

MANAGEMENT DISCUSSION AND ANALYSIS



Regenerating our dilapidating built environment is a race against time. The task is made even more challenging by financial constraints and the various regulatory regime which could not meet current and future development needs.

**We therefore have to
constantly reinvent ourselves to
find creative and smart solutions to
turn the finite (resources)
into the infinite (possibilities) and
achieve seemingly impossible goals.**

Our greatest challenge is the limited capacity for redevelopment, as urban districts are already densely populated with fully utilised plot ratios, making redevelopment projects financially unviable. Possibilities or opportunities will, however, present themselves if we think out of the box and adopt an innovative approach to the planning process, making the best use of latest technologies to maximise development potentials.

Other than the physical and planning constraints facing URA, another major challenge is the need to remain financially sustainable. Faced with market volatilities, we need to anticipate and minimise potential future risks. One solution is to build up planning reserves through Preliminary Project Feasibility Studies which will help identify potential renewal projects to build up a project reserve. Another initiative is the use of advance tendering for future projects; by this means, the acquisition of one project will match the timing of the tender award of another within the same financial year, as a way of fund hedging.

Challenges

Volatile Economic and Operation Environment

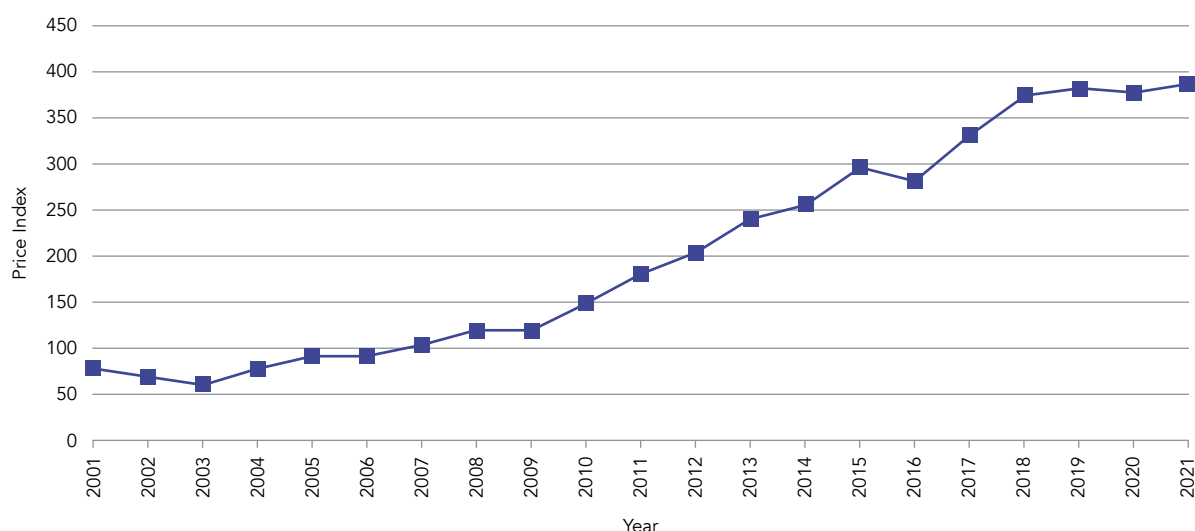
The persistent and unpredictable development of COVID-19 since early 2020 has adversely affected both global and local economies. It compounded the lagging effects of the Sino-US relationship tension that had been weighing down the overall financial situation. All of which have contributed to the economic recession in most part of 2020 and increased volatility in the property market, bearing implications on URA's financial stability.

The pandemic has posed challenges to URA's operation at the same time. In terms of project commencement, three redevelopment projects originally scheduled for commencement in the fourth quarter of 2019/20 were deferred to 2020/21 to reduce the risk of infection through interpersonal contacts during freezing surveys. A few statutory approval processes of URA's ongoing projects were delayed due to temporary suspension of Government offices and deferral of public hearings/consultations. Extra efforts and resources had to be mustered to minimise the adverse impacts on our projects, especially in terms of financial viability.

Notwithstanding the short term fluctuations, the property market has continued to follow a largely upward path since 2003, and has seen an about six-fold surge in prices for all classes of accommodation in the private domestic market (see Figure 1). With the blooming property market, the URA has been acquiring building stock at soaring prices, making it more vulnerable to market downturn. Meanwhile, the URA is obliged to bear higher development costs by acquiring properties under the 'seven-year rule' and is subject to ex-gratia payments markedly higher than those incurred by private sector developers. Moreover, the URA is required to commence acquisition as soon as possible after authorisation by the Secretary for Development or approval by the Chief Executive in Council. This practice exacerbates the risk of 'buy high, sell low' since the URA lacks flexibility to slow down the acquisition process in view of unfavourable market conditions.

