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Hong Kong banking update

From a financial perspective, Hong Kong is still one of the freest places in the world. At a time when the rest of the world is cracking down on its productive citizens and confiscating as much wealth as possible, Hong Kong is actually cutting tax rates (and even issuing tax rebates—shocking, I know) and making things easier for business.

When you step back and look at the situation, it's really no wonder why the economy is so strong. Regulations, taxes, and obstruction to commerce are minimal, so business and trade flourish as people are allowed and incentivized to produce and invest.

If there's anything holding Hong Kong back, it's the currency peg. The Hong Kong dollar has been pegged to the US dollar at it's current rate (7.75-7.85) since 1983, which means that Hong Kong effectively has to mirror US monetary policy.

Low interest rates have caused a flood of cheap money into the Hong Kong real estate market, making it one of the most expensive places in the world to buy property... but quite frankly, aside from property, Hong Kong is actually a pretty cheap place.

On my most recent trip there, I spent an afternoon getting my haircut, eating out at a Korean burrito place (delicious), and took an Uber from Sheung Wan in Central to the Victoria Peak mountain (which has some spectacular views of Hong Kong)—and it all cost me less than $40.

Hong Kong is still an excellent place to plant financial and business flags. We'll talk more about setting up a company in Hong Kong and what they're good for in an upcoming Alert; today I wanted to address personal banking in Hong Kong specifically.

Overall, Hong Kong's banking system remains very sound by world standards. The banks are well capitalized, and have much better liquidity and loan-to-deposit ratios than their Western peers.

What about China?

The dark cloud that has some people worried is what effect the Chinese slowdown will have on Hong Kong banks and the Hong Kong dollar.

We've talked about the current economic trouble in China extensively.

The Chinese economy is slowing down, capital is fleeing the country, trade and exports are declining. Given an unprecedented credit creation in China in recent years, it's inevitable that this will cause serious problems to financial institutions with significant exposure to China.

Mind you, most of the world would still salivate at the prospect of having China's current growth rate. But it turns out that breakneck speed of growth of 10%+ is... well... bound to break some necks.

Undeniably, Hong Kong banks have been extending much larger volumes of credit to mainland Chinese entities during the past decade. So there is some risk.

But Hong Kong still has one of the most advanced, stable banking systems in the world.

And it's backed by one of the most well capitalized central banks in the world—the Hong Kong Monetary Authority, or HKMA, has a capital ratio of 18.9%, versus the Fed's paltry 1.29%.

Plus, Hong Kong is one of the most financially successful governments in the world.

And the Hong Kong Deposit Protection Board (their version of the FDIC) is, unlike most of its counterparts in the West, actually solvent, and **guarantees deposits up to HK$500,000**, or roughly US$64,000, **regardless of the currency the account is denominated in.**

What about the Hong Kong dollar?

As I said, the Hong Kong dollar has been pegged to the US dollar for over 30 years and only trades in a very narrow band of 7.75 to 7.85 HK dollars to the US dollar.

This means that the Hong Kong dollar is a great alternative if your primary currency is otherwise the US dollar, because you're not taking any foreign exchange risk, while keeping your savings in a much safer currency that's backed by a solvent central bank.

At the same time, there's a very real possibility that the peg will at one point be abolished and the HK dollar revalued.

The Swiss did something similar earlier this year; they ended their peg to the euro, giving anyone holding Swiss francs an immediate boost to their savings by 20-30% overnight.

Why would the Hong Kong dollar's peg be abolished?

Because as capital floods out of Chinese yuan and into the HKD, there's enormous pressure for the Hong Kong dollar to rise.

This forces the Hong Kong Monetary Authority to buy USD and sell HKD to weaken the exchange rate and prevent the peg to the USD from breaking to the strong side.

For years, savers in Hong Kong enjoyed what they considered a one-way bet. They could keep their savings in Chinese yuan instead of Hong Kong dollars, earn a higher rate of interest, and enjoy an added bonus from the steady appreciation of the yuan against the Hong Kong dollar.

