

# Chairman's Letter to Shareholders



## Dear Shareholders,

In 2015, the volatility in commodity, currency and capital markets, together with China's slowing growth rate, were the headline themes preoccupying investors globally. However, we see that the absolute scale and opportunity of China's economy remains massive, with China in the midst of a structural transition towards a more service-and consumption-oriented economy. China's development may have entered a "new normal," but increasingly Chinese businesses are becoming more globally competitive as they focus on sustainable growth and innovation.

The macroeconomic environment has been turbulent and, internally, 2015 was a year of change. Investors such as CP Group, Itochu Corporation and Youngor provided substantial new capital to CITIC Limited. As a result, we have a much stronger balance sheet, which provides us with the financial flexibility to seize the right opportunities. Our transformation continues in 2016, as evidenced most recently by our decision to reposition our property business.

In this letter, I want to highlight four areas. First, I would like to explain why we have decided to partner with a leading Chinese property developer. Second, I will talk about our investments outside China and our continuing journey of "going global." Third, following a serious challenge in our brand and risk management, I want to provide assurance that strengthening oversight

for our affiliated companies is something we take very seriously. Finally, I will talk about how we are ensuring competitiveness across our businesses to create long-term value for you.

Our annual report, including my letter, is one of the important ways we communicate with you, our shareholders, as well as potential investors. We strive to improve our disclosure incrementally each year and offer detailed descriptions and reports on our businesses. There are a number of companies within CITIC Limited that are unlisted and as such don't report publicly. We have heard clear feedback from our shareholders that you wish to receive more information about these companies. Therefore, we've decided to spotlight one business each year. We will begin with CITIC Dicastal, the largest automobile aluminium wheel manufacturer and exporter in the world.

## Financial Performance

Naturally, our results reflect the events of the past year, and they are also indicative of our efforts to retain strong market leadership in our industries and to invest in innovation.

For 2015, our profit attributable to ordinary shareholders was HK\$41.8 billion, 5% more than last year. The bulk of the profit was contributed by financial services, particularly by CITIC Bank. Our results were affected by a significant loss recorded in our resources business due to

historically low crude oil prices as well as the depressed price of other commodities. A HK\$12.5 billion after tax non-cash impairment charge was also taken on our magnetite iron ore project in Western Australia, primarily due to a sharp decline in the price of iron ore, which was another factor that affected the bottom line.

In my letter to you last year, I said that we wanted to achieve a better balance between our financial and non-financial businesses. Unfortunately, progress in 2015 has been slower than we would have liked, and the impairment made was a key factor. Clearly, we still have a lot of work ahead to grow and improve the profitability of our non-financial businesses.

Our board recommends a final dividend of HK\$0.20 per share to shareholders, giving a total dividend of HK\$0.30 per share for the year 2015.

## Business Restructuring

One of our priorities in the past year was the restructuring of our property business, which was under two separate entities — CITIC Real Estate and CITIC Pacific Properties.

As we evaluated how best to position CITIC in today's changing property market in mainland China, we took a deep, critical look at our assets, operating model and position in the market. Given the size and scale of our residential land bank, it would be difficult for us to achieve a leading position on our own. As I wrote in my previous letter, our management team and I strongly adhere to the principle of aiming to be the best in what we do and a leader in the fields in which we operate. We also believe in partnering with leaders, particularly in businesses where we cannot independently achieve our full potential.

After careful consideration, we decided that it made good sense to align our property business with China Overseas Land and Investment, a company with a solid track record in China's residential property market. In addition to being a leader in its space, COLI is already well known to us: their largest shareholder, China State Construction Engineering Corporation, is a long-term strategic partner of CITIC Group, our company's largest shareholder. Earlier this month, we announced a deal through which we will sell our mainland residential property assets to COLI, and in return we will hold a

10% stake in COLI and some of its commercial real estate assets.

Our rationale for this transaction is simple. We believe COLI can best unlock the value of our quality residential land bank. This partnership also ensures that we can continue to participate in the growth of China's residential market. Fundamentally, this change in our property business model is a constructive, commercially sensible way to add value to CITIC Limited.

