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## INDUSTRY OVERVIEW

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### REPORT CONDUCTED BY IPSOS HONG KONG LTD.

We commissioned Ipsos Hong Kong Ltd. to conduct an analysis of, and to report on, pawn loan market and mortgage loan market in Hong Kong for the period from 2007 to 2016. The information and analysis contained in the Ipsos Report was assessed independently by Ipsos Hong Kong Ltd. and Ipsos Hong Kong Ltd., including all its subsidiaries, divisions and units, is not connected to our Group in any way. Ipsos Hong Kong Ltd. charged us a total fee of approximately HK\$219,000 for the preparation and the use of the Ipsos Report, which our Directors consider to reflect market rates.

Ipsos Hong Kong Ltd., being one of the worldwide offices of the Ipsos Group, is specialised in conducting researches across all industrial sectors including tourism, financial services, cosmetics, regional luxury and high net worth research.

The following assumptions are used in the Ipsos Report:

- The economy is assumed to maintain a steady growth across the forecast period
- The demand for mortgage loan in Hong Kong is assumed to rise and more industry players entering the market
- It is assumed that there is no external shock such as financial crisis or the wide outbreak of diseases to affect the demand and supply of pawn and mortgage loan services in Hong Kong during the forecast period

The following parameters are considered in the marketing sizing and forecast model of the Ipsos Report:

- GDP and inflation growth rate in Hong Kong
- Sales of residential and non-residential properties from 2007 to 2012
- New residential and non-residential building completion from 2007 to 2012
- Government credit policies
- Lending rate in Hong Kong
- Growth in the number of foreign domestic helpers in Hong Kong
- Growth in the number of Mainland Chinese entering Hong Kong for residence
- Number of licensed money lenders

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### OVERVIEW OF HONG KONG MACRO ECONOMIC ENVIRONMENT AND FINANCIAL INDICATIONS

#### GDP and GDP Growth Rate in Hong Kong

Demand for money borrowing exists during both the times of economic downturn and boom.

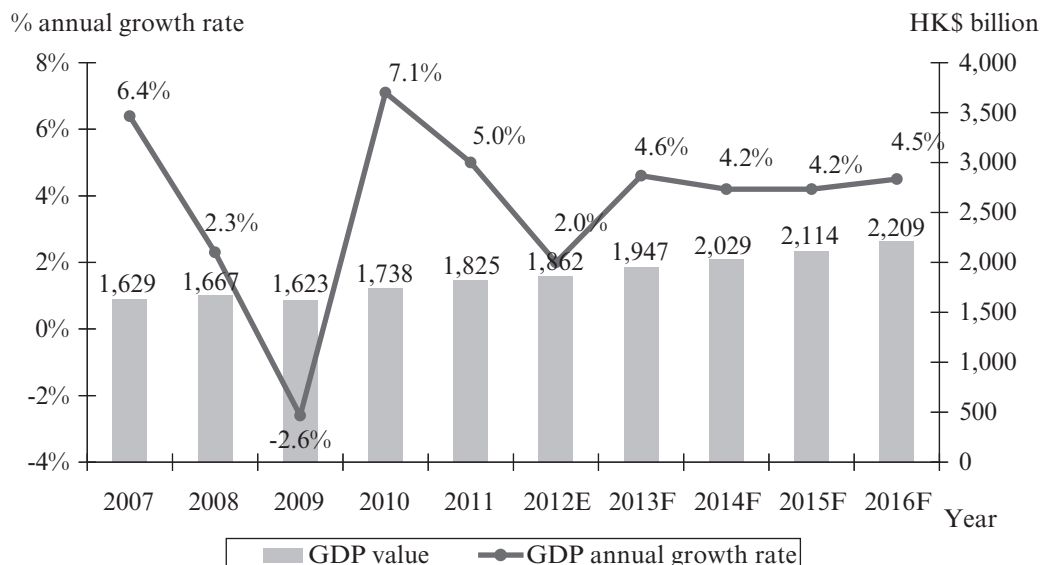


Figure 1. GDP value and GDP annual growth rate of Hong Kong from 2007 to 2016

Notes:

- (1) Definition of GDP value: Gross Domestic Product (in chained 2009 dollars).
- (2) Definition of GDP annual growth rate: The change in Hong Kong's Gross Domestic Product (in chained 2009 dollars from one year to the next).

Sources: Census and Statistics Department, Hong Kong; Economist Intelligence Unit; Ipsos Report

Despite the adverse impact of the global financial crisis in 2008, the GDP value in Hong Kong grew from about HK\$1,629 billion in 2007 to about HK\$1,825 billion in 2011 at a CAGR of about 2.9%. The global financial crisis caused the GDP value to drop from annual growth rate of about 2.3% in 2008 to about -2.6% in 2009. The total GDP value declined from about HK\$1,667 billion in 2008 to about HK\$1,623 billion in 2009. The economy of Hong Kong rebounded quickly in 2010 at GDP annual growth rate of about 7.1%. Although at a slower pace, the Hong Kong economy continued its growth momentum and the GDP value grew at about 5.0% in 2011 as a result of growing exports and tourism activities. Under increasing concern of the European debt crisis however, the Hong Kong economy slowed down at an annual growth rate of about 2.0% in 2012 and is expected to pick up thereafter.

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### CPI Growth Rate in Hong Kong

Inflation rate in Hong Kong as represented by growth in Consumer Price Index in Hong Kong correlates to the economy growth in the past 5 years.

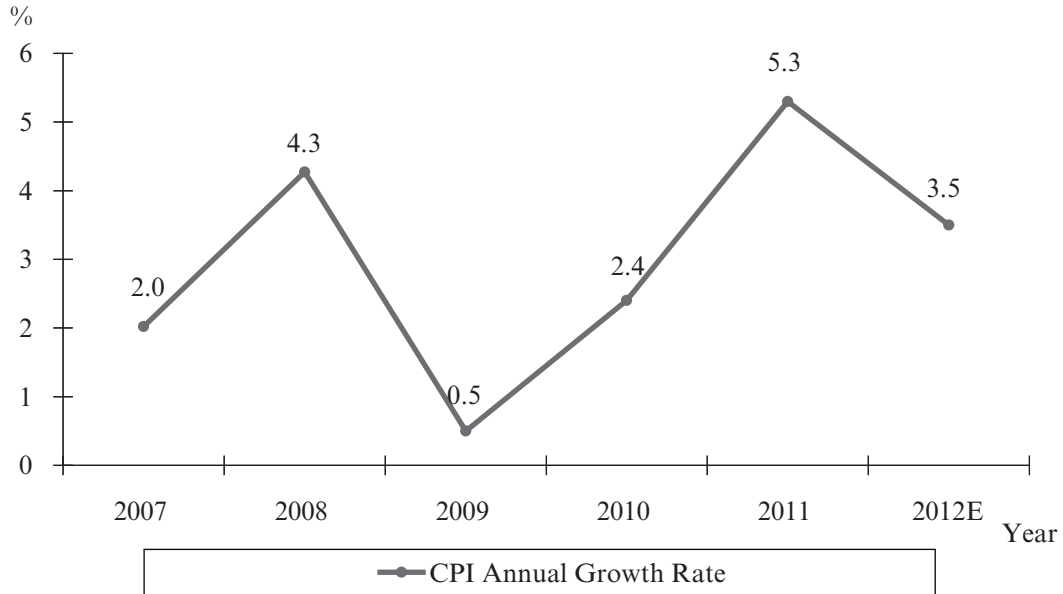


Figure 2. CPI growth rate of Hong Kong from 2007 to 2012

Sources: Census and Statistics Department, Hong Kong; Ipsos Report

Inflation rate surged from an annual rate of about 2.0% in 2007 to an annual rate of about 4.3% in 2008, and was held back to an annual rate of about 0.5% in 2009 because of the economic downturn and the outbreak of Swine Flu and H1N1 that caused local consumption to slump. Upon the recovery of the economy and 2011 as driven by the implementation of minimum wage, inflation rate peaked at about 5.3% in 2011. Inflation is expected to drop to about 3.5% in 2012. Weakened spending power as a result of the inflation, coupled with an increase in consumer spending supported by restored consumer confidence are expected to fuel the demand for short-term loans as consumers fall short of liquidity and seek to borrow to sustain their higher costs of living.

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### Annual Median Household Disposable Income and Average Household Expenditure in Hong Kong

The demand for pawn loans and mortgage loans correlates to consumer sentiments to spend which can be reflected in the household disposable income and consumption expenditure.

CAGR of annual median household disposable income in Hong Kong from 2007 to 2011 = 1.2%

CAGR of average annual household consumption expenditure in Hong Kong from 2007 to 2011 = 4.1%

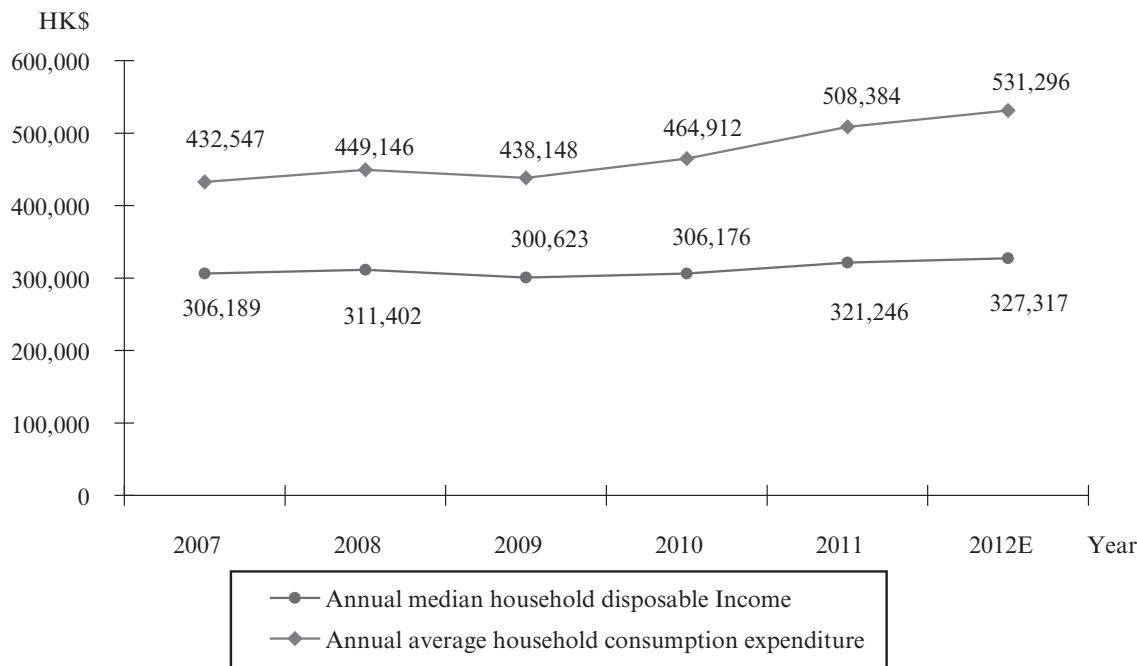


Figure 3. Annual median household disposable income and annual average household consumption expenditure in Hong Kong from 2007-2012

Notes:

- (1) Annual average household consumption expenditure refers to the final consumption expenditure by households on individual consumption goods divided by the total number of households in Hong Kong.
- (2) Annual median household disposable income refers to median nominal disposable income earned by households per annum.

