

Developments in the Banking Sector

by Banking Supervision Department

HIGHLIGHTS OF KEY TRENDS

Banking sector performance

The aggregate pre-tax operating profit of retail banks decreased by 5.2% in the first quarter of 2019 compared with the same period last year. An increase in net interest income (+9.7%) was offset by declines in fee and commission income (-12.1%) and income from foreign exchange and derivatives operations (-31.2%) (Exhibit 1).

Retail banks' net interest margin widened to 1.58% in the first quarter of 2019 from 1.52% in the same period of 2018 (Exhibit 2), thanks to higher levels of interest rates.

Total loans of the banking sector recorded a moderate growth of 2.3% in the first quarter of 2019 (Exhibit 5). Among the total, loans for use in Hong Kong grew by 1.8%, loans for use outside Hong Kong rose by 2.7%, and trade finance increased by 6.8%. As total loans grew faster than total deposits in the first quarter, the loan-to-deposit ratio of the banking sector edged up to 73.4% at end-March 2019 from 72.6% in the previous quarter (Exhibit 6).

The banking sector's Mainland-related lending showed an increase of 3.9% in the first quarter to HK\$4,415 billion (17% of total assets), from HK\$4,249 billion (16.1% of total assets) in the previous quarter (Exhibit 9).

The loan quality of the banking sector remained healthy with the classified loan ratio slightly edging up to 0.56% at end-March 2019 from 0.55% in the previous quarter (Exhibit 10). Similarly, the classified loan ratio of retail banks increased slightly to 0.52% from 0.51% over the same period (Exhibit 11).

The classified loan ratio of the banking sector's Mainland-related lending also increased to 0.63% at end-March 2019 from 0.55% in the previous quarter (Exhibit 10). The classified loan ratio of retail banks' Mainland-related lending increased to 0.75% from 0.64% during the same period (Exhibit 11).

The key performance indicators of the banking sector are provided in the Appendix.

Profitability

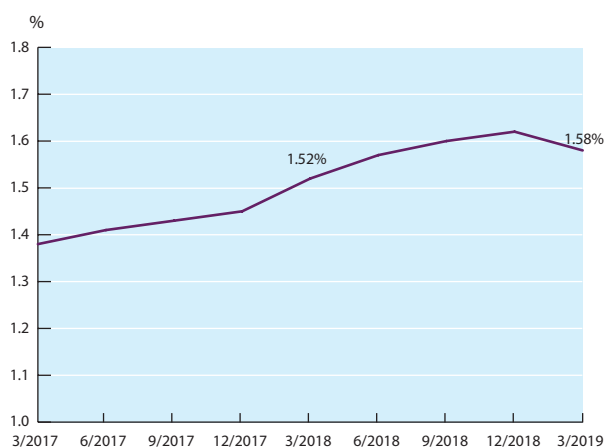
EXHIBIT 1

Pre-tax operating profit of retail banks' Hong Kong offices

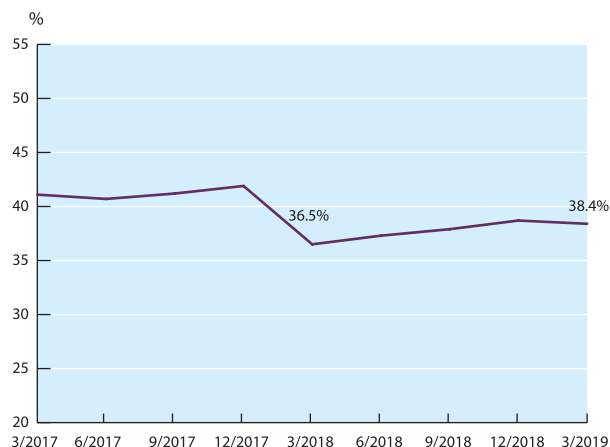
Key items	Change of pre-tax operating profit Q1 2018 vs Q1 2019	
	Percentage change	Contribution to the percentage change in pre-tax operating profit (ppt)
Fee and commission income	-12.1%	-4.8
Income from foreign exchange and derivatives operations	-31.2%	-4.3
Total operating expenses	+6.3%	-3.6
Net interest income	+9.7%	+9.3
Pre-tax operating profit	-5.2%	

