

Economic Situation

Hong Kong's economy grew modestly in 2015, with real GDP growth slowing to 2.4% from 2.7% in 2014, reflecting weaker domestic demand and a deteriorating export performance due to the austere external environment. While domestic demand remained the key engine of growth, net exports also played a part as total imports declined faster than total exports. The labour market remained largely stable in 2015, with the seasonally adjusted unemployment rate staying low at 3.3%.

The local stock market experienced large swings in 2015. Following a flat first quarter, the Hang Seng Index picked up, reaching a seven-year high in April, amid increased optimism in the Mainland A-share market and capital inflows. The growth trend reversed from late June and the Hang Seng Index hit a year-low in September against the backdrop of heightened volatility on financial and foreign exchange markets in the third quarter. The local stock market regained some ground in the final quarter when the global and Mainland financial markets stabilised, with the Hang Seng Index closing the year 7.2% lower than at the end of 2014. The residential property market started the year strongly, but softened after the announcement of the seventh round of countercyclical prudential measures on property mortgage in February, the downturn in the local stock market in summer, and growing concerns over an interest rate hike in the US. The commercial and industrial property markets moderated in the second half of the year, with both prices and rentals coming under pressure towards the end of the year. Underlying inflation eased further to 2.5% in 2015 from 3.5% a year earlier alongside the overall weakening in economic growth.

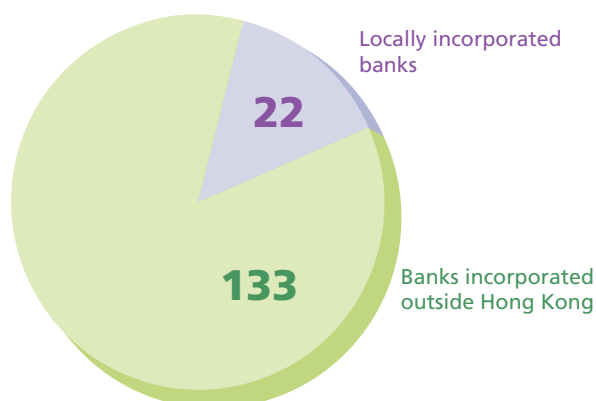
Hong Kong Banking Environment

The local banking sector remained resilient in 2015 despite further divergence in the monetary policies of advanced economies and the accumulating vulnerabilities in emerging market economies. The asset quality of retail banks deteriorated slightly during the year, but remained at a healthy level by historical standards. The classified loan ratio edged up to 0.70% at the end of 2015 from a very low level of 0.52% the previous year. All locally incorporated authorized institutions (AIs) remained well capitalised. Their consolidated capital adequacy ratio increased to 18.3% at the end of 2015 from 16.8% a year earlier, which was well above the international minimum standard of 8%. The Banking (Liquidity) Rules, which implement the Basel III's Liquidity Coverage Ratio (LCR) for AIs (designated as "category 1 institutions"), together with a local Liquidity Maintenance Ratio (LMR) for all other authorized institutions (category 2 institutions) became effective on 1 January 2015. In the fourth quarter of 2015, the average LCR of category 1 institutions was 142.9%, well above the statutory minimum requirement of 60% applicable for the year, and the average LMR of category 2 institutions was 53.9%, also well above the statutory minimum requirement of 25%.

Scheme Members' Profile

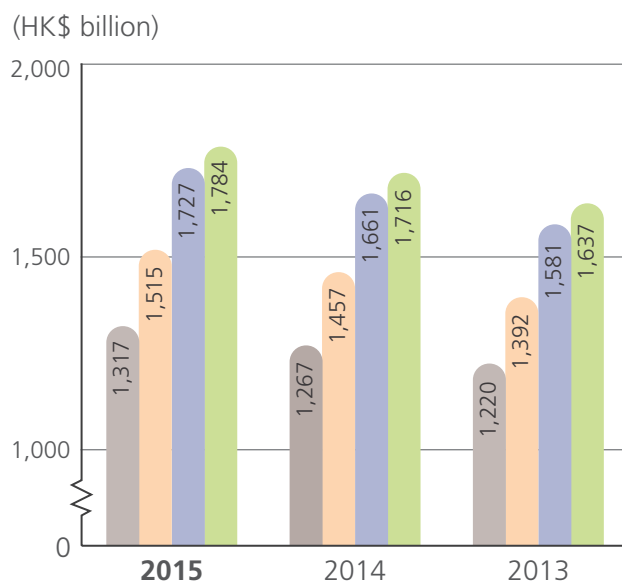
The Scheme had 155 members at the end of March 2016, the same as a year ago. Two newly licensed banks became members of the Scheme, while two memberships were revoked because of group restructuring. Twenty-two of the Scheme members were locally incorporated banks and 133 were banks incorporated outside Hong Kong. This was largely in line with the number of retail and wholesale banks in Hong Kong.

