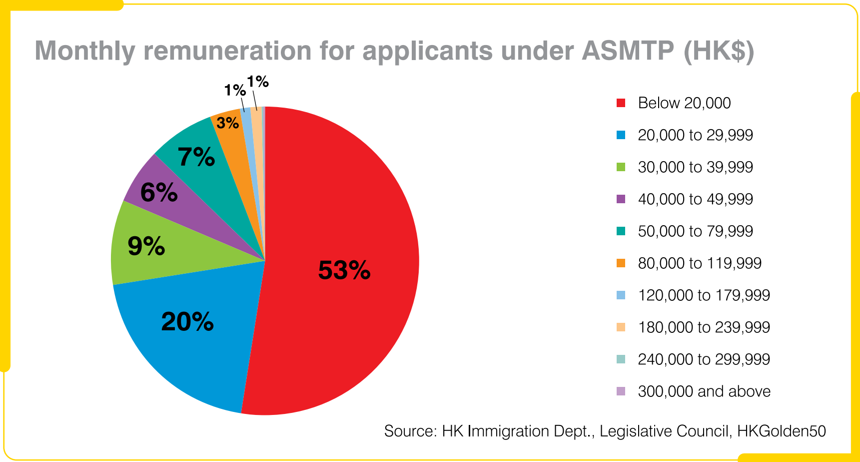
Hong Kong's population policy fails to create a pool of talents who can generate job opportunities and enhance Hong Kong's competitiveness

Admission Scheme for Mainland Talents and Professionals (2011)



Source: HK Immigration Dept., Legislative Council, HKGolden50

53% of mainland talents are employed in non-business sector; 53% earn below HK$20,000



Hong Kong's ascent to World City will be frustrated if we fail to attract a continuous inflow of talents that draws businesses and customers to the city. Singapore has attracted 75,000 talents per year to settle down in the city for almost a decade, while Hong Kong has only brought in a couple thousand of talented permanent residents each year, and this is directly dragging our economic growth behind as we are letting businesses opportunities slip away due to lack of talents. As we have repeatedly emphasized in our previous two reports, flows beget more flows in business, and with China's emerging economy, broadening our city's network with the mainland market should be flagged as key priority for both China and Hong Kong (for details, refer to "How to become a World City: Lessons from London" pages 19-25).

Hong Kong needs policies to attract talents and the jobs they bring with them, increasing connectivity to China and the rest of the World or they will flock to other potential World Cities like Singapore

Simulation of the Effect of Immigration Policies

Singapore Before and After Immigration				**Hong Kong Before and After Immigration**			
	Before	Immigrants	After		Before	Immigrants	After
Population	100	**15**	115	Population	100	**11**	111
GDP Per Capita	10.0	**20.0**	11.3	GDP Per Capita	10.0	**4.5**	9.5
Total GDP	1,000	300	1,300	Total GDP	1,000	50	1,050
Increase in Total GDP			30%	Increase in Total GDP			5%
Change in GDP Per Capita			+13%	Change in GDP Per Capita			**-5%**

Just as one cannot become a World City without the continuous influx of global talents, proper policies to retain the ones who choose to come are equally, if not more important. A quick glance at Hong Kong's immigration statistics readily reveals the flaws of our existing population policy, and the urgency to replace it with an accretive one to retain talents and accelerate Hong Kong ascent to become a World City. While Singapore's recruited talents added 13% to the Lion City's per capita income, Hong Kong's immigrants brought about a 5% drop in our per capita income. (For a more detailed discussion, please refer to our second report "How to become a World City: Lessons from London" pages 11-14)

Hong Kong's existing population policy is dilutive

Five Types of Employment Permits of Hong Kong

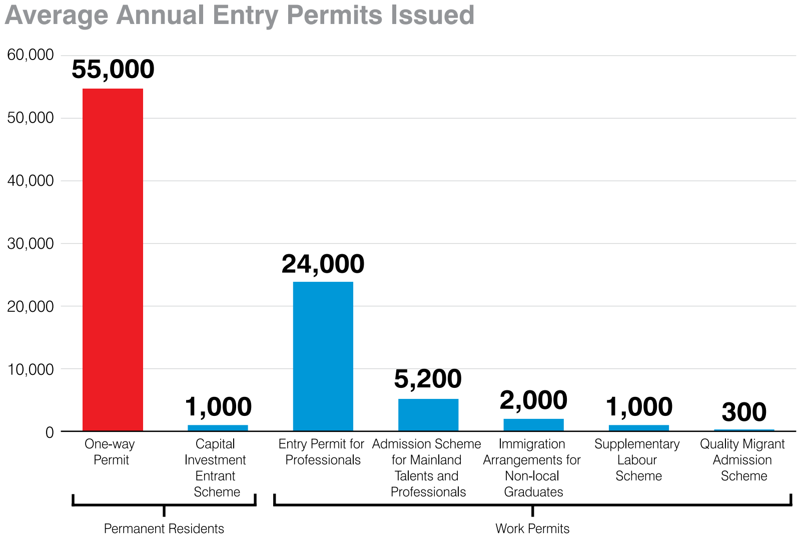
Permit type	Type of Applicants	Eligibility of Long Term Visit Pass for relatives	Presence of Quota	Notes
Entry Permit for Professionals	Non-Mainland professionals	Yes	No	Conditioned on being secured offer in Hong Kong
Immigration Arrangements for Non-local Graduates	Non-local fresh graduates	Yes	No	Conditioned on being employed within 12 months
Admission Scheme for Mainland Talents and Professionals	Mainland talents and professionals in commercial, financial, arts, culture, sport and culinary fields	Yes	No	Conditioned on being secured offer in Hong Kong
Quality Migrant Admission Scheme	People with first degree from recognized university/good technical qualifications, proven professional abilities and/or experience and achievements supported by documentary evidence	Yes	Yes	Points-based selection system
Supplementary Labour Scheme	Labour at technician level or below	No	No	N/A

Source: Immigration Department, Hong Kong Yearbook

There are two main sources of immigrant population in Hong Kong: those who enter with the five types of employment passes and the ones that come in with 150-per-day One-way Permit quotas. Our population policy fails to attract talents yet retains relatively low-educated individuals

A simple analysis of the annual entry permits' breakdown explains the long overlooked yet crucial element to our becoming of a World City. A population policy that maps out the demographic needs of our city is non-existent. The Immigration Department's five entry permits granted specifically to both mainland and overseas talents predominantly for shorter work permits purposes attract on average less than 30,000 global citizens per year since the schemes were introduced, accounting for only 1% of our labour force. While our city falls short on attracting global talents, we fair well in expanding our population base. Through the One-way permit (150 per day), 55,000 spouses and children of Hong Kong citizens, of which only 8% have received post-secondary education or above, settle down in Hong Kong each year. This group makes up c.90% of Hong Kong's new PRs each year, adding up to 700,000 of our city's population since 1997. While it is important for Hong Kong-mainland families to reunify especially for the well-being of these children, better policies should address the economic implications that come along with the rapidly expanding population without successfully increasing the base of our talents.