To mitigate the risk, the URA has explored the possibility of advanced tendering for projects, such that the tender award of one project will time with the acquisition of another within the same financial year as a way of fund hedging. Oak Street/Ivy Street Project (YTM-011) was selected to pilot the advanced tendering and the response was promising. URA will continue to explore suitable project(s) for advanced tendering.

Figure 1:
Private Domestic Price Index
2001 – 2021 (up to June) – All Classes*



* Source: HKSAR Government, Rating & Valuation Department, Hong Kong Property Review Monthly Supplement, July 2021

Constraints in the Built Environment

Hong Kong is characterised by its population density, congested road traffic and a high density mix of old and new buildings in close proximity of each other. The situation is even more profound in older urban districts with a large cluster of dilapidated buildings. Besides, the existing building bulk of many URA projects, particularly those commenced in recent years, is almost close to the maximum permissible plot ratio under the prevailing planning regime resulting that less than half of the commenced projects could provide a high return on plot ratio gain upon redevelopment. This necessitates the URA to explore restructuring and replanning opportunities to optimise land use and maximise the planning gains of our urban renewal initiatives. Through restructuring and replanning, the development potential of some old Government, Institution or Community (G/IC) facilities, temporary government land allocations and roads in the project sites could be unleashed to enhance the overall development potential of the projects whilst G/IC or open space provisions will be raised in terms of both quality and quantity.

Accelerating Pace of Urban Decay

In view of the increasing pace of building deterioration and ageing, the importance of building rehabilitation and preventive maintenance cannot be underestimated.

Rehabilitation, as one of the two URA's core businesses, is a linchpin of URA's efforts to tackle the problem of urban decay in Hong Kong. Through proper maintenance, the service life of buildings can be extended thus reducing the pressure on redevelopment, and thereby relieving the financial burden on URA. According to the Study on New Strategy on Building Rehabilitation, while repairing and maintaining one's building has always been the responsibility of building owners, the lack of awareness on building maintenance, financial reserve and technical support to organise building rehabilitation works among owners have become major obstacles towards proper and regular maintenance. The URA must press on with our rehabilitation efforts to help building owners overcome these hurdles through proactive and targeted measures.

Additional Government Initiatives

As detailed in the Operating Review, a number of Government initiatives have been entrusted to the URA in recent years, namely the active provision of Starter Homes (SH) in URA's redevelopment projects, and assisting non-governmental organisations to develop transitional housing and redevelop community facilities on their sites under the 'Single Site, Multiple Uses' model. Implementing these new initiatives for the Government would inevitably incur additional cost (e.g. provision of SH units at discounted price) thus putting pressure on the cash flow and financial well-being of the URA. Given our resource constraints, it is therefore important for the URA to strike a balance between the sustainable development of our core businesses in urban renewal and delivering Government initiatives as part of URA's social responsibility. Possible support from the Government, in terms of both policy and resources, may be required to enable the URA to optimise our resources to deliver Government initiatives without jeopardising our urban renewal missions.

Opportunities

Adopting a Holistic and Forward Looking Approach

The URA has strived to pursue a holistic approach to optimise the planning benefits from our urban renewal efforts, by shifting from a traditional project-based approach to a more forward looking and district-based planning-led approach.

Two important strategic studies, namely Yau Mong District Study (YMDS) and Study on New Strategy on Building Rehabilitation (NSBR), were envisaged to establish new integrated business directions and executions embracing redevelopment, rehabilitation, preservation, revitalisation and retrofitting. The Preliminary Project Feasibility Studies (PPFSs) introduced in 2018/19 would further help identify the '5Rs' urban renewal projects with replanning and restructuring opportunities.

With a view to promptly responding to market fluctuations or new Government initiatives to support various needs of Hong Kong, the URA has built planning and project reserves so that suitable renewal projects can be timely proposed to make the best use of our financial resources for urban renewal. PPFSs and YMDS have formed the basis of the planning reserve. Based on findings from the ongoing PPFSs in selected action areas and early projects identified from YMDS, 'Potential Projects' have been selected as project reserve items for timely inclusion into the URA's Business Plans/Corporate Plans with due regard to the then URA's financial position, market situation, availability of resources required for rehousing and Government's support.

