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$45b Midland price tag

HK Bank discloses reserves of $16.6b

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THE Hongkong Bank group last night revealed an offer for Midland Bank which values the British bank at $45 billion.

The chairman, Mr William Purves, said the offer, a combination of stocks and bonds, was worth 27 per cent more than Midland's actual value.

The terms of the offer, which appear as an eight-page section in today's *South China Morning Post*, disclose the Hongkong Bank's best kept secret – the size of its inner reserves.

HSBC Holdings, the holding company for the Hongkong Bank Group, had accumulated $16.6 billion by the end of last year, stashing away large amounts before declaring each year's profits.

The Hang Seng Bank, of which Hongkong Bank owns 61 per cent, holds $7.1 billion of the group's inner reserves.

In addition, the group had also undervalued investments to a value of $6.7 billion, meaning the bank actually had hidden capital worth $23.3 billion.

The Hongkong Bank group has held just over 14 per cent of Midland since 1987, but announced the planned merger four weeks ago after it appeared the UK bank was recovering from the ills of the recession.

Acquisition of the remaining 86 per cent will cost the Hongkong Bank $38 billion, based on the exchange rate of HK$14.56 to the pound used in the merger papers.

INSIDE
Business Post
Page 1: Brokers react
Page 4: US Marine Midland in the black
See also 8-page special section

If shareholders of both groups approve the deal, the merged group will have 3,300 offices in 68 countries and assets of £145 billion (HK$2,100 billion).

The holding company, HSBC, would be headquartered in London and come under the lead regulation of the Bank of England, but the Hongkong Bank would keep its headquarters in the territory.

Mr Purves said both Hongkong Bank and Midland would benefit from the merger, since the enlarged bank could capitalise on growing investment and trade between Europe and Asia.

"I don't think the board of HSBC would be recommending this purchase if in the long term and the medium term . . . we weren't buying a very valuable asset that has very good growth potential," he said.

HSBC Holdings will offer stock and bonds worth £3.78 for each Midland share, which represents a 27 per cent premium over the net asset value of £2.99 per share.

HSBC shares in London initially climbed to HK$40.50 from $39.50 when the details of the merger were announced but settled back to $39.90 in afternoon trading.

Midland stock, which was £2.53 when the merger was announced four weeks ago, was trading at about £3.70 yesterday afternoon. London analysts said the price was suppressed when the Kuwait Investment Office, which held more than 10 per cent of Midland's stock before yesterday, began selling three-quarters of its stake.

Hongkong analysts are largely sceptical of the merger, saying HSBC shareholders would receive better returns if the group concentrated on Hongkong and the Asia Pacific region.

They are also concerned that the cost of the merger is £190 million, and that HSBC will make a provision of £200 million against tax increases that will come from being a UK resident company.

But some analysts say the revelation of the inner reserves should help to buoy the HSBC share price in the short term, and the Hongkong Bank did well to negotiate a takeover price of £3.78 per share.

HSBC also announced yesterday that Marine Midland Bank, its perennial money-losing subsidiary based in Buffalo, New York, earned US$2.6 million (HK$20.1 million) in the first quarter, compared with a loss of US$72 million in the first quarter of last year.