Hong Kong's population policy lacks planning and policies to attract highly entrepreneurial and productive talents are virtually non-existent or ineffective



Source: HK Immigration Dept., HKGolden50

In stark contrast, Singapore's population is heavily shaped by its immigration policy. As of 2010, only 64% of the total population are made up of local citizens. With the goal of recruiting more talents to drive Singapore's economic and social growth, the Singaporean government has liberalised immigration policies to attract greater inflow of foreigners taking up permanent residence, including several schemes to offer instant permanent residency to individuals with a top-notch education or professional background. As a result, PRs and equivalents increased by c.450,000 on a high-skilled population of 3.5m between 2005 and 2010.

A stark contrast: Singapore's immigration policy shapes the Lion City's population composition

Singapore limits the entry of middle and low-skilled workers with the quota of its S and R passes, and issues 3 types of passes to professionals, maintaining its foreign labour force at a high educated level, while ensuring enough low skilled labour (36% of total workforce) to support a stable supply of labour force to support the country's expansion in infrastructure works.

Singapore takes proactive measures to create the right mix of immigrants

The Five Types of Employment Passes of Singapore

Pass type	Type of Applicants	Level of fixed monthly salary required	Educational Qualification	Eligibility of Long Term Visit Pass for relatives	Usual waiting time for PR application	Presence of Quota
P1	Professional, managerial, executive or specialist workers	≥ $8,000	Degree or above	Yes	1 year	No
P2		≥ $4,000		Yes	≥ 2 years	
Q1		≥ $2,800		No (only Dependent Pass)	≥ 2 years	
S	Middle-skilled workers	≥ $2,000	Degree/ Diploma	No (only Dependent Pass)	4-5 years + stable working history in Singapore	Yes
R	Middle and low-skilled workers	< $2,000	N/A	No	N/A	Yes (and employers have to pay foreign worker levy)

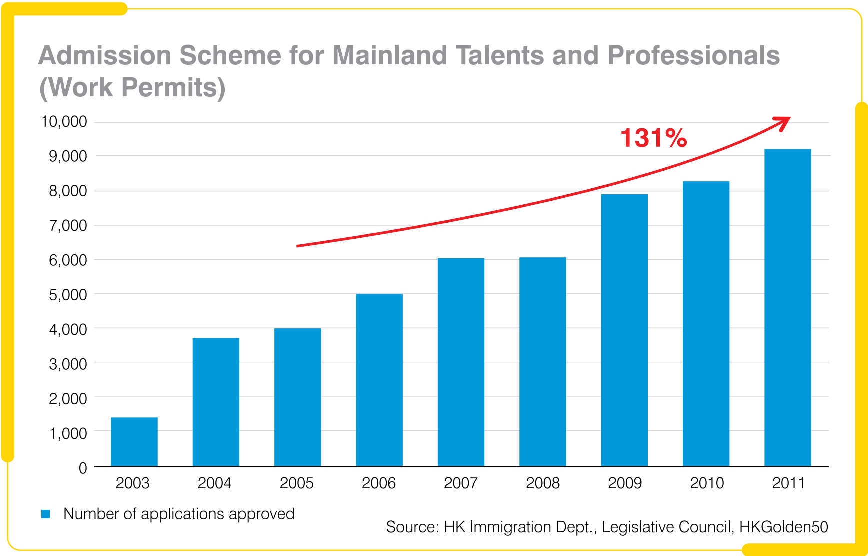
Source: Singapore Ministry of Manpower

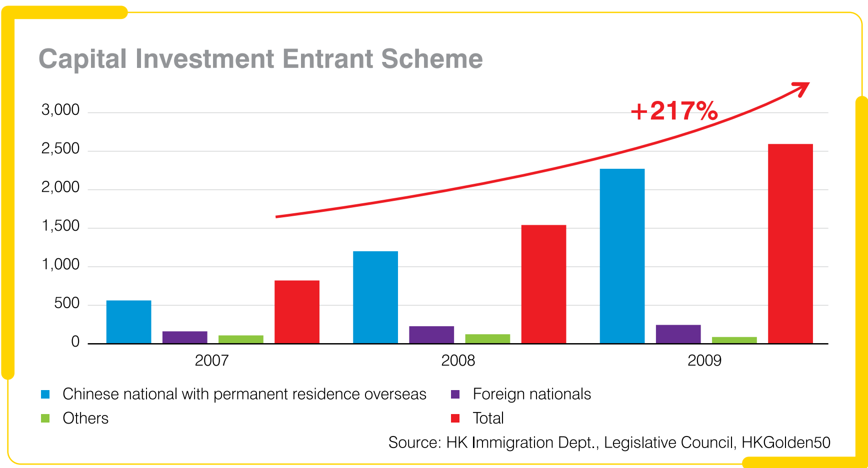
Singapore's successful accretive immigration policy attracts global talents with high education attainment (80% are post-secondary educated) to fuel its economic growth, while Hong Kong's non-existent population policy introduces only 8% post-secondary educated immigrants. If we continue to let our ineffective population policy persist, Hong Kong would eventually lose our bid to become a World City.

As Singapore and Hong Kong import the majority of immigrants amongst whom 80% and 8% received post-secondary education prior to their arrival respectively, Hong Kong would eventually lose competitiveness

Recent years have witnessed a rapid surge in the number of applications to work and reside in Hong Kong. The ASMTP applicants have more than doubled since 2005, and immigrants to Hong Kong through the Capital Investment Entry Scheme increased by three folds from 2007-2009. There is plenty of potential to tap into this pool and Hong Kong needs to take action now.

Hong Kong's fortuitous geographic location offers us a backyard full of talents who can bring in connections and business opportunities





Proposals

"One country, one market" should be made priority when determining our population policy

For the past 170 years, Hong Kong has played a dominant role in directing flows from the West to China. The Closer Economic Partnership Arrangement (CEPA) allowed a continuation of this by making access to the Chinese market easier for a number of sectors, but what we need today is a reverse flow that attracts mainland talents southward to enhance our appeal as a gateway to China. "One country, one market" cannot play out fully without the free flow of talents (Please refer to pages 8 to 12 of our first report). An increased porosity of the southward talent flow brings about multiply effects, including more offices being set up in this city, a congregation of business partners to travel or relocate to Hong Kong, and the synergy of ideas. The possibilities are endless when one major flow—the south bound talent stream—becomes unblocked, and this should be a priority when we draft our population policy.

