Our Ref.: B4/1C

19 November 2010

The Chief Executive
All Authorized Institutions

Dear Sir/Madam,

Prudential Measures for Property Mortgage Loans

As you aware, like many other economies, Hong Kong is currently facing exceptional global monetary conditions. With the announcement by the US Federal Reserve on the launching of the second round of "quantitative easing" on 3 November 2010, the market situation of abundant liquidity and ultra-low interest rates is expected to continue for a period of time. This will add further pressure to the property market and increase the risk of an asset price bubble. After some slow down in the mortgage lending market in September and early October following the introduction of the prudential measures for residential mortgage loans in mid-August 2010 by the Hong Kong Monetary Authority (HKMA), data received by the HKMA recently indicates that activities in the property market are showing renewed signs of heating up.

In view of these developments, the HKMA considers it necessary to take proactive actions to introduce further prudential measures for mortgage lending to address the increasing risk to the stability of the Hong Kong banking system. Authorized Institutions (AIs) are required to observe the following guidelines in undertaking mortgage business:

(a) lowering the maximum loan-to-value (LTV) ratio for residential properties with a value of HK$12 million or above to 50%;

(b) limiting the maximum LTV ratio for residential properties with a value of HK$8 million or above but below HK$12 million to 60%, subject to a maximum loan cap of HK$6 million;

(c) maintaining the 70% maximum LTV ratio for residential properties with a value below HK$8 million, subject to a maximum loan cap of HK$4.8 million;

(d) lowering the maximum LTV ratio for the following properties to 50% irrespective of their value:

  (i) residential properties which are not intended to be occupied by the owners;

  (ii) properties held by companies;

  (iii) commercial and industrial properties; and

  (iv) properties with mortgage loans based on borrowers' net worth (i.e. net worth-based property mortgage loans).

The above guidelines take immediate effect. To avoid causing hardship to borrowers who have signed a provisional sales and purchase agreement on or before the date of this letter, AIs may assess mortgage applications of these borrowers based on their existing underwriting criteria.

Detailed guidance on the above guidelines can be found in **Annex 1** of this letter. The HKMA will monitor compliance with the guidance in this letter through its routine onsite examinations and off-site reviews.

In addition, the HKMA has conducted a review of some AIs' policies and practises for net worth-based mortgage loans. It was noted that these AIs have adopted either the net asset value (NAV) concept or the asset-to-total debt obligation (ATD) ratio concept in determining borrowers' net worth positions and their eligibility to obtain a net worth-based mortgage. Both concepts are considered acceptable by the HKMA. Some AIs have adopted prudent benchmarks on the minimum NAV and ATD ratio required and on the eligibility of assets included in the NAV or ATD ratio calculation. These benchmarks are summarised in **Annex 2** of this letter. AIs are required to review and assess their existing policies and take immediate measures to bring them in line with these prudent benchmarks within a reasonable timeframe.

If your institution has any questions about this letter, please approach your usual contacts at the HKMA.

Yours faithfully,

Arthur Yuen
Deputy Chief Executive

Encl

Prudential Measures for Property Mortgage Loans

1. Lowering the maximum LTV ratio for residential properties with a value of HK$12 million or above to 50%

AIs are required to lower the maximum LTV ratio for residential properties with a value of HK$12 million or above to 50%.

This requirement, as well as Requirements 2 and 3 below, expect AIs to apply an LTV ratio lower than 70% under different circumstances. In cases where more than one of these requirements is applicable, AIs should apply the lowest LTV ratio dictated by the relevant requirement.

2. Limiting the maximum LTV ratio for residential properties with a value of HK$8 million or above but below HK$12 million to 60%

AIs are required to limit the maximum LTV ratio for residential properties with a value of HK$8 million or above but below HK$12 million to 60%. However, to avoid the anomaly that the maximum amount a purchaser of a property with a value of slightly below $12 million could borrow would be higher than that for a property valued at HK$12 million[1], the maximum loan amount for properties with a value of HK$8 million or above but below HK$12 million should be subject to a cap of $6 million.

The 70% LTV policy will continue to apply for properties with a value below $8 million, but subject to a maximum loan cap of $4.8 million. In other words, the only properties with a value of $6.86 million or below can enjoy a maximum LTV ratio of 70%.

3. Lowering the maximum LTV ratio for the following properties to 50% irrespective of the value of the properties:

(a) *Non-owner-occupied residential properties (Please refer to the Annex to the HKMA's circular of 13 August 2010 regarding the circumstances where properties may be regarded as owner-occupied, and the requirement for borrowers to make a formal declaration about their occupancy and intended occupancy of the mortgage property)*

(b) *Properties held by companies*

(c) *Commercial and industrial properties*

(d) *Properties under net worth-based mortgage*

---

1 Had there not been a cap of $6 million, a purchaser of a property valued at $11 million would have been able to borrow $6.6 million ($11 million x 60%), whereas a purchaser of a property valued at $12 million would only have been able to borrow $6 million ($12 million x 50%).

Annex 2

Prudent Benchmarks for Net worth-based Mortgage Loans

Minimum NAV / ATD ratio	Limiting net worth-based mortgage lending to borrowers with a positive NAV position or a minimum ATD ratio of at least 100%
NAV	Borrower's total eligible assets (net of the down payment amount of the property being acquired) minus his/her total debt obligations (including the mortgage loan being applied)
ATD ratio	$\dfrac{\text{Borrower's total eligible assets (net of the down payment amount of the property being acquired)}}{\text{Borrower's total debt obligations (including the mortgage loan being applied)}} \times 100\%$
Eligible assets	• Financial assets: cash, deposits, stocks, bonds, open-end unit trust, precious metals, etc, net of any credit facilities made against the assets.
	• Properties located in Hong Kong and free of encumbrance: ➢ 50% of the current market value (CMV) of the property. • Properties located in Hong Kong which are mortgaged as security for other credit facilities: ➢ 50% of the CMV of the property less the outstanding balance of credit facility made against the property. For example, if a borrower has a property with a CMV of HK$9 million which is mortgaged as security for a loan of, say, HK$4 million, then HK$0.5 million (HK$9 million x 50% – HK$4 million) may be included as eligible assets.
	Other assets that satisfy the following criteria: • Their market prices can be readily and objectively valued. • With an established liquid market in which they can be liquidated readily; and Generally speaking, assets such as art pieces, jewellery and other collectible items may not fulfil these criteria. AIs are expected to exercise due care in considering whether to accept these assets.
Total debt obligations	All outstanding debt obligations (including the mortgage loan being applied and other undrawn credit facilities) of a borrower should be included in order to avoid multiple loan applications using the same pool of eligible assets. Credit facilities which have been deducted in the calculation of a borrower's eligible assets should be included in determining the borrower's total debt obligations.