Number of Scheme Members at 31 March 2016



Based on the returns submitted by Scheme members, the aggregate amount of their relevant deposits grew by 4% to HK\$1,784 billion during 2015, compared with HK\$1,716 billion in 2014. According to statistics provided by Scheme members, 90% of depositors were fully protected by the DPS. The distribution of relevant deposits among Scheme members remained similar to that of the previous year. The top 20 Scheme members (most of which were retail banks) held 97% of the industry's aggregate relevant deposits.

Relevant Deposits Held with Scheme Members



% of total	2015	2014	2013
Top 5	74%	74%	75%
Top 10	85%	85%	85%
Top 20	97%	97%	97%
Total	100%	100%	100%

Relevant Deposits Held by Retail Banks and Wholesale Banks

(HK\$ billion)	2015	2014
Retail banks	1,731	1,666
Wholesale banks	53	50

Enhancing the Scheme

The Deposit Protection Scheme amendment bill was introduced into the Legislative Council in November 2015 and passed on 17 March 2016. The Board provided full support to the Government throughout the public consultation and legislative process for the implementation of enhancements to the DPS. Upon implementation of the new legislation which enabled the adoption of the gross payout approach in compensation determination, the target payout time frame for making full compensation payments to depositors has been shortened to within seven days in most cases, as compared with the previous payout time frame of six weeks. Together with other new measures, such as empowering the Board's use of electronic communications to notify affected depositors, the enhanced DPS provides better protection to depositors and strengthens their confidence in the DPS as an integral part of Hong Kong's financial safety net. It also further contributes to banking stability and Hong Kong's status as an international financial centre.

During the year, the Board continued its collaboration with the HKMA in exploring possible synergy between the proposed resolution regime for financial institutions and the prevailing DPS, in particular the incorporation of temporary additional DPS coverage for deposits transferred from a failed bank to a healthy transferee bank under the proposed resolution regime.

Ensuring Payout Readiness of the DPS

Information Readiness of Scheme members

The calculation of compensation amounts payable to depositors relies heavily on the accuracy and completeness of depositor records provided by Scheme members. To ensure the quality of data and the timeliness of the information provided, a new policy of compliance surveillance was introduced during the year. Scheme members were required to submit an annual self-declaration and the results of 2015 in relation to their compliance with the information requirements were satisfactory. On top of the self-declaration, an independent assessment needs to be conducted by Scheme members once every three years. During the year, the Board scrutinised assessment reports submitted by 50 Scheme members and noted a few compliance issues reported by the assessors. In this connection, we required the Scheme members concerned to take prompt remedial action and to strengthen their internal processes. Also, two briefing sessions were held to raise Scheme members' awareness of common issues noted by the Board during the review process.



Briefing for Scheme members on compliance with information submission requirements

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Separately, depositor statistics and banking product information are collected in the annual returns and are maintained in a central repository. The establishment of a central repository helps speed up the payout preparations, especially when there is a possible trigger of the DPS.

Payout Rehearsal

The Board places high emphasis on the Scheme's preparedness to respond quickly to a range of contingencies. Payout rehearsals are therefore conducted regularly to test the process and systems as well as the external payout agents to help ensure the Scheme's preparedness.

A payout rehearsal was conducted in 2015 involving an extensive network of payout agents. The rehearsal was based on a scenario of a retail bank failure as notified by the banking supervisor under the agreed co-operative arrangements. The payout agents had to activate their service within a very short notice as if they were going through a real banking crisis situation. The rehearsal was successfully completed, demonstrating the effective co-ordination between the Board and its payout agents in carrying out the payout process.



A rehearsal conducted with payout agents

Simulations

To help enhance the data handling process and procedures, six simulation tests were conducted alongside the compliance reviews using the full set of depositor records provided by the Scheme members. The scope of the tests was also expanded to cover the preparatory work before the DPS was triggered. Based on the simulation test results, new data quality checking procedures have been developed to improve the efficiency of identifying data which do not conform to the requirements.

