

**Analyst: Paul Sham**
**FUBON BANK (HONG KONG) LIMITED (富邦銀行(香港))**

Sector	: Banking	Chairman	: Mr. Tsai Ming-Hsing, Richard
HKSE Code	: 0636	Managing Director & CEO	: Mr. Lee Jin-Yi
Market Price	: HK\$5.49 (11/03/2008)		
Shares Issued	: 1,172.2m		
Mkt. Cap.	: HK\$6,435.2m		
52 weeks Hi/ Lo	: HK\$6.20 / HK\$4.00		
HSI	: 22,995.35 (11/03/2008)		
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	853.7	+22.5%	
• Non-interest income	567.8	+31.9%	
• Total operating income	1,421.5	+26.1%	
• Operating expenses	(834.8)	+16.5%	
• Operating profit before impairment losses	586.7	+42.9%	
• Impairment losses on loans and advances	(37.6)	-42.6%	
• <b>Impairment losses on AFS securities</b>	<b>(162.4)</b>	<b>NA</b>	
• <b>Net gains on disposals of AFS securities</b>	<b>132.5</b>	<b>+182.6%</b>	
• Profit before taxation	517.1	+32.1%	
• Taxation	(56.2)	-12.6%	
• <b>Attributable profit to shareholders</b>	<b>461.0</b>	<b>+40.9%</b>	
• Total loans	31,633.0	+22.1%	+10.6%
• Total deposits	45,228.8	+16.7%	+10.3%
• Total assets	60,622.9	+13.6%	+10.5%
• Basic EPS (HK\$)	0.3933	+40.9%	
• Final DPS (HK\$)	0.13	+8.3%	
• Total DPS (HK\$)	0.19	+5.6%	
<b>Selected Ratios</b>	<b>FY2007</b>	<b>FY2006</b>	<b>1H2007</b>
• Net interest margin	1.65%	1.44%	1.64%
• Cost-income ratio	58.7%	63.6%	59.4%
• Return on average assets	0.81%	0.63%	0.83%
• Return on average equity	11.4%	8.5%	11.3%
• Impaired loan ratio	0.55%	0.93%	0.59%
• Impaired advances coverage	88.6%	68.0%	96.5%
• Loan-deposit ratio	69.9%	66.9%	69.7%
• Capital adequacy ratio	14.4%	16.6%	15.4%
• Average liquidity ratio	44.4%	44.5%	45.5%

- **FY2007 net profit beat market expectations** FY2007 results of Fubon Bank (HK) beat market consensus (HK\$278.6m to HK\$387.4m) with net profit increasing 41% y-o-y to HK\$461m, driven by strong growth momentum from almost all lines of business.
- **Dividend payout lowered to 48.3%** Basic EPS rose 40.9% to HK\$0.3933 for FY2007 while the bank proposed a final dividend of HK\$0.13 per share, bringing the full-year DPS to HK\$0.19 per share. Its dividend payout ratio fell to 48.3% from 64.49% a year ago. Management of the Bank said that more capital is required to be reserved for future expansion.

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- **Surge in net interest income** Net interest income grew 23% on 22.1% increase in loan balance and widening of 21bps in its net interest margin. Strong performance was seen in trade finance (+130% y-o-y) and overseas loans (+63%), mainly loan demand from Taiwan-related corporate lending and hire purchase loans for use in China. Taiwan-related loans now accounted for 18% of Fubon HK's loan book, up from 10% in FY2006.
- **Non-interest income grew on strong sales of wealth management** Net fee income rose 100% y-o-y to HK\$285.8m on better fee income from the sale of Unit Trust (+197%), financial market products (+47%), insurance products (+101%) and brokerage-related services (+90%). But the overall non-interest income was partly dragged by the mark-to-market losses on CDOs.
- **Cost efficiency improved** Fubon HK's operating expenses rose 16.5% in FY2007, with a majority of the increase in staff costs due to increase in headcount (31/12/2007: 1,101, +20.9%). As operating income growth (+26.1%) outpaced the rise in operating expenses, the bank's cost-to-income ratio improved to 58.7%, compared with 63.6% a year earlier.
- **CDO Provisions and impaired losses on SIVs partly offset by gains in AFS** Fubon HK has made HK\$90m provision charge against the HK\$234m CDOs (38% provisioning) and HK\$162m charge against the HK\$273m SIVs (59% provisioning). The combined HK\$252m losses were partly offset by a HK\$132m disposal gain of available-for-sale securities.
- **Improvement in loan book quality** Impairment losses on loans dropped 42.6% on write-backs of loan provisions in 2H2007. The bank's impaired loan ratio also dropped to 0.55% as of 31<sup>st</sup> Dec 2007 from 0.93% a year earlier, lower than industry's 0.89%.
- **Improving profitability and firm financial position** Fubon HK's ROA increased from 0.63% in FY2006 to 0.81% in FY2007 while ROE jumped from 8.5% in FY2006 to 11.4% in FY2007. Average liquidity ratio was maintained at 44.4%. The management said that the decline of CAR (14.4% as of 31<sup>st</sup> Dec 2007) was due to the adoption of Basel II.

