

# CHAIR'S LETTER TO SHAREHOLDERS



**Adriel Chan**  
Chair

Thank you for joining us for another year on this journey. 2024 was a trying year, and I do not take your continued support for granted. It was the first time in 24 years that our Mainland rental income fell in Renminbi (RMB) terms, as postulated by our Honorary Chair this time last year. Even then, we had foreseen the challenging trading environment that ultimately materialized as predicted.

## Results and Dividends

We ended the year with our total revenue up by 9% to HK\$11,242 million, partly due to residential property sales that we did not have last year. However, our core business – rentals – declined by 6% to HK\$9,515 million. Our mainland China results were exacerbated by a 1.5% depreciation in the RMB against Hong Kong Dollar (HKD) over the year. In mainland China, rents were down 5%, while Hong Kong rents slipped by 9%. As a result of reduced sales rent and increased interest costs, our underlying leasing profit attributable to shareholders dropped by 18% to HK\$3,422 million. It is important to highlight here a net loss we recorded for property sales owing to provisions made for certain unsold inventory – a direct reflection of the weakness in both the Hong Kong and mainland China residential property markets. After revaluations across our portfolio, net profit after tax attributable to shareholders fell by 46% to HK\$2,153 million. Reflecting these challenging numbers, and as a means to bring down the Company's gearing, the Board recommends a final dividend of HK40 cents per share, payable on June 16, 2025, to shareholders of record on May 9, 2025. If approved by shareholders, the total dividends per share for the year ended December 31, 2024 will be HK52 cents.

## Business Review

Considering the sizeable drop in the net profit after tax attributable to shareholders, I want to give a brief breakdown here, as this merits some explanation. There were three main reasons for the decrease: Firstly, the straightforward reduction in rents collected, which were primarily tenant sales rents. This was partially offset by increased fixed rents of our malls and is basically a mathematical extrapolation from the total sales revenue of our tenants. By tracking tenant sales, we were more or less able to predict where this would land. Secondly, the increased interest costs associated with the Company's borrowings for the construction of projects and our daily operations. This figure has essentially been known by the Company from the day the borrowings were made and is not a surprise. Often, what takes investors and analysts by surprise is the jump in P&L impact by loans associated with construction projects that transition from "projects under development" to "operating projects". Thirdly, the revaluation of investment properties, as made by our independent third-party valuers. This is based on a combination of metrics, including rentals, market transactions, and market expectations. As markets deteriorate, valuations move in the same direction.

For those keeping track of the luxury brands and high-end retailers, who make up some of our most important tenants, you will know that we are not alone in feeling the pinch. Most of our fall in rentals resulted from reduced sales rents (rentals taken as a percentage of sales), including those of luxury tenants. However, we were able to partially offset this by meaningfully increasing overall occupancies of our malls.

These achievements are no small feat in this market and speak to our strong team and the high quality and resilience of our portfolio. In short, they demonstrate solid execution of our strategy. I will come back to the retail conditions in mainland China later.

Office space has been under pressure in all markets, primarily as a result of decreased demand due to market uncertainty. In Hong Kong, there was also supply-side pressure from Grade A office completions across the city, most notably in Central, the city's central business district. There is little hope for a quick rebound since office demand is less volatile and tends to be a trailing indicator. However, I am happy that, yet again, our mainland China office portfolio has proven to be highly resilient. Since we offer, with the exception of Shanghai, by far the best physical office space in the top locations in each city, putting us in a strong defensive position, we have been able to maintain high occupancy and, to some extent, rents. As our Shanghai offices are facing abundant new supply with an aggressive pricing strategy, both occupancy and rentals have been under more pressure there than elsewhere. However, thanks to the "halo" effect that our successful malls and prime locations granted to us, we are still in an enviable position relative to most of the market.

Almost everyone one speaks to in China – from market observers and investors to the media and business owners – is calling the current market situation one of unprecedented uncertainty. Consumer and business confidence are as low as they have been in recent memory, and there is no clear path to improvement. As a business, we must face this reality and get on with it. I will highlight a few of the main challenges that our business currently faces below, along with some commentary and interpretation. After all, retail leasing accounts for more than 80% of our Mainland leasing revenue (which in turn accounts for over two-thirds of our total leasing revenue). Before delving in, however, it is worth noting that if one were to visit our malls across the country today, one would find the mood and sentiment to be not nearly as negative as they might expect from hearsay. I observed this on my own visits, as have others. I will also touch on this below.

There has been a serious drop in consumer spending on luxury goods, especially in first-tier cities. Our Shanghai malls' (Plaza 66 and Grand Gateway 66) tenant retail sales fell significantly, by about 20%, but our overall luxury mall sales (including at those two malls) declined by a somewhat more moderate 15%. By any standards, a 15% drop in sales is still significant. Household savings outstripped household spending in 2024, which is reflected in our own sales data. In luxury, we have seen this reduced spending in smaller basket sizes, the retreat of entry-level "aspirational" luxury consumers, and an increase in shopping internationally – particularly in Japan. In my mid-year letter, I mentioned that Chinese consumers were making about 60% of their luxury purchases onshore in mainland China and 40% offshore, primarily in Japan. This number seems to have held stable. The year before, in 2023, Chinese consumers made 82% of their luxury



PLAZA 66, SHANGHAI

purchases onshore and only 18% offshore. Assuming that total Chinese customer luxury consumption was similar in 2024 as in 2023 – as reported by several luxury groups – this implies a 22 percentage-point reduction in onshore spending but no reduction in their total spending power. While it would have benefited our shareholders if Chinese shoppers made more purchases onshore, the silver lining is that their total spending on luxury has not decreased.

