

Speech

PSFS' Speech at the Luncheon Hosted by the Toronto Section of the Hong Kong Canada Business Association

11 June 2010

Mr. Armstrong (Bob), Mr. Matheson (David), ladies and gentlemen,

Good afternoon to you all. It is indeed a pleasure to be back to this wonderful city. Hong Kong and Toronto have been enjoying close friendship. Among the 2.5 million population in Toronto, about 400 000 (4%) come from Hong Kong. Really I do not know anybody in Hong Kong who does not have a relative or friend in Toronto. May I thank the Hong Kong Canada Business Association and our Toronto Office for organising this luncheon, which provides a valuable opportunity for exchanges between the two places.

Today I would like to speak briefly on how we position Hong Kong as an international financial centre (IFC). The financial services sector is one of our major economic pillars, accounting for 16% of our GDP and 6% of our workforce. We have achieved quite a lot, and aspire to achieve even more.

A snapshot

To start with, let me give you an update on our post-tsunami development. Hong Kong economy has bounced back four quarters in a row. By the first quarter of 2010, GDP has largely recouped all the lost ground in the 2009 recession. Given the current economic momentum in Hong Kong and in the region, and barring any major external shocks, real GDP growth for 2010 as a whole may exceed our earlier forecast of 4-5%. But of course latest news on European woes has brought uncertainties.

To reflect, Hong Kong has weathered the tsunami relatively well when compared to many economies. The Government acted swiftly, reassuring the industry and the public that the necessary measures would be taken to mitigate the crisis. Our financial system has remained relatively stable. The stock market stays robust. Our clearing and settlement

system remains smooth and efficient. No financial institution in Hong Kong required a bail-out. Our banking sector remains healthy and well capitalised. For example, the capital adequacy ratio of our locally incorporated banks is 16.9%, far above the Basel standard of 8%.

There is however no room for complacency. We spare no effort to sharpen and capitalise our strengths in positioning ourselves as an IFC. These include [our simple and low taxes, free flow of information and capital, a stable and fully convertible currency, a predictable and certain regulatory regime, a versatile and flexible workforce, as well as a free economy buttressed by the rule of law and an independent judiciary.

IFC Strategic Positioning – Market Development

During the financial tsunami, a new economic order has emerged, with Mainland China playing a more prominent role in the international financial arena, and the centre of gravity moving more to the East. Hong Kong is participating in and facilitating this process, and as a result, further strengthening our position as an IFC. Our strategic focus is on three key areas, namely offshore Renminbi (RMB) business, asset management and capital formation. Let me walk you through these briefly.

Hong Kong as an offshore RMB centre

First, Hong Kong as an offshore RMB centre.

China has announced its policy goals for the internationalisation of RMB. It has to map out its strategies with care to avoid undermining its financial security. Through the development of offshore RMB business in Hong Kong, Mainland China can make use of Hong Kong as the preferred testing ground for RMB reforms before the capital account becomes fully open. We believe this is the best way to promote the use of RMB outside the Mainland in an orderly manner.

Banks in Hong Kong can now offer a range of RMB services, including RMB deposit-taking, loans, bonds issuance and trading, and trade settlement and related services. At the end of April 2010, the outstanding RMB deposits in Hong Kong totalled RMB 80.9 billion.

