



HONG KONG MONETARY AUTHORITY

2017 Exchange Fund Results

29 January 2018



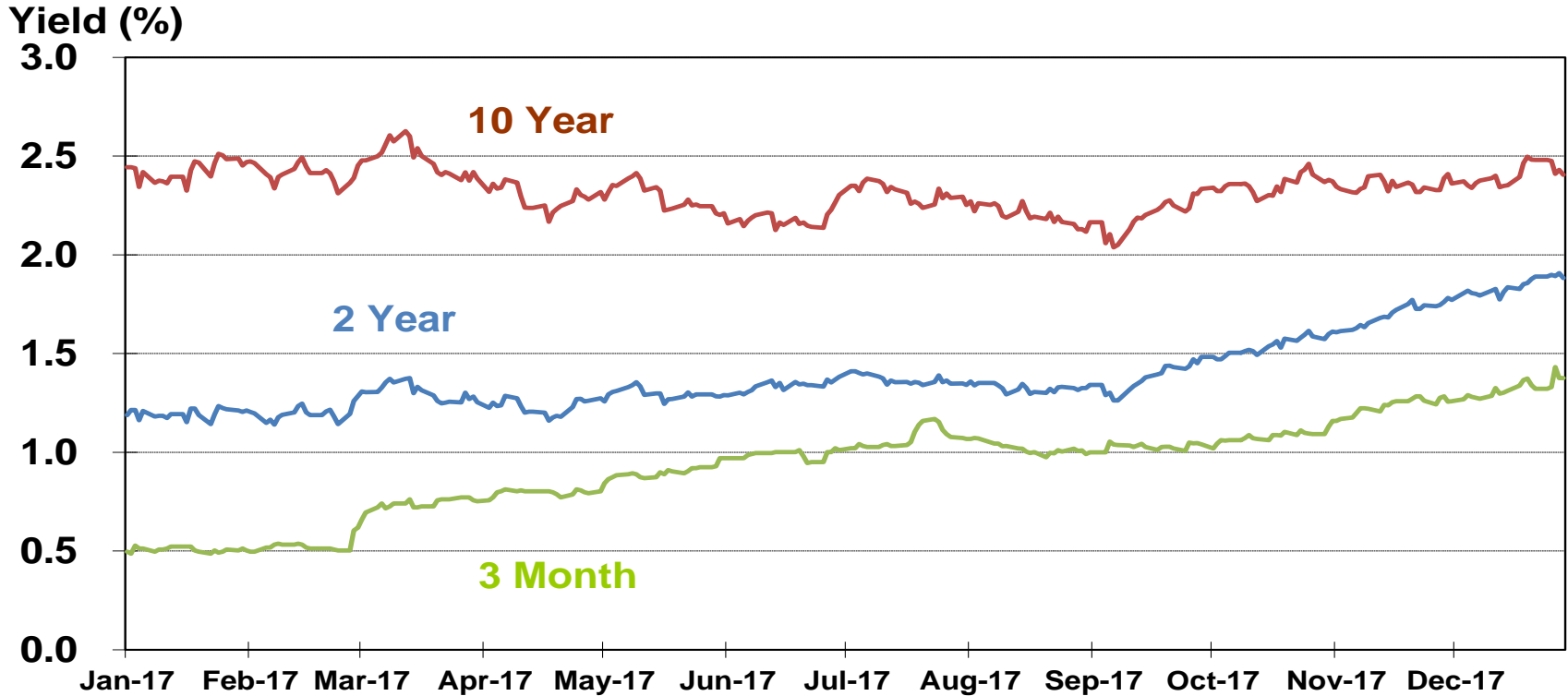
INVESTMENT OBJECTIVES OF THE EXCHANGE FUND

Investment objectives of the Exchange Fund:

- (1) to preserve capital;**
- (2) to ensure that the entire Monetary Base at all times will be fully backed by highly liquid US dollar denominated assets;**
- (3) to ensure sufficient liquidity for the purpose of maintaining monetary and financial stability; and**
- (4) subject to (1) – (3), to achieve an investment return that will preserve the long-term purchasing power of the Fund.**



