

**Press Release****Exchange Fund 2002 results announced**

The Hong Kong Monetary Authority (HKMA) announced today (Thursday) the operating results\* of the Exchange Fund for the year 2002.

The Exchange Fund recorded an investment income of HK\$47 billion in 2002. The main components of this income were (Annex 1):

- income and valuation gains of HK\$54.3 billion from bonds and other investments;
- a valuation loss of HK\$11.8 billion on the Hong Kong equities portfolio (net of dividends);
- a valuation loss of HK\$22.8 billion on other equities (net of dividends); and
- an exchange valuation gain of HK\$27.3 billion, mainly as a result of the appreciation of the euro against the US dollar.

Commenting on the operating results for the year, Mr Joseph Yam, Chief Executive of the HKMA, said that the slowdown in global economic recovery in the latter half of 2002 had been positive for bonds but negative for equities. The Exchange Fund had benefited from overweighting bonds and underweighting equities. The strength of the euro had also contributed to the investment performance.

Although direct comparisons are not always easy or appropriate, generally speaking, the Exchange Fund achieved an investment return that was favourable in comparison to that of other similar funds in the private sector (Annex 2). In 2002, the Exchange Fund achieved an investment return of 5.1%, which is 120 basis points above the return of its strategic investment benchmark. Since the adoption of the current strategic investment benchmark four years ago, the Exchange Fund has achieved a compounded 5.3% annual return, or an annual out-performance of 190 basis points above the benchmark's compounded 3.4% annual return for the

same period. Since 1994, the Exchange Fund has generated an average annual return of 6.4%, compared with the average annual inflation rate of 1.7% over the same period (Chart 1).

The Abridged Balance Sheet (Annex 3) shows that in 2002 the total assets of the Exchange Fund decreased by HK\$24 billion, from HK\$979.1 billion at the end of December 2001 to HK\$955.1 billion at the end of December 2002. While net drawdowns of the fiscal reserves, amounting to HK\$78.9 billion, were the main reason for the decrease in total assets in 2002, this decrease was partly compensated for by net investment income of HK\$40.4 billion (Annex 4). The Fiscal Reserves' share of this net investment income for the year amounted to HK\$15.7 billion. The balance of HK\$24.7 billion has been added to the Exchange Fund's Accumulated Surplus for 2002.

Commenting on the prospects for 2003, Mr Yam said that the investment climate was even more murky than in 2002. Further gains from the bond markets were likely to be limited, since interest rates were at historic lows. Uncertainties surrounding the strength of the US economy were complicated by geopolitical factors and by the despondent mood of investors bruised by three consecutive years of negative equity returns. Until the outlook became clearer, the markets were expected to be volatile.

An accompanying Statement of Valuation of the Hong Kong Equity Portfolio is published (Annex 5), showing that the market value of the equity investments of the Portfolio at the end of December 2002 amounted to HK\$50.9 billion. These holdings, representing what remains after the completion of the disposal programme for the stocks originally purchased in August 1998, have become part of the Exchange Fund's investment portfolio.

## Attachments

Annex 1: Exchange Fund Performance

Annex 2: Supplementary Figures

Annex 3: Exchange Fund – Abridged Balance Sheet as at 31 December 2002

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\* Unaudited figures for 2002

Annex 4: Exchange Fund – Change in Accumulated Surplus

Annex 5: Statement of Valuation of the Hong Kong Equity Portfolio

Chart 1: History of Investment Return of Exchange Fund (1994 to 2002)

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Hong Kong Monetary Authority

16 January 2003

**Exchange Fund Performance****(Expressed in billions of Hong Kong dollars)**

	2002	2001
Gain/(Loss) on Hong Kong equities *	(11.8)	(27.1)
Gain/(Loss) on other equities *	(22.8)	(3.3)
Exchange gain/(loss)	27.3	(13.0)
Total return from bonds, etc	<u>54.3</u>	<u>50.8</u>
Investment income	47.0	7.4

\* Including dividends

## Supplementary Figures

**Table 1: Major Components of the Investment Income  
(2001 to 2002)**

	Full year 2002 (HK\$ bn)	1H 2002 (HK\$ bn)	Full year 2001 (HK\$ bn)
Investment Income	+47.0	+22.8	+7.4
Loss on Hong Kong equities	-11.8	-4.6	-27.1
Gain/Loss on other equities	-22.8	-10.9	-3.3
Exchange gain(+)/loss(-)	+27.3	+17.4	-13.0
Total return from bonds etc.	+54.3	+20.9	+50.8

**Table 2: Market Performance  
(2001 to 2002)**

	Full Year 2002	1H 2002	Full Year 2001
S&P 500 *	-23.4%	-13.8%	-13.0%
Hang Seng Index *	-18.2%	-7.0%	-24.5%
Merrill Lynch World Govt Bond Index 1-10 years	+18.6%	+9.9%	-0.8%
Euro vs USD	+17.9%	+10.9%	-5.6%
Yen vs USD	+10.4%	+9.4%	-13.1%

\* Market performance on equities is based on index price change during the year.

