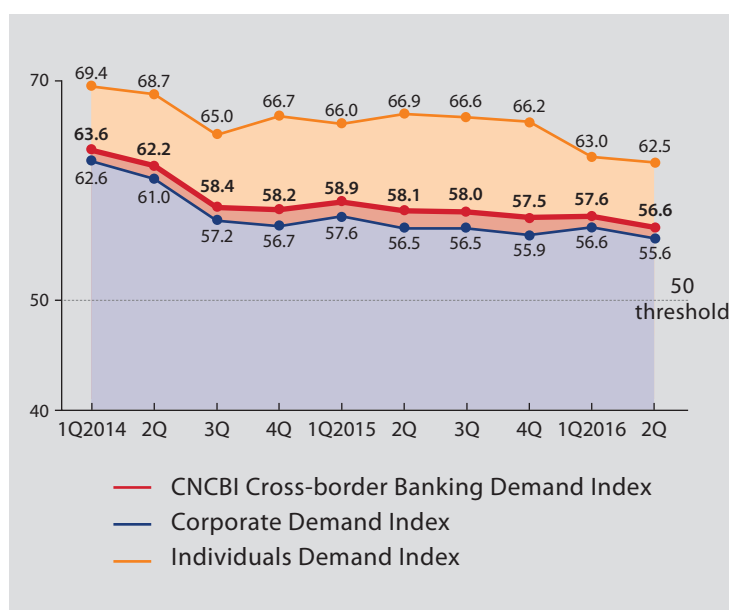


2Q2016 cross-border banking demand back on slow trend

Corporate and individual demand indices both hit new lows

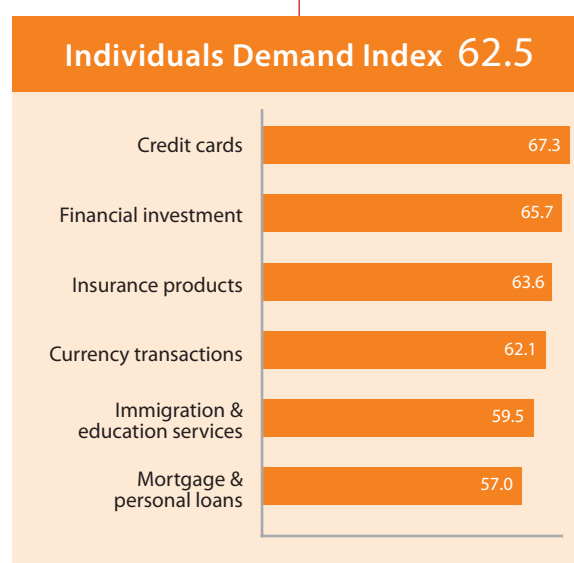
www.cncbinternational.com/cross-border-index



- 2Q2016 growth of cross-border banking demand for Hong Kong's banking service back on decline after slight 1Q increase
- Corporate and individual demand growth both hit new lows since Index launch

- On the corporate side, slow demand growth most significant in corporate loans and bond issuance whereas demand growth of currency transactions and derivative products gains strength
- On the individuals side, demand growth for credit card and immigration & education services rise but that for other services and products decelerate significantly

