

INDUSTRY OVERVIEW

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MACROECONOMIC ENVIRONMENT IN HONG KONG

Hong Kong Airport and Port

Located at the centre of Asia-Pacific region, Hong Kong is considered as an international transshipment port for import and export activities. With its geographic advantage, Hong Kong has been benefiting from being a free port with mature logistics industry and well-developed legislative system. Furthermore, Hong Kong is well regarded as a gateway between China and oversea countries. Efficient and prompt delivery is essential to air cargo transportation. According to a survey conducted by World Economic Forum in 2019, Hong Kong international Airport is one of the two most efficient airports in the world based on factors such as flight frequencies, punctualities and handling charges. It was ranked the world’s busiest cargo airport by Airports Council International in 2019, occupying the top spot for ten consecutive years, with an international freight traffic volume of 4.7 million tonnes in 2019. Also, Hong Kong Port ranked 8th among all ports in the world with a throughput volume of 18.3 million TEUs in 2019. However, the economic performance of Hong Kong deteriorated in 2019 due to the unstable political environment and the on-going trade war between China and the U.S.. Major economic indicators showed slight decrease compared to the same period in 2018. For example, (i) Hong Kong’s real GDP growth rate in 2019 was negative 1.2%, compared to the annual growth rate of 2.9% in 2018; (ii) overall export value and export volume through Hong Kong decreased by approximately 4.1% and 6.7%, respectively, in 2019 compared to the same period in 2018. Further, due to the U.S.-China trade war and weak performance of global economy, Hong Kong’s import value from China dropped by 5.9% in 2019, compared to the same period in 2018. Nevertheless, the throughput volume in Hong Kong increased by 1.1% from 285.2 million tonnes in 2018 to 288.2 million tonnes in 2019, which was mainly due to the establishment of the Greater Bay Area.

Hong Kong Re-export Activities

Re-export value, which is the value of goods imported to Hong Kong then exported to other countries, accounted for approximately 99% of the total export value in 2019. The major commodity for re-export include electrical machinery and parts, telecommunications, sound equipment, office machines and automatic data processing machines, which in aggregate accounted for more than 60% of the total re-export value in 2019. Furthermore, due to the strict policies in China, some of these electrical products, such as lithium batteries, some electronic products and certain metal parts, are not allowed to be transported by airplanes in China whereas only major multinational companies with shipping approval issued by the government can ship

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products with batteries by air and only in bulk. However, these kind of products usually require timely delivery from manufacturers to customers. In order to transport them in the shortest time possible, manufacturers usually export these products to Hong Kong from China, then re-export to their final destinations by air, taking advantages of the relatively flexible policies in Hong Kong. The growing trend of external merchandise trade by air in Hong Kong was considered relatively stable from 2015 to 2018. In 2019, the external merchandise trade by air in Hong Kong decreased by 4.3% as compared with 2018, mainly due to the intensified trade war between China and the U.S. along with weak performance of global economy.

Due to years of experience in cargo operation, Hong Kong International Airport's cargo operation efficiency and cargo storage capacity are relatively high, which provides ground for the growth of external merchandise trade. Hong Kong is a free port which pursues a free trade policy and does not maintain barriers on trade nor charges tariff on import or export of goods. Connectivity of an airport is a critical factor for prompt delivery of air cargo, as direct flight can effectively shorten delivery time. Compared with other major airports in the Guangdong-Hong Kong-Macau Greater Bay Area, the Hong Kong International Airport is the only airport with more than 100 international flight routes, making it an effective cargo transshipment hub for China. Most recently, the opening of Hong Kong-Zhuhai-Macau Bridge should boost the transshipment hub status of the Hong Kong International Airport, as the bridge shortens the transportation time between the Hong Kong International Airport and Zhuhai from four hours to 45 minutes. Based on the above, and given Hong Kong's relatively flexible requirements for cargo shipment, favourable trading policies and mature logistics system, Hong Kong has been holding a larger share of international flights in terms of total flights than China and Hong Kong will continue to attract exporters from China to re-export their shipments through Hong Kong.

Trade Activities Downturn and Recovery

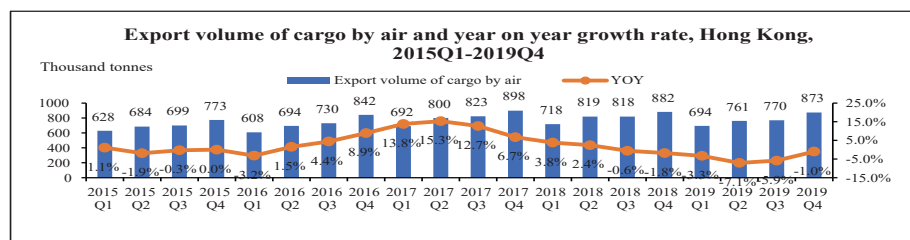
The overall global and regional import/export activities are relatively unstable in terms of import/export value and volume as they are subject to various factors including international politics, regulations, tariffs, exchange rates, domestic and foreign supply of products, domestic and foreign demand, seasonality, etc. Each of these factors can affect global trading and hence the import/export activities in a certain region in either ways.

Hong Kong's trading activities recovered from the 2008 financial crisis and remained relatively stable from 2011 to 2014, however, affected by the economy slowdown and various events during 2014 to 2016, such as global terrorism, anti-globalization movements, U.S. presidential elections, and Brexit, the import and export activities worldwide suffered downturn from 2014 onwards, and resulted in the freight transport and freight forwarding logistics industry developing issues of overcapacity, drop in shipping cost, lowering of average oil price, and low yield rate, etc. for the time period of 2014 to mid 2016. In early 2016, many organizations including airlines, industry associations, third-party consulting agencies and companies in air freight forwarding industry expressed concerns and pessimistic expectations for the rest of 2016. However, after a weak start to 2016, the export volume by air in Hong Kong started to increase from the third quarter since 2016. Export by air in Hong Kong recorded a strong growth from late 2016. The year-on-year growth rate of export volume by air was 4.4% in the third quarter of 2016 and 8.9% in the fourth quarter of 2016. The strong growth was mainly driven by global economic recovery, which was attributable to (i) the relatively stable international political environment; (ii) the periodical recovery of economy after a long period of underperformance; (iii) the increased confidence of the market due to the U.S. government's emphasis on developing the infrastructure construction and manufacturing industry in the U.S.; (iv) the increased import activity in China; as well as China's favorable policies, such as the 13th Five-Year Plan, which is to achieve growth

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in the import and export industry; (v) the increase in shipment of silicon materials and growth in new export orders which stimulated the global air freight volume; (vi) the early Chinese New Year in 2017 which contributed to the strong performance in trading activity in late 2016; and (vii) the global air freight volume recovery in late 2016. Furthermore, the fast growth of cross-border e-commerce industry in China strongly drove the export volume and export value by air in Hong Kong, especially in the fourth quarter of 2016. Some of the top e-commerce companies in China recorded approximately 50% year-on-year growth. The enhanced market efforts of e-commerce platforms such as Tmall.HK, g.suning.com, and JD.HK in 2016 stimulated the growth in export activities in Hong Kong.

Since the third quarter of 2018, several factors have resulted in the decrease of the freight forwarding logistics industry in Hong Kong: (i) the U.S.-China trade war which commenced in July 2018 and intensified in 2019 has resulted in the export volume of air cargo experiencing a continuous decline; (ii) the outbreak of COVID-19 pandemic worldwide in late December 2019 has resulted in the significant decrease in air cargo space of the freight forwarding logistics industry in Hong Kong, in which loss could not be entirely offset by the surge in the price of cargo space. Nevertheless, Hong Kong has been historically capable of recovering from economic downturn recessions caused by emergencies and crises within a short period of time. For example, Hong Kong’s GDP growth rate in 2003 reached approximately 3.0% despite the outbreak of the Severe Acute Respiratory Syndrome that year. Therefore, despite the temporary negative impacts on Hong Kong’s economy due to the intensified U.S.-China trade war and the COVID-19 pandemic, it is expected that Hong Kong’s economic activities and the air and ocean freight forwards industrial will return to normal and still have growth potential, which is driven by the market drivers as mentioned in the paragraph headed “Freight Forwarding Logistics Industry in Hong Kong — Air Freight Forwarding — Market Drivers” in this section.