**Table 3: Investment Performance of the Exchange Fund and Comparable Balanced Funds**

	Percentage of Global Equity in benchmark	Performance in 2000	Performance in 2001	Performance in 2002
Fund A	20%	+2.3%	-0.9%	(unaudited) +0.5%
Fund B	25%	+0.6%	-0.1%	+4.7%
Fund C	30%	-2.0%	-4.7%	+4.1%
Fund D	30%	-3.7%	-4.4%	+0.7%
Fund E	30%	-6.2%	-6.1%	+6.2%
Fund F	30%	-3.2%	-1.7%	-0.5%
Fund G	30%	-2.6%	-4.5%	+4.7%
Fund H	30%	n.a. <sup>(Note 1)</sup>	-8.9%	+4.8%
<b>Exchange Fund</b>	<b>20%</b>	<b>+4.8%</b>	<b>+0.7%</b>	<b>+5.1%</b>

Source: Watson Wyatt and S&P

Note 1: The date of inception fell within 2000. The fund is newly included in the Comparable Balanced Funds for comparison.

**Exchange Fund Abridged Balance Sheet**

(Expressed in billions of Hong Kong dollars)

	As At 31 December 2002	As At 31 December 2001	Change
<b>ASSETS</b>			
Deposits	51.2	99.2	(48.0)
Debt securities	764.5	732.7	31.8
Hong Kong equities	50.9	85.9	(35.0)
Other equities	63.2	35.3	27.9
Other assets	25.3	26.0	(0.7)
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<b>Total assets</b>	<b>955.1</b>	<b>979.1</b>	<b>(24.0)</b>
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<b>LIABILITIES AND ACCUMULATED SURPLUS</b>			
Certificates of Indebtedness	118.5	107.5	11.0
Government-issued currency notes and coins in circulation	5.9	5.7	0.2
Balance of banking system	0.5	0.7	(0.2)
Exchange Fund Bills and Notes	122.9	118.1	4.8
Placements by other Hong Kong Special Administrative Region government funds	301.7	380.6	(78.9)
Other liabilities	78.3	63.9	14.4
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<b>Total liabilities</b>	<b>627.8</b>	<b>676.5</b>	<b>(48.7)</b>
<b>Accumulated surplus</b>	<b>327.3</b>	<b>302.6</b>	<b>24.7</b>
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<b>Total liabilities and accumulated surplus</b>	<b>955.1</b>	<b>979.1</b>	<b>(24.0)</b>

**Exchange Fund**  
**Change in Accumulated Surplus**

(Expressed in billions of Hong Kong dollars)

	I ←	2002				→ I	
	Full year	Q1	Q2	Q3	Q4	Full year	2001
Investment income/(loss)	47.0	(3.7)	26.5	(2.1)	26.3	7.4	
Other income	0.2	0.0	0.1	0.0	0.1	0.2	
Interest and expenses	<u>(6.8)</u>	<u>(1.6)</u>	<u>(1.7)</u>	<u>(1.7)</u>	<u>(1.8)</u>	<u>(10.5)</u>	
Net investment income/(loss)	40.4	(5.3)	24.9	(3.8)	24.6	(2.9)	
Treasury's share	<u>(15.7)</u>	<u>1.6</u>	<u>(9.7)</u>	<u>0.8</u>	<u>(8.4)</u>	<u>(1.6)</u>	
Increase/(Decrease) in EF accumulated surplus	24.7	(3.7)	15.2	(3.0)	16.2	(4.5)	



**Statement of Valuation of the Hong Kong Equity Portfolio**

HONG KONG SPECIAL ADMINISTRATIVE REGION GOVERNMENT  
EXCHANGE FUND  
HONG KONG EQUITY PORTFOLIO  
STATEMENT OF VALUATION  
AS AT 31 DECEMBER 2002

A. EQUITY VALUATION

The market value of the equity investments of the Portfolio was HK\$50,891 million as at 31 December 2002 (HK\$85,864 million as at 31 December 2001)