CNCBI Cross-border Banking Demand Index 56.6



1. Overview

- According to the 1Q2016 survey results, the 2Q2016 CNCBI Cross-border Banking Demand Index drops 1.0 on the quarter to 56.6, indicating a return to the downtrend following last quarter's slight rebound in the overall growth of demand from mainland corporations and individuals for Hong Kong's cross-border banking services.
- Corporate demand growth falls to a new low since the Index's launch with the corresponding index shedding 1.0 from the last quarter to 55.6 whereas growth of individuals' demand also hits a new low albeit less acutely with a 0.5 drop to 62.5.
- Of the corporate sub-indices, bond issuance, loans, trade finance, settlement & cash management, asset management & financial consultancy and structured finance drop from last quarter's 54.5, 60.3, 54.9, 59.2, 59.2 and 53.7 to 51.1, 57.2, 53.7, 58.5, 59.1 and 53.6 respectively with the first two showing the sharpest fall of 3.4 and 3.1 respectively, whereas the derivative products and currency transactions sub-indices rise from 52.9 and 57.4 to 54.8 and 58.1 respectively. As for the ranking of the sub-indices, loans, bond issuance and trade finance drop from 1st, 5th, and 6th to 4th, 6th and 8th respectively, while asset management & financial consultancy, currency transactions, and derivative products rise from 3rd, 4th and 8th to 1st, 3rd and 5th respectively. Settlement & cash management and structured finance remain 2nd and 7th respectively.
- Among the individuals demand sub-indices, currency transactions, financial investment, insurance products and mortgage & personal loans fall respectively from 63.6, 67.0, 64.6 and 58.0 to 62.1, 65.7, 63.6 and 57.0. Conversely, credit cards and immigration & education services are up from 66.2 and 58.5 to 67.3 and 59.5 respectively. As such, financial investment swaps places with credit card which claims the top spot as the former comes 2nd in the ranking while other sub-indices stay put in 3rd to 6th places.
- The overall lull of 2Q2016 corporate demand growth, especially the significant softening of loans and bond issuance demand are attributed to the continuous slowdown of Mainland China's economic growth and the consistently decreasing financing cost. It is also attributable to the dampened investment sentiment caused by the second crash of the country's A stock market and drastic RMB devaluation in early January. In particular, the financing cost in the mainland market has plummeted from being well above that in Hong Kong market to below since the dawn of 2016, significantly weakening cross-border financing demand in 2Q2016 and beyond. Unexpectedly, demand growth for currency transactions and derivative products climbs, which may reflect the increase in trade between RMB and HKD, USD and other foreign currencies as well as the rise of RMB-linked derivative products under the anticipation of RMB devaluation.
- The softening of cross-border demand growth from individuals, especially that for financial investment and insurance products, is believed to be a result of the impact of the weak economic environment on the eagerness of individuals "going out" as well as of RMB devaluation and of the A stock market crash on individuals' capital strength for "going out". The meagre increase in demand growth for credit card and immigration & education services should be seen as a correction from the acute decrease in the previous quarter. Meanwhile, the Hong Kong government has not eased the spicy measures on property purchases by mainlanders despite a noticeable decline in Hong Kong property prices. And in view of this, demand for mortgage & personal loans is to fall further.

2. Sub-index analysis

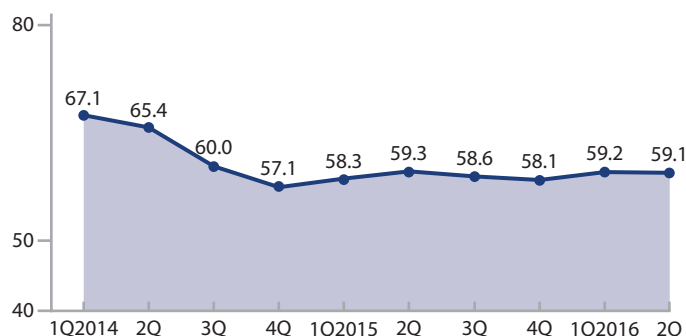
2.1 Corporate demand sub-indices



Asset management & financial consultancy (59.1)

The sub-index of asset management & financial consultancy drops slightly by 0.1, but it jumps over the settlement & cash management sub-index and becomes 1st in the ranking, implying that the downturn of the macro-economic and cross-border financing environment has little impact on cross-border demand for non-financial and highly value-added asset management & financial consultancy services. Of the corporations polled, 22% predicted a demand "Increase" while 4% did the opposite. Meanwhile, 64% and 59% of the samples would choose financial consultancy and asset management respectively. As for the major reasons for the increased demand growth, 54%, 53% and 45% of the corporations stated respectively confidence in the related services from Hong Kong banks, confidence in business prospects and increase in asset amount.

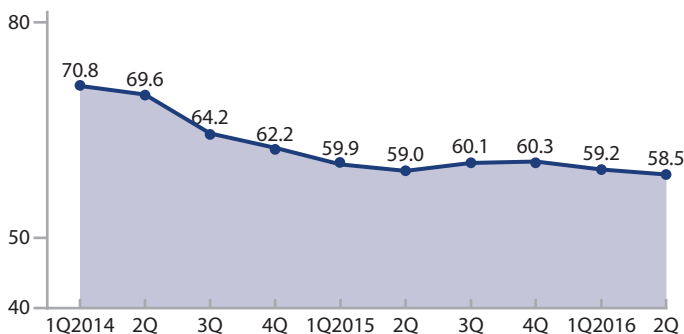
Trend of sub-index



Settlement & cash management (58.5)

