CHAIRMAN'S STATEMENT

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GENERAL ECONOMY

Major geopolitical surprises marked the year 2016. Protectionism, populism and de-globalization sentiments spread across the globe to cast a long shadow over international trade and global collaboration.

Economic growth stayed subdued around the world. Before China could complete its economic rebalancing, the threat of a Sino-U.S. economic or even military confrontation started to raise its head. In the event the adversary escalates, Hong Kong will not be able to escape the crossfire. Furthermore, currency instability, sustained U.S. dollar/Hong Kong dollar strength, interest rate hike, Brexit, a much more nationalistic and protectionist U.S. administration, monetary policy divergence as well as refugee and terrorist issues around the world, cast elevated levels of uncertainty over the global outlook.

Nevertheless, China remains a crucial driver of growth and economic restructuring continues in full swing. While China's GDP growth rate cooled further to 6.7% in 2016, it remained among the fastest in the world. Adjustment to a "new normal" of slower but higher-quality growth continued. Services and consumption are now contributing more to growth than investment. The housing market heated up for most of 2016 and the government introduced new measures late in the year to dampen further overheating. That raised new uncertainty over trading conditions. Furthermore, Renminbi devaluation reduced the appeal of onshore assets and fueled offshore investment. On the other hand, it also stimulated higher domestic consumption and lower overseas consumption.

Hong Kong's economy grew by a modest 1.9% in 2016. The strong local currency, pegged to the U.S. dollar, continued to drive both locals and visitors to other overseas destinations. Total visitor arrivals declined by 4.5% to 56.7 million and total retail sales by 8.1% to HK$436.6 billion. The overall situation, however, appeared to have started to stabilize since mid-2016. That said, uncertainty over the retail and hospitality sectors remains.

BUSINESS PERFORMANCE - PROPERTIES GROWTH CONTINUES

Properties contributed to 92% of Group core profit (2015: 88%). Contribution from Hong Kong exceeded HK$10 billion, representing a growth rate of 35%, while that from the Mainland increased by 16% to HK$2.6 billion, despite the translation impact arising from Renminbi devaluation.

Performance of Investment Properties ("IP"), our largest contributor, remained solid and steady. High occupancy and positive rental reversion in our unique IP portfolio drove a 6% rise in IP core profit to nearly HK$9 billion.

Management and execution capabilities become increasingly crucial in today's retail environment. Our iconic retail landmarks in Hong Kong (led by Harbour City and Times Square) exhibited solid rental growth despite a retreat in overall retail sales amidst market softness. Critical mass, showcase effect, best-positioned destination retail and unrivalled productivity underpinned our malls' success. The value of our malls has been further underlined with a host of enhancement initiatives and innovative marketing programmes. Office performance continued to offer pleasant surprises.

Harbour City retains its position as one of the most compelling destinations and a global showcase for best-in-class retailers. Its critical mass underscores an unmatched competitive advantage. The two million square feet of contiguous mall space with a 550-yard retail frontage on Canton Road in Tsim Sha Tsui's most dynamic retail area makes it the most productive retail complex in Hong Kong and one of the most productive in the world. It anchors the six-million-square-foot "Greater Harbour City" cluster of the golden square mile covering high-traffic shopping, entertainment, dining and lifestyle. With a comprehensive range of retail selection across a finely-calibrated price point matrix (480 retailers), the iconic landmark provides unique and captivating "shoppertainment" experiences for its patrons. Harbour City remains the most preferred location for the world's best brands, as manifested in the consistently solid retailers' demand, even in a soft market. The introduction of a spate of differentiating, aspirational brands, as well as exquisite culinary offerings, extends the appeal to a wider range of customers. The upcoming 4-storey extension building at Ocean Terminal, coupled with other value-accretive initiatives underway, are set to throw a new spotlight on Harbour City and to strengthen the pole position of the destination retail landmark.

Times Square, among the most successful vertical malls globally, is even better-positioned upon completion of a value-accretive revamp in end-2015. The creation of a lifestyle hub on the 9th-10th floors and a kids zone on 13A floor pique shoppers' interests and drive repeated visits. Proactive measures including constant trade mix refinement and tenants reshuffling with new images opportunely tapped into shoppers' evolving demand, staying abreast of the latest trends in fashion and dining.

The Mainland IP portfolio is poised for growth with a pipeline of IFS developments. Against the backdrop of an over-expansion of brands, abundant new supply of malls and the advent of e-commerce to pose additional threats to traditional brick-and-mortar retail as well as a wave of consolidation in the industry, the overall retail market in China is immensely competitive.