In the years from 2006 to 2014 the yuan rose from being worth just HK$0.942 to being worth about HK$1.29, at its peak in early 2014.

Since then, the yuan has weakened. Initially, it dropped modestly. But since the Chinese government's move to deliberately devalue the yuan in August this year, it has dropped to about HK$1.22.

Seeing that the trend has changed, and that the yuan is now most likely to weaken going forward, Hong Kong's army of savers has started to reverse this years-long shift into the yuan, and are instead dumping their yuan in droves, and buying back into Hong Kong dollars.

Besides the Chinese and the Hong Kongers themselves, plenty of others realize the benefits of holding HK dollars as well—for example, the appetite for the HK dollar has increased significantly recently among Russian businesses because of US sanctions.

In short, the Hong Kong dollar has rarely been stronger. And Hong Kong's equivalent of a central bank is selling the currency to prevent it from busting up through the ceiling.

I don't personally think the HKMA is going to let the Hong Kong dollar appreciate beyond HK$7.75 = US$1. And they have plenty of ammunition to keep selling HK$ to keep the peg intact.

So, regardless of what happens in China (and in fact even because the Chinese are fleeing the yuan), the Hong Kong dollar remains a strong currency that market forces are actually pushing up, giving it potential for appreciation in the future.

Also, note that Hong Kong experienced much more ominous times before. The 1980s were particularly shaky, and the 1990s saw the Asian financial crisis come and go, plus the scare of the handover of Hong Kong from the UK to China at the same time.

And they've been able to withstand all of that without dropping the peg.

But, as with anything that we advise, you should always do what makes you comfortable.

If you're a US-based person, or have your expenses in US dollars, and you don't want to take any chances whatsoever with the HKD, then it's a simple matter with most Hong Kong banks to shift your money from HKD back into USD.

How to open a bank account in Hong Kong

Opening a bank account in Hong Kong used to be extremely easy just a few years ago. You would walk into any bank branch, have your passport and a proof of address with you, and you'd walk out with a bank account, online banking set up, and an ATM card in half an hour.

We noticed things started to change about two years ago. Banks became unwilling to open accounts for non-residents of Hong Kong; all the banks were terrified of violating some US government regulation, or getting fined billions of dollars.

During my most recent trip to Hong Kong several banks still required that you be a Hong Kong resident in order to open an account—Bank of China and OCBC Wing Hang, for example.

Bankers at HSBC and Citibank did, however, confirm that it's possible for non-residents to open an account. Indeed, several of my friends and colleagues (all non-residents of Hong Kong, including some US citizens) opened an account at Citibank successfully in recent months.

A personal visit to Hong Kong is required, however, to open an account.

One thing to note is that even though Citibank is a subsidiary of a US bank, Citibank Hong Kong is a separate entity with its own balance sheet that conforms to the rules of the Hong Kong Monetary Authority regarding capital requirements and reserve ratios.

So, it's a big step up from banking with the US parent.

Citibank Hong Kong has a liquidity ratio (cash and cash equivalents that it holds as a percentage of customer deposits) of 7.91%, for example.

This tells us how much cash the bank has on hand to pay out depositors before it has to start selling its assets to keep that promise. Most banks in the US and Europe have levels of liquidity of even below 3%, making them very susceptible to a bank run.

I consider this as the primary metric of importance when it comes to a bank's financial health.

Citibank's capitalization ratio (equity as a percentage of total assets) stands at 12.86%.

This tells us what the bank's margin of safety is before it becomes insolvent. If the bank doesn't have enough liquid assets to repay its obligations, then it will have to start selling its other assets—and if it doesn't have enough capital, or equity (total assets minus total liabilities), to support those assets, then the bank will become insolvent and go under, just like Lehman Brothers and many other banks did during the financial crisis.

Again, most banks in the US and Europe are very thinly capitalized, giving them a very fine margin of safety.