The sub-index decreases slightly by 0.7 and remains second in the ranking. This reflects that the impact of RMB devaluation would slowly weaken and that demand for RMB trade settlement & related cash management would stabilise. However, the situation for export and import between Mainland China and Hong Kong will become more challenging this year and will continue to affect demand for cross-border settlement & cash management services. Of the sampled corporations, 21% expected an demand "Increase" while 4% did otherwise. Meanwhile, 57%, 53% and 29% chose cash management, trade settlement and investment settlement respectively. Regarding the reasons for demand growth, 65%, 55% and 49% cited confidence in business prospects, a need for adequate capital for business development and confidence in the settlement & cash management services from banks in Hong Kong respectively.

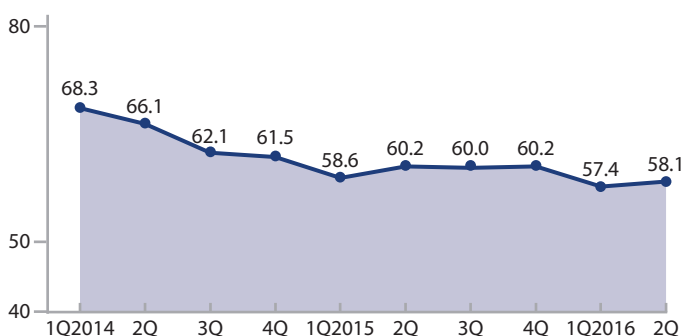
Trend of sub-index



Currency transactions (58.1)

An increase of 0.7 in the sub-index from the last quarter reveals the trend where mainland corporations have started to trade HKD, USD and other foreign currencies for RMB under the continuous devaluation of the mainland currency. Of the sampled corporations, 20% expected an "Increase" in demand while 4% believed otherwise. Regarding currency choices, 65%, 43% and 32% would opt for RMB, USD and HKD respectively, which continues to reflect the expectation of RMB devaluation. The reasons for higher demand are increased cross-border business (64%), confidence in business prospects (57%), and confidence in the currency transaction services from banks in Hong Kong (53%).

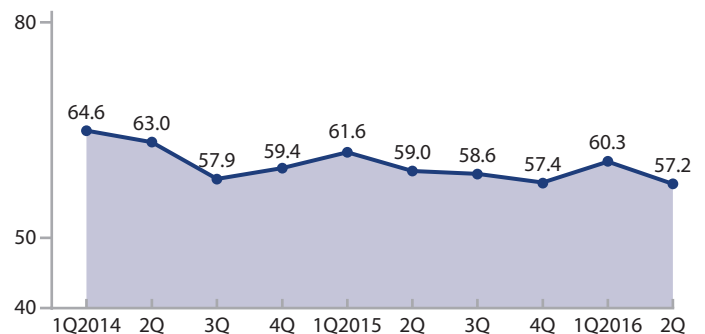
Trend of sub-index



Loans (57.2)

Sampled data shows an acute quarterly decrease of 3.1 in the loans sub-index, indicating a marked slowdown in demand for cross-border loans. Economic growth in Mainland China is yet to stabilise and the country's loose monetary policy has also led financing requirements to relax and the cost to drop, causing significant decreases in demand for cross-border loans. Of the corporations polled, 19% expected a demand "Increase" whereas 5% expected a "Decrease". Also, 66% and 51% would take out loans for investment and liquid capital respectively. Regarding the demand growth drivers, 60%, 46% and 42% of the surveyed corporations stated confidence in business prospects, confidence in the loan services from Hong Kong banks, and a need for more operational capital respectively.

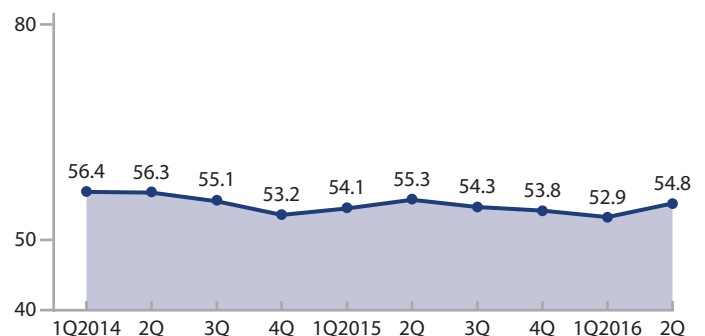
Trend of sub-index



Derivative products (54.8)