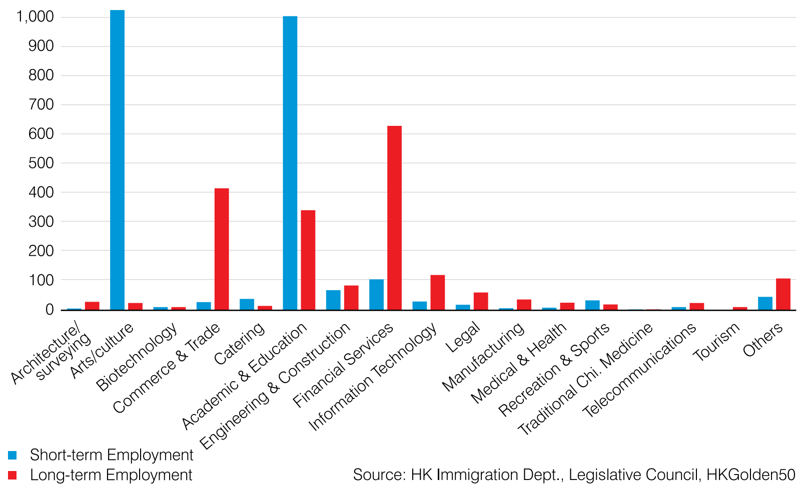
Channel 200,000 opportunity/job-creating talents to become PRs in the next 10-15 years

This pool of talents and business connections are the yeast to ferment Hong Kong's long term economic growth and our quest to become a World City. Attracting 200,000 talents over the next 15 years is an easy target that our society can achieve, given the Lion City's success in absorbing 450,000 foreign talents within 6 years. Especially in the face of 300,000 baby boomers retiring in the next decade, Hong Kong can definitely use extra helping hands and heads that can concurrently bring in more businesses and demand for services across all sectors. These entrepreneurial minded talents are the catalyst to Hong Kong's development whom can create jobs, induce higher wages and increase our population's earning power to race against the long term inflation.

The pool of global talent is unlimited and fluid, yet our existing immigration policies limit our intake and fail to retain talents. We are in urgent need to reexamine our existing work permit schemes, such as the Quality Migrant Admission Scheme's quota capped at 1,000 per year. The ASMTP also offers too few long term jobs, with 85% of the two largest employment sectors (Academic and Arts & Culture) giving out short term contracts. These barriers are extremely counteractive to our quest for talents, especially when we are competing against liberal immigration policies like instant permanent residency that Singapore gives out. We therefore urge for a revision of our immigration restrictions and shorten the minimum stay of seven years to two years for permanent residency limited to selected applicants who can add value to our economy, bring along their entrepreneurial skills, and generate more business and employment opportunities.

Revise population policy and shorten the required length of stay from 7 years to 2 years for selected applicants to obtain permanent residency

Admission Scheme for Mainland Talents and Professionals (2011)



Source: HK Immigration Dept., Legislative Council, HKGolden50

Existing immigration measures are stringent and not designed to catered for recruiting well-connected and talented individuals to our city. The entrepreneurs who can generate the most jobs, flows and global connectivity may not be the ones that most fit the criteria of our immigration department's existing guidelines on paper. Many successful entrepreneurs started off with credentials that would never make it to the list with the official guidelines. One of the world's richest men Huang Guangyu, founder and chairman of Gome Electrical Appliances had a 9th grade education and only US$500 when he first started his career as an entrepreneur. His success story is the epitome of potential that the combination of can-do spirit and astute business acumen can achieve. We need more of these warriors to reawake Hong Kong's can-do soul and reinstate our connections with these talents. Hence, we propose setting up a special committee to fill this loophole and offer these special talents an alternative stream to bring their expertise to Hong Kong. A panel from the business sector can well judge the potential of such talents and provide them an opportunity to unleash their potential and bring in their connections to our city.

Create a panel of business representatives from relevant sectors to help civil servants exercise discretion in granting permanent residence

3.4: Invest $40bn in Expanding Medical Capacity and Capability to keep our People Healthy & Active

A. What are we investing in?

Invest HK$40bn to expand medical capacity and add 6,600 beds in our medical system by expanding existing hospitals and/or building additional hospitals in ten years' time

B. Why should we invest in expanding our medical system??

Address the lack of medical facilities, equipment and manpower to prepare the medical system for the imminent rise in patients as baby boomers mature

Hong Kong has been offering quality medical services, but it is unlikely to last

Hong Kong's medical system has been one of the world's best, with one of the lowest infant mortality rates and remarkably higher cancer survival rates than those of Europe and the US. However, the quality of our medical services is unlikely to sustain as baby boomers are ageing, and thus rapidly increasing the demand for medical attention by one-third. However, both hardware are severely stressed (e.g. hospitals and equipment) and software (e.g. doctors and nurses) of the medical system is severe stressed.

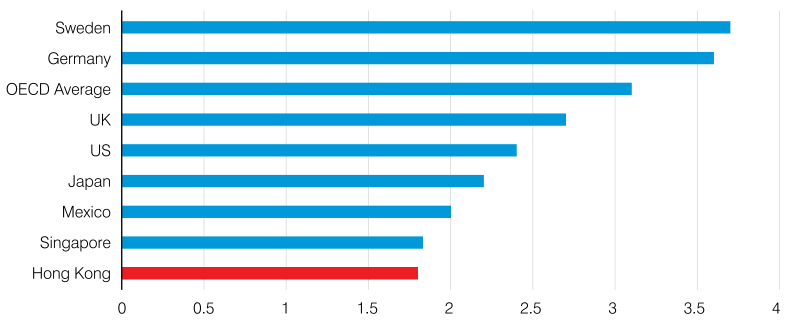
As far as medical hardware is concerned, we have characterised, in our previous report, the last ten years of Hong Kong as the "Lost Decade": in the 2000s, not even one new hospital was established and operational, whereas eight hospitals were constructed during the 1990s. While there are plans for new hospitals in various locations, none of them will be fully operational until 2016. Surely the demand of medical attention did not drop in the last decade as opposed to the ten years before as population grew and aged. This is a clear reflection that our medical system has been under-invested for years.

Medical demand has been increasing as population grows and matures, yet no new hospitals were established in the last decade

Besides hospitals, our medical system also lags behind in terms of equipment. As Dr. Ho Pak-leung, President of the Centre for Infection of HKU, pointed out in September last year, 90% of the apparatus at the Centre for Infection are at least 20 years old and even the UV-Light Box for rapid test and genetic diagnosis is "home-made" by staff of the centre. Dr. Ho believes that as the frontline fighting against infectious diseases, the Centre for Infection should be always well-equipped to produce reliable and timely detection results in case of emergence of new viruses. He described the current situation as "driving an antique car and you never know when it will break down" and Hong Kong will be under great threat in the case of an outbreak of infectious diseases.

