The Hong Kong Mortgage Corporation Limited
香 港 按 揭 證 券 有 限 公 司

www.hkmc.com.hk

Annual Report 2000 二零零零年年報

Financial Highlights

	2000	1999	1998
	HK$'000	HK$'000	HK$'000
FOR THE YEAR			
Net interest income	**357,711**	406,517	221,228
Profit after taxation	**233,106**	271,232	106,398
Mortgage purchases	**6,345,111**	1,341,803	11,440,327
Mortgage-backed securities issued	**-**	1,635,760	-
Debt issued	**6,625,000**	6,250,000	5,191,000
Mortgage insurance			
- net premiums underwritten	**29,174**	6,526	-
AT YEAR END			
Mortgage portfolio, net	**11,083,025**	8,726,776	11,376,485
Total assets	**14,844,616**	13,980,627	11,592,862
Debt securities	**11,621,000**	11,441,000	5,191,000
Mortgage insurance - risk in force	**1,552,765**	530,479	-
OTHER STATISTICS			
Net interest margin	**2.8%**	3.9%	4.9%
Capital-to-assets ratio	**12.3%**	10.1%	9.0%
Cost-to-income ratio	**25.1%**	21.9%	33.9%
Return on total assets	**1.8%**	2.5%	2.1%
Return on shareholder's equity	**9.4%**	12.1%	7.9%

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Chairman's Statement

The business environment presented many challenges to the Hong Kong Mortgage Corporation ("HKMC") in 2000. I am pleased to report that the Corporation was able to adapt its strategy to maintain a strong financial performance and convert many of these challenges into business opportunities.

The Honourable Donald TSANG, JP
Chairman
Financial Secretary

The business environment presented many challenges to the Hong Kong Mortgage Corporation ("HKMC") in 2000. I am pleased to report that the Corporation was able to adapt its strategy to maintain a strong financial performance and convert many of these challenges into business opportunities. Through a prudent widening of business scope, product innovation and effective marketing, we exceeded most of our targets despite the difficult business environment. The Corporation took a big step forward in its mission to promote home ownership in Hong Kong. The expanded Mortgage Insurance Programme ("MIP") helped over 4,600 families advance the purchase of their own flats. The decision to expand the range of Approved Sellers will enable the Corporation to form a strategic alliance with the Government housing agencies to promote home ownership for the lower income groups. Both homebuyers and banks will also benefit from the HKMC's initiative to standardize mortgage origination documents so as to make them more "user-friendly". Moving in step with the industry, the Corporation kicked off a project to build an electronic link with its business partners with a view to moving its operational processes onto an e-business platform.

The achievements of the HKMC in 2000 were set against a background of a difficult operating environment. A subdued residential property market, coupled with a dwindling loan-to-deposit ratio of the banking industry, resulted in a further intensification of the mortgage price war. Driven by severe competitive pressure, the prevailing mortgage rate fell sharply, to a historically low level of Prime rate minus 2.25%. Responding to the various incentives offered by banks, there was also a sharp surge in re-financing activities by homebuyers. The combined effect was a three-pronged problem of banks not being keen to offload mortgages, a sharp reduction in the profit margin on mortgage loans and a high prepayment rate.

The HKMC responded with agility and creativity to these challenges. The business strategy was adapted with a range of short-term measures to mitigate the adverse effect on profitability and long-term strategic moves to broaden the business to achieve sustained growth in future years.

In order to enhance the efficacy of its Mortgage Purchase Programme ("MPP"), the range of eligible mortgages was expanded in June to include those priced on the basis of the Hong Kong Interbank Offered Rate ("HIBOR"), staff mortgage loans and those held in company names. In July, the HKMC launched an innovative Mortgage-Bond Asset Swap programme to enable the banks to sell mortgage loans to the HKMC without depleting their pool of assets. The Programme offers advantages to banks in terms of yield enhancement, risk reduction, improved capital adequacy and liquidity ratios, and the ability to convert illiquid mortgages into highly liquid HKMC debt securities. Through these efforts, the HKMC purchased a total of HK$6.35 billion of mortgage loans in 2000 - nearly four times the 1999 figure. The Corporation attaches great importance to maintaining asset quality in expanding its mortgage portfolio. Through effective risk control and prudent purchasing criteria, the delinquency ratio of the retained portfolio was maintained at a low level. The proportion of loans overdue for more than 90 days was, at 0.42% in December 2000, significantly lower than the overall market ratio of 1.26%.

The HKMC also made significant strides in assisting homebuyers to accelerate home purchase through an expansion of the MIP to cover mortgage loans with loan-to-value ("LTV") ratios of up to 90%. Over 4,600 families took advantage of insurance provided under the Programme in 2000 to advance the purchase of their own flats. The banks also benefited from a timely increase of the lending ceiling for mortgage loans to 90% without incurring additional risk. For the HKMC, the expanded MIP provided a stable source of fee and premium income that is not susceptible to the banks' appetite to offload mortgage assets. Reflecting increasing public acceptance of the Programme, the market penetration rate of mortgage loans with insurance increased significantly, from 4.3% in 1999 to 8.0% in 2000.

On the funding side, a key priority in 2000 was to minimize the HKMC's cost of funds in order to mitigate the severe pressure on profitability from the sharp reduction in the interest margin of its mortgage portfolio. The Corporation adopted a pro-active pre-funding strategy to take full advantage of favourable market conditions during the year to issue debt securities at low cost. The Note Issuance Programme ("NIP") and Debt Issuance Programme ("DIP") provided an efficient and sturdy platform for the HKMC to execute this strategy. The Corporation issued a record HK$6.63 billion of corporate debt under the two Programmes in 2000, making it one of the most active issuers of debt securities in Hong Kong. Reflecting investor confidence in the HKMC, the average over-subscription ratio of the NIP issues increased from 5.4 times in 1999 to 8.2 times in 2000. Through successful execution of the pre-funding strategy, the Corporation achieved an average cost-of-fund for the NIP notes at sub-HIBOR in 2000, and estimated savings of about HK$36 million, compared with the alternative of issuing debt right before the mortgage purchase. The HKMC continued its effort to promote the development of a retail bond market in Hong Kong by reserving a portion of its NIP notes for subscription by retail investors. The issues were over-subscribed and subsequently listed for trading on the Stock Exchange.

Through these efforts of product diversification and effective cost control, the HKMC succeeded in mitigating to a significant extent the adverse impact of the sharp fall in mortgage rates and the high mortgage prepayment rate on its profitability. Profit after tax was maintained at a healthy level of HK$233.1 million, despite a significant drop of 28.2% in the net interest margin. The Corporation also produced a return on equity of 9.4% and a return on assets of 1.8%, broadly in line with those of local banks of comparable size. It did so whilst maintaining a strong capital-to-asset ratio of 12.3%.

The HKMC made two important strategic decisions in 2000 which provide new impetus for growth in its business and profitability in future years.

In December, the Board of Directors decided to expand the range of Approved Sellers to include the Government housing agencies, other public bodies and property developers. Through the expanded Programme, the HKMC will be able to form a strategic partnership with the Government housing agencies to promote home ownership for the lower income groups in Hong Kong.

The Government housing agencies are facing increasing financing needs as they are relying less on providing “bricks and mortar” and more on providing subsidized mortgage loans to promote home ownership. The HKMC provides a convenient and cost-effective channel for the agencies to offload mortgage loans in order to replenish funding for their subsidized mortgage programmes. At the same time, a steady supply of mortgage loans from these programmes would enable the HKMC to expedite the launch of its mortgage-backed securitization (“MBS”) programmes. The considerable synergy to be generated from this partnership will provide a “win-win” solution to both parties. The initiative was well received by the Government housing agencies. The Hong Kong Housing Authority decided in early 2001 that it would sell HK$17-18 billion of mortgage loans originated under its Home Purchase Loan Scheme to the HKMC in the period up to September 2002.

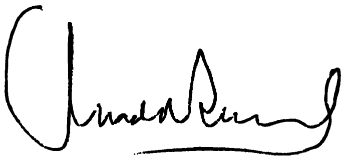
Another major strategic decision made by the HKMC during the year was to establish an on-line communication link with its business partners to conduct transactions over the Internet. The Corporation's mortgage purchase and mortgage insurance businesses have become an important integral part of the mortgage industry in Hong Kong. It is important for the HKMC to move in step with its business partners, the banks and the mortgage reinsurers, to embrace the e-business technology as a means to enhance efficiency and contain costs as it further expands its business. In July 2000, the Board of Directors approved the development of an Integrated Information Delivery System to establish the e-business platform. After completion in the fourth quarter of 2001, the on-line communication link will support the processing of mortgage purchase and mortgage insurance applications over the Internet. It will substantially enhance efficiency and productivity by shortening the process cycle and eliminating to a large extent manual processes. In order to ensure a proper interface with the systems of our business partners, a Working Group involving the banks and mortgage reinsurers has been formed to collate feedback on system design and implementation.

Through the MPP and MIP, the HKMC has gained considerable experience in various facets of mortgage business in Hong Kong. The Corporation intends to make good use of its knowledge of best market practice by raising the industry standard in mortgage origination for the benefit of both banks and homebuyers. Specifically, the HKMC launched a project in 2000 that aims to standardize the mortgage origination documents in Hong Kong. Currently, these documents vary significantly among banks in terms of both content and presentation. In some cases, the documents still retain clauses drafted in archaic language. With the support of the banks and the legal fraternity, the HKMC set up a Steering Committee to coordinate the preparation of a set of model documents that represents best market practice. The documents will be drafted in simple English with a Chinese translation. The opportunity will be taken to review the key terms and conditions to ensure a proper balance in the rights and obligations between the banks and the homebuyers. Other than enhancing consumer awareness, the model documents will help reduce the lead time and cost for the issuance of MBS by removing the need for investors and credit rating agencies to conduct due diligence on the documents. Good progress had been made during the year. It is expected that the draft model documents will be issued for consultation in the first half of 2001. I would like to take this opportunity to thank Mr. Justice Henry Litton, The Law Society of Hong Kong, Hong Kong Bar Association and The Law Faculty of The University of Hong Kong for contributing their valuable time and expertise to this important project.

Looking ahead to the year 2001, I am confident that the HKMC will be even more effective in performing its pioneering role in developing the residential mortgage and capital markets in Hong Kong.

With the expansion of the MPP, and having secured the major transaction of HK$17-18 billion of mortgage purchase from the Hong Kong Housing Authority, the HKMC is firmly on track to build a critical mass for its key businesses. We expect a significant growth in the size of the retained mortgage portfolio in 2001 through purchases from banks, the Government housing agencies and property developers. This will provide a solid platform for the Corporation to launch a new and active MBS Programme targeting both institutional and general investors. To meet its increased financing requirements in a cost-effective manner, the Corporation now needs to widen its investor base to include overseas investors. With this in mind, it has decided to seek credit ratings to pave the way for the launch of a multi-currency Medium Term Notes Programme. In response to the requests of homebuyers and the banks, the Corporation is also planning to further expand the MIP to include equitable mortgages secured on residential properties under construction.

Finally, I would like to pay tribute to my fellow Directors on the Board for their invaluable advice and contributions, without which the HKMC would not have been able to achieve so much within such a short time. I would also like to thank the staff of the HKMC for their dedication, hard work and innovative thinking. The HKMC will continue to work closely with the banks, the capital market participants and the insurance industry to further develop the secondary mortgage market in Hong Kong.



Donald Tsang
Chairman

The Honourable Donald TSANG, JP
Chairman
Financial Secretary

Mr. Joseph YAM Chi-kwong, JP
Deputy Chairman
Chief Executive,
Hong Kong Monetary Authority

Board of Directors

Mr. Dominic WONG Shing-wah, GBS, OBE, JP
Director
Secretary for Housing

Mr. Stephen S. K. IP, JP
Director
Secretary for Financial Services

Mr. Tony LATTER, JP
Executive Director
Deputy Chief Executive,
Hong Kong Monetary Authority

Mr. Norman CHAN Tak-lam, SBS, JP
Executive Director
Deputy Chief Executive,
Hong Kong Monetary Authority

Dr. The Honourable David LI Kwok-po, LLD (Cantab), JP
Director
Legislative Councillor
Chairman and Chief Executive of The Bank of East Asia, Limited

Mr. Ronald Joseph ARCULLI, JP
Director
Managing Partner of Arculli and Associates

Mr. Eddy C. FONG, SBS, JP
Director
Certified Public Accountant and Partner of PricewaterhouseCoopers

The Honourable Bernard Charnwut CHAN
Director
Legislative Councillor
Executive Director, Asia Financial Group

The Honourable SIN Chung-kai
Director
Legislative Councillor

Ms. Anita FUNG
Director
Director, Head of Fixed Income and Derivatives, Asia-Pacific, Treasury and Capital Markets, The Hongkong and Shanghai Banking Corporation Limited

The Honourable CHAN Kwok-keung
Director
Legislative Councillor

Mr. NG Kwok-wai
Director
Chief Executive, Allied Capital Resources Limited

Mr. Paul A. THURSTON
Director
Assistant General Manager & Head of Personal Financial Services, The Hongkong and Shanghai Banking Corporation Limited

Professor Andrew Chi-fai CHAN, Ph.D.
Director
Associate Dean, B.A. Faculty, The Chinese University of Hong Kong
Chairman of Consumer Council

Management Team

1. Mr. Peter Pang, JP
2. Mr. Philip Li
3. Mr. Kenny Fok
4. Ms. Susie Cheung

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1. Mr. Raymond Luk
2. Mr. Jonathan Chan
3. Mr. Zarino Tong
4. Mr. Raymond Liu
5. Mr. Desmond Cheng
6. Ms. Angela Leung
7. Ms. Frances Ng
8. Mr. Paul Ting
9. Ms. Grace Lee
10. Ms. Irene Mok
11. Ms. Melina Lai

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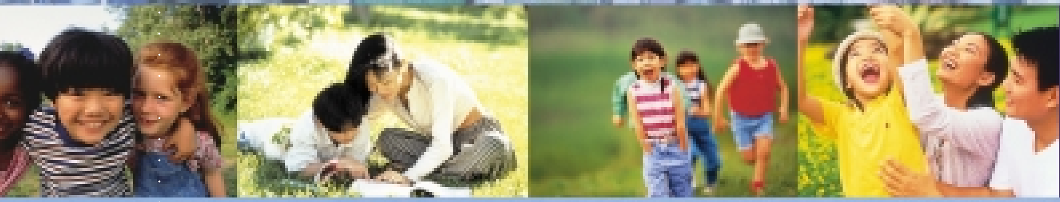
Organisation Structure

As at end of March 2001

- **Chief Executive Officer**
  Peter Pang
  - **Senior Vice President**
    (Operations)
    Kenny Fok
    - **Vice President**
      (Credit & Risk)
      Jonathan Chan
    - **Vice President**
      (Operations)
      Irene Mok
    - **Vice President**
      (Marketing & Research)
      Angela Leung
    - **Vice President**
      (Pricing)
      Desmond Cheng
  - **Vice President**
    (Administration & Human Resources)
    Melina Lai
  - **Vice President**
    (Corporate Development)
    Frances Ng
  - **Vice President**
    (Internal Audit)
    Paul Ting
  - **Senior Vice President**
    (Finance)
    Philip Li
    - **Vice President**
      (Information Technology)
      Zarino Tong
    - **Vice President**
      (Financial Control)
      Raymond Luk
    - **Vice President**
      (Treasury)
      Raymond Liu
  - **General Counsel & Company Secretary**
    Susie Cheung
    - **Legal Counsel**
      Grace Lee

Business
Review



The HKMC exceeded most of its business targets in 2000 and further consolidated its role as a pioneer in the secondary mortgage market with the launch of a variety of innovative initiatives, despite a difficult market environment.