EXHIBIT 2

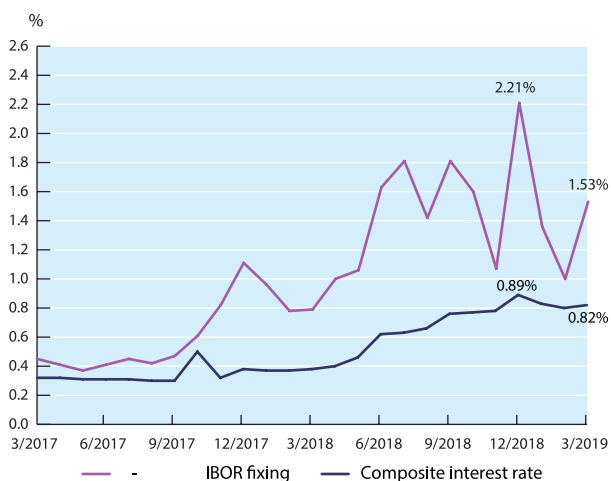
Net interest margin (year-to-date annualised) of retail banks widened in the first quarter of 2019 compared with the same period last year

**EXHIBIT 4**

Cost-to-income ratio (year-to-date) of retail banks edged up in the first quarter of 2019 compared with the same period last year

**EXHIBIT 3**

Hong Kong-dollar interbank interest rates remained volatile; the composite interest rate hovered around 0.8% during 2019

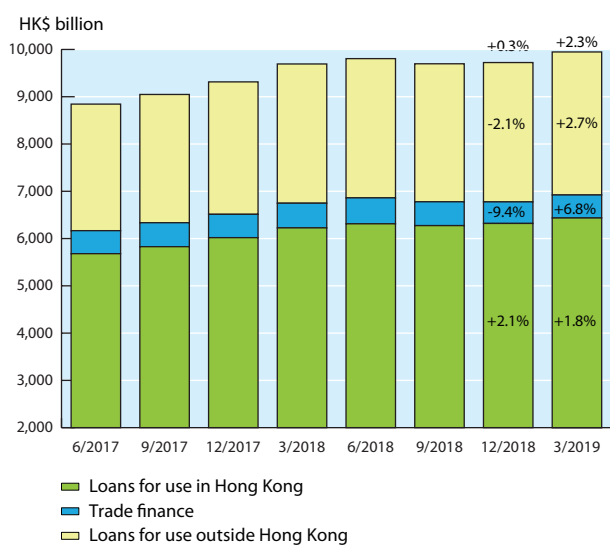


Notes:

1. HIBOR fixing (monthly average) refers to the Hong Kong Interbank Offered Rates released by the Hong Kong Association of Banks.
2. Composite interest rate is a weighted average interest rate of all Hong Kong-dollar interest-bearing liabilities of retail banks.

Loans and deposits**EXHIBIT 5**

Loan growth was broad-based in the first quarter of 2019



Notes:

1. "Loans for use outside Hong Kong" include "others" (i.e. unallocated).
2. Percentage denotes quarter-on-quarter growth rate.

Within loans for use in Hong Kong, the percentage changes in the amount of credit extended to the key economic sectors in the first quarter of 2019 were:

Key items	Change in loans for use in Hong Kong in the first quarter of 2019	
	Percentage change	Contribution to the percentage change in loans for use in Hong Kong (ppt)
Loans to private individuals (excluding credit card advances and residential mortgage loans)	+7.1%	+0.6
Property lending	+1.3%	+0.6
Financial companies excluding stockbrokers (mainly investment companies)	+3.5%	+0.5
Loans for use in Hong Kong	+1.8%	

