

Exchange Fund Position at end-December 2018

The following is issued on behalf of the Hong Kong Monetary Authority:

The Hong Kong Monetary Authority (HKMA) today (January 29) published the unaudited financial position of the Exchange Fund at end-December 2018.

The Exchange Fund recorded an investment income of HK\$13.9 billion in 2018. The main components were:

- gains on bonds of HK\$57.4 billion;
- losses on Hong Kong equities of HK\$20.7 billion;
- losses on other equities of HK\$38.3 billion;
- negative currency translation effect of HK\$9.0 billion on non-Hong Kong dollar assets (Note 1); and
- gains on other investments of HK\$24.5 billion (Note 2).

Fees on placements by the Fiscal Reserves and placements by HKSAR government funds and statutory bodies were HK\$43.8 billion (Note 3) and HK\$13.8 billion respectively in 2018 (the rate of fee payment is 4.6 per cent for 2018). After deducting all expenses and fees, the Accumulated Surplus of the Exchange Fund recorded a decrease of HK\$113.7 billion (Annexes 1 and 2).

The Abridged Balance Sheet shows that the total assets of the Exchange Fund increased by HK\$44.1 billion, from HK\$4,015.3 billion at the end of 2017 to HK\$4,059.4 billion at the end of 2018. The increase was mainly attributable to increased placements by the Fiscal Reserves.

The Exchange Fund recorded an investment return of 0.3 per cent in 2018 (Note 4). Specifically, the Investment Portfolio recorded a negative rate of return of 2.4 per cent, while the Backing Portfolio gained 2.1 per cent. The Long-Term Growth Portfolio (LTGP) recorded an annualised internal rate of return of about 13.8 per cent since its inception in 2009 up to the end of September 2018.

Commenting on the performance of the Exchange Fund in 2018, the Chief Executive of the HKMA, Mr Norman Chan, said, "Looking back, several risk factors (including the pace of interest rate normalisation in the US, the negative impact of the US government's foreign trade policy and protectionism on global trade, and geopolitical risks), which had been under-priced by the markets, materialised one after another during the year, and there were considerable volatilities and adjustments in global financial markets. Despite a combination of falling equity prices, rising bond yields and a strong US dollar, the Exchange Fund managed to record a positive investment income of HK\$13.9 billion in 2018, instead of a loss."

Looking ahead, Mr Chan said, "It is very likely that the investment environment in 2019 will remain as unpredictable and difficult as in 2018. First, the global economy and financial markets will continue to be affected by the US-China trade tension. There are no winners in a trade war. The deteriorating market sentiment and slowing investment activities last year reflected to a large extent the market concerns on such a situation. Furthermore, the macroeconomic environment and financial markets in Europe will be badly hit in case of a 'hard' Brexit. Last but not least, the future direction of the US economic and monetary policies is unclear. Recently, there have been increasing market concerns about the US economy beginning to slow down. Emerging market economies including Mainland China are also facing increasing downside risks. All these risk factors will bring about greater uncertainties and potential risks to the global macroeconomic environment and asset markets.

The HKMA will continue to manage the Exchange Fund prudently. We will monitor market developments closely and enhance our defensive measures as and when appropriate. We will also continue to diversify our investments so as to further strengthen the Exchange Fund's resilience against market volatilities."

Note 1: This is primarily the effect of translating foreign currency assets into Hong Kong dollar after deducting the portion for currency hedging.

Note 2: This is the valuation change of investments held by investment holding subsidiaries of the Exchange Fund. This figure represents valuation changes up to the end of September 2018. Valuations of these investments from October to December are not yet available.

Note 3: 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.

Note 4: This return excludes the performance of the Strategic Portfolio and only includes the performance of LTGP up to the end of September 2018. The audited full year return will be disclosed in the 2018 annual report to be released later this year.