

The global economy nosedived last year and the domino effect triggered by the terrorist attacks on the United States was especially far-reaching. The major economies had yet to be nursed back to health as we entered the year of 2002. The US economy, as the locomotive of the market at large, appears to be rather unstable. The spell of cloudiness will therefore take some more time to dissipate.

The local economy, which is still under the influence of last year's sluggishness, has remained in the doldrums so far this year. Although the territory's gross domestic product for the first quarter of this year rose slightly by 0.3 percent compared with that of the previous quarter, unemployment rate still tends to be on the rise. The latest number of unemployed persons reached 275,000, translating into an unemployment rate of 7.8 percent, which is rare in recent times. This has a direct adverse effect on investment activities and consumption sentiments. The property and the stock markets – the two major pillars of the local economy – are fluctuating, leaving a lot to be desired. The banking and financial industries are experiencing ever-mounting difficulties for lack of avenues to use their capital. And the situation regarding loan delinquencies, as well as bad and doubtful debts, has yet to improve. Those who work in the trade are therefore not optimistic about this year's earnings prospects.

The Bank's unaudited, consolidated results for the first half of 2002 dropped in comparison with those for the previous corresponding period. Net interest income fell 9.28 percent to HK\$375.368 million. Operating profit before provisions sank 7.97 percent to HK\$257.931 million. Provisions for bad and doubtful debts increased 12.01 percent to HK\$57.457 million. Profit attributable to shareholders amounted to HK\$161.038 million, a drop of 20.40 percent. As of 30 June 2002, total customers' deposits rose 3.17 percent to HK\$33.63 billion compared with the previous corresponding figure. Total loans and advances to customers (after provisions for bad and doubtful debts) increased 7.03 percent to HK\$19.168 billion. Total assets edged up slightly by 1.20 percent to HK\$40.392 billion. As of 30 June 2002, capital adequacy ratio dropped 5.88 percent to 20.96 percent, while average liquidity ratio for the first half of 2002 decreased 9.93 percent to 53.44 percent. Loan-to-deposit ratio, as of 30 June 2002, stood at 49.89 percent, an increase of 3.85 percent against last year's corresponding ratio. The various figures mentioned above are indicative of the good progress made in respect of the use of the Bank's capital. After more than a year's contraction, loans and advances have grown some 7 percent for the first time. The reduction in profit is due mainly to the general state of the economy which has yet to recover swiftly as originally expected. Furthermore, some of the Bank's borrowing customers, who have provided collateral to secure their loans, have experienced short-term cash flow problems and defaulted on a number of their repayments of principal and interest. Although such customers are still fundamentally sound, the market value of their collateral has changed somewhat. More provisions have been called for under the circumstances to adequately cover bad and doubtful debts, hence the increase over last year's provisions. Considering the extent of satisfactory progress made thus far in the wake of the Bank's active debt collection efforts, it is expected that the situation can be improved with some clawbacks by the end of this year.

As far as board composition changes are concerned, I stepped down as your Managing Director immediately after the Bank's annual general meeting on 25 April 2002. I, however, stayed on as your Executive Chairman. Mr Liu Lit Chi was promoted at the same time from Deputy Managing Director to Managing Director and Chief Executive Officer. Mr Don Tit Shing Liu, Executive Director, was then appointed the Bank's Deputy Chief Executive Officer as well. Dr Liu Lit Chung resigned as a Non-executive Director of the Bank on 11 July 2002, and Mr Christopher Kwun Shing Liu was appointed a Non-executive Director of the Bank on that same day. I would like to take this opportunity to not only thank Dr Liu for his contributions to the Bank during his term of office, but also welcome those who have assumed their new positions. I expect that we will continue to forge ahead by cooperating closely with one another.

Although the current state of the global economy is murky and the financial market mercurial, the fundamentals are still strong. Corporate accounting scandals in the United States may have a dampening effect in the short term. Once the various reforms proposed by the regulators are implemented, the operations concerned can be expected to return to the right track. The Hong Kong Special Administrative Region Government launched the accountability system for principal officials on 1 July 2002. It is hoped that this will usher in a new economic-political regime for Hong Kong. Moreover, the softening of the US currency in the international market will favour the local economy by facilitating the growth of exports.

As far as the performance of the local banking sector is concerned, despite fierce competition, it still managed to keep up with the times in the midst of numerous cyclical economic ordeals. The Bank will work hard to seek the best possible return for its shareholders by continuing to make judicious use of its capital, growing quality loan portfolios and devoting itself to the development of new products.

By Order of the Board

Liu Lit Man

Executive Chairman

19 August 2002