

**Analyst: Paul Sham**
**WING LUNG BANK LIMITED (永隆銀行)**

Sector	: Banking	Chairman	: Dr. Michael Po-ko Wu
HKSE Code	: 0096	Chief Executive	: Dr. Philip Po-him Wu
Market Price	: HK\$89.65 (05/03/2007)	General Manager	: Mr. Che-shum Chung
Shares Issued	: 232.2m		
Mkt. Cap.	: HK\$20,816.7m		
52 weeks Hi/ Lo	: HK\$99.90 / HK\$72.00		
HSI	: 23,114.34 (05/03/2007)		
Main Business	: Banking and related financial services		

**SUMMARY OF THE FINAL RESULTS FOR THE YEAR ENDED 31<sup>ST</sup> DECEMBER 2007**
**Final Results Highlights**

	HK\$ million	Vs FY2006 (%)	Vs 30/06/2007 (%)
• Net interest income	1,491.6	+6.6%	
• Non-interest income*	848.7	+23.7%	
• Total operating income	2,340.3	+12.2%	
• Operating expenses	(738.5)	+9.4%	
• Operating profit before impairment losses	1,601.8	+13.6%	
• Impairment losses on loans and other credit risk provisions	<b>(503.4)</b>	<b>+1036.3%</b>	
• Net gain on fair value adjust. on investment properties	305.3	-40.4%	
• Profit before taxation	1,576.1	-18.1%	
• Taxation	(204.6)	-35.6%	
• <b>Attributable profit to shareholders</b>	<b>1,371.5</b>	<b>-14.6%</b>	
• Total loans	41,934.5	+8.1%	+1.2%
• Total deposits	74,413.6	+9.9%	+6.0%
• Total assets	93,048.1	+9.5%	+3.5%
• Basic EPS (HK\$)	5.91	-14.6%	
• Final DPS (HK\$)	1.50	-42.3%	
• Total DPS (HK\$)	2.40	-29.4%	

**Selected Ratios**

	FY2007	FY2006	1H2007
• Net interest margin	1.81%	1.88%	1.84%
• Cost-income ratio*	31.6%	32.4%	30.6%
• Return on average assets	1.54%	2.01%	1.96%
• Return on average equity	11.5%	14.9%	14.8%
• Impaired loan ratio	0.26%	0.47%	0.34%
• Impaired advances coverage	141.9%	92.5%	107.9%
• Loan-deposit ratio	56.4%	57.2%	58.2%
• Capital adequacy ratio	14.7%	16.0%	15.2%
• Average liquidity ratio	46.8%	46.1%	46.4%

Remark (\*): Non-interest income and cost-to-income ratio were adjusted for charge for insurance claims.

- **FY2007 results disappointed market expectations** Wing Lung Bank (WLB) posted a net profit of HK\$1,372m for 2007, down 14.6% y-o-y and was below market expectations of HK\$1,414m to HK\$1,694m. This was mainly due to narrowing net interest margin and the HK\$594m provisions for the CDO and SIV exposures.
- **Earnings dragged by losses in CDOs and SIVs** Wing Lung wrote down a combination of HK\$131m (reported under non-interest income) or 15% of its investments in CDOs, and HK\$463m (reported

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under impairment charge) or 60% of its SIVs investments, representing 25.4% of total operating income.

- **Mild growth in net interest income** Despite a y-o-y drop in NIM from 1.88% to 1.81%, net interest income grew 6.6% y-o-y to HK\$1,492m in FY2007. The narrowed NIM was offset by a steady increase in loan portfolios (+8.1% y-o-y) on faster loan growth in China. Within HK, mortgages were up only 3.1%. The slow growth amid the booming property market was attributed to the intense competition in the mortgage business.
- **Non-interest income remains the key driver** Non-interest income grew 23.7% y-o-y as a result of sustainable fee income growth (+73.4% y-o-y), but offset by lower net trading income (-52.3% y-o-y) due to the loss arising from its CDO investments. Within fee income, securities brokerage & investment services recorded an impressive growth of 123% y-o-y on the back of robust stock market activities.
- **Cost-to-income ratio slightly improved** Operating expenses rose by 9.4% y-o-y in FY2007, mainly reflecting staff increase and the rise in rentals and computer-related expenses. Cost-to-income ratio dropped from 32.4% in 2006 to 31.6% in 2007.
- **Surprising cut in dividend** WLB surprised the market by cutting its final dividend for 2007 (down 42.3% y-o-y). Management guided that the bank needed to retain the capital to support its expansion in the Mainland and to pay RMB200m for the stake in Yantai City Commercial Bank (YTCB), rather than concerns over CDO or SIV exposures.
- **Sound financial position amid weakened profitability** WLB's ROA and ROE plunged to 1.54% and 11.5% respectively in FY2007 from 2.01% and 14.9% a year earlier. However, the bank's financial position remained strong, with a reasonably high capital adequacy ratio of 14.7% as of 31/12/2007.