PERFORMANCE HIGHLIGHTS

The HKMC exceeded most of its business targets in 2000 and further consolidated its role as a pioneer in the secondary mortgage market with the launch of a variety of innovative initiatives, despite a difficult market environment. The Corporation made further progress in its three core missions:

- to enhance the stability of the banking sector through offering a reliable source of liquidity;
- to promote wider home ownership in Hong Kong; and
- to facilitate the growth and development of the mortgage-backed and debt securities markets in Hong Kong.

In 2000, the HKMC:

- purchased HK$6.35 billion of mortgage loans – significantly exceeded the 1999 figure of HK$1.3 billion by nearly 4 times and the Year 2000 target of HK$4 billion by 58.8%, despite a difficult market environment;
- issued a record amount of HK$6.63 billion of debts and achieved a significant saving in funding cost of about HK$36 million, through adopting a pro-active pre-funding strategy;
- exceeded the target of writing insurance for mortgage loans of HK$4.8 billion by 27.1% to HK$6.1 billion;
- maintained superb asset quality with 0.42% and 0.03% of loans overdue for more than 90 days in the retained portfolio and the mortgage insurance portfolio respectively, as compared with the industry average of 1.26%.

As a result, the HKMC succeeded in mitigating to a significant extent the severe adverse impact of the sharp fall in mortgage rates and the high mortgage prepayment rate on the Corporation's profitability. Most notably, in 2000, the Corporation:

- maintained profit after tax at a healthy level of HK$233.1 million, a moderate reduction of 14% from the 1999 figure of HK$271.2 million, despite the 28.2% drop in the net margin of its interest-bearing assets from 3.9% to 2.8% in 2000;
- provided a return on shareholder's equity of 9.4% – as against 12.1% in 1999;
- provided a return on total assets of 1.8% – as against 2.5% in 1999;
- maintained a strong capital-to-assets ratio of 12.3% – as against 10.1% in 1999; and
- achieved a low cost-to-income ratio of 25.1% – substantially below the banking sector average of 36.4%.

PRODUCT INNOVATION

The Corporation responded swiftly and creatively to the challenging business environment in 2000:

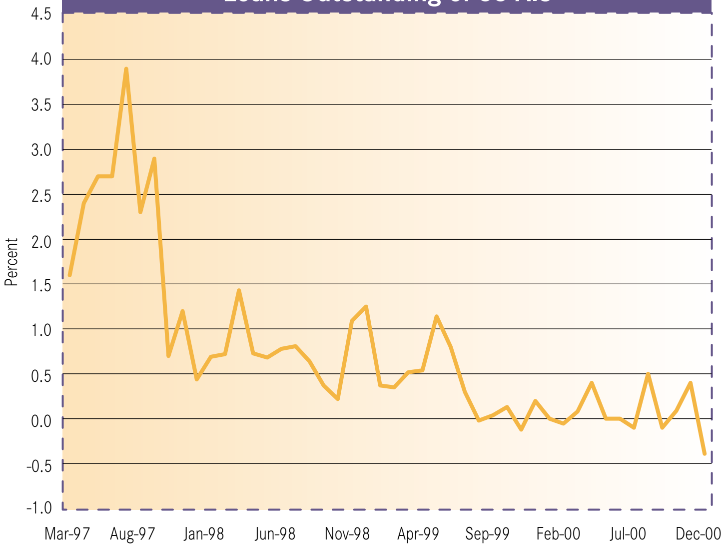
- In June 2000, it introduced the Mortgage-Bond Asset Swap Programme for banks to swap mortgage loans with the debt securities issued by the Corporation. This enables the banks to sell mortgage loans to the HKMC without depleting their pool of assets. The inaugural deal of HK$600 million was arranged with Dao Heng Bank in July.
- In August 2000, the Corporation expanded the Mortgage Insurance Programme ("MIP") which allows homebuyers to obtain mortgage loans up to 90% of the value of the property. This has resulted in an increase in market penetration rate of the MIP from 4.3% to 8%.
- In December 2000, the Corporation widened the scope of Approved Sellers under the Mortgage Purchase Programme ("MPP") to include Government housing agencies, other public bodies and property developers. This achieves the dual objectives of helping the Government housing agencies meet their financing needs and enlarging the source of mortgage purchase for the HKMC.

MORTGAGE PURCHASE ACTIVITIES

Market environment — slow growth in mortgage loans

Year 2000 turned out to be another difficult year for the mortgage industry. Despite a sharp rebound of 10.5% in the GDP, the total outstanding principal balance of residential mortgage loans almost remained static. According to the Hong Kong Monetary Authority's ("HKMA's") monthly survey of 33 Authorized Institutions ("AIs") in Hong Kong, the total number of new loans made increased only slightly by 1.13% to 82,704 loans (81,771 loans in 1999). The total principal amount of new loans made actually dropped by 3.0% to HK$115.6 billion (HK$119.2 billion in 1999). At year-end, the total amount of residential mortgage loans outstanding recorded a scanty 0.8% increase to HK$482 billion.

Figure 1: Monthly Growth Rate of Gross Residential Loans Outstanding of 33 AIs



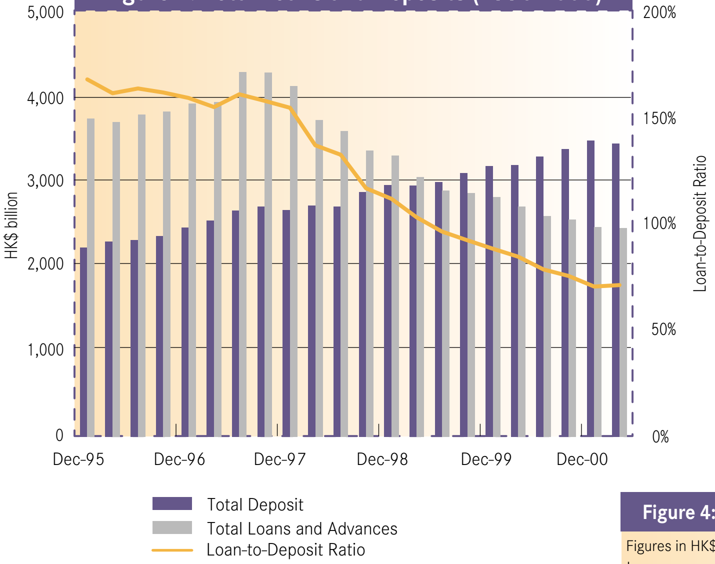
Source: HKMA

The slow growth in mortgage loans was mainly due to a combination of the weak sentiment of homebuyers and the active mortgage refinancing activities. Potential homebuyers were generally concerned about the possible adverse impact of the large supply of new housing units (estimated at around 28,000 to 30,000 units per annum in the next two years) on property prices. The several rounds of short-lived rally in property sale and prices in the last two years had also made them more cautious. The intensive mortgage price war had resulted in a sharp surge of refinancing activities in 2000 (Figure 5). Reflecting the significant drop in the value of residential properties in recent years, mortgage loans were generally re-financed at a substantially lower value. According to the HKMA's monthly survey, the average size of mortgage loans dropped by 13.3% from HK$1.5 million to HK$1.3 million during the year.

Intensive competition for mortgage loans continued

The slow recovery of corporate lending and the dwindling loan-to-deposit ratio of the banks continued to exert strong pressure on the banks to compete for consumer lending. Figure 2 shows that the loan-to-deposit ratio of all Authorized Institutions dropped by more than 50% from 168% at the end of 1995 to 71% at the end of 2000. The competition for consumer loans focused particularly on residential mortgages as they have demonstrated excellent asset quality in the aftermath of the Asian financial crisis. The delinquency ratio of mortgage loans was maintained at a low level of 1.26% at the end of 2000, substantially below the delinquency ratio of 4.49% for the total loan portfolio of the local banks.

Figure 2: Total Loans and Deposits (1995-2000)



Source: HKMA and CEIC

High prepayment and refinancing of mortgages

A direct result of the intense price competition was a sharp surge in the re-financing of mortgage loans as borrowers responded to the banks' various incentives and tried to reduce outstanding debts that were incurred in the previous higher interest rate environment.

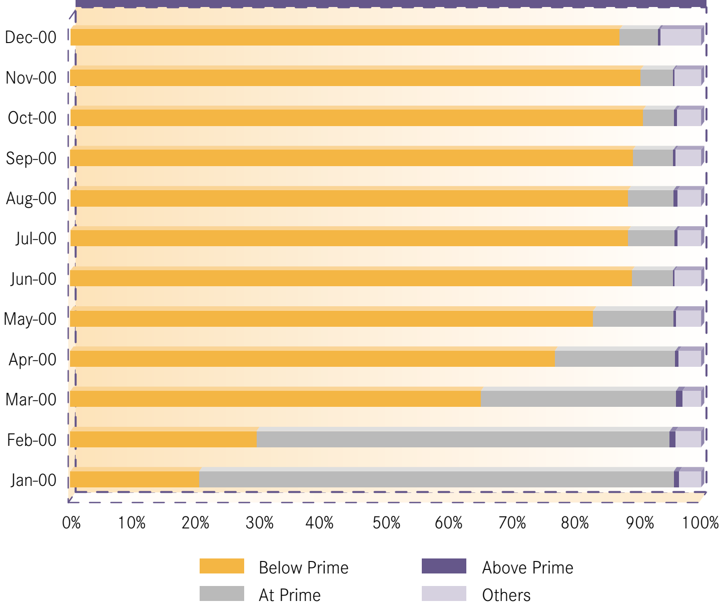
Many banks offered mortgage loans at interest rates below their Prime rates in order to attract more mortgage business. During the year, the prevailing mortgage rate fell sharply from around the Prime rate to Prime rate minus 2.25%. The HKMA's monthly survey also showed that the percentage of new loans originated at sub-Prime rate increased sharply from 10.5% in December 1999 to 87.1% by the end of 2000 (Figure 3).

Figure 4: Gross New Loans Made Between 1996 and 2000 (33 AIs)

Figures in HK$ million	1996	1997	1998	1999	2000
January	9,312	20,626	8,305	8,572	10,506
February	8,999	18,799	8,178	7,192	9,961
March	11,012	16,797	12,627	9,387	10,780
April	11,181	22,713	10,275	9,147	10,095
May	13,247	26,047	9,526	13,754	9,727
June	14,627	25,529	9,384	14,088	10,093
July	17,659	32,495	9,314	12,173	10,058
August	13,397	24,917	8,427	9,708	11,452
September	11,673	25,452	6,425	8,861	8,554
October	15,499	17,865	6,416	8,124	8,910
November	16,807	15,299	10,298	7,715	9,552
December	19,544	9,760	13,239	10,504	5,918
Gross new loans made	162,957	256,299	112,414	119,225	115,606
yoy % change	76.9	57.3	-56.1	6.1	-3.0
Outstanding balance at December	330,426	425,469	459,338	478,244	481,958
yoy % change	21.2	28.8	8.0	4.1	0.8
Net growth	57,731	95,043	33,869	18,906	3,714

Source: HKMA

Figure 3: Trend of Pricing of New Mortgage Loans in 2000

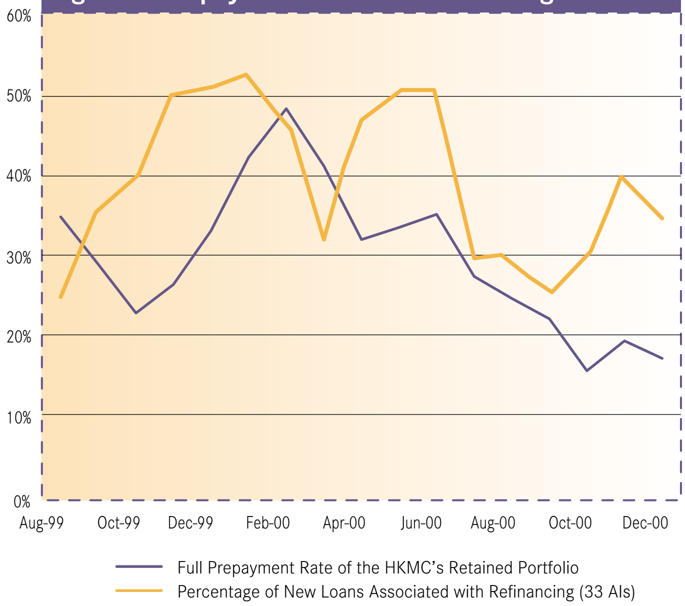


Source: HKMA

According to the monthly survey by the HKMA, gross new mortgage loans originated in 2000 amounted to HK$115.6 billion (3% less than in 1999), while the amount of loans outstanding only grew by HK$3.7 billion, or 0.8%, to HK$482 billion. The balance of HK$111.9 billion was accounted for by repayments and refinancing activities.

This pattern was also evident in the annualized prepayment rate of the HKMC's retained mortgage portfolio, which reached a peak of 49.9% in February before gradually easing to 18.5% in December 2000.

Figure 5: Prepayment Rate and Refinancing Activities



Note:Data on the percentage of new loans associated with refinancing was available starting August 1999

Source: HKMA/HKMC

HKMC's response

The HKMC was proactive in adapting its business strategy to the changed market conditions. In particular, a three-pronged approach was adopted to maintain profitability and to further expand its businesses:

- to build an enlarged platform for continued growth of the MPP by expanding the scope of eligible mortgage loans and the range of Approved Sellers to include new strategic partners, in particular the Government housing agencies;
- to minimize funding cost by adopting a pro-active pre-funding strategy to capture market opportunities to issue debts at low cost; and
- to enhance operational efficiency through developing an electronic linkage with business partners to conduct e-business over the Internet.

Widening of the scope of eligible mortgage loans

In response to the challenging market environment, the Corporation adopted a prudent and incremental approach to widen the range of mortgage loans eligible for sale under the MPP. In June 2000, the Programme was expanded to include mortgage loans held in company name, HIBOR-based mortgage loans and staff mortgage loans.

Loans held in company name

Apart from loans to an individual, it has been an accepted practice for banks in Hong Kong to grant mortgage loans on properties held in company names. In order to contain the credit risk exposure of this type of mortgage loan, the Corporation applies the following criteria to confine its purchase to mortgage loans on properties that are used for residential rather than investment purpose:

- the company is 100% owned by its shareholder/director(s) who are the effective borrower(s);
- owner-occupancy;
- the company is incorporated in Hong Kong; and
- the company does not have any business activities apart from the holding of the property.

HIBOR-based mortgage loans

Taking advantage of the low and stable interbank interest rates in Hong Kong, the banks launched a variety of HIBOR-based mortgage products to offer attractive mortgage rates to borrowers. The mortgage rate is usually subject to a cap (typically set at Prime) to alleviate the borrowers' concern about possible sharp surges in HIBOR as seen in 1998. In June 2000, recognizing the market demand for these products, the Corporation added HIBOR-based mortgage loans as an eligible product under both the MPP and MIP.

Staff mortgage loans

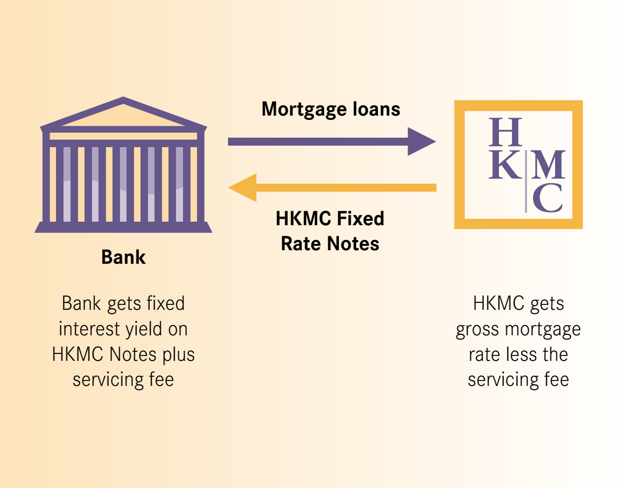
Some banks, especially those that are not in the mortgage business, are interested in offloading their staff mortgage loans. A common feature of these staff loans is the low repayment risk as the monthly repayment is deducted directly from the employee's salary. On the other hand, as the LTV ratio and debt-to-income ("DTI") ratio of the staff mortgage loans at origination are generally higher than commercial-based mortgage loans, the credit risk would increase substantially when the staff's employment with the bank is terminated. To address this risk, the HKMC adopts a risk-based approach in pricing such transactions and, where appropriate, requires the seller to set up a reserve fund to absorb an agreed amount of default losses.