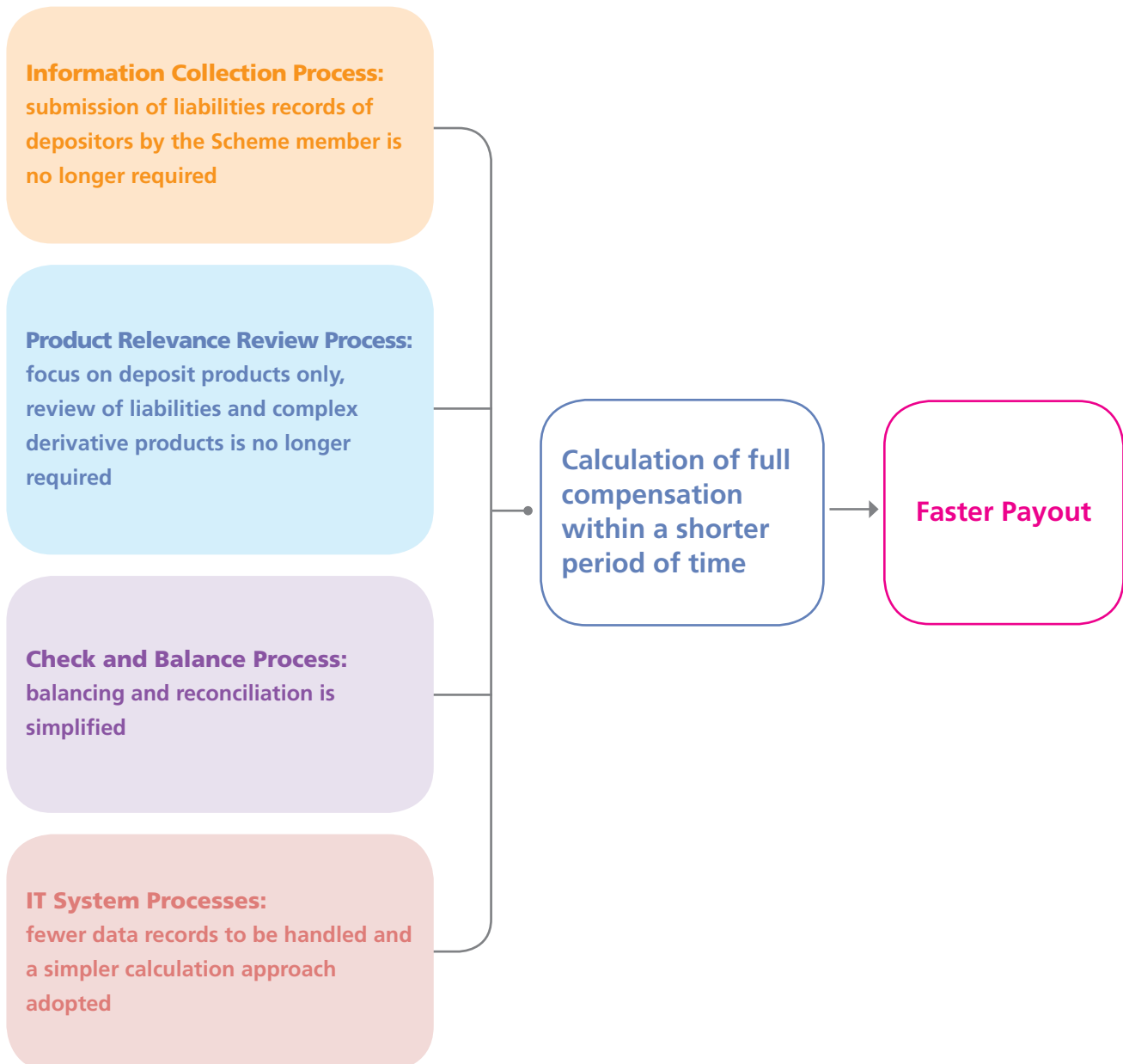
Gross Payout Readiness

To ensure smooth transition to the gross payout approach, amendments have been made to systems and event management procedures. Payout walk-throughs were held with the payout agents to get them familiar with the gross payout approach. The focus of the exercise was to shorten the payout time frame for making full compensation payments to depositors to within seven days in most cases, compared with the previous arrangement of releasing an interim payment within two weeks. The exercise also identified approaches for enhancing the management of depositors' expectation and public communication amid the shorter payout time frame.