### Outlook & Prospects

- **WLB earning volatility remains high** The stock market related fees of WLB contributed 67% of its total gross fees. In addition, the sharp increase in the valuation of its investment properties contributed over 20% of its pre-tax profit in the past two years. If there is any significant downturn in stock market activities and / or the property price of commercial properties, WLB's profitability would be significantly undermined.
- **Late comer in the PRC market** Wing Lung will pay RMB200m for a 4.99% stake of Shandong-based YTCB. Given WLB's small investment amount to YTCB, the profit contribution will not be significant. But as it is the first move in mainland by WLB, which lacks mainland presence before, the future contribution from YTCB might offer a better growth prospect for WLB.
- **Remains a potential acquisition target** Similar to Chong Hing Bank, WLB is another hottest M&A candidate among the local lenders. Despite the bank denied the rumour and said the company was not in talks toward a possible transaction back in mid-February, WLB did draw attention from potential bidders as the majority of senior management are approaching retirement.
- **Expensive valuations supported by M&A theme** Given the bank's conservative business strategy and intense competition in the Hong Kong market, it would be a challenge for WLB to further expand its market shares. Business expansion is also slow in China. Coupled with the surprising cut in dividend payout in FY2007 which sent the dividend yield to only 2.7%, WLB appears expensive valued at 15.2x 2007 P/E and 1.66x 2007 P/B. But again, similar to Chong Hing Bank, the M&A theme might give some supports to WLB's current stock price.

**Recommendation: Neutral**

**I. Impairment allowances, overdue and rescheduled advances of Wing Lung Bank**

As % of total customer advances	Individual allowance	Portfolio allowance	Non-performing loans	Overdue and rescheduled advances
<b>As of 31/12/2007</b>	0.11%	0.26%	0.26%	0.46%
<b>As of 30/06/2007</b>	0.13%	0.24%	0.34%	0.63%
<b>As of 31/12/2006</b>	0.16%	0.27%	0.47%	0.80%