Source: Hong Kong Census and Statistics Department

FREIGHT FORWARDING LOGISTICS INDUSTRY IN HONG KONG

Ocean Freight Forwarding

In 2019, the revenue of the ocean freight forwarding logistics industry in Hong Kong was HK\$51.2 billion, representing a CAGR of -2.3% from 2015 to 2019. The unsatisfactory performance was mainly due to competition from ports in China and the global economic downturn. In 2019, approximately 74.8% of Hong Kong’s exports were transported to other countries and regions in Asia in terms of trading value. The emerging and developing countries in Asia, including China, India, Indonesia, Malaysia, Thailand, etc., recorded a real GDP growth rate of 4.6% in 2019. Economic growth in emerging and developing countries in Asia remains robust and the bright prospect of intra-Asia trade underpins the development of Hong Kong’s freight forwarding logistics industry. However, further growth in the ocean freight forwarding logistics segment is limited by the competition from ports in China. With the outbreak of COVID-19, the exported volume of goods by ocean is expected to further decline in 2020 due to the temporary suspensions of some factories. However, as it is generally expected that the global economy will

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be gradually recovered with the control of the COVID-19 and Hong Kong continues to serve as a free port, ocean freight forwarding logistics industry is expected to recover between 2021 and 2024. Thus, the ocean freight forwarding logistics industry in Hong Kong is expected to have a CAGR of 4.2% between 2020 and 2024 and reach HK\$55.4 billion by 2024.

Air Freight Forwarding

Market Overview

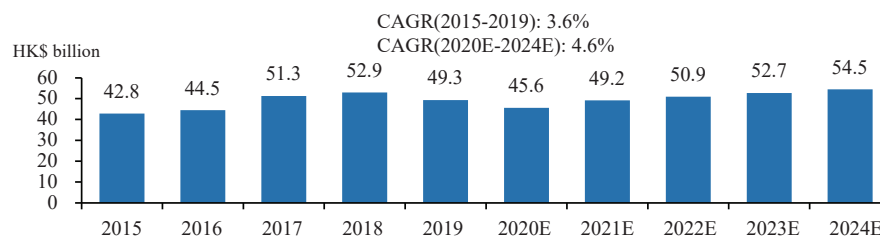
Between 2015 and 2018, the revenue of Hong Kong's air freight forwarding logistics industry grew from HK\$42.8 billion to HK\$52.9 billion. Such growth was mainly driven by the increasing air cargo re-export volume of products manufactured in China such as electrical machinery and parts, telecommunications, sound equipment, office machines and automatic data processing machines, etc.

In 2019, the revenue of Hong Kong's air freight forwarding logistics industry recorded a decline of HK\$3.6 billion, from HK\$52.9 billion in 2018 to HK\$49.3 billion in 2019, such decline was mainly due to the intensified trade war between China and the U.S.. As an important gateway between the U.S. and China, approximately 50% of Hong Kong's exports were of China origin and approximately 55% were destined for China in 2019. Many Chinese goods, such as telecommunication products, electronic device, electrical machinery, apparatus and appliances, are being imported into Hong Kong and then re-exported to the U.S. by air. The ongoing and intensified U.S.-China trade war in 2019 brings pressure to global trading activities and causes uncertainties for the global economy and the global trade landscape. Hong Kong's total air cargo export volume decreased approximately 4.3% in 2019 as compared to 2018. In addition, the protest activities against the extradition bill in Hong Kong, has caused damages to the supply chain. Notwithstanding the above, in December 2019, both the U.S. and China announced to eliminate the tariffs which are scheduled to be imposed on 15th December 2019. The U.S. and China entered into a phase one trade agreement on 15 January 2020 aimed at easing the U.S.-China trade war. According to the phase one agreement, both countries agreed on, inter alia, expanding trade in the future through cutting U.S. tariffs and boosting China's purchases of U.S. products. On 6 February 2020, the Chinese government announced that it will halve its tariff on US\$75 billion worth of U.S. goods effective from 14 February 2020, to reciprocate the fulfillment of commitment by the U.S. to slash its tariffs from 15.0% to 7.5% on US\$120 billion worth of Chinese goods on the same date. On 17 February 2020, China has granted tariff exemptions on about 700 U.S. items to support purchase effective from 2 March 2020. Further, on 21 February 2020, China has unveiled two new tariff exemption lists for U.S. imports from 28 February 2020. On 12 May 2020, China announced a new list of 79 U.S. products eligible to be excluded from retaliatory tariffs. In July, China made its biggest single day purchase of U.S. corn, purchasing 1.762 million metric tons of American corn. The favorable development between these two largest economies, with commitments on both sides, should bring positive effects and stabilise business sentiment on global trading activities. The trade war between the U.S. and China that commenced in July 2018, has upended trading activities worldwide and slowed down global trade growth. The phase one trade agreement is expected to benefit the freight forwarding logistics industry since it will restore the trading activities between the U.S. and China, as well as international trading activities, in the coming years.

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In the PRC and Hong Kong, typically between 45% and 50% of air cargo are carried in the bellies of passenger aircrafts. Due to the COVID-19 pandemic, most airlines has suspended partly or all services, especially services for passenger flights. Hong Kong passenger flights have less Asia shipment in the first four months of FY2020 as compared with the same period in FY2019 due to the outbreak of the COVID-19 pandemic. For example, Cathy Pacific and Cathy Dragon, the two native airlines in Hong Kong, had decreased over 20 Asia routes by April, which exceeded the reduced number of European and American routes. The significant decrease in passenger flight movements has led to a tremendous disruption in air transportation, short supply of cargo space and surge in the price of air cargo space. In the first six months in 2020, the exported air freight forwarding cargo volume in Hong Kong decreased by approximately 7% as compared to the same period in 2019. Meanwhile, the air freight price recorded significant increase, which partly offsets the decrease in air freight forwarding volume. It is currently expected that the market size of the air freight forwarding logistics industry in Hong Kong will decrease to approximately HK\$45.6 billion in 2020. After the COVID-19 pandemic is effectively controlled, it is expected that consumer confidence will be restored and existing factories will completely go back to normal, resulting in a recovery in the air freight forwarding logistics industry in Hong Kong accordingly. Driven by the closer economic connections between Hong Kong and China due to the development of the Greater Bay Area, which have descriptions in details in the paragraph headed “Market Drivers” below in this section, the revenue of the air freight forwarding logistics industry in Hong Kong is expect to rebound and reach approximately HK\$54.5 billion by 2024, representing a CAGR of around 4.6% between 2020 and 2024.

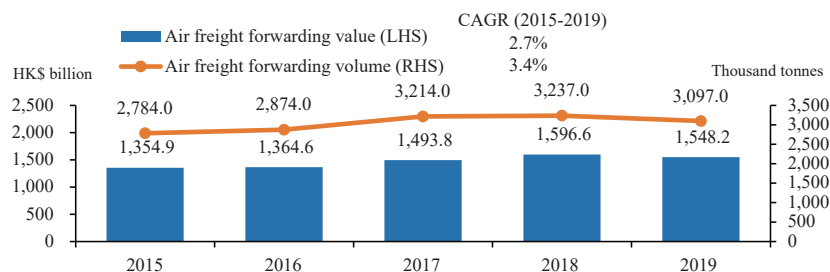
Market size of the air freight forwarding logistics industry in terms of revenue, Hong Kong, 2015-2024E



Note: Based on the assumption that foreign freight forwarders receive major portion of the revenue generated from import freight forwarding logistics services, and local freight forwarders receive major portion of the revenue generated from export freight forwarding logistics services in Hong Kong.