To manage our property business going forward, we established CITIC City Development and Investment Co. CITIC Limited's vice chairman and president, Mr Wang Jiong, is personally taking charge as chairman of the new company, CITIC City. Mr Liu Yong, who previously led CITIC Pacific Properties, now serves as CEO of CITIC City and is responsible for day-to-day operations.

We recognise that a growing number of property companies in the mainland are using the "asset-light" model, whereby new pools of capital are being raised through non-traditional channels. CITIC has a unique position in that we have a strong and large financial services business as part of our company, including affiliates such as CITIC Trust and CITIC Securities. As the property market becomes increasingly competitive, we are excited by the opportunity to integrate our financial resources with our core skills and expertise in property development. We believe this will enable us to capitalise on our strengths and advantages to build a sustainable property business.

## Expanding Our Global Footprint

While China continues to be a big part of the CITIC story, we've always been an outward-looking organisation, ready to follow our customers abroad and take advantage of growth opportunities in new markets. CITIC Dicastal, CITIC Construction and Special Steel, among others, have substantial global customer bases. By expanding our global footprint, our institutional skill base will grow meaningfully. Our past experiences, which include both successes and challenges, have delivered rich learnings. Our ability to understand local laws, practices and the culture of the regions in which we invest makes us a more logical and attractive global partner.

One of my personal highlights in 2015 was being in London for the Sino-British Business Summit, presided over by Chinese President Xi Jinping who was in the UK on a state visit, and British Prime Minister David Cameron. Both leaders were present on 21 October when I signed a contract for CITIC Construction to manage the construction of the Asia Business Port on the site of East London's Royal Albert Dock. Further expanding our global footprint, this project will create commercial and residential property in what is set to become London's third business district.

CITIC Dicastal invested over a year ago in an aluminium wheel plant in Michigan in the US, which began trial production early this year. CITIC Dicastal also operates a global facility in Germany, and at this point managing workers from different national backgrounds has become routine. You can read more about Dicastal in the Business Review section of our annual report.

Our largest overseas investment is the Sino Iron magnetite iron ore project in Western Australia. Although Sino Iron is now a small portion of an enlarged CITIC Limited, it is a major investment and we know its performance and future is on investors' minds.

In terms of project development, 2015 was a year in which Sino Iron made significant progress. Lines three and four entered commissioning in the last quarter, and production and export of magnetite iron ore concentrate from the first four lines continued to ramp up. I'm pleased to report that construction of the remaining two lines is nearing completion, with commissioning targeted for the first half of this year. We're on track to have all six lines running in 2016.

As we transition from construction to operation, our challenge will be to enhance the performance of the lines, lower production costs and improve efficiencies. An example is our recent decision to build a small airstrip and terminal onsite, which will reduce travel time for our workforce by 30% and deliver major cost savings, productivity gains and safety benefits over the life of the project. Our goal is to become the lowest cost magnetite producer in the world, providing long-term value for our shareholders.

As occasionally documented in the media, we continued to be in a legal dispute with tenement holder Mineralogy on a range of matters. In 2015, the Australian Federal

Court rejected Mineralogy's attempt to have CITIC vacate the Cape Preston port area where the Sino Iron project is located. We continue to exercise our rights under Australian law in the interests of the project, our company and you, our shareholders.

## Compliance, Risk and Brand Management

One of the companies in which we hold a 16.7% stake, CITIC Securities, has been in the news more often than we would have liked. CITIC Securities is the largest securities company in China, but it has been hurt by allegations of misconduct by a few senior managers.

Frankly, what happened at CITIC Securities was a wakeup call for us. We've had to admit that risk management and the education of employees on appropriate conduct had not kept pace with CITIC Securities' growth. As its single largest shareholder, we have a duty to stand by CITIC Securities to ensure that recent short-term challenges are overcome through appropriate internal changes to protect this valuable franchise and to ensure that the long-term prospects for the business remain positive.

