

## FINANCIAL PERFORMANCE

## profit and loss account

SUMMARY OF FINANCIAL PERFORMANCE (HK\$M)	2000	1999
Operating profit before provisions	11,540	11,065
Profit on ordinary activities before tax	11,675	9,784
Profit attributable to shareholders	10,014	8,307
Earnings per share (HK\$)	5.24	4.35

Hang Seng Bank Limited (the Bank) and its subsidiary companies (Hang Seng) reported a profit attributable to shareholders of HK\$10,014 million for 2000, an increase of 20.5 per cent compared with 1999, and for the first time exceeding the HK\$10 billion level. Earnings per share of HK\$5.24 were 20.5 per cent higher than in 1999.

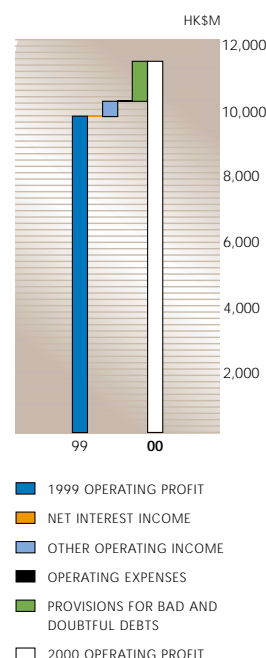
Operating profit before provisions increased by 4.3 per cent to HK\$11,540 million, mainly due to encouraging growth in other operating income, stable net interest income and lower operating expenses. Operating profit rose by 17.6 per cent to HK\$11,344 million, benefiting from a substantial reduction in provisions for bad and doubtful debts. Profit before tax amounted to HK\$11,675 million, 19.3 per cent higher than 1999, with an increase in profit on the disposal of long-term investments and a surplus on property revaluation which was credited to the profit and loss account (representing the reversal of revaluation deficits on the same properties which had been previously charged to profit and loss).

## economic profit

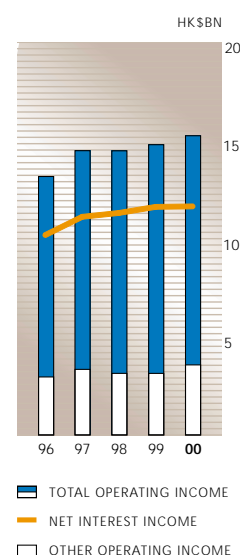
In implementing its Managing for Value strategy, Hang Seng has adopted economic profit as a value-based performance measurement. This is to align the objectives of Hang Seng's management to that of its shareholders. Economic profit is calculated from profit after tax, adjusted for non-cash items, and takes into account the cost of capital invested by Hang Seng's shareholders. For this purpose, the cost of capital is currently estimated to be 15.0 per cent.

Economic profit increased by HK\$2,540 million, or 84.9 per cent, to HK\$5,532 million, the combined effect of an increase of 19.7 per cent in the return on invested capital and a reduction of 16.3 per cent in the cost of capital. The improvement in the return on invested capital (defined as profit after tax adjusted for non-cash items) reflected the satisfactory operating results of the year. Average invested capital fell as a result of the distribution of the special interim dividend in November 1999 to achieve more efficient use of capital, leading to the reduced charge for the cost of capital.

## OPERATING PROFIT ANALYSIS



## TOTAL OPERATING INCOME



HK\$M	2000	%	1999	%
Average invested capital	30,259		36,229	
Return on invested capital*	10,068	33.3	8,408	23.2
Cost of capital	(4,536)	(15.0)	(5,416)	(15.0)
Economic profit	5,532	18.3	2,992	8.2

\*Return on invested capital represents profit after tax adjusted for non-cash items.

