

Financial Review

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The global economic recovery remained moderate and uneven, with US economic growth increasingly gaining traction while the eurozone and Japanese economies remained subdued. Against this backdrop, real economic activities in Hong Kong showed a moderate growth.

The residential property market revived and remained active from the second quarter of 2014. Market sentiment was supported by the expectation of a lingering low interest rate environment and a tight demand-supply balance in the property market. The overall residential property price increased by 13.5% over the year.

Income Statement

Financial Performance

The Corporation continued to maintain a solid financial position in 2014. The profit attributable to shareholders was HK\$746 million (2013: HK\$982 million) (Table 1). The reduction in profitability was mainly due to rundown in loan portfolio and reduced contributions from the mortgage insurance business and other income. Accordingly, return on equity was 8.4% (2013: 10.4%). The cost-to-income ratio increased to 24.3% (2013: 18.1%), mainly due to the reduction in operating income. The capital adequacy ratio remained solid at 23.5%, well above the minimum requirement of 8% stipulated by the Financial Secretary.

Table 1

Summary of financial performance	2014	2013
	HK\$ million	HK\$ million
Operating profit before impairment	798	1,064
Profit before tax	797	1,068
Profit attributable to shareholders	746	982
Return on shareholders' equity	8.4%	10.4%
Return on assets	1.4%	1.9%
Cost-to-income ratio	24.3%	18.1%
Capital adequacy ratio	23.5%	21.0%

Net Interest Income

The net interest income for the year was steady at HK\$651 million (2013: HK\$652 million). As a result of runoff in loan portfolio, the average loan portfolio reduced by HK\$4.2 billion. It was offset by an increase in cash and investments of HK\$7.8 billion, arising from cost-effective pre-funding. The net interest spread reduced to 1.2% from 1.3% in 2013, and the net interest margin dropped to 1.3% from 1.4% (Table 2).

Table 2

Net interest income	2014	2013
	HK\$ million	HK\$ million
Net interest income	651	652
Average interest-earning assets	50,021	46,430
Net interest margin	1.3%	1.4%
Net interest spread on interest-bearing liabilities ¹	1.2%	1.3%

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

Net Mortgage Insurance Premium Earned

After some consolidation in the previous year, the residential property market became more active in 2014. The total number of sale and purchase agreements for residential property registered at the Land Registry increased by 80% from a year earlier in the third quarter of 2014. In tandem with the development of the property market, mortgage lending also showed growth, with new mortgage loans drawn down in the residential property market increasing to HK\$214 billion from HK\$159 billion in 2013.

Due to the active property market, new business underwritten under the MIP increased to HK\$16 billion in 2014 from HK\$13.3 billion in 2013. The net premium earned after commission expenses was HK\$305 million. Taking into account the write-back of provisions for outstanding claims of HK\$6 million (2013: HK\$9 million), the net premium earned was HK\$311 million (2013: HK\$346 million).

Other Income

Other income was HK\$89 million (2013: HK\$297 million). Net gain on disposal of investments, which was mainly a result of rebalancing the investment portfolio, amounted to HK\$59 million (2013: HK\$136 million). As a consequence, dividend income of HK\$35 million (2013: HK\$89 million) was received. An exchange loss of HK\$13 million (2013 exchange gain: HK\$72 million) was recorded, primarily due to the effect of renminbi volatility from deposits and high-grade debt investments.

Operating Expenses

The Corporation continued to maintain stringent cost control to contain expenses and improve operating efficiency. Operating expenses rose 8.9% year on year to HK\$256 million, but this was HK\$18 million less than the budget. Staff costs, which were well contained at 61.3% of total operating expenses, amounted to HK\$157 million (2013: HK\$144 million). Premises rentals and related costs stood at HK\$39 million.

Allowance for Loan Impairment

Asset quality remained strong, with the delinquency ratio staying at 0.02%. Taking into account the development of the residential property market and local economic conditions, a collective assessment for loan impairment of HK\$1 million was charged in 2014 according to the approved prudent provisioning policy. During the year, loans written off were HK\$2 million (2013: HK\$0.5 million) with a recovery of HK\$1 million (2013: HK\$2 million).

Financial Position

Loan Portfolio

During the year, the Corporation purchased Hong Kong loan assets of about HK\$0.2 billion (2013: HK\$3.2 billion). After accounting for the prepayments and repayments during the year, the outstanding balance of the loan portfolio recorded a runoff of HK\$6.9 billion, leaving an outstanding balance of HK\$15.6 billion.

Investment Securities

The Corporation adopts a prudent, low-risk approach in managing its surplus funds and investment activities in accordance with the Board's investment guidelines. As at 31 December 2014, the total investment portfolio was HK\$14.9 billion (2013: HK\$12.4 billion), which included HK\$5.7 billion of available-for-sale investments and HK\$9.2 billion of held-to-maturity investments. There was no impairment loss from the investments.

Debt Securities Issued

In 2014, the Corporation issued HK\$30.5 billion of debt securities under the MTN Programme. All the non-Hong Kong dollar debts issued under the MTN Programme were swapped into Hong Kong dollars or US dollars for hedging purposes. As at 31 December 2014, the total outstanding balance of the debt securities increased by HK\$1.9 billion to HK\$33.3 billion from a year earlier, mainly reflecting the adoption of prudent pre-funding strategy.

Key Off-balance Sheet Exposure

Mortgage Insurance

The Corporation operates the MIP on a risk-sharing basis with the approved reinsurers. At the end of 2014, the total risk-in-force was about HK\$13.1 billion (2013: HK\$14.4 billion), of which HK\$2.1 billion (2013: HK\$2.4 billion) was ceded to the approved reinsurers. The off-balance sheet risk-in-force exposure borne by the Corporation decreased marginally to HK\$11 billion (2013: HK\$12 billion). Of this exposure, the excess loss of HK\$0.7 billion of risk-in-force was hedged through the excess-of-loss reinsurance arrangement to reinsure the middle layer risk exposure, while the Corporation retains a portion of the total risks comprising the first-loss and residual risks.

The provision for outstanding claims remained steady at 0.2% of the retained risk-in-force at the year-end. The delinquency ratio remained healthy at 0% (2013: 0%).

Dividend

At the Annual General Meeting held on 21 April 2015, the shareholders, having considered the financial performance and the capital requirements for business development, approved an ordinary dividend of HK\$0.175 (2013: HK\$0.25) per share, representing a dividend payout ratio of about 47% totalling HK\$350 million.

