

# ABF Hong Kong Bond Index Fund Interim Report 2009



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# Investment Adviser's Report

## **ABF Hong Kong Bond Index Fund**

The Asian Bond Fund was able to deliver a total return of 7.74 percent for the six month period ending January 2009, thanked to the declining interest rates during the period.

The stunning collapse of Lehman Brothers in mid-September sent shockwaves throughout the global financial markets. In coordination with the other major central banks, the U.S. Federal Reserve decisively cut the Fed funds rates and hastily instituted numerous financial measures to stabilize the financial markets. Over the July to January period, the yield on the 2-year benchmark note fell from 2.50 percent to 0.95 percent, while the yield on the ten-year benchmark note fell to 2.84 percent from 3.95 percent. The dramatic interest rate cuts and extremely loose liquidity conditions precipitated an extensive bullish steepening of the U.S. Treasury yield curve with the spread between the two-year and ten-year benchmark notes widening to 262 bps in mid-October. Following the easing of Fed funds rate to a range of 0 percent to 0.25 percent, the long end of U.S. Treasury yield curve rallied on the back of both economic recession fears and receding inflation expectations. The spread between the two-year and ten-year U.S. Treasury yield narrowed considerably to 190 bps by January 2009.

Hong Kong dollar interest rates also posted stellar performance during this period; bullish steepening trend was seen in both government and swap curves. Global interest rate easing, the rally in U.S. Treasuries and extreme liquidity injection provided by the HKMA all conspired to drive local rates lower. More importantly, the HKMA amended the calculation method on the Base Rate in October by adjusting calculation method from U.S. Federal Fund Rate (FFR) plus 150 bps to FFR plus 50 bps. As a result, an additional 100 bps of easing was realized. The Hong Kong dollar swap rates outperformed U.S. swap rates where the one- and five-year Hong Kong dollar swap rates fell by -168 and -196 basis points versus U.S. swaps falling -128 and -164 basis points respectively. Government exchange funded bills and notes (EFB/EFNs) and Hong Kong swaps moved more or less by the same magnitude over the reporting period.

As problems of the global financial sector escalated, global and local liquidity conditions practically froze with the 1-month HIBOR spiking up from 1.88% to 4.99%. In response, the HKMA introduced both liquidity assistance measures to ease inter-bank liquidity and deposit protection programs to boost confidence. By January, Hong Kong's inter-bank liquidity conditions steadily improved in unison with the stabilization in the global stage.

During the reporting period, massive global de-leveraging precipitated the heavy demand for Hong Kong dollars and the extensive unwinding of long Hong Kong dollar forward hedges. As a result, the 12-month Hong Kong dollar TT forward discount narrowed from -330 pips to -30 pips, while the spot USD/HKD exchange rate threatened to breach the 7.75 level and forced the HKMA to buy U.S. Dollars on many occasions to enforce the lower barrier of the Two-way Convertibility band. The Aggregate Balance exploded from HKD 4.7 billion in July 2008 to HKD157.5 billion by January 2009.

As global economic condition worsened, local economic conditions have rapidly deteriorated as well. After peaking in July at 6.3%, year-on-year inflation deflated quickly to 3.1% in January. The unemployment rate steadily increased to 4.6% in January after reaching a long-time low of 3.2 percent in August. Amid the ongoing economic malaise, we expect shorter maturity Hong Kong interest rates to remain low, alongside with the U.S. in the short run. However, the announcement of the massive new bond issuance program by the Hong Kong government will exert upward pressure on longer maturity Hong Kong interest rates going forward.

