

Financial Review

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In 2016, global economic growth remained modest with the US reporting good domestic growth while recovery in Europe and Japan remained sluggish. Global monetary divergence again widened while the US Federal Reserve continued to gradually normalise its monetary policy. Growth in China was moderating with signs of stabilisation in the second half of 2016.

In Hong Kong, economic growth was moderate amid a lacklustre global economy. Domestic demand strengthened, supported by further employment growth and sustained increases in labour earnings. Inflation pressures remained contained. The residential property market recorded a rebound since the second quarter of the year.

Income Statement

Financial Performance

The Corporation continued to uphold a solid financial position in 2016. The profit attributable to shareholders for 2016 was HK\$604 million (2015: HK\$725 million) (**Table 1**). The reduction in profitability was mainly due to the rundown in the loan portfolio and decrease in mortgage insurance premium income, partly offset by an increase in disposal gain and dividend income from investments. Accordingly, return on equity was 6.8% (2015: 8.1%). The cost-to-income ratio increased to 30.8% (2015: 25.7%), mainly due to the reduction in operating income coupled with resources devoted to support policy initiatives. The capital adequacy ratio remained solid at 21.3% (2015: 21.9%), well above the minimum requirement of 8% stipulated by the Financial Secretary.

Table 1

Operating profit before impairment	621	769
Profit before tax	622	770
Profit attributable to shareholders	604	725
Return on shareholders' equity	6.8%	8.1%
Return on assets	1.1%	1.4%
Cost-to-income ratio	30.8%	25.7%
Capital adequacy ratio	21.3%	21.9%

Net Interest Income

The net interest income for the year was HK\$491 million (2015: HK\$590 million). The drop was mainly due to the reduction of average loan portfolio by HK\$2.5 billion as a result of rundown in loan portfolio, partially mitigated by cost-effective pre-funding. The net interest spread reduced to 0.9% from 1.1% in 2016, and the net interest margin dropped to 1.0% from 1.2% (**Table 2**).

Table 2

Net Interest Income	2016 HK\$ million	2015 HK\$ million
Net interest income	491	590
Average interest-earning assets	49,281	49,842
Net interest margin	1.0%	1.2%
Net interest spread on interest-bearing liabilities ¹	0.9%	1.1%

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

Net Mortgage Insurance Premium Earned

The residential property market has recorded a rebound since the second quarter. The total number of sale and purchase agreements for residential property registered at the Land Registry increased by about 75% in the second half of 2016 as compared to the first half of 2016.

New business underwritten under the MIP increased to HK\$24.6 billion in 2016 from HK\$17.2 billion in 2015. Taking into account the provisions for outstanding claims of HK\$3 million (2015: write-back of HK\$2 million), the net premium earned was HK\$190 million (2015: HK\$289 million).

Other Income

Other income was HK\$213 million (2015: HK\$143 million). Net gain on disposal of investments, mainly a result of rebalancing the investment portfolio, amounted to HK\$160 million (2015: HK\$122 million). Dividend income was HK\$83 million (2015: HK\$73 million). An exchange loss of HK\$21 million (2015: HK\$39 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 moderately rose 3.7% year on year to HK\$277 million, but this was HK\$19 million less than the budget. Staff costs, which were well contained at 65% of total operating expenses, amounted to HK\$180 million (2015: HK\$168 million). Premises rentals and related costs were contained at HK\$37 million (2015: HK\$37 million).

Allowance for Loan Impairment

Asset quality remained strong, with the delinquency ratio of the Corporation's mortgage portfolio staying low at 0.03% (2015: 0.02%). Taking into account the rundown in loan portfolio and the low average current loan-to-value ratio of retained loan portfolio, a write-back on collective assessment for loan impairment of HK\$1 million was recorded in 2016 according to the approved prudent provisioning policy. During the year, loans written off were HK\$1 million (2015: HK\$2 million) with a recovery of HK\$1 million (2015: HK\$2 million).

Financial Position

Loan Portfolio

During the year, the Corporation purchased Hong Kong loan assets of about HK\$0.2 billion (2015: HK\$0.3 billion). After accounting for the prepayments and repayments during the year, the outstanding balance of the loan portfolio recorded a rundown of HK\$2 billion, leaving an outstanding balance of HK\$9.5 billion.

Investment Securities

The Corporation adopts a prudent, low-risk approach in managing its surplus funds and investment activities in accordance with the investment guidelines approved by the Board. As at 31 December 2016, the total investment portfolio maintained at HK\$16.9 billion (2015: HK\$16.9 billion), which included HK\$7 billion of available-for-sale investments and HK\$9.9 billion of held-to-maturity investments. There was no impairment loss from the investments.

Debt Securities Issued

In 2016, the Corporation issued HK\$24.5 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. The Corporation continued to adopt a prudent pre-funding strategy, with the total outstanding balance of the debt securities maintained at HK\$34.2 billion as at 31 December 2016 (2015: HK\$33.5 billion).

Key Off-Balance Sheet Exposure

Mortgage Insurance

The Corporation operates the MIP on a risk-sharing basis with approved reinsurers. At the end of 2016, the total risk-in-force was about HK\$16.8 billion (2015: HK\$13.4 billion), of which HK\$2.7 billion (2015: HK\$2.1 billion) was ceded to the approved reinsurers. The off-balance sheet risk-in-force exposure borne by the Corporation increased to HK\$14.1 billion (2015: HK\$11.3 billion).

The provision for outstanding claims remained steady at 0.1% of the retained risk-in-force at year-end. The delinquency ratio remained healthy at 0.01% (2015: 0%).

Reverse Mortgage

The Corporation operates the RMP as an insurer to provide mortgage insurance cover for a premium on reverse mortgage loans advanced by participating banks in Hong Kong. After taking into account undrawn future payout of reverse mortgage loans, the risk-in-force exposure¹ borne by the Corporation increased to HK\$4.3 billion (2015: HK\$2.9 billion) as at 31 December 2016.

Dividend

The Financial Secretary announced in the 2017–18 Budget that the Corporation had commenced the design and feasibility study of a public annuity scheme to help the elderly turn their assets into stable monthly retirement income. Having considered the capital requirements for business development, no dividend was declared for 2016 (2015: an ordinary dividend of HK\$0.3625 per share in a total amount of HK\$725 million).

¹ The risk-in-force includes the outstanding balance and undrawn commitment of a reverse mortgage loan. Undrawn commitment refers to the amount of expected future payout to the borrower based on the payment term.