Source: China Insights Consultancy

Air freight in terms of cargo value and volume, Hong Kong, 2015-2019



Note: Data represent the export value and volume

Source: China Insights Consultancy

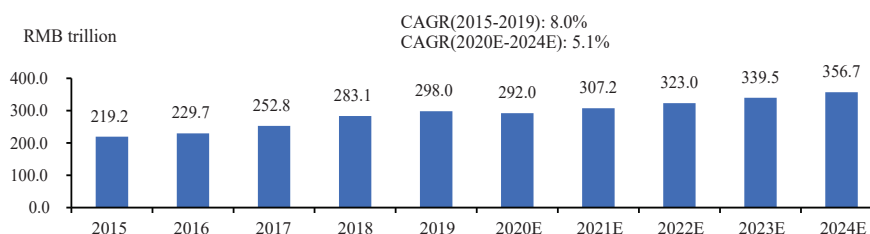
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Market Drivers

A. Increasing cross-border e-commerce sales in Hong Kong and China

From 2015 to 2019, China’s total demand for logistics services maintained a strong growth momentum. The total value of logistics goods grew from RMB219.2 trillion in 2015 to RMB298.0 trillion in 2019, representing a CAGR of 8.0%, which was mainly due to the increasing domestic demand and the ongoing structural changes in China’s economy. China’s economy is reallocating resources from low-productivity to high-productivity sectors. Consumption such as cross-border e-commerce activities, products with higher brand recognition and better quality, is expected to rise following the growth of income level and population. Logistics services, as supporting services, are expected to enjoy steady growth in the future, particularly due to the growth of the e-commerce industry and consumption of consumer goods.

Total value of logistics goods, China, 2015-2024E



Source: National Bureau of Statistics of China, China Insights Consultancy

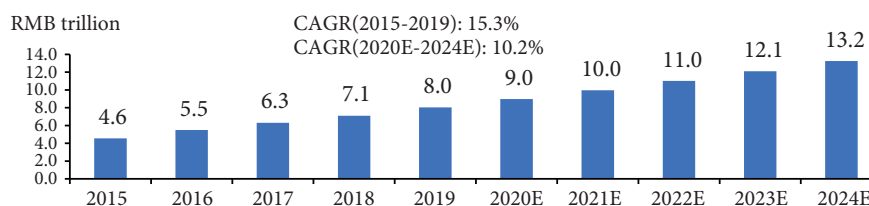
Cross-border e-commerce is a type of e-commerce service that transports products from one country to the customers in another country. Usually the service focuses on providing services to individual customers in a timely manner. As a result, the cargos from cross-border e-commerce industry are not in bulk. Due to the extra administration, packaging and sorting services required, separate parcels cost higher than bulk cargo, which leads to higher profit for freight forwarders.

Cross-border e-commerce industry in China mainly focuses on providing products manufactured in China directly to foreign consumers without foreign distributor and wholesaler’s markup on the prices. In China, some products purchased through cross-border e-commerce channels are electronic devices which contain batteries. Due to the strict policies in China, some of these electrical products, such as lithium batteries and certain metal parts, are not allowed to be transported by airplane in China, whereas only major multinational companies with shipping approval issued by the government can ship products with batteries by air, and only in bulk. Cross-border e-commerce parcels which are individual parcels that contain batteries cannot be shipped by air in China. To cope with this problem, many cross-border e-commerce companies choose to ship their parcels through Hong Kong International Airport and then re-export to other countries. With the special characteristics of cross-border e-commerce parcels, which requires timely delivery and often contain batteries, Hong Kong International Airport becomes the first priority for shippers in the PRC. There has been a strong synergy between cross-border e-commerce industry and Hong Kong International Airport, which benefits the air freight forwarders in Hong Kong. In the past few years, an increasing number of foreign consumers shop online and look for products with relatively lower prices from China and other Asian countries, which in turn stimulate the growth of cross-border e-commerce export value and volume in China. Between 2015 and 2019, the revenue of China’s cross-border e-commerce market size in terms of export value grew from RMB4.6 trillion to RMB8.0 trillion, representing a CAGR of 15.3%. In particular, approximately 80% of the total trading value was export value and approximately RMB1 trillion to RMB1.5 trillion of the export value was through Hong Kong. It is expected that China’s exports value will continue to grow in the future, reaching RMB13.2 trillion in 2024. Driven by the advancement of e-commerce platforms, and strong support

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from the government, China’s total import and export value of cross-border e-commerce increased by 26.2% in the first half of 2020, as compared to the import and export value in the same period of the previous year, of which export value increased by 28.7% and import value increased by 24.4%. Small and medium enterprises obtained a large number of overseas orders through cross-border e-commerce platforms during this process. With the fast growth and strong performance of cross-border e-commerce industry, particularly in the PRC, it is generally expected that Hong Kong, as a regional hub for import and export, will experience an increasing demand for air freight forwarding services. The real GDP growth rate in the PRC is expected to reach 1.0% in 2020 and 8.2% in 2021, according to the World Economic Outlook (WEO) Database updated in June 2020, and is expected to remain stable between 5.5% and 5.7% from 2022 to 2024 according to the WEO Database released in October 2019. The future growth of cross-border e-commerce in the PRC will be expected to outpace the growth of the real GDP growth rate.

Cross-border e-commerce export value, China, 2015-2024E



Source: China E-commerce Research Centre, China Insights Consultancy

In 2018, the major destinations for cross-border e-commerce export are the U.S., Europe, and 10 countries of the Association of Southeast Asian Nations (i.e. Thailand, Indonesia, Malaysia, Singapore, etc). To be more specific, in 2018, China’s top 5 destination countries for cross-border e-commerce export are the U.S., France, Russia, the UK and Brazil, with 17.5%, 13.2%, 11.3%, 8.4% and 5.6% share respectively. The top 5 countries accounted for an aggregated 56.0% of the total cross-border e-commerce export value. In addition, the Association of Southeast Asian Nations (ASEAN), a regional intergovernmental organization comprising ten countries in Southeast Asia, namely Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam, is China’s important trading partner, accounted for more than 10% in aggregate of the cross-border e-commerce export value in 2018. Increasing cross-border e-commerce export to these countries demonstrates emerging opportunities for freight forwarders in their strategic expansion.

Although COVID-19 has caused an unprecedented negative impact on the worldwide economy in 2020, it has favoured and speeded up the further growth of the e-commerce sector because lockdowns, quarantines and social distancing boost demand for online shopping and express delivery services. In the first six months of 2020, China’s cross-border e-commerce retail import and export value registered an increase of 26.2% as compared with the same period in 2019. Further, the State Council Information Office of the Peoples’ Republic of China published an announcement on 13 April 2020 that the PRC government fully affirms and strongly supports the new foreign trade format of cross-border e-commerce and announced to set up an additional 46 new cross-border e-commerce comprehensive pilot zones. Together with the 59 e-commerce comprehensive pilot zones approved in 2019, there will be a total of 105 cross-border e-commerce comprehensive pilot zones nationwide, covering 30 provinces (the number of total provinces in China is 31). The PRC government fully affirms and strongly supports the new foreign trade format of cross-border e-commerce. With the release of the State Council’s circular on 6 May, 2020, confirming the approval to establish 46 additional new cross-border e-commerce

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comprehensive new pilot zones, the cross-border e-commerce industry has been pinpointed as a new pillar for China’s foreign trade. This move will help to stabilise the fundamental landscape of foreign trade and subsequently stimulate the freight forwarding logistics industry in the long run.

