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.

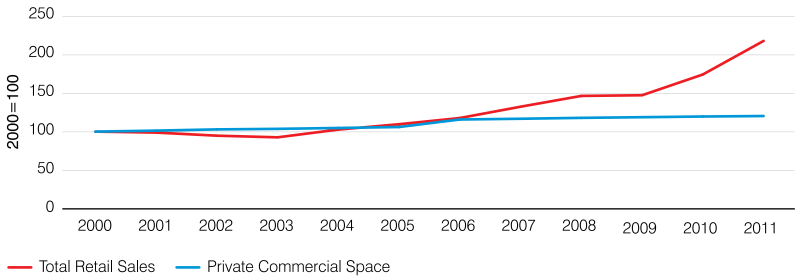
Demand has outstripped supply to result in unprecedented rentals – things will worsen as more inflows are on the cards

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



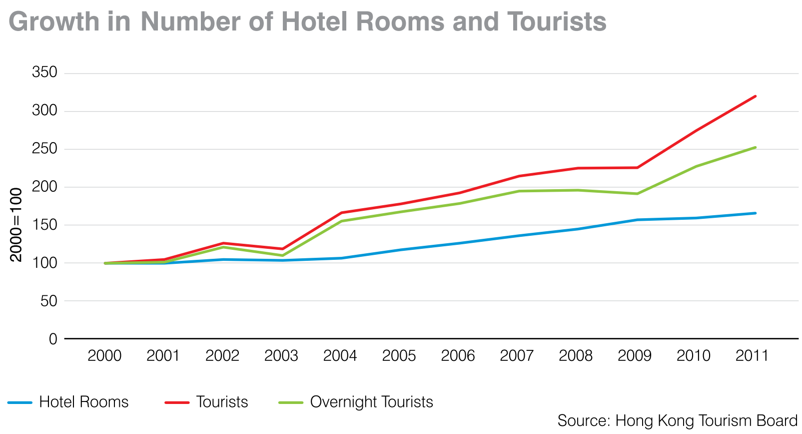
Source: HK Census Stat. Dept., Rating and Valuation Dept.

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

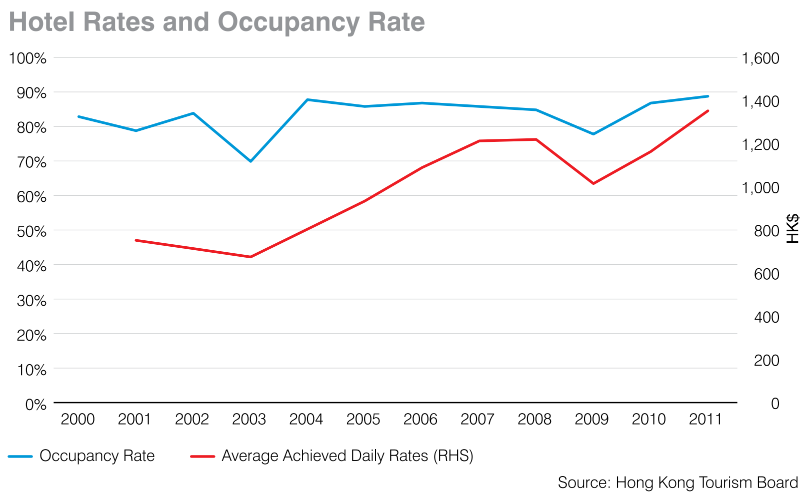
The situation with our hotels is hardly better – while overnight visitors surged 32% in 2010 and 2011 (visitor arrivals actually spiked 42% but the unavailability of rooms probably forced many tourists to stay in Macau or Shenzhen), the first two of the Golden 5 Years, marking a sharp acceleration of 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%



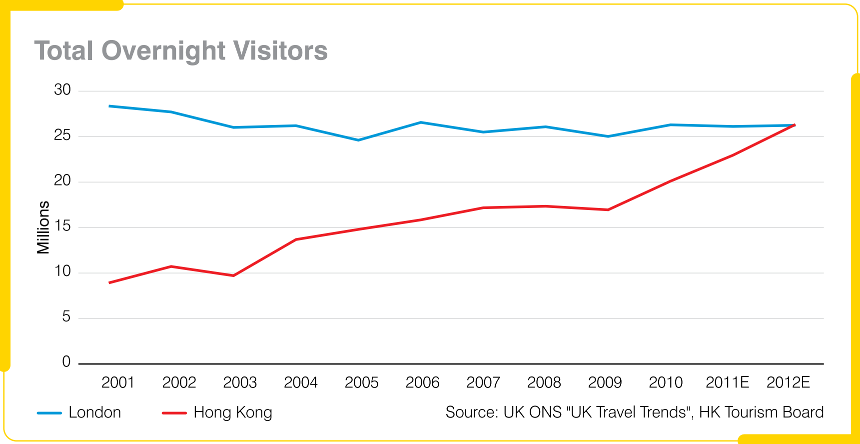
While overall hotel occupancy has remained at around 88% throughout the past decade, the relative absence of supply has translated to record all-grade blended daily rates of cHK$1,400 and represents c.45% jump from 2005 levels. It is likely that a shortage of hotel rooms and shopping spaces has conspired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



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.