Transcript of Analyst Briefing for
2019 Annual Results

Question and Answer Session

Gurpreet Singh Sahi from Goldman Sachs: What is the impact of Covid 19 on your asset quality? So far this year, has there been any change in your asset quality? In particular, have you seen that any client experienced repayment difficulties? What counter strategies do you have to deal with it?

Chief Executive Gao Yingxin: Since the outbreak of the coronavirus, SME customers, especially those in food & beverage, and tourism, have experienced large impact. They have encountered difficulties in many operating aspects, which are however temporary in our view. In this regard, BOCHK have taken initiative to launch relief measures, such as principal moratorium, to alleviate their problems and help them to weather this difficult time. In addition, SME loans including those vulnerable sectors, account for a small proportion of our loan portfolio. Overall speaking, our asset quality has remained stable, and we have not seen large number of corporates experiencing repayment issue.

Chief Risk Officer Zhuo Chengwen: We have been closely monitoring those vulnerable sectors and clients, and maintaining communication with them in order to understand their operating status and repayment capability. We have established necessary pre-warning system and watchlists, and undertook risk mitigation measures. At the same time, we will base on the latest economic forecasts to update our ECL model and to maintain a sufficient level of impairment allowances.

Gary Lam from HSBC: Your risk-weighted assets (RWA) growth in 2019 outpaced the asset growth, what were the reasons? Given the epidemic impact this year, growth in net interest margin and earnings should moderate slightly, will BOCHK maintain its dividend payout level? In terms of Southeast Asian business, what was its size as a percentage of BOCHK Group with respect to loans or assets? Affected by the epidemic, what is your view on the risk profile and growth outlook of the Asia Pacific region?

Chief Financial Officer Sui Yang: In 2019, BOCHK's RWA increased by 6.5%, mainly driven by a 6% growth of credit risk weighted assets. Overall speaking the growth in our RWA remains manageable. In terms of capital, both our Tier 1 and CET 1 capital ratios were maintained at a relatively good position while continuing to improve. Adhering to our long-standing capital management principle, we will invest precious capital resources to support our organic growth. Since the rate cuts by Federal Reserve has exceeded expectation and brought US dollar rates to close to zero levels in March, our net interest margin will be negatively affected. In response, we will continue to enhance our asset-liability management. While maintaining an appropriate liquidity position, we will strive to promote customers loan growth as a way to increase the proportion of high-yielding assets in our balance sheet. Meanwhile we will also control deposit cost. These efforts should help us to reduce margin pressure. As to dividend payout, we will keep our guidance range between 40% and 60% unchanged, and do not have plans to change our policy.

Chief Executive Gao Yingxin: Our dividend payout ratio guidance is ranged between 40% and 60%, and the actual payout ratio was about 50% for 2019. Even in the existing environment, we still have the capacity to maintain the level of our dividend payout. With regard to Southeast Asian business, our regional entities accounted for less than 5% of our customer loans or assets, which implies substantial room for future growth. In 2019 our Southeast Asian entities achieved growth in various aspects doubling the pace of BOCHK's. Observing the growth in the recent two years, and the future potential, we believe that we will be able to sustain a favourable growth in Southeast Asian market. In addition, BOCHK plays both the roles of the Asia Pacific syndication loan center and offshore flagship arm of the credit business for Bank of China. We will continue to support the offshore development of large-sized Chinese corporations, and large sized cross-border M&A deals, as part of our growth strategy.

Winnie Wu from Bank of America: In the face of potential global economic recession, will BOCHK take into account the "Black Swan" event of coronavirus outbreak and make substantial increase in provision charges upon updating its ECL model? Will such update be made in the first quarter of 2020? Also, since the relatively high HIBOR level in the recent period might not be sustainable, and the Federal Reserve have substantially cut interest rates, what is your perspective on the margin outlook for this year, and if the Federal Reserve do not increase interest rate in the next one to two years, will your net interest margin fall to the levels as low as those in 2015 and 2016? What is your counter-strategy?