B. Rising export value of electronics products in Hong Kong and China

As the production cycle for electronics products is relatively short, and fast delivery is of increasing importance for electronic products, manufacturers may opt for air-based logistics because it can provide timely deliveries. With the continued development of technology worldwide and economic improvements, the market for electronics is expected to continue expanding, which will drive increasing demand on the air freight forwarding logistics services.

C. Trusted legal system and a well-established logistics value chain

Hong Kong has a long history as a logistics hub in Asia. Hong Kong’s legal and logistics systems are relatively mature compared with other countries. Moreover, the logistics value chain in Hong Kong is already well-established and includes a large group of logistics professionals operating in different domains. Therefore, companies can benefit from greater conveniences while saving time when transporting their goods from/to Hong Kong. Such advantages will boost development of the air freight forwarding logistics services in Hong Kong.

D. The expansion of Hong Kong International Airport

Connectivity of an airport is a critical factor for prompt delivery of air cargo, as direct flight can effectively shorten delivery time. Compared with other major airports in the Guangdong-Hong Kong-Macau Greater Bay Area, the Hong Kong International Airport is the only airport with more than 100 international flight routes, making it an effective cargo transshipment hub for China.

Hong Kong International Airport has been recognised as a five-star airport for many years in terms of its service quality, efficiency, and customer satisfaction. Currently, Hong Kong International Airport is constructing its third runway which is estimated to be completed by 2024, which will largely boost the capacity of cargo throughput in Hong Kong. According to the Construction and Mainland Affairs Bureau, land has been reserved in the South Cargo Precinct of the Hong Kong International Airport to support the growth in transshipment, cross-boundary e-commerce and high value-added air cargo business, and facilitate the development of air cargo industry. The expansion works will commence in the fourth quarter of 2019, and the handling capacity of the express air cargo terminal will increase by 50% in 2022. According to Hong Kong’s 2020-2021 budget plan, the Hong Kong government set aside HK\$5 billion (US\$642 million) for redevelopment of the air mail centre at the Hong Kong International Airport, which aims to be completed as soon as 2024-2025. Additionally, the new plan also implements a US\$44 million subsidy pilot program, allowing third-party logistics providers to receive subsidies, thus further driving the development of air freight forwarding logistics industry in Hong Kong in the future. Furthermore, a joint venture led by Cainiao Network (the logistics arm of Alibaba Group) with shareholders including China National Aviation Corporation (Group) Limited and YTO Express, will develop a premium logistics centre at Kwo Lo Wan in the South Cargo Precinct of the Hong Kong International Airport, which is scheduled to be completed and put into operation in 2023, making the Hong Kong International Airport a more competitive air cargo terminal in the future.

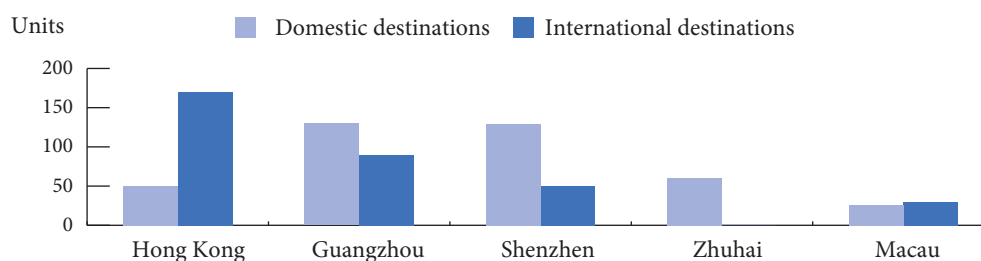
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E. The establishment of the Greater Bay Area

The concept of the Greater Bay Area, which consists of Hong Kong, Macau, and nine cities in South China, was first mentioned in China’s 13th Five-Year Plan, aiming to reinforce the connection between Hong Kong, Macau and China. The Greater Bay Area project includes major infrastructure projects, such as the construction of airports and seaports in Hong Kong and Guangdong Province. The project can help realize the transregional coordination of multimodal transportation services connecting cities located in China, Hong Kong, and overseas. The project also includes the establishment of a global manufacturing centre, a trade centre, and a logistics hub in the Greater Bay Area, which can further strengthen Hong Kong’s competitiveness as an international logistics hub as Hong Kong has established a proven track record of being a trusted logistics hub in Asia. As such, the future demand for Hong Kong’s air freight forwarding logistics services is expected to continue expanding. The value of total merchandise traded in the Greater Bay Area reached approximately RMB15.7 trillion in 2019.

Connectivity of an airport is crucial for express delivery of air cargo, as direct flight can reduce delivery time. Compared with other major airports in the Greater Bay Area, Hong Kong International Airport is the only airport with more than 100 international flights routes, making it an effective cargo transshipment hub for China. As the Hong Kong-Zhuhai-Macao Bridge shortens the transportation time between Hong Kong International Airport and Zhuhai from four hours to about 45 minutes, the opening of Hong Kong-Zhuhai-Macao Bridge would further enhance the transshipment hub status of Hong Kong International Airport. The following chart represents the number of destinations of major airports in the Greater Bay Area in 2019.

Connectivity of major airports in the Greater Bay Area in 2019



Note: Domestic destinations for Hong Kong and Macau refer to cities in China.

Source: Legislative Council Secretariat, China Insights Consultancy

F. Implementation of Belt and Road Initiative

The economic growth in Asia is at a faster pace (GDP at 5.4% in 2019) than other locations in the world (GDP growth at 2.2% for the U.S. and 1.5% for Europe in 2019). The “Belt and Road” initiative sets up ground and ocean-related infrastructure in order to connect Central and South Asia, Europe, the Middle East and Africa. In addition, port investment under the Belt and Road Initiative is anticipated to boost the air and ocean logistics and shipping networks. Thus, increasing cooperation among countries is likely to benefit the growth of the international trades and freight forwarding logistics industries. An increase in demand for international logistics and freight forwarding logistics services is anticipated, especially for seaborne and airborne logistics.

Market Trends

A. Faster responses to satisfy customer demands

Clients demand quicker logistics and higher service quality at lower prices, especially for cross-border e-commerce industry. Logistics with faster response can improve clients’ efficiency, productivity and profitability. This is a common demand from clients in the retail sector, which are currently under increasing pressure from massive multichannel challenges. Faster response requires investments in improving the logistics process in order to elevate service standards.

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B. Consolidating and co-loading between freight forwarders

Consignments of air freight forwarding industry are usually of relatively small volume. It is important for freight forwarders to consolidate their cargos to fully load the cargo space. In recent years, with the fast development of cross-border e-commerce industry, the consignments are becoming smaller. Small-and medium-scale freight forwarders usually bundle together small consignments to fill the cargo space, which is considered a common practice. It becomes a collaborative industry effort to address the increasing demand of cross-border e-commerce goods. Due to the need to fully load cargo spaces, it is also common for freight forwarders to take other freight forwarders as customers, sometimes as suppliers.

C. Higher efficiencies created by paperless customs procedures

The development of technology has simplified customs procedures. China implemented a paperless customs system in 2013, with individuals now being able to receive warehouse warrants, customs clearances, and release permits using an online platform. This online platform is accessible 24/7, leading to higher efficiencies compared with the processing of paperwork. A paperless customs system allows for faster customs clearance, while preventing shipments from being stored in warehouses for long periods of time. Thus, freight forwarding logistics companies are able to process a greater number of requests from consigners and hence shorten the warehousing turnover period.