Demand for derivative products goes the same way as that for currency transactions against the downtrend towards a rebound with an increase of 1.9 and a move from the last to the 5th in the ranking. This should reflect the rise of RMB devaluation linked derivative products in place of RMB appreciation linked derivative products. Of the sampled corporations, 13% expected an "Increase" whereas 3% expected the opposite. As regards relevant product demand, 56%, 51% and 24% chose Non-deliverable Forward (NDF), Interest Rate Swap (IRS) and Digital Forward respectively. Meanwhile, 58%, 48% and 44% claimed confidence in future prospects of business, confidence in derivative products from banks in Hong Kong and increase in risk adverse demand respectively as the important factors for the demand increase.

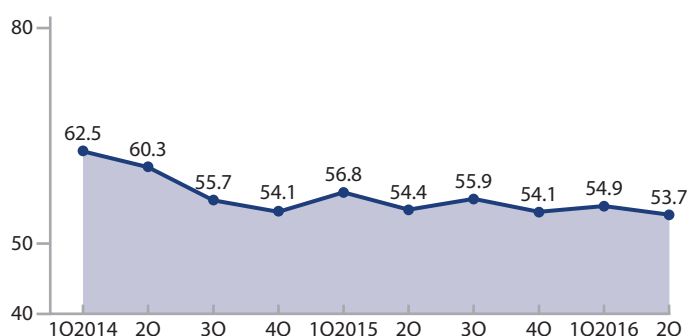
Trend of sub-index



Trade finance (53.7)

The sub-index drops 1.2 from the last quarter, indicating that cross-border trade finance demand has been affected by weak economic growth, decrease in foreign trade and RMB devaluation. Of the sampled corporations, 13% expected an "Increase" and 6% a "Decrease". Also, 68% and 47% claimed that demand stems from export financing and import financing respectively, while 54%, 52%, and 46% of those who expected an "Increase" stated confidence in the trade finance services from banks in Hong Kong, confidence in the prospects of business and a need for adequate capital for trading respectively as the demand drivers.

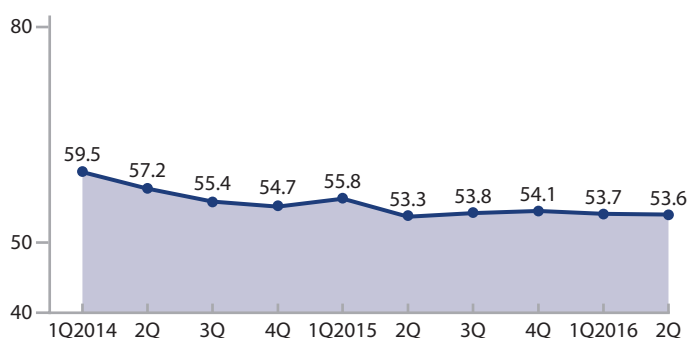
Trend of sub-index



Structured finance (53.6)

The sub-index falls merely 0.1 from the last quarter and stays 7th in the ranking. The pace of mainland corporations "going out" remains robust and cross-border merging activities vigorous, offsetting to a large extent the impact of certain negative factors on cross-border structured finance services demand. Of the sampled corporations, 11% predicted an "Increase" while 4% predicted the opposite. Also, 63%, 28% and 24% of the sample would opt for syndicated loans, M&A financing and pre-IPO financing respectively, while 61%, 53% and 49% cited a need for adequate capital for business expansion, confidence in the structured finance services from banks in Hong Kong and confidence in business prospects respectively as the major demand drivers.