Chief Risk Officer Zhuo Chengwen: In the second half of 2019, we took prudent steps to update our ECL model parameters, mainly related to GDP growth, unemployment rate, residential property prices, and others, in line with the macroeconomic and external environment. In 2019, we added about HK$400 million in impairment allowances due to the macro-parameter update in the model. Many countries recently adopted stringent prevention measures, which are expected to impact economic growth, logistics, employment and corporate revenue. We will base on the latest economic forecasts to update our model parameters. In the near term, we expect moderately higher pressure on our provision charges and credit cost. Part of the adjustments will be reflected in the first quarter of this year. Nonetheless, it is a necessary step in boosting our capability to withstand unforeseen incidents such as the epidemic. In the future, we will continue to dynamically update our model based on our judgement in accordance with the macro and market conditions.

Chief Financial Officer Sui Yang: In March, the Federal Reserve reduced the target level of Fed Fund rate to 0-0.25%. Our house view is that the U.S is not likely to adopt negative interest rate based on the current conditions. We expect the Fed Fund rate will remain at 0-0.25% for the next 12 months. In Hong Kong dollar market, the inversion of HKD-USD interest spread was quite apparent in the recent period, mainly due to the volatility in HK dollar interest rate affected by such factors as liquidity conditions, IPO, corporate dividend payment, and seasonality. In the short term, HIBOR should be maintained at a level above LIBOR. Over long term, the Hong Kong dollar interest rate should fall with US dollar's. In RMB market, it is expected that PBOC will sustain an accommodative monetary policy, and RMB interest rate should be relatively stable. Overall speaking, it is inevitable to see interest rates moving lower which definitely poses greater challenges to banks. In response to that, we will continue to effectively deploy our funds in high yielding assets, while continuing to drive deposit growth and control deposit cost. To promote CASA growth, we will continue to optimise our payroll and cash pooling services. These efforts will be helpful for us to alleviate the negative impact from interest rate cuts.

Jemmy Huang from JP Morgan: In the second half of 2019, it seems to me that the NPL ratios rose in Hong Kong, Mainland and Southeast Asia. Did you see distinctive changes in the asset quality in Hong Kong or Mainland corporate clients? In addition, with the recent launch of a virtual bank in the market, do you see any impact on customer transactions or deposit behaviours? With livi coming online soon, is its strategy different from other virtual banks?

Chief Risk Officer Zhuo Chengwen: As of end of 2019, BOCHK's NPL ratio edged up from the end of the previous year, mainly due to the internal credit rating downgrade of a Mainland corporate and a few Southeast Asian corporates. Currently we do not see any systemic risk, and continue to be confident in our asset quality. As to our Non-Bank-Mainland-Exposure (NBME), the NPL ratio of the on-balance sheet loan exposure was 0.21%, which was similar to the Group's overall level. The quality of our Mainland corporate client base is good as it is mainly composed of leading players in their own industry. Despite the NPL ratio of our Southeast Asian entities was higher than the Group's average, they were still better than the markets' averages based on their local regulatory standard. There was no systemic or structural risk as their non-performing loans came from different industries. In the face of new situation now, we will closely monitor the operating conditions of those industries which are hardest hit by the epidemic, such as tourism, leisure and entertainment, and we will adopt proper risk control measures.

Chief Operating Officer Zhong Xiangqun: Currently all virtual banks are proactively making preparation. Their strategic focuses are different both in product and customer development. As to livi, its early products will be simple, secure and convenient banking services, which involve deeply in the daily life scenarios of customers and will gradually expand in the future. At the moment, virtual bank's impact on banks is still not apparent. Moreover traditional banks are stepping up in digitalisation and strengthening fintech applications. Taking ourselves as an example, we witnessed rapid development in our e-banking and mobile banking businesses, while the number of young customers has also increased strongly.

Tian Yafei from Citigroup: Recently many US corporates faced liquidity pressure, and drew loans from banks. Did you see the same phenomena so that it drove stronger loan growth? What is your loan growth target for this year? Given the substantial volatility in the financial markets around the world, and drawing parallel to the global financial crisis in 2008, during which time banks suffered losses on their equity or debt securities investments, do you see BOCHK's investments to be affected by the external environment?