With the development of information technology and internet, the information regarding cargo transportation is becoming more and more transparent. The transparency in information will benefit airlines and consigners in various aspects, including the pricing, space matching, electronic payment, etc. However, air freight forwarders will still be an important part of the process. Firstly, the airlines will not directly interact with individual consigners since they do not offer consolidation service, palletization service, etc. Certain manpower is still required to administrate, process, load, match and transport the cargo. With the trend of division of labour, it is unlikely the consigner will be expending effort in this area, and it is also unlikely for the airlines to take charge of these works. Secondly, certain bank guarantee is required in order to purchase cargo space from airlines, which will affect the liquidity of air freight forwarders if they want to buy air cargo space directly from airlines rather than through other freight forwarders. The payback period set by airlines is relatively short, which will also add to the pressure on liquidity for freight forwarders. Thirdly, the freight forwarding service is a supporting industry which facilitate the manufacturing, retailing and other functions of a company. By outsourcing the logistics to third parties, a company can focus its capital, manpower and administrative effort on their main business, which will significantly lower the operation risks. The advantages of outsourcing logistics to third parties include low capital commitment, cost savings, and flexibility. In conclusion, it is unlikely the development of information technology will diminish the value created by freight forwarders.

Competitive Landscape

The Hong Kong air freight forwarding logistics industry is considered to be a fragmented market. In 2019, more than 1,500 freight forwarding companies were registered in Hong Kong, and most of them were in both air freight forwarding logistics industry and ocean freight forwarding logistics industry. There are two tiers of freight forwarding companies in Hong Kong. Tier 1 players are the leading participants in the industry, who are mainly multinational enterprises. They usually possess global network of offices with own transportation fleets and have long-term relationships with international large carriers. The bulk shipment opportunities over the past years had been dominated by these participants. There are around 20 to 30 companies in this group and these multinational enterprises contributed about nearly half of the total revenue of air freight forwarding logistics industry in Hong Kong.

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Apart from tier 1 players, tier 2 players are small- and medium-scale Hong Kong-based local enterprises. These enterprises usually have a turnover of below HK\$1.5 billion per year, with deeper understanding of customers’ business nature and have long-term relationships with customers based in Hong Kong and Pearl River Area. There were over 1,000 tier 2 players in Hong Kong in 2019. The table below shows the ranking and details of the top ten local tier 2 participants, which accounted for approximately 7.9% in total in 2019, while our Company accounted for about 0.6% market share of air freight forwarding logistics industry in 2019, and ranked 6th place among all tier 2 air freight forwarding companies.

Ranking of tier 2 air freight forwarding companies, Hong Kong, 2019

| Ranking | Company | Specialised destinations | Approximate revenue from air freight forwarding services in Hong Kong in 2019 (HK\$ million) | Approximate market share in 2019 |
|---------|-------------|--|---|----------------------------------|
| 1 | Company A | The U.S. and the Netherlands | 1,053.0 | 2.1% |
| 2 | Company B | Africa, Central and South America, Europe, etc. | 408.2 | 0.8% |
| 3 | Company C | Europe, North and South America | 397.0 | 0.8% |
| 4 | Company I | North America, Europe, Asia, etc. | 370.4 | 0.8% |
| 5 | Company D | Southeast Asia | 341.2 | 0.7% |
| 6 | Our Company | The U.S., Europe and Asia | 292.3 | 0.6% |
| 7 | Company E | The U.S. and Japan | 285.4 | 0.6% |
| 8 | Company F | Europe, Africa, North America, etc. | 260.8 | 0.5% |
| 9 | Company G | Europe, Japan, Scandinavia, etc. | 240.8 | 0.5% |
| 10 | Company H | Europe, Southeast Asia, etc. | 229.7 | 0.5% |
| | | Subtotals of top 10 tier 2 players | 3,878.8 | 7.9% |
| | | Others (including tier 1 players and other tier 2 players) | 45,447.6 | 92.1% |
| | | Total | 49,326.4 | 100.00% |

*Note: the ranking only considered tier 2 companies’ revenue from air freight forwarding services in Hong Kong market, which is the major business section our Company operates in. Our Company also has operations in China and Macau, the revenue from these export origins is not considered. Comparable tier 2 companies’ revenue listed above only include revenue generated from air freight forwarding services in Hong Kong market.

The air freight forwarding logistics industry is fragmented in China, and is in fast development. The top three companies took market share of approximately 5.3%, 4.3% and 4.1% of the total market respectively in 2019, and accounted for a total of 13.7% of the market. In 2019, our Company gained a market share of approximately 0.04% of China’s air freight forwarding logistics industry.

Key Success Factors

A. Well-established partnerships with upstream carriers

Successful companies have benefitted from first-mover advantages in the market, having acquired stable and long-term partnerships with upstream carriers over the course of their long-term cooperation with these carriers, which include airlines, vessel companies, etc. By developing close partnerships with these upstream carriers, a logistics company better understands their clients’ products and needs, while also gaining foreknowledge of upstream carriers’ capacities, which makes it easier to provide accurate solutions at the best prices.

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B. Expert knowledge regarding different industries

Downstream industries, such as pharmaceuticals, chemicals, FMCGs, machinery, etc., each has different needs during international transportation. Many goods are temperature sensitive, time sensitive or fragile. Therefore, expert knowledge of downstream industries becomes a major success factor for market participants.

C. Provision of value-added services

The freight forwarding logistics service market is fragmented and characterised by a large number of small to medium-scale enterprises. Value-added services can help freight forwarding companies in attracting more customers. This is particularly true in recent years with the growing popularity of cross-border e-commerce, since end customers now usually demand faster, more reliable, and safer deliveries of products. Thus, a successful freight forwarding logistics company is able to cater to different demand by offering tailored value-added services.

D. Strong capability to consolidate cargos

As the customers entrust air freight forwarders with various amount of cargos, it is important for successful companies to have a strong ability to consolidate cargos from different customers in order to accommodate the cargo to the shipping standards of the airlines. Fast and accurate consolidation of the cargo is a key ability to provide better service to customers.

Entry Barriers

A. Access to capital

Access to capital is especially essential in the freight forwarding logistics industry. The payment period for carriers and freight forwarders is usually 15 days, while the collection period with consigners can range anywhere from 45 to more than 60 days, with the longest up to 120 days. In order to have sufficient cashflow for daily operations, freight forwarding logistics companies have to be well-managed and retain enough capital to continue operations. Furthermore, in order to operate in air freight forwarding logistics industry in China and Hong Kong, a certain amount of bank guarantee has to be provided to cooperate with airlines. A bank guarantee is a promise from a freight forwarding logistics company's bank that the bank will cover the airlines loss if the company is unable to pay the payment by default. Banks usually require mortgage value of at least 50% of the freight forwarding payment value.

B. Brand awareness

Usually downstream consigners prefer freight forwarding companies with a good reputation so as to ensure better services and relatively lower prices. A freight forwarding company with an established brand also indicates a degree of stability in terms of service quality and reliable deliveries. For new entrants, establishing a brand can be difficult as it takes time to prove that their business can meet the requirements of different clients.

C. Partnerships with clients and suppliers

The market remains highly fragmented and so each company offers similar shipping prices and services. The ability to attract potential clients therefore becomes an entry barrier to new entrants. A well-operated company is able to successfully engage potential clients and maintain long-term partnerships with them. Therefore, the need for a well-established sales network and a good sales team creates another entry barrier to new companies. Furthermore, more than 80% of the tier 2 companies in Hong Kong air freight forwarding industry cooperate directly with airlines to book cargo space. By establishing direct relationships with airlines, a well-operated company is able to response to clients' demand rapidly. Steady relationships with airlines are formed by long-term cooperation and trust, which is considered an entry barrier to new entrants.

