

**Supplementary information in relation to the meeting of the
Legislative Council Panel on Financial Affairs
held on 29 May 2017**

**Agenda Item III –
Briefing on the work of Hong Kong Monetary Authority**

The Hong Kong Monetary Authority (HKMA) sets out below supplementary information as requested by the Legislative Council Panel on Financial Affairs —

- (a) To provide information (including the amount and the proportion to the total amount of loans) on Mainland-related loans made in Hong Kong, particularly those using assets in the Mainland as collateral, and HKMA’s assessment of the potential risks of such loans to Hong Kong’s financial stability**

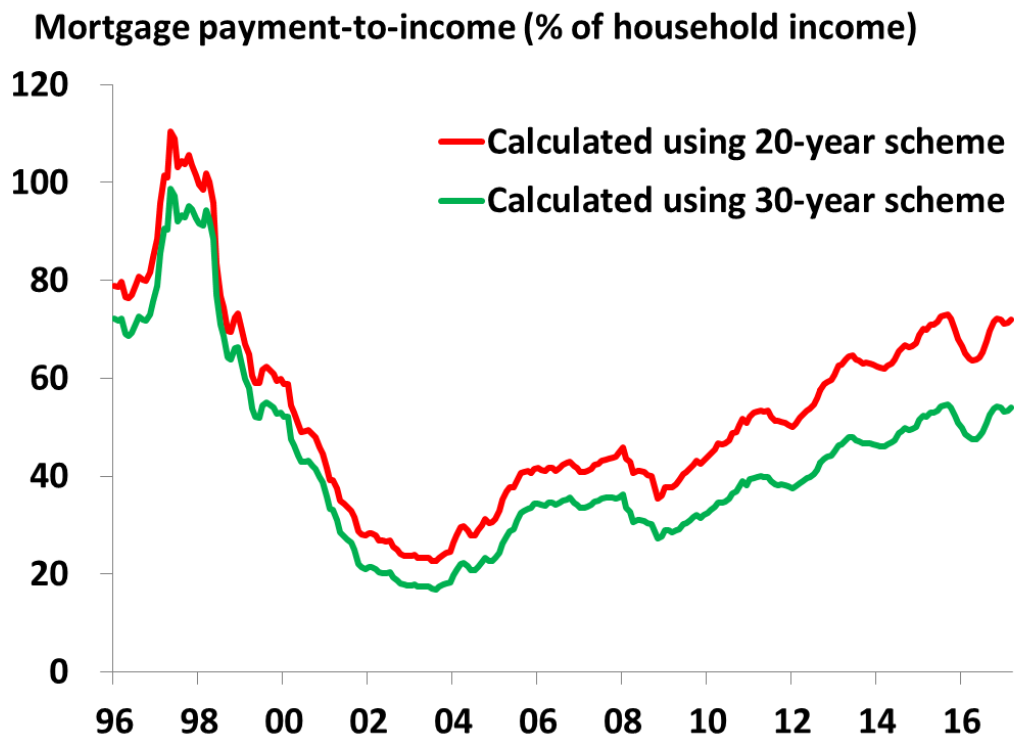
Total Mainland-related loans (“MRL”) of the Hong Kong banking sector was HK\$3,804 billion at the end of the first quarter of 2017, representing 39.7% of total loans of the Hong Kong banking sector. The asset quality of the MRL portfolio remained at a healthy level, with its classified loan ratio standing at 0.79% at end-March 2017, well below the long-run historical average of classified loan ratio of 2.1% for total loans in Hong Kong since 2000.

According to the statistics collected by the HKMA, close to 80% of the MRL was extended to large state-owned enterprises, or multinational firms and Hong Kong enterprises for developing their Mainland businesses. The remaining MRL (of around 20%) was extended to private enterprises on the Mainland, of which 63% was covered by tangible collateral or bank guarantees while 17% was covered by other forms of guarantee. The relevant credit risks are considered manageable. We do not collect data on the subcategory of loans using assets on the Mainland as collateral.

The HKMA has all along put great emphasis on supervising banks' Mainland-related lending business to ensure that their credit risk management systems can effectively control the relevant risks. Supervisory efforts include stepping up on-site and off-site reviews, and strengthening communication with the banking industry. These help ensure that banks maintain prudent credit underwriting standards and risk management. The HKMA also increases the frequency of collecting granular data from banks, with a view to identifying emerging risks and conducting in-depth analysis. Stress tests are also conducted regularly to assess banks' resilience under extreme scenarios.

- (b) To refine the information on the housing affordability of the public (i.e. slide 19 of the powerpoint presentation), taking into account the fact that the mainstream mortgage terms have changed from 20 years in 1997 to 30 years in 2016

We calculate the mortgage payment-to-income ratio in order to track the influence of main factors such as housing price and interest rate development on housing affordability in general. As such, we fix the loan period to 20 years so as to maintain the consistency of the ratio and facilitate the comparison of housing affordability in different periods. If a fixed 30-year mortgage term is used, the mortgage payment-to-income ratio would be lower than that based on a 20-year scheme, but the broad trend would be similar (see the chart below). The ratio based on a 30-year scheme also rose to high levels in the first quarter of 2017, reflecting further deterioration of housing affordability.



