



HONG KONG MONETARY AUTHORITY

2018 Exchange Fund Results

29 January 2019



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 2018

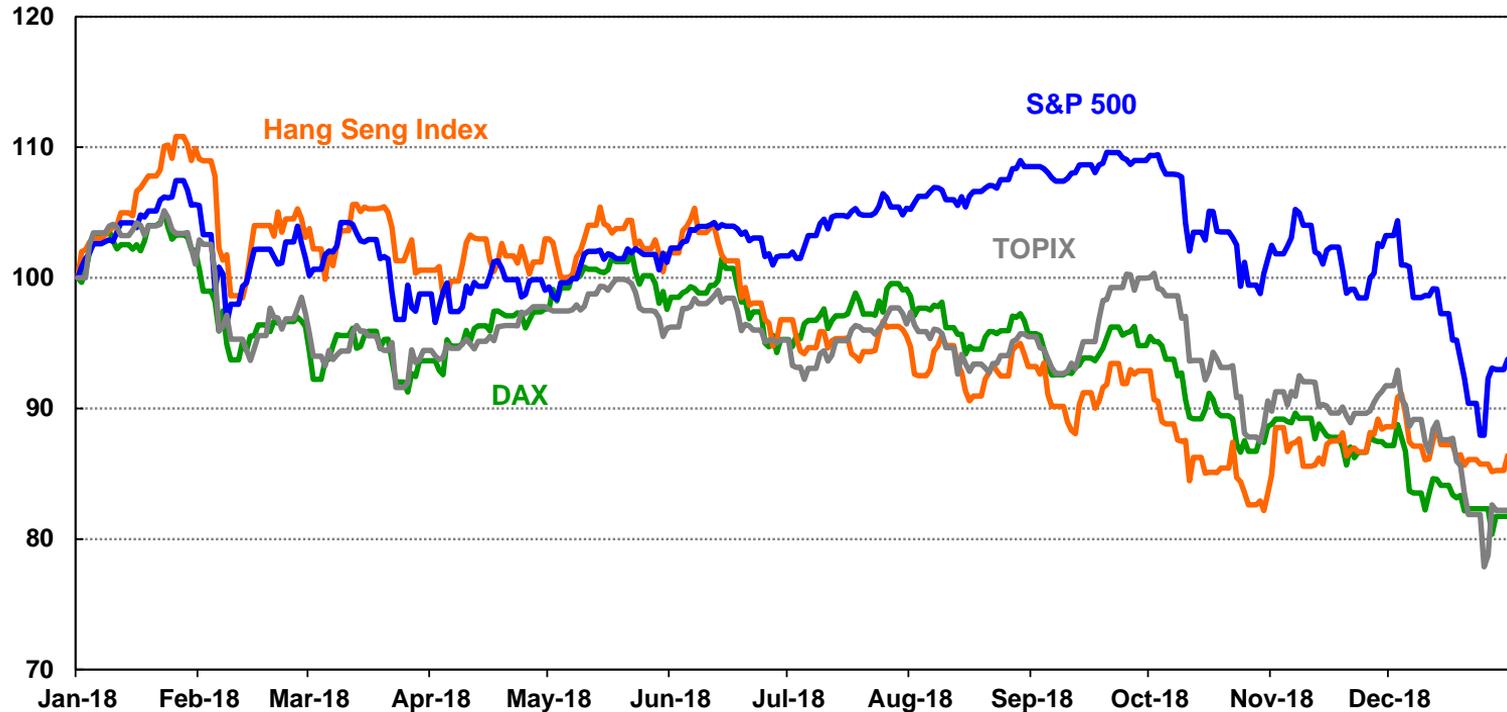
Yield (%)





