



HONG LEONG FINANCE

Chairman's Statement

On behalf of the Board of Directors, I am pleased to present this annual report of the Group and the Company for the financial year ended 31 December 2016.

FINANCIAL OVERVIEW

Group profit after tax attributable to shareholders for the year ended 31 December 2016 amounted to \$53.1 million, equivalent to 12.0 cents per share. The results for the year were arrived at after topping up provision (net of write back of provision/recoveries) amounting to \$1.1 million against a write back of \$3.6 million in 2015.

Loans and advances (before allowances) decreased to \$9.63 billion from \$10.20 billion in 2015, a decrease of 5.6% over the previous year. Deposits and balances of customers registered a decrease of 8.8%, closing at \$10.44 billion as at 31 December 2016. There are no bank borrowings outstanding.

At the end of the financial year, Group shareholders' funds totalled \$1.70 billion, equivalent to \$3.82 per share. The Group continues to maintain a strong capital adequacy ratio of 16.4% as at 31 December 2016, higher than the prescribed requirement.

An interim dividend of 3 cents per share (tax exempt one-tier) was paid on 16 September 2016. Subject to the approval of shareholders at the forthcoming Annual General Meeting, the Board is proposing the payment of a final dividend of 6 cents per share (tax exempt one-tier) in respect of 2016. The aggregate distribution for the year will amount to approximately \$40 million, compared to \$49 million for 2015.

OPERATING PERFORMANCE

Global economic growth in 2016 remained lacklustre. With the weak and precarious nature of global recovery and geopolitical changes brought about by BREXIT and the then incoming US administration, exports and investment across Asia weakened and the drag permeated Singapore's economy.

Local GDP growth was moderate at 1.9% (revised) for the first two quarters of the year. It dipped to 1.2% (revised) in the third quarter before rebounding to 2.9% for the last quarter. Besides facing cyclical winds, Singapore was concurrently undergoing structural transformation intended to bring about higher productivity and a new mode of growth.

The bleak economic conditions posted serious challenges for SMEs. The situation was exacerbated by stiff competition, high operating costs and a lack of manpower support. To achieve sustainable growth, many SMEs restructured their operations while others ventured abroad to manage their costs and in search of innovation and growth opportunities.

As a committed SME supporter, Hong Leong Finance rolled out a series of SME-friendly initiatives during this period of slow economic growth. An innovative SME HDB loan was launched in 1H 2016 to provide targeted help to HDB SMEs to revitalise their businesses. The loan could be used for productivity related staff training to complement government grants from Singapore Workforce Development Agency, premises refurbishment and promotion costs, working capital or process improvements. The loan was priced based on fixed rate to give SMEs more certainty in their cash flow commitment.

Hong Leong Finance also participated in the latest Enhanced Equipment Loan and SME Working Capital Loan introduced by SPRING Singapore in April and July to help local enterprises access equipment and unsecured working capital financing. Furthermore, to assist SMEs in business capabilities building, Hong Leong Finance unveiled an exciting SME Capability Ready (SME Care) Programme that offered SMEs more financing options in 2H 2016. It aimed to support companies looking to apply for government grants for capability-boosting investments. Hong Leong Finance relationship managers shared useful grant information with SMEs. Bridging loans helped SMEs wait out the grant reimbursement period and financing options were available for those that did not qualify for the grants. The programme complemented the government capabilities grants to help transform SMEs to become more competitive and future-ready.

In spite of the volatile capital market and poor investor sentiment, our Corporate Finance led two up-and-coming companies, Katrina Group Ltd, a food and beverage company and AGV Group Limited, a company that provides hot dip galvanising services to the steel and iron fabrication industries, to successful listing on the Catalist Board of the Singapore Exchange. Shares for these Initial Public Offerings were fully subscribed. In all, Corporate Finance also acted as a Continuing Sponsor for ten Catalist companies and an independent financial advisor for a listed company corporate exercise.

Under the SME Connector Programme, piloted at Hong Leong Finance SME Centre @ Upper Bukit Timah in November 2016, several high-growth resilient SMEs were selected to experience first-hand one-to-one corporate advisory services from Corporate Finance, the subject matter expert. Their expertise was borne from practical experience: they brought real life experience to bear and reviews from these SMEs were very positive. Via the programme outreach, Hong Leong Finance aimed to make corporate finance and advisory services more accessible to SMEs.

Hong Leong Finance continued to invest in our core capabilities to deliver value to our clients. To bring greater convenience to our retail customers, a new Sengkang Branch was opened at the refurbished Compass One Mall which is strategically located with easy access to Sengkang MRT Station and Bus Interchange. Since its opening, the branch has seen strong uptake of new deposit accounts by residents in the vicinity. This latest branch replaced the Rivervale Mall Branch.

Deposit taking at branches remained as the main source of funds for our lending business. Besides offering a range of savings accounts and Fixed Deposits with a variety of tenures to meet different customers' time horizon requirement, Hong Leong Finance developed a new regular savings product, both to support and meet customers' needs and to grow and support our own business. Called Fixed Savings Account, it gave customers a hassle-free option to save and grow their money faster by using GIRO. Customers could earn attractive bonus interest on the monthly Giro contributions in their Fixed Savings Account on top of the base interest. The simple and convenient saving account was an instant hit with two groups of customers: those who had left money idling in their bank accounts that paid little interest and those who wanted disciplined saving but could not find time to save up regularly. With Fixed Savings Account, customers could enjoy saving money faster with ease.