Our Chengdu IFS, however, has outshone the competition with its location, critical mass and management. In particular, it has promptly positioned itself as a global showcase in the Western China metropolis for the world's coveted brands. The 200,000-square-metre destination mall houses an impressive portfolio of 300 global premium brands including over 100 debuts in Western China. Presence at Chengdu IFS has become a "must" for celebrated international retailers. Capitalizing on its most prime location at the busiest intersection in the city's busiest pedestrian shopping area (comparable to a combination of Hong Kong's Central CBD, Causeway Bay and Tsim Sha Tsui), Chengdu IFS achieved robust retail sales growth of 17% to RMB3.85 billion in 2016 . Raising the bar for commercial developments in the city, it won the most prestigious global award "VIVA Best-of-the-Best Design and Development Award" presented by the International Council of Shopping Centers in 2016, the first shopping mall in China receiving such global acclaim. Niccolo Chengdu, our first "Niccolo" hotel, has also rapidly emerged as the market leader for room yield in just one year since opening.

CHAIRMAN'S STATEMENT

The performance of Chengdu IFS sets a good model for other future IFS developments and creates synergy. The upcoming retail-oriented IFS complexes in Chongqing and Changsha are set to mirror the success of Chengdu IFS, as evidenced by their promising retail pre-leasing status. Currently, over 90% and 85% of the respective retail floor plates at Chongqing IFS and Changsha IFS are either committed or nearly committed to key tenants. The fact that our tenants come with us to these new markets bear testimony to their confidence in our value creation capability. Targeted for opening in 2017, the new mega malls in Chongqing and Changsha will tap the huge experience-based consumption markets in the regions.

Changsha Times Outlet, aiming to replicate the success of its 'sister' in Chengdu, celebrated its grand opening in November 2016.

Core profit from Development Properties ("DP") in 2016 nearly tripled to approach HK$4 billion, thanks to record sales in Hong Kong and the Mainland of HK$40 billion and record revenue recognition of HK$37 billion.

In China, favourable market conditions helped to lift the Group's attributable share in contracted sales to a record RMB31.4 billion, 21% over 2015 and 31% above target. A disciplined approach to land bank replenishment continued to be practised, focusing on first-tier and top second-tier cities.

Back to Hong Kong, the Group's prestigious Mount Nicholson nestled on the Peak met with excellent demand. A total of 7 villas and 19 luxurious apartments, out of 19 villas and 48 apartments in total, were sold for combined proceeds of HK$11.6 billion or an average of HK$80,400 per square foot year-to-date. In particular, two adjoining apartments and one villa were sold at over HK$100,000 per square foot each, breaking the record price for Asian homes on a per unit basis.

A strategic review started in early 2016 led to the conclusion to exit the Communications, Media & Entertainment segment completely. Our entire equity interest in Wharf T&T was disposed in November 2016 at a consideration of HK$9.5 billion. No agreement to dispose of i-CABLE has been entered into and the current funding commitment would be neither increased nor extended upon expiry.

A study has commenced to consider the possibility of separately listing some of the Group's IP assets by way of introduction achieved by a distribution in specie to shareholders in the Company. A simple segregation may provide investors with more and better choice. A proposal to evaluate all pros and cons will be submitted to the Board for consideration as soon as practicable.

FINANCIAL RESULTS

Group core profit increased by 25% to HK$13.8 billion, thanks to a robust 31% growth from properties. Taking into account the net surplus from IP revaluation and other exceptional items including the HK$7.3 billion gain arising from the Wharf T&T disposal, profit attributable to Shareholders was HK$21.4 billion and earnings per share were HK$7.07. With the acquisition of Wheelock House in Central and further Mainland completions, IP assets expanded by 3% to HK$319.3 billion, driving total assets to HK$443.8 billion. Book net asset value increased to HK$316.8 billion (or HK$104.48 per share) net of decreases in exchange and investment reserves.

Net debt at year-end decreased by HK$23.4 billion to HK$23.8 billion. Gearing ratio further dropped to 7.3% (2015: 14.9%). Net cash inflow on and off balance sheet totaled HK$31 billion, after dividends but before financing activities and the acquisition of Wheelock House for HK$6.2 billion.

In 2016, Wharf became the first Hong Kong property developer to have obtained approval to issue panda bonds on the Mainland, with an aggregate amount not exceeding RMB20 billion. The first tranche of RMB4 billion 3-year medium term note was issued in October with an oversubscription of three times.

In lieu of a final dividend, a second interim dividend of HK$1.57 per share (2015: HK$1.35) has been declared to bring the total dividend for the year to HK$2.15 per share (2015: HK$1.90).

BUSINESS-IN-COMMUNITY

The Group's long-standing mission of "Building for Tomorrow" extends to Wharf's "Business-in-Community" pursuit.

Project *WeCan*, our flagship school improvement programme launched in 2011, has scaled up to 51 deserving schools, supporting over 43,000 students who are disadvantaged in learning in Hong Kong. A number of enrichment activities including company visits and job tasting have been arranged to widen student's exposure, nurture their confidence and facilitate personal fulfillment. The "Young Innovators Bazaar" at Plaza Hollywood has become an annual gala occasion and is gearing upwith over 1,000 students from 41 Project *WeCan* participating schools taking the lead to run the vast assortment of stalls in this fair in 2016.