EXHIBIT 6

Total loans grew faster than total deposits in the first quarter of 2019

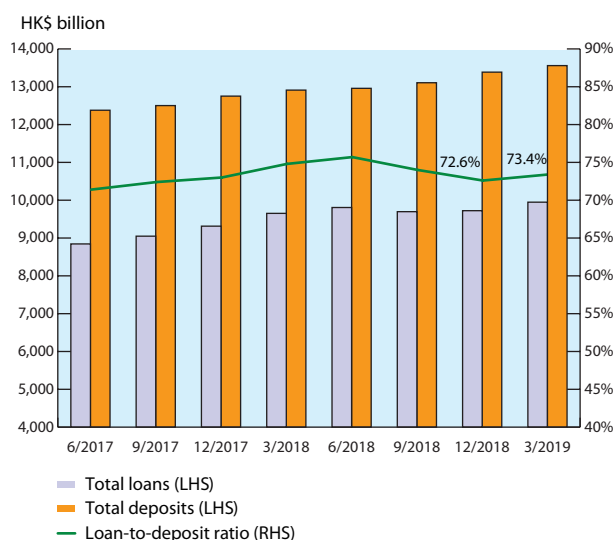
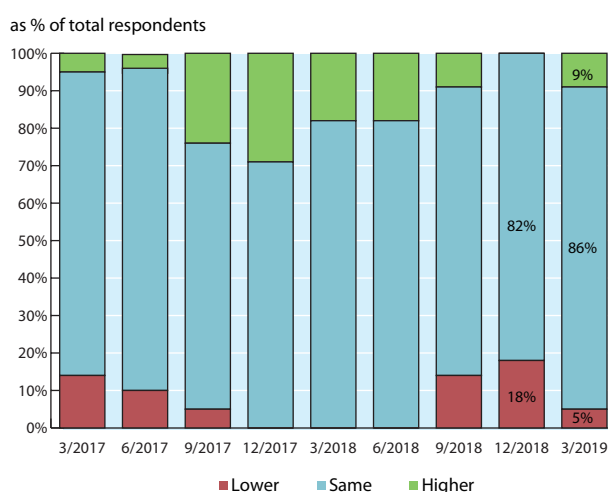


EXHIBIT 8

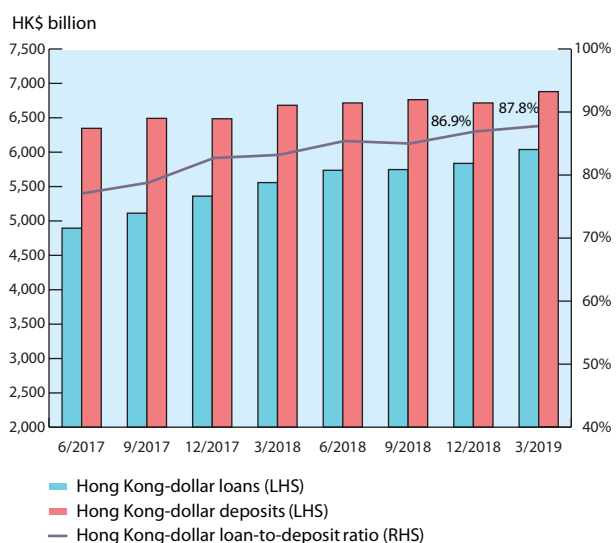
Most of the respondents to the HKMA Opinion Survey on Credit Conditions Outlook expected loan demand to stay at the same level in the next three months



Note: Expectation of loan demand to change in the next 3 months relative to the past 3 months

EXHIBIT 7

Hong Kong-dollar loans rose at a faster pace than Hong Kong-dollar deposits in the first quarter of 2019



Mainland-related lending

EXHIBIT 9

Mainland-related lending

	Dec 2018 HK\$bn	Mar 2019 HK\$bn
Mainland-related loans excluding trade finance	3,985	4,103
Trade finance	264	312
Total	4,249	4,415