The addition of the three types of eligible mortgage loans had made a significant contribution to mortgage acquisition in 2000. During the year, the Corporation bought a total of HK$1.65 billion of staff mortgage loans, HK$605 million of HIBOR-based mortgage loans and HK$161 million of mortgage loans held in company name.

Innovation in deal structure — Mortgage-Bond Asset Swap Programme

The Asset Swap Programme was an initiative launched in May 2000 to enable the banks to sell mortgage loans to the HKMC without depleting their pool of assets. The arrangement became feasible as the mortgage price war had reduced the mortgage rate to a level close to the annualized yields of HKMC's unsecured debt securities. Under the arrangement, the Corporation issues notes under its Debt Issuance Programme (DIP) directly to the counter-party bank in exchange for an equivalent amount of mortgage loans from the bank.

Figure 6: Asset Swap Structure



By entering into an asset swap transaction with the HKMC, instead of holding on to the loans, the banks could achieve a yield enhancement when the combined income from the bond coupon and the servicing fee exceeds the interest income from the mortgage loans. The arrangement therefore offers a win-win solution for both parties. In addition to the yield pick-up, the bank can derive other benefits from the asset swap transaction:

- Higher return: after selling the mortgage loans to the HKMC, the bank may release the related general and specific loan provisions which usually range from 0.5% to 1.0% of the total loan amount;
- Lower risks: instead of holding a portfolio of mortgage loans, the bank will be holding an HKMC paper which is of a higher credit quality;
- Better financial ratios: there will be savings in capital charge for the bank as the HKMC paper carries a 20% risk-weighting as against a 50% risk-weighting for a mortgage asset under the capital adequacy regime. The liquidity ratio of the bank will also be enhanced as the HKMC's debt securities qualify as liquefiable assets under the Banking Ordinance; and
- Liquidity: through the asset swap, the banks convert an illiquid mortgage loan portfolio into a liquid asset, as the HKMC paper can be off-loaded easily in the bond market.

In 2000, the Corporation concluded one asset swap transaction and purchased HK$600 million of mortgage loans under this Programme.

Widening the scope of Approved Sellers to include Government housing agencies and property developers

In December 2000, the Board of Directors approved a widening of the range of Approved Sellers under the MPP to include the Government housing agencies, other public bodies and property developers. The expanded Programme enables the HKMC to form a partnership with the Government housing agencies to promote homeownership for the lower-income groups. It will also substantially enlarge the source of mortgage purchase for the HKMC.

The Housing Authority is a major originator of subsidized mortgage loans for the lower-income groups in Hong Kong. It is putting increasing emphasis on providing financing in the form of subsidized loans to promote home ownership. Forming a partnership with the HKMC would produce a lot of synergy in achieving this common objective. The Corporation provides a convenient and cost-effective channel for the Housing Authority to offload subsidized loans under the Home Purchase Loan Scheme so that it can replenish funding for this housing loan programme. At the same time, a steady supply of subsidized mortgage loans from this programme would enable the HKMC to expedite the launch of its MBS programmes. The expanded MPP therefore provides a "win-win" solution to all parties concerned.

In order to boost the sale of new housing units, many property developers, including the Housing Society, provide top-up loans to homebuyers who are not able to pay for the 30% down payment. In general, the top-up loans are up to 20% of the value of the property. Many property developers are inclined to offload their top-up mortgage portfolios as loan origination is not their core business. The purchase of the top-up loans is not expected to adversely affect the asset quality of the HKMC's retained portfolio. The banks that provide the 70% co-financing are required by the HKMA to apply its normal underwriting criteria to such loans and to take account of any capital and interest repayments on the top-up loan in assessing the DTI ratio. As an additional safeguard, the HKMC would normally enter into a risk-sharing arrangement with the seller by setting up a reserve fund to absorb an agreed amount of default losses.

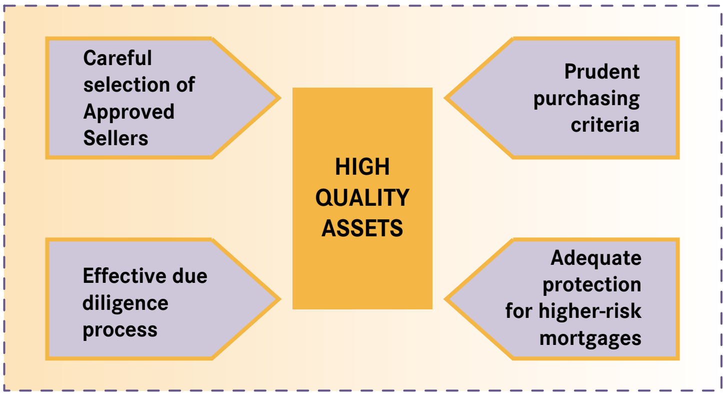
Mortgage purchase in 2000

Through a prudent widening of the scope of eligible mortgage products, product innovation and effective marketing, the Corporation continued to make significant progress in mortgage purchase despite the difficult market environment. In 2000, the Corporation purchased 4,380 mortgage loans with a total principal amount of HK$6.35 billion. The figure significantly exceeded the 1999 mortgage purchase amount of HK$1.3 billion by nearly four times and the Year 2000 business target of HK$4 billion by 58.8%. As a result, the Corporation's retained mortgage portfolio increased by 27.1% to reach HK$11.1 billion by year end.

The expansion of the scope of Approved Sellers to include the Government housing agencies and property developers is expected to generate a significant increase in mortgage purchase activities in future years. Following the Board's approval in December 2000, the Corporation mounted a major marketing campaign targeting these two new groups of Approved Sellers. The general response is very positive. In February 2001, the Housing Authority agreed to sell HK$17 – $18 billion of mortgage loans originated under its Home Purchase Loan Scheme to the HKMC in the period up to September 2002.

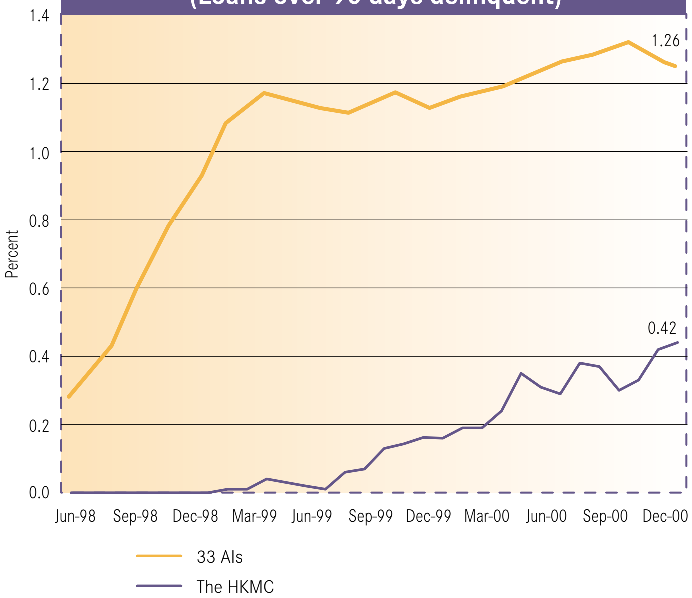
High Quality of the Mortgage Portfolio

The HKMC attaches great importance to maintaining good asset quality in expanding its MPP. This is necessary to protect the long-term profitability and credit standing of the Corporation, which in turn will help lower its funding cost. The HKMC adopts a four-pronged approach in upholding the asset quality of its mortgage portfolio:



The effectiveness of the HKMC's prudent purchasing criteria and risk management processes is borne out by the track record of the low delinquency of mortgages in its retained portfolio. It is noteworthy that the mortgage portfolios of banks in Hong Kong in general have performed very well by international standards – despite the recent economic downturn. The industry average of loans overdue for more than 90 days for the 33 Authorized Institutions surveyed by the HKMA was 1.26% in December 2000. The HKMC's portfolio considerably outperformed this average with a ratio of 0.42%.

Figure 7: Comparison of Delinquency Ratio of the HKMC's Portfolio and the Mortgage Market (Loans over 90 days delinquent)



MORTGAGE-BACKED SECURITIZATION ACTIVITIES

The HKMC launched its back-to-back MBS Programme in 1999 with two issues worth a combined HK$1.6 billion with Dao Heng Bank and American Express Bank. The establishment of this Programme signaled both the start of the second phase of the HKMC's business plan and a new era of product diversification for the Hong Kong MBS market.

The MBS issued under the Programme adopt a back-to-back and pass-through structure. This involves the HKMC acquiring mortgage loans from a bank and selling them directly to a bankruptcy-remote special purpose company ("SPC"). The SPC then issues MBS back to the bank with the HKMC's guarantee for the timely payment of principal and interest on the MBS. The HKMC has appointed Dao Heng Bank, Deutsche Bank, J.P. Morgan and Merrill Lynch Far East as market makers for MBS issued under the Programme.

Due to keen competition for mortgage loans and the banks' strong inclination to hold on to their mortgage loan portfolios, no new issues had been arranged under the back-to-back MBS Programme in 2000. Nevertheless, the Corporation has been keeping closely in touch with the market makers to review the operation and structure of the Programme. While the operation of the Programme, as demonstrated by the two outstanding issues, has been smooth, it was agreed that converting the pass-through structure into a bond style structure would further improve the liquidity of the MBS in the secondary market. The HKMC intends to adopt the revised structure for future issues. With the expanded scope of the MPP, and having secured the HK$17-18 billion contract for loan purchase from the Housing Authority, the HKMC plans to launch an MBS Programme targeting the institutional and general investors in the second half of 2001. The Programme will add further depth to the financial system and the MBS market in Hong Kong.

MORTGAGE INSURANCE ACTIVITIES

The MIP was introduced in March 1999 with the following objectives:

- to enfranchise a new class of homebuyers who were previously unable to afford the down-payment to achieve property ownership;
- to allow banks to satisfy their clients' needs without exposing themselves to additional risk;
- to provide a new line of business to the local insurance industry; and
- to provide a new line of profitable business for the HKMC.

Under the initial Programme, the HKMC provided insurance cover for a fee to its Approved Sellers for an amount up to 15% of the value of the property to enable homebuyers to secure mortgage loans up to an 85% LTV ratio. The HKMC hedges the exposure of the insurance by taking out reinsurance with the Approved Reinsurers.

Expansion of MIP to 90% LTV ratio

In response to a strong demand from homebuyers and banks to increase the lending ceiling for mortgage loans, the HKMC expanded the MIP in August 2000 to cover mortgage loans with LTV ratios of up to 90%.

In order to properly address the additional credit risk of mortgage loans with LTV ratios above 85%, the Corporation engaged Trowbridge, an international actuarial consulting firm, to construct an actuarial model to determine the premium rates for the expanded Programme. The following additional underwriting criteria are also applied as a risk-mitigating measure:

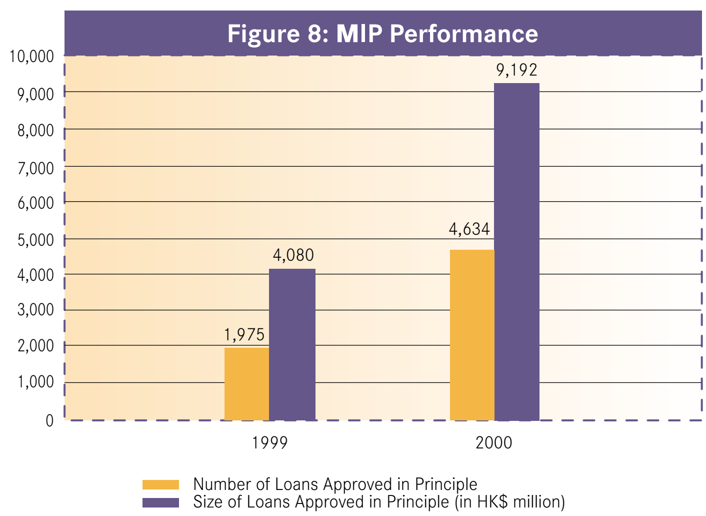
- the exclusion of applicants who are self-employed (except doctors, accountants and lawyers) as the level of their income, and hence repayment ability, is less certain;
- the exclusion of mortgage arrangement that involves the use of bridging loans for financing the funding gap between the sale of an existing property and the purchase of a new property;
- credit check on the applicant by external credit agencies; and
- reduce the maximum term of the mortgage loan from 30 years to 25 years.

MIP Advertising Promotional Campaign

As a reflection of the prudent underwriting policy adopted by the HKMC, the delinquency (overdue for more than 90 days) ratio of the mortgage loans covered by the MIP was maintained at a low level of 0.03% in 2000.

In order to further enhance consumers' awareness of the MIP, the Corporation mounted a major advertising campaign to tie in with the launch of the 90% LTV product. Started in August 2000, the campaign provided sustained media advertising through newspapers, magazines and bus panels, as well as detailed product information through printed leaflets and linkage to the Internet websites of the major property agencies.

Through the expanded Programme and the advertising campaign, the HKMC achieved a significant growth in business volume under the MIP in 2000. The number of participating banks increased from 30 to 37 during the year. The Corporation approved a total of 4,634 applications in 2000 involving total mortgage principal amount of HK$9.19 billion, more than doubled the corresponding figures of 1,975 applications and mortgage principal amount of HK$4.08 billion for 1999. As a result, the market penetration rate of mortgage loans with insurance provided by the HKMC increased to 8.0% in 2000 (4.3% in 1999). The fact that secondary property transactions accounted for 87% of the applications received in 2000 indicates that the Programme has also served to improve the liquidity of the secondary property market in Hong Kong.



The HKMC has received numerous requests from homebuyers and the banks for a further expansion of the MIP to cover equitable mortgage loans secured on residential properties under construction. The Corporation conducted a survey of its Approved Sellers in early 2001 with the objective of understanding the risks of equitable mortgage loans and the mitigating measures adopted by the banks to address these risks. Taking into account the findings of the survey and the discussions with the Approved Reinsurers, the Board of Directors decided in March 2001 to expand the MIP to cover equitable mortgage loans.

FUNDING ACTIVITIES

With its good credit standing, the HKMC has built an extensive investor base for its NIP and DIP. Supported by active mortgage purchase activities, the Corporation further consolidated its status as a major issuer of debt securities in Hong Kong. In 2000, the Corporation issued nine debts issues for an aggregate amount of HK$6 billion under the NIP and two issues for HK$625 million under the DIP. The proceeds were used to fund the purchase of HK$6.35 billion of mortgage loans and to redeem debts matured during the year.

The sharp decline in mortgage rates (see Figure 3) reinforces the need for the HKMC to minimize its cost of fund. Market conditions were favourable for debt issuance in 2000, especially in the first half of the year, as the abundance of liquidity created strong demand for bonds and the bond-swap spread was exceptionally wide. The HKMC adopted a pro-active pre-funding strategy to take full advantage of the market conditions. The successful execution of the strategy enabled the Corporation to achieve a significant saving in funding cost of about HK$36 million, compared with the alternative of issuing debts right before the mortgage purchases.

Investor Demand

Demand for HKMC debt securities – stimulated by increased secondary market liquidity – increased markedly in 2000. Launched through the tender mechanism administered by the HKMA, the HKMC's NIP issues attracted enthusiastic response from the financial institutions as well as institutional and retail investors. The average over-subscription ratio of the NIP issues increased sharply from 5.4 times in 1999 to 8.2 times in 2000.