Old equipment may jeopardise people's health in case of an epidemic

Physicians per 1000 Population (2011 or latest year)



Source: OECD Health Data, WHO World Health

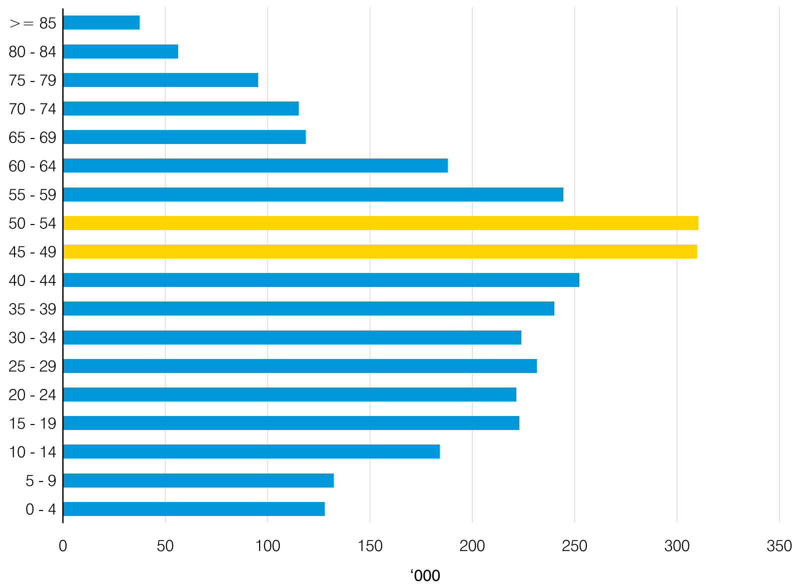
The number of doctors per 1,000 population is 1.8 in Hong Kong, a level lower than that of Mexico where per capita income is less than one-third of Hong Kong, not to mention the average of 3.1 in OECD countries. Dr. W.L. Cheung, Director of Cluster Service Division of HKHA has remarked that the public medical system is in acute shortage of doctors and importing overseas doctors would certainly help alleviate the problem. We are also in dire need of nurses and healthcare assistants for the elderly.

Per capita doctors in Hong Kong is even lower than that of Mexico

Insufficient supply of medical hardware and software both in the public and private sectors has led to a remarkable one-third jump in number of reported medical negligence in hospitals. There were a total of 44 cases from October 2010 to September 2011, up 33% from the previous year. Other problems from shortage of medical services have been well illustrated in the media and here we do not go into the details.

Increasing number of medical negligence suggests that the medical system is stretched to the limit

Biggest Age Group of HK Male: 45-54 (The Golden 50)



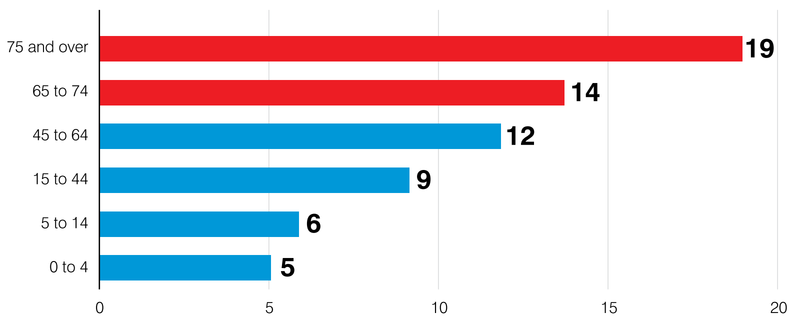
Source: Census and Stat. Dept.

The medical system in Hong Kong will deteriorate to third-world country level unless serious investment is allocated. The current age distribution of the Hong Kong population brings two important implications: (1) demand for medical services, especially geriatric medical services, will at least double in 20 years' time and (2) supply of medical staffs will contract significantly as a result of the waves of retirement of baby-boomers in the coming decade.

The current age distribution suggests that the existing capacity of the medical system caters for about 200,000 men aged 65-74 (similar size for women), but 15 years from now when the two yellow bars in the population pyramid shift up, the medical system has to support over 600,000 men in the same age group. This represents a huge increase in demand, especially when we take into account that, an elderly inpatient's average length of stay per admission is three times that of those below 15 and that patients aged 65 pay 50% more visits to hospitals compared with those aged below 45. These figures suggest that a demand spike is inevitable as population matures.

Demand for medical services will increase but supply of medical staffs will drop as population ages

Average Length of Stay Per Patient (Bed Days) 2009



Source: Hong Kong Hospital Authority

Our medical system will lose a large number of veteran doctors and nurses as baby-boomers retire in the coming decade. This will exacerbate the shortage of medical staff that is present in many public hospitals now. While detail projection is still in progress, given an already overstretched medical system, an expected jump in demand and drop in supply of medical manpower, we must take action now to invest in increasing medical capacity by at least one-third.

	Capital expenditure HK$bn	Operating cost per year HK$bn
Increase hospital capacity by one-third • Expansion of 6,600 hospital beds • Replace and upgrade old equipment for hospitals and research centres • Corresponding increase in operating expenses (staff, drugs, medical supplies etc.)	40	13

Expand the current medical system by one-third

We call for an expansion of hospital capacity of 6,600 beds and funding hospitals and research centres (e.g. Centre for Infection) to replace and upgrade their equipment. This involves a capital expenditure of HK$40bn and a recurrent expenditure of HK$13bn per year for the cost of additional medical staff, drug and other medical supplies for operation.

The relative shortage of medical services is different across districts and the expansion of capacity should correspond to such spatial imbalances. For example, Kowloon East has only three hospitals in the Cluster although the neighbourhood has the highest portion of population aged 65+. Also, Kwong Wah Hospital and Queen Mary Hospital have long requested funds for refurbishment and expansion. These projects should be considered first.

Besides expanding the public medical system, the government also has to speed up the approval of the four sites (in Wong Chuk Hang, Tseung Kwan O, Tai Po and Lantau) designated for new private hospitals.

Import overseas doctors to meet immediate demand; expand medical schools to increase supply in the longer term

The provision of medical services of world-class quality requires a strong team of medical staff too. We believe the current rate of expansion of medical schools in Hong Kong (420 graduates starting 2018) is far slower than the increase in demand in response to an ageing population. While it takes six years to nurture a general practitioner, another six years is needed to produce a specialist (e.g. a geriatrician). Therefore the solution to the immediate problem is to import foreign-qualified doctors and expand medical and nursing schools at a larger scale to increase supply of medical professionals in the medium term.

Valuable lessons could be learnt from Singapore's experience of importation of doctors

Singapore has also been aggressively "importing" overseas doctors, which has actually contributed to over half of the total increase in number of doctors during 2006-2009. More importantly, the performance of Singapore's medical system after importing overseas doctors has been satisfactory and is more or less on par with Hong Kong. Singapore's infant mortality rate, for example, is even lower than Hong Kong. Hong Kong certainly needs some more radical reform if we are to catch up with our peers. We shall address these issues in greater details in our next report, "How to create a World-class Medical System".