#### net interest income

NET INTEREST INCOME (HK\$M)	2000	1999
Interest income	31,913	28,072
Interest expense	(20,222)	(16,405)
Net interest income	11,691	11,667
Average interest-earning assets	435,759	406,113
Net interest spread (% p.a.)	2.19	2.36
Net interest margin (% p.a.)	2.68	2.87

Net interest income was held broadly in line with last year, with a slight increase of HK\$24 million, or 0.2 per cent. Average interest earning assets grew by HK\$29.6 billion, or 7.3 per cent, to HK\$435.8 billion. The net interest margin, however, fell by 19 basis points to 2.68 per cent due to the 17 basis points fall in net interest spread to 2.19 per cent and a 2 basis points reduction to 0.49 per cent in the contribution from net free funds.

The reduction in net interest spread was attributable to the adverse effect of the continued fall in the mortgage portfolio yield and the fall in the average advances to deposits ratio from 54.3 per cent to 52.7 per cent. Together, these factors outweighed the benefits of the growth in lower cost savings deposits, improvements in the spread earned from time deposits and the widening of the BLR/HIBOR gap. The average portfolio yield of residential mortgages (excluding those under the Government Home Ownership Scheme and Staff Housing Loan Scheme) fell from 49 basis points above BLR in 1999 to 26 basis points below BLR in 2000 as a result of intense price competition.

The contribution from net free funds declined due to the reduction in average balances following the payment of the special interim dividend of HK\$7.8 billion in November 1999, and despite an improvement in average yield due to higher market interest rates.

#### other operating income

Other operating income increased by HK\$433 million, or 13.8 per cent, compared with 1999. Net fees and commissions rose substantially by HK\$521 million, or 33.6 per cent, reflecting the encouraging growth in income from wealth management initiatives including securities broking and related services, sale of retail investment funds and commissions from life insurance products. There were also increased contributions from credit facilities, card services and trade finance. Dealing profits decreased by HK\$55 million, or 9.4 per cent, affected by lower foreign exchange income and a small loss in securities and other

trading activities. Other operating income fell by HK\$25 million, or 3.8 per cent, due to a decrease in general insurance underwriting profits.

#### operating expenses

Operating expenses were reduced by HK\$18 million, or 0.5 per cent, although there were significant new investments in IT and business development. Staff costs decreased by HK\$147 million, or 6.7 per cent, mainly as a result of careful headcount control. Depreciation increased by HK\$10 million, or 2.6 per cent, compared with 1999. Premises and equipment expenses increased by HK\$34 million, or 4.6 per cent, mainly in IT costs, although repair and maintenance, rates and utilities expenses fell. Other operating expenses increased by HK\$85 million, or 19.4 per cent, mainly attributable to increases in marketing expenditure. The cost:income ratio improved to 24.4 per cent (25.3 per cent for 1999), the lowest since this ratio was first published in 1989.

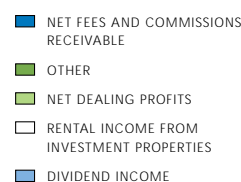
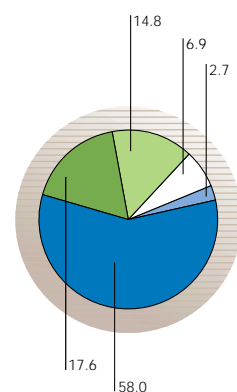
#### provisions for bad and doubtful debts

NET CHARGE TO PROFIT AND LOSS ACCOUNT (HK\$M)	2000	1999
Net charge/(release) for bad and doubtful debts		
Specific	199	1,427
General	(3)	(8)
Total	196	1,419
Average gross advances to customers	214,662	201,121
Net charge for bad and doubtful debts as a percentage of average gross advances to customers		
Specific	0.1%	0.7%
General	-	-
Total	0.1%	0.7%

The charge for bad and doubtful debts decreased significantly by HK\$1,223 million, or 86.2 per cent, to HK\$196 million compared with last year. The net charge for specific provisions fell by HK\$1,228 million to HK\$199 million, the combined effect of a substantial reduction in new and additional provisions made and increases in releases of provisions and recoveries from doubtful accounts. There was a net release of HK\$3 million from general provisions, with provisions of HK\$122 million made against loan growth for the year and a release of HK\$125 million from the additional general provision of HK\$250 million made in 1997. In view of the slowdown in the US economy and its possible implications for the Hong Kong economy, the balance of the additional provision of HK\$125 million has been transferred to the general provisions for bad and doubtful debts.