Snapshot of a walk-through conducted with payout agents

Contributors to Faster Payout under the Gross Payout Approach



Building up the DPS Fund

Composition of the Fund

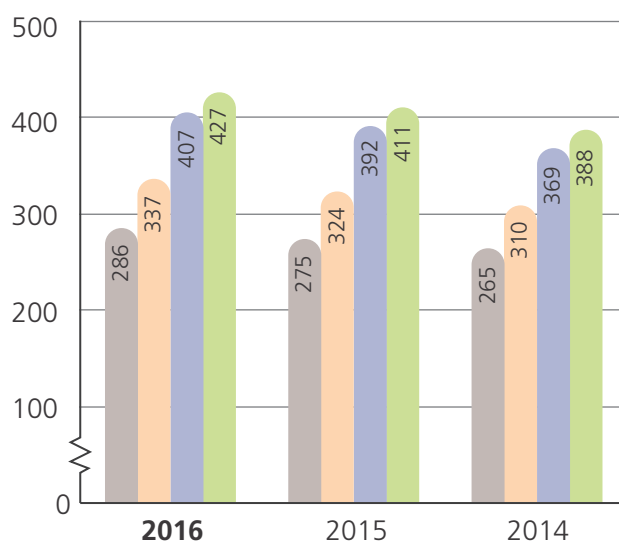
The build up of the DPS Fund is mainly from two sources, namely annual contributions paid to the Board by Scheme members, and the returns generated by the Fund's investments. The amount of relevant deposits reported by Scheme members, together with the supervisory rating provided by the HKMA, serves as the basis for determining their contributions for the coming year.

Assessment and Collection of Contributions

The contributions collected from Scheme members during the year amounted to HK\$427 million, an increase of 4% from the previous year. All contributions were paid during the first quarter of 2016. Similar to the distribution of relevant deposits, the amount of contributions collected from the top 20 Scheme members accounted for more than 95% of the total. To ensure that the deposit data reported by Scheme members is accurate, the Board, since 2007, has requested Scheme members to conduct regular audit reviews of their returns of relevant deposits in accordance with the policy for reviewing returns. At the request of the Board, 15 Scheme members submitted an audit report on the accuracy of their returns in 2016. The review results were satisfactory, and no reporting error leading to a material impact on the amount of contributions collected by the Board was noted.

Contributions Paid by Scheme Members

(HK\$ million)



By Relevant Deposits Held

% of Total	2016	2015	2014
Top 5	67%	67%	68%
Top 10	79%	79%	80%
Top 20	95%	95%	95%
Total	100%	100%	100%

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The fact that all Scheme members subject to regular audit review requirements had completed their reviews under the current reporting basis increased the Board's confidence in the accuracy of the total amount of contributions payable by the industry. A regular survey for monitoring the popularity of structured deposits (which are excluded from the protection net under the ambit of the DPS) was conducted in the fourth quarter of 2015. The results showed that the number of depositors with structured deposits was not material. In view of this, the Board concluded that the non-protection status of structured deposits should remain unchanged.

DPS Fund Investments

Due to the volatility and uncertainties of global financial markets, the Board once again exercised extra caution by adopting a capital preservation and conservative investment strategy for the investment of the Fund. Investments were also made in strict compliance with the DPS Ordinance and the investment control policies of the DPS Fund, which set out clear guidelines on risk assessment and control measures, and the segregation of duties required for investment activities. At the end of March 2016, the DPS Fund's assets were predominantly held as Hong Kong dollar deposits. Despite the low interest-rate and uncertain investment environment, the DPS Fund achieved an investment return of 0.57% for the year.

The DPS Fund's Mix of Cash and Investments (at 31 March)

(HK\$ million)	2016	2015
Cash and deposit balance	3,138	2,766
Investment securities	0	0
Total	3,138	2,766

The DPS Fund's Currency Mix of Cash and Investments (at 31 March)

(HK\$ million)	2016	2015
Hong Kong dollars	3,138	2,765
US dollars	0	1
Total	3,138	2,766

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Enhancing Public Awareness and Understanding of the Scheme

The Board continued to assign a high priority to increasing the public awareness and understanding of the DPS. An integrated approach has been adopted to reinforce the message and mission of the Scheme. As a result, mass publicity campaigns were conducted during the year through various communication channels, and were augmented with tailor-made engagement and education activities targeting Hong Kong's diverse community.

Multimedia Publicity Campaigns

Television, Out-of-home and Digital Publicity

The campaign highlighting the important message, "Where is the best place to keep my money?", was extended from advertisements on major television channels to the infotainment systems on buses and MTR trains, supplemented with wall posters at high-traffic MTR stations and on buses. To reach out to the ever-growing digital audience, online banners of the series were also displayed on mobile networks, websites and search engines.

