(I) Review of 2011/12 Results

(a) Revenues

Revenues for the year ended 31 March 2012 amounted to $3.7 billion (2010/11 $3.6 billion), a minor improvement of $0.1 billion or 3% over the last financial year which was mainly attributable to the increase in share of net surplus from an URA project under owner participation scheme and the shares of sales proceeds from jointly controlled development projects with the proceeds exceeding certain thresholds stipulated in the development agreements. The increase was a result of a generally favourable property market prevailing since early 2009. Furthermore, the thresholds were set years ago when the URA arranged the relevant revenue tendering exercises in a market where property market values were relatively lower. The projects contributed to the surplus during the year included Island Crest in Sai Ying Pun, Florient Rise in Tai Kok Tsui, Vision City in Tsuen Wan and Hanoi Road in Tsimshatsui, with development or participation agreements executed in 2005, 2004, 2002 and 1998 (by the Land Development Corporation, the predecessor of the URA) respectively. One redevelopment project site, namely Chi Kiang Street / Ha Heung Road with 931 m^2 in total area, was tendered and awarded during the year. In 2010/11, two sites with a combined total area of 2,710 m^2 were tendered and awarded, which explained the lower aggregate value of upfront amounts reported by the URA in 2011/12.

(b) Other net income

Of the $190 million (2010/11: $72 million) included as other net income for the year, $153 million (2010/11: $49 million) was interest income earned from bank deposits, with an average yield of 1.68% p.a. (2010/11: 0.90% p.a.). There were also gains of $12 million (2010/11: $12 million), principally from funds managed by the investment manager with a gross yield of 1.27% p.a. (2010/11: 1.61% p.a.).

(c) Administrative expenses

Administrative expenses mainly covered staff costs, accommodation costs and depreciation charges. Administrative expenses before depreciation for the financial year was $278 million (2010/11: $269 million). The slight increase was largely due to the headcount growth required to meet the workload of the URA's planned projects and the new initiatives under the Urban Renewal Strategy (URS). The depreciation charge for office capital expenditure was $19 million (2010/11: $20 million) for the financial year 2011/12.

To cope with the expansion of urban renewal activities, including the increased scope of rehabilitation works arising from Operation Building Bright which will be implemented over a number of years and the Integrated Building Management Assistance Scheme which was launched on 1 April 2011 to replace principally the previous material incentive scheme, the staffing level increased by 26 from 423 in 31 March 2011 to 449 in 31 March 2012. Of the 449 staff, 96 (31 March 2011: 97) were employed on contracts of less than three years in duration. It is expected that the headcount will increase further to cope with the planned expansion in future years of the building rehabilitation works including the technical assistance and financial subsidy provided to the building owners for the first inspection under the Mandatory Building Inspection Scheme.

(d) Provision for Urban Renewal Trust Fund (URTF)

In one of the new initiatives under the URS, the URA is committed to providing $0.5 billion funding as an endowment for the establishment of the URTF. This was recorded as a provision in the account of 2010/11 and the actual contribution was made by the URA to the URTF during the year. The URS also requires the URA to provide additional funding in the future to the URTF.

(e) Write back of / provision for impairment on properties and committed projects

The URA's properties and committed projects are valued by in-house professionals at the end of each financial year. Based on its accounting policy detailed in Notes 2(g) and 2(n) to its financial statements, a net provision for loss aggregating $0.6 billion was made in this financial year. The provision for loss for the year mainly covers losses on Pak Tai Street / San Shan Road project which started acquisition during the year and additional provision for loss made for Kwun Tong Town Centre project due to general increase in land assembly costs; offset by the write-back of provision for loss for Sai Yee Street project and other projects resulting from changes in development plans and approaches to the projects, and in the projects' respective assessed development values as compared with those a year ago at 31 March 2011.

(f) Operating surplus for the year

For the year ended 31 March 2012, the URA recorded a net operating surplus of $2.6 billion as explained in paragraph (I) (a) above, reflecting an increase of $0.4 billion or 18% compared to the $2.2 billion net operating surplus reported in 2010/11.

(II) Financial Position at 31 March 2012

(a) Properties under development

The value of "Properties under development" as at 31 March 2012 was at a historically high level of $19.2 billion (2010/11: $15.9 billion), representing the acquisition costs for projects for redevelopment or preservation purposes at various stages of implementation, comprising three projects under acquisition; five projects pending completion of resumption process; one project with over 90% ownership of interests acquired pending reversion to the Government; five projects with ownership reverted to the Government pending final clearance; and two projects with site clearance and pending tendering process. The aforesaid cost was set off against the cumulative provision for loss on nine projects of $5.6 billion (2010/11: $5.2 billion for nine projects) giving rise to a net cost of $13.6 billion (2010/11: $10.7 billion). The increase in the net cost reflects mainly the higher number of projects now being implemented and the generally higher levels of acceptance of offers for acquisition of properties in these projects. During 2011/12, the URA commenced acquisition of three redevelopment projects, two located in Ma Tau Kok and another one in Shau Kei Wan.