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D. Licenses and certificates

The PRC government requires freight forwarding companies to have a “First Class Certificate of Freight Forwarding,” which is needed if companies are yet another directly booking shipping spaces with carriers. Organizations like FIATA, ICAO, and the Federal Maritime Commission, also provide different licenses and certificates for different purposes. These licenses and certificates therefore create additional entry barriers to new entrants.

Market Threats and Challenges

A. Insufficient labour forces

Labour shortage is a major threat to the air freight forwarding logistics industry in Hong Kong. Freight forwarders need professional talents to establish an efficient and reliable operating system to consolidate cargos for both air and ocean freight forwarding services. Furthermore, workers are needed to process and handle the cargos. The shortage of workforces will result in a higher labour cost.

B. Increasing competition due to industry consolidation and integration

Large transportation and logistics companies usually cooperate with freight forwarders to provide services to their customers. However, they are now pursuing a one-stop service strategy for the customers. In order to achieve that, they are acquiring small freight forwarders to achieve economies of scale, as well as to own the customer relationships. This will present a threat to the freight forwarders.

AIR FREIGHT FORWARDING MARKET IN CHINA

Nominal GDP in Jiangsu Province and Greater Bay Area

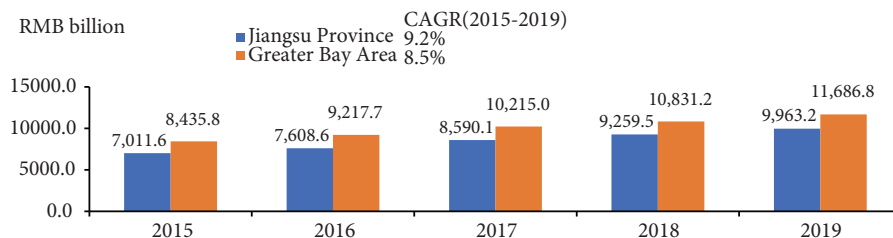
Nominal GDP in Jiangsu Province increased from RMB7,011.6 billion in 2015 to RMB9,963.2 billion in 2019, representing a CAGR of 9.2%. It ranked as no.2 province in Eastern China in terms of GDP in 2019, second only to Guangdong Province. There are over 30 industrial parks in Jiangsu Province. The output value of strategic emerging industries (which mainly include energy conservation and environmental protection, IT, biology, high-end equipment manufacturing, new energy, new materials, and new energy vehicles) increased by 7.6% in 2019, accounting for approximately 32.8% of the total industrial output value of industrial enterprises with revenues of over RMB20 million annually. The industrial development of Jiangsu Province would facilitate its freight forwarding market as these industrial products manufactured will be exported to overseas markets. Along with the completion of the industrial structure upgrade, which refers to businesses that realise rapid growth primarily through new technologies, new business forms or new business models, Jiangsu Province is expected to realize a new round of rapid economic development.

Greater Bay Area refers to the urban agglomerations consisting of two special administrative regions of Hong Kong and Macau and 9 cities in Guangdong province. The construction of Greater Bay Area is conducive to deepening cooperation between the mainland and Hong Kong and Macau. The development of Greater Bay Area has been written into the 19th National Congress report and enhanced as national development strategy. On 1 July 2017, *the Framework Agreement on Deepening Guangdong-Hong Kong-Macau Cooperation in the Development of the Greater Bay Area* was signed. This aims to elevate the Greater Bay Area’s position and role in the national economic development and opening up, as well as set out the key cooperation fields including promoting infrastructure connectivity, enhancing market integration, building a global technology and innovation hub, etc. The adoption of intelligent manufacturing and international cooperation in logistics, technology and innovation are encouraged, which will in turn stimulate the development of logistics industry in Hong Kong.

Nominal GDP in Greater Bay Area increased from RMB8,435.8 billion in 2015 to RMB11,686.8 billion in 2019, representing a CAGR of 8.5%.

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Nominal GDP, Jiangsu Province and Greater Bay Area, 2015-2019



Source: National Bureau of Statistics of China

Air Freight Forwarding

The air freight forwarding logistics industry in China is still in an early stage of development. Between 2015 and 2018, the size of China’s air freight forwarding logistics industry grew from RMB39.6 billion to RMB57.8 billion, representing a CAGR of 13.4%. In 2019, the market size of the air freight forwarding logistics industry in China decreased by approximately 2.5% to RMB56.4 billion, attributing to the U.S.-China trade war. In the first five months of 2020, China’s total air cargo throughput volume in major air ports decreased by approximately 12.7% under the effect of COVID-19 pandemic. At the same time, the cancellation of most air flights and gradual business resumption in China boosted a significant increase in air freight price. Considering the collective effects of decreasing cargo volume and increasing air freight price, the market size is estimated to reach approximately RMB55.4 billion in 2020. Nevertheless, it is estimated that the air freight forwarding logistics market will increase to RMB70.4 billion by 2024, based on the trading agreements achieved in phase one trade agreement by the U.S. and China and the assumption that economic activities will return to normal globally once the COVID-19 pandemic is under control.

The growth of China’s air freight forwarding industry is highly correlated with export volumes. China has a large manufacturing industry, with many of the manufactured goods being produced for export to foreign countries. Similar to Hong Kong, Shanghai shares the same cargo catchment area in the Pearl River Delta region while Singapore shares the same positioning as a regional hub for intra-Asia trade and as a logistics centre.

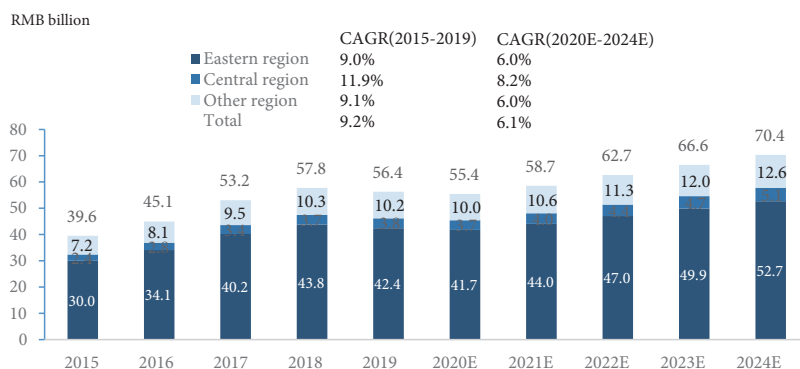
The most important competitive advantage of air freight forwarding is its short lead time. Faced with challenge from the U.S.-China trade war, China has strengthened cooperation with other countries. China’s trading value with other partners witnessed stable growth, especially the European Union, Association of Southeast Asian Nations (ASEAN) and countries along the “One Belt, One Road” route, recording year-over-year growth rates of 8.0%, 14.1%, and 10.8%, respectively in 2017, 2018 and 2019. The continuously increasing volume of exports, especially considering the ongoing development of cross-border e-commerce, will boost the demand for air transport. In addition, the construction and expansion of airports in Beijing, Shanghai, Guangzhou, Shenzhen and Chengdu will further enhance the China’s air cargo handling capacity. As at the end of 2019, there were 238 civil airports in China. According to the General Administration of Civil Aviation of China, the number of airports will be increased to 320 by 2025, in order to meet the growing amount of air cargo volume, improve air connectivity and address the problem of unevenly distributed of airports throughout the country. The establishment of China Pilot Free Trade Zone reduced taxes in these trade zones and improved custom clearance process, which will in turn elevate trade activities and improve the efficiency of the air freight forwarding in China.

Hong Kong International Airport, as the irreplaceable key link in China’s supply chain, has improved its integration with China by establishing cargo depots at strategic locations in the Pearl River Delta, which enables easy access to consigners in China and facilitates the flow of Chinese goods via Hong Kong. Electronic products, which are under strict regulation when transported by air in China, can be transported by Hong Kong International Airport instead. Thus, Hong Kong will also benefit from the growth of China’s air cargo transport.