Finally, Citibank's' loan-to-deposit ratio is 80%, which is not the most conservative, but is still at the upper end of my range of acceptability.

HSBC Hong Kong's liquidity stands at 10.22% and its capitalization is 8.77%. Their loan-to-deposit ratio, meanwhile, is more conservative at 62%.

It's also interesting to note that HSBC holds physical gold bullion on its balance sheet that amounts to 5% of its current account deposits.

Based on the financial data, I grade HSBC Hong Kong as B+, and Citibank as B at this point.

Overall these numbers are weaker than they were just a few years ago. But they're still far better than the financial condition of most US and European banks.

This is a trend that we're seeing worldwide—banks everywhere are becoming riskier, with their balance sheets deteriorating. It's a reflection that mainstream banking globally is certainly not a risk-free proposition.

This is not something we're pleased about, of course, and it's our job to be objective and look at the facts when talking about solutions that we cover in Sovereign Man.

But when compared to its peers globally, banking in Hong Kong is still one of the best options that exists.

And remember, bank accounts in Hong Kong are covered by an actually solvent deposit insurance scheme of up to HK$500,000.

If you're banking in Hong Kong, your ultimate counterparty is the local central bank, and a government that is actually solvent and has very little debt.

For now we remain comfortable with Hong Kong as a preferred banking destination for transactional banking.

This is the great thing about banks in Hong Kong—they have some of the most competitive fees and lowest exchange rate spreads you'll find anywhere in the world.

Outgoing wires via HSBC's Internet banking platform, for example, are just HK$115 worldwide, or less than US$15.

Citibank's outward remittances worldwide in any currency via its online banking platform are even lower—HK$100 per transaction. And wires to another Citibank account overseas are free.

Fees for receiving international transfers are low as well.

And exchange rate spreads on the Hong Kong dollar/US dollar cross rate are as low as 0.35% with HSBC as well.

But there are some minor irritations to be aware of.

For example, Hong Kong Monetary Authority guidelines now require all Hong Kong ATM card users to register for overseas ATM withdrawals. It's not a big deal, just don't be surprised if you can't withdraw money overseas with your ATM card after opening an account—you need to activate "overseas withdrawals" first.

Many Hong Kong banks also moved away from the global Cirrus/Maestro/Visa/MasterCard networks in recent years and switched to the Chinese payment network called "Union Pay".

And there are still several countries where Union Pay cards simply don't work yet, or where their use is limited. Chile is one example.

For global Union Pay acceptance, see: http://www.unionpayintl.com/en/enserviceCenter/englobalCard

So if access to cash from ATMs while traveling is a priority for you, be sure you quiz your potential Hong Kong bank about it, and make sure they have a solution for you—usually you'll be able to get an additional card from one of the worldwide accepted networks.

Citibank

Bankers at Citibank cite that a **valid reason** to open an account is necessary if you're not a Hong Kong resident.

There are no steadfast requirements for this. It just requires you to demonstrate some sort of link to Hong Kong. For example, a contract with a Hong Kong company, evidence of frequent travel to and from Hong Kong for business purposes, a son or daughter that's dependent on you financially studying full time in Hong Kong, and so on.

As I said, several of my friends and colleagues recently opened accounts at Citibank successfully, with some saying that they're intending to move to Hong Kong and start the residency process there, or that they're about to open a company in Hong Kong and want a personal account as well etc.

All of them walked out with an account and a Visa debit card in about half an hour.

The Visa debit card is good for ATM withdrawals and POS (point-of-sale, or in-person) purchases; it doesn't work online, however. POS transactions are subject to a 1.95% foreign currency transaction handling fee if effected in a currency other than Hong Kong dollars.

The card gives you **free ATM withdrawals worldwide**, though, which is a great perk. (To be clear, Citi won't charge an ATM withdrawal fee, though the local ATM might.)

You can also apply for a credit card, for which you need to place a minimum of HK$50,000 in a term deposit (like a CD, or certificate of deposit).