Sources: Economist Intelligence Unit; Ipsos Report

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Annual median household disposable income grew at a CAGR of about 1.2% while annual average household consumption expenditure grew at about 4.1% from 2007 to 2011. Both income and expenditure slumped in 2009 as a result of the global financial crisis which weakened consumer confidence but both picked up in 2010 as the economy recovered. Annual median household disposable income and annual average household consumption expenditure accelerated in 2011 to reach about HK\$321,246 and HK\$508,384 respectively as a result of restored consumer confidence, falling unemployment rate and surge in inflation rate. With increased expenditure and income, total value of loans and advances granted by authorised institutions and other licensed lenders in Hong Kong surged at a CAGR of about 10.3% and 10.6% respectively from 2007 to 2011. As Hong Kong's living standard continues to rise along with inflation, income and expenditure are expected to continue its growing trend in 2012 to reach about HK\$327,317 and HK\$531,296 respectively.

### **Total Number of Authorised Institutions and Other Licensed Lenders in Hong Kong**

The money lending industry in Hong Kong can mainly be classified into two categories: authorised institutions and other licensed lenders.

Authorised institutions include licensed banks, restricted licensed banks and deposit-taking companies. Only licensed banks may operate current and savings accounts, and accept deposits of any size and maturity from the public and pay or collect cheques drawn by or paid in by customers. Restricted licensed banks are principally engaged in merchant banking and capital market activities. They may take deposits of any maturity of HK\$500,000 and above. Deposit-taking companies are mostly owned by, or otherwise associated with banks. These companies engage in a range of specialised activities, including consumer finance and securities business. They may take deposits of HK\$100,000 or above with an original term of maturity of at least three months. As a whole, authorised institutions are subject to the restrictive requirements bound by the supervision of the HKMA and the regulations under the Banking Ordinance (Chapter 155 of the laws of Hong Kong).

Other licensed lenders include money lenders and pawnbrokers which are governed by the Money Lenders Ordinance and the Pawnbrokers Ordinance respectively. The services of money lenders include provision of both secured and unsecured loans such as mortgage loans, consumer and corporate loans, equipment leasing, credit cards, cheque and invoice discounting, loan syndication etc. Pawnshops on the other hand only offer secured loans with items of personal chattels used as collaterals. In general, although authorised institutions and other licensed lenders offer both secured and unsecured loans, authorised institutions such as banks offer a much broader product portfolio including credit card services, overdraft (OD), stock and bonds and other financial products. For secured loans, they will also accept various forms of collaterals including stock, bonds and receivables while other licensed lenders including both pawnbrokers and money lenders tend to accept personal items and real estates respectively. For unsecured loans, banks would also offer term loans, while personal instalment loans are most typically offered by money lenders.

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Pang & Co., legal advisers to our Company as to Hong Kong law, have advised that as we are not an authorised institution, we are not required to follow the guidelines and restrictive requirements issued by the HKMA.

CAGR of the number of the licensed banks in Hong Kong from 2007 to 2012 = 1.8%

CAGR of the number of the restricted licensed banks in Hong Kong from 2007 to 2012 = -6.3%

CAGR of the number of the deposit taking companies in Hong Kong from 2007 to 2012 = -3.7%

CAGR of the number of the other licensed lenders in Hong Kong from 2007 to 2012 = 4.5%



Figure 4. The number of authorised institutions and other licensed lenders in Hong Kong from 2007 to 2012

Notes:

- (1) Other licensed lenders include money lenders and pawnshops.
- (2) The number of other licensed lenders = money lenders + pawnshops - (money lenders with Pawnbrokers Licences).
- (3) 12 Money Lender Licences' holders in Hong Kong possessed Pawnbrokers Licences by the year end of 2012.

Sources: Hong Kong Monetary Authority; Companies Registry, Hong Kong; Hong Kong Police Licensing Office; Ipsos Report

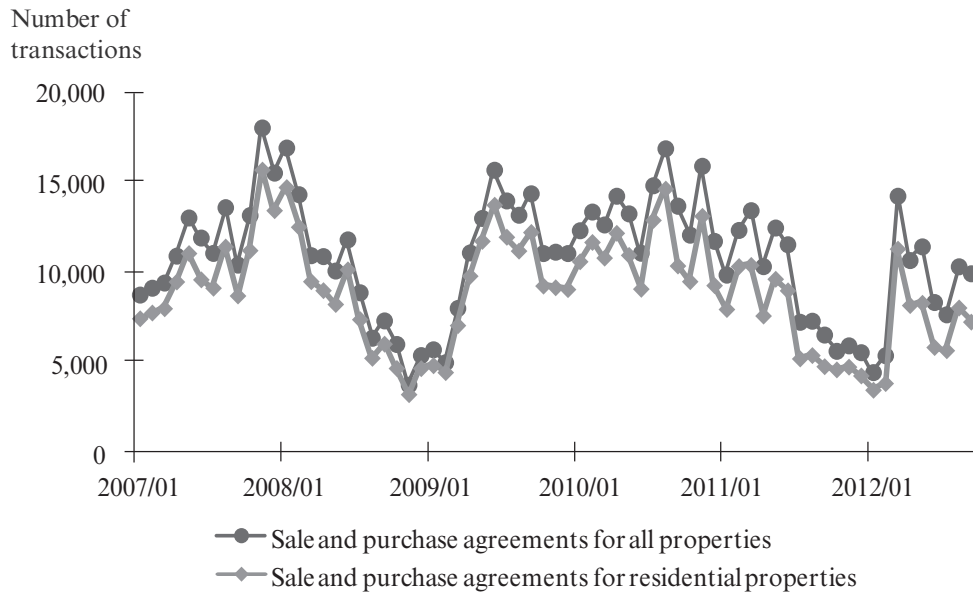
Hong Kong has one of the highest concentration of banking institutions in the world with about 200 authorised institutions in 2012. The number of authorised institutions in Hong Kong declined slightly from 200 in 2007 to 193 in 2010 but climbed back to 200 in 2012. Despite the fact that the scope of services of other licensed lenders may not be as wide as authorised institutions, their role in the money lending industry in Hong Kong has been increasing with the number of other licensed lenders increased significantly from 922 in 2007 to 1,151 in 2012, represented by a CAGR of about 4.5%. This is largely because other

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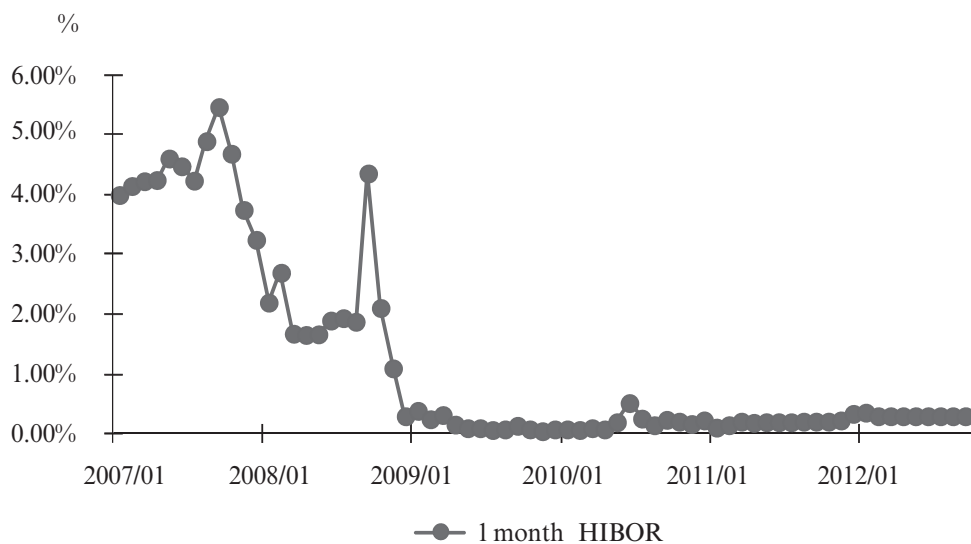
licensed lenders are able to enjoy a greater flexibility in their business operations in terms of loan sizes, requirement of income proof and types of collaterals under the regulation of the Money Lenders Ordinance or the Pawnbrokers Ordinance, as opposed to tight restrictions on authorised institutions imposed by the HKMA.

### Hong Kong property market and interest rate environment

Interest rate is one of the key factors affecting buyers' decision to purchase properties. Increase in the market mortgage interest rate increases the cost of funding, and thus increases the financial burden of home buyers.