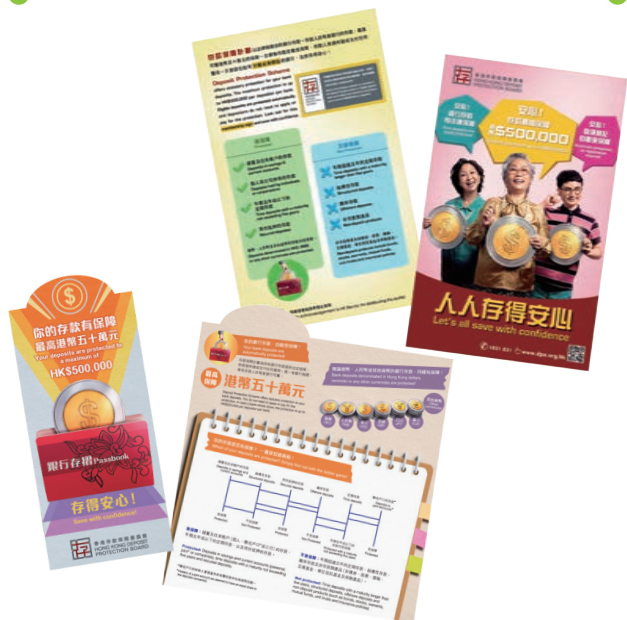


Digital and out-of-home publicity campaigns reinforce the message of the TV advertisement

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Print Publicity

Key DPS messages with daily examples covering all walks of life were published in advertorials and informative articles in free newspapers, weekly magazines and newsletters. These covered a wide range of readership from the younger generation to working adults and senior citizens. During the year, the Board also launched a newly designed leaflet to present the key messages in a light-hearted manner.



DPS print material gets support from a range of organisations for wider distribution

Engaging and Educating the Public

Facebook Page

In September 2015, the Board entered a new phase in its publicity drive with the launch of a Facebook page titled "Save with confidence" (存得安心) to connect with a wider audience, particularly the younger generation. A month later, the Board organised its first Facebook engagement campaign "Treasure Hunt" to stimulate community-level interaction. During the campaign period, the DPS Facebook page mascot "Ah Chuen" (阿存) visited different parts of Hong Kong. The Facebook engagement continued with quizzes and games, in addition to sharing the DPS messages and interesting tips.

Deposit Story Campaign

In keeping with the old saying "every dollar counts" and the notion that there is a story behind every deposit, the Board launched a deposit story recruitment campaign during the year. More than 2,000 entries were received from a wide cross-section of the community. The campaign encouraged members of the public to share their deposit stories, and enabled a greater understanding of deposit protection. The winning entries will be shared with the wider community in 2016-2017.



DPS Facebook page mascot "Ah Chuen" meeting his fans

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Neighbourhood Outreach

In reaching out to neighbourhoods, the Board introduced an eye-catching campaign from October to December 2015, involving a moving mirror truck with the slogan “存程照住你” (Cantonese slang for “DPS looking after you all the way”) stationed in high-traffic business districts and residential areas to promote the DPS messages. Passers-by were invited to take an instant photo with a “deposit dream” caption to share on the DPS Facebook page.

The weekend outreach campaign at public housing estates and near old tenement buildings continued during the year. And, the Board again participated in popular consumer shows, namely the Retiree and Senior Fair and the 50th Hong Kong Brands and Products Expo Fair, to reinforce the key DPS messages.



Board Chairperson Mrs Pamela Chan and DPS ambassadors at the “Mirror Truck” campaign



DPS booths prove a popular attraction at consumer shows

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DPS Board Game

A board game, "Around the World in \$80", was designed by the Board as an interactive and interesting community education tool to promote to younger people money management, the basic concept of DPS protection and the importance of saving. With the support of schools and parent volunteers, the game was introduced to junior-grade students in liberal studies lessons and extra-curricular activities, with the longer-term objective of encouraging players to save and learn more about the DPS. The game was also displayed at an exhibition at the Jao Tsung-I Academy.



Eager students playing the new DPS board game

DPS Mobile Training Application

Another initiative of the Board was the development of a new community education training tool, the DPS mobile application. The "app" facilitates interaction with the participants of the DPS talks and seminars mainly for secondary students, and helps arouse their interest in the Scheme. It comprises a brief introduction to the Scheme, a question and answer game to test users' DPS knowledge, as well as a savings-and-expenses tracker.



