

A Letter from Our Chairman

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Dear Shareholders,

In the last decade, all businesses around the world have faced unprecedented change and disruption from technology and geopolitical turmoil. In many industries, companies need to create new business models and reinvent themselves. Li & Fung has a long history of embedding an institutionalized mechanism for reinvention in our three-year planning process. We take a zero based approach in planning our business every three years and rather than waiting until changes are upon us, we want to anticipate changes and have a system of governance and management that facilitates this. The present Three-Year Plan (2017-2019) is one of the most important in our history and we developed a new business model to take advantage of the new digital world and create the supply chain of the future for the global movement of consumer goods. This is the first year of our new Three-Year Plan and I am happy to report that we are firmly on track to meet our goals.

Uneven Global Economic Growth

In the world's biggest economy and our biggest market, the US unemployment rate has been declining steadily and recently reached the lowest level in 17 years. Some of our customers in the retail sector saw the strongest holiday sales in more than a decade. This momentum has given the Fed higher confidence to unwind quantitative easing at a steady pace. While the US is seeing some economic green shoots, economic recovery is less visible in Europe. Asia, led by China, is seeing healthy economic trends with the fruits of decades of globalization turning into large middle class consumption and growing markets. I believe Asia will be the greatest winner in the economic growth story of the future.

US Tax Reform to Boost Economy and Consumption

Our customers in the US should benefit additionally from the Tax Cuts and Jobs Act. The National Retail Federation (NRF), which had been highly supportive of the tax reform and called its passing a major victory for retailers, estimates that savings from lower corporate tax bills can potentially translate to 500,000–1.5 million new jobs. We consider the US tax reform a positive development and expect stronger consumption to result from wage growth and the wealth effect.

International Relations and Trade Agreements

The world entered 2017 anticipating major shifts in the geopolitical sphere and trade relationships as a new US president took office. Economic and political relationships have always been intertwined. As of March 2018, US, Canada and Mexico already had multiple rounds of talks on changes to the North American Free Trade Agreement (NAFTA). Quick resolution seems unlikely given the election cycles in both the US and Mexico.

Sino-US economic relations continue to be rocky. While the two countries collaborate on a wide range of matters such as security in the Korean Peninsula, differences also manifest themselves in potential trade frictions. The recent announcement by the US on potential punitive duties on Chinese exports to America is of grave concern to the whole world and to Li & Fung in particular. While so far, the target list of potential products does not include our main product categories, we will be monitoring changes in the landscape and have taken steps to prepare our customers and suppliers for any potential fallout. The fact that we have one of the largest sourcing networks in the world should allow us to cope with any potential production dislocation in this Sino-US conflict. However, we are hopeful that the two powers will be able to resolve their differences without triggering a trade war.

The Trans-Pacific Partnership (TPP), which experienced a setback last year as the US withdrew, evolved into the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and regained momentum. The new pact elicits renewed interest not only from the US but also from the UK, which is exploring different trade pacts as Brexit looms. The development reaffirms our belief that protectionist sentiment is transient and free trade will eventually prevail.

The Death of Regular Commerce?

The past few years have seen the lopsided emphasis on the loss of market share by traditional brick-and-mortar retailers to the online market. However, by today, all the players are acutely aware of the impact and the need to use online data, communications and technology to service the consumer. The demarcation between brick-and-mortar and online retailers is fast becoming blurred as the concepts of omni-channel and O-to-O take hold. The two formats complement each other and it seems clear that consumers want both. The only question is just a matter of the varying split between online and offline channels for retailers and brands depending on their product lines. In fact, in recent years, we already saw key online retailers acquiring offline chains or building physical stores to enlarge their footprints and capture a broader customer base. I believe players with sound omni-channel strategies and the strong financial strength to implement this strategy will be the ultimate winners.

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The Supply Chain of the Future

By the end of this decade, we aim to digitalize major parts of the supply chain which is currently highly analog. A digitalized supply chain will be the prerequisite to work with the already highly digitized consumer space in terms of speed and inventory position. Also, a digitalized supply chain is key to data-aggregation which will enable advanced analytics for gauging and satisfying consumer demand. We are very pleased with our early successes in digitalization which is rapidly gaining traction with our customers and suppliers and I am grateful to our colleagues for their dedication and hard work in making the supply chain of the future a reality so quickly.

Yours sincerely,

William Fung Kwok Lun
Group Chairman