Sources: Land Registry, Hong Kong; Ipsos Report



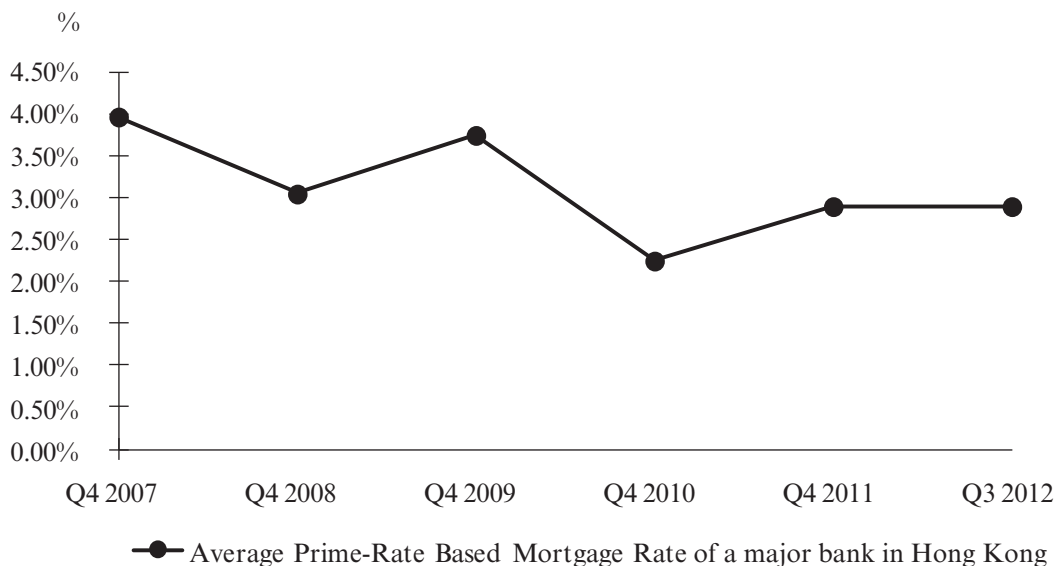
Source: Ipsos Report



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Source: Ipsos Report

The number of sale and purchase agreements for all properties remained at a high level in Hong Kong in 2007 as the stable interest rate environment, and the best lending rates remained unchanged in the first nine months, boosted the confidence of consumers and investors. The property market in Hong Kong was buoyant from 2007 to second quarter of 2008. The successive hikes in mortgage rates by the local banks in September 2008 and the heightened uncertainties surrounding the global economy caused by the global financial crisis also fuelled the cautious sentiment in the property market in Hong Kong, which led to a dramatic drop in the number of transactions in the property market since the second half of 2008. The number of transactions in the property market picked up in 2009 as a result of the historically low mortgage rates and rebound of the Hong Kong economy from the global financial crisis. The influx of wealthy buyers from the PRC purchasing properties in Hong Kong also caused the number of property transactions in Hong Kong to remain at a high level for the rest of the year and afterwards.

In view of the over-heating of the property market, the Hong Kong government intended to cool down the property market by launching the Special Stamp Duty (“SSD”) with effect from 20 November 2010, which imposed additional stamp duty for reselling any residential property within 24 months of purchase, as well as significantly boosting land supply for residential development in 2011. With these government policies and slowdown in economic growth, the total number of sale and purchase agreement registrations dropped from about 12,000 in April 2011 to about 5,000 in January 2012.

The greater transaction volume in the second quarter of 2012 compared to the first quarter is due to the rather low transaction volume in January and February, which could be partly attributed to seasonal effects. In fact, the transaction volume in June in 2012 decreased by about 26.7% to 8,597 compared with May. Vendors remained aggressive in pricing, since there were fewer flats available after the purchase rush in February and March in 2012. In October 2012, the Hong Kong government adjusted the rate of SSD and extended the holding period of residential property to 36 months. It also introduced a

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Buyer's Stamp Duty ("BSD") to charge non-Hong Kong residents an additional 15%, on top of the existing stamp duty and SSD, if applicable. With both policies effective from 27 October 2012, the number of transactions for residential properties plunged from about 8,714 in October to 3,286 in December 2012, represented by a decrease of about 62%.

### MARKET ANALYSIS ON PAWN LOAN INDUSTRY IN HONG KONG

#### Overview of Pawn Loan Industry in Hong Kong

Pawn loan has a longstanding history and is the most traditional form of banking emerged in Hong Kong. The first legal pawnshop was established in Sheung Wan in 1926 when the government legalised the business. Before the establishment of authorised institutions in Hong Kong, customers pawned their personal belongings such as shoes, clothing, quilts in exchange for instant money to fulfill their short term financial needs and redeemed the pawned goods later with interest payment. Before the enactment of the relevant laws, pawn loans were generally categorised by contract term of 3 years, 1 year and half year with no fixed interest requirement. The open door market policy and commercial development of Hong Kong in the early 20th century has accelerated the growth of the pawn loan industry in Hong Kong.

#### The Current Situation of Pawn Loan Industry in Hong Kong

The number of pawnshops has increased from less than 10 in 1926 to about 202 in 2011. Today, pawnshops are monitored by the Hong Kong Police Force (Licensing Office) under the Pawnbrokers Ordinance. As Hong Kong people's living standard changes and technology advances, people nowadays pawn more valuable goods with high resale value such as gold, watches, cellphones and laptop computers in exchange for money. The term of a pawn loan under the Pawnbrokers Ordinance is four lunar months where customers are granted a loan at amount below the estimated resale value of the pawned goods. In order to redeem the pawned goods, customers have to pay an interest rate of 3.5% per lunar month at maximum pursuant to the Pawnbrokers Ordinance during the loan term. Pawnshops generally allow extension of the pawn loan upon the expiry of its term. Once the loan term expires and the customers do not redeem their pawned goods, pawnshops are entitled to sell the goods to buyers or second-hand product dealers and jewellery shops to redeem its value. Pawnshops usually have established relationships with different buyers and second-hand product dealers. Pawnshops largely rely on these buyers or second-hand product dealers to assess the resale value of pawned goods. Restricted by the resale value of the pawn items, most pawnshops now only accept gold, watches, jewellery or electronic products such as cellphones and laptop computers. The target customers of pawn loans are mainly relatively low income Hong Kong residents who are 18 years old or above. Majority of customers seeking for pawn loan are returned customers with increasing number of foreign domestic helpers and Chinese immigrants in recent years. Convenience and instant payment without loan floor and credit check requirement have sustained the development of pawn loan industry in Hong Kong.

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### Feature of the Major Customers of Pawn Loan in Hong Kong

The majority of customers of pawn loans are Hong Kong residents which accounted for about 70% of the total number of customers of pawn loans in 2011. Middle-age populations and elders with relatively low income are the major customers of pawn loans, in particular, those with monthly income of below HK\$8,000. Majority of the customers of pawn loans are returned customers, these customers sometimes only need a few hundreds or thousands for emergency which banks would fail to offer. There are also customers who tend to obtain quick cash for purposes such as gambling and investment. In the past few years, there has also been an increasing number of young population aged in their 20s-30s seeking for pawn loans as people sought for better standard of living and luxury goods at a younger age. Increasing poverty gap and living standard will sustain the demand for pawn loan amongst Hong Kong customers, while changing technology will provide more opportunities for young people as they pawn their electronic gadgets to resolve short-term financial needs. Foreign domestic helpers as a whole accounted for about 25% of the total number of customers in the same period while Mainland Chinese accounted for the rest of the 5% of pawn loan customers.

CAGR of total number of foreign domestic helpers in Hong Kong from 2007 to 2011 = 5.1%

CAGR of total number of foreign domestic helpers in Hong Kong from 2012 to 2016 = 1.6%

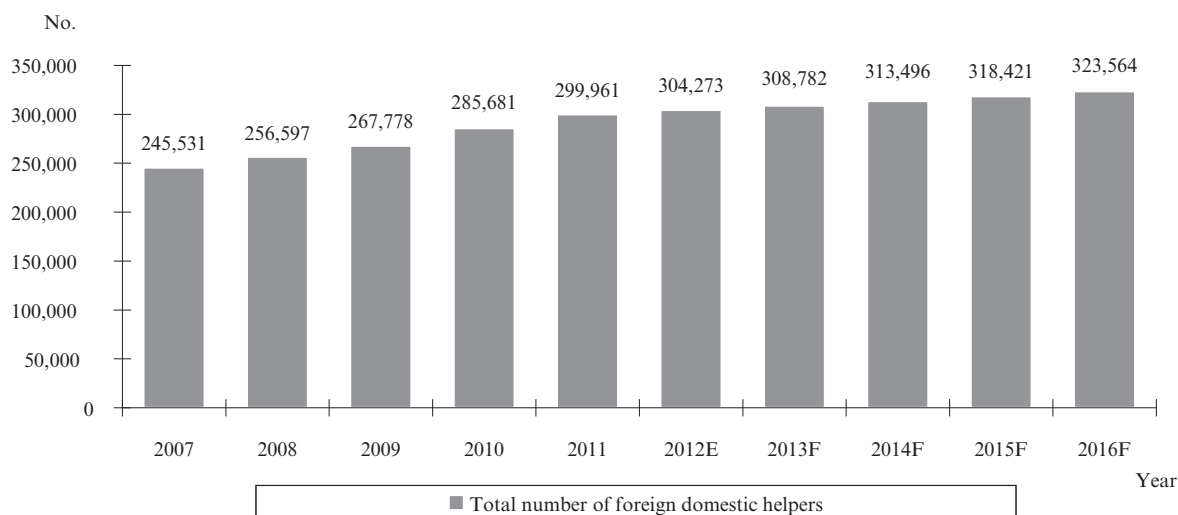


Figure 5. Total Number of foreign domestic helpers in Hong Kong from 2007 to 2016

Sources: Immigration Department, Hong Kong; Ipsos Report

The total number of foreign domestic helpers in Hong Kong increased from about 246,000 in 2007 to about 300,000 in 2011 at a CAGR of about 5.1% mainly driven by the surge of Indonesian domestic helpers which grew at a CAGR of about 6.7% during the same period. Due to the intention of the Indonesian government to reduce the outflow of Indonesian domestic helpers into Hong Kong in the future years, the number of foreign domestic helpers is expected to increase at a slower pace than before at a CAGR of about 1.6% from 2012 to 2016.

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The number of Mainland Chinese customers seeking for pawn loans has been increasing in recent years. Mainland Chinese accounted for about 5% of the total number of customers of pawn loans in 2011.