# Statement of Assets and Liabilities

## ABF Hong Kong Bond Index Fund

	31 January 2009 HKD	31 July 2008 HKD
<b>ASSETS</b>		
Investments	2,180,989,633	2,360,041,133
Accounts receivable	57,360,601	89,868,632
Cash at banks	6,374,958	3,353,623
	<hr/>	<hr/>
	2,244,725,192	2,453,263,388
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<b>LIABILITIES</b>		
Accounts payable	695,484	21,344,012
Distribution payable	41,682,542	51,244,442
	<hr/>	<hr/>
	42,378,026	72,588,454
	<hr/>	<hr/>
<b>TOTAL NET ASSETS</b>	2,202,347,166	2,380,674,934
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<b>Number of units outstanding</b>	20,946,001	23,946,001
	<hr/>	<hr/>
<b>Net asset value per unit</b>	105.14	99.42
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# Portfolio Statement

## ABF Hong Kong Bond Index Fund

as at 31 January 2009

	Holdings	Market value HKD	% of NAV		Holdings	Market value HKD	% of NAV
<b>Bonds</b>				HK GOVERNMENT BOND			
EUROFIMA 4.18% EMTN				7205 3.61% 28MAY2012	1,850,000	1,999,772	0.09
8JUN2015	46,000,000	51,148,877	2.32	HK GOVERNMENT EX FD			
HK GOVERNMENT				NT 1006 7.31% 21JUN10	24,300,000	26,548,357	1.21
4.49% 26NOV2012 7211	61,000,000	68,378,700	3.11	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1106 6.13% 20JUN11	67,600,000	75,947,904	3.45
1012 7.01% 6DEC2010	31,300,000	34,866,948	1.58	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1112 5.92% 5DEC11	68,500,000	77,892,898	3.54
1412 3.51% 8DEC2014	10,000,000	11,142,489	0.51	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1206 5.8% 19JUN12	92,800,000	107,116,701	4.86
3.56% 25JUN2018	45,000,000	52,570,125	2.39	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1212 4.5% 4DEC12	65,800,000	73,803,359	3.35
3.63% 19DEC2011 5112	24,000,000	25,773,919	1.17	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1306 3.73% 5JUN13	55,450,000	61,040,979	2.77
3.78% 6DEC2016 1612	22,000,000	25,567,901	1.16	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1312 4.32% 2DEC13	9,400,000	10,676,374	0.49
3.97% 19SEP2011 5109	44,000,000	47,452,236	2.16	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 1406 4.82% 2JUN14	16,500,000	19,358,671	0.88
4.13% 22FEB2013 7302	41,500,000	46,140,393	2.10	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 7005 3.19% 28MAY10	18,300,000	18,932,357	0.86
4.33% 7DEC2015 1512	12,000,000	14,183,197	0.64	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 7011 3.95% 26NOV10	55,550,000	58,772,555	2.67
4.83% 7JUN2016 1606	15,500,000	19,017,466	0.86	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 7102 3.27% 25FEB11	84,950,000	89,255,572	4.05
5003 3.52% 22MAR2010	5,000,000	5,170,950	0.24	HK GOVERNMENT EX FD			
HK GOVERNMENT BOND				NT 7105 4.5% 27MAY11	96,800,000	104,862,143	4.76
5012 4.26% 20DEC2010	41,300,000	44,010,560	2.00	HK GOVERNMENT NOTE			
HK GOVERNMENT BOND				1912 7.47% 8DEC2009	45,300,000	48,023,436	2.18
5912 2.69% 21DEC2009	13,550,000	13,824,387	0.63	HK GOVERNMENT SER			
HK GOVERNMENT BOND				1506 3.5% 22JUN2015	31,500,000	35,332,696	1.60
7002 3.8% 26FEB2010	65,550,000	67,872,109	3.08	HK GOVERNMENT SER			
HK GOVERNMENT BOND				5009 3.79% 20SEP2010	40,700,000	42,757,589	1.94
7008 3.92% 20AUG2010	68,550,000	72,006,634	3.27	HK GOVERNMENT SER			
HK GOVERNMENT BOND				7208 4% 27AUG2012	40,000,000	43,933,112	2.00
7108 3.93% 26AUG2011	38,150,000	41,049,614	1.86	HK MORTGAGE CORP			
HK GOVERNMENT BOND				3.8% 6APR2011 EMTN	1,000,000	1,041,342	0.05
7111 3.12% 25NOV2011	13,550,000	14,343,961	0.65	HKSAR GOVERNMENT			
HK GOVERNMENT BOND				5.125% 23JUL2019	12,500,000	15,701,668	0.71
7202 3.14% 24FEB2012	72,550,000	77,079,812	3.50	HONG KONG (GOVT OF)			
				1.61% 10DEC2018	42,000,000	41,887,650	1.90