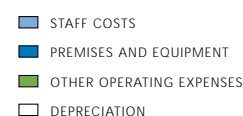
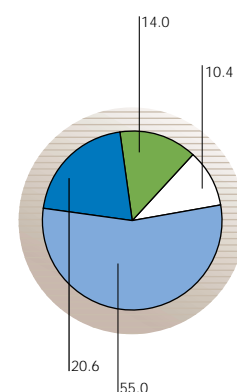
#### OTHER OPERATING INCOME FOR 2000

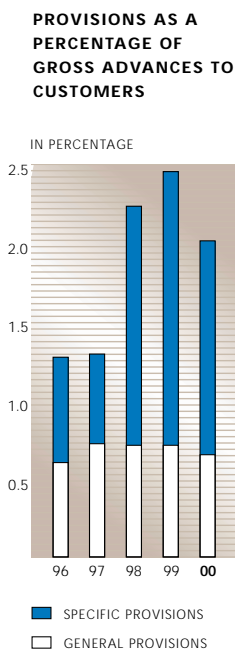
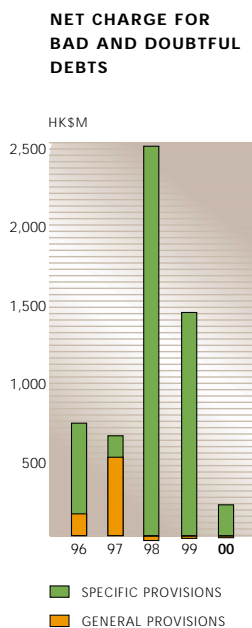
IN PERCENTAGE



#### OPERATING EXPENSES FOR 2000

IN PERCENTAGE





ADVANCES TO CUSTOMERS AND PROVISIONS (HK\$M)	2000	1999
Gross advances to customers*	221,973	202,244
Specific provisions	(3,017)	(3,522)
General provisions	(1,438)	(1,441)
Advances to customers**	217,518	197,281
Gross non-performing advances*	7,434	8,658
Non-performing advances* as a percentage of gross advances to customers*	3.3%	4.3%
Provisions as a percentage of gross advances to customers*		
Specific provisions	1.36%	1.74%
General provisions	0.65%	0.71%
Total provisions	2.01%	2.45%
Specific provisions as a percentage of gross non-performing advances*	40.6%	40.7%

\*After deduction of interest in suspense.

\*\*After deduction of interest in suspense and provisions.

Gross non-performing advances (after deduction of interest in suspense) fell by HK\$1,224 million, or 14.1 per cent, compared with the end of 1999, due to a combination of write-offs and the upgrading of certain rescheduled advances and doubtful accounts to performing status. The percentage of gross non-performing advances to total gross advances to customers was 3.3 per cent, a reduction of one percentage point compared with the end of 1999.

#### profit on tangible fixed assets and long-term investments

Profit on disposal of tangible fixed assets and long-term investments rose by HK\$143 million to HK\$248 million compared with last year, mainly from the disposal of locally-listed equities.

#### surplus on property revaluation

The Bank's premises and investment properties were revalued by HSBC Property (Asia) Limited, which is a fellow subsidiary company of the Bank, as at 30 November 2000. The valuations were carried out by qualified valuers who are members of the Hong Kong Institute of Surveyors. The basis of the valuation for premises was open market value for existing use. The basis of the valuation for investment properties was open market value. The property revaluation has resulted in a surplus on HK\$612 million, of which HK\$584 million has been credited to the Bank's revaluation reserves at 31 December 2000. The remaining amount of HK\$28 million has been credited to the profit and loss account. This represented the reversal of revaluation deficits of the same properties which had been previously charged to the profit and loss account when their market values fell below depreciated historical costs.