3.5: Invest HK$15bn in Expanding University Capacity & Improving Quality of our Economy's New Blood

A. What are we investing in?

Invest HK$15bn to expand university capacity and increase publicly subsidised university places by 10,000 (67%) in five years and admit more non-local students

B. Why should we invest in more university places?

We believe there are two major reasons supporting the proposal of expansion of universities:

(1) To produce more university graduates to meet labour demand

(2) To attract more talented students from the mainland and the rest of the world to establish Hong Kong as a regional education hub

(3) To extend the channels through which the value system and excellence of this World City can be exported to the world, increasing its global influence. London universities do not cater only for students in London or the United Kingdom, but the world. By absorbing such a wide range of talents, the perspectives of both local and overseas student are greatly shared and extended

Labour Supply and Demand:
Degree Holders or above (2010-2018E)

('000)	2010	2011	2012E	2013E	2014E	2015E	2016E	2017E	2018E
(a) Labour Demand*	817	850	884	918	952	985	1017	1050	1082
(b) Adjusted Labour Supply^	837	864	893	921	949	978	1006	1037	1066
Shortage (a-b)					3	7	11	13	16

*Assume 5% GDP growth
^ Allowed for natural rate of unemployment
Source: Census and Stat. Dept., HK University Grants Committee, various HK universities, HKGolden50

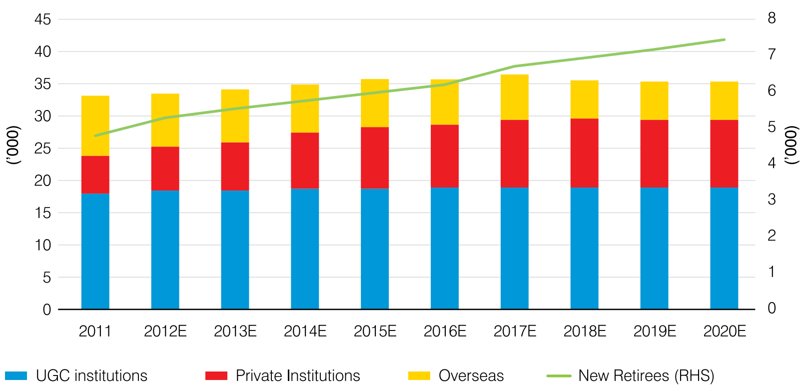
There will be insufficient university graduates to meet labour demand in two years' time

(1) To meet labour demand

We expect that labour demand for university graduates to expand less than proportionately with our economy, creating about 35,000 new jobs for higher-educated workers each year (i.e. employment grows at c.4% per annum), assuming the economy achieves an annual real growth of 5%.

However, our current education system is not supplying enough talents to meet labour demand. At the moment, around 30,000 university graduates (incl. undergraduates and post-graduates) enter the job market every year. Half of this figure comes from local publicly funded degree programs, while the remaining stems from existing local degree-awarding private institutions and overseas universities.

Graduates by Sources and Retirees



Source: Census and Stat. Dept., HKUGC, HKGolden50

Although there are more private universities to be established in the near future, the pace of expansion is apparently too slow to catch up with the rising demand for labour. Ageing population definitely plays a role: we estimate that new retirees with qualification of degree or above will grow by 60% in a decade to 7,000+ per year by 2020.

Expansion of private universities is not fast enough and the number of retirees is growing

As a result, problem of labour shortage will occur as soon as 2014. The shortage is expected to grow to over 16,000 by 2018, more than the current annual quota of government subsidised degree places (15,000) in Hong Kong. Expanding university capacity now is necessary to alleviate the problem of labour shortage.

(2) To establish Hong Kong as a regional education hub

Hong Kong has a huge potential demand for university education from its hinterland

The Hinterlands: Guangdong Province vs. the UK

In 2010	Guangdong	United Kingdom
Population	104,303,000	62,262,000
Total Area (sq. km)	178,000	242,000
Dependency Ratio	31%	52%
Nominal GDP (HK$ bn)	5,219	17,480
Nominal GDP Per Capita (HK$)	50,000	281,000
Nominal GDP Growth p.a., 1990-2010 (Local Currency)	18.4%	4.8%

Source: Statistics Bureau of Guangdong Province, UK ONS, CIA World Factbook

A city is only as great as its people. Even with the best architecture in the world, a World City requires a continuous inflow of talent available to work for the international financial institutions and multinational corporations to maintain its position as a World City. We believe that Hong Kong should aspire to become a regional education hub in Asia, particularly for China, but Hong Kong needs more university places. While London produces 30,000 graduates every year, Hong Kong only has subsidised first-year first-degree (FYFD) places of 15,000. Given that London receives students from its hinterland (the UK), one should also consider Hong Kong's hinterland – Guangdong, the most populated province of China, when determining the optimal size of the tertiary education system as we move towards 'One country, one market'.

Hong Kong has all the makings of a recognised regional education hub: a well-established system of rule of law, freedom of speech and expression, high quality education constitute irreplaceable attractiveness for bright students from the rest of the world. The quality of Hong Kong universities are reflected in the rankings: four out of the eight UGC-funded institutions in Hong Kong are ranked top 20 in Asia while only three mainland universities are so ranked despite the vastly bigger student catchment, with two of them situated in Beijing.

Global Ranking of Universities

Rankings	Asia	Worldwide
University of Hong Kong	**2**	**34**
Peking University	4	49
Hong Kong University of Science and Technology	**7**	**62**
Tsinghua University	8	71
The Chinese University of Hong Kong	**15**	**151**
University of Science and Technology of China	19	192
City University of Hong Kong	**20**	**193**

Source: Times Higher Education 2011-2012

In other words, students from the mainland and the rest of Asia would find universities in Hong Kong desirable institutions for their education. This is especially true for students in southern China due to geographical proximity.

In fact, the first survey on mainland graduates at the University of Hong Kong (HKU) conducted by HKGolden50 has confirmed this view, with 88% of the respondents find their education at HKU had given them an advantage over mainland degrees and 70% of these mainland graduates would recommend their friends and relatives coming to Hong Kong to pursue their studies. These findings suggest that mainland students do hope to study in Hong Kong but there are not enough places for them.

Our survey shows that mainland students do want to pursue their undergraduate studies in Hong Kong

Considering the planned expansion of the private institutions (c.5,000 places), we propose to increase publicly subsidised university places by 10,000, expanding the tertiary education system of Hong Kong by 67% to a level comparable to London. We believe that adding university places and accommodating more global talents creates a "clustering effect" of high calibre that attracts even more bright individuals – just like London and New York, where top-notch universities admit the best students from all around the globe.

Expand university capacity by 67%, to a level comparable to London

	Capital expenditure HK$ bn	Operating subsidy per year (per 4-year degree for 10,000 students) HK$ bnHK$ bn	Return per year (extra income of 10,000 students earned over 35-year work life) HK$ bn
Add 10,000 university places	15	2 (8)	3.2 (112)

This translates into an estimated HK$15bn capital expenditure on constructions of campuses, amnesties, hostels, laboratories and research centres etc., and recurrent cost is estimated to be HK$2bn.

Prof. Francis Lui of the HKUST has observed that one year of university education could increase income by 15-18%. We estimate that aggregating the extra income gained by the 10,000 students after completing a four-year degree programme would amount to some HK$3.2bn per year or HK$112bn over the course of a 35-year working life. This income gain represents the gain by society and which significantly exceeds the education subsidy to run such a course of HK$2bn a year, or HK$8bn over the four-year programme.