Deputy Chief Executive Wang Bing: Since the start of this year, the global financial markets saw big fluctuations due to the epidemic. Notwithstanding that, we have not felt liquidity pressure, and our asset business has been normal. In 2019, the China-US trade friction and the local social events brought certain challenges to the banking sector. In spite of these factors, BOCHK was able to achieve 10.2% growth in loans with market share further up by 0.33 percentage point. Of which, our growths in loans for use outside Hong Kong, and loans for use in Hong Kong both outpaced the market. The loan growth of our Southeast Asian entities ran at a pace more than doubled the group's average. These achievements were attributable to our solid customer base, a diversified business presence, and comprehensive service capabilities.

The coronavirus outbreak will definitely make this year tougher than the last. Globally many countries and central banks have actively launched new initiatives in fiscal and monetary policies, to inject liquidity into the market, restore confidence and support economic growth. After the gradual easing of the epidemic, we believe the combination of policies and measures will produce greater effect. We will balance among risk, income, demand and capital, and dynamically capture loan growth opportunities. We are confident in meeting our mid-to-high single digit loan growth target for the full year.

In Hong Kong market, our customer base is solid and has an appropriate structure. We are capable of capturing customer needs and expanding business. In cross-border market, the implementation of various national strategic initiatives will present many opportunities, and our focus will be on Guangdong, Hong Kong and Macao, Beijing-Tianjin-Hebei, and Yangtze River Delta regions. In particular new infrastructure projects is a key investment theme for the market this year, and major areas such as 5G, artificial intelligence, big data, ultra-high-voltage projects, intra-city railway, etc. are all part of our focus. Therefore, we are confident in achieving good growth in cross-border loans. In Southeast Asian market, we fully leveraged the capability of the Hong Kong's headquarters and successfully realised synergy with our Southeast Asian entities through deepening regional business strategy over the past two years. Capitalising on our comparative advantages and capabilities, we will capture the business opportunities in Belt and Road related projects, industrial transfer projects, as well as those associated with local leading family groups, and large-sized state-owned enterprises. We will further leverage our role as the Asia Pacific Syndication Loan Centre of the BOC, and enhance our capabilities in structural and project financing services. We will seize the business opportunities in the M&A and privatisation projects to grow our assets in the international markets. In conclusion, we are confident in achieving a solid loan growth for this year.

Chief Executive Gao Yingxin: Due to the tightening of liquidity in the US dollar market, we believe that certain corporates who relied on debt financing before might turn to banks for financing. We also saw increasing demand for working capital funding in both US dollars and other foreign currencies. With the new easing measures launched by the Federal Reserve starting to effect, liquidity condition should gradually improve. BOCHK has solid positions in capital and liquidity, and a diversified client base. We can satisfy the demand of our key customers while keeping risk under control and ensuring a reasonable level of returns.

Chief Risk Officer Zhuo Chengwen: As of end of 2019, the balance of our debt securities portfolio exceeded HK$860 billion. In mid-March, bond prices generally dropped due to increased liquidity premium and widened credit spreads, but they did recover to some extent in recent days. Our debt securities portfolio offers high quality, with about 90% in grade A3 or above. By issuers, 60% are issued by governmental or supranational entities, and therefore pricing fluctuations are smaller. By currencies, above 50% are in US dollar, which provides strong liquidity. For these debt securities, above 90% is accounted for as investment securities at amortised cost or at fair value through other comprehensive income. Since our investment objective is to provide stable income, short-term price movements therefore will not cause material impact on our financials. At the same time, we also keep tracking of the issuers' credit condition, and intend to hold their debt securities to maturity if their credit status remain relatively stable. Overall speaking we will continue to monitor market conditions and step up risk management measures.

Deputy Chief Executive Yuan Shu: Our investment strategy follows BOCHK's overall principle of solid operations. Within our debt securities portfolio, the majority of them are government bonds, and only a small portion are corporate and financial institution bonds which are mainly issued by large banks, large insurers or large corporations. Although the prices of corporate and financial institution bonds declined in recent days, the rapid decrease of interest rates also benefited the valuation of government bonds. From this perspective our debt securities portfolios remain a solid investment.