Loan quality

EXHIBIT 10

Quality of loans and advances of the banking sector*

	Mar 2018	Jun 2018	Sep 2018	Dec 2018	Mar 2019
	<i>% of total loans</i>				
Special mention loans	1.28	1.31	1.31	1.32	1.28
Classified loans (gross)	0.65	0.61	0.60	0.55	0.56
of which:					
Substandard	0.21	0.20	0.23	0.20	0.16
Doubtful	0.38	0.34	0.31	0.29	0.31
Loss	0.06	0.07	0.07	0.06	0.09
Classified loans (net of specific provisions)	0.34	0.32	0.32	0.26	0.28
Overdue > 3 months and rescheduled loans	0.48	0.40	0.38	0.36	0.41
of which:					
Overdue > 3 months	0.42	0.36	0.34	0.33	0.38
Rescheduled loans	0.05	0.04	0.04	0.03	0.03
	<i>% of Mainland-related lending</i>				
Classified loans (gross) of Mainland-related lending**	0.60	0.62	0.64	0.55	0.63

Note: Figures may not add up to total due to rounding.

* Unless stated otherwise, figures covered all AIs' Hong Kong offices, as well as locally incorporated AIs' overseas branches and major overseas subsidiaries.

** Figures covered all AIs' Hong Kong offices, as well as locally incorporated AIs' Mainland branches and subsidiaries.

EXHIBIT 11

Quality of loans and advances of retail banks*

	Mar 2018	Jun 2018	Sep 2018	Dec 2018	Mar 2019
	<i>% of total loans</i>				
Special mention loans	1.09	1.06	1.09	1.21	1.20
Classified loans (gross)	0.55	0.53	0.54	0.51	0.52
of which:					
Substandard	0.19	0.18	0.20	0.19	0.18
Doubtful	0.33	0.31	0.31	0.29	0.31
Loss	0.03	0.04	0.04	0.03	0.03
Classified loans (net of specific provisions)	0.35	0.33	0.34	0.30	0.32
Overdue > 3 months and rescheduled loans	0.39	0.31	0.35	0.32	0.33
of which:					
Overdue > 3 months	0.32	0.26	0.29	0.28	0.30
Rescheduled loans	0.07	0.06	0.05	0.04	0.04
	<i>% of Mainland-related lending</i>				
Classified loans (gross) of Mainland-related lending**	0.68	0.70	0.74	0.64	0.75

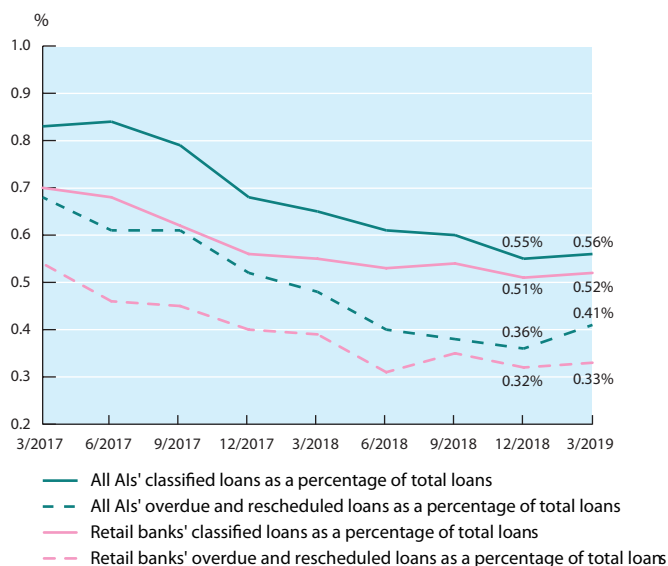
Note: Figures may not add up to total due to rounding.

* Unless stated otherwise, figures covered retail banks' Hong Kong offices, as well as locally incorporated retail banks' overseas branches and major overseas subsidiaries.

** Figures covered retail banks' Hong Kong offices, as well as locally incorporated retail banks' Mainland branches and subsidiaries.