New DPS mobile "app"

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Bun-making and the DPS

Continuing with the success of the previous publicity campaign, the latest bun-making class for housewives involved The Family Planning Association of Hong Kong as partner. Apart from the hands-on bun-making experience, information about deposit protection was also delivered to the participants.



Hands-on bun makers learn about the DPS

DPS Talks

The Board continued to conduct tailor-made talks on major aspects of the DPS for different audience groups, including senior citizens and students. We also partnered with the Investor Education Centre and The Hong Kong Association of Banks to include key features of the DPS in their respective financial education workshops. Information about the DPS was also introduced to secondary school students participating in public education seminars held by the HKMA.



DPS community education programmes for the young and not-so-young

Effectiveness of Publicity Campaigns

The results of independent public opinion surveys conducted in 2015 showed that the level of awareness and understanding of the DPS continued to be impressive. The DPS awareness level remained high at 77%. Of those aware of the Scheme, the rising trend of understanding also continued, with 81% having knowledge of the HK\$500,000 protection limit, a rise of nearly two percentage points over the 2014 survey, and 87% knew the protection provided by the DPS was covered by law, recording an impressive rise of nearly seven percentage points. These findings, together with other public views, will be taken on board for fine-tuning the publicity and communication strategies.

Compliance with Representation Rules

The Representation Rules govern representations made by Scheme members about their DPS membership and the protection status of the financial products offered by them. To monitor their compliance with the representation requirements, Scheme members were asked to conduct a self-assessment review covering the period from 1 July 2014 to 30 June 2015. In addition, on-site examinations continued to be undertaken to ascertain in greater detail the level of Scheme members' compliance with the Representation Rules. The Board reviewed the self-assessment reports and findings of the on-site examinations conducted by the HKMA to decide whether or not follow-up actions were required. The results indicated that the overall compliance level was satisfactory in general, and no non-compliance cases with a systemic impact were identified.

Relationships with Other Safety Net Players

Co-operation with the HKMA

The Board and the HKMA are both financial safety net players, sharing the common objective of promoting the stability of the banking system. To accomplish this, the two parties have signed an MoU that sets out how they co-operate in the performance of their respective functions. In addition, since the Board is required by the DPSO to perform functions through the HKMA, the Board and the HKMA have agreed on the extent of the support provided by the HKMA to the Board on a day-to-day basis. The Board also has in place a standby facility from the Exchange Fund to provide the liquidity required to pay compensation in the event of a bank failure. In addition, there is a co-operative agreement between the Board and the HKMA on an early warning system of a potential bank failure to enable a faster DPS payout.

Relationship with the Securities and Futures Commission and the Investor Compensation Company

In the event of a bank failure, the funds of a depositor or a portion of those funds may, in certain circumstances, be covered by both the DPS and the Investor Compensation Fund (ICF) established under the Securities and Futures Ordinance to compensate securities or futures investors. To ensure that no person receives double compensation, the Board and the Securities and Futures Commission (SFC) have agreed on a set of arrangements to co-ordinate and exchange information between them. These have been documented in an MoU between the Board, the SFC and the Investor Compensation Company, the company established by the SFC to administer the ICF. The MoU recognises that the DPS will normally pay the depositors first in the event of a bank failure, and that the parties involved will avoid double compensation by exchanging relevant information.

International Co-operation

As a member of the International Association of Deposit Insurers (IADI), the Board actively participates in its conferences and seminars and other events organised by member deposit insurers and international organisations, and exchanges knowledge and views on issues relevant to deposit protection in international forums. This is particularly important for keeping up to date with international developments, and for sharing experience about the effectiveness of overseas reform measures that may provide insights and impetus for changes to ensure the robustness of Hong Kong's DPS.

In 2015-2016, the Board's personnel took part in a number of international meetings, including:

- The IADI Asia-Pacific Regional Committee 13th Annual Meeting and International Conference in Taipei
- The 14th IADI Annual General Meeting and 2015 Annual Conference in Kuala Lumpur, Malaysia
- The IADI Research Conference, "Current Issues Facing Deposit Insurers", in Basel, Switzerland
- The Joint Financial Stability Institute-IADI Conference: Bank Resolution, Crisis Management and Deposit Insurance Issues in Basel, Switzerland
- The 9th DICJ Round Table, "Lessons learned from Respective Countries", organised by the Deposit Insurance Corporation of Japan.

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The IADI Asia-Pacific Regional Committee 13th Annual Meeting and International Conference (Taipei)



The 14th IADI Annual General Meeting and 2015 Annual Conference (Kuala Lumpur)