Mr Zhang Youjun was elected Chairman of CITIC Securities early this year. A veteran of the securities industry in China, Youjun joined CITIC Securities in 1995, the year it was established. He also ran China Securities. Youjun is also a member of the senior management team at CITIC Group.

We have learned from CITIC Securities' recent experience and are redoubling our efforts to firmly embed CITIC Limited's strong risk management system across all of our subsidiaries and affiliates. We will work with subsidiaries on branding standards, as well as strengthening protocols and procedures associated with information management.

As our businesses expand and we pursue more partnerships, it's imperative to be disciplined about how our name is used. It's fair to say that CITIC is a well-recognised name in China, and this is increasingly true overseas. Our brand's reputation has been earned over time through the provision of quality products, services and infrastructure, as well as our overall socio-economic contributions to the regions in which we operate. It's critical that our heritage and brand are protected, and additional work is being done in this area.

## Ensuring a Competitive Edge to Create Long-Term Value

CITIC gets some criticism for being in “old economy” industries, such as banking and manufacturing. Yet they are the backbone of the country. We have built market leading positions and enjoy economies of scale in these industries, and we are fortunate to have deep roots in them. It is our view that they will not cease to be important and that manufacturing will continue to be very relevant in China. Naturally, businesses thrive more easily when faster economic growth is the norm. But it is during the tougher cycles when the excellent companies more clearly differentiate themselves from the mediocre and the weak.

CITIC is a conglomerate with diversified businesses, and we continue to believe that this model serves us well. Some investors find conglomerates somewhat hard to analyse and, as a result, assign a “conglomerate discount” to them. It is incumbent on us to explain our value strategy as clearly as possible to avoid this default approach by the market. Rather, if we explain our vision and plans, our competitive landscape and rationale behind each business decision, investors are likely to reward us and the discount will narrow.

Therefore, we want to reiterate our faith in our business model. Our diversity and commitment to excellence in all fields is our strength. We are invested in businesses that are here to stay and, within our industries, we will be the leaders even when enduring uncertain periods and downturns. For example, our special steel business leads the market and is more profitable than its peers, defying sceptics and riding through cycles. CITIC Dicastal continues to lead globally in the supply of aluminium wheels. Both companies embrace agile manufacturing and intelligent automation. The success of these businesses can be attributed not only to innovation but also basic good management, including aggressive cost control. So we know it to be true that internationally-capable Chinese manufacturers such as ours, when managed skilfully, have every opportunity to thrive.

Of course, we also participate in some “new economy” industries, such as environmental protection and ecommerce. They are small today, relative to the stalwart businesses in our group. Nevertheless, we will continue to grow and build them as we see private consumption

and the service sectors increasing and have noted the collective desire for improved quality of life. We believe these trends will open up new opportunities for us.

While we cannot control the external environment or commodity prices, what we can do is to ensure our businesses are well managed, especially during the tougher times, so that we are well positioned when the outlook improves. Staying ahead of the pack in terms of productivity and cost control requires constant discipline and continuous improvement.

As demonstrated by the repositioning of our real estate business, we continue to evaluate options to increase long-term value for investors. We are confident in the Chinese economy, in our business plans, and in our ability to seize the right opportunities, at the right time.

This company takes strategic planning and long-term value creation seriously. When we held our annual meeting with senior managers in January, we reflected on the fact that when we have faced economic challenges, we’ve come together as a team to manage through them and refocus ourselves on long-term value creation. This focus serves our company and it serves you, our shareholders. We know that investors’ patience is finite, and we want to assure you that we are both managing the businesses prudently and trying to ensure you earn a fair return on capital.

Our focus on the long-term will not be diverted by short-term difficulties, which will pass and be overcome. We urge you to keep the faith in China and in the industries that matter now, and will still matter to China in decades to come, through the ups and downs.

I am proud to lead a dedicated team at CITIC, and I thank them, our board, our investors and our lenders for their unwavering support. I ask everyone to take a long-term view and accompany us on the next phase of China’s exciting journey.



**Chang Zhenming**

*Chairman*

Hong Kong, 24 March 2016