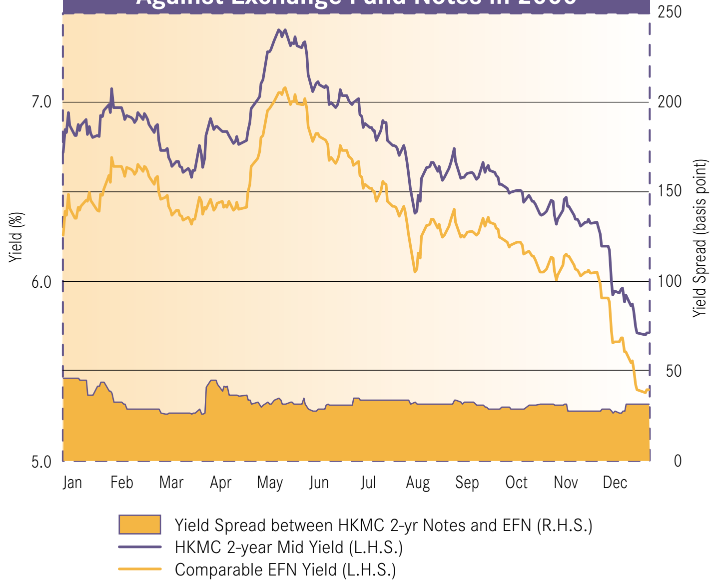
The appeal of NIP notes as a high-quality investment alternative to Exchange Fund Notes ("EFNs") with an attractive yield pick-up has also been demonstrated. Yield spreads of HKMC securities over comparable EFNs tightened steadily throughout 2000, for example, the yield spread of the benchmark 2-year NIP Notes tightened to end the year at 32 basis points compared to 48 basis points at the beginning of the year. After swapping the proceeds into floating rate payment obligations, the average cost of fund of the NIP notes issued in 2000 was below HIBOR. The low funding cost had helped significantly in mitigating the adverse impact of the sharp decline in mortgage rate on the Corporation's profitability in 2000.

The HKMC continued its effort to promote the development of the retail bond market in Hong Kong. In 1999, the HKMC became the first Corporation in Hong Kong to list and trade its debt securities on the Stock Exchange. The listing of the NIP notes achieved the dual objectives of, firstly, broadening the Corporation's investor base outside its already highly receptive institutional investor community and, secondly, raising the level of awareness among retail investors about the positive features of fixed income investments.

Following the success of the initial launch, the HKMC reserved a portion of two NIP notes issued in 2000 for subscription by retail investors. In order to boost the interest of retail investors in investing in the debt securities, two retail banks with an extensive branch network, namely HSBC and Hang Seng Bank, were appointed as underwriters for the two issues respectively. Both issues recorded an impressive over-subscription rate and notable trading activities on the Stock Exchange.

The HKMC launched two issues for a total amount of HK$625 million under the DIP in 2000. An issue of HK$600 million was arranged as part of the Mortgage-Bond Asset Swap Programme with Dao Heng Bank in July 2000.

Figure 9: HKMC NIP Notes Yield Spread Against Exchange Fund Notes in 2000



Credit Rating

With the expansion of the MPP to include mortgage loans originated by Government housing agencies and property developers, the HKMC expects strong growth in its annual mortgage purchase amount in the next few years. For 2001, the business target of HK$12.5 billion is almost doubled the actual amount of HK$6.35 billion acquired in 2000. In order to fund the expanding MPP, it is likely that the Corporation would need to tap the international capital markets through the introduction of a multi-currency Medium Term Note ("MTN") Programme. In October 2000, the Board of Directors approved the proposal for the HKMC to seek credit ratings from credit rating agencies to pave the way for the launch of the MTN Programme. The Corporation has appointed HSBC as the rating adviser and the rating process is expected to commence in the first half of 2001.

E-BUSINESS

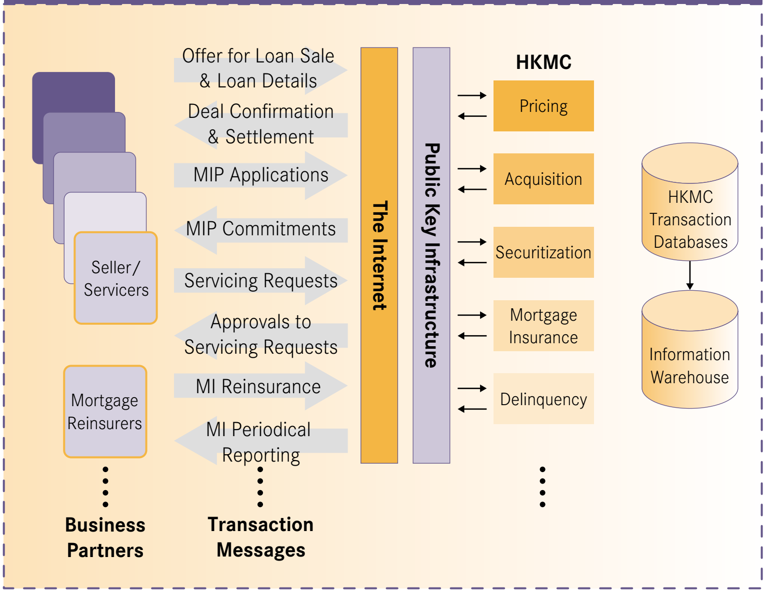
There is a clear trend of the banks making increasing use of the Internet to conduct e-business with business partners and e-banking with customers. As the HKMC's MPP and MIP have become an integral part of the mortgage business in Hong Kong, the Corporation has decided to move in step with the industry to adopt e-business as the platform to conduct future transactions.

In 2000, the HKMC appointed Fannie Mae, the industry leader in the secondary mortgage market in the U.S., as consultant to formulate a strategic plan for its IT development in the next five years.

The HKMC has accepted the consultant's recommendation to establish an on-line communication link to process transactions between the Corporation and its business partners. After completion, it will substantially enhance efficiency and productivity by shortening the process cycle and reducing the risk of error due to human intervention:

- using software provided in the system, the banks and reinsurers will be able to validate the transaction data to ensure their accuracy before sending them to the HKMC through the Internet;
- the received data will be fed directly into the HKMC's systems, thereby eliminating manual data entry to a great extent; and
- within the HKMC, subsequent processing of the transactions will be automated and the work processes will be integrated through workflow software.

Figure 10: Integrated Information Delivery System



In December 2000, the Corporation appointed Hewlett Packard to develop the Integrated Information Delivery System. To ensure proper interface with the IT systems of the external users, the Corporation invited the major Approved Sellers and Approved Reinsurers to form a Working Group to discuss issues related to system design and implementation.

The Integrated Information Delivery System is tentatively scheduled for implementation in the fourth quarter of 2001. After completion, the processing of mortgage purchase/servicing and mortgage insurance applications will be conducted over the Internet under a secure and robust environment.

STANDARDIZATION OF MORTGAGE ORIGINATION DOCUMENTS

Currently, the mortgage origination documents adopted by banks in Hong Kong vary significantly in terms of both content and presentation. Standardization of the documents would bring about significant benefits to the homebuyers, the banks and the Corporation. It would also promote the development of the secondary mortgage market in Hong Kong. In particular, it would help shorten the timeframe for the issuance of MBS and reduce issuance costs as it would remove the need for investors and the credit rating agencies to conduct due diligence on the mortgage origination documents. Since the HKMC has had the opportunity to review the mortgage origination documents of the major mortgagee banks in Hong Kong, it is well positioned to co-ordinate the efforts of the mortgage industry and the legal profession to develop a set of model documents that represents the best market practice.

The HKMC set up a Steering Committee in May 2000 to oversee the implementation of the project. The Committee is chaired by the Chief Executive Officer of the HKMC and the members consist of representatives from the major banks, the mortgage reinsurers, the credit rating agencies, The Law Society of Hong Kong, Hong Kong Bar Association and the Law Faculty of The University of Hong Kong. The terms of reference and membership of the Steering Committee are set out in Annex C. The Steering Committee had made significant progress in drafting the model Mortgage Deed and Mortgage Guarantee. Drafting work is expected to complete in the first quarter of 2001. This will be followed by extensive consultation with the banks, mortgage reinsurers, the relevant regulators, rating agencies and the Consumer Council. The HKMC plans to introduce the model mortgage origination documents in the second half of 2001.

STAFFING

The Corporation is committed to developing a team of professional staff with expertise in the secondary mortgage business. The Corporation's staffing policy is based on the following principles:

- The maintenance of a lean, efficient and professional workforce. The size of the permanent establishment will be kept to the minimum necessary to support the Corporation's business plan.
- A continued adoption of automation and information technology solutions, as well as the streamlining of work processes, to maximize efficiency and minimize costs.
- The maintenance of a cost-to-income ratio at a level below the average of banks and other financial institutions.

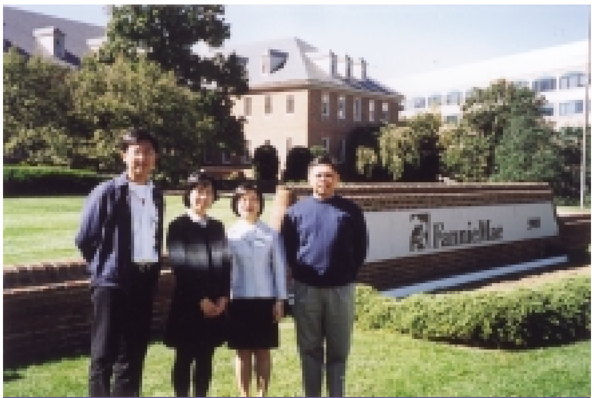
Staff attending in-house training seminar

In response to the dynamic growth and diversification of the Corporation's business, the Board has approved an increase in the permanent establishment from 74 to 97 staff for 2001.

All staff members are encouraged to attend in-house and external courses that aim to enhance their management and technical capability. In 2000, staff members attended more than 50 external courses that covered business negotiation, e-marketing, e-commerce and other mortgage-related technical courses.

In order to retain critical skills and motivate staff to operational excellence and outstanding financial performance, the HKMC commissioned a consultancy firm to develop a Performance-based Bonus Scheme for the Corporation. The Scheme was designed in accordance with two key parameters:

- in line with best market practice, the size of the bonus reward is based on both the company and individual performance and is at a level adequate to attract and retain the key employees required to successfully manage the Corporation's business; and
- it is designed to focus staff's attention on organizational performance and motivating them to achieve and exceed specified financial and operational objectives of the Corporation.



Staff attending training at Fannie Mae of USA

The scheme was introduced in 2000 with the unanimous support of the HKMC staff.

The HKMC had also launched three major initiatives in 2000 to enhance staff efficiency through process re-engineering:

- the Corporation commissioned Fannie Mae to conduct a Process Improvement Study to identify potential areas for streamlining the key work processes;
- an internal Task Force was formed to identify deficiencies in the current work processes and to propose appropriate solutions; and
- a Quality Improvement Programme was introduced to provide a channel for all staff to put forward suggestions on new business ideas and proposals on streamlining of work processes.

OUTLOOK FOR 2001

The HKMC will continue its strategy of product diversification and building a critical mass for its core businesses. Working closely with its Approved Sellers/Servicers, the insurance companies, regulators and others, the Corporation plans to support the growth and development of the residential mortgage market and capital markets in Hong Kong by:

- purchasing HK$12.5 billion of mortgages for its retained portfolio;
- issuing HK$10 billion debt securities under the NIP and DIP;
- arranging the issuance of HK$2-3 billion of MBS;
- providing mortgage insurance on mortgages with a principal amount of HK$8.5 billion;
- standardizing the mortgage origination documents with the aim to making it more "user-friendly" and more effective for securitization; and
- implementing the Integrated Information Delivery System to move the HKMC's business operations onto an e-business platform.

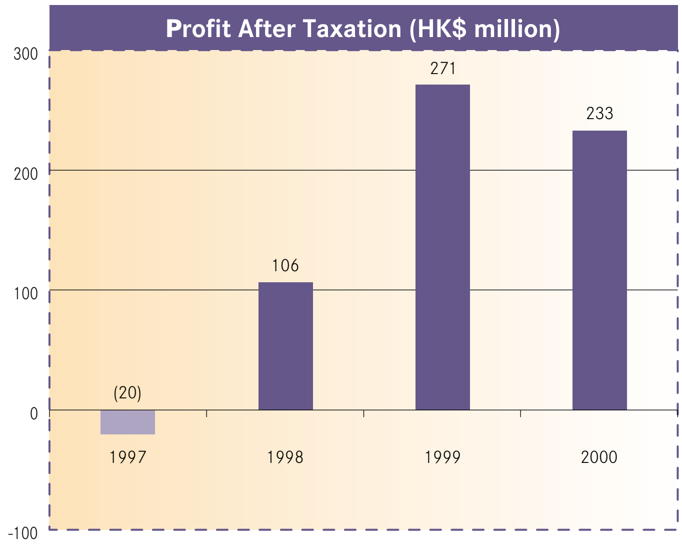
Financial Review

During 2000, total assets grew by 6.2%, from HK$13.98 billion to HK$14.85 billion.

PROFIT AND LOSS

Operating results

In 2000, the residential mortgage market was characterized by slow growth in business volume and intense price competition amongst banks, resulting in a significant reduction in the mortgage rate and high re-financing activities. Despite the difficult business environment, the Corporation managed to mitigate the adverse impact on profitability by increasing the amount of mortgage purchase, lowering debt issuance cost by a successful execution of its pre-funding strategy and generating additional fee income from its mortgage insurance and MBS programmes. As a result, the Corporation's profit after tax recorded a moderate decline of 14% to HK$233.1 million, despite a 28.2% drop in its net interest margin. Return on assets and return on shareholder's equity were maintained at healthy levels of 1.8% (1999: 2.5%) and 9.4% (1999: 12.1%) respectively. Due to the Corporation's persistent efforts in controlling its operating expenses, the cost-to-income ratio was kept at a low level of 25.1% (1999: 21.9%). The capital-to-assets ratio remained strong at 12.3% (1999: 10.1%).



Net interest income

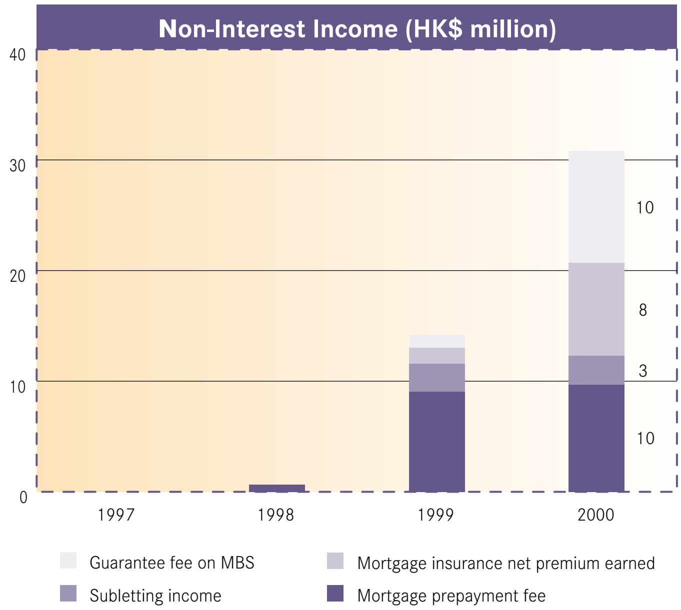
	2000 **HK$' 000**	1999 HK$' 000
Interest income	**1,009,737**	913,147
Interest expense	**(652,026)**	(506,630)
Net interest income	**357,711**	406,517
Average interest-earning assets	**12,882,363**	10,545,741
Net interest margin	**2.8%**	3.9%
Net interest spread on interest-bearing liabilities[1]	**1.6%**	2.6%

Net interest income for the year reduced by 12% to HK$357.7 million. It mainly reflected the downward adjustments in the mortgage rate of the Corporation's retained portfolio due to the keen competition in the residential mortgage market. As a result, the average net required yield of the mortgage portfolio reduced by 0.96% from Prime + 0.23% in 1999 to Prime - 0.73% in 2000 and the net interest spread on interest-bearing liabilities from 2.6% to 1.6%.