In addition, the new preliminary framework for implementing the Demand-led Pilot Scheme as a result of its effectiveness review is envisioned to create greater planning impact under the planning-led approach. Given the chance to understand owners' needs through a survey system, the URA will be able to bring bigger planning gains to the community or neighbourhood by incorporating them into the urban renewal project plans.

Leveraging Smart and Innovative Technologies

The URA has strived to embrace the latest technologies to optimise our operation process in order to facilitate urban renewal. The Urban Renewal Information System (URIS) being developed in-house contains a suite of location intelligence tools which enable spatial analytics, data mining and 3D visualisation of the mining results. With over 100 sets of 2D/3D demographic and geographic data, the URIS is envisaged to form the basis of developing digital twin solutions to facilitate data-driven decisions integrating the URA's '5Rs' strategies. The URA received the Special Achievement in GIS¹ (SAG) Award, in recognition of our efforts to set new precedents of applying GIS technology with the development of URIS that standardises and consolidates a wide range of spatial data from various sources for supporting a people-centric and data driven urban renewal approach.

Meanwhile, the URA continues to adopt Building Information Modelling (BIM) in project design and construction as a common platform for communication and collaboration among contractors and consultants in areas of data validation, clash analysis and implication assessments of design change, etc. during project implementation. The use of BIM has been further extended to facility management. The first BIM-Facility Management (BIM-FM) system for 618 Shanghai Street was completed in the fourth quarter of 2019 with an aim to enhance the efficiency of property management of the project. The BIM-FM platform has been further applied to eResidence and the Central Market.

The URA also intends to expand our smart initiatives not only in buildings but also in the wider district area in a bid to pave ways for building a 'Smart City'. A study on the smart use of underground space and smart provisions of city infrastructural facilities in Kowloon City area was completed in early 2021. Some of the recommendations will be incorporated in the development agreements of Kowloon City projects for implementation.

Promulgating a Culture of Preventive Maintenance

To tackle the problem of a lack of building rehabilitation awareness among owners, the URA has formulated a strategy focusing on the promotion of good practices on preventive maintenance and voluntary maintenance fund through collaborations with various stakeholders, such as professional institutes and practitioners.

¹ GIS stands for Geographic Information System

In 2020/21, the URA devised an action plan for the promotion strategy and started implementing the action items. To assist building owners to carry out preventive maintenance, the URA has compiled a maintenance manual template for conducting a trial on URA's rehousing blocks and self-developed projects. The trial aims to test the practicability of the template and help compile the guidelines for formulating the maintenance plan and funding arrangement. In addition, the URA has applied the design of a maintainability checklist in URA's self-developed projects. The application will be extended to other joint-venture projects to test the practicability of the guidelines before promoting to private buildings.

To implement 'stakeholder-based' promotion, the URA has approached the Property Management Services Authority to advocate preventive maintenance to property management practitioners through incorporating the relevant messages into training materials and guidelines. Three of the property management training course providers have confirmed to adopt the training materials recommended by the URA. The URA has also approached a professional institute and four large property management companies to explore the practicality of the preventive maintenance measures proposed by the URA. With these promotions and assistance in place, the URA looks forward to boosting confidence among building owners in carrying out preventive maintenance, so that the ageing of buildings can be slowed down.

Retaining Productivity Amid COVID-19

The COVID-19 pandemic has brought abrupt changes to the work environment across the globe demanding swift adjustments at the organisation level, and the URA is no exception. As valuable asset to the URA, our staff have once again shown their unremitting efforts in overcoming challenges and ensuing business operation by continuing to seek opportunities while overcoming various constraints. To tide over the disruptions caused by COVID-19, we have implemented a number of initiatives. Among these initiatives are making remote desktops available for all staff to facilitate the Work-From-Home arrangement, and replacing physical meetings and briefings by teleconferencing, webinars and live streaming for both internal and external events/meetings.

While physical contact is inevitable during the statutory freezing surveys immediately conducted after project commencement, we continue to apply technology to maintain the productivity and efficiency of our workforce. A mobile application has been developed and remote webcams were provided to minimise physical contacts between URA staff and the residents during surveys with residents. Furthermore, the URA has developed its own Health Code to send out alerts of COVID cases in nearby buildings in a bid to further safeguard the health of our staff and affected tenants in our redevelopment project (details as described on page 61 of the Corporate Sustainability Chapter for details).