CAGR of total number of Mainland Chinese entering Hong Kong for residence from 2007 to 2011 = 6.4%

CAGR of total number of Mainland Chinese entering Hong Kong for residence from 2012 to 2016 = 5.5%

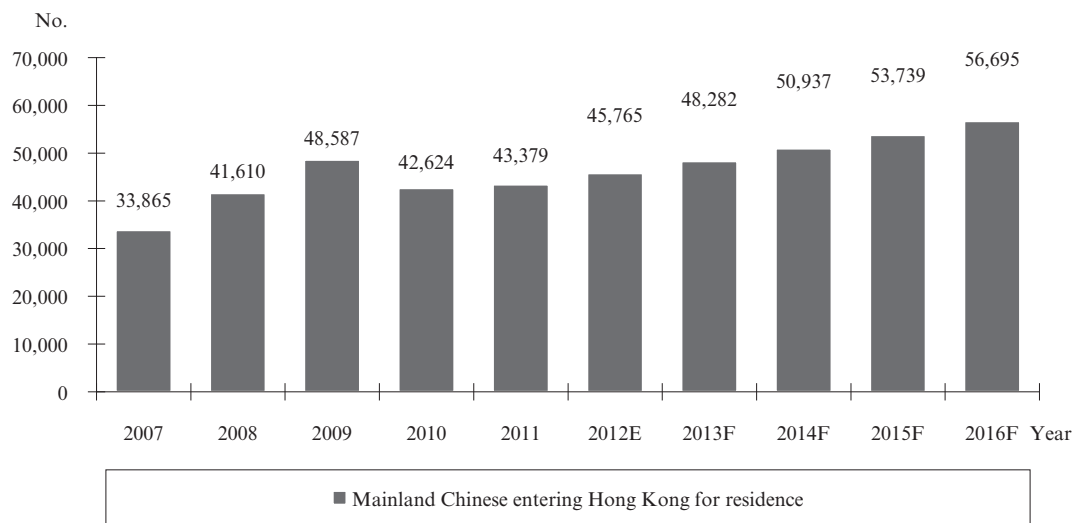


Figure 6. Number of Mainland Chinese from PRC to Hong Kong for residence from 2007 to 2016

Note: Definition of Mainland Chinese entering Hong Kong for residence: Number of one-way permit holders.

Sources: Home Affairs Department and Immigration Department, Hong Kong; Ipsos Report

The number of Mainland Chinese entering Hong Kong for residence increased at a CAGR of about 6.4% from 2007 to 2011. The entry of One-way Permit Scheme allows the entry of Mainland residents into Hong Kong for the purpose of settlement with aim to facilitate family reunion. One-way Permits are issued by the relevant authorities of the Public Security Bureau in the PRC. The daily quota of One-way Permits is 150, including 60 permits reserved for persons who were born in the PRC and have the right of abode in Hong Kong by descent from their either parent in accordance with Article 24(2)(3) of the Basic Law, and 30 permits reserved for separated spouses. Mainland Chinese entering Hong Kong for residency is estimated to grow at a CAGR of about 5.5% from 2012 to 2016. In 2011, it is estimated that the total number of Mainland Chinese customers for pawn loan accounted for about 11% of the total number of Mainland Chinese from the PRC.

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### Total Number of Pawn Loan Service Operators and Pawnshops in Hong Kong

The number of pawn loan service operators and pawnshops in Hong Kong grew steadily at a CAGR of about 0.3% and 1.1% respectively from 2007 to 2011. The pawn loan industry is highly fragmented with no single pawn loan service operator dominating the market. Less than 10% of the pawn loan service operators own more than 5 pawnshops in Hong Kong.

CAGR of total number of pawn loan service operators in Hong Kong from 2007 to 2011 = 0.3%

CAGR of total number of pawn loan service operators in Hong Kong from 2012 to 2016 = 1.1%

CAGR of total number of pawnshops in Hong Kong from 2007 to 2011 = 1.2%

CAGR of total number of pawnshops in Hong Kong from 2012 to 2016 = 1.0%

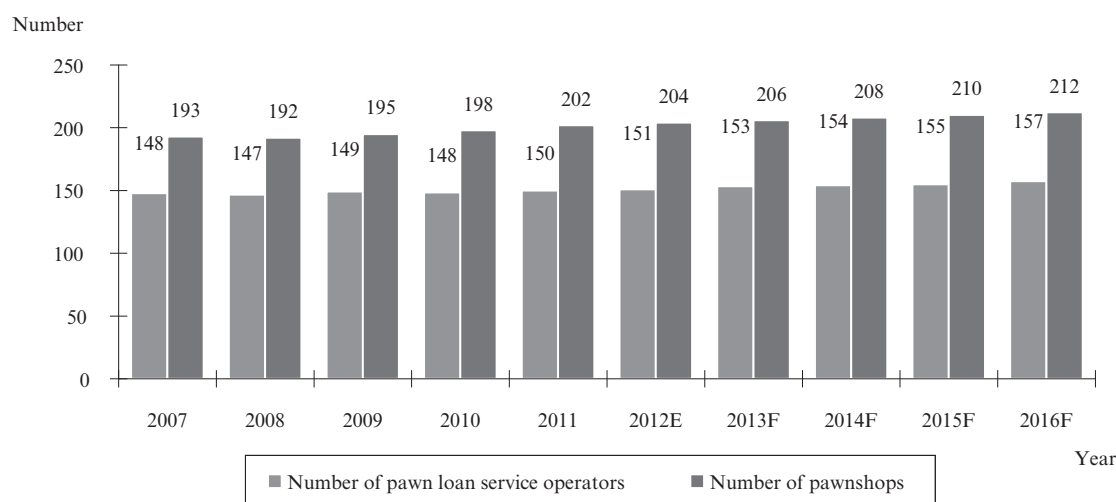


Figure 7. The total number of pawn loan service operators and pawnshops in Hong Kong from 2007 to 2016

Sources: Hong Kong Police Licensing Office; Ipsos Report

There were about 150 pawn loan service operators in Hong Kong in 2011, operating 202 pawnshops. Most of the pawn loan service operators have over 40 years of experience in the industry. Despite the maturity of the business in Hong Kong, pawn loan service operators in Hong Kong are striving to increase their business coverage with some opening more than one pawnshop to diversify their businesses. Increasing number of financial tools such as credit card advances has been substituting the need for pawn loans in the past years which lowered the demand for pawn loans. Operation in chains has been means to sustain the business with increasing number of pawn loan service operators expanding their service scope by acquiring money lender licences to offer different types of loans such as mortgage loans and personal loans. However, the demand for pawn loans continues to exist for the relatively low income population in Hong Kong (population with monthly income less than HK\$8,000 that accounted for about 26.8% of the total number of employed people), along with the increasing number of foreign domestic helpers and new immigrants from the PRC, the pawn loan market in Hong Kong will remain optimistic with the number of pawn loan

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service operators expecting to grow steadily at a CAGR of about 1.1% while the number of pawnshops expecting to increase at about 1.0% from 2012 to 2016. With 12 pawnshops, the Company is the largest pawn loan service operators in Hong Kong in 2011.

### Value of Loans and Advances Granted by Pawnshops in Hong Kong

The value of loans and advances granted by pawnshops increased from about HK\$4,274 million in 2007 to about HK\$5,438 million in 2011 at a CAGR of about 6.2%.

CAGR of total value of loans and advances granted by pawnshops in Hong Kong from 2007 to 2011 = 6.2%

CAGR of total value of loans and advances granted by pawnshops in Hong Kong from 2012 to 2016 = 8.0%

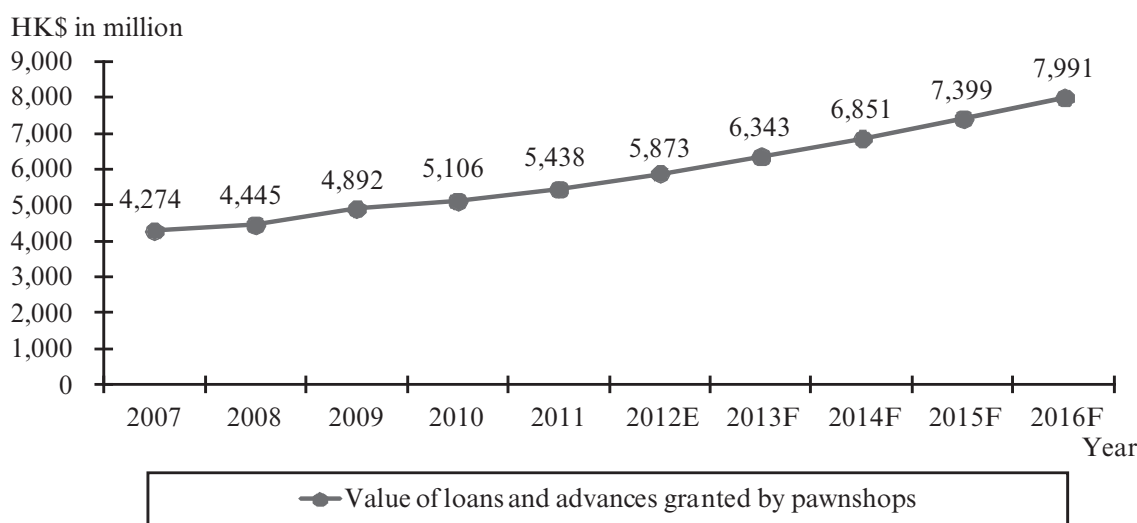


Figure 8. Total value of loans and advances granted by pawnshops in Hong Kong from 2007 to 2016

Source: Ipsos Report

The value of loans and advances granted by pawnshops grew steadily in the past few years despite the economic instability. During the economic recession, the value of loans and advances granted by pawnshops increased by 10.1% in 2009, compared to about 4.0% in 2008. Increased in total value of loans was sustained in 2011 at about 6.5% as a result of the increase in the number of foreign domestic helpers and Mainland Chinese customers. With inflation growth and increased spending as triggered by the recovering economy in the same year, value of loans per transaction increased as more valuable items were pawned for loans.