EQUITY MARKETS IN 2018

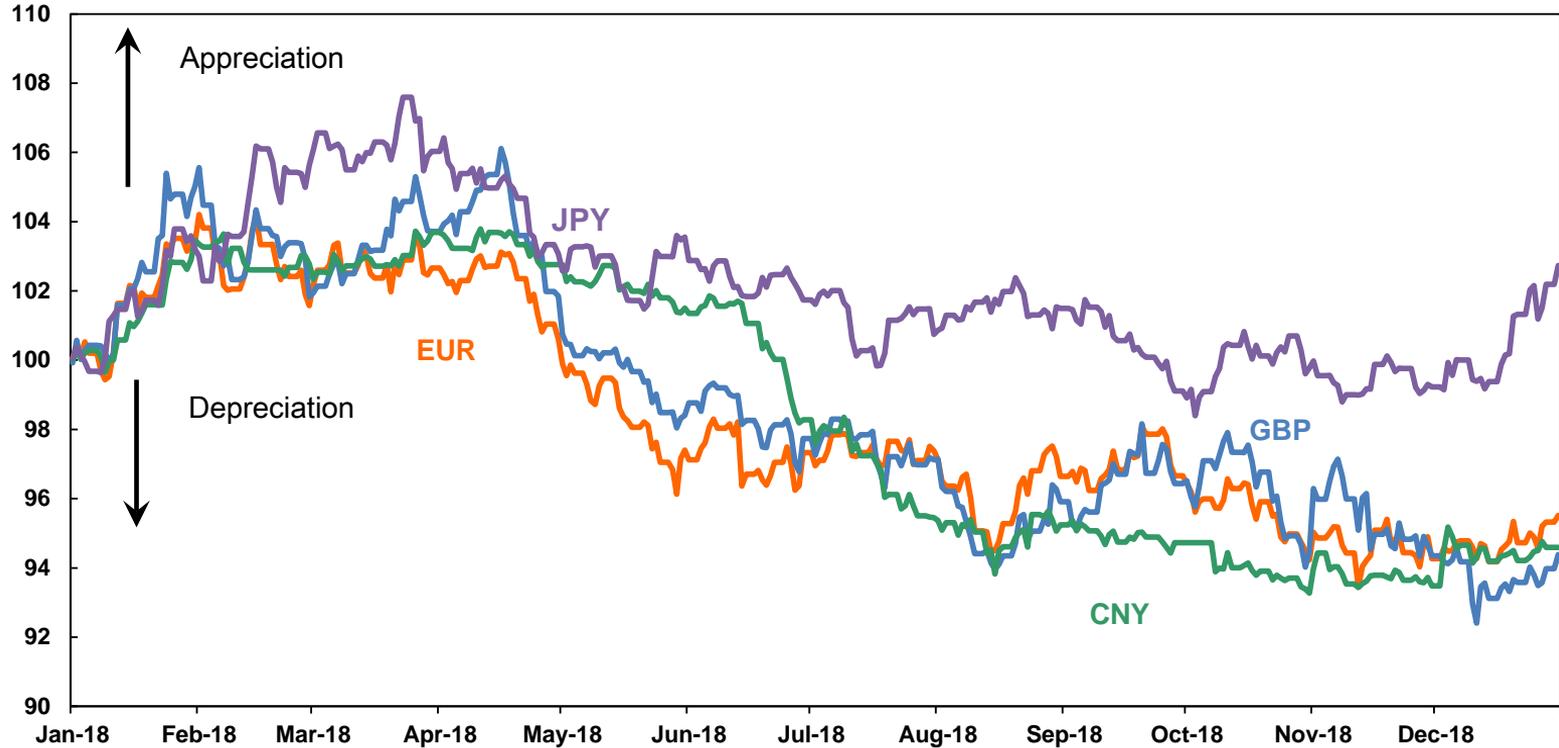
Normalized Index Level (2017 year-end = 100)





CURRENCY MARKETS IN 2018

Normalized FX Level Against USD (2017 year-end = 100)





MAJOR ASSET CLASS PERFORMANCE IN 2018

| Asset Class | Index | Change in 2018 |
|-------------|--------------------------------------|----------------|
| Equities | MSCI World Index (Developed Markets) | -10.4% |
| | MSCI Emerging Markets Index | -16.6% |
| Bonds | Barclays Global Aggregate Index | -1.2% |
| Commodities | Bloomberg Commodity Index | -11.2% |



INVESTMENT INCOME

←———— 2018 —————→

(unaudited)

| (HK\$ billion) | Full year | 2H | 1H | Full year | Full year |
|---------------------------------|-------------|---------------|-------------|--------------|-------------|
| Bonds | 57.4 | 37.9 | 19.5 | 34.4 | 33.1 |
| Hong Kong equities* | (20.7) | (17.3) | (3.4) | 58.3 | 5.3 |
| Other equities | (38.3) | (35.6) | (2.7) | 80.4 | 28.6 |
| Foreign exchange# | (9.0) | (14.0) | 5.0 | 53.5 | (15.8) |
| Other investments@ | <u>24.5</u> | <u>7.9</u> | <u>16.6</u> | <u>37.4</u> | <u>16.9</u> |
| Investment income/(loss) | 13.9 | (21.1) | 35.0 | 264.0 | 68.1 |

* 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. This figure represents valuation changes up to the end of September 2018. Valuations of these investments from October to December are not yet available.