(b) Cash and bank balances

As at 31 March 2012, the URA's cash and bank balances and the fair value of the funds managed by the investment manager totaled $10.6 billion (2010/11: $7.1 billion). The increase in bank balances of $3.5 billion from last year was substantially due to the receipts, in 2011/12, of the balances of the upfront payments of the projects tendered in 2009/10 and 2010/11.

The URA placed its surplus cash on short-term deposits with a number of financial institutions and invested in HK$ and RMB bonds of the required credit rating in accordance with the URA's investment guidelines, which have been approved by the Financial Secretary with capital conservation as the priority. The investment manager who manages a portion of the surplus funds also adhered to the same guidelines.

Off-set by the borrowings of $1.7 billion mentioned in paragraph II (c) below, the net cash position including the fair value of the financial assets at 31 March 2012 was $8.9 billion (31 March 2011: $5.6 billion).

(c) Debt securities issued

In December 2010, in conjunction with the upgrading of the Government of HKSAR's rating, the URA's rating was also adjusted by Standard & Poor's (S&P) to AAA from AA+. This rating was reaffirmed after an annual review in February 2012.

As at 31 March 2012, the debt securities issued by the URA was $1.7 billion. In April and July 2012, additional debt securities totaling $1.8 billion were issued, a substantial part of which would be used to refinance the debts due in 2012/13.

(d) Net assets value

The URA's net assets value as at 31 March 2012 was $21.8 billion (31 March 2011: $19.2 billion), representing the Government's capital injection of $10 billion (31 March 2011: $10 billion) and an accumulated surplus from operations of $11.8 billion (31 March 2011: $9.2 billion).

The financial highlights of the past ten years are summarized on page 85 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 billion of equity capital into the URA in five tranches of $2 billion over a five-year period from 2002/03 to 2006/07. The Government has exempted the URA from taxation.

(IV) Waiver of Land Premia by the Government

Under the URS, the Government waives the land premia for redevelopment sites granted to the URA. In 2011/12, the land premia waived by the Government on a land grant amounted to $0.1 billion. Since May 2001, a total of 17 land grants, including the one made in 2011/12 have been waived in respect of all the tendered projects with aggregate land premia totalling $5.5 billion.

Without this waiver, the URA's net operating surplus for 2011/12 of $2.6 billion for the year would have been lowered by $0.1 billion to $2.5 billion; its accumulated surplus since May 2001 would have been lowered by $5.5 billion to $6.3 billion; and its net assets value as at 31 March 2012 would have been decreased to $16.3 billion.

(V) Financial Resources, Liquidity and Commitments

As at 31 March 2012, the URA's net cash position including the fair value of the funds managed by the investment manager totaled $8.9 billion as mentioned in paragraph II (b) above. At the same date, the URA's accruals and estimated outstanding commitments to the commenced projects based on the valuation carried out by the URA's in-house professionals stood at $13.1 billion.

In addition to the US$1 billion MTN Programme mentioned in paragraph II (c) above, the URA maintained a total of $1.0 billion and $0.7 billion in committed and uncommitted bank facilities as at 31 March 2012. Securing the external funding and the credit facilities ensured that the URA will have sufficient financial resources to carry out its urban renewal programme as planned.

When implementing its urban renewal programme, the URA is necessarily exposed to financial risks arising from property market fluctuations. Individual projects with various development potentials are launched for tender at different times during property cycles after the site clearance. 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 2012, the total costs of properties under development was $19.2 billion. Taken together with the outstanding commitments, the URA's exposure to the property market was at a historically high level.

The URA estimates in its latest Corporate Plan that from 1 April 2012, a total cash outlay of about $25 billion, excluding operational overheads, will be required in the next five years to meet the costs of both its currently outstanding commitments and its forthcoming expenditure on implementation of the projects contained in the Plan. This expenditure covers the URA's work in redevelopment, rehabilitation, preservation and revitalisation. It should be noted that while the Corporate Plan has been drawn up taking into full account of the new initiatives under the URS promulgated in February 2011, expenditure may nevertheless vary subject to the levels of interest shown in these new initiatives, including in particular demand-led redevelopment, flat for flat scheme, the expanded programme of building rehabilitation and other additional initiatives which may be added subsequent to the preparation of the Plan.

To ensure that its urban renewal programme is sustainable for the longer term, the URA is tasked to maintain a highly prudent financial position and have due regard for commercial principles in its operations.