# Portfolio Statement

## ABF Hong Kong Bond Index Fund

as at 31 January 2009

	Holdings	Market value HKD	% of NAV
HONG KONG (GOVT OF)			
1.67% 19DEC2013	25,000,000	25,344,083	1.15
HONG KONG (GOVT OF)			
1.77% 17MAY2010	15,000,000	15,235,650	0.69
HONG KONG (GOVT OF)			
2.71% 20FEB2023	23,000,000	26,060,150	1.18
HONG KONG (GOVT OF)			
3.52% 5DEC2017	26,000,000	30,086,030	1.37
HONG KONG (GOVT OF)			
4.65% 29AUG2022	26,550,000	36,121,142	1.64
HONG KONG (GOVT OF)			
4.85% 27JUN2017	13,000,000	16,318,640	0.74
HONG KONG MTG CORP			
3.8% 6APR2011	32,500,000	33,842,250	1.54
HONG KONG MTG CORP			
4.1% 9JAN2012 MTN	5,500,000	5,805,632	0.26
INTER-AMERICAN DEV BANK			
4.2% 24MAR2014	36,000,000	39,226,003	1.78
KOWLOON-CANTON RAILWAY			
4.65% 10JUN2013	10,000,000	10,817,793	0.49
MTR CORP (C.I.) 4.15%			
13NOV2009	27,000,000	27,542,700	1.25
MTR CORP (C.I.) 4.28%			
6JUL2020 EMTN	8,000,000	9,265,290	0.42
MTR CORP (C.I.) 4.5%			
11MAY2015	33,500,000	37,317,526	1.69
MTR CORP (C.I.) 4.6%			
3JUN2013	25,500,000	27,828,150	1.26
MTR CORP (C.I.) 4.75%			
11MAY2020	66,000,000	79,312,735	3.60
MTR CORP (C.I.) 5.25%			
21MAY2013	500,000	558,500	0.03
NORDIC INVESTMENT			
BANK 3.77% 12JUL2010	72,000,000	73,821,946	3.35
<b>Total Investments</b>		2,180,989,633	99.03
<b>Other Net Assets</b>		21,357,533	0.97
<b>Total Net Assets</b>		2,202,347,166	100.00
<b>Total Cost of Investment</b>		2,056,355,326	

# Statement of Movements in Portfolio Holdings

## ABF Hong Kong Bond Index Fund

	<b>% of NAV 31 January 2009</b>	<b>% of NAV 31 July 2008</b>
<b>Bonds</b>	99.03	99.13
<b>Total Investments</b>	99.03	99.13
<b>Other Net Assets</b>	0.97	0.87
<b>Total Net Assets</b>	100.00	100.00

# Performance Record

## ABF Hong Kong Bond Index Fund

	Net asset value per unit	
	Lowest HKD	Highest HKD
2007	96.10 <sup>(a)</sup>	100.69 <sup>(a)</sup>
2008	96.32 <sup>(a)</sup>	105.99 <sup>(a)</sup>
1 August 2008 to 31 January 2009	99.69 <sup>(a)</sup>	108.45 <sup>(a)</sup>
	<b>31 January 2009 HKD</b>	<b>31 July 2008 HKD</b>
<b>Total net asset value</b>	2,202,347,166	2,380,674,934
<b>Net asset value per unit</b>	105.14	99.42

In accordance with chapter 8.6(l) of the Code on Unit Trusts and Mutual Funds, the Trust is required to provide a comparison of the Trust performance and the actual index performance over the relevant period.