Investment in university education generates significant income growth

While details of the expansion should be subject to further study and public discussion, we believe the general direction is that we need to nurture talents that support the development of "credibility businesses" by leveraging on the brand of Hong Kong: we definitely need to train more doctors and nurses to cope with the imminent shortage in medical staff brought by ageing population and in the longer term, to establish Hong Kong as a regional hub for medical services; more engineers to provide testing and certification services and more artists to promote the city's art scene.

Hong Kong needs a larger talent pool to support "credibility businesses"

To accomplish these, we are in need of more land to accommodate the extra facilities and students. Here we list some possible options to create more spaces for our universities:

We need to have more proactive ways to create land: reclamation, rezoning and the development of the LMC Loop are possible solutions

(1) Reclamation

This is a more convenient option for universities with a water frontage like the Chinese University of Hong Kong (CUHK) and HKUST.

(2) Re-configuration of land usage and density

This is particularly important for universities located in urban areas. Take HKU as an example, the ex-Kennedy Town Abattoir site may be rezoned for educational use and a higher density may be adopted to make for more buildable space for the expansion of HKU.

(3) Development of the Lok Ma Chau Loop (LMC Loop)

In the current development plan of the LMC Loop that lies to the south of the Shenzhen Futian, the government suggests to use 25 ha of the LMC Loop for higher education and new high technology. A few local universities have already expressed interests in establishing campuses in the Loop. We suggest the government to allocate extra resources to establish research centres and laboratories in this area to create the synergies and clustering effect that is necessary for new high technology and testing and certification industry to flourish.

3.6: Invest $4bn to Promote & Enrich Art & Culture for a Vibrant, Upbeat & Cultural World City

A. What are we investing in?

Allocate the extra HK$4bn necessary to re-work the delivery programme of opening 9% of the project by 2015 and start constructing the West Kowloon Cultural District (WKCD) immediately so that 25% of the project will be opened by 2018

B. Why should we invest in promoting and enriching Hong Kong's art and culture?

We believe there are two major reasons supporting the proposal of investing in opening 25% of WKCD in 2018:

1. Enhance Hong Kong's content as a World City
2. Capitalise on the demand of art and cultural appreciation from baby boomers as they retire

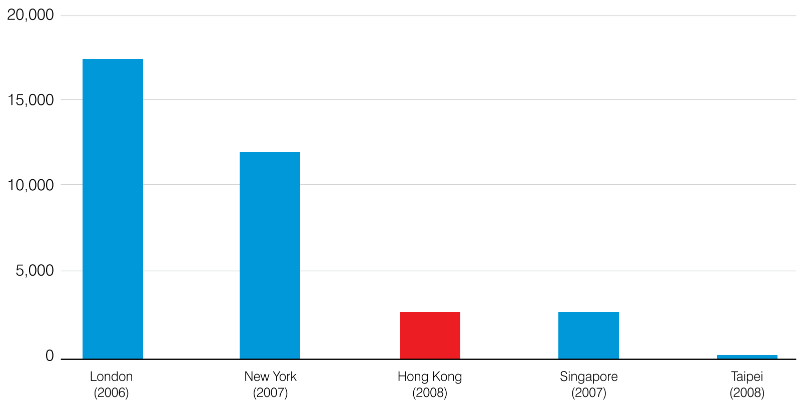
1. Enhance Hong Kong's content as a World City

Hong Kong lags behind New York, London, Singapore and Taipei in art and cultural offerings, in both hardware and software.

Both Hong Kong's offering and Hong Kong people's interest in attending art performance are low compared to other World Cities

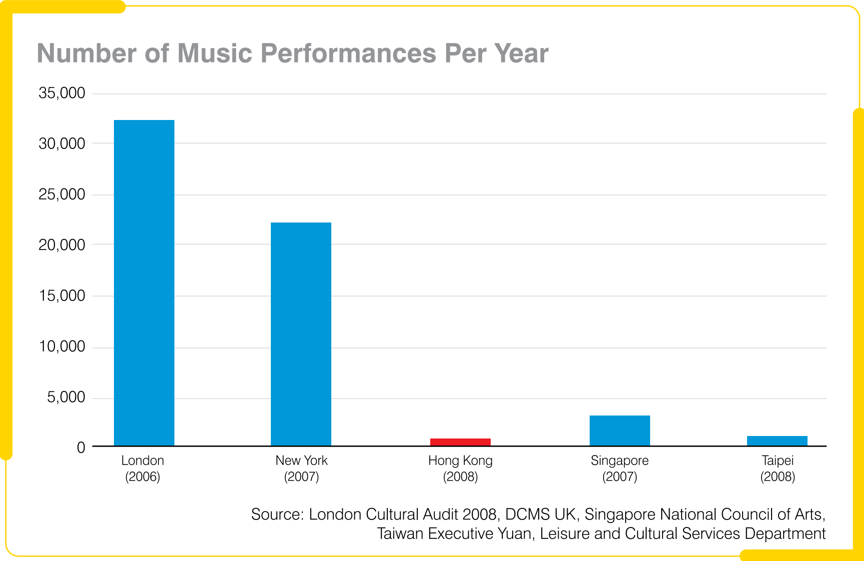
Every World City needs a vibrant art and cultural industry; for instance, New York has Broadway and London has the West End, but Hong Kong does not have comparable performance offerings. In terms of the number of art and cultural offerings, Hong Kong lags behind World Cities like those of New York and London, and even our Asian neighbours Singapore and Taipei: each year, Hong Kong has 2,480 theatre performances at major theatres, whereas London has 17,825 (7 times that of Hong Kong), and New York has 12,045 (5 times that of Hong Kong).

Number of Theatre Performances at Major Theatre Per Year

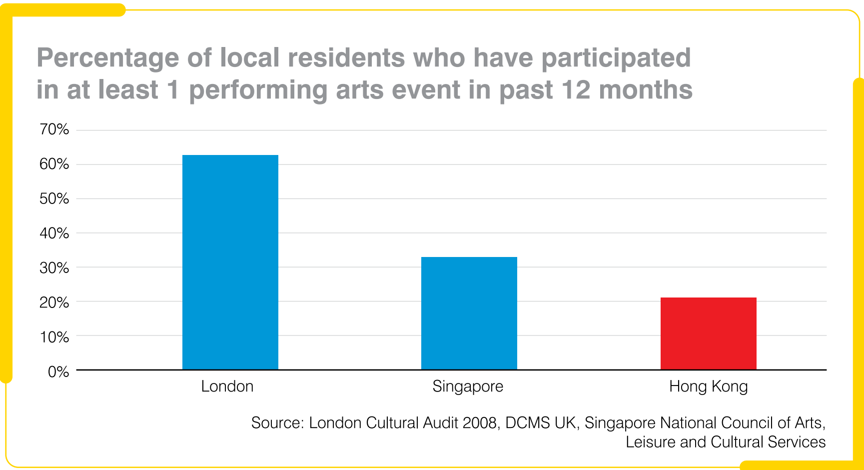


Source: London Cultural Audit 2008, DCMS UK, Singapore National Council of Arts, Taiwan Executive Yuan, Leisure and Cultural Services Department

Hong Kong's number of music performances equally lags behind other cities. Our 1,058 music performances each year are 3% that of London's 32,292 and even Singapore has 3,093, triple the amount of our performances each year. Hong Kong also offers very few international performances compared to other World Cities. Our best performance facility, the Hong Kong Cultural Centre, despite housing similar amount of shows per year as Singapore's Esplanade and the London Barbican Centre, carries only 12% international artists or art groups, when Singapore and London offers 36% and 52% respectively.