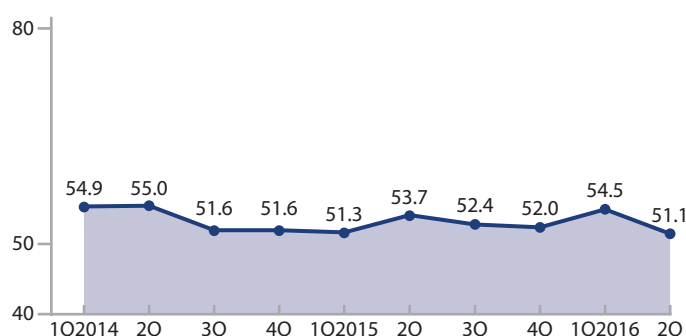
Trend of sub-index



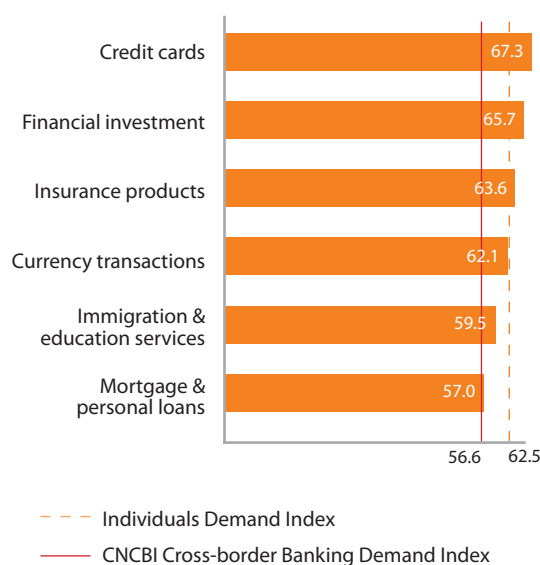
Bond issuance (51.1)

This sub-index posts the biggest fall of 3.4 among all the others and it drops from the 6th to become last (8th) in the ranking. The major reasons for the marked decrease should be the significant decline in mainland bond financing cost and the loosening of the bond issuance criteria. Of the corporations polled, 9% and 7% predicted a demand "Increase" and "Decrease" respectively. As regards the choice of currency, 56% and 54% would opt for FX and RMB respectively. The proportion that would choose RMB continues to fall, underscoring the lingering effect of the RMB devaluation expectation. Meanwhile, 56%, 47% and 38% of the sampled corporations attributed demand growth to a need for adequate capital for business expansion, confidence in bond issuance services from banks in Hong Kong and long repayment periods respectively.

Trend of sub-index



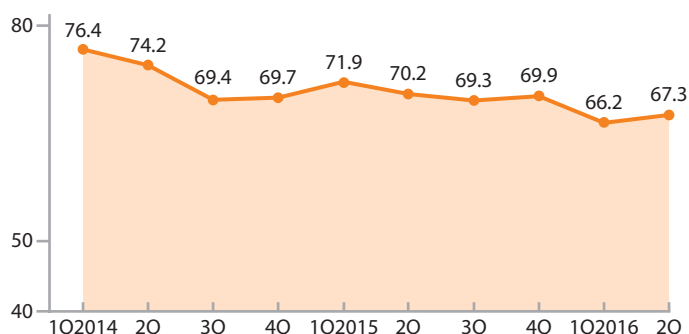
2.2 Individuals demand sub-indices



Credit cards (67.3)

The credit card sub-index rises 1.1 and climbs unexpectedly to the top from its second place in the ranking. On the one hand, this can be interpreted as a correction from last quarter's significant slide. On the other, it reflects mainlanders' usage of credit card in Hong Kong has increased proportionally. Of the surveyed individuals, 39% predicted a demand "Increase" while 4% replied with a "Decrease". Meanwhile, 82% signalled a higher usage of credit cards and 41% expressed an intention to apply for new credit cards. As for the reasons for demand increase, 67% and 47% said that it would be to facilitate spending in Hong Kong and that they have confidence in the credit card services offered by banks in Hong Kong respectively, while 42% attributed this to the attractive merchant offers.

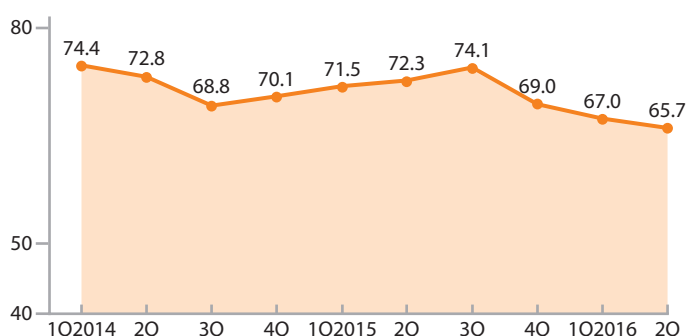
Trend of sub-index



Financial investment (65.7)