INCOME AND EXPENDITURE

| | ← 2018 → | | | 2017 | 2016 |
|---|---------------|---------------|--------------|--------------|--------------|
| | (unaudited) | | | | |
| (HK\$ billion) | Full year | 2H | 1H | Full year | Full year |
| Investment income/(loss) | 13.9 | (21.1) | 35.0 | 264.0 | 68.1 |
| Other income | 0.2 | 0.1 | 0.1 | 0.2 | 0.2 |
| Interest and other expenses | <u>(18.1)</u> | <u>(10.8)</u> | <u>(7.3)</u> | <u>(9.9)</u> | <u>(6.4)</u> |
| Net (loss)/income | (4.0) | (31.8) | 27.8 | 254.3 | 61.9 |
| Fee payment to Fiscal Reserves** | (43.8) | (21.6) | (22.2) | (46.2) | (33.1) |
| Fee payment to HKSAR government funds and statutory bodies* | (13.8) | (6.9) | (6.9) | (8.6) | (9.6) |

* The rate of fee payment is 4.6% for 2018, 2.8% for 2017 and 3.3% for 2016.

This does not include the 2018 fee payment to the Future Fund because such amount will only be disclosed when the composite rate for 2018 is available.

(The composite rate was 9.6% for 2017 and 4.5% for 2016. Fee payable to the Future Fund was HK\$22.7 billion for 2017 and HK\$10.1 billion for 2016).



EXCHANGE FUND ABRIDGED BALANCE SHEET

(HK\$ billion)

At 31 Dec 2018

At 31 Dec 2017

Change

ASSETS

(unaudited)

| | | | |
|---------------------|-----------------------|-----------------------|--------------------|
| Deposits | 326.0 | 346.9 | (20.9) |
| Debt securities | 2,826.2 | 2,761.6 | 64.6 |
| Hong Kong equities* | 175.5 | 204.2 | (28.7) |
| Other equities | 456.9 | 507.5 | (50.6) |
| Other assets# | <u>274.8</u> | <u>195.1</u> | <u>79.7</u> |
| Total assets | <u>4,059.4</u> | <u>4,015.3</u> | <u>44.1</u> |

LIABILITIES AND EQUITY

| | | | |
|---|-----------------------|-----------------------|-----------------------|
| Certificates of Indebtedness | 485.7 | 456.7 | 29.0 |
| Government-issued currency notes & coins in circulation | 12.6 | 12.2 | 0.4 |
| Balance of the banking system | 78.6 | 179.8 | (101.2) |
| Exchange Fund Bills and Notes issued | 1,129.6 | 1,045.8 | 83.8 |
| Placements by banks and other financial institutions | 56.3 | 59.4 | (3.1) |
| Placements by Fiscal Reserves® | 1,173.5 | 1,073.8 | 99.7 |
| Placements by HKSAR government funds and statutory bodies | 320.6 | 305.1 | 15.5 |
| Placements by subsidiaries | 7.7 | - | 7.7 |
| Other liabilities | <u>194.8</u> | <u>169.4</u> | <u>25.4</u> |
| Total liabilities | <u>3,459.4</u> | <u>3,302.2</u> | <u>157.2</u> |
| Accumulated Surplus | 599.4 | 713.1 | (113.7) |
| Revaluation reserve | <u>0.6</u> | - | <u>0.6</u> |
| Total equity | <u>600.0</u> | <u>713.1</u> | <u>(113.1)</u> |
| Total liabilities and equity | <u>4,059.4</u> | <u>4,015.3</u> | <u>44.1</u> |