Other income, net

In 2000, the other income earned by the Corporation increased substantially to HK$34.4 million (1999: HK$11.9 million). These included early prepayment fee income of HK$9.7 million, sub-letting income of HK$2.6 million, mortgage insurance premium of HK$8.4 million, MBS guarantee fee income of HK$10.1 million and other income of HK$3.6 million.

[1] Net interest spread on interest-bearing liabilities = Return on interest-earning assets – Funding cost on interest-bearing liabilities



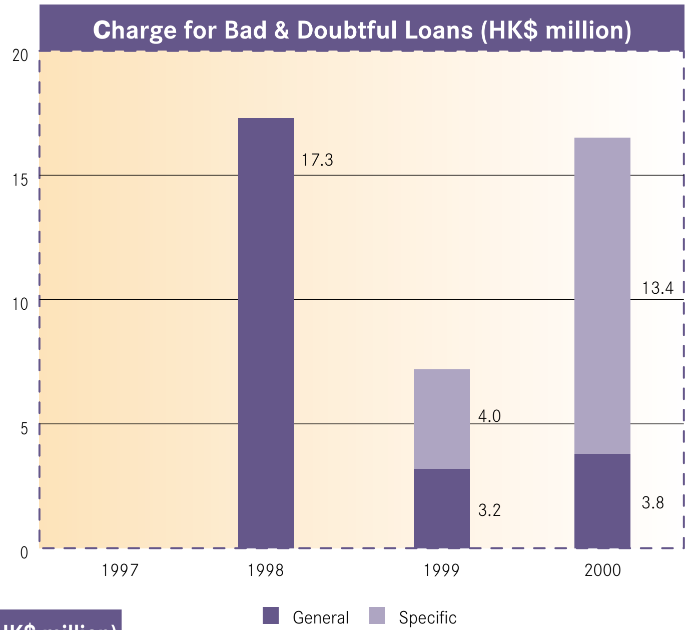
(1999: HK$53.1 million and 58.1%). The permanent establishment of the Corporation increased from 74 to 97 for 2001 to support the expanded business operation. Premises costs and depreciation charges on fixed assets remained stable at HK$13.5 million and HK$12.2 million respectively.

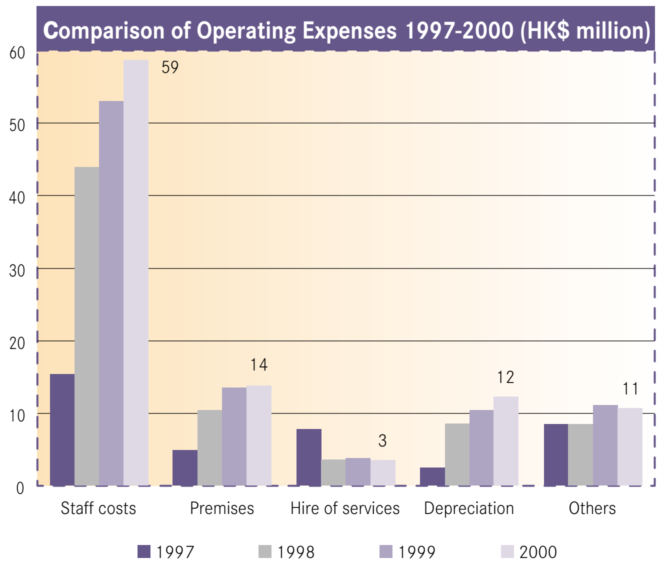
Provisions for bad and doubtful loans

The Corporation made additional general and specific provisions for bad and doubtful loans amounting to HK$3.8 million and HK$13.4 million respectively in 2000. Of the HK$3.8 million general provision for bad and doubtful loans, HK$0.6 million related to the provisions written back on the mortgage loans sold under the MBS Programme to the HKMC Funding Corporation (1) Limited, a special purpose company for issuing MBS. Total loan provisioning was 0.33% (1999: 0.26%) of the outstanding principal balance of the retained mortgage portfolio at the year-end, reflecting the prudent loan provisioning policy adopted by the Corporation.

Operating expenses

The operating expenses of the Corporation increased by HK$7.0 million to HK$98.4 million for 2000. This reflected the additional costs incurred in the course of expanding its business activities such as the provision of mortgage insurance for loans with LTV ratios of up to 90%, widening of the scope of mortgage loans eligible for sale under the Mortgage Purchase Programme and the development of an electronic linkage with banks to conduct business over the Internet. Staff costs of HK$58.7 million accounted for 59.7% of the total operating expenses





Mortgage portfolio and provisions

	2000 HK$' 000	1999 HK$' 000
Gross mortgage portfolio	**11,119,240**	8,749,370
Provisions for bad & doubtful loans		
Specific	**(13,248)**	(4,042)
General	**(22,967)**	(18,552)
Net mortgage portfolio	**11,083,025**	8,726,776

Ratios

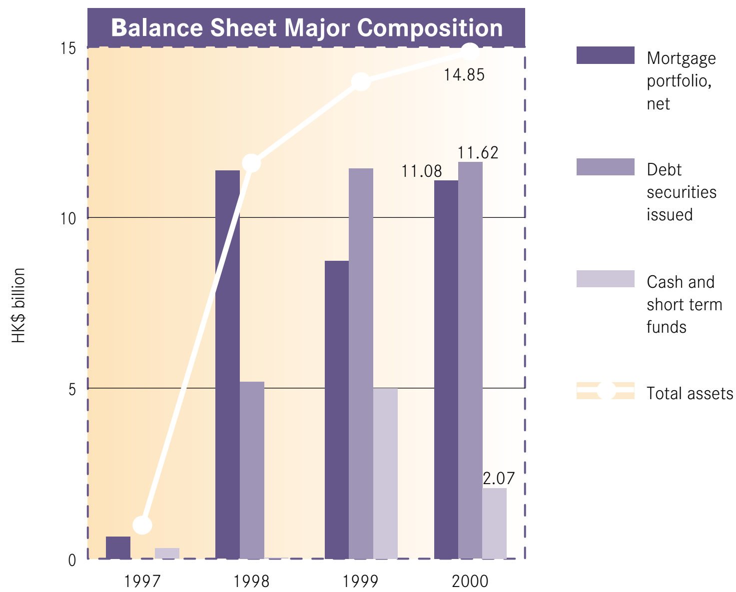
Delinquency ratio for loans overdue more than 90 days	**0.42%**	0.16%
Total provisions as a percentage of gross mortgage portfolio	**0.33%**	0.26%
Specific provision as a percentage of overdue loan principal	**28.4%**	28.5%

BALANCE SHEET

During 2000, total assets grew by 6.2%, from HK$13.98 billion to HK$14.85 billion. This reflected increases in the net mortgage portfolio by HK$2.36 billion and investment in debt securities by HK$1.30 billion and a reduction of HK$2.93 billion in cash and short-term funds.

The net mortgage portfolio of the Corporation was HK$11.08 billion, an increase of HK$2.36 billion for the year. The high prepayment rate, mainly driven by mortgage refinancing activities, reduced the retained portfolio by HK$3.97 billion in 2000. The Corporation took a pro-active approach in enhancing the flexibility of its mortgage purchase programme, including an expansion of the types of mortgages eligible for sale to the Corporation and the introduction of a Mortgage-Bond Asset Swap Programme. Through these efforts, the Corporation succeeded in purchasing a total of HK$6.35 billion of mortgage loans during the year despite the difficult operating environment. The retained mortgage portfolio consisted of 94.7% of floating rate mortgages and 5.3% of fixed adjustable rate mortgages as of the year-end.

To fund the mortgage purchases and the redemption of the HKMC debt securities during the year, the Corporation issued a total of HK$6.63 billion of notes and bills (1999: HK$6.3 billion) under the Note Issuance Programme ("NIP") and Debt Issuance Programme ("DIP") in 2000. As at 31 December 2000, the outstanding balances of the notes under the NIP and DIP were HK$9 billion and HK$2.62 billion respectively.



CAPITAL ADEQUACY RATIO

To ensure that the Corporation is managed in a prudent manner, the Financial Secretary issued guidelines in 1997 to require the Corporation to comply with a minimum Capital-to-assets ratio ("CAR") of 5%.

With the Board's approval in October 2000, the Corporation proposed to the Financial Secretary to modify the capital requirement framework to account for the different levels of risk of the products in the retained loan portfolio, mortgage insurance and MBS portfolio as follows:

Product	Minimum Capital-to-Assets ratio
Mortgage Portfolio	5% of retained portfolio (based on notional amount)
Mortgage-backed Securities	2% of MBS portfolio (based on notional amount, currently at 5%)
Mortgage Insurance	0% of risk-in-force value of exposure covered by the re-insurance arrangement with Approved Reinsurers (currently at 5%)
	5% of risk-in-force value of exposure not covered by reinsurance arrangement (no change).

The CAR of the Corporation was maintained at a healthy level of 12.3% as at 31 December 2000. After implementation of the revised framework, the CAR would be further improved to 13.5%.

RISK MANAGEMENT

The Corporation is subject to three major areas of risk: interest rate risk, credit risk and operations risk. To support the growth of business, the Corporation adopts prudent measures to address these risks in the different areas of its business activities. The following highlights the Corporation's strategy in managing these risks.

Market Risk Management

Market risk is the exposure to an adverse change in the value of the financial instruments caused by changes in market prices or rates, including changes in interest rates, foreign exchange rates and the market prices of securities.

Asset and Liability Committee

The Corporation has formed an Asset and Liability Committee ("ALCO") to monitor, assess and control various market risk facing the Corporation. The Committee sets and monitors compliance with risk limits, approves financing strategies and develops risk management methodologies. The Corporation's ALCO is chaired by the Chief Executive Officer and its members consist of the Senior Vice President (Finance), Senior Vice President (Operations), senior staff of the Treasury Department and Financial Control Department. The Committee holds meeting on a weekly basis.

1. *Interest Rate Mismatch Risk*

   Interest rate mismatch risk is the most significant type of market risk exposure arising from the Corporation's asset-liability portfolio. Interest rate mismatch risk refers to the potential decline in net interest income ("NII") of the Corporation due to the volatile and adverse movements of market interest rates. Interest rate mismatch risk arises from a variety of factors, including the difference in the timing of maturity or repricing for the assets, liabilities and related derivatives in the portfolio. For example, the Corporation's net interest income is affected by changes in the level of market interest rates, as the repricing characteristics of interest-earning assets (e.g. Prime or HIBOR-based mortgage loans) do not necessarily match exactly those of interest-bearing liabilities.

The Corporation employs, as part of its active Asset and Liability Management process, a variety of cash and derivatives instruments, e.g. Interest Rate Swap, Basis Swap and Forward Rate Agreement, in managing its exposure to fluctuations in market interest rates. In monitoring and managing the interest rate exposure, the Corporation uses duration gap exposure to quantify its earnings at risk (the risk to NII from adverse movements in interest rates). Depending on the prevailing interest rate outlook, the Corporation takes a proactive approach in balancing the duration gap of its outstanding asset-liability portfolio under the guidance and supervision of ALCO. In 2000, the average duration gap was kept within a very prudent range of plus and minus half-a-month, close to the perfect level of a zero duration gap.

2. *Basis Risk*

The Corporation is also exposed to basis risk, which is the difference in the pricing characteristics of two instruments or benchmarks. For example, basis risk arises when Prime-based assets are financed by HIBOR-based liabilities. While there has been a healthy Prime-HIBOR spread, as in the case of Authorized Institutions in Hong Kong, the Corporation currently cannot fully hedge the Prime-HIBOR basis risk in an economical manner. This risk can be more effectively addressed as more mortgage loans are originated based on HIBOR and by the time that the Prime/HIBOR basis swap market or related risk management instrument become better developed in Hong Kong.

3. *Funding Mismatch Risk*

Funding Mismatch Risk refers to the risk in maturity mismatch between assets and liabilities. Despite their legal maturity, the average life of the mortgage assets depends on the actual prepayment speed. The retained mortgage portfolio of the Corporation has a shorter average life if the prepayment speed increases as more loan amount is repaid. Prepayment occurs for two major reasons in Hong Kong namely (i) housing turnover (i.e. borrowers repay the entire mortgages when they sell their homes) and (ii) refinancing (i.e. borrowers refinance their mortgage loans at a lower prevailing mortgage rate). The Corporation closely manages the average life of overall interest-earning assets through ongoing purchases of mortgage assets to replenish the portfolio. The Corporation also diversifies its investment into high-grade debt securities and cash deposit to adjust the overall average life of its assets. To achieve the desired average life for its overall liability portfolio to match its mortgage loan assets, the Corporation issues bills and notes across a broad spectrum of final maturities from 1 month to 10 years. The Corporation also considers usage of callable debt and off-balance-sheet risk management instruments, including interest rate swaptions, to achieve its desired liability structure and actively manage the prepayment risk of the mortgage portfolio.

Liquidity Risk Management

Liquidity management refers to the Corporation's ability to repay obligations including the redemption of debt issues and maturing money market drawings, and to fund for the new mortgage purchases and investments as opportunity arises. The Corporation manages liquidity by monitoring the actual and expected inflows and outflows of funds on a daily basis, by projecting longer-term inflows and outflows across the entire maturity spectrum, and by developing diversified sources of funding with the objective of maintaining stable financing at low funding costs.

The Corporation has secured a diversified base of investors and funding sources to support the future growth of its business:

1. Capital: HK$3 billion authorized capital of which HK$2 billion has been paid up and HK$1 billion is available on call from the shareholders.

2. HK$20 billion NIP: Under the Programme, the HKMC's NIP Bills or Notes are covered by the same tendering and market-making arrangements for the Exchange Fund Bills and Notes which enhance the secondary liquidity and provide a useful benchmark for HKMC's debt issuance. The NIP has provided, and will continue to provide, a stable and cost-effective source of funding to the Corporation.

3. HK$20 billion DIP: Under the Programme, the Corporation has appointed 5 Primary Dealers to perform underwriting and market making activities for public issues drawn under the DIP. A Selling Group consisting of 13 major financial institutions has also been established to broaden the DIP's distribution network. The DIP helps extending the Corporation's yield curve up to 10 years and broadening its investor base to a wider spectrum of institutional investors.

4. HK$10 billion Revolving Credit Facility: The Exchange Fund has provided a HK$10 billion revolving credit facility to the Corporation since January 1998.

5. Investment Portfolio: The Corporation holds marketable securities and other short-term investments that can readily be converted to cash.

6. Money Market lines: The Corporation has set up extensive money market lines with local and international banks to bridge financing. The Corporation's Public Sector Entity status under the Banking Ordinance has established a favorable 20% risk-weighting treatment for financial institutions investing in the Corporation's debt securities or lending to the Corporation.

7. MBS Programme: The MBS Programme can be utilized to facilitate securitization or disposition of mortgage assets of the Corporation's retained portfolio when deemed desirable.

Credit Committee

The Credit Committee is responsible for developing and overseeing the implementation of the Corporation's policies for managing all aspects of the underlying credit risks of its business. Its major tasks include approving applications to become Approved Seller/Servicers under the Mortgage Purchase Programme and Approved Reinsurers under the MIP. The Committee also sets limits for individual Approved Sellers and Approved Reinsurers and counterparty limits for treasury activities and reviews the Corporation's mortgage purchasing criteria. It is chaired by the Chief Executive Officer and its members include the Senior Vice President (Finance), Senior Vice President (Operations), General Counsel and senior staff of the Operations and Finance Divisions.

Pricing Committee

The Pricing Committee meets weekly in conjunction with the ALCO to review the current pricing for products under the Mortgage Purchase Programme, MBS Programme and MIP in the light of current market conditions and business strategies. It also reviews all risk-based pricing transactions prior to submission to Executive Directors for final approval.

