HSBC

News Release

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HSBC Bank Malta announces lower profits but increases dividends

- Reported profit before tax of €49.8m for the year ended 31 December 2017, a decrease of €12.4m, or 19.9%, compared with prior year.
- Adjusted profit before tax, which excludes the effect of notable items, was €55.6m, 9.5% down on 2016.
- Net dividend for 2017 was €40.2m, up 54.0% compared with prior year. It includes a special dividend of €20m to be distributed from surplus retained earnings.
- Common equity tier 1 ratio increased to 13.9% at 31 December 2017 from 13.2% at 31 December 2016. The total capital ratio was 14.4% at 31 December 2017, compared with 14.2% at 31 December 2016.
- Adjusted cost efficiency ratio was 66.2%, compared with 58.7% in 2016.
- Adjusted return on equity for the year ended 31 December 2017 was 7.2% compared with 8.4% in 2016.
- Earnings per share of 8.6 cent compared with 11.2 cent in 2016.
- The advances to deposits liquidity ratio remained stable at 65.6%.
- Net loans and advances to customers were €3,129m, down 5.8% compared with 2016.
- Customer deposits decreased by 4.7% to €4,766m at 31 December 2017.

This news release is issued by
HSBC Bank Malta p.l.c.

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HSBC Bank Malta p.l.c. ('the bank') reported a profit before tax of €49.8m for the year ended 31 December 2017. This represents a decrease of €12.4m or 19.9% on the previous year.

The bank confirms its business model and risk management change programme was substantially completed in 2017 leading to a short term reduction in profitability. HSBC has announced €20m extraordinary dividend to reward shareholders given the strong progress made with implementation of the bank's strategic plan.

The reported profit before tax incorporates three notable items which are excluded from the adjusted results as this is considered a better reflection of management's performance.

In 2016, the bank recognised the gain on disposal of the bank's membership interest in Visa Europe amounting to €10.8m and raised a provision totalling €8m in relation to a remediation of the legacy operational failure in the bank's brokerage business. During 2017, the remediation programme was largely completed and it was assessed that a partial reversal of the conservatively estimated provision was warranted. In this regard, a reversal of €1.8m was effected in 2017.

During the year, the bank re-examined its approach to the provision for the collective agreement clauses related to future employee benefits. A longer-term view was assumed in the application of the current clauses which resulted in an additional charge of €7.6m in 2017 as compared with the charge of €2m in 2016. While the movements in this provision will periodically occur depending on the changes in the composition of the bank's employee base, the provision adjustment in 2017 was not related to the business performance of the year.

	2017	2016
	€000	€000
Reported profit before tax	**49,823**	62,221
Notable items:		
Gain on VISA transaction	**-**	(10,787)
Movement in the brokerage remediation provision	**(1,800)**	8,000
Costs of the provision for collective agreement benefits	**7,600**	2,000
Adjusted profit before tax	**55,623**	**61,434**

Profit attributable to shareholders amounted to €30.9m resulting in earnings per share of 8.6 cent compared with 11.2 cent in 2016. The Board recommended maintaining a current dividend payout ratio of 65% of net profit. The Board also made a decision to return part of retained earnings to the shareholders and recommended an extraordinary dividend of €20m in addition to the regular dividend paid out of the net profit for the year. The final gross dividend will be 12.4 cent per share (8.1 cent per share net of tax). Together with the interim dividend paid in September 2017, the total gross dividend for 2017 will be 17.1 cent per share (11.1 cent per share net of tax) or €61.6m (€40.2m net of tax) representing a 54.0% increase on the dividends paid for 2016. The final dividend will be paid on 19 April 2018 to shareholders who are on the bank's register of shareholders at 13 March 2018.

The year under review was characterised by broadly stable but persistently low interest rates and increasing excess liquidity in the market while attractive investment opportunities remained limited. In this environment, a record number of debt issuances by corporate entities was registered on the Malta Stock Exchange fuelled by investors' demand for higher yield.

Andrew Beane, Chief Executive Officer at HSBC Bank Malta p.l.c., said: "In 2017 we largely completed changes to our business model in order to meet the highest global standards for compliance and risk management. While these actions reduced profitability during the year due to lower revenues and higher costs, they have materially strengthened the bank's risk profile and position it well for the future.

Our changed business model is creating value for our shareholders, notably by generating dividends. Indeed, given the strategic progress the bank has made, the Board was pleased to declare an exceptional dividend of €20m which reflects HSBC's capacity to generate more capital than is required by our risk profile.