Particularly in 2009, the Hong Kong government has raised the maximum loan amount from HK\$50,000 since 1990 to HK\$100,000 for each single pawn loan granted pursuant to the Pawnbrokers Ordinance. The increase in the cap was largely as a result of inflation that the value of pawned goods such as gold and jewellery increased significantly since 1990. However, since it has been the industry's practice to break down the value of pawn loan into several transactions for high valued worth items, the new policy only worked to save the

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administrative work of operators without significant effect on the value of loans and advances granted. Our Directors confirmed that it is not our Group's practice to break down the value of pawn loan into several transactions for a high value item. As we are also holding a Money Lenders Licence for all of our Pawnshops, we would grant the loan using our Money Lenders Licence for a high value item (i.e. in excess of HK\$100,000) instead. It is expected that personal belongings such as gold, cellphones and jewellery will continue to dominate the pawn items as collaterals. Hence, the value of loans and advances granted by pawnshops is expected to grow steadily at a CAGR of about 8.0% from 2012 to 2016.

### **Factors Affecting the Growth and Development of Pawn Loan Industry in Hong Kong**

Increase in the number of foreign domestic helpers and Mainland Chinese, availability of alternative means of money lender, high poverty rate and general economic conditions are key factors affecting the development of pawn loan industry in Hong Kong.

#### *Increase in the number of foreign domestic helpers and Mainland Chinese: High, Positive Impact*

There has been an increase in the number of foreign domestic helpers and Mainland Chinese seeking for pawn loans in recent years, particularly Fillipinos and Indonesians as they make up the majority of the total number of foreign domestic helpers in Hong Kong. Most of the foreign domestic helpers and Mainland Chinese not only face difficulty in adapting the high living standard in Hong Kong with their low salary, but also need to send money home each month. They tend to borrow from pawnshops when they are financially constrained and redeem their pawned collaterals once they receive their salary. Foreign domestic helpers and Mainland Chinese together make up about 30% of the current customer base of pawnshops and is expected to be the key engine for growth for the pawn loan industry in the next few years.

#### *Increase in the value of collaterals: High, Positive Impact*

As a result of inflation, value of popular pawn items such as gold and jewellery has increased over the years. Inflation rate surged from 2007 to 2011 from annual growth rate of about 2.0% to 5.3%. Increase in inflation, hence the value of pawn items, will drive the increase in the value of loans granted by pawnshops.

#### *Alternative means of money lending: High, Negative Impact*

There has been an increasing number of financial tools in the market, offering both short-term and long-term money lending services such as credit card advances and mortgage loans without the need for credit check and income assessment. Such services have provided customers alternatives for quick and safety cash withdrawal as well as lowered the barriers of money borrowing. New customers also tend to borrow larger sum of money from more reputable lenders such as licensed banks and money lenders with high brand awareness. This limits opportunities and reduces demand for pawn loans in Hong Kong.

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### *High poverty rate: High, Positive Impact*

Despite the growing economy and beneficial links with the PRC, there has been a growing gap between the rich and the poor in Hong Kong. As the cost of living remains high and increasing, increase in household income has failed to keep pace with the high inflation and soaring real estate prices. The median household income in the fourth quarter of 2011 for one person family was about HK\$7,200, HK\$ 15,900 for a two persons family, HK\$22,700 for a third persons family and HK\$27,300 for a fourth persons family. With poverty defined as those earning less than half the median household income, it is estimated that about 18% of the Hong Kong population was living under poverty in 2011, which is equivalent to approximately 178 thousand families. It is expected that high poverty rate will sustain the demand for pawn loans in Hong Kong as the poor struggle to meet the high living standard in Hong Kong.

### *Economic condition: Low, Positive Impact*

Demand for money borrowing exists in Hong Kong during both the time of economy downturn and boom. During economic recession, more people suffer from tight liquidity and require quick cash to solve their financial difficulties. Money is hard to come by and credit standards are tightening. Pawn loan provides a convenient and safe alternative at the time of financial difficulty and serves to sustain individual living, particularly the poor people in the case of sudden emergency. During economic boom, more people seek to invest and increase spending as consumer confidence picked up, gambling activities tend to increase along with increased money spent on non-necessities such as electronic devices and luxury items etc. Such also induces the demand for pawn loan which provides quick cash to satisfy the gambling and shopping impulse.

## **Future Trends and Developments of Pawn Loan Industry in Hong Kong**

### *Pawn loan will remain an alternative means to borrowing*

Unlike other secured or unsecured loans granted by authorised institutions and money lenders, pawn loan by its nature, offers an alternative for people to pledge their personal chattels such as jewellery and watches as collaterals for quick cash and to redeem the collaterals within a given time without complicated and lengthy application procedure. This enables pawn loan service operator to continue to grow in such market niche.

### *More pawnshops are engaging in mortgage loan*

Collective operation of pawn and mortgage loan services is observed in the market as money lenders possessing both Money Lenders Licence and Pawnbrokers Licences are able to “cross-sell” their loan services to their customers. This has contributed to the increasing value of loans and advances granted by pawnshops which grew at a CAGR of about 6.2% from 2007 to 2011.



### MARKET ANALYSIS ON MORTGAGE LOAN MARKET IN HONG KONG

#### Overview of Mortgage Loan Market in Hong Kong

The money lending market in Hong Kong is highly fragmented with different service providers including authorised institutions and money lenders providing similar services for both secured and unsecured loans. Secured loans are protected by an asset or collateral of some sort. Authorised institutions and money lenders will hold the deed or title of the collateral until the loan has been fully paid off by the borrower, including interest and all administration fees. If the borrower defaults on the loan, the service provider can seize the collateral and sell it to settle the borrower's debt. Mortgage loan is the most common type of secured loans, while collaterals include but not limited to real estate, equipment, car, stock, bonds etc. On the other hand, an unsecured loan is obtained without collateral but with a signed agreement by borrower to pay back the loan within a set term. In event of default, additional fees may be assessed and legal actions can be taken against the borrowers. Personal loan and credit card advances are the most common type of unsecured loans offered in the market.

Most of the secured loans in Hong Kong are provided by authorised institutions which are estimated to account for over 80% of the total number of secured loans granted in Hong Kong. Under the supervision of the HKMA, authorised institutions generally adopt prudent and stable policies in approving mortgage loans. For mortgage loan, they are required to conduct credit assessment which involves an analysis of the borrower's financial status and background, the purpose of the loan, the value of the real estate being mortgaged, employment status etc. Borrowers are required to provide income proof of the previous six months or financial report of business for the previous three years. Banks will charge interest on early loan repayment as well as handling fees of 1–2%. On average, the approval process of an application for a mortgage loan could take at least two to three weeks. As a whole, the stringent policies adopted by banks have given rise to money lenders in the market with relatively lenient requirements.

In Hong Kong, authorised institutions and money lenders typically quote interest rate with reference to the Hong Kong Dollar Prime Rate (P) or Hong Kong InterBank Offered rate (HIBOR), which is known as the prime-based rate and the HIBOR-based rate respectively. The other type of mortgage rate which is the fixed rate is less popular in Hong Kong. Prime rate in Hong Kong (which is also referred to as best lending rate) was about 5.0 to 5.5% in 2011 while HIBOR was about 0.3% (for three months) over the same period. Different authorised institutions, such as licensed banks, offer different mortgage rate in Hong Kong. The mortgage rates charged by money lenders are generally higher than banks because of the higher risk associated by their relatively lenient requirements. In the first three quarters of 2011, Hong Kong's three largest banks charge borrowers at an annual rate of about 1.7 % to 2.2%, or 1.5% to 2% above the HIBOR for mortgage loans, while the prime-based rate remained steadily at about 2.2% of 3.1% below the prime rate. The HIBOR-based rate increased to about 2.4% in January of 2012. As the gap between the prime-based rate and HIBOR-based rate is narrowing, more borrowers are shifting from HIBOR-based rate to prime-based rate for mortgage loans from banks. Money lenders on the other hand offer services at monthly interest rate ranging from 1.0% to 1.6% on

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average, with rate varies by types of mortgage loan. The annual rate could go up to over 30% in some cases. Although interest rates charged by money lenders vary across service providers by different type of mortgage loan, interest rate which exceeds 60% per annum is illegal under the Money Lenders Ordinance.

### **First Mortgage Loan Versus Second Mortgage Loan**

A real estate can be mortgaged for more than one loan. A loan that is registered first is considered the first mortgage loan and one that is registered second is considered a second mortgage loan. In the event of default, first mortgage loan would first get paid off, and any funds remaining would be used to pay off second mortgage loans, if any. Second mortgage loan typically demands a higher interest rate for this reason. Customers may borrow up to the amount of equity they have in the real estate. For example, if the owner has a real estate valued at HK\$1,000,000 and currently owes HK\$750,000 on the first mortgage loan, a second mortgage loan can be obtained for HK\$250,000. This is the most common type of second mortgage loan that is 100% secured by equity. In Hong Kong, banks are the most common providers for first mortgage loan and can grant loans amounted up to 70% of the value of the real estate, while money lenders offer both first and second mortgage loans. For residential real estate second mortgage loans, money lenders in Hong Kong typically can grant loan amounted up to 70%–100% of the value of the residential real estate, depending on the type of real estate. There are some money lenders who are able to offer mortgage loan amounted up to 100% with unlimited loan repayment period. By and large, revenue of money lenders is typically recognised as interest income.

Regardless of the service provider, the target customers of mortgage loans include both corporations and individuals. Since mortgage loan granted by money lenders can provide more flexibility to borrowers at shorter approval period, they are strongly preferred by small-and-medium enterprises (SMEs) and individuals who could not fully meet the mortgage loan requirements of banks. Mortgage loan offered by money lenders has become a useful tool for corporations to resolve their unexpected cash flow needs and for individuals to fulfill their short-term needs such as credit card bill settlement. As a whole, the convenient and flexible services offered by money lenders have reduced the barriers for borrowing significantly and provided alternatives means to corporations and individuals to solve their urgent financial needs.