Moreover, as stated in the Sub-Culture section of this report, Hong Kong people's interest in attending art performance seems low compared to other World Cities: while 63% of Londoners and 33% of Singaporeans have seen a performance in the past 12 months, only 21% of Hong Kong citizens have done the same.



Eminent Taiwan-Hong Kong literary and music critic Leo Ou-fan Lee, having interviewed with a wide range of international artists and art groups, concludes in his two books of music criticism "Symphony" and "Music Essays" that the low quality acoustic facilities concert halls provide (even in our biggest facilities like the Hong Kong Cultural Centre and City Hall) are one of the major reasons why international groups are reluctant to stage in Hong Kong. Hong Kong needs to address the shortage of World-class standard facilities before more quality performances can be brought in; artists are only willing to come if they can sell enough tickets and guarantee a quality performance that will not be bogged down by hardware problems. Building sizable and quality hardware facilities is therefore a prerequisite to gain an equal standing with other World Cities.

Lack of hardware is the meat of the problem; artists are only willing to come if they can sell enough tickets and guarantee a quality performance that will not be bogged down by hardware problems

World-class facilities like the concert halls and theatres in London are designed specifically to accommodate the professional demands of international groups. Most of Hong Kong's performance venues, however, are multifunctional but not professionally catered for world-class performances. Take concert halls for example, Hong Kong has 17 facilities that serves the function as concert halls under the Leisure and Cultural Services Department. However, out of the 17 venues only the City Hall and the Hong Kong Cultural Centre have large-sized concert halls that hold more than 900 seats. The four town halls and four civic centres have multifunctional auditoriums or theatres which are not tailor-made (for instance, acoustics-wise) for international music performance; they are also used as makeshift theatres, exhibitions and congregation activities. In contrast, all of the 12 concert halls in London are professionally catered to international performances, with five of them holding 900 up to 3,000 seats.

Most of Hong Kong's performance venues are multifunctional but not professionally catered for world-class performances

Furthermore, art philanthropy in Hong Kong is not common. Out of 5,311 non-profit organisations (registered charities) in Hong Kong, only 5% of them are art-related, which reflects that Hong Kong people do not tend to donate to the arts. Art philanthropy is crucial for a World City attracting international and local art talents residing and practising their art there, since many art talents need funds to pursue their creative projects. However, there is yet philanthropic foundation for arts in Hong Kong comparable to the scale and scope of the Guggenheim Foundation in the United States or the Art Fund in the United Kingdom.

Unlike other World Cities, art philanthropy in Hong Kong is not common

2. Capitalise on the demand of art and cultural appreciation from baby boomers as they retire

Inadequate supply of blockbuster shows cannot meet surging demand for professional performances.

Hong Kong local art groups' blockbuster shows such as co-production of the Hong Kong Philharmonic and world-class groups in the Hong Kong Arts Festival and ballet performance by the Hong Kong Ballet cooperating with local celebrities generally draw a 90% attendance rate, 15 percentage points higher than the independent performances of these local groups. However, these world-class quality co-productions and blockbuster shows only account for the 30% of these local groups' performance time over a year-long performance season. In addition, in the WKCD Authority's (WKCDA) Draft Stakeholder Groups for PE exercise in 2009, 96% of all music art groups in Hong Kong are either part-time or amateur in nature, but they are responsible for 70%+ of all performances every year in all town halls and civic centres. All these suggest that there is adequate demand for professional blockbuster shows, yet 70% of our supply of performances is amateur in nature. These suggest that Hong Kong people are quite willing to attend "blockbuster" shows which performance quality could be safeguarded, whereas the inevitably uneven quality of part-time or amateur performances are not able to generate as much interest as "blockbuster" shows. We need to address the mismatch of performance supply by drawing more professional groups into our city.

Hong Kong people are quite willing to attend "blockbuster" shows which performance quality could be safeguarded, whereas the inevitably uneven quality of part-time or amateur performances are not able to generate as much interest as "blockbuster" shows

As stated in our previous report "How to Become a World City: Lessons from London" Section 3, the surge in demand for art and culture has been a prominent trend of our society for the last decade. Our art auction sales have increased by 10 folds in 10 years; the number of art exhibitions held in Hong Kong has become top of the world for four years; Hong Kong International Film Festival is by now larger in scale than the longstanding BFI London Film Festival; amateurs and even laymen flock to art-jamming every weekend. These recent trends all demonstrate that more of our community's acquired taste in art and culture, and, as stated in the said report Section 4, we should expect a further increase in demand for art and culture as baby boomers are retiring and have more time for art and cultural appreciation.

The surge in demand for art and culture has been a prominent trend of our society for the last decade

The above points to the conclusion: build the hardware and people will come. However, the WKCD Authority's (WKCDA) plan to open 9% of WKCD by 2015 has reflected its slow reaction to our city's upsurge in demand for art. As reported in the WKCDA 2011 announcement of opening, the opening of WKCD should be delayed in phases to ensure enough demand, i.e. demand may be bred gradually and the scale of WKCD could then expand according to the growth of demand until all facilities are finally open; this is a play-safe option to avoid early loss due to insufficient attendance. However, insufficient attendance is very unlikely as indicated here above – with world-class hardware, world-class artists and art groups would be willing to come to Hong Kong, and locals and tourists alike would come to see the world-class performances and exhibitions.

The WKCD Authority's plan to open 9% of WKCD by 2015 has reflected its slow reaction to our city's upsurge in demand for art

Proposal

Allocate the extra HK$4bn necessary to start constructing WKCD immediately and re-work the delivery programme so that facilities will not be opened until 2018 when 25% of the entire project is complete.

We have discussed in details the inevitable failure of the whole WKCD project if following the 9% 2015 opening plan in our second report, Section 4. In order to ensure its success, the government should allocate the needed additional funding of HK$4bn to the WKCD project, commence and lead construction in full speed such that 25% of the entire would be opened in 2018. Only by this concrete commitment would the government be able to prevail in the financial debate in the Legislative Council, freeing up the prolonged headache of WKCDA trying to fund its construction in whatever means, like issuing bonds, borrowing, or seeking sponsor from individuals or companies (for instance, selling naming rights).

Following the 9% 2015 opening plan will result in inevitable failure

According to information provided in WKCD Stage 3 Public Engagement Exercise, only part of the Great Park, an Outdoor Theatre, Freespace with Music Box and the Xiqu Centre would be ready for public use in around 2015, amount to a mere 9% of the total WKCD GFA; the Centre for Contemporary Performance may be opened by 2018, yet depending on the progress of Express Link construction.