Pricing Committee Meeting

Audit Committee

In order to minimize the operational risk, the Corporation has put in place adequate checks and balances in its business operations. The Audit Committee performs a major role in ensuring that the intended checks and balances are properly implemented and that the checking procedures are constantly upgraded to suit changes in the business needs.

Audit Committee Meeting

Appointed by the Board, the Audit Committee comprises not less than four Directors, one of whom must be an Executive Director. The Committee is currently chaired by Mr. Eddy Fong and its members include Mr. David Li, Mr. Ronald Arculli, Mr. Tony Latter and Mr. Norman Chan. The Committee met twice in 2000 to review the financial accounts and other on-going audit work of the Internal Audit Department.

The Directors have pleasure in presenting their report together with the audited financial statements for the year ended 31 December 2000.

Principal Activities

The principal activities of the Company are (i) to purchase portfolios of mortgages or other loans, pursuant to predetermined prudent and stringent purchasing criteria, secured by residential properties situated in Hong Kong from authorized institutions as defined under the Banking Ordinance of Hong Kong; (ii) to raise financing for its purchase of mortgages through the issuance of debt securities in the capital markets; (iii) to sell mortgages to special purpose corporation(s) for the purpose of issuing mortgage-backed securities to investors; and (iv) to act as an insurer authorized under the Insurance Companies Ordinance of Hong Kong in relation to mortgage insurance business.

Results and Appropriations

The results for the year ended 31 December 2000 are set out on page 38 of this annual report.

The Directors do not recommend the payment of a final dividend, and recommend that the retained profit of HK$589,814,000 at 31 December 2000 be carried forward.

Fixed Assets

Details of the movement in fixed assets during the year are set out in Note 15 to the financial statements.

Debt Securities Issued

The Company issued bills and notes under the Note Issuance Programme ("NIP") and Debt Issuance Programme ("DIP") during the year ended 31 December 2000, details of which are set out in Note 20 to the accounts.

Directors

The Directors of the Company during the year and up to the date of this report are as follows:

The Honourable Donald TSANG, JP,
Chairman and Executive Director
Mr. Joseph YAM Chi-kwong, JP,
Deputy Chairman and Executive Director
Mr. Norman CHAN Tak-lam, SBS, JP,
Executive Director
Mr. Tony LATTER, JP, *Executive Director*
Mr. Ronald Joseph, ARCULLI, JP, *Director*
The Honourable Bernard Charnwut CHAN,
Director
Professor Andrew CHAN Chi-fai, *Director*
(appointed on 24 March 2000)
The Honourable CHAN Kwok-keung, *Director*
Mr. Eddy FONG Ching, SBS, JP, *Director*
Ms. Anita FUNG, *Director*
Mr. Rafael HUI Si-yan, GBS, JP, *Director*
(retired on 24 March 2000)
Mr. Stephen IP Shu-kwan, JP, *Director*
(appointed on 24 March 2000)
Mr. David LAM Yim-nam, *Director*
(retired on 24 March 2000)
Dr. The Honourable David LI Kwok-po,
LLD (Cantab), JP, *Director*
Mr. NG Kwok-wai, *Director*
The Honourable SIN Chung-kai, *Director*
Mr. Paul THURSTON, *Director*
(appointed on 24 March 2000)
Mr. Dominic WONG Shing-wah,
GBS, OBE, JP, *Director*

In accordance with Article 109 of the Articles of Association, all those directors who are not Executive Directors shall retire but shall be eligible for re-election at the next annual general meeting.

Directors' Interests in Transactions and Contracts

The following Directors may be deemed to be interested in any contracts which have been entered, or may be entered, into between the Company and them for the reasons set out below:

(1) The Hon. Donald Tsang is the Financial Secretary of Hong Kong as Controller of the Exchange Fund. Mr. Joseph Yam is the Monetary Authority appointed by the Financial Secretary under the Exchange Fund Ordinance. The Monetary Authority acts as the arranger, agent and operator in respect of the Company's HK$20 billion NIP. At 31 December 2000, the outstanding balance of the notes under the NIP was HK$9 billion. The Monetary Authority also acts as the custodian and clearing agent for the Company's HK$20 billion DIP. At 31 December 2000, the outstanding balance of the notes under the DIP was HK$2.6 billion. In addition, the Company has a revolving credit facility of HK$10 billion from the Exchange Fund through the Monetary Authority. At 31 December 2000, there was no outstanding balance.

(2) Dr. The Hon. David Li is the Chairman and Chief Executive of The Bank of East Asia, Limited which is (a) a selling group member under the DIP; (b) an approved seller/servicer under the Mortgage Purchase Programme ("MPP") of the Company and (c) an approved authorized institution which has entered into a Master Mortgage Insurance Policy with the Company under the Mortgage Insurance Programme ("MIP"). Dr. Li is also the Chairman and a director of United Chinese Bank Limited which is (a) an approved seller/servicer under the MPP and (b) an approved authorized institution under the MIP. In addition, Dr. Li is a director of First Pacific Bank Limited which is (a) an approved seller/servicer under the MPP and (b) an approved authorized institution under the MIP.

(3) The Hon. Bernard Chan is a director of (a) Asia Commercial Bank Limited which is an approved seller/servicer under the MPP and (b) an approved authorized institution under the MIP. He is also a director of Asia Insurance Company, Limited which is an approved reinsurer with which the Company has entered into a Master Mortgage Reinsurance Policy under the MIP.

(4) Mr. Paul Thurston is the Assistant General Manager and Head of Personal Financial Services of HSBC which is (a) a primary dealer under the DIP; (b) an approved seller/servicer under the MPP; and (c) an approved authorized institution under the MIP. Mr. Thurston is also a director of HSBC Insurance (Asia) Limited which is an approved reinsurer under the MIP.

Except for the above disclosure and the related party transactions as stated in Note 24 to the Financial Statements, no contracts of significance in relation to the Company's business to which the Company was a party and in which any of the Directors had a material interest, either directly or indirectly, subsisted at the end of the year or at any time during the year.

At no time during the year was the Company a party to any arrangement to enable any of its Directors to acquire benefits by means of the acquisition of shares or debt securities of the Company or of any body corporate.

Additional Disclosures in Compliance with the Provisions of the Insurance Companies Ordinance ("ICO")

The Controllers of the Company as defined in the ICO are The Hon. Donald Tsang and Mr. Pang Sing Tong. Mr. Tsang is the Chairman of the Company. Mr. Pang is the Chief Executive Officer of the Company, and he did not have any interests in the transactions or the contracts which the Company had entered into during the year ended 31 December 2000.

The Company has not carried on insurance business relating to liabilities or risks in respect of which persons are required by any Ordinance to be insured.

Under the back-to-back mortgage insurance business, the Company reinsures the risk exposure with the approved reinsurers on a 100% basis. The approved reinsurers include Asia Insurance Company, Limited, Hang Seng Insurance Company Limited, HSBC Insurance (Asia) Limited, PMI Mortgage Insurance Co. and United Guaranty Mortgage Indemnity Company. Since April 2000 the Company has retained 20% of the risk exposure under its mortgage insurance covers before ceding the remaining 80% of the risk exposure to the above approved reinsurers. At 31 December 2000, the total risk-in-force was approximately HK$1.553 billion (1999: HK$530 million) of which HK$1.381 billion risk exposure was ceded to the approved reinsurers, and the balance of HK$172 million was retained by the Company.

Auditors

The financial statements have been audited by Arthur Andersen & Co. A resolution for their reappointment as auditors for the following year is to be proposed at the forthcoming annual general meeting.

On behalf of the Board of Directors

Donald Tsang
Chairman

Hong Kong,
1 March 2001

ARTHUR ANDERSEN

Auditors' Report to the Shareholder of
The Hong Kong Mortgage Corporation Limited
(Incorporated in Hong Kong with limited liability)

Arthur Andersen & Co

21st Floor Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

We have audited the financial statements of The Hong Kong Mortgage Corporation Limited (the "Company") on pages 38 to 58, which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective responsibilities of directors and auditors

The Companies Ordinance requires the directors to prepare financial statements that give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Company, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2000 and of its profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Ordinance.

Arthur Andersen & Co.

Certified Public Accountants
Hong Kong,
1 March 2001

Profit and Loss Account

For the year ended 31 December 2000

	Notes	2000 HK$'000	1999 HK$'000
Interest income	3	**1,009,737**	913,147
Interest expense	4	**(652,026)**	(506,630)
Net interest income		**357,711**	406,517
Other income, net	5	**34,359**	11,852
Operating income		**392,070**	418,369
Operating expenses	6	**(98,427)**	(91,474)
Operating profit before provisions		**293,643**	326,895
Provisions for bad and doubtful loans	7	**(17,229)**	(7,246)
Profit before taxation		**276,414**	319,649
Taxation	8(a)	**(43,308)**	(48,417)
Profit after taxation		**233,106**	271,232
Transfer to contingency reserve	2(j)	**(670)**	–
Net profit for the year		**232,436**	271,232
Retained profit brought forward		**357,378**	86,146
Retained profit carried forward		**589,814**	357,378

A separate statement of recognized gains and losses is not presented because there were no recognized gains or losses other than the net profit for the year.

Balance Sheet

As at 31 December 2000

	Notes	2000 HK$'000	1999 HK$'000
ASSETS			
Cash and short-term funds	10, 17	**2,068,134**	4,996,738
Interest and remittance receivables	11	**249,112**	185,052
Prepayments, deposits and other assets	12	**5,636**	8,155
Deferred expense, net	13	**112,879**	39,050
Mortgage portfolio, net	14(a)	**11,083,025**	8,726,776
Investment in debt securities	16, 17	**1,304,753**	–
Fixed assets	15	**21,077**	24,856
		14,844,616	13,980,627
LIABILITIES			
Short-term bank loans	17	**427,200**	–
Interest payable	18	**120,240**	96,770
Accounts payable, accrued expenses and other liabilities	19	**45,646**	38,037
Provisions for taxation	8(b)	**14,152**	42,424
Unearned premiums	9	**25,894**	5,018
Debt securities	17, 20	**11,621,000**	11,441,000
		12,254,132	11,623,249
SHAREHOLDER'S EQUITY			
Share capital	22	**2,000,000**	2,000,000
Retained profit		**589,814**	357,378
Contingency reserve	2(j)	**670**	–
		2,590,484	2,357,378
		14,844,616	13,980,627

Approved by the Board of Directors on 1 March 2001 and signed on behalf of the Board by:

Yam Chi Kwong, Joseph
Deputy Chairman

Anthony Robert Latter
Executive Director

Cash Flow Statement

For the year ended 31 December 2000

	Notes	2000 HK$'000	1999 HK$'000
Net cash (outflow)/inflow from operating activities	23	**(1,969,797)**	2,973,170
Taxation			
Hong Kong profits tax paid		**(71,580)**	(27,917)
Investing activities			
Purchase of fixed assets		**(8,402)**	(11,289)
Purchase of investment in debt securities		**(1,740,733)**	–
Proceeds from redemption of investment in debt securities		**436,000**	–
Net cash outflow from investing activities		**(1,313,135)**	(11,289)
Net cash (outflow)/inflow before financing		**(3,354,512)**	2,933,964
Financing			
Proceeds from issue of notes		**6,443,708**	6,218,676
Redemption of notes		**(6,445,000)**	–
Net cash (outflow)/inflow from financing		**(1,292)**	6,218,676
(Decrease)/increase in cash and cash equivalents		**(3,355,804)**	9,152,640
Beginning cash and cash equivalents		**4,996,738**	(4,155,902)
Ending cash and cash equivalents		**1,640,934**	4,996,738
Analysis of the balance of cash and cash equivalents			
Cash and short-term funds	10	**2,068,134**	4,966,738
Short-term bank loans	17	**(427,200)**	–
		1,640,934	4,996,738

1. Basis of Preparation

The financial statements of The Hong Kong Mortgage Corporation Limited (the "Company") have been prepared in accordance with the provisions of the Hong Kong Companies Ordinance and Statements of Standard Accounting Practice issued by the Hong Kong Society of Accountants.

2. Principal accounting policies

a. Recognition of interest and fees

Interest income and expense are accrued on a time-apportioned basis on the principal outstanding and at the rate applicable, except in case of bad and doubtful loans (Note 2(f)). Fee income and expenses are recognized when earned or incurred.

b. Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after the fixed assets have been put into operation, such as repairs and maintenance and overhaul costs, is normally charged to the profit and loss account in the year in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of fixed assets, the expenditure is capitalized as an additional cost of the fixed asset.

Depreciation is calculated on a straight-line basis at annual rates estimated to write off the cost of each asset over its expected useful life.

The annual rates are as follows:

Leasehold improvements	over the unexpired period of the lease
Furniture and fixtures	over the unexpired period of the lease
Computer and related software	$33\frac{1}{3}\%$
Office equipment	$33\frac{1}{3}\%$
Motor vehicle	25%

c. Foreign currencies

The books and records are maintained in Hong Kong dollars. Transactions in other currencies during the year are translated into Hong Kong dollars at exchange rates prevailing in effect at the time of the transactions. Monetary assets and liabilities denominated in other currencies at the balance sheet date are translated into Hong Kong dollars at rates of exchange in effect at the balance sheet date. Exchange differences are dealt with in the profit and loss account.

d. Deferred taxation

Deferred taxation is provided under the liability method at the current tax rate in respect of significant timing differences between profit as computed for taxation purposes and profit as stated in the financial statements, except where it is considered that no liability will arise in the foreseeable future.

Deferred tax assets are not recognized unless the related benefits are expected to crystallize in the foreseeable future.

e. Operating leases

Leases where substantially all the rewards and risks of ownership remain with the leasing company are accounted for as operating leases. Rental payments under operating leases are charged to the profit and loss account on a straight-line basis over the period of the relevant leases.

f. Bad and doubtful loans

Provisions for bad and doubtful loans are charged to the profit and loss account on a monthly basis in accordance with the guidelines approved by the Board of Directors. Specific provision for bad and doubtful loans generally applies to a mortgage loan that is overdue for more than 90 days and the current market value of the underlying property is less than the outstanding principal balance ("OPB") of the mortgage loan. When there is no longer any realistic prospect of recovery of the OPB of the mortgage loan, it will be written off at the discretion of the Credit Committee.

The accrual of interest on mortgage loans is discontinued when they become overdue for 90 days or more. Any previously accrued and uncollected interests on the loans are reversed against current period's interest income. Interest income on the overdue loans is only recognized when all arrears of principal and interest from the borrowers have been cleared and it is probable that the customer is capable of fully servicing his obligations under the terms of the loans for the foreseeable future.

Properties repossessed from the existing mortgage portfolio in order to achieve an orderly realization continue to be reported under the heading of Mortgage Portfolio, Net in the balance sheet. The repossessed properties are recorded at the OPB of the loans less any provisions made thereof.

g. Investment in debt securities

Held-to-maturity investments are investments which the Company has the expressed intention and ability to hold to maturity. They are carried at amortized cost less any provision for impairment in value.

The carrying amounts of held-to-maturity securities are reviewed at each balance sheet date to assess the credit risk and whether the carrying amounts are expected to be recovered. Provisions are made when the carrying amounts are not expected to be recovered and are recognized as an expense in the profit and loss account.

Provision against the carrying value of held-to-maturity securities are reversed to the profit and loss account when the circumstances and events that led to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist in the foreseeable future.

Upon disposal or transfer of held-to-maturity securities, any profit and loss thereon is accounted for in the profit and loss account.

h. Notes issued under the Note Issuance Programme ("NIP") & Debt Issuance Programme ("DIP")

The notes issued under the NIP and DIP are stated at par value under debt securities in the balance sheet. Interest on the notes is accrued on a daily basis and charged to the profit and loss account. Discount on the notes is regarded as deferred expense whereas premium is accounted for as deferred income. Discount and premium are amortized over the entire life of the notes on an effective interest rate method and are accounted for as adjustment to the interest expense of the notes. The arranger and custodian fees paid under the NIP and DIP are amortized to the profit and loss account over the life of the notes issued.