	<b>6 months ended 31 January 2009</b>	<b>12 months ended 31 July 2008</b>
ABF Hong Kong Bond Index Fund	7.74% <sup>(a)(b)</sup>	7.50% <sup>(a)(b)</sup>
iBoxx ABF Hong Kong Index	8.02% <sup>(c)</sup>	7.79% <sup>(c)</sup>

- (a) The net asset value presented in the financial statements and that quoted for pricing and performance calculation purposes ("Dealing NAV") are different due to the principles for calculating the Dealing NAV as set out in the prospectus being different from that required for financial reporting purposes under Hong Kong Financial Reporting Standards. The following reconciliation provides details of these differences:

	<b>As at 31 January 2009 HKD</b>	<b>As at 31 July 2008 HKD</b>
Net asset value as reported in the financial statements	2,202,347,166	2,380,674,934
Adjustments for different bases adopted by the Trust in arriving at the Dealing NAV:		
– Deferred formation expenses	480,326	645,214
Dealing NAV	<u>2,202,827,492</u>	<u>2,381,320,148</u>



# Performance Record

## **ABF Hong Kong Bond Index Fund**

The statistics of lowest and highest net asset value per unit and the performance of the Trust disclosed above are calculated accordingly to the Dealing NAV calculated on the relevant Dealing Days of the Trust.

- (b) The Trust's returns are calculated on NAV-to-NAV basis (Dealing NAV on the relevant Dealing Day), dividends reinvested.
- (c) The benchmark returns are stated on a total return basis. Unlike the Trust, the benchmark returns do not include the impact of Trust expenses or Trust transaction costs.

Investor should note that investment involves risk and past performance may not be indicative of future performance. Investors should refer to the Trust's prospectus before making any investment decision.

# Distribution Disclosure

## ABF Hong Kong Bond Index Fund

	<b>Date of Ex-distribution</b>	<b>Date of Payment</b>	<b>Distribution Per Unit HKD</b>	<b>Total Distribution HKD</b>
2009 Interim Distribution	29 January 2009	9 February 2009	1.99	41,682,542
2008 Final Distribution	30 July 2008	8 August 2008	2.14	51,244,442
2008 Interim Distribution	30 January 2008	12 February 2008	1.76	42,144,962

# Administration

## **ABF Hong Kong Bond Index Fund**

### **Manager and Listing Agent**

HSBC Investment Funds (Hong Kong) Limited  
HSBC Main Building  
1 Queen's Road Central  
Hong Kong

### **Directors of the Manager**

Po Yee Lam  
Ngar Yee Louie  
Rudolf Eduard Walter Apenbrink  
Edmund Richard Stokes  
Patrice Pierre Henri Conxicoeur  
(appointed on 1 August 2008)  
Ayaz Hatim Ebrahim (appointed on 13 August 2008)  
King Lun Au (resigned on 1 August 2008)

### **Members of Supervisory Committee**

Anthony Yuen  
Andrew Malcolm  
Carmen L K Chu  
Stephen Y L Cheung

### **Investment Adviser**

HSBC Global Asset Management (Hong Kong) Limited  
HSBC Main Building  
1 Queen's Road Central  
Hong Kong

### **Investment Sub-Adviser**

Halbis Capital Management (Hong Kong) Limited  
HSBC Main Building  
1 Queen's Road Central  
Hong Kong

### **Trustee, Administrator, Custodian, Receiving Agent and Registrar**

HSBC Institutional Trust Services (Asia) Limited  
HSBC Main Building  
1 Queen's Road Central  
Hong Kong

### **Processing Agent**

HK Conversion Agency Services Limited  
2/F Vicwood Plaza  
199 Des Voeux Road Central  
Hong Kong

### **Legal Adviser**

Clifford Chance  
29th Floor, Jardine House  
One Connaught Place Central  
Hong Kong

### **Auditors**

KPMG  
8th Floor, Prince's Building  
10 Chater Road Central  
Hong Kong