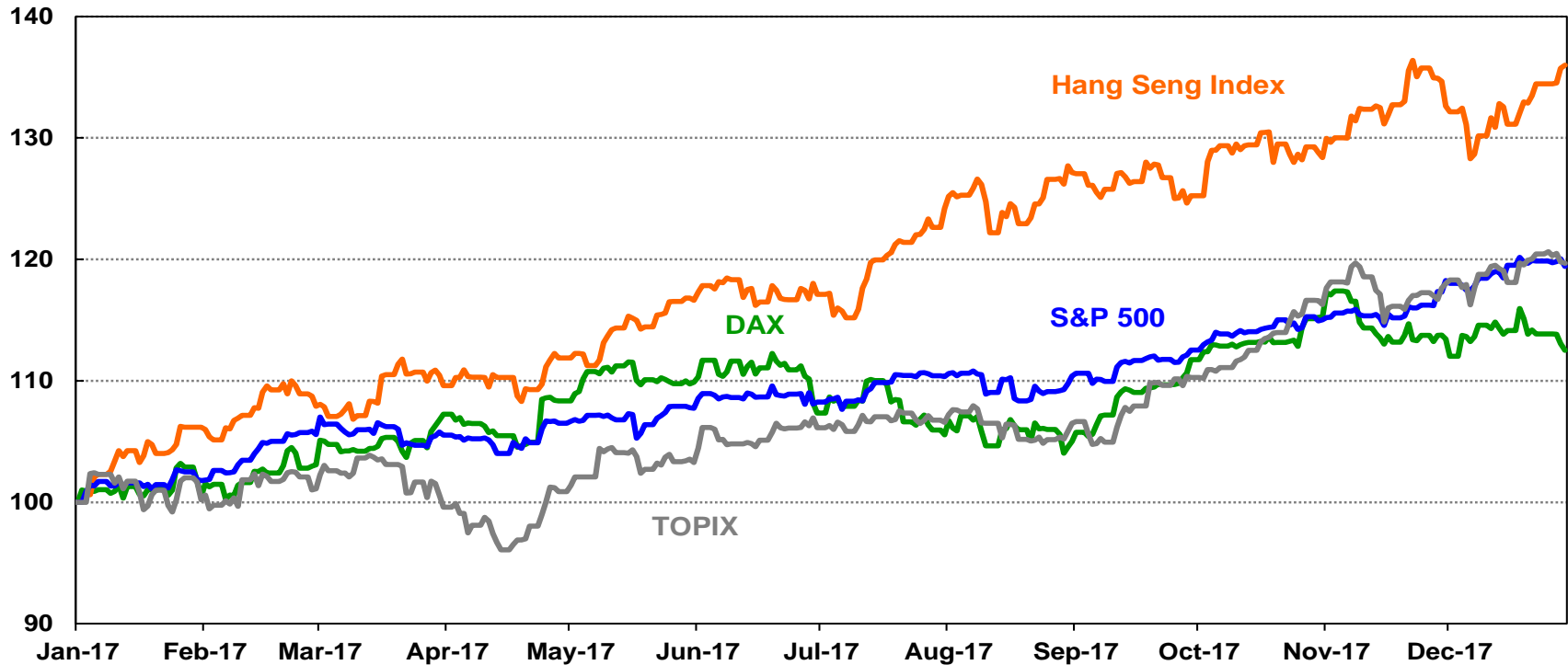
US GOVERNMENT BOND YIELDS IN 2017





EQUITY MARKETS IN 2017

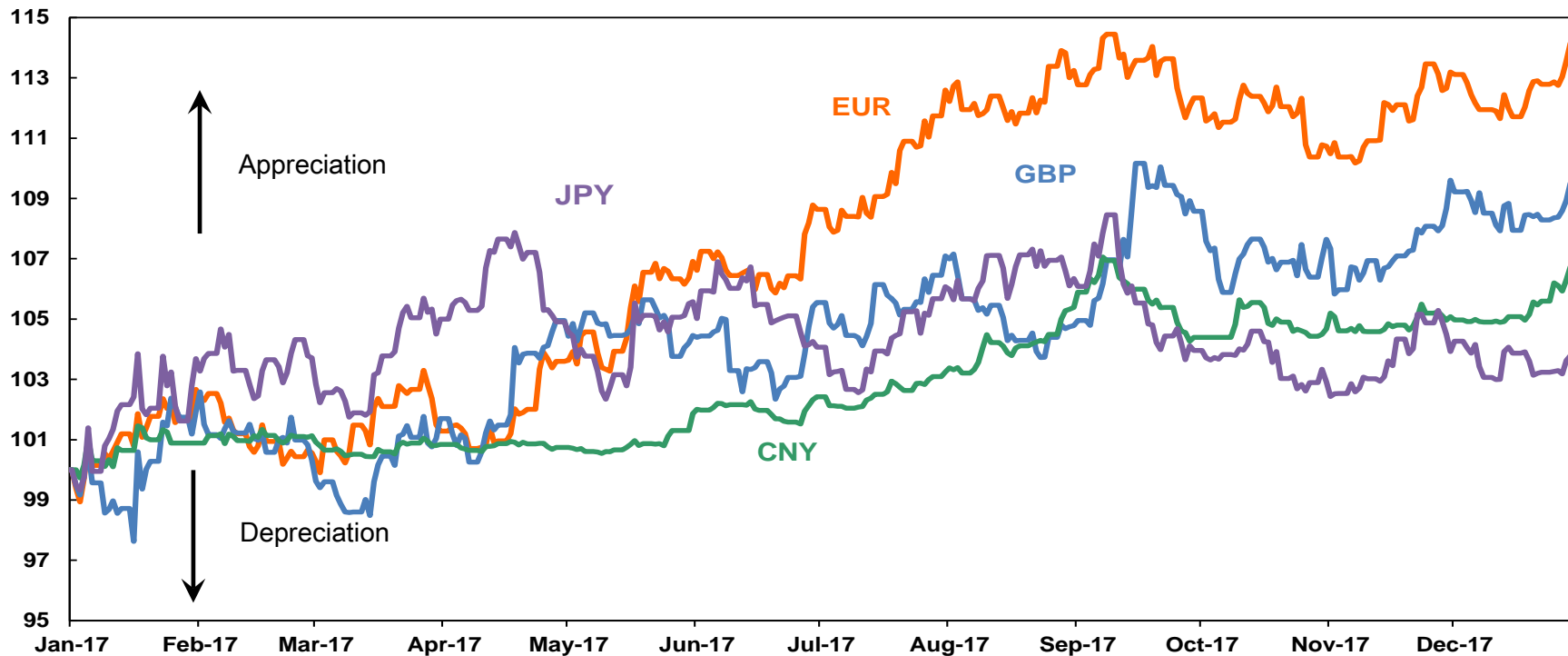
Normalized Index Level (2016 year-end = 100)





CURRENCY MARKETS IN 2017

Normalized FX Level Against USD (2016 year-end = 100)





INVESTMENT INCOME

← 2017 → 2016 2015 2014 2013

(unaudited)

(HK\$ billion)	Full year	2H	1H	Full year	Full year	Full year	Full year
Hong Kong equities*	58.3	30.5	27.8	5.3	(5.0)	6.5	10.1
Other equities	80.2	40.1	40.1	28.6	7.1	33.7	71.8
Bonds	34.3	17.8	16.5	33.1	15.9	47.3	(19.1)
Foreign exchange#	53.5	19.2	34.3	(15.8)	(44.9)	(52.7)	1.6
Other investments@	25.7	8.2	17.5	16.9	11.1	9.9	16.8
Investment income/(loss)	252.0	115.8	136.2	68.1	(15.8)	44.7	81.2

* Excluding valuation changes of the Strategic Portfolio

This is primarily the effect of translating foreign currency assets into Hong Kong dollar after deducting the portion for currency hedging.