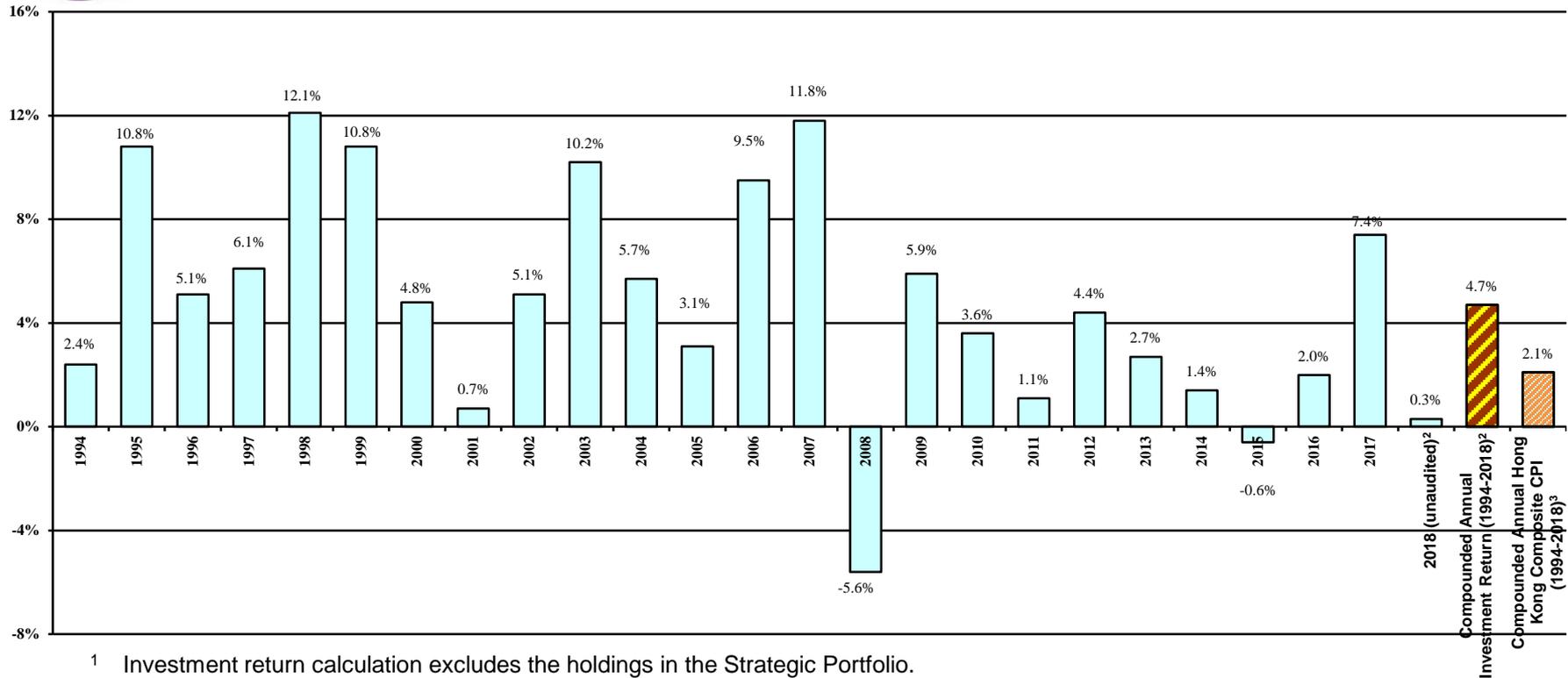
* Including shares of the Hong Kong Exchanges and Clearing Limited in the Strategic Portfolio.

Including fund injection to Exchange Fund's investment holding subsidiaries at a carrying amount of HK\$162.4 billion at 31 Dec 2018 (HK\$135.2 billion at 31 Dec 2017).

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



INVESTMENT RETURN OF THE EXCHANGE FUND (1994-2018)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 2018. The audited full year return will be disclosed in the annual report of 2018 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 2018 has been good. Positions at the end of September 2018 and performance since inception are as follows:

As of end-September 2018 (unaudited)

| Asset Classes | Market Value HK\$ billion | Annualised IRR (Since inception from 2009 till end-Sep 2018) |
|----------------|------------------------------|--|
| Private Equity | 190.9 | } 13.8% |
| Real Estate | 87.4 | |
| Total | 278.3 | |

Note: Outstanding investment commitments at the end of 2018 amounted to HK\$200.0 billion



OUTLOOK FOR 2019

- Investment environment in 2019 will remain challenging
- A number of uncertainties may lead to market volatilities:
 - US-China trade tension
 - Progress of Brexit
 - Direction of monetary policy of the US Federal Reserve
 - Geopolitical risks
- Will continue to manage the Exchange Fund prudently, monitor market developments closely, enhance our defensive measures as and when appropriate, and further diversify our investments



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