Sources: Rating and Valuation Department, Census and Statistics Department and HKMA.

(c) To provide information on changes in (i) the Aggregate Balance of Hong Kong dollar (HKD); and (ii) the Monetary Base of HKD since 2016, and HKMA's assessment of the impacts of such changes to the stability of HKD

The changes in the HKD Monetary Base and Aggregate Balance since 2016 are summarised at **Table 1** below. During this period, the HKD Monetary Base increased moderately, with the increase in the outstanding Exchange Fund Bills and Notes (EFBNs) largely offsetting the decline in the Aggregate Balance. The increase in EFBNs mainly took place between January and September 2016 (see **Chart 1**), during which the HKMA issued a total of HK\$132.0 billion worth of additional Exchange Fund Bills (EFBs) to meet the strong demand by banks for such bills for liquidity management purpose. To settle the issuance of such additional EFBs, the HKMA debits the HKD settlement accounts of the purchasing banks.¹ Thus, there was a corresponding decline in the Aggregate Balance.

It is worth highlighting that under the Linked Exchange Rate System, all monetary operations (including the issuance of additional EFBs as mentioned above) are conducted strictly in accordance with Currency Board principles. Specifically, the entire Monetary Base is fully backed by foreign exchange reserves. It is envisaged that the changes in the relative weights of the components of the Monetary Base would not have any impact on the stability of HKD.

¹ This is the settlement arrangement of issuances of EFBNs.

Table 1: Changes in the Monetary Base and Aggregate Balance since 2016

(HK\$ billion)

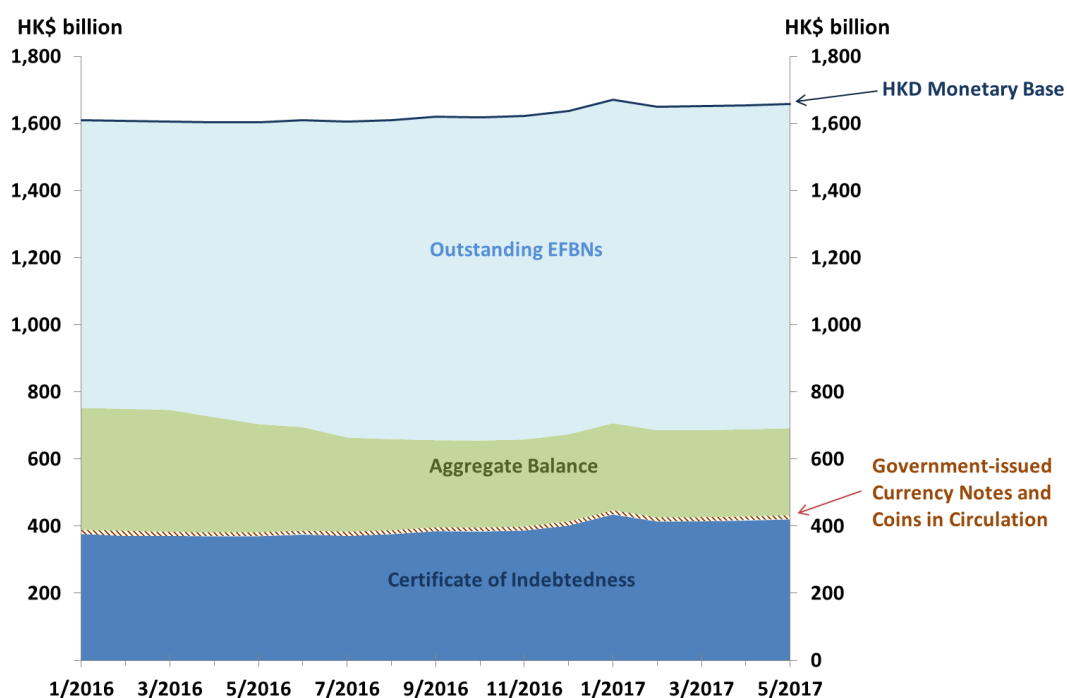
	31 Dec 2015	31 May 2017	Changes since 2016
Monetary Base	1,592.8	1,657.9	+65.1
Of which:			
• Certificates of Indebtedness ^{note 1}	360.2	420.1	+59.9
• Government-issued Currency Notes and Coins in Circulation	11.7	12.3	+0.6
• Aggregate Balance ^{note 2}	391.3	259.5	-131.8
• Outstanding EFBNs	829.6	966.1	+136.5

The figures may not add up due to rounding.

Note 1: These are certificates issued by the Financial Secretary under the Exchange Fund Ordinance, and held by note-issuing banks as cover for the banknotes they issue.

Note 2: The Aggregate Balance refers to the sum of the balances in the clearing accounts maintained by banks with the HKMA for settling interbank payments and payments between banks and the HKMA.

Chart 1: Changes in the components of HKD Monetary Base since 2016



(d) To provide information on the Exchange Fund's investment, if any, in renminbi-denominated bonds issued by the Central Government

The Exchange Fund has been pursuing investment diversification and has begun investing in RMB assets in recent years. For RMB bonds, the investments are primarily made in quality debt instruments including RMB-denominated bonds issued by the Central Government. The HKMA cannot disclose the details of investments.