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The eastern region in China, including Beijing, Shanghai, Shandong, Jiangsu, Tianjin, Zhejiang, Hainan, Hebei, Fujian and Guangdong, is its primary economic, trading and shipping centre, accounting for approximately 75% of China’s total air freight forwarding logistics market. The air freight forwarding logistics market in the eastern region is expected to grow from RMB41.7 billion in 2020 to RMB52.7 billion in 2024, representing a CAGR of approximately 6.0%. The air freight forwarding logistics industry in the central region has developed rapidly over the past five years, driven by the continuous expansion of air transportation capacity and improvement of air connectivity. The air freight forwarding logistics market in the central region reached RMB3.8 billion in 2019, and is projected to continue to increase to RMB5.1 billion by 2024. The booming of cross-border e-commerce is one of the key factors driving such growth.

Market size of the air freight forwarding logistics industry in terms of revenue, China, 2015-2024E



Note: Eastern region includes Beijing, Shanghai, Shandong, Jiangsu, Tianjin, Zhejiang, Hainan, Hebei, Fujian and Guangdong; Central region includes Jiangxi, Hubei, Hunan, Henan, Anhui and Shanxi.

The above table only includes freight forwarding revenue generated from cargo volume transported by domestic airlines.

Source: China Insights Consultancy

Market Drivers

A. Construction of new airports

In major cities and regions, the construction of new airports and the extension of existing airports is aimed at expanding cargo throughput volumes, which is expected to provide the industry with the essential infrastructure it needs to continue growing. Shanghai, Guangzhou, Shenzhen, Beijing, Chengdu, and Hong Kong all achieved their highest recorded throughput volumes in 2016, with these cities considered to be major air freight forwarding hubs within China. These cities are currently expanding their existing airports to further expand their throughput volumes. New airports in Beijing and Chengdu are also under construction, which is expected to encourage the further expansion of throughput volumes for the air freight forwarding industry in China.

B. Establishment of China Pilot Free Trade Zone (PFTZ)

The construction of China Pilot Free Trade Zone (PFTZ) aims at boosting international trade and logistics-related industry. The four different PFTZs in China have different advantages and strengths. As listed, these four PFTZs welcome logistics-related services and industries. The main purpose of China PFTZs is to boost China’s economy by elevating trade activities. For companies, they are anticipated to benefit from the establishment of PFTZs from various aspects, such as reduced taxes, convenient custom clearance process, etc., as well as more opportunities from both overseas markets and local market.

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C. *Development of e-commerce in China*

Between 2015 and 2019, the revenue of China's entire cross-border e-commerce market size in terms of trading value grew from RMB4.6 trillion to RMB8.0 trillion, representing a CAGR of 15.3%. More foreign consumers shop online and look for products at a relatively lower price from China and other Asian countries, which in turn stimulate the growth of cross-border e-commerce export value and volume in China, thus facilitating the development of the air freight forwarding logistics industry in China.

SHIPPING COSTS

Air Freight Price Index

The air freight price is influenced by different factors, including oil prices, freight capacities, the length of transportation, etc. For instance, as oil is the most used fuel for air freight forwarding services currently, the increase of oil prices will cost more for the freight carrier to transport the freight, and therefore the air freight forwarder is going to be charged more to make up for this. The freight capacity will also have effects on the air freight price, with the smaller capacity leading to higher prices due to the shortage of space. In addition, the air freight price is positively correlated with the length of transportation. The relatively longer length of transportation enhances the difficulty of transporting, thus resulting in higher air freight prices. In recent years, downstream consigners and end customers have started recognizing the advantages of air transport, including a guarantee of fast, timely, and reliable deliveries, which has consequently led to increasing quantities of cargo being transported by air. Generally, the air freight price is strongly correlated to the shipping quantity. During peak seasons, namely the fourth quarter in each year with western holidays such as Thanksgiving, Christmas and New Year's Eve, the price of air freight goes up with the increasing export activities. Between 2015 and 2018, air freight price index recorded annual growth rate of -5.5%, -8.8%, 5.1%, and 5.7% respectively. In 2017 and 2018, the recovery of economy and growth in global trading boosted the increase in air freight price. The air freight price index decreased 7.2% in 2019 due to the decrease in air transport volume caused by unstable global trading environment. Air freight price in March 2020 increased rapidly due to the short supply of cargo capacity. It is expected that the air freight price will remain at high level in 2020 considering the limited air cargo capacity.

The profit before tax of freight forwarders is primarily affected by the state between supply and demand rather than oil price. The increase in oil price can be passed to consigners when the demand for cargo space is high. In contrast, when the air cargo transportation volume decreases and cargo space is in sufficient supply, most freight forwarders will choose to decrease price to attract more customers, which will adversely affect the profitability.

POTENTIAL EFFECT ON TRADING ACTIVITIES FROM U.S. TARIFFS AGAINST CHINA

The U.S. has implemented three rounds of import tariffs on Chinese goods since July 2018. In the first round in 2018, the U.S. imposed a 25% tariff on US\$50 billion worth of Chinese goods, and the tariff was set to take effect in July and August 2018 respectively. In September 2018, the U.S. implemented a 10% tariff on US\$200 billion worth of Chinese goods, and this tariff was subsequently increased to 25% in May 2019. On 1 September 2019, the U.S. imposed new 15% tariffs on about US\$112 billion of Chinese imports and will impose additional tariffs on a further list of additional categories of products of Chinese origin in December 2019.

In October 2019, the U.S. and the Chinese governments achieved phase one trade agreement after the meeting in Washington. Pursuant to which, the U.S. has delayed a tariff increase scheduled to go into effect on 15 October 2019. The delay will apply to tariffs that were scheduled

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to increase from 25% to 30% on US\$250 billion of Chinese goods. China agreed to buy more agricultural products from the U.S.. The U.S. implemented a tariff ranging from 15% to 25% on approximately US\$362 billion worth of goods imported from China. China imposed 5% to 10% tariffs on one-third of the 5,078 goods it imports from the U.S., with tariffs on the remainder scheduled for 15 December 2019.

On 15 January 2020, the U.S. and China entered into a phase one trade agreement on 15 January 2020 aimed at easing the U.S.-China trade war. According to the phase one agreement, both countries agreed on, inter alia, expanding trade in the future through cutting U.S. tariffs and boosting China's purchases of U.S. products. On 6 February 2020, the Chinese government announced that it will halve its tariff on US\$75 billion worth of goods effective from 14 February 2020, to reciprocate the fulfillment of commitment by the U.S. to slash its tariffs from 15.0% to 7.5% on US\$120 billion worth of Chinese goods on the same date. On 17 February 2020, China has granted tariff exemptions on about 700 U.S. items to support purchase effective from 2 March 2020. Further, on 21 February 2020, China has unveiled two new tariff exemption lists for U.S. imports from 28 February 2020. On 12 May 2020, China announced a new list of 79 U.S. products eligible to be excluded from retaliatory tariffs. In July 2020, China made its biggest single day purchase of U.S. corn, buying 1.762 million metric tons of American corn. As the trade war is temporarily cooling off, Hong Kong's air freight forwarding logistics industry is expected to recover after 2019. In July 2020, the U.S. government ended Hong Kong's special trading status. The impact on Hong Kong is limited, as Hong Kong does not have a large amount of direct trade with the U.S.. After signing the phase one trade agreement and before the outbreak of COVID-19 worldwide, the International Monetary Fund expected that the phase one trade agreement would promote the China's GDP growth by 6% for 2020.