### **Total Number of Money Lenders in Hong Kong**

Money lenders are governed by the Money Lenders Ordinance. A person carrying on business as a money lender must obtain a money lenders licence from the licensing court and the Registrar of Money Lender while the Commissioner of Police is responsible for enforcing the Money Lenders Ordinance in Hong Kong. Business of money lenders typically include (i) consumer and commercial loan, (ii) mortgage loan, (iii) vehicle, plant and equipment leasing, (iv) credit card, (v) Small and Medium Enterprises loan, (vi) cheque and invoice discounting and (vii) loan syndication. With similar service offering for secured and unsecured loans, money lenders are able to grant certain types of mortgage loans that are not usually available from authorised institutions, for example, when banks are not willing to accept relatively old real estates, or if the borrower requires a mortgage loan of

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over 70% of the value of the real estate, and is not eligible for the Mortgage Insurance Programme. In such cases, the borrower would resort to money lenders to obtain a mortgage loan. In general, money lenders have relatively lenient requirements for the application and approval of loans. Most of them are able to offer mortgage loan without the need for financial assessment or income proof. Borrowers only need to pledge the real estate as collateral for the mortgage loan. The complicated application processes as those required by the banks are cut to speed up the application process. In terms of first mortgage loan, some money lenders can even grant loans up to 100% of the property value to customers. The number of money lenders in Hong Kong increased from about 741 in 2007 to 959 in 2012 at a CAGR of about 5.3%.

CAGR of total number of money lenders in Hong Kong from 2007 to 2012 = 5.3%

CAGR of total number of money lenders in Hong Kong from 2013 to 2016 = 3.3%

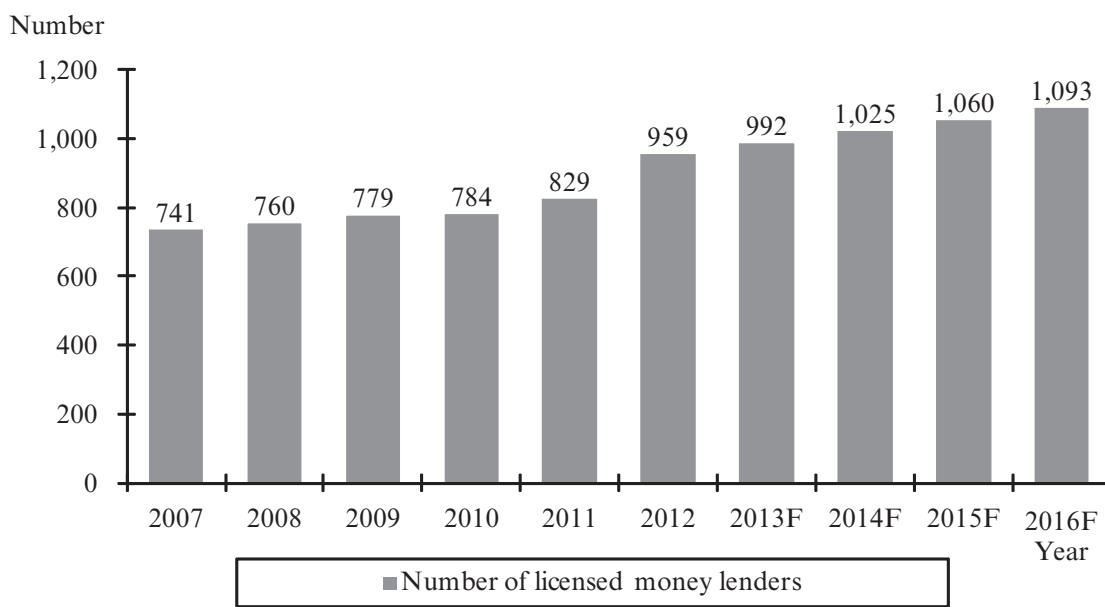


Figure 9. The total number of money lenders in Hong Kong from 2007 to 2016

Note: Number excluded authorised institutions and included pawnshops who possess money lenders licence.

Sources: Companies Registry, Hong Kong; Ipsos Report

There were about 959 money lenders in Hong Kong in 2012. Due to the increasing demand for housing and enhanced lifestyle of Hong Kong consumers, more money lenders have entered the Hong Kong market in the past few years to capture consumers' increasing liquidity need. These money lenders have emphasised on their fast and convenient application process without need of credit and background assessment to successfully attract customers, who fail to meet the loan requirements of authorised institutions. Regardless of the growing demand, the mortgage loan market (excluding authorised institutions) is dominated by some money lenders who operate in chains and have achieved high brand awareness through aggressive market advertising campaigns and tele-calls over

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the years. These leading market players leverage on their wide network of retail spots and relatively lenient borrowing requirements to enlarge their customer base. They offer mainly second-mortgage loans and personal loans. It is expected that the tightening credit measures at authorised institutions will continue to attract more new entrants into the market, with growth in the number of money lenders expected at a CAGR of about 3.3% from 2013 to 2016.

### Total Value of Loans and Advances Granted by Money Lenders in Hong Kong

The total value of loans and advances granted by money lenders accounted for about 3.8% of the total value of loans granted by authorised institutions and other licensed lenders altogether in 2011. The value of loans and advances granted by money lenders grew significantly at a CAGR of about 10.8% from 2007 to 2011.

CAGR of total value of loans and advances granted by money lenders in Hong Kong from 2007 to 2011 = 10.8%

CAGR of total value of loans and advances granted by money lenders in Hong Kong from 2012 to 2016 = 7.9%

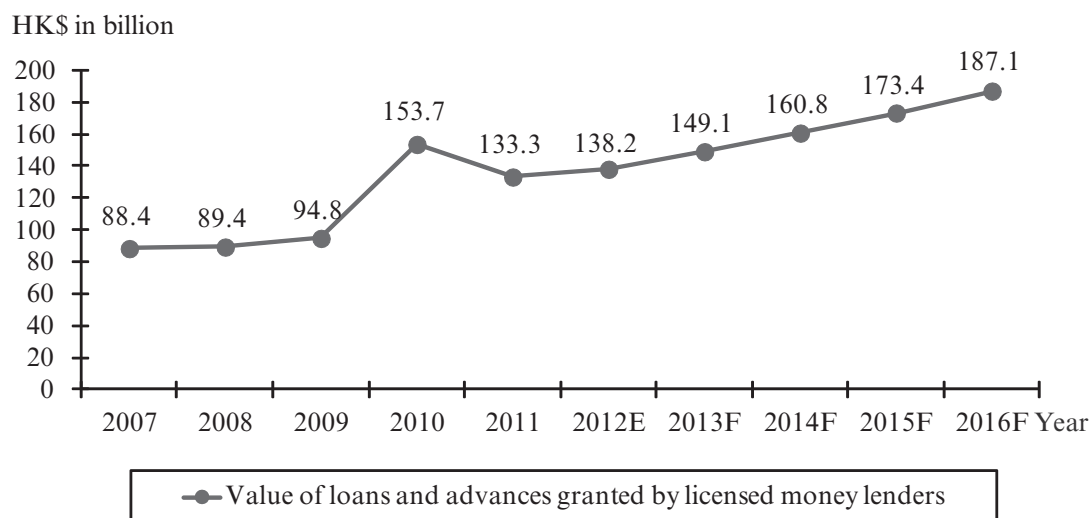


Figure 10. Total value of loans and advances granted by money lenders in Hong Kong from 2007 to 2016

Notes:

- (1) Value of loans and advances granted for secured loans and exclusive of pawn loans and unsecured loans.
- (2) Figures excluded authorised institutions.

Source: Ipsos Report

Due to the strong economic rebound that encouraged investment and spending, value of loans and advances granted by money lenders surged tremendously in 2010 at growth rate of about 62.1% with growth mainly from mortgage loans as the real estate market

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became active, especially in the first half of 2010. Market uncertainty as a result of the European debt crisis, coupled with tightening credit measures hindered consumers' confidence with reduced spending, particularly in the second half of 2011, value of loans and advances granted by money lenders fell back to about HK\$ 133.3 billion. With a total of about 829 money lenders in the market, the average value of loans granted by a money lender was about HK\$ 160.8 million in 2011. It is expected that the market to pick up in 2012 due to the tightening monetary policies in the authorised institutional sector. Under the assumption that there is no external shock to the Hong Kong economic in the next few years, it is expected that the value of loans and advances granted by money lenders to continue its growth momentum at a CAGR of about 7.9% from 2012 to 2016.

### Total Number of Mortgage Loans Granted in Hong Kong

Amongst all types of secured loans offered in the market, mortgage loan is the most common type of loan offered by both authorised institutions and money lenders in Hong Kong. It is estimated to account for over 90% of the total number of secured loans granted in the market in 2011. In 2011, there were about 134,600 mortgage loans granted, of which about 82.8% and 17.2% were granted by authorised institutions and money lenders respectively.

*Total Number of mortgage loans granted by authorised institutions  
in Hong Kong from 2007 to 2016*

| Year                       | Mortgage on residential real estate |       | Mortgage on other types of real estate (commercial, industrial real estates etc.) |       | Total no. of mortgage |       |
|----------------------------|-------------------------------------|-------|---|-------|-----------------------|-------|
|                            |                                     | Share |   | Share |                       | Share |
|                            | Number                              | (%)   | Number  | (%)   | Number                | (%)   |
| 2007                       | 98,600                              | 87.0  | 14,700  | 13.0  | 113,300               | 100.0 |
| 2008                       | 92,800                              | 86.0  | 15,100  | 14.0  | 107,900               | 100.0 |
| 2009                       | 96,600                              | 86.0  | 15,700  | 14.0  | 112,300               | 100.0 |
| 2010                       | 142,000                             | 87.0  | 21,200  | 13.0  | 163,200               | 100.0 |
| 2011                       | 95,900                              | 86.0  | 15,600  | 14.0  | 111,500               | 100.0 |
| CAGR from 2007 to 2011 (%) | -0.7                                |       | 1.5   |       | -0.4                  |       |
| 2012E                      | 97,200                              | 86.0  | 15,900  | 14.0  | 113,100               | 100.0 |
| 2013F                      | 98,900                              | 86.0  | 16,200  | 14.0  | 115,100               | 100.0 |
| 2014F                      | 100,500                             | 86.0  | 16,400  | 14.0  | 116,900               | 100.0 |
| 2015F                      | 102,200                             | 86.0  | 16,700  | 14.0  | 118,900               | 100.0 |
| 2016F                      | 104,000                             | 86.0  | 16,900  | 14.0  | 120,900               | 100.0 |
| CAGR from 2012 to 2016 (%) | 1.7                                 |       | 1.6   |       | 1.7                   |       |

*Note:* Number of mortgage loans granted by authorised institutions only and exclude unsecured loans.