Looking to the future, the outlook for the local economy remains favourable with strong GDP growth, low unemployment and inflation and government finances forecast to remain in surplus. Amidst this positive economic landscape, it is essential to ensure that growth remains broad based and sustainable and that risks are managed appropriately including an increasing level of long-term risk in the local bond market which has become a greater cause for concern.

In 2018, within our changed business model, HSBC will increase investment in customer service and innovation to support growth over the medium term while sustaining the bank's signature conservative credit discipline that supports strong performance through the full economic cycle.

I would like to thank my colleagues for their outstanding commitment to HSBC in 2017 and our customers and shareholders for their continued trust."

Net interest income of the bank decreased by 4.6% to €120.7m compared with the prior year principally due to the reduction in the corporate loan book and in the bonds portfolio. While lending margins remained largely unchanged, the average yield of the investment book declined further due to continuing amortisation of higher yielding bonds. Retail banking performed well and increased its interest income by 2.9%. The European Central Bank negative deposit rate remained unchanged during 2017 resulting in additional interest expense on the bank's excess liquidity. The reduction in interest expense due to the maturity of the bank's subordinated debt in February 2017 partially mitigated the decline in interest income.

Net non-interest income reduced by 9.7% compared with 2016. A lower level of credit activity and the ongoing review of the bank's risk appetite had an adverse impact on fees and commissions as well as trading income. Other operating income was adversely impacted by lower valuation of investment property held by the bank.

HSBC Life Assurance (Malta) Limited reported a profit before tax of €7.3m, which was broadly in line with the prior year. In 2017, the volume of new 'with-profits' business increased resulting in a higher premium income. In November 2017, the company announced a partial sale of the unit-linked portfolio acquired in 2014 from another HSBC Group entity. As the transfer of this portfolio will be at the consideration of €1, no gain or loss will be registered as a result of this transaction.

Operating expenses were €112.2m, 1.8% higher compared with previous year. Two notable cost items described above had a negative impact on the level of expenses in 2016 and 2017. The bank accelerated the work in raising risk and compliance standards which resulted in higher administrative costs. At the same time, the bank continued to benefit from the early voluntary retirement programme implemented in 2016 and saw a decline in underlying staff costs by 3% absorbing the annual pay increase.

A net reversal of loan impairment charges amounting to €1.2m was recorded in 2017. The bank continued to improve the asset quality by managing down non-performing exposures by over 20% year on year notably in the corporate book. Non-performing loans as a percentage of total gross loans reduced further to 5.3% compared with 6.4% in 2016. This resulted in a number of reversals of corporate impairment provisions raised in the past. Furthermore, the bank has reviewed its conservative provisioning approach to certain legacy defaulted mortgage exposures as the observed rates of recovery picked up as a result of improved collection practices. In addition, the collateral securing the relative exposures was prudently assessed as adequate. This led to a net recovery on retail impairment provisions in 2017.

Net loans and advances to customers decreased by 5.8% and stood at €3,129m. The decline was registered in the corporate loan book as a result of lower business activity due to prioritisation of compliance agenda. Moreover, several corporate customers chose to replace bank funding with externally issued debt. The retail loan book grew by 4.9% compared with the prior year partially offsetting the reduction in corporate lending.

Customer deposits decreased by 4.7% to €4,766m in 2017 driven by the reduction in corporate deposits in line with the ongoing review of the risk appetite. Deposits from retail customers increased by 2.6% compared with prior year as the bank continued to expand its primary-banked customer base. The bank maintained a healthy advances-to-deposits ratio of 65.6% and its liquidity ratios were well in excess of regulatory requirements.

The available-for-sale financial investments portfolio decreased by 12.1% compared to 2016. The bank's risk appetite for investment quality remained unchanged – this portfolio is managed as a high-quality liquidity buffer and consists entirely of securities of sovereign and supranational issuers rated A- (S&P) or better. While the bank partially replaced maturing bonds during the year, attractive investment opportunities in an environment of record low interest rates in Europe were extremely limited.

The bank's capital ratios continued to improve as risk weighted assets decreased year on year. Common equity tier 1 capital increased to 13.9% from 13.2% and the total capital ratio was 14.4% up from 14.2% at the end of 2016. The bank remained fully compliant with its end-point regulatory capital requirements during 2017. Its strong capital position enables the bank to sustain its high dividend payout ratio at 65% of profit after tax and to pay extraordinary dividend out of retained earnings.

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