@ Including valuation changes of private equity and real estate investments held under the Long-Term Growth Portfolio (LTGP). (The above figures represent valuation changes up to the end of September 2017. Valuations of these investments from October to December are not yet available.)



INCOME AND EXPENDITURE

(HK\$ billion)	← 2017 →			2016
	Full year	2H	1H	Full year
	(unaudited)			
Investment income	252.0	115.8	136.2	68.1
Other income	0.2	0.1	0.1	0.2
Interest and other expenses	<u>(9.8)</u>	<u>(4.8)</u>	<u>(5.0)</u>	<u>(6.4)</u>
Net income	242.4	111.1	131.3	61.9
Fee payment to Fiscal Reserves**	(23.5)	(12.1)	(11.4)	(33.1)
Fee payment to HKSAR government funds and statutory bodies*	(8.6)	(4.3)	(4.3)	(9.6)

* The rate of fee payment is 2.8% for 2017 and 3.3% for 2016.

This does not include the 2017 fee payment to the Future Fund because such amount will only be disclosed when the composite rate for 2017 is available (For 2016, the composite rate was 4.5% and fee payable to the Future Fund was HK\$10.1 billion).



EXCHANGE FUND ABRIDGED BALANCE SHEET

(HK\$ billion)

	At 31 Dec 2017	At 31 Dec 2016	Change
ASSETS	(unaudited)		
Deposits	346.4	386.7	(40.3)
Debt securities	2,762.2	2,466.1	296.1
Hong Kong equities*	204.2	147.3	56.9
Other equities	510.4	429.3	81.1
Other assets#	<u>200.3</u>	<u>189.3</u>	<u>11.0</u>
Total assets	<u>4,023.5</u>	<u>3,618.7</u>	<u>404.8</u>
LIABILITIES AND FUND EQUITY			
Certificates of Indebtedness	456.7	405.4	51.3
Government-issued currency notes & coins in circulation	12.2	11.9	0.3
Balance of the banking system	179.8	259.6	(79.8)
Exchange Fund Bills and Notes issued	1,045.8	961.0	84.8
Placements by banks and other financial institutions	59.3	56.1	3.2
Placements by Fiscal Reserves@	1,073.8	914.6	159.2
Placements by HKSAR government funds and statutory bodies	305.1	302.5	2.6
Other liabilities	<u>175.9</u>	<u>161.1</u>	<u>14.8</u>
Total liabilities	3,308.6	3,072.2	236.4
Accumulated Surplus	<u>714.9</u>	<u>546.5</u>	<u>168.4</u>
Total liabilities and fund equity	<u>4,023.5</u>	<u>3,618.7</u>	<u>404.8</u>