**II. Comparison of Wing Lung Bank's loan book: 31/12/2007 vs 31/12/2006**

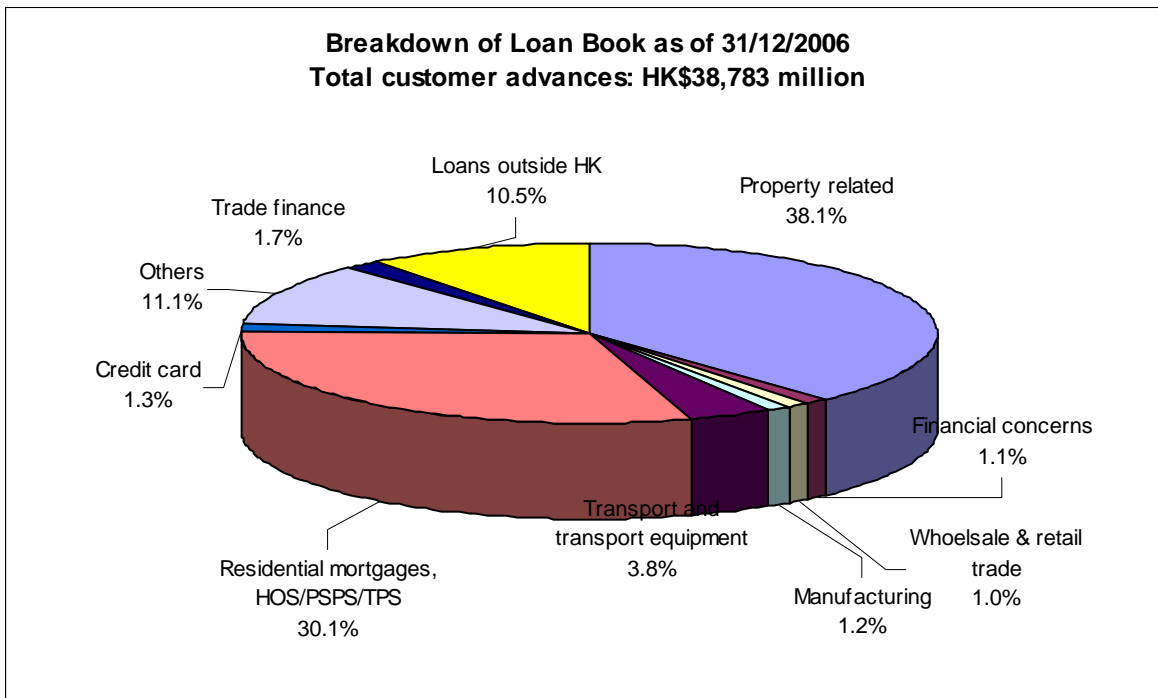
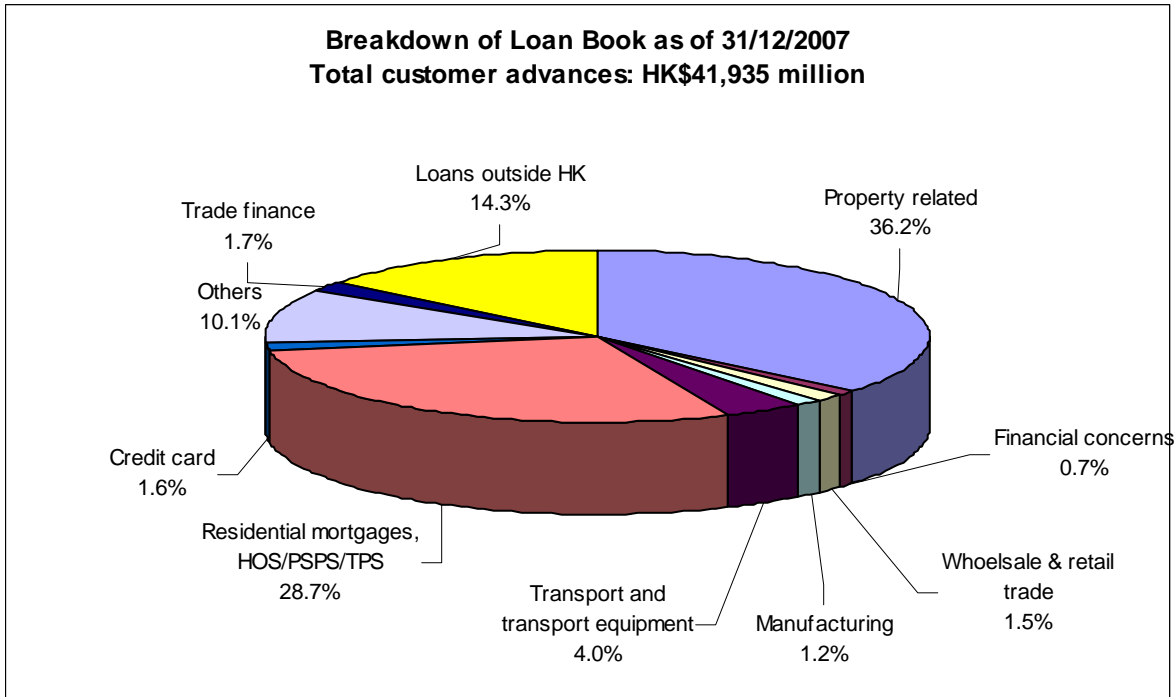
Loans-by industry	31 <sup>st</sup> Dec, 2007	Up/(down)	31 <sup>st</sup> Dec, 2006
	HK\$ million		HK\$ million
Property related	15,194.0	+2.8%	14,778.4
Financial concerns	285.4	-34.4%	435.3
Wholesale & retail trade	622.9	+55.7%	400.0
Manufacturing	523.7	+8.2%	484.2
Transport & transport equipment	1,690.9	+16.3%	1,454.5
Residential mortgages, HOS/PSPS	12,023.2	+3.0%	11,668.1
Credit card	660.3	+27.7%	517.0
Others	4,227.5	-1.7%	4,301.5
Trade finance	725.1	+9.1%	664.4
Stockbrokers	0.4	-77.4%	1.6
Loans outside HK	5,981.1	+46.7%	4,078.0
	<u>41,934.5</u>	+8.1%	<u>38,783.0</u>

**III. Comparison of Wing Lung Bank's loan book: 31/12/2007 vs 30/06/2007**

Loans-by industry	31 <sup>st</sup> Dec, 2007	Up/(down)	30 <sup>th</sup> June, 2007
	HK\$ million		HK\$ million
Property related	15,194.0	-1.9%	15,492.8
Financial concerns	285.4	-26.5%	388.2
Wholesale & retail trade	622.9	+15.9%	537.4
Manufacturing	523.7	+3.7%	505.0
Transport & transport equipment	1,690.9	-4.8%	1,776.7
Residential mortgages, HOS/PSPS	12,023.2	+6.3%	11,314.3
Credit card	660.3	+52.6%	432.7
Others	4,227.5	-24.2%	5,573.8
Trade finance	725.1	-2.4%	743.2
Stockbrokers	0.4	NA	0.0
Loans outside HK	5,981.1	+28.1%	4,667.4
	<u>41,934.5</u>	+1.2%	<u>41,431.6</u>



**Breakdown of loan book of Wing Lung Bank**



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