The Group continued to support Hong Kong Ocean Day 2016 in October to participate in an underwater clean-up dive around Sharp Island in Sai Kung with professional divers. Also, about 200 Project *WeCan* students joined the eco-tour and scuba-diving that raised their awareness of marine and coastal conservation.

These achievements would not have been possible without the support of our corporate partners and our staff volunteers from various business units. Here, I wish to convey my warmest gratitude for their generous contribution and gift of time to serve the community.

The Wharf Hong Kong Secondary School Art Competition and Wharf Architectural Design Internship Programme have gained traction over the years. Wharf held the Art Competition annually to boost young people's creativity and interests in the aspect, with an ultimate goal of promoting local art development and nurturing young art talents. The top 18 finalists are eligible to apply for The Wharf Art Scholarship, which supports students financially in undertaking art-related bachelor programmes in local or overseas institutions. Currently, 11 students have been awarded scholarships to study creative arts and related subjects in renowned institutions around the world.

The Wharf Architectural Design Internship Programme provides local students with placement opportunities in renowned architectural firms in different countries including France, Germany, Japan, Switzerland and the United Kingdom. 12 outstanding architectural postgraduates have benefitted from the scheme since 2011.

We also published our second standalone CSR Report with an expanded scope of our stakeholder engagement in accordance with the Global Reporting Initiative (GRI) G4 sustainability reporting guidelines.

CHAIRMAN'S STATEMENT

OUTLOOK

2017 is set to be a year of riding out global economic and political shocks as the geopolitical surprises in 2016 continue to unfold. In particular, Sino-U.S. relations, including the heightened trade tension and South China Sea conflicts, will be a critical issue for Hong Kong in the coming months. Various external risks further cloud the outlook for 2017. These include currency volatility, the extent of Brexit and European instability, various general elections in Europe, the new U.S. administration, the prospect of U.S. interest rate rises, volatile fund flows caused by monetary policy divergence, and capital outflows from China exacerbated by RMB devaluation.

Against this backdrop, Asia may need to overcome diverse pressure from a stronger U.S. dollar and greater capital outflow. "Competitive devaluation" will be another potential development to watch. Looking forward, more fiscal stimulus that the world needs would certainly help.

China is on course to gradually shift to more consumer-oriented and services-led. Although the rising trade tension and a possible trade war may pose a new challenge for the country, the world's second largest economy on our doorstep is still a global powerhouse and will continue to buttress Hong Kong. GDP growth is on track to meeting an annual target of at least 6.5% until 2020. This, together with the commitment to double per-capita income by 2020 over 2010 levels, is still of primary importance. It will not only accelerate the pace of economic restructuring, urbanisation and wealth accumulation but also generate immense property and consumption demand for decades to come. Furthermore, the Belt and Road Initiative may present tremendous new potential, though new risks are inevitable in exploring new markets. We must open our minds to welcome the boundless opportunities that this exciting new era may bring us.

Hong Kong, being the world's leading super service platform, is best positioned to meet the enormous demand stemming from China's urbanization, service sector intensification and consumerism. Our city, however, is set to see its fair share of uncertainties in 2017 including possibly higher interest rates, political and economic tensions as well as a new Chief Executive administration. The local economy is projected to expand by 3% per annum from 2018 to 2021.

The retail and hospitality industries, despite signs of stabilisation in recent months, may remain soft. The government has stepped up efforts in achieving a more balanced inbound visitor portfolio to resuscitate the industries. That initiative has proved effective and may help shape the visitor trend. Moreover, construction of the Hong Kong-Zhuhai-Macau Bridge and the Guangzhou-Shenzhen-Hong Kong Express Rail Link is underway, which may facilitate the social and economic interactions with the metropolitan cities across the country, capturing new opportunities for our retail and personal services platform.

The volatile Yen and the constant devaluation of the Euro and pound in recent years are drags on the retail sector in town. Price harmonization of international brands continues, which may help mitigate the adverse impacts.

Last but not least, we have remarkable assets in prime locations. Our proven management and execution track record has earned trust and confidence of tenants, shoppers and investors in our destination retail properties with unique showcase effects and productivity. This is underscored by the consistently solid tenant demand and positive lease renewals, which buttress business resilience and continued growth.

On behalf of all Shareholders and my fellow directors, I wish to express my sincere gratitude to all customers and business partners for their unwavering support, and to all Staff for their professional competence, commitment and dedication throughout the year.

Wharf weathered plenty of ups and downs with its sturdy foundation in the past. With the macro uncertainties ahead, I, together with the seasoned management team, have full confidence in steering the Group towards riding over the challenges in a changing world.

Stephen T H Ng
Chairman and Managing Director
Hong Kong

9 March 2017