*Source:* Ipsos Report

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CAGR of total value of residential mortgage loans granted by authorised institutions in Hong Kong from 2007 to 2011 = 7.0%



*Figure 11. Value of residential mortgage loans granted by authorised institutions in Hong Kong from 2007 to 2011*

Sources: Hong Kong Monetary Authority; Ipsos Report

Residential mortgage loan market in Hong Kong is one of the most advanced mortgage loan markets in Asia. In 2011, about 115,000 residential mortgage loans were granted in Hong Kong, of which about 83.3% and 16.7% were granted by authorised institutions and money lenders respectively. Within the authorised institutions, residential mortgage loans and non-residential mortgage loans accounted for about 86.0% and 14.0% of the total number of mortgage loans granted respectively in 2011. The total number of residential mortgage loans granted by authorised institutions in Hong Kong decreased at a CAGR of about -0.7% from 2007 to 2011 while value of residential mortgage loans granted increased at a CAGR of about 7.0% during the same period. On the other hand, there has been a slight increase in the number of mortgage loan on other types of real estate which increased at a CAGR of about 1.5% from 2007 to 2011. Despite the surge in the number of residential mortgage loans granted in 2010, the number of residential mortgage loans granted declined significantly in 2011 as a result of the higher mortgage rates and tightening credit measures. Regardless of the higher mortgage rate, it is expected that the high demand in residential housing by Hong Kong consumers will sustain the growth of residential mortgage loans at CAGR of about 1.7% from 2012 to 2016.

In 1999, the Hong Kong Mortgage Corporation introduced the Mortgage Insurance Programme with the aim to encourage home ownership in Hong Kong. According to the programme, if the amount of a residential mortgage loan exceeds 70% of the assessed value of the residential real estate or the present market value (whichever is lower), it is compulsory for a borrower to join the Mortgage Insurance Programme. As long as an application meets the relevant eligibility criteria, the bank can lend a mortgage loan of up to 90% loan-to-value ratio under the Mortgage Insurance Programme. The programme lowered the amount of down payment required

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by homebuyers and reduced the level of credit risk exposure for authorised institutions substantially. While the Mortgage Insurance Programme offered by banks in Hong Kong has been a preferred selection by home buyers since its launch, particularly first-time buyers, the amount of loans covered by the Mortgage Insurance Programme decreased about 36% in 2011 from a year earlier to HK\$26 billion shows buyers are having trouble borrowing from the banks the full amounts they need. Such is expected to fuel demand for residential mortgage loan provided by money lenders as being the second resort of home buyers.

*Note:* For the purpose of processing Mortgage Insurance Programme applications, any application with applicant(s) currently working outside Hong Kong (hereinafter “Overseas Income Applicant(s)”) and contributing over 50% of the verified household income (of the application) will not be accepted unless the applicant can provide any one of the following documents:

1. Justification with documentary proof, subject to the satisfaction of Hong Kong Mortgage Corporation, showing the employment relationship of the Overseas Income Applicant and a local employer;
2. Declaration from the Overseas Income Applicant confirming his/her immediate family member (spouse, parents and descendants only) is residing in Hong Kong.

### *Total Number of mortgage loans granted by money lenders in Hong Kong from 2007 to 2016*

| Year                       | Mortgage on residential real estate |                  | Mortgage on other types of real estate (commercial, industrial real estates etc.) |                  | Total no. of mortgage |                  |
|----------------------------|-------------------------------------|------------------|---|------------------|-----------------------|------------------|
|                            |                                     |                  |   |                  |                       |                  |
|                            | <i>Number</i>                       | <i>Share (%)</i> | <i>Number</i>   | <i>Share (%)</i> | <i>Number</i>         | <i>Share (%)</i> |
| 2007                       | 18,700                              | 82.0             | 4,100   | 18.0             | 22,800                | 100.0            |
| 2008                       | 18,600                              | 82.0             | 4,100   | 19.0             | 22,700                | 100.0            |
| 2009                       | 19,300                              | 83.0             | 4,000   | 17.0             | 23,300                | 100.0            |
| 2010                       | 28,400                              | 84.0             | 5,400   | 16.0             | 33,800                | 100.0            |
| 2011                       | 19,200                              | 83.0             | 3,900   | 17.0             | 23,100                | 100.0            |
| CAGR from 2007 to 2011 (%) | 0.7                                 |                  | -1.2  |                  | 0.3                   |                  |
| 2012E                      | 19,500                              | 83.0             | 4,000   | 17.0             | 23,500                | 100.0            |
| 2013F                      | 20,000                              | 83.0             | 4,100   | 17.0             | 24,100                | 100.0            |
| 2014F                      | 20,400                              | 83.0             | 4,200   | 17.0             | 24,600                | 100.0            |
| 2015F                      | 20,900                              | 82.0             | 4,500   | 18.0             | 25,400                | 100.0            |
| 2016F                      | 21,300                              | 83.0             | 4,500   | 17.0             | 25,800                | 100.0            |
| CAGR from 2012 to 2016 (%) | 2.2                                 |                  | 3.0   |                  | 2.4                   |                  |

*Note:* Number of mortgage loans granted by money lenders only and exclude unsecured loans.

*Source:* Ipsos Report

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Residential real estate loan and non-residential real estate loan accounted for about 83.0% and 17.0% of the total number of mortgage loans granted by money lenders respectively in 2011. The total number of residential mortgage loan granted by money lenders in Hong Kong grew at a CAGR of about 0.7% from 2007 to 2011 while mortgage on other types of real estate decreased at a CAGR of about -1.2% over the same period. Increase in the number of residential mortgage loans was mainly due to the relatively stringent requirements by banks that drove customers away to money lenders for alternative financing tools. Due to the same reason, demand for residential mortgage loans provided by money lenders, particularly for second mortgage loan is expected to sustain and drive growth in the segment at a CAGR of about 2.2% from 2012 to 2016, while non-residential mortgage loan grow at a CAGR of about 3.0% during the same period.

### **Factors Affecting the Growth and Development of Mortgage Loan Market in Hong Kong**

Government policies and regulations, economic conditions and the changing living standards are the key factors affecting the growth and development of mortgage loan market in Hong Kong.

#### *Government or relevant authorities' regulations: High, Positive Impact*

With the recovery of the Hong Kong economy, along with record low mortgage rates in 2009 to 2010 and an influx of investors from the PRC, residential real estate prices in Hong Kong have risen to a record high, reaching the peak level as in 1997. Several government measures have been launched by the Hong Kong government since 2010 to curb the booming residential real estate market and reduced speculations. This includes placement of restrictions on the loan-to-value ratio, stamp duty of up to 15% on home purchased and resold within 24 months, announcement of plans to increase land supply, resume the Home Ownership Scheme (approval of the sharing of positive credit data by local banks for mortgage applications etc. On 26 October 2012, the Hong Kong government further adjusted the rates of SSD and extended the holding period of residential property. On the same day, it also announced to introduce a BSD on residential properties which targeted at reducing home buying by foreign investors. With effect from 27 October 2012, any residential property acquired either by an individual or a company, and resold within 36 months, will be subject to the new rates of SSD, and any residential property acquired by an person except a Hong Kong Permanent Resident is charged at a flat rate of 15%, on top of the existing stamp duty and SSD, if applicable.

Although the new policies were successful in reducing transaction volume of residential properties from about 8,714 in October to 3,286 in December 2012, residential property prices remained high in Hong Kong, the new measures and announcements have lowered consumer sentiment in home purchases. In response to the government policies, authorised institutions are likely to impose a more conservative strategy towards residential mortgage loan by adopting stricter underwriting standards. They will also shift focus from residential mortgage loans to



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other personal lending products, which generate higher profit margins. Such will further raise the barriers of borrowing from banks and give rise to more opportunities amongst money lenders as a second resort.

*Changing living standards: Moderate, Positive Impact*

Strong economic growth and technology advances have boosted people's standard of living in the past decade. Not only housing, food and education are viewed as primary needs, but cars, recreation, smart phones are also increasingly viewed as necessities by many people as a reflection of their social status. In order to meet their needs, people are seeking to use consumer credit facilities, despite high or increasing interest rates. This has driven tremendous growth in credit card advances. According to the HKMA, the rollover amount (which reflects the amount of borrowing by customers using their credit cards) grew by 8.3% in the fourth quarter of 2011 while the delinquent amount increased from HK\$166 million in September to HK\$188 million in December in 2011. Increasing delinquent amount will raise the demand of credit card revolving loan services, particularly from money lenders.

*Economic conditions: Low, Positive Impact*

Benefited from strong economic rebound and low lending rates, amount of loans and advances rallied in 2010. With improved economic conditions, banks are looking for better profit margins in their loan business and subsequently raised mortgage rates in 2011. As a result, the total number of mortgage loans granted by authorised institutions decreased from about 163,000 to 111,500 from 2010 to 2011, while that for money lenders grew from about 33,800 to 23,100 for the same period.

With better employment opportunities and wages, a growing pool of consumers in Hong Kong meets income eligibility requirements for credit cards. Many banks have joined retailers to roll-out promotional events to attract new customers. Rapid credit approval, competitive rates and low initial payments will attract customers to borrow unsecured loans from banks, rather than money lenders.

### **Recent government measures to curb speculation in the real estates market**

The Hong Kong Government has recently introduced measures to curb speculation in the real estates market, including (i) the introduction of SSD on residential properties of all values at the point of resale if the properties are acquired and resold within a certain period of times after acquisition; and (ii) the introduction of BSD for residential properties acquired by any person, including companies, except a permanent resident of Hong Kong.

The introduction of SSD and BSD may deter the potential property buyers to acquire residential properties due to the increased transaction cost and thus lowering the liquidity of the real estate market.

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Real estates owners who wish to sell their real estates for their financing needs may face difficulties, since the lowered liquidity of the real estate market may lead to a decline in the prices of real estates, and those owners who wish to sell their real estates may as a result not be able to sell their real estates on terms acceptable to them.