The financial investment sub-index declines further by 1.3 and falls to the 2nd place in the ranking, indicating that factors such as slowing economic growth, the dim stock markets in both Mainland China and Hong Kong, and the expectation of RMB devaluation have continued to curb the enthusiasm and capital strength of mainland individuals' seeking cross-border financial investment. Of the survey respondents, 37% and 6% expected demand to "Increase" and "Decrease". As regards investment tools, 76%, 54%, 30% and 21% of would choose stocks, funds, bonds and derivative products respectively. The proportion of those who would choose stocks further reduces by 4% from the last quarter. This should be attributable to the weak performance of the Hong Kong stock market. As for the reasons for the increase, 60% of the respondents stated confidence in the future prospects of Hong Kong, while another 60% said that they have confidence in the related services provided by Hong Kong banks and 44% noted that it would be adequate investment capital.

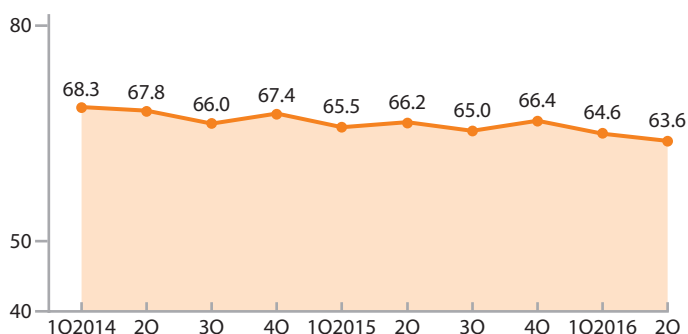
Trend of sub-index



Insurance products (63.6)

The sub-index drops 1.0 from the last quarter but staying 3rd in the ranking. The declining figures of mainland visitors to Hong Kong continue to affect insurance product sales. Of the individuals polled, 31% and 4% reported a demand "Increase" and "decrease" respectively. Insurance products denominated in RMB and in FX are preferred by 66% and 64% of the respondents respectively. The expected RMB devaluation has also continued to eat into the proportion of respondents choosing insurance products denominated in RMB. As for the top 3 demand drivers, they are confidence in insurance products provided by banks in Hong Kong (69%), confidence in the future prospects of Hong Kong's insurance sector (57%), and having adequate capital for buying insurance products (47%).

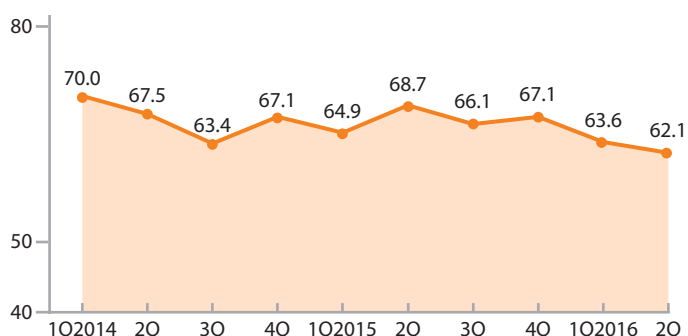
Trend of sub-index



Currency transactions (62.1)

The sampled data shows that demand from individuals for currency transactions services continues to slow down, going in an opposite direction from corporate demand and implying that mainland individuals' motivation for trading HKD, USD and other foreign currencies for RMB is weaker than mainland corporations. Its respective sub-index drops 1.5 the last quarter but remains 4th in the ranking. Of the respondents, 30% expected an "Increase" in demand while merely 6% expected a "Decrease". Regarding the currency for transactions, 58%, 54% and 49% would choose USD, HKD and RMB respectively. Attractive exchange rate of currency (51%), confidence in the future prospects of Hong Kong (50%) and confidence in the currency transaction services offered by Hong Kong banks (49%) were cited as the major drivers for the demand increase. The proportion of respondents choosing RMB transactions has decreased further as a consequence of the ongoing expectation of RMB devaluation.