Outlook

Operating under the Urban Renewal Authority Ordinance and guided by the Urban Renewal Strategy, the URA is committed to implementing urban renewal in a sustainable and forward looking manner to support the development of Hong Kong and improve the living conditions of residents in old districts. While the city's rapidly ageing building stock remains a daunting task and challenge to overcome at present, the URA will press on to pursue the overarching goal of the holistic approach embracing our '5Rs' to maximise benefits of urban renewal. Findings of the YMDS and NSBR study will underpin the future direction and implementation of our urban renewal works. The URA's future trajectory will continue to follow a planning-led approach through efforts to build up its planning and project reserves for '5Rs' projects, with an emphasis on the optimisation of community benefits and social impacts. In addition, conscientious efforts will be devoted to the promotion of preventive maintenance for building rehabilitation in order to curb the pace of urban decay.

As the URA ventures beyond the 20th anniversary, we endeavour to find smarter solutions to Hong Kong's urban renewal problem by harnessing innovative technologies. Apart from focusing on our core businesses of redevelopment and rehabilitation, the URA will carry on to support the Government in supplying more affordable housing for the general public. Although the URA currently enjoys a strong cash position, we will continue to uphold the core principle of prudent financial management, especially given the recent downturn of the economy and the uncertain outlook of the future property market, while balancing the enduring risks of high acquisition costs. In the coming year, the URA will continue to strive towards a sustainable and holistic urban renewal programme aiming to generate greater benefit for the community at large.

Financial Review

(I) Review of 2020/21 Results

(A) Revenue

The revenue for the year ended 31 March 2021 was \$3,439 million, which comprised upfront payment from a tendered project, share of surplus from joint development projects and proceeds from flat sale. The amount was higher than the revenue of \$2,107 million in 2019/20 by \$1,332 million.

The upfront payment in 2020/21 of \$913 million was comparable to that in 2019/20 of \$883 million. There was only one project tendered in both years, namely Tonkin Street / Fuk Wing Street with site area of 1,268 m² in 2020/21 and Hang On Street with site area of 865 m² in 2019/20.

The share of surplus from joint development projects of \$426 million in 2020/21 (2019/20: \$1,185 million) was revenue from projects where the sales proceeds exceeded the thresholds stipulated in the development agreements.

The revenue from sale of properties of \$2,100 million in 2020/21 largely related to the residential units at eResidence sold at discounted prices under the Starter Homes Scheme.

(B) Other Income

Of the \$265 million (2019/20: \$479 million) in other income for 2020/21, \$195 million (2019/20: \$396 million) were interest income from bank deposits and fixed income investment products, with an average yield of 1.62% p.a. (2019/20: 2.61% p.a.). The lower average yield reflected the gradual decrease in interest rates over the year.

Other income also included rental income of \$66 million (2019/20: \$98 million) from certain properties retained by the URA. The decrease in rental income in 2020/21 was primarily attributable to enhanced rent relief measures for the Authority's domestic and commercial tenants to help them tide over financial difficulties amid COVID-19 pandemic.

(C) Administrative Expenses

Administrative expenses for 2020/21 of \$593 million (2019/20: \$515 million) mainly covered staff costs, accommodation costs and office expenses. Cost control measures were implemented whenever possible to minimise administrative expenses.

To cope with the continuous expansion of urban renewal activities, including commencement of four redevelopment projects in 2020/21 and implementation of two new building rehabilitation subsidy schemes, namely Lift Modernisation Subsidy Scheme and Building Maintenance Grant Scheme for Needy Owners, the staffing level was increased from 557 at 31 March 2020 to 650 at 31 March 2021. Of the 650 staff, 51 (31 March 2020: 27) were employed on contracts of less than three years.

(D) Provision for Impairment on Properties and Committed Projects

Based on the accounting policy detailed in Notes 2(h) and 2(n) to the financial statements, provision for impairment on properties and committed projects of \$101 million was written back in 2020/21, as a result of the changes in the development plan of some projects and adjustment to the estimated project costs.

(E) Surplus for the Year

For the year 2020/21, the URA recorded a net surplus of \$150 million, showing an increase of \$32 million as compared to \$118 million for 2019/20. The major contributing factors to the increase were (a) higher surplus from a tendered project and (b) the write back of provision for impairment on properties and committed projects during the year.

(II) Financial Position at 31 March 2021

(A) Properties Under Development

Properties under development before provision for impairment of \$33,287 million as at 31 March 2021 (31 March 2020: \$33,494 million) was maintained at a high level. This sum represented the acquisition and development costs of 15 projects under various states of implementation, out of which Kowloon City Projects and Kwun Tong Town Centre Project accounted for 78% of the total value.