EXHIBIT 12

Classified loan ratios and overdue and rescheduled loan ratios remained at low levels



Note: Figures covered Hong Kong offices, overseas branches and major overseas subsidiaries.

EXHIBIT 13

Delinquency ratios of residential mortgages and credit card lending remained low

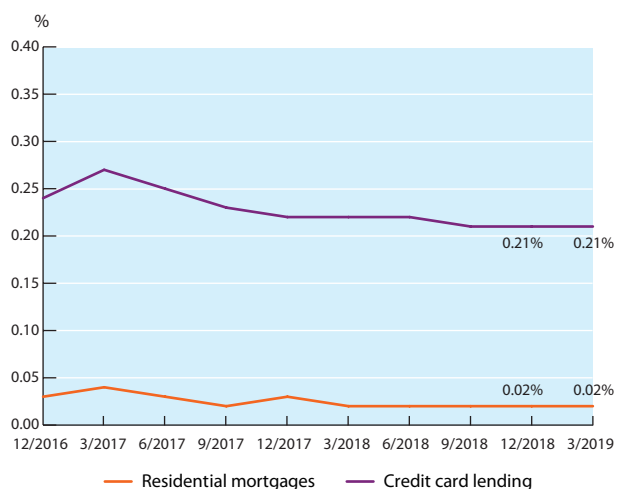
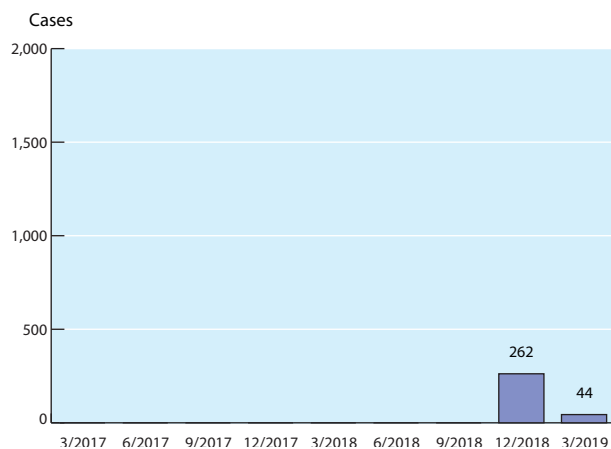


EXHIBIT 14

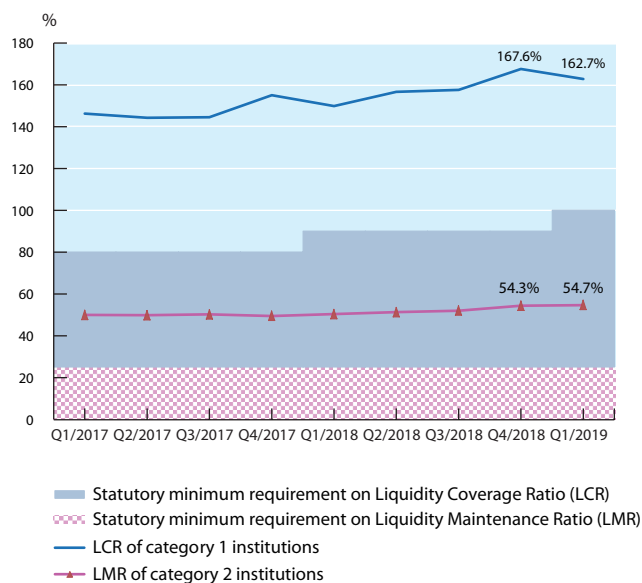
The number of negative equity cases dropped to 44 in the first quarter of 2019



