

CHAIRMAN'S STATEMENT



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Chairman & Managing Director

Economic Review

The global economy continued to wander in the doldrums in 2001. At first, it was generally expected that the US economy, having undergone frequent rate cuts in the first half of last year, would gradually recover in the second half. However, things do not happen as one wishes. The unexpected attacks of September the eleventh shocked the United States, leading to falling stock markets and sagging consumer confidence. The Federal Reserve had cut interest rate for the eleventh time, adding up to 475 basis points for the whole year, with an eye to stabilising public spirits and boosting market vitality. And the cuts are only beginning to bear fruit. It is hoped that the US market, having ridden out the various attacks, has tended to consolidate enough to gradually nurse the global economy back to health.

In the light of such factors as the flagging global economy, uncertain prospects, and the local economic transformation which is still groping for the right track, the Hong Kong economy remained stagnant in 2001, assessing its position before making its next move. The local property market witnessed the timely introduction by the Government of certain adjusted measures in response to market conditions last year. Such measures include the temporary halt in the sale of flats under the subsidised home ownership schemes, the relaxation of mortgages' loan-to-value ratio, and the provision of second mortgages by developers which has effectively enabled flats to be purchased without any down payment. The Hong Kong Monetary Authority has also permitted the refinancing of negative-equity mortgage loans up to 100 percent of the current market value of the mortgaged property. Moreover, the deduction of home loan interest has been raised. These measures have revitalised the new housing development market whose transaction activities has tended to pick up gradually. However, the secondary property market remained fragile with a trying outlook. The local stock market was volatile in 2001. And the Hang Seng Index dropped 24.5 percent last year. Although the Hang Seng Index was plagued by the drastic decline in the global economy in the first half of the year, it still managed to stay above the 12,000 points level. The attacks of September the eleventh added yet another blow to the Hang Seng Index in the second half of the year, causing it to sink to the 9,000 points level. Trading volumes have remained low to date with the Hang Seng Index hovering around the 12,000 points level. With the exception of utility stocks, which have increased slightly in value, stock prices in general are still subdued because of a lack of investor confidence. It is expected that the local stock market as a whole will mirror the movements of its overseas counterparts. In the face of the current predicament and the ongoing economic transformation, the Government can only plan to streamline its structure, reduce expenses, lower the budget deficit, strive for more mainlanders to visit the territory, and assist the tourism, hotel and other consumer industries to create a more favourable operating environment. It is hoped that, at this stage, these initiatives will help to pacify the public while riding out the storm.

As far as the banking industry is concerned, the trade remains fiercely competitive in such hotly contested areas as mortgage loans, credit cards, insurance and securities lending. Profit margins have generally been squeezed because of competitive pricing and other measures to secure market share. Furthermore, given the current sluggish global economic environment, banks still have to look for lending opportunities in a contracting market while maintaining credit quality at the same time. Admittedly, this is a very demanding task.

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Results Announcement

For the financial year of 2001, on an audited, consolidated basis, profit attributable to shareholders amounted to HK\$0.346 billion, a drop of 24.25 percent against that of the previous year. Customers' deposits increased 4.99 percent to HK\$32.686 billion. Total loans to customers (after accounting for provisions for bad and doubtful debts as well as interest accrued and suspended) rose 1.92 percent to HK\$18.5 billion. On 31 December 2001, the Bank's loan portfolios were made up as follows: property developments and investments (22.63 percent), personal real estate purchases (21.55 percent), financial and securities concerns (11.86 percent), trade finance (4.51 percent), wholesale and retail trade (2.87 percent), manufacturing, transportation and other businesses (22.52 percent), loans outside Hong Kong (8.63 percent), and others (5.43 percent). Adjusted capital adequacy ratio dipped 3.38 percent to 20.87 percent at the end of 2001, while average liquidity ratio for 2001 increased 7.75 percent to 58.56 percent. Loan-to-deposit ratio was merely 49.44 percent. Since the local economy remained sluggish in 2001, the various businesses have stayed on the sidelines without any substantial development plans. The reduction in capital investments has resulted in a quiet market. And the continual drop in the loan-to-deposit ratio reflects the fall in the need for capital. Total assets edged up 1.21 percent to HK\$39.463 billion. Shareholders' funds (after final dividend) amounted to HK\$5.665 billion, an increase of 1.6 percent. Given the rising unemployment rate, falling consumer confidence, continual deflation and limited lending opportunities, there is barely anything encouraging to report on the Hong Kong economy in 2001. In the light of these operating conditions, the Bank's results can be regarded as passably satisfactory. Your board has recommended paying the final dividend for the financial year of 2001 of HK\$0.30 per share to shareholders whose names appear on the Register of Members at the close of business on Friday, 19 April 2002. Total dividends for the financial year of 2001 (including the interim dividend of HK\$0.15 per share paid earlier) amounted to HK\$0.45 per share.

Profit Analysis

On an audited, consolidated basis, interest income fell 24.13 percent from that of 2000 to HK\$1.979 billion in 2001. Interest expenses decreased 29.13 percent to HK\$1.183 billion. Net interest income dropped 15.26 percent to HK\$0.797 billion, translating into net interest margin of 2.03 percent (a drop of 19.12 percent). After taking other operating income into consideration (which netted HK\$0.156 billion), the Bank recorded total operating income at HK\$0.953 billion. Operating expenses amounted to HK\$0.424 billion. Cost-to-income ratio was 44.45 percent. Operating profit before provisions and disposal of long-term assets decreased 25.7 percent to HK\$0.529 billion. Hong Kong's economic prospects are still murky, not to mention the intricacies of the international political and economic landscapes. The Bank has therefore persisted in adopting a prudent approach in order to ensure the security of its funds. Even though this means a temporary drop in profits, the Bank would rather be safe than sorry, bearing in mind that it strives to preserve its strength for the rosier days. Provisions for bad and doubtful debts continued to decrease, having fallen 20.46 percent to HK\$0.136 billion. After accounting for the provisions for bad and doubtful debts as well as the charge for taxation, the Bank recorded a decrease of 24.25 percent in the profit attributable to shareholders to HK\$0.346 billion, translating into earnings of HK\$0.80 per share. Net asset value (after final dividend) amounted to HK\$13.02 per share, a slight increase of 1.6 percent.