The U.S. is China's third largest trading partner, following the European Union and Association of Southeast Asian Nations (ASEAN). Approximately 19% of China's export was purchased by the U.S.. It is estimated that goods subject to the increased tariffs implemented by the U.S. account for approximately 10% of China's total export value. The trade war will increase trading costs with China and force U.S. companies to purchase goods from other regions, which will lead to decrease in China's export value. In 2019, China's export value to the U.S. decreased by 8.7%. The trade war has put pressure on China's external trade market and the freight forwarding logistics industry. However, Chinese goods are relatively competitive and China is the largest exporter in the world. For some commodities, such as motors, electrical machinery and parts, telecommunications, sound equipment, optical equipment, etc., it is difficult for the U.S. companies to find substitutes in a short time. Moreover, China's export to other regions is still prosperous and the export structure is getting more diversified. In 2019, China's export to the European Union and ASEAN increased by 9.6% and 17.8% respectively in terms of export value. China's trading value with countries along the "One Belt, One Road" route also witnessed a significant increase, recording a year-over-year growth rate of 10.8% in 2019. With the easing of the U.S.-China trade relation after China and the U.S. entered into the phase one trade agreement on 15 January 2020, China's import and export value with the U.S. reached approximately RMB2.8 trillion in the first three quarters of 2020, with an increase of 2% compared to the import and export value in the same period of the previous year. For further details, please refer to the section headed "Summary – Recent Development and Material Adverse Change – U.S.-China Trade War" in this document.

As a re-export hub for trade between the U.S. and China, Hong Kong will also bear the pressure from the trade war. The Hong Kong government estimated that 1.4% and 2.2% of Hong Kong's total export are affected as a result of U.S. tariffs on US\$50 billion and US\$200 billion worth of Chinese goods respectively. The U.S. goods imported by China under the tariffs in effect are mainly agricultural products and auto vehicles. These products are primarily transported by ocean from the U.S. to China. Therefore, the Chinese tariffs on the U.S. products have slighter effects on Hong Kong's air freight forwarding industry.

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The U.S.-China trade war, which has reached a periodical agreement, mainly focused on adding tariffs on bulk products exported from China and the U.S. Cross-border e-commerce industry, with its individual parcels containing products by each individual customer from overseas countries, were not heavily affected by the trade war. On the contrary, due to the trade war, the price of some products in the U.S and in China raised. Cross-border e-commerce industry, which usually offer more affordable products shipped directly from the manufacture, can benefit from the price rise. As a result, the trade war has limited effect on cross-border e-commerce industry, as well as the air freight forwarding logistics industry in Hong Kong. The phase one trade agreement is expected to benefit the freight forwarding logistics industry since it will restore the trading activities between the U.S. and China, as well as international trading activities, in the coming years.

POTENTIAL EFFECT ON THE CARGO CAPACITY FROM THE OUTBREAK OF COVID-19

In the PRC and Hong Kong, between 45% and 50% of air cargo are typically carried in the bellies of passenger aircraft. Due to the COVID-19 pandemic, most airlines have suspended partly or all services, especially services for passengers. In February 2020, (i) the passenger flight movements in Hong Kong decreased by 50.7% due to the COVID-19 pandemic; (ii) the cargo flight movements increased by 3.6% due to the short supply of air cargo capacity caused by significant decrease in passenger flight movements; (iii) the total flight movements in the PRC decreased by approximately 60% to 70%, which was also mainly caused by cancellation of most passenger flights. The number of passenger flights carried in Hong Kong decreased from 28 thousand units in January 2020 to 14 thousand units in February 2020. The significant decrease in passenger flight movements led to short supply of air cargo space and increase in air freight price.

The PRC government has taken various drastic measures in February to curb the spread of COVID-19. In most provinces, factories are not required to resume operation before 10th February, which was 11 days later than scheduled. Therefore, some factories may not be able to deliver goods on time that have been ordered before the outbreak of COVID-19, facing risks of default. As a result, commercial goods that are usually transported by ocean would be transported by air instead, in order to make up for lost time. Those exporters may choose to bear the higher cost rather than facing default and damaging their relationship with customers. Additionally, medical supplies, like masks and protective clothing, need to be transported by air to countries in urgent needs, although these products were usually transported by sea before COVID-19 pandemic.

By the end of March 2020, COVID-19 in China is under control, and companies have almost resumed business operation except for companies in Hubei province. The resumption rate of business in Hubei province reached approximately 80% as of 22th March 2020. The resumption of business will boost the increase in air cargo demand. To ease the bottleneck of capacity supplied by passenger flights, some freight forwarders chose air cargo charter services.

In March 2020, one of the major airlines in Hong Kong announced that, in addition to the previously announced 40% capacity reduction between China and Hong Kong, it will further suspend flight routes between several cities in China, Kaohsiung, Taichung, New York, Washington, D.C., until 28 March 2020. In light of the deterioration of virus outbreak in Europe, it has further suspended flight routes between Rome, Milan, Tel Aviv, London and Barcelona at the end of March 2020. Flight routes between Seoul, Jeju, and Maldives will also be suspended at the same time. The suspension in flight routes will reduce the overall cargo capacity and affect the demand and supply balance of freight forwarding logistics industry.

In April 2020, Wuhan lifted the control measures of city lockdown, indicating China has effectively controlled the COVID-19 outbreak in China temporarily. Although there has been several new cases in regions such as Beijing, Hong Kong and Xinjiang since June 2020, the regional government sectors have taken quick action to prevent the pandemic from worsening, leading the whole country under steady operation.

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Due to the COVID-19 pandemic, most airlines have suspended partly or all services, especially services for passenger flights, which has led to short supply of air cargo space and increase in the air freight price. However, with the resumption of business in major cities and countries of the U.S. and Europe, demand for air cargo space will recover accordingly. In the situation with unbalanced supply-demand relationship for air cargo space, the air freight forwarders that have close and stable relationships with airlines have the opportunity to purchase corresponding amount of air cargo space, thus achieving greater growth of revenue.

SOURCE OF INFORMATION

CIC was commissioned to conduct research and analysis of, and to produce a report on industry development, market trend, and competitive landscape of Hong Kong and China's air and ocean freight forwarding logistics industry at a fee of HK\$1,050,000. This commissioned report has been prepared by CIC independent of the influence of our Company or any other interested parties. CIC's services include industry consulting, commercial due diligence, strategic consulting, etc. Its consulting team has been tracking the latest market trends in various industries, and has extensive experience in and insightful market knowledge of the abovementioned industries.

The methodology used by CIC involves conducting research and analysis based on both primary and secondary research in a two-step process: (i) conducting primary and secondary research to gather the necessary industry information and data; (ii) conducting quantitative and qualitative research analysis through the calculation and projection of relevant market data, with this data based on historical data, including macroeconomic data, import/export data, data from the freight forward industry, etc., which is sourced from the World Bank, the International Monetary Fund, the National Bureau of Statistics of China, the Hong Kong Census and Statistics Department, Hong Kong and China's logistics and freight forwarding industry associations, etc. Primary research involves interviewing key industry experts and leading industry participants.

The market projection were obtained based on analysis of historical market data and specific data and information associated with that market data, such as import/export volumes, shipping prices, macroeconomic statistics, etc. The market projections in the commissioned report are based on the following key assumptions:

- (i) Hong Kong, China, Asia, the United States, and Europe's economic and industrial development are likely to maintain a steady growth trend during the forecast period;
- (ii) Hong Kong, China and the world's social and political environment are likely to remain stable in the forecast period;
- (iii) related key industry drivers including implementation of China's favorable trade policies, the gradual recovery of the world economy, the growth of cross-border (from one country to another country) e-commerce activities and the continuous growth in trade volumes between China and other countries; and
- (iv) there is no extreme force majeure or industry regulations in which the Hong Kong air and sea freight forwarding markets may be affected dramatically or fundamentally.