On redemption/repurchase of the notes, the resulting gains or losses, being the difference between the redemption/repurchase amount and the carrying amount, are recognized in the profit and loss account in the year in which the redemption/repurchase takes place.

i. Interest rate swap ("IRS") contracts for hedging purposes

The IRS contracts are solely entered into as a hedge against interest rate risk on the notes issued under the NIP, DIP and investment in debt securities.

The net interest payable or receivable arising from the IRS contracts is recorded on an accrual basis and charged against the interest expense of the notes or interest income of the debt securities for the year.

i. Interest rate swap ("IRS") contracts for hedging purposes (continued)

Gains and losses on early termination of the IRS contracts are immediately recognized in the profit and loss account when the underlying debt is early redeemed.

Gains and losses on early termination of the IRS contracts originally accounted for as a hedge to a debt are amortized over the remaining original life of the IRS contracts when the underlying debt is not early redeemed.

j. Mortgage guarantee business

The mortgage guarantee business of the Company is accounted for on the annual accounting basis. Under the annual accounting approach, the Company makes provisions based on credible estimates of future income and outgoings to determine the underwriting result for the current accounting period. The underwriting result includes any adjustments arising from the correction of the previous estimates.

Gross premiums represent direct business written through the Authorized Institutions during an accounting period. The gross premiums include a major portion of reinsurance premiums paid to Mortgage Reinsurers and the net premiums including risk premium portion and/or servicing fee to be earned by the Company. The net premiums are recognized as income on a time-apportioned basis when the insurance coverage has been effective.

Unearned premiums represent that portion of net premiums written which are estimated to relate to risks and services subsequent to the balance sheet date.

Provisions are made for outstanding claims, claims incurred but not reported, loss reserve and unexpired risk at the end of each year. For risk sharing business, 50% of the net risk premiums earned is set aside as a Contingency Reserve for a reasonable period of time in accordance with relevant regulatory guidelines and considered by directors as appropriate.

k. Guaranteed mortgage-backed pass-through securities ("MBS")

Upon completion of the sale of a mortgage pool to an independent Special Purpose Corporation ("SPC") under the MBS programme, the Company derecognizes the applicable mortgage pool from its balance sheet; recognizes all assets obtained and liabilities incurred in consideration as proceeds of the sale, including cash and contingent liability in respect of guarantee on timely payment of principal and interest on the MBS; and recognizes in the profit and loss account any gain or loss on the sale.

As a separate arrangement, the Company guarantees the collectibility of the mortgage pool and recognizes a monthly guarantee fee income from the SPC in the profit and loss account on a time-apportioned basis. Since the Company assumes all credit risks arising from the mortgage loans under the MBS programme, it adheres to the loan provisioning guidelines in Note 2(f) approved by the Board of Directors for making necessary provisions in the profit and loss account.

3. Interest income

	2000 HK$'000	1999 HK$'000
Mortgage portfolio	**736,337**	894,243
Cash and short-term funds	**187,367**	18,904
Investment in debt securities – listed	**1,935**	–
Investment in debt securities – unlisted	**84,098**	–
	1,009,737	913,147

4. Interest expense

	2000 HK$'000	1999 HK$'000
Bank loans and short-term bills	**108,410**	78,969
Debt securities	**543,616**	427,661
	652,026	506,630

5. Other income, net

	2000 HK$'000	1999 HK$'000
Early prepayment fees and late charges	**9,706**	9,057
Subletting income of office premises (Note 24)	**2,640**	2,534
Net premiums earned (Note 9)	**8,352**	1,454
Guarantee fee income on MBS	**6,060**	1,246
Excess servicing receipts on MBS	**4,053**	(79)
Issuance costs of debt securities	**(1,823)**	(1,441)
Others	**5,371**	(919)
	34,359	11,852

6. Operating expenses

	2000 HK$'000	1999 HK$'000
Staff costs		
Salaries and benefits	**58,736**	53,101
Premises		
Rental	**10,422**	10,356
Others	**3,118**	3,106
Directors' emolument	**–**	–
Depreciation	**12,181**	10,284
Consultancy fee	**3,450**	3,660
Auditors' remuneration	**250**	250
Other operating expenses	**10,270**	10,717
	98,427	91,474

7. Provisions for bad and doubtful loans

	2000 HK$'000	1999 HK$'000
Provisions against mortgage portfolio		
– specific	**13,418**	4,042
– general	**3,811**	3,204
	17,229	7,246

8. Taxation

(a) Taxation in the profit and loss account represents:–

	2000 HK$'000	1999 HK$'000
Hong Kong profits tax	**43,684**	49,012
Deferred taxation	**(376)**	(595)
	43,308	48,417

Hong Kong profits tax has been provided at the rate of 16% (1999: 16%) on the estimated assessable profit for the year. Deferred taxation has been provided on the timing difference arising from tax allowance in excess of depreciation. There is no significant unprovided deferred taxation.

(b) Taxation in the balance sheet represents:–

	2000 HK$'000	1999 HK$'000
Hong Kong profits tax	**11,512**	39,408
Deferred taxation	**2,640**	3,016
	14,152	42,424

9. Revenue account for mortgage guarantee business

	2000 HK$'000	1999 HK$'000
Gross premiums written	**122,698**	51,218
Reinsurance premiums	**(93,524)**	(44,692)
Net premiums written	**29,174**	6,526
Add: unearned premium brought forward	**5,018**	–
unearned premium carried forward	**(25,894)**	(5,018)
Increase in unearned premiums	**(20,876)**	(5,018)
Net premiums earned before provision	**8,298**	1,508
Write-back/(provisions) for outstanding claims (Note 21)	**54**	(54)
Net premiums earned (Note 5)	**8,352**	1,454
Management expenses	**(2,554)**	(4,002)
Underwriting gains/(losses)	**5,798**	(2,548)

The management expenses formed part of the operating expenses in Note 6.

10. Cash and short-term funds

	2000 HK$'000	1999 HK$'000
Cash at banks (Note 17)	**2,393**	2,062
Time deposits with banks (Note 17)	**2,065,741**	4,994,676
	2,068,134	4,996,738

11. Interest and remittance receivables

	2000 HK$'000	1999 HK$'000
Interest receivable from mortgage portfolio	**36,298**	29,368
Interest receivable from interest rate swap contracts	**124,715**	48,190
Interest receivable from investment in debt securities	**22,618**	–
Interest receivable from time deposits with banks	**6,638**	13,680
Loan instalments, in transit, from the Servicers	**58,843**	93,814
	249,112	185,052

12. Prepayments, deposits, and other assets

	2000 HK$'000	1999 HK$'000
Office rental deposit	**2,239**	2,239
Corporate club debentures	**670**	670
Others	**2,727**	5,246
	5,636	8,155

13. Deferred expense, net

	2000 HK$'000	1999 HK$'000
Deferred expenses/(income) arising on issuance of debt securities		
At 1 January	**39,050**	25,691
Additions for the year		
– deferred expenses	**182,447**	33,442
– deferred income	**(1,155)**	(2,118)
Less: amortization	**(107,463)**	(17,965)
At 31 December	**112,879**	39,050

14. Mortgage portfolio, net

(a) Mortgage portfolio less provisions

	2000 **HK$'000**	1999 HK$'000
Outstanding principal balance of mortgage portfolio (Note 17)	**11,119,240**	8,749,370
Provisions for bad and doubtful loans		
– specific	**(13,248)**	(4,042)
– general	**(22,967)**	(18,552)
	11,083,025	8,726,776

At 31 December 2000, the mortgage portfolio had a weighted average remaining term of 15 years on a contractual basis, without taking into account any prepayment of the mortgage loans. Final maturity of the mortgage portfolio is in the year 2030.

(b) Provisions for bad and doubtful loans

	Specific HK$'000	**General HK$'000**	**Total HK$'000**	**Suspended Interest HK$'000**
At 1 January 2000	**4,042**	**20,496**	**24,538**	**661**
Amounts written off	**(4,212)**	**–**	**(4,212)**	**(1,137)**
Charge to profit & loss account	**13,418**	**3,811**	**17,229**	**–**
Interest suspended during the year	**–**	**–**	**–**	**4,042**
Suspended interest recovered	**–**	**–**	**–**	**(608)**
At 31 December 2000	**13,248**	**24,307**	**37,555**	**2,958**

	Specific HK$'000	**General HK$'000**	**Total HK$'000**	**Suspended Interest HK$'000**
At 1 January 1999	–	17,292	17,292	–
Amounts written off	–	–	–	–
Charge to profit & loss account	4,042	3,204	7,246	–
Interest suspended during the year	–	–	–	1,156
Suspended interest recovered	–	–	–	(495)
At 31 December 1999	4,042	20,496	24,538	661

14. Mortgage portfolio, net (continued)

(b) Provisions for bad and doubtful loans (continued)

As regards the loan provisioning on the guaranteed mortgage loans under the MBS programme, a sum of HK$1,340,000 was grouped under "Other provisions" (Note 19). (1999: HK$1,944,000). The loan provision written back amounting to HK$604,000 was included in the profit & loss account.

(c) The total mortgage loans on which interest has been placed in suspense or has ceased to accrue are as follows:–

	2000 HK$'000	1999 HK$'000
Gross mortgage loans	**46,148**	12,826
Specific provisions	**(11,392)**	(4,042)
	34,756	8,784

Specific provisions were made after taking into account the current market value of the collateral of the delinquent loans.

15. Fixed assets

	Leasehold improvements HK$'000	**Furniture and fixtures** HK$'000	**Computers & related software** HK$'000	**Office equipment** HK$'000	**Motor vehicle** HK$'000	**Total** HK$'000
Cost						
As at 1 January 2000	10,062	1,515	32,229	1,609	539	45,954
Additions	1,171	260	6,831	140	-	8,402
As at 31 December 2000	11,233	1,775	39,060	1,749	539	54,356
Accumulated depreciation						
As at 1 January 2000	4,183	744	14,691	1,143	337	21,098
Charge for the year	1,257	165	10,274	350	135	12,181
As at 31 December 2000	5,440	909	24,965	1,493	472	33,279
Net book value						
Ending balance as at 31 December 2000	5,793	866	14,095	256	67	21,077
Ending balance as at 31 December 1999	5,879	771	17,538	466	202	24,856

16. Investment in debt securities

	2000 HK$'000	1999 HK$'000
Held-to-maturity securities		
Listed outside Hong Kong	**129,832**	–
Unlisted	**1,174,921**	–
	1,304,753	–
Market value of listed securities		
Issued by:		
– corporate entities	**30,912**	–
– others	**99,900**	–
	130,812	–

17. Maturity profile

	2000						
	Repayable on demand HK$'000	3 months or less HK$'000	1 year or less but over 3 months HK$'000	5 years or less but over 1 year HK$'000	After 5 years HK$'000	Undated HK$'000	Total HK$'000
Assets							
– Cash and short-term funds	2,393	2,065,741	–	–	–	–	2,068,134
– Mortgage portfolio	1,696	132,880	401,722	2,431,559	8,133,774	17,609	11,119,240
– Investment in debt securities	–	649,954	125,023	429,875	99,901	–	1,304,753
	4,089	2,848,575	526,745	2,861,434	8,233,675	17,609	14,492,127
Liabilities							
– Short-term bank loans	–	427,200	–	–	–	–	427,200
– Debt securities	–	2,600,000	4,546,000	4,275,000	200,000	–	11,621,000
	–	3,027,200	4,546,000	4,275,000	200,000	–	12,048,200

17. Maturity profile (continued)

	1999						
	Repayable on demand HK$'000	3 months or less HK$'000	1 year or less but over 3 months HK$'000	5 years or less but over 1 year HK$'000	After 5 years HK$'000	Undated HK$'000	Total HK$'000
Assets							
– Cash and short-term funds	2,062	4,994,676	–	–	–	–	4,996,738
– Mortgage portfolio	2,713	92,499	290,617	1,804,680	6,558,536	325	8,749,370
– Investment in debt securities	–	–	–	–	–	–	–
	4,775	5,087,175	290,617	1,804,680	6,558,536	325	13,746,108
Liabilities							
– Short-term bank loans	–	–	–	–	–	–	–
– Debt securities	–	4,000,000	2,445,000	4,796,000	200,000	–	11,441,000
	–	4,000,000	2,445,000	4,796,000	200,000	–	11,441,000

18. Interest payable

	2000 HK$'000	1999 HK$'000
Short-term bank loans	**251**	–
Debt securities	**119,989**	96,770
	120,240	96,770

19. Accounts payable, accrued expenses and other liabilities

	2000 HK$'000	1999 HK$'000
Accounts payable and accrued expenses	**39,942**	33,044
Other provisions (Note 14(b))	**5,704**	4,993
	45,646	38,037

20. Debt securities

	2000 HK$'000	1999 HK$'000
Fixed-rate bills and notes issued under the		
– NIP	**9,000,000**	8,000,000
– DIP	**2,621,000**	3,441,000
	11,621,000	11,441,000

Notes and bills issued during the year comprise:

	NIP HK$'000	**DIP** HK$'000
Amount issued	6,000,000	625,000
Consideration received	5,818,738	624,970

All the debt securities issued are unsecured obligations of the Company, and are issued for the purposes of providing general working capital and refinancing.

21. Provisions for outstanding claims

Provisions for outstanding claims for MIP are recorded net of recoveries from the mortgage reinsurers. At 31 December 2000, there was no loss reserve made for risk sharing business and no provision made in respect of "claims incurred but not reported" for both back-to-back and risk sharing businesses. At 31 December 2000, the gross outstanding claim was HK$497,000, which was fully recovered from the Approved Reinsurer.

22. Share capital

	2000 & 1999 HK$'000
Authorized	
3 billion ordinary shares of HK$1 each	**3,000,000**
Issued and fully paid	
2 billion ordinary shares of HK$1 each	**2,000,000**

23. Note to the cash flow statement

Reconciliation of profit before taxation to net cash (outflow)/inflow from operating activities:

	2000 **HK$'000**	1999 HK$'000
Profit before taxation	**276,414**	319,649
Depreciation	**12,181**	10,284
Amortization of deferred expenses	**107,463**	17,965
Provisions for bad and doubtful loans	**17,833**	5,302
Mortgage portfolio written off net of recoveries	**(4,212)**	–
Amortization of investment in debt securities	**(20)**	–
Decrease in interest and remittance receivables	**(64,060)**	(49,174)
Decrease/(increase) in prepayments, deposits and other assets	**2,519**	(3,296)
(Increase)/decrease in mortgage portfolio	**(2,369,870)**	2,644,407
Increase in interest payable	**23,470**	15,504
Increase in accounts payable and accrued expenses and other liabilities	**7,609**	7,511
Increase in unearned premiums	**20,876**	5,018
Net cash (outflow)/inflow from operating activities	**(1,969,797)**	2,973,170

24. Related party transactions

Mr. Norman Chan and Mr. Tony Latter are the respective Deputy Chief Executives of the Hong Kong Monetary Authority. The Company is a member under the Central Moneymarkets Unit ("CMU") Membership Agreement with the Monetary Authority through his CMU in respect of the Company's HK dollar debt issuance and securities investment.

On 12 February 1999, the Company entered into a sub-tenancy agreement with Exchange Fund Investment Limited ("EFIL") in which EFIL occupies part of the Company's office premises at a fair market price. EFIL is wholly owned by the Exchange Fund. The sub-letting income was approximately HK$2.6 million for the year ended 31 December 2000 (1999: HK$2.5 million). Mr. Norman Chan and Mr. Eddy Fong are the respective directors of EFIL.