To open at least 25% of WKCD (2m sf) by 2018, the targeted opening time of the majority of Phase I should be brought forward from 2020 to 2018, comprised of:

The majority of Phase I should be opened in 2018 instead of 2020

- M+ (Phase I)
- Exhibition Centre
- **Half of the total area** of Performing Arts Facilities (Phase I)
- Other Arts and Cultural Uses
- Communal Facilities
- **Half of the total area** of Retail/Dining/Entertainment Facilities

By 2015, construction of the Express Rail Link would be finished, thus M+ (Phase I), Exhibition Centre, Communal Facilities and Public Open Space should have a plenty three to four years to be finished on time.

There will be a plenty three to four years to finish the majority of Phase I on time after finishing construction of the Express Rail Link in 2015

The only thing is that our proposal of opening Phase I Performing Arts Facilities requires government effort to speed up the process of settling the land lease and construction problems of non-cultural land on the WKCD site, since most of these Performing Arts Facilities (five main clusters as appeared in the map in WKCD Stage 3 Public Engagement Exercise: Lyric Theatre, Music Centre, Centre for Contemporary Performance, Musical Theatre, and Medium Theatre I) occupy the lower floors of residential and office buildings. WKCDA does not have jurisdiction over the non-cultural facilities in the site, and that is why construction of Performing Arts Facilities is currently on hold. As our art and cultural demand increases rapidly right now, both our supply of performance space and world-class performance shall be significantly enhanced when these Performing Arts Facilities could open earlier.

Opening Phase I Performing Arts Facilities requires government effort to speed up the process of settling the land lease and construction problems of non-cultural land on the WKCD site

Moreover, the government should prepare to allocate an extra HK$3-5bn within the next few years of Golden 5 Years to have all existing performing venues refurbished and/or upgraded, as well as build more future performing venues with world-standard specifications in mind.

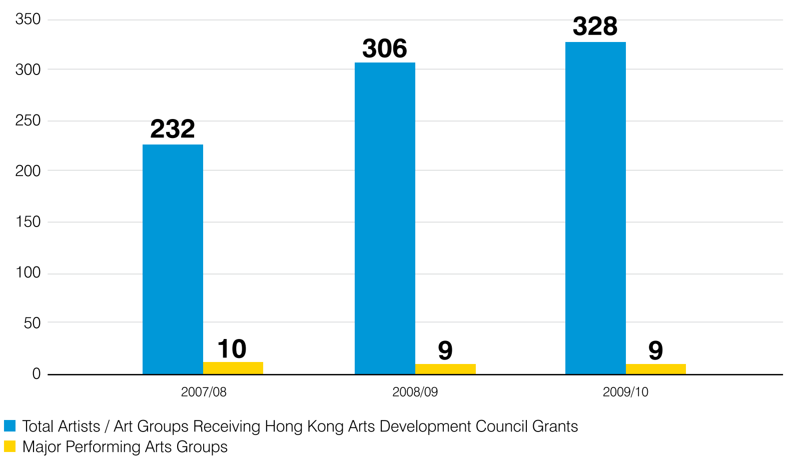
Furthermore, the government can complement WKCD development with effort to allocate art subsidies more fairly and proactively.

With WKCD hardware standing by, we need to attract quality international as well as local art offerings. Addressing the government art subsidies allocation problem shall enhance the latter.

The government allocates artist/art group subsidies through the Hong Kong Arts Development Council (HKADC) annually, and nine "major performing art groups" through the Home Affairs Bureau. The former has three main schemes, namely One-Year and Two-year Grants, Project Grant, and Multi-project Grant, subsidising a total of 328 artists/art groups in 2009/10. Whereas 328 HKADC-subsidised artists/art groups number much more than the nine major performing art groups, in 2009/10 the latter received a total of HK$264m subsidies whilst the former only HK$46m, 15% of all artist/art group subsidies. Fairness of this allocation result is questioned by eminent Hong Kong art advocate Ada Ying-kay Wong in her Mingpao interview (18th January, 2012). Moreover, the Home Affairs Bureau's "Committee on Performing Arts Consultation Paper" in November 2005 reflects that small art groups and independent artists frequently find it difficult to apply for and receive approval of subsidies due to bureaucracies that only large art groups could handle.

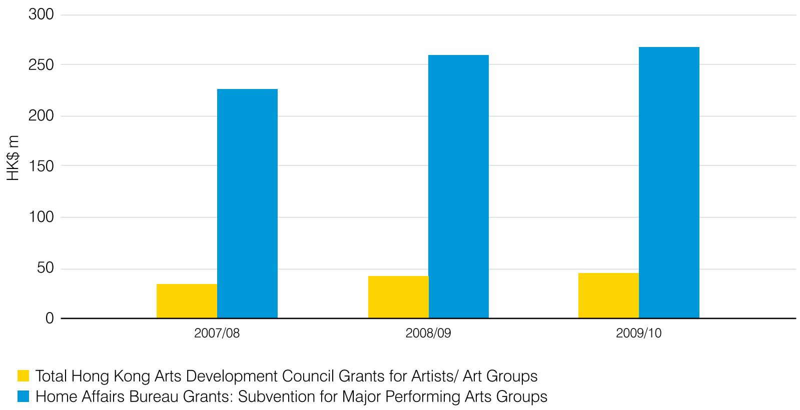
Whereas 328 HKADC-subsidised artists/art groups number much more than the nine major performing art groups, in 2009/10 the former only 15% of all artist/art group subsidies

Number of Artists/ Art Groups Receiving Government Grants



Source: Hong Kong Arts Development Council, Home Affairs Bureau

Government Grants for Artists/ Art Groups (HK$ m)



Source: Hong Kong Arts Development Council, Home Affairs Bureau

In order to complement development between our new art and cultural hardware (as exemplified by WKCD) and software (quality local art and cultural participation in WKCD), the government should allocate art subsidies fairly and proactively, raising quality local art and cultural participation and aspiring to be a international art centre as well as a hub of artists/art groups as what a World City is.

In order to complement development between our new art and cultural hardware and software, the government should allocate art subsidies fairly and proactively

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In the immediate 5 years, Hong Kong will enjoy some of the strongest inflows of business opportunities and talents in our history. If Hong Kong people think through the issues calmly and sensibly, we can capture these and enhance the long-term growth and quality of our economy, thereby supporting jobs and fostering social harmony for the next generation. If we choose to do nothing and allow these opportunities to disappear, we may well regret the decline that may follow the Golden 5 Years.

Our younger generation, in particular, should be more proactive in changing to a pro-growth mindset in the Golden 5 Years as what they choose will likely define their next 50 years.

HKGolden50 is an optimist – we believe Hong Kong's golden years will run far into the future because Hong Kong people will choose wisely. Our mission is to encourage awareness, discussion, research and ownership of these immediate issues in society in the hope that Hong Kong can move forward boldly again.

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