The aforesaid value was off-set against the cumulative provision for impairment totalling \$724 million (31 March 2020: \$1,221 million), resulting in a net value of \$32,563 million (31 March 2020: \$32,273 million). The increase in the net value was mainly due to continued acquisition of Kowloon City Projects during 2020/21. It was off-set by (a) Tonkin Street / Fuk Wing Street Project, which was already tendered; and (b) certain projects, including eResidence and Central Market, which construction works were completed during the year.

(B) Total Liquidity

As at 31 March 2021, the URA's total liquidity, including cash, bank deposits and debt securities investments, was \$9,618 million (31 March 2020: \$11,067 million).

The URA placed the surplus cash on deposits with a number of financial institutions, and also invested in fixed income products of the required credit rating in accordance with the investment guidelines as approved by the Financial Secretary with capital preservation as the priority.

The liquidity position, off-set by the borrowings of \$1,097 million (31 March 2020: \$1,796 million) mentioned in paragraph II (C) below, resulted in the net liquidity position including the securities holdings as at 31 March 2021 of \$8,521 million (31 March 2020: \$9,271 million).

(C) Debt Securities Issued

The URA is rated AA+ by Standard & Poor's Rating Services. As at 31 March 2021, the outstanding debt securities issued by the URA was \$1,097 million under the Medium Term Note (MTN) Programme.

(D) Net Asset Value

The URA's net asset value as at 31 March 2021 was \$47,242 million (31 March 2020: \$47,092 million), representing the Government's capital injection of \$10,000 million (31 March 2020: \$10,000 million) and an accumulated surplus of \$37,242 million (31 March 2020: \$37,092 million).

The financial summary of the past ten years is described on page 109 of this Annual Report.

(III) Capital Injection and Tax Exemption

Following approval by the Finance Committee of the Legislative Council on 21 June 2002, the Government injected \$10,000 million of equity capital into the URA in five tranches of \$2,000 million each over a five-year period from 2002/03 to 2006/07. The Government continues to exempt the URA from taxation.

(IV) Waiver of Land Premia by the Government

The Government waives the land premia for redevelopment sites granted to the URA. For 2020/21, the land premia waived by the Government on a land grant amounted to \$17 million. Since May 2001, a total of 45 land grants have been waived in respect of all the tendered projects with aggregate land premia totalling \$19,699 million.

Without this waiver, the URA's net surplus for 2020/21 of \$150 million for the year would have been lowered by \$17 million to \$133 million; its accumulated surplus as at 31 March 2021 would have been lowered by \$19,699 million to \$17,543 million; and its net asset value as at 31 March 2021 would have been decreased to \$27,543 million.

(V) Financial Resources, Liquidity and Commitments

As at 31 March 2021, the URA's net liquidity position totaled \$8,521 million. At the same date, the URA's outstanding commitments to the commenced projects, together with the construction cost on projects based on the valuation carried out by the URA's in-house professionals, were estimated at \$7,060 million.

In addition to the MTN Programme mentioned in paragraph II (C) above, the URA also maintained uncommitted credit facilities with major banks in Hong Kong. The external funding and credit facilities ensured the URA would have sufficient financial resources to carry out its urban renewal programme as planned.

Individual projects, with various development potentials, are tendered out at different times during property market cycles. Subject to the market conditions prevailing at the time of tender submission, the upfront payments may be higher or lower than the URA's acquisition costs. As at 31 March 2021, the total costs of properties under development, excluding provision for impairment, was \$33,287 million. The value of properties under development is exposed to the risk of property price fluctuation. Should the projected future value of the properties under development is lower than its actual/estimated acquisition and clearance costs, impairment loss will be recognised in the URA's books.

It is estimated that a total cash outlay of about \$66,000 million, excluding operational overheads, will be required in the coming five years to meet both of the URA's currently outstanding commitments and its forthcoming cash outlay for the implementation of the projects. This amount covers the URA's work in redevelopment, rehabilitation, preservation, revitalisation and retrofitting. The projected cash outlay will be met by future upfront payments from project tenders, share of surplus sales proceeds from joint development projects and proceeds from sale of properties in the corresponding period. To ensure that the URA has sufficient funding available for its urban renewal works, it will conduct a financing strategy study to explore different financing options.

Operating in a 'new normal' environment after the outbreak of COVID-19, the URA will continue to manage its businesses in an agile manner and monitor its financial position closely, with an aim to accomplishing its urban renewal missions while maintaining long-term sustainability.