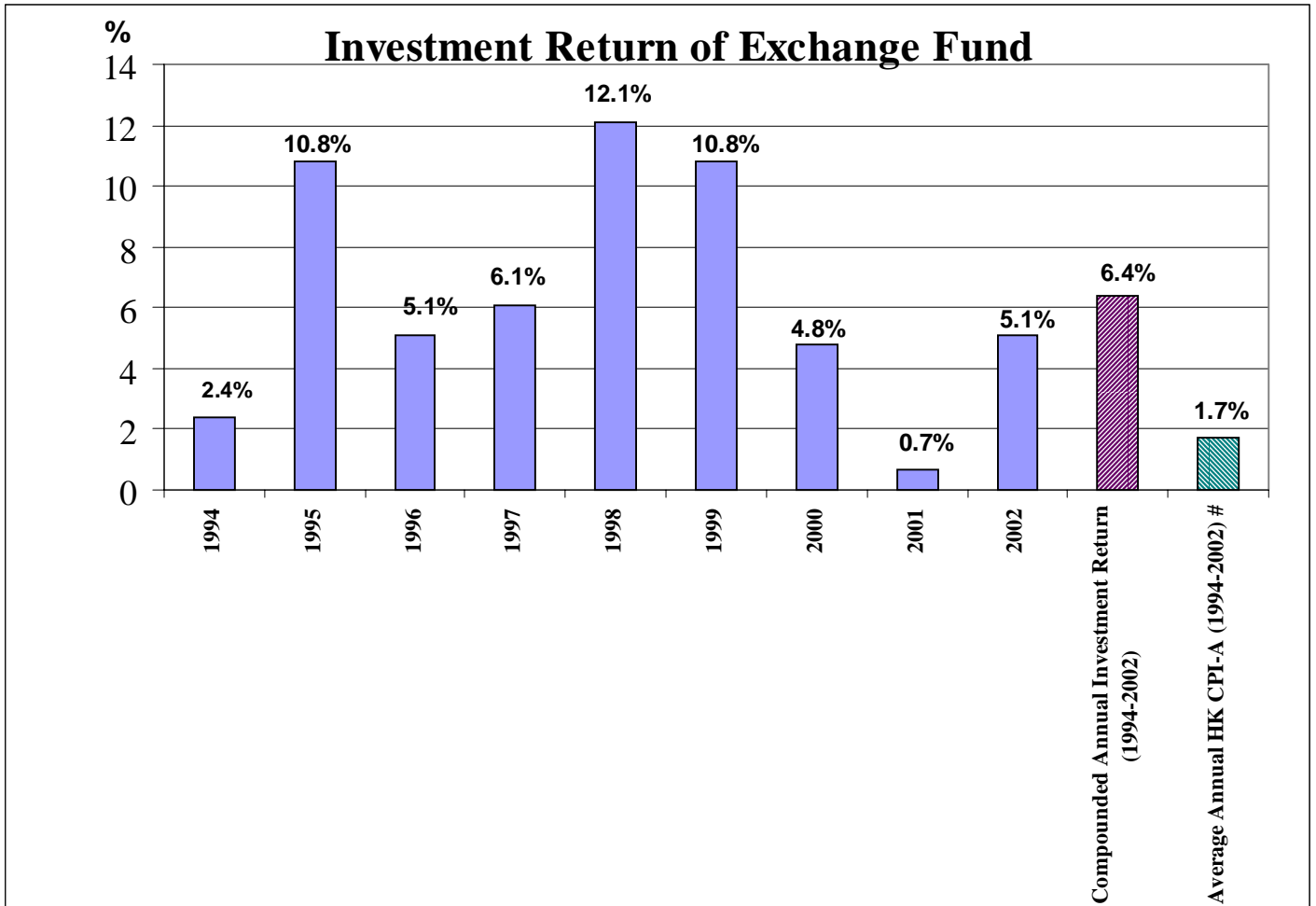
B. EQUITY DISPOSAL (1 January – 31 December 2002)

During the period, a portion of the Portfolio's shares were sold, under the terms of the Tap Facility for the Tracker Fund of Hong Kong for a gross consideration of HK\$21,977 million.

C. SHAREHOLDINGS EQUAL TO OR IN EXCESS OF 10%

As at 31 December 2002, the Portfolio had no shareholdings in any companies equal to or in excess of 10% of their issued share capital.

**Chart 1: History of Investment Return of Exchange Fund  
(1994 to 2002)**



# HK CPI-A as of end-November 2002