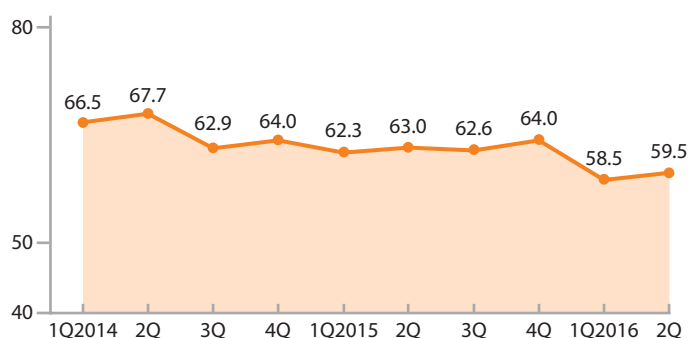
Trend of sub-index



Immigration & education services (59.5)

Remaining 5th in the ranking, the immigration & education services sub-index increases by 1.0 over the quarter. The increase can largely be seen as a positive adjustment of last quarter's slide. Of the sampled individuals, 23% and 4% reported an "Increase" and a "Decrease" in demand respectively, while 81% showed interest in educational services and 44% in immigration services. Regarding the main demand growth drivers, 68%, 52% and 50% cited confidence in related services provided by Hong Kong banks, confidence in the prospects of Hong Kong, and possessing adequate capital for supporting immigration and education services respectively.

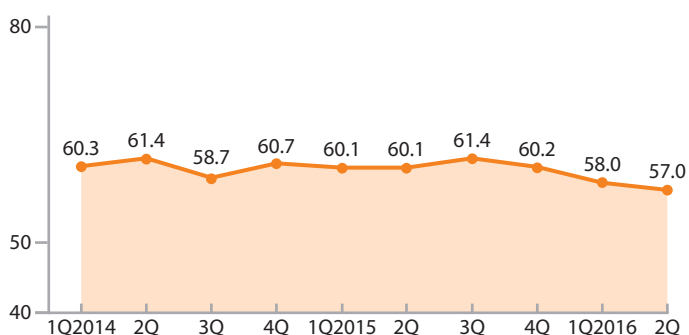
Trend of sub-index



Mortgage & personal loans (57.0)

Staying the lowest in the ranking, this sub-index continues its decline with a 1.0 decrease from 1Q2016. The Hong Kong government has yet to relax the market-cooling restrictions imposed on property buyers from the mainland despite a noticeable decrease in property prices in the city, which contributes to the consistently low demand for cross-border mortgages. The dampened stock market situation in Hong Kong has also continued to diminish motivation for mainlanders to seek personal loans. Among the sampled individuals, 21% reported an "Increase" while 7% a "Decrease" in demand. Personal loans are preferred by 70% of the individuals polled whereas 45% would choose mortgage loans. The percentages of respondents who considered confidence in future prospects of Hong Kong, confidence in related services provided by Hong Kong banks and the need for adequate capital for investment as the major demand drivers were 47%, 47% and 46% respectively.

Trend of sub-index



Appendix: Methodology and data

Definition and calculation

The CNCBI Cross-border Banking Demand Index captures the trends of cross-border demand from mainland companies and individuals for banking services provided by banks in Hong Kong in the next quarter, based on the results of a quarterly survey over mainland companies and individuals conducted by international market research firm Ipsos.

The CNCBI Cross-border Banking Demand Index is a weighted average of the Corporate Demand Index and the Individuals Demand Index, while the Corporate Demand Index and the Individuals Demand Index are in turn weighted averages of eight service-specific corporate demand sub-indices and six service-specific individuals demand sub-indices respectively.

Each of the sub-indices is a diffusion index and is calculated from the replies of survey respondents to the question: "Do you expect your/your company's demand for the cross-border banking service (as specified) will increase, decrease or remain the same in the next quarter as compared to the current quarter?" The value of the diffusion index is the sum of the responses of "Increase" plus half of those responding "Same" in percentage terms.

Diffusion indices have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading of above 50 indicates a strengthening of demand, and below 50 a weakening.

Sample data

The CNCBI Cross-border Banking Demand survey spans 15 cities across the Pearl River Delta, Yangtze River Delta, Pan-Bohai and Central & Western areas of China. This quarterly survey covers 500 companies and 500 affluent mainlanders who are currently using cross-border banking services or indicated an intention to do so. Data is collected mainly through telephone interviews.

The corporate sample represents a wide spectrum of industries including import/export trade, manufacturing, real estate, construction, power & energy, etc, with quotas on small, medium and large enterprises based on their annual turnover. Finance managers or directors of qualified companies are interviewed. The individuals sample consists of high-net-worth (>US\$1 million liquid assets) and upper affluent (>HK\$1 million liquid assets) individuals.

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