Another important note on Chinese luxury consumption is that, compared to 2019 (pre-COVID) sales figures, 2024 sales are still up by almost 100%. That is to say, our luxury tenants today are doubling their pre-COVID sales amounts. This is an average across brands but on a like-for-like, same-store-sales basis. If you include new stores, the difference between 2019 and 2024 luxury sales is more than 125%, and if you only take the very top brands, their sales increase is almost 200%. Thus, the main concern is the trajectory and whether or not the market has “found the bottom”. Our data, corroborated with our tenants, demonstrates a meaningful narrowing of the decrease in November and December, which we hope will continue into 2025. If it does, there would be reason to believe that 2025 will see improved sales performance. Similarly, the pace of offshoring luxury sales has markedly slowed between the first and second halves of 2024.

During 2024, and for as long as this decline in onshore luxury spending continues, the competition between retailers and malls has been and will be more “zero-sum” than in previous years, when total sales were growing. In particular, those cities where luxury retail distribution was already “at saturation” will see intense competition. In this environment, an increase in one mall’s sales has meant a necessary decline in another. Therefore, the tactics and approaches to this type of market must differ from those deployed in the previous decade, in which there was healthy luxury growth. The result has been a grueling competition for the best tenants – competition on pricing, marketing, service, and ancillary offerings. Over the course of the year, there was one notable case of price competition in Wuhan, with one competitor instigating a “price war” by offering what were effectively discounts of about 20% on luxury brands. They did this by providing rebates and vouchers that could be used to purchase other products being sold at their department store, despite several brands’ explicit prohibitions on discounting their products. However, given consumer sentiment, the tactic was highly effective. Eventually, the brands caught on, and several insisted that mall operators cease the practice. Although we are thankful that some of the most prestigious brands have stopped that discounting method, the practice continues among some of the less influential (and less successful) brands in our competitor malls. When markets get tough, there is a return to “bare-knuckle” tactics, and we will not be immune from this. Assuming that rents will find parity among the landlords, the main competition will be how we can offer more value to tenants in our malls – primarily by driving more sales and foot traffic. This is what we will be focusing on in 2025.

## Prospects

The market consensus on China seems to be one of low sentiment and high uncertainty. There are no obvious catalysts for growth, but at the same time, there are no obvious reasons for the market to worsen. The current sentiment is driven by several factors: Primarily, the negative wealth effect from depressed real estate prices, a flagging economy with increasing unemployment and decreasing wages, an overhang from previous market upheavals (namely in the technology and education sectors and from COVID), and a lackluster stock market. The keen interest of the Chinese to travel abroad is making the domestic retail environment even tougher, with the primary beneficiary being Japan, although brands have also noted a mild uptick of Chinese tourists in Europe. For our prospects to look up, we need improvement on at least a few of these fronts. Among these, perhaps the easiest would be the stock market, with its event-driven reactions, followed by a return to consumption onshore, given the fickle nature of consumption patterns. Unfortunately, I do not see the impetus for real estate values to come back in a way that will provide a meaningful boost to homeowners’ sense of wealth in the near future; the impact on Chinese households’ net worth was perhaps too significant to recover quickly in the short term, not to mention the complexity of the

real estate market and its intertwining with upstream, downstream, and neighboring industries. The hangovers in technology and education sectors seem to be slowly working themselves out as policies start to show noticeable warming to them, but whether or not there is confidence that a similar crackdown will not happen again depends largely on the government's actions, along with broader economic indicators.

Despite these challenges, Chinese consumers are skipping along. I highly recommend that you visit one or more of our malls to get a more nuanced and realistic sense of the state of Chinese consumers and retail. Without seeing the dynamism, continued creativity, and increasing sophistication of consumers and retailers firsthand, it would be easy to fall prey to pessimism, which is not merited at this stage. On weekdays, even if malls look quiet in the afternoons, there are lines outside restaurants during mealtimes. Overall, in 2024, most of our malls saw foot traffic increase, with some by as much as 12%, though a few experienced slight declines, while mall occupancies were also mostly positive.

Considering our 2024 performance in the face of such challenges, I think it would be fair to target single-digit top-line rental growth in 2025, which is the expectation we have set for ourselves. I hope that you will be here mid-year and this time next year to continue this conversation.

As a final point, I wish to recognize the efforts of the incredible Hang Lung team – led by our CEO, Weber Lo – through such a challenging year. Although we did not face the same extraordinary operational complexities as those experienced during COVID, the trading environment has been unrelenting. The challenges were manifold, from finance, leasing, and marketing to legal and government relations. Navigating these markets takes high resilience, constant adjustment, and quick reflexes, not to mention the mental and organizational agility required to stay competitive. Thank you.

**Adriel Chan**

*Chair*

Hong Kong, January 24, 2025