### Outlook & Prospects

- **Growing Taiwan business** Compared to its peers, Fubon HK is able to leverage its ties with its parent and benefit from Taiwanese companies investing in HK/China. Its Taiwan-related business contributed 34% of operating income in 2007, compared with 12% in 2006, reflecting its successful business strategy. Given the growing trade and investment flows among Taiwan, Hong Kong and Mainland China, Fubon HK should continue to benefit from its Taiwan business.
- **Potential China exposure** Based on the recent implementation of CEPA IV, which might allow Taiwan banks to make investments in Chinese banks via their HK subsidiaries, market rumoured that Fubon HK was in talks to acquire a 20% stake in Xiamen City Commercial Bank. Despite it was denied by the bank in Feb 08, management admitted in the result presentation that they had aggressively tried to tap into the Mainland market and the cut in dividend payout ratio also supports the argument. We believe Fubon HK would announce its expansion plan in China shortly after confirmation of approval to open branches in the PRC.
- **Improving fundamentals** With the ROE rising from 8.5% in 2006 to 11.4% in 2007 and the impaired loan ratio dropping to 0.55% from 0.93%, Fubon HK showed substantial improvement in its profitability and credit quality. We believe the image of being at the bottom of the league amongst other Hong Kong-based listed banks begins to fade out.
- **Reasonable valuations** Trading at 1.6x FY2007 P/B and 14.0x FY2007 P/E, valuations of the counter look reasonable in view of its improving fundamentals and its unique business-ties with Taiwan. The potential China exposure can also offer some short-term supports to the share prices so we accordingly recommend a "Buy" on the counter.

**Recommendation: Buy**

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**I. Impairment allowances, overdue and rescheduled advances of Fubon (Hong Kong)**

As % of total customer advances	Individual allowance	Portfolio allowance	Non-performing loans	Overdue and rescheduled advances
<b>As of 31/12/2007</b>	0.23%	0.26%	0.55%	0.49%
<b>As of 30/06/2007</b>	0.24%	0.33%	0.59%	0.49%
<b>As of 31/12/2006</b>	0.32%	0.31%	0.93%	0.80%