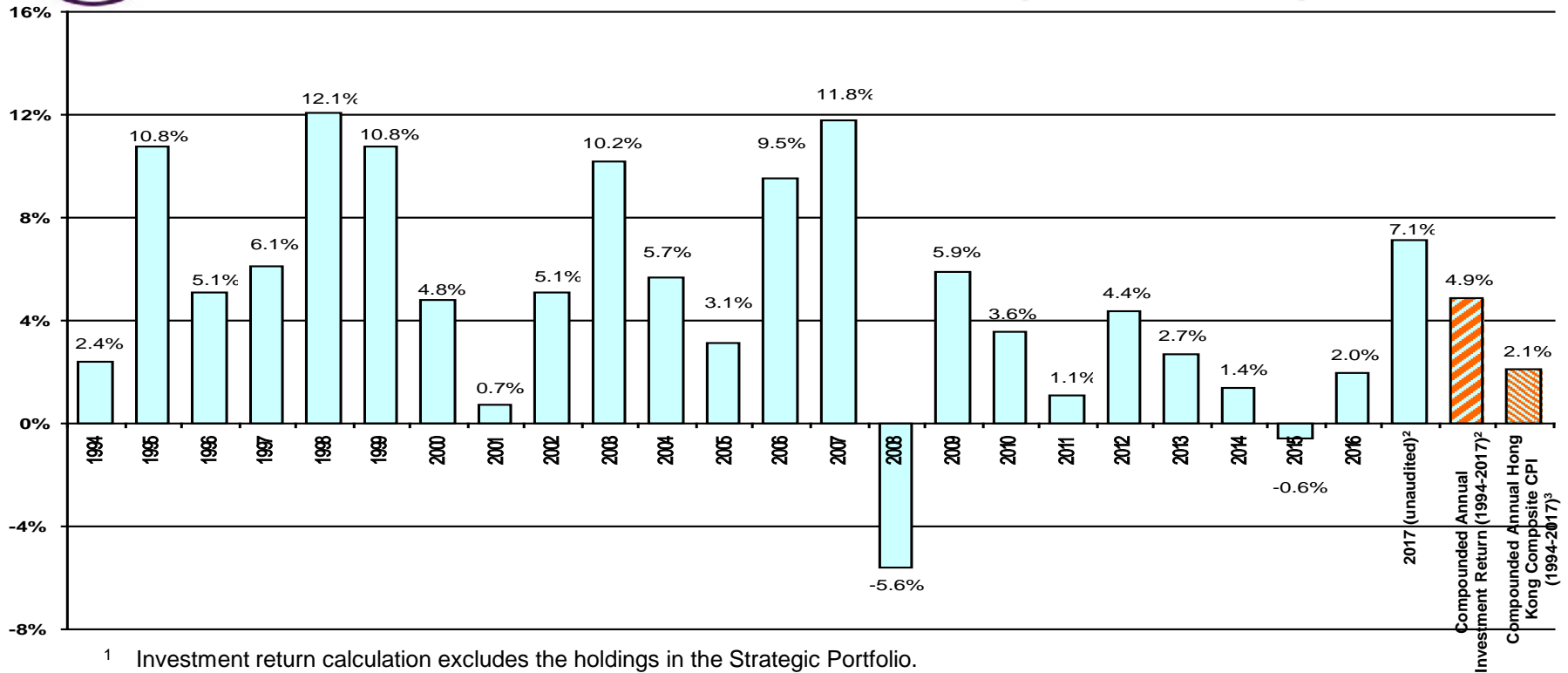
* Including shares of the Hong Kong Exchanges and Clearing Limited in the Strategic Portfolio

Including fund injection to Exchange Fund's investment holding subsidiaries at a carrying amount of HK\$135.2 billion at 31 Dec 2017 (HK\$118.8 billion at 31 Dec 2016)

@ Including placements by the Future Fund of HK\$224.5 billion



INVESTMENT RETURN OF THE EXCHANGE FUND (1994-2017)¹



1 Investment return calculation excludes the holdings in the Strategic Portfolio.

2 The return includes the performance of LTGP up to the end of September 2017. The audited full year return will be disclosed in the annual report of 2017 to be released later this year.

3 Composite CPI is calculated based on the 2014/2015-based series.



INVESTMENT DIVERSIFICATION

- Began to invest in alternative assets in 2009 under the Long-Term Growth Portfolio (LTGP). The progress of the LTGP in 2017 has been good. Positions at the end of September 2017 and performance since inception are as follows:

As of end-September 2017 (unaudited)

Asset Classes	Market Value HK\$ billion	Annualised IRR (Since inception from 2009 till end-Sep 2017)
Private Equity	141.1	} 13.5 %
Real Estate	73.4	
Total	214.5	

Note: Outstanding investment commitments at the end of 2017 amounted to HK\$162.7 billion



OUTLOOK FOR 2018

- As asset valuations in many financial markets have surpassed their historical highs, the sustainability of the upward momentum will hinge crucially on whether some of the markets' current optimistic expectations will materialise
- At present, it seems that the markets may have under-priced some risk factors, including
 - Will the pace of US interest rate normalisation need to quicken if inflationary pressure is greater than expected?
 - Will the US government's trade policy and protectionism have adverse effects on global trade and economy?
 - Will geopolitical tensions flare up?
- Will continue to manage the Exchange Fund prudently, remain agile and nimble, monitor market developments closely, deploy some defensive measures as and when appropriate, and continue to expand our investments under the LTGP



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