The auto industry witnessed a surge of new vehicle registration due to an increase in vehicle deregistration supplemented by additional supply of COEs during the year. This was supported by the Early Turnover Scheme for commercial vehicles and announcement on relaxation of rules on Motor Vehicle Financing on maximum loan-to-value ratios and loan tenure. The brisk vehicle sales attracted keen interest and competition from financiers such as banks and credit houses. Through strong and continued collaboration with motor dealers and agents, we defended and grew our vehicle loan portfolio.

The property market continued to be subdued with low transaction volumes. The effects of residential market cooling measures persisted, resulting in continued decline in property prices. Resale HDB flats supply was low as owners were putting off selling. Demand by Singapore Permanent Residents was also reduced due to tighter immigration policy and the minimum three-year wait out period rule to buy a resale HDB flat. Notably, more HDB flat buyers took up financing directly from HDB. As the market interest rates increased, these buyers were prepared to pay a slight premium for loans with HDB in exchange for rate stability. To attract borrowers, banks undercut one another on rates. Hong Leong Finance upheld a disciplined pricing strategy to avoid engaging in the price war. We focused on customer retention and yield management. Loan writing for private residential properties also remained selective in view of the unattractive yield.

Commercial property market was also muted. Overall economic pessimism led to lowered demand for office, shop and industrial spaces. Accordingly, new loan market for commercial properties and for development similarly shrank. Hong Leong Finance was cautious with new loan assessment given the weak sentiment and subpar price trend.

Sound underwriting standards and policies were observed for all loans and stringent quality reviews and stress tests were conducted regularly to ensure asset quality was maintained.

Excellent customer service delivery is our linchpin in winning over customers, earning their trust and keeping their loyalty for the past decades. It was about providing them creative and real solutions that met their needs in this fast changing environment.

Our cutting-edge mobile responsive corporate website, launched in December 2015, was a boon to customers. It had interactive search options and offered consumers on-the-go access to bite-sized information on products and services with their handy mobile devices. We challenged the perception of a “corporate” website and in recognition of the superb user interactive interface design in creating a seamless experience for end-users, the website won the title award of the “Best Website of the Year – Singapore Award” at the Asian Banking and Finance Retail Banking Awards 2016 (“ABF”).

Hong Leong Finance also clinched the crown for the third consecutive year as the region’s top finance company with the “ASEAN Finance Company of the Year” accolade at ABF for performing and responding well to challenges, while managing to distinguish ourselves with outstanding products and unparalleled services.

OUTLOOK

Economic risks remain in the economies of major trading partners. Persistent stagnation in the global economy could fuel some of them into trade protectionism. Going into the current year, economic growth for Singapore is expected to be slower.

To keep up our business momentum, we will continue to drive a strategy of building successful alliances and collaboration with partners to build a strong network for outreach and referrals to harness synergies and maximise cost savings. We will also build capabilities and enhance our processes to engage our customers as well as to cut costs and increase productivity.

Confronted with a weak economy, it underscored the importance for us to have a comprehensive, consistent and coordinated approach from sales to service and risk management. Managing credit risk inherent in the entire portfolio as well as the risk in individual credits will continue to be robust.

SMEs in the growth sectors will be in the spotlight. More accessible funding options will be made available to them to help them build up their mettle to restructure, transform and grow further to stay ahead of competition. Lending to HDB dwellers remain a key focus for us.

We continually build trust and confidence from our customers by listening to them and being responsive to their needs. Hong Leong Finance will innovate, invest and create value to support them.

We are also committed to creating values for the communities in which we operate. The Company believes in effecting change, inspiring volunteerism and sharing success while ensuring that our products and services remain accessible to all.

On 14 February 2017, the Monetary Authority of Singapore ("MAS") announced forthcoming changes to Finance Company regulations to enhance the industry's ability to finance and support SMEs. The proposed measures are a relaxation of some of the business restrictions, and as an example include an increase in the limit for the grant of unsecured business loans. The Company welcomes the relaxation which represents further opportunities for the Company to expand its business with SMEs and further support them in their quest to grow and expand both domestically and overseas. Management will actively study the applicable regulatory changes as and when they are phased in by the regulator. MAS also announced liberalisation of their current policy, which disallowed foreign takeover of a finance company, so as to provide flexibility for partnerships or new business models to further strengthen SME financing.

APPRECIATION

I wish to take this opportunity to extend a warm welcome to Mr Kevin Hangchi who joined the Board on 1 October 2016 as a Non-Independent Non-Executive Director. I am sure the Company will benefit from Mr Hangchi's professional experience and counsel. Aged 43 at appointment, he brings to the Board experience and perspectives of the younger age group.

On behalf of the Board of Directors, I would like to convey our sincere gratitude to all our valued customers, shareholders and business partners for their continued support, trust and confidence in us. I would also like to express my appreciation and thanks to my fellow Directors for their invaluable advice and guidance during the year and to the management and staff for their commitment and efforts in 2016.

KWEK LENG BENG

Chairman

24 February 2017