Ms. Anita Fung is a Director, Head of Fixed Income and Derivatives, Asia Pacific, Treasury and Capital Markets of HSBC, and The Hon. Sin Chung-kai is an Assistant IT Project Manager of HSBC. HSBC is (a) a primary dealer under the Company's HK$20 billion Debt Issuance Programme; (b) an approved seller/servicer under the Mortgage Purchase Programme of the Company; and (c) an approved authorized institution which has entered into a Master Mortgage Insurance Policy with the Company under the Mortgage Insurance Programme.

25. Commitments

	2000 HK$'000	1999 HK$'000
(a) Capital		
Authorized and contracted for	**4,774**	342
Authorized but not contracted for	**17,378**	14,363
	22,152	14,705

(b) Operating lease

Operating lease commitments at 31 December 2000 amounted to HK$41,686,000 (1999: HK$52,108,000) of which HK$10,422,000 (1999: HK$10,422,000) is payable in the next twelve months. Such operating lease commitments at 31 December 2000 payable over the next twelve months, analysed according to the period in which the lease expires, are as follows:

	2000 HK$'000	1999 HK$'000
Land and buildings		
expiring in the first year	**–**	–
expiring in the second to fifth years	**10,422**	10,422
expiring after the fifth year	**–**	–
	10,422	10,422

26. Forward commitment facility

Under this facility, the Company has committed to purchase eligible floating rate mortgages from the approved seller/servicers for an agreed amount within a specified period of up to twelve months. The Company has adopted a flexible pricing approach through which the net required yield of the mortgages to be offered for sale will be subject to negotiation with the approved seller/servicers on a case-by-case basis. At 31 December 2000, the outstanding commitment amount to purchase floating rate mortgages was HK$400 million (1999: HK$3,886 million).

27. Fixed adjustable rate mortgages ("FARM") programme

The Company has committed to purchase a certain amount of eligible FARM from the approved seller/servicers on a first come, first served loan-by-loan basis. The gross mortgage rates are fixed for a period of one, two or three years. At 31 December 2000, the outstanding commitment amount to purchase FARM was HK$3.453 billion (1999: HK$3.453 billion).

28. Mortgage insurance programme ("MIP")

The Company offers mortgage insurance which provides cover to the approved seller/servicers for credit loss of up to 20% of the property value of a mortgage loan when the loan amount has exceeded 70% of the property value at origination.

Under the back-to-back arrangement, the Company reinsures the risk exposure with the approved Mortgage Reinsurers ("MR") on a 100% basis. The Company has started to assume a 20% risk sharing in mortgage insurance business with some MR since April 2000. At 31 December 2000, the risk-in-force was approximately HK$1.553 billion (1999: HK$530 million) of which HK$1.381 billion risk for credit loss was ceded to the MR and the balance of HK$172 million was assumed by the Company.

29. Off-balance-sheet exposures

(a) Contingent liabilities

	2000 **HK$'000**	1999 HK$'000
Guarantees under MBS programme	**642,546**	1,601,096

(b) Financial contracts

Interest rate swap contracts are entered into for hedging the fixed-rate bills and notes issued under the NIP and DIP and an investment in debt securities.

i) The outstanding contracted notional amount of the interest rate swap contracts is as follows:

	2000 **HK$'000**	1999 HK$'000
Interest rate swap contracts	**11,228,000**	6,691,000

29. Off-balance-sheet exposures (continued)

(b) Financial contracts (continued)

ii) The replacement costs and credit risk-weighted amounts of the interest rate swap contracts are as follows. These amounts do not take into account the effects of bilateral netting arrangements with the counterparties.

	2000		1999	
	Replacement cost HK$'000	**Credit risk-weighted amount HK$'000**	Replacement cost HK$'000	Credit risk-weighted amount HK$'000
Interest rate swap contracts	**247,323**	**24,225**	89,722	23,230

The replacement costs represent the cost of replacing all interest rate swap contracts that have a positive value when marked to market. The credit risk-weighted amounts refer to the amount as computed in accordance with the Capital-to-Assets ratio guidelines (Note 30). The Company has not experienced any non-performance by its counterparties.

30. Capital-to-Assets ratio

To ensure that the Company is managed in a prudent manner, the Financial Secretary of the Government of the Hong Kong Special Administrative Region issued guidelines in 1997 in respect of the minimum Capital-to-Assets ratio ("CAR") to be maintained by the Company. The minimum CAR stipulated in the guidelines is 5%.

	2000	1999
Capital-to-Assets ratio	**12.3%**	10.1%

The Capital-to-Assets ratio is calculated as a ratio, expressed as a percentage, of its total capital base to the sum of its total on-balance sheet assets and total off-balance sheet exposures.

31. Comparative Figures

Certain comparative figures for 1999 have been reclassified to conform to the current year's presentation.

32. Approval of financial statements

The financial statements were approved by the Board of Directors on 1 March 2001.


14 March 2000

Expansion of the Mortgage Purchase Programme to include mortgage loans originated under the Home Starter Loan Scheme, loans held in corporate names and staff mortgage loans

24 March 2000

Third Annual General Meeting

13 May 2000

Issued the second listed notes of HK$500 million with a retail portion of HK$100 million under the Note Issuance Programme

29 May 2000

First meeting of the Steering Committee on “Standardization of Mortgage Origination Documents”

30 May 2000

Signing Ceremony with Dao Heng Bank for the HK$1 billion Mortgage - Bond Asset Swap Programme

30 May 2000

Issued DIP notes of HK$600 million to Dao Heng Bank under the Mortgage - Bond Asset Swap Programme

27 July 2000

Announced half-year results with an unaudited operating profit after tax of HK$127 million for the six months ended 30 June 2000

18 August 2000

Launched the expanded Mortgage Insurance Programme to cover loans with LTV ratio of up to 90% and the MIP Advertising Promotional Campaign

2 December 2000

Public seminar on "Interest Trend & Prudent Investment Strategy" jointly organized with the Hong Kong Capital Markets Association, Financial Markets Association, Hong Kong Exchanges and Clearing, City University of Hong Kong and Hong Kong Economic Times

14 December 2000

Issued the third listed notes of HK$500 million with a retail portion of HK$100 million under the Note Issuance Programme

22 December 2000

Appointed Hewlett Packard as the developer for the Integrated Information Delivery System project

27 December 2000

Approval granted by the Board of Directors to purchase mortgage loans from Government housing agencies and property developers

List of Approved Seller/Servicers

As at December 2000

1. ABN AMRO Bank N.V.
2. AIG Finance (Hong Kong) Limited
3. American Express Bank Ltd.
4. Asia Commercial Bank Limited
5. Bank of America (Asia) Limited
6. Bank of China
7. Bank of Communications
8. The Bank of East Asia, Limited
9. The Chase Manhattan Bank
10. Chekiang First Bank Limited
11. The China and South Sea Bank Limited
12. The China State Bank Limited
13. Chiyu Banking Corporation Limited
14. Citibank, N.A.
15. CITIC Ka Wah Bank Limited
16. Dah Sing Bank, Limited
17. Dao Heng Bank Limited
18. DBS Kwong On Bank Limited
19. First Pacific Bank Limited
20. Fortis Bank Asia HK
21. GE Capital (Hong Kong) Limited
22. Hang Seng Bank Limited
23. Hang Seng Credit Limited
24. Hang Seng Finance Limited
25. The Hongkong Chinese Bank, Limited
26. The Hongkong and Shanghai Banking Corporation Limited
27. Hua Chiao Commercial Bank Limited
28. Industrial and Commercial Bank of China (Asia) Limited
29. International Bank of Asia Limited
30. Kincheng Banking Corporation
31. The Kwangtung Provincial Bank
32. Liu Chong Hing Bank Limited
33. Nanyang Commercial Bank, Limited
34. The National Commercial Bank, Limited
35. ORIX Asia Limited
36. Overseas Trust Bank, Limited
37. Po Sang Bank Limited
38. Shanghai Commercial Bank Limited
39. Sin Hua Bank Limited
40. Standard Chartered Bank
41. United Chinese Bank Limited
42. Wing Hang Bank, Limited
43. Wing Lung Bank, Limited
44. The Yien Yieh Commercial Bank Limited

List of Mortgage Reinsurers, DIP Primary Dealers, Selling Group Members and NIP Market Makers

Mortgage Reinsurers

Asia Insurance Company, Limited
Hang Seng Insurance Company Limited
HSBC Insurance (Asia) Limited
PMI Mortgage Insurance Co.
United Guaranty Mortgage Indemnity Company

DIP Primary Dealers

Dao Heng Bank Limited
The Hongkong and Shanghai Banking Corporation Limited
Merrill Lynch Far East Limited
Tokyo-Mitsubishi International (HK) Limited
UBS AG, Hong Kong Branch

DIP Selling Group Members

ABN AMRO Bank N.V.
The Bank of East Asia, Limited
Barclays Bank PLC, Hong Kong Branch
Chase Manhattan Asia Limited
Citicorp International Limited
Commonwealth Bank of Australia
Deutsche Bank AG, Hong Kong Branch
Goldman Sachs (Asia) L.L.C.
Hang Seng Bank Limited
Jardine Fleming Bank Limited
J.P. Morgan Securities Asia Private Limited
Société Générale Asia Limited
Standard Chartered Bank

NIP Market Makers

ABN AMRO Bank N.V.
BA Asia Limited
Bank of China
The Bank of East Asia, Limited
Barclays Bank Plc
BNP PARIBAS
Chase Manhattan Asia Limited
Citicorp International Limited
Commonwealth Bank of Australia
Credit Agricole Indosuez
Credit Lyonnais
Dah Sing Bank Limited
Dao Heng Bank Limited
Deutsche Bank Aktiengesellschaft
Fortis Bank
Hang Seng Bank Ltd
The Hongkong and Shanghai Banking Corporation Limited
Jardine Fleming Bank Limited
The Kwangtung Provincial Bank
Nanyang Commercial Bank, Limited
National Westminster Bank plc
Société Générale Asia Limited
Standard Chartered Bank
Tokyo-Mitsubishi International (HK) Limited
UBS AG, Hong Kong
Wing Lung Bank Limited

Steering Committee for the Standardization of Mortgage Origination Documents

Terms of reference

- To review and draft mortgage origination documents with a view to developing a set of model documents that represents the best market practice;
- To develop a strategy to promote the adoption and use of standardized documents by the mortgage originating banks in Hong Kong, including consultation with the banks, credit rating agencies and the relevant regulators on the draft model documents; and
- To adopt user-friendly language in the drafting of the model documents with a view to promoting the use of plain English in legal documentation.

Members

Banks

1. American Express Bank Ltd.
2. Bank of America (Asia) Limited
3. Bank of China
4. The Bank of East Asia, Limited
5. The Chase Manhattan Bank
6. Chekiang First Bank Limited
7. Dao Heng Bank Limited
8. First Pacific Bank Limited
9. The Hongkong and Shanghai Banking Corporation Limited
10. Standard Chartered Bank

Credit Rating Agencies

11. FITCH IBCA Hong Kong Limited
12. Moody's Investors Service

Legal Professions

13. Hong Kong Bar Association
14. The Law Society of Hong Kong

Legal Academics

15. Law Faculty of The University of Hong Kong

Mortgage Reinsurers

16. Hang Seng Insurance Company Limited
17. United Guaranty Mortgage Indemnity Company

Key Statistics of the HKMC's 2000 Mortgage Portfolio

Retained portfolio	Jan	Feb	Mar	Apr
Aggregate				
Number of Approved Seller/Servicers	43	43	43	44
Number of active Sellers	24	24	24	24
Number of loans	6,393	6,143	6,084	5,878
Outstanding principal balance (HK$ million)	8,229	7,823	7,839	7,551
Delinquency (%)				
– > 90 days	0.16	0.19	0.19	0.24
Prepayment (%)				
– Partial	0.22	0.22	0.25	0.18
– Full	4.49	5.36	4.34	3.19
Weighted Average				
LTV ratio at origination (%)	62.5	62.7	62.6	62.7
Estimated current LTV ratio (%)	72.4	71.9	71.9	73.2
DTI at origination (%)	38.0	38.0	37.9	37.9
Remaining contractual term to maturity (months)	177.7	177.0	178.0	177.0
Seasoning (months)	36.4	37.0	37.0	38.0
Contractual life (months)	214.1	214.0	216.0	215.6
Geographical distribution				
Outstanding principal balance (HK$ million)				
– Hong Kong	2,342	2,193	2,285	2,225
– Kowloon	1,696	1,631	1,614	1,545
– New Territories	4,191	3,999	3,940	3,781
Number of Loans				
– Hong Kong	1,556	1,482	1,504	1,465
– Kowloon	1,351	1,314	1,286	1,241
– New Territories	3,486	3,347	3,294	3,172

Mortgage Insurance Programme	Jan	Feb	Mar	Apr
Number of Participating Banks	30	31	32	33
Applications received				
Number of applications	2,495	2,721	3,017	3,334
Total amount of mortgage loans (HK$ million)	5,169	5,639	6,241	6,924
Total risk in force (HK$ million)	919	1,002	1,113	1,232
Average size of mortgage loan (HK$ million)	2.1	2.1	2.1	2.1
LTV ratio at origination				
– 80% or below (%)	23	23	23	23
– above 80% and up to 85% (%)	77	77	77	77
– above 85% and up to 90% (%)	Nil	Nil	Nil	Nil
Applications approved				
Number of approved applications	2,277	2,440	2,702	2,924
Total amount of mortgage loans (HK$ million)	4,723	5,059	5,593	6,077
Total risk in force (HK$ million)	840	899	996	1,082
Types of property transaction				
Primary (%)	10	9	9	9
Secondary (%)	90	91	91	91
Choice of premium payment method				
Single payment (%)	86	86	86	86
Annual payment (%)	14	14	14	14

May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
44	44	44	44	44	44	44	44
24	24	24	24	24	24	25	25
5,689	6,004	6,881	6,730	7,235	8,570	8,482	8,587
7,243	7,713	8,960	8,697	9,387	11,141	11,023	11,119
0.35	0.31	0.29	0.38	0.37	0.30	0.33	0.42
0.34	0.24	0.24	0.22	0.16	0.11	0.15	0.16
3.37	3.57	2.66	2.36	2.09	1.44	1.81	1.54
62.8	62.7	63.5	63.5	63.6	62.9	63.0	63.1
74.7	77.2	80.5	79.4	79.9	79.3	80.8	84.4
37.9	37.9	38.0	38.0	38.0	37.3	37.3	37.6
175.0	177.0	175.0	179.0	178.0	176.0	176.0	175.0
39.0	37.0	36.0	35.0	35.0	36.0	38.0	38.0
214.0	214.0	211.0	213.0	214.0	212.0	214.0	214.0
2,141	2,310	2,698	2,616	2,882	3,455	3,446	3,501
1,472	1,531	1,803	1,744	1,928	2,268	2,240	2,260
3,630	3,873	4,459	4,337	4,577	5,418	5,337	5,358
1,422	1,521	1,760	1,719	1,903	2,284	2,272	2,327
1,199	1,242	1,433	1,400	1,523	1,820	1,802	1,814
3,068	3,241	3,688	3,611	3,809	4,466	4,408	4,446

May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
33	33	33	34	36	36	37	37
3,717	4,133	4,534	5,092	5,856	6,505	6,974	7,367
7,716	8,508	9,288	10,434	11,996	13,264	14,111	14,797
1,378	1,522	1,671	1,886	2,207	2,476	2,659	2,807
2.1	2.1	2.1	2.0	2.0	2.0	2.0	2.0
22	22	21	20	19	19	18	18
78	78	79	79	75	70	68	66
Nil	Nil	Nil	1	6	11	14	16
3,180	3,469	4,006	4,495	4,970	5,611	6,284	6,609
6,627	7,198	8,196	9,213	10,174	11,472	12,715	13,272
1,180	1,285	1,470	1,659	1,852	2,126	2,390	2,511
8	9	10	11	13	13	13	13
92	91	90	89	87	87	87	87
86	86	87	88	88	89	89	89
14	14	13	12	12	11	11	11