The minimum deposit to open a checking account is HK$10,000 (US$1,290), and if your balance goes below that amount, there's a monthly service fee of HK$400 if you're a non-resident.

You don't have to fund the account in cash when opening an account—you can do it within 30 days by wiring the money as well.

Your online banking security device gets sent to you by mail and you should receive it within two weeks.

All you need to open an account is to walk into any Citibank branch in Hong Kong with your passport and proof of address.

The proof of current residential address can take the form of a utility bill—an electricity, gas, or water bill is best. But a bank statement or a secondary identity document that has your address on it, such as a driver's license, may also be accepted—and indeed that's what my friends used recently.

The utility bill or bank statement cannot be more than three months old. And the name on it must match that in your passport exactly

HSBC

Not long ago, HSBC was among the banks in Hong Kong that stopped opening accounts for non-residents, as a result of several scandals that HSBC was involved in globally.

Recently it was revealed that Colombian drug cartels used banks in Hong Kong to launder billions of dollars, and HSBC US division was already fined US$1.9 billion a few years ago for allowing Mexican and Colombian drug cartels to launder proceeds through its banks.

So HSBC has become a bit twitchy about their customers.

But on my recent trip to Hong Kong, they were still willing to open personal accounts for non-residents, including US citizens.

The requirements at HSBC are essentially the same as with Citibank:

- Passport and proof of address (bank reference letter or correspondence, driver's license, utility bill),
- Minimum deposit of HK$10,000,
- And a valid reason to open an account.

They may also ask you to provide proof of funds. This can either take the form of:

- Savings/return on investment: bank statement, investment statement, land search
- Pension: benefit statements for the past 3-12 months
- Business statement: tax bill, company document, annual report, receipt of earnings etc.
- Inheritance: will, estate document, trust document
- Property sale proceeds: agreement for sale of property

There are three levels of personal accounts at HSBC.

The 'Smart Vantage' account has a minimum balance of HK$10,000, the 'Advance' account has a minimum of HK$200,000, and the 'Premier' account has a minimum of 1 million HKD—roughly US$125,000.

The transactional pricing structure for each account type is essentially the same—like I said, sending a wire transfer worldwide, for example, will cost you only a bit over US$14.

Each account type also has access to HSBC's gold deposit services—an unallocated 'paper gold' solution without physical possession.

The key difference among the accounts is increasing levels of prestige and service. Premier members are serviced at any HSBC Premier center around the world, have access to a global concierge service, receive a free credit card, get a dedicated relationship manager, and enjoy even better exchange rates, for example.

But for the casual bank customer the difference may be trivial.

Conclusion

So, let's recap—a bank account in Hong Kong is a great idea because:

- The banks in Hong Kong are much safer than their counterparts in the West, with better liquidity and capitalization, and lower loan-to-deposit ratios.

- Hong Kong is one of the most important financial centers in the world, so the banks there are used to dealing with foreigners, and are especially great for transactional banking. It also means that you could move half a billion dollars into Hong Kong and it wouldn't cause a blip on the radar.

- The Hong Kong Monetary Authority and the Hong Kong government are actually prudent institutions, with ample tools at their disposal should any type of financially cataclysmic event occur.

- As a result, the Hong Kong dollar is a great alternative to keep your savings in, especially if your primary currency is otherwise the US dollar and you don't want to take the foreign exchange risk. So in many ways, your downside is protected, but you still get the upside potential if the US dollar peg is revalued or abandoned. And since the central bank is so highly capitalized, the currency risk is quite low.

On the other hand, it's worth noting that the numbers for banks in Hong Kong (as well as all over the world) have gotten worse in recent years. We would of course like to see that trend reverse, but we're still comfortable recommending banking in Hong Kong, and indeed bank there ourselves.

We will let you know if the recommendation changes.

As an aside, we're also examining banks in Singapore and will update our view on their financial health and risk level in an upcoming Alert.