The HKMA has also imposed tightening measures on the provision of mortgage loans by authorised institutions, including but not limited to the lowering of debt servicing ratio and the loan-to-value ratio for certain applications of mortgage loans. These tightening measures will bring difficulties to borrowers who wish to obtain financing from authorised institutions such as banks as they will need to meet additional requirements.

As such, borrowers who have difficulties selling their real estates by reason of the imposition of the aforesaid SSD and BSD or who do not meet the additional requirements will need to seek alternatives for obtaining financing.

### **Future Trends and Developments of Mortgage Loan Market in Hong Kong**

*Banks are expected to raise lending rate to compensate for the higher funding cost*

As the abundant liquidity in the banking system in Hong Kong in 2009 and 2010 being gradually drained out, along with the rising funding costs as a result of higher deposit rates and interbank fees in Hong Kong, mortgage loans offered by banks have become less profitable. To increase profit margin, banks in Hong Kong will pause their price competition and pass on some of the rising funding costs to customers by raising lending rate. Increase of lending rate by leading banks will encourage other banks to follow and re-price their mortgage loan services. Higher lending rate by Hong Kong banks is expected in the short-term, particularly in residential mortgage loan which makes borrowing from authorised institutions less attractive, hence, giving rise to mortgage loan offered by money lenders. Banks' mortgage rate is expected to surge to 4% by the end of 2012 from the current 2.4%.

*Money lenders in Hong Kong are expanding their business coverage to borrowers in the PRC*

Liquidity in Hong Kong is falling as tightening measures in the PRC have driven companies to borrow in Hong Kong. With the PRC government's initiative to tighten credit to curb inflation, prevent asset price bubble and credit crisis, many banks in the PRC have began tightening their credit measures in various degrees. In face of the increasing demand of borrowing and tightening measures in the PRC, money lenders in Hong Kong are eyeing on the potential opportunities in the PRC and are considering to expand their coverage in the PRC to fulfill the local customer demands.

*Entry from the PRC*

In face of credit tightening in the PRC as well as low reserve in Hong Kong, established money lenders based in the PRC have been eyeing on the market in Hong Kong with exploited need of liquidity. A number of Chinese enterprises may enter the

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mortgage loan market in Hong Kong, particularly for residential mortgage loan to fulfil the growing demand of mortgage loans from small-and-medium enterprises and young entrepreneurs.

### COMPETITIVE LANDSCAPE OF PAWN LOAN AND MORTGAGE MARKET IN HONG KONG

#### Competition situation on both pawn loan and mortgage loan market

The pawn loan market is highly fragmented while mortgage loan market (excluding authorised institutions) is dominated by the top 3 market players. Only about five pawn loan service operators possess both Pawnbrokers Licences and Money Lenders Licences in 2011.

There were about 202 pawnshops in Hong Kong in 2011. Most pawnshops are small and single-shop operators which dominate over 90% of the market. The number of employees within these small and single-shop operators are about 3–5 staff, while those for large operators have 10–15 staff. These pawnshops are evenly distributed in different districts in Hong Kong. Most of the pawn loan service operators on the Hong Kong Island are located in Wan Chai and Causeway Bay, while in Kowloon and New Territories, most are concentrated in Mongkok and Yau Ma Tei, and Tsuen Wan and Tuen Mun, respectively. Although the majority of customers for pawn loan are adults and returned customers, there has been a growing number of foreign domestic helpers and young population seeking for short-term financing in the past few years. Nonetheless, the market is dispersed with the operators focusing on their own business regardless of competitors' performance.

There were about 829 money lenders in Hong Kong in 2011, inclusive of pawn loan service providers possessing money lenders' licence. The mortgage loan market (excluding authorised institutions) is highly competitive and dominated by the top 3 market players. These competitors are mainly competing on marketing and advertisement, innovative services and after-sales service to acquire new customers and outstand in the market.

#### Factors of competition

##### *Marketing and advertisement*

Leading money lenders are competing aggressively on marketing and advertisement to raise their brand awareness. Placing of TV commercials in particular was the most common channel of competition. These TV commercials not only serve to raise brand awareness of the money lender, but also to educate customers the alternatives to solving personal financial difficulties. Some new entrants have also entered the competition in recent years in attempt to gain position in the market.

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### *Customer-oriented and after sales services*

Relatively lenient borrowing requirements compared to those of traditional banks have enabled money lenders to gain position in the mortgage loan market in Hong Kong in the past decade. In particular, flexible and convenient application processes are main factors to attract customers. Money lenders are increasingly providing tailor-made services to raise accessibility to their services, 24-hours hotline services, extended office hour, online chat services, one-to-one consultation services etc, were all means to increase service flexibility and reduce barriers of borrowings by borrowers.

### *Innovative services*

All leading money lenders have launched new services which they stress to be the first and the only services in town to better serve their customers. These service providers were striving to launch new services to differentiate themselves in the market, with the premises of being customer-oriented.

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### Ranking of Pawn Loan Service Operators in Hong Kong

*Ranking of pawn loan service operators in Hong Kong in 2011*

The top 2 pawn loan service operators accounted for about 11% of the total number of pawnshops in Hong Kong and 16.0% of the total value and advances granted in 2011.

| Rank   | Name of Company | Number of<br>Branches | Value of loans<br>and advances<br>granted<br>(HK\$ million) | Share of Loan<br>and advances<br>granted<br>(%) |
|--------|-----------------|-----------------------|---|---|
| 1      | Our Group       | 12                    | 513   | 9.4   |
| 2      | Competitor A    | 11                    | 358   | 6.6   |
| 3      | Competitor B    | 2                     | 70  | 1.3   |
| 4      | Competitor C    | 1                     | 32  | 0.6   |
| 5      | Competitor D    | 1                     | 29  | 0.5   |
| Others |                 | <u>175</u>            | <u>4,436</u>  | <u>81.6</u>                                     |
| Total  |                 | <u><u>202</u></u>     | <u><u>5,438</u></u>   | <u><u>100.0</u></u>                             |

*Pawn loan service providers in Hong Kong in 2011*

*Notes:*

- (1) Ranking includes pawnshops only.
- (2) Value of loans and advances granted represented the amount of pawn loans, including the loans granted under Money Lenders Licence.

*Source:* Ipsos Report

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### *Ranking of pawn loan service operators possessing both Pawnbrokers Licences and Money Lenders Licences in 2011*

Of the 150 pawn loan service operators in Hong Kong, only five of them also engage in mortgage loan business in 2011. Our Company and another competitors are the pawn loan service operators in Hong Kong who engage in both pawn loan and mortgage loan business.

| <b>Rank</b> | <b>Name of Company</b> | <b>Number of Branches</b> | <b>Value of loans and advances granted<br/>(HK\$ million)</b> |
|-------------|------------------------|---------------------------|---|
| 1           | Our Group              | 12                        | 551   |
| 2           | Competitor A           | 11                        | 388   |
| 3           | Competitor B           | 2                         | 84  |
| 4           | Competitor C           | 1                         | 38  |
| 5           | Competitor D           | 1                         | 33  |

*Notes:*

- (1) 5 pawn loan service operators possess both Pawnbrokers Licences and Money Lenders Licences.
- (2) Value of loans and advances granted represented the amount of pawn loans and mortgage loans, including the loans granted under Money Lenders Licence.

*Source:* Ipsos Report

Valuation experience and risk management are the key factors for successful pawn loan service operators and money lenders in Hong Kong. In the pawn loan business, as loans are granted at the estimated resale value of the pawned goods, the valuation experience of employees becomes critical since they need to ensure that the pawned goods can still be resold at the approximate market rate, in case customers do not redeem their collaterals. This translates to effective risk management in the mortgage loan market, especially during economic hardships when customers are rejected from banks in respect of their mortgage loan applications and turn to money lenders.

On the other hand, sound financial capability or stable source of funding is also key to the development of money lenders. The leading money lenders provide various services including both secured and unsecured loans which allow them to diversify their portfolio and maintain interest rate margins. Competitive interest rate is another key differentiator that enables the top money lenders to attract customers, who have failed to meet the banks' borrowing requirements.

With the recent tightening credit measures, especially those by banks, business opportunities have been presented to money lenders in mortgage loans, the deterioration of the credit market and the slowing down of the economy in 2012 will induce higher credit risk in the potential borrowers. Therefore, while opportunities exist, money lenders are expected to adopt more cautious credit approval on each loan application.

### **Market Drivers and Entry Barriers of Pawn Loan and Mortgage Loan Industries in Hong Kong**

The tightening credit measures by banks as a result of government policies and increased consumer sentiment will drive the growth and development of the pawn loan and mortgage loan industries while strong cash flow and extensive valuation experience of pawned items posts huge barriers for new entrants.

#### *Market drivers*

- The tightening measures of banks in Hong Kong will drive greater competition in the mortgage loan market as banks increase their lending rate which will further raise the barriers of borrowing from banks.
- Strong economic rebound in Hong Kong will restore consumer sentiment and drive increased spending. Such is expected to drive demand in money borrowing and sustain growth in the pawn loan and mortgage loan market.
- The changing lifestyle of Hong Kong consumers along with technology advancement will raise demand for luxury products as a reflection of one's social status. Such would increase individual spending as well as give rise to new items for pawn loan, such as luxury items and high-tech devices which have high resale value.
- Aggressive marketing and advertisement by money lenders will raise awareness of alternative financial tools and raise demand for mortgage loan.

#### *Entry barriers*

- Although there is no minimum capital requirement for money lenders in Hong Kong, strong cash flow and financial capability are still fundamental for the pawn loan service operators and money lenders. The nature of non-deposit taking company for pawn loan and mortgage loan industry has limited pawn loan service operators and money lenders' potential to attract capital, and hence, posted barriers for new entrants.
- Increasing rental and wage in Hong Kong are placing pressure on the development of pawnshops. The rental cost of office had increased year-on-year in the fourth quarter of 2010 and 2011 at about 34.7% and -1.9% respectively. The rental cost of retail space grew significantly year-on-year in the fourth quarter of 2010 and 2011 at about 12.0% and 23.2% respectively. The minimum wage regulation has been effective from 1 May 2011, further pushed the operation cost up.
- Majority of pawnshops has over 40 years of experience in the industry. Extensive experience of employees in the valuation of pawned items sets high barriers for new entrants who have insufficient knowledge about the business.