Liquidity conditions

EXHIBIT 15

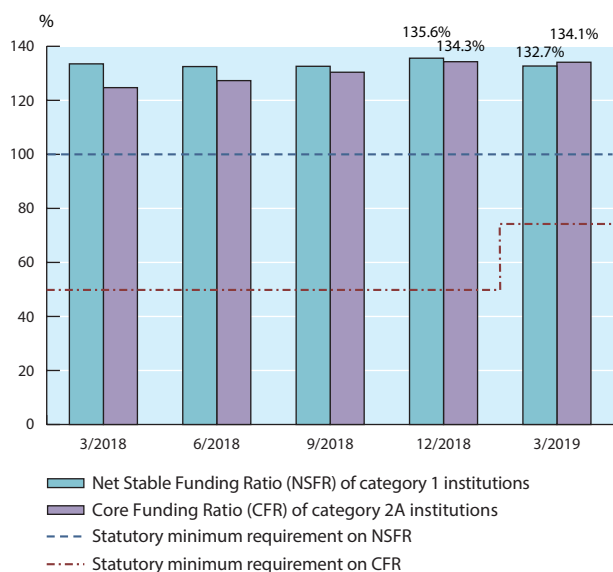
Liquidity positions of AIs remained sound



Note: For a category 1 institution, the statutory minimum requirement of the LCR applicable for 2019 is 100%. A category 2 institution must maintain an LMR of not less than 25% on average in each calendar month.

EXHIBIT 16

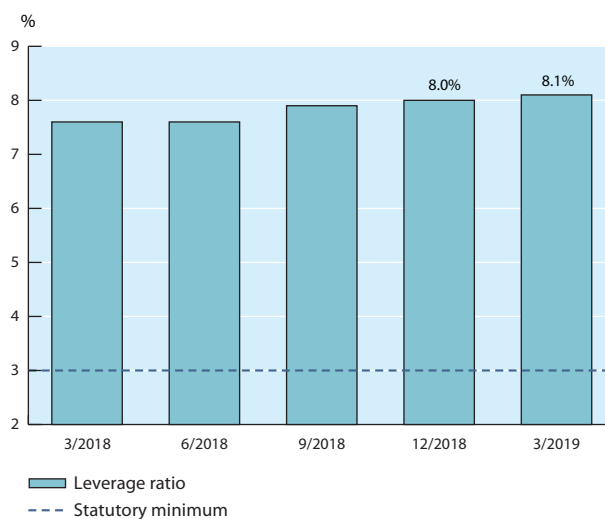
Funding positions of AIs remained stable



Note: For a category 1 institution, the statutory minimum requirement of the NSFR is 100%. A category 2A institution must maintain a CFR of not less than 50% on average in each calendar month during 2018. The minimum CFR rose to 75% starting from 1 January 2019.

EXHIBIT 18

Leverage ratio remained at a healthy level

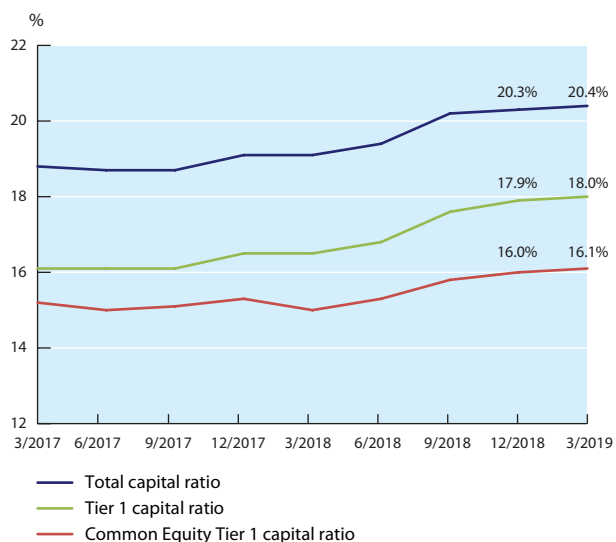


Note: Leverage ratio is defined as the ratio of Tier 1 capital to an exposure measure, where the exposure measure includes both on-balance sheet and off-balance sheet exposures. All locally incorporated AIs are required to maintain leverage ratios of not less than 3%.