**II. Comparison of Fubon (Hong Kong)'s loan book: 31/12/2007 vs 31/12/2006**

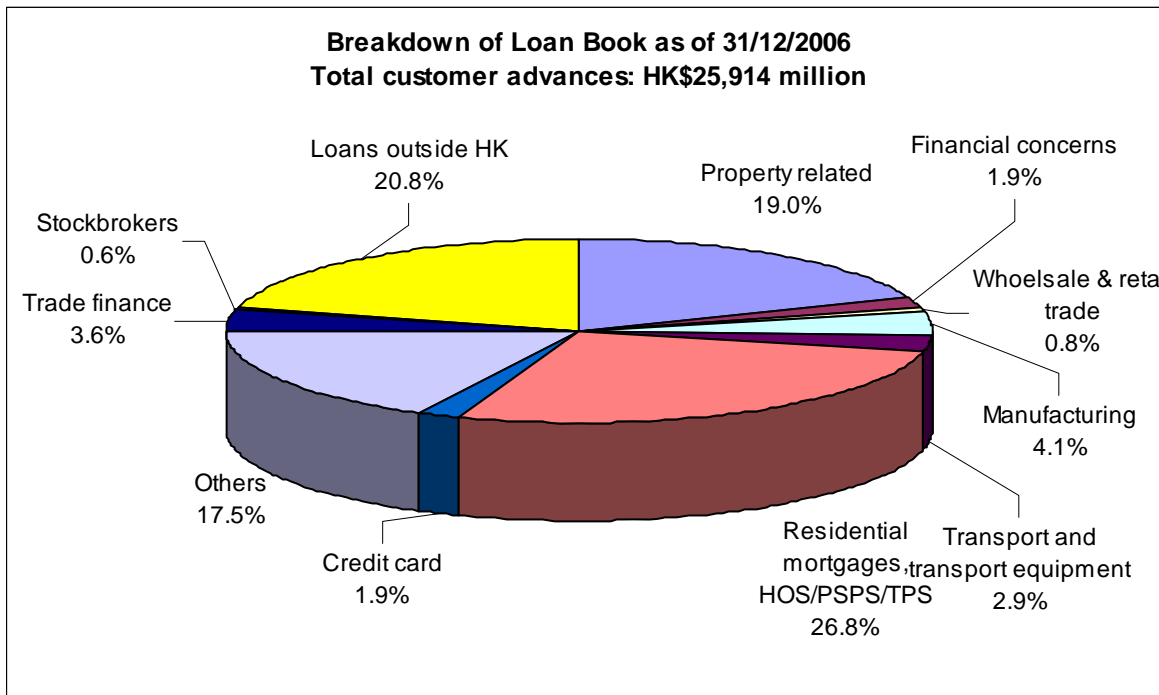
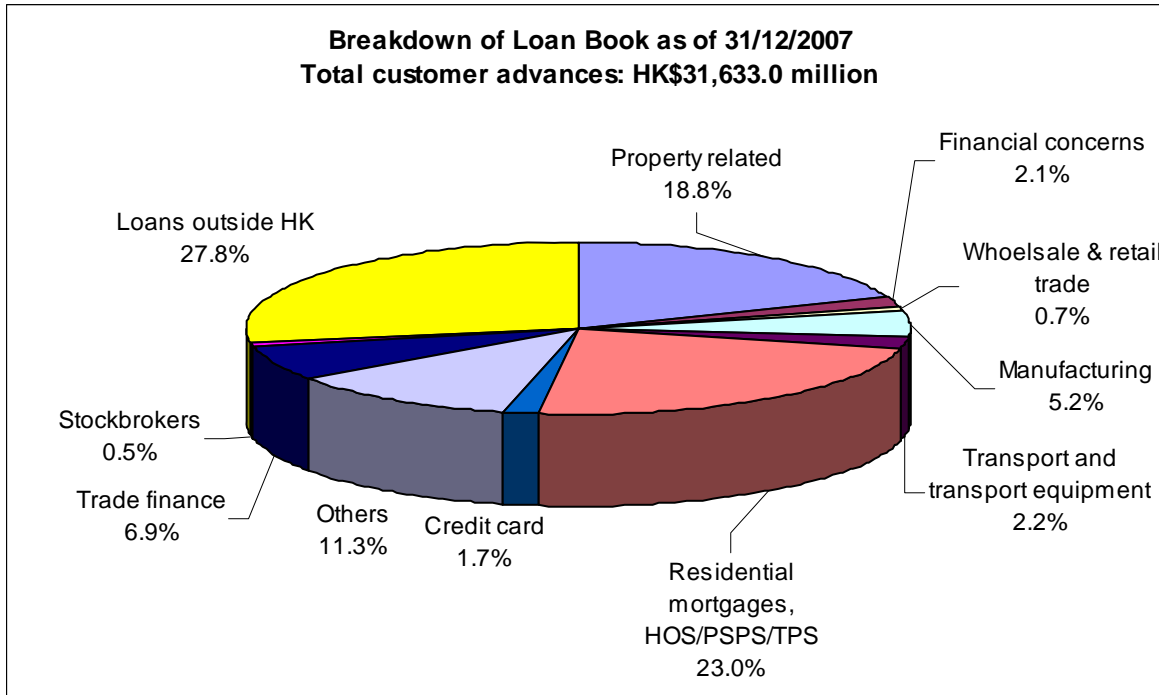
Loans-by industry	31 <sup>st</sup> Dec, 2007	Up/(down)	31 <sup>st</sup> Dec, 2006
	HK\$ million		HK\$ million
Property related	5,933.5	+20.4%	4,929.7
Financial concerns	678.3	+40.1%	484.3
Wholesale & retail trade	221.6	+9.5%	202.4
Manufacturing	1,634.1	+54.2%	1,059.5
Transport & transport equipment	699.0	-7.6%	756.2
Residential mortgages, HOS/PSPS	7,280.2	+4.7%	6,950.2
Credit card	533.2	+5.8%	504.2
Others	3,558.9	-21.7%	4,547.1
Trade finance	2,169.8	+130.0%	943.4
Stockbrokers	144.3	-8.3%	157.4
Loans outside HK	8,780.0	+63.2%	5,380.0
	<u>31,633.0</u>	+22.1%	<u>25,914.4</u>

**III. Comparison of Fubon (Hong Kong)'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	5,933.5	+11.1%	5,339.1
Financial concerns	678.3	+101.6%	336.5
Wholesale & retail trade	221.6	+28.9%	171.9
Manufacturing	1,634.1	+17.6%	1,389.0
Transport & transport equipment	699.0	-4.5%	731.6
Residential mortgages, HOS/PSPS	7,280.2	+5.1%	6,925.9
Credit card	533.2	+6.7%	499.5
Others	3,558.9	-18.3%	4,357.9
Trade finance	2,169.8	+33.2%	1,628.6
Stockbrokers	144.3	-8.5%	157.8
Loans outside HK	8,780.0	+24.5%	7,051.0
	<u>31,633.0</u>	+10.6%	<u>28,588.8</u>



**Breakdown of loan book of Fubon (Hong Kong)**





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