Capital adequacy

EXHIBIT 17

Capital positions of locally incorporated AIs continued to be strong



APPENDIX

KEY PERFORMANCE INDICATORS OF THE BANKING SECTOR¹ (%)

	Mar 2018	Dec 2018	Mar 2019
Interest rates			
1-month HIBOR fixing ² (quarterly average)	0.84	1.63	1.29
3-month HIBOR fixing (quarterly average)	1.16	2.16	1.74
BLR ³ and 1-month HIBOR fixing spread (quarterly average)	4.16	3.50	3.83
BLR and 3-month HIBOR fixing spread (quarterly average)	3.84	2.97	3.38
Composite interest rate ⁴	0.38	0.89	0.82
	All AIs		
Balance sheet developments⁵			
Total deposits	1.2	2.1	1.3
Hong Kong dollar	3.0	-0.7	2.4
Foreign currency	-0.6	5.2	0.1
Total loans	3.6	0.3	2.3
Domestic lending ⁶	3.6	1.3	2.2
Loans for use outside Hong Kong ⁷	3.7	-2.1	2.7
Negotiable instruments			
Negotiable certificates of deposit (NCDs) issued	-5.6	-6.2	-4.1
Negotiable debt instruments held (excluding NCDs)	5.9	4.2	3.9
Asset quality			
As a percentage of total loans ⁸			
Pass loans	98.07	98.13	98.17
Special mention loans	1.28	1.32	1.28
Classified loans ⁹ (gross)	0.65	0.55	0.56
Classified loans (net) ¹⁰	0.34	0.26	0.28
Overdue > 3 months and rescheduled loans	0.48	0.36	0.41
Classified loan ratio (gross) of Mainland related lending ¹¹	0.60	0.55	0.63
Liquidity ratios (consolidated)			
Liquidity Coverage Ratio — applicable to category 1 institutions (quarterly average)	149.8	167.6	162.7
Liquidity Maintenance Ratio — applicable to category 2 institutions (quarterly average)	50.3	54.3	54.7
Net Stable Funding Ratio — applicable to category 1 institutions	133.5	135.6	132.7
Core Funding Ratio — applicable to category 2A institutions	124.7	134.3	134.1
	Retail banks		
Profitability			
Loan impairment charges as a percentage of average total assets (year-to-date annualised)	-0.01	0.05	0.04
Net interest margin (year-to-date annualised)	1.52	1.62	1.58
Cost-to-income ratio (year-to-date)	36.5	38.7	38.4
	Surveyed institutions		
Asset quality			
Delinquency ratio of residential mortgage loans	0.02	0.02	0.02
Credit card lending			
Delinquency ratio	0.22	0.21	0.21
Charge-off ratio — quarterly annualised	1.64	1.53	1.52
— year-to-date annualised	1.64	1.51	1.52
	All locally incorporated AIs		
Capital adequacy (consolidated)			
Common Equity Tier 1 capital ratio	15.0	16.0	16.1
Tier 1 capital ratio	16.5	17.9	18.0
Total capital ratio	19.1	20.3	20.4
Leverage ratio	7.6	8.0	8.1

Notes:

1. Figures are related to Hong Kong offices only except where otherwise stated.
2. The Hong Kong Interbank Offered Rates are released by the Hong Kong Association of Banks.
3. With reference to the rate quoted by The Hongkong and Shanghai Banking Corporation Limited.
4. The composite interest rate is a weighted average interest rate of all Hong Kong-dollar interest-bearing liabilities, which include deposits from customers, amounts due to banks, negotiable certificates of deposit and other debt instruments, and Hong Kong-dollar non-interest-bearing demand deposits on the books of banks. Further details can be found on the HKMA website.
5. Quarterly change.
6. Loans for use in Hong Kong plus trade finance.
7. Including "others" (i.e. unallocated).
8. Figures are related to all AIs' Hong Kong offices, as well as locally incorporated AIs' overseas branches and major overseas subsidiaries.
9. Classified loans are those loans graded as "substandard", "doubtful" or "loss".
10. Net of specific provisions/individual impairment allowances.
11. Figures are related to all AIs' Hong Kong offices, as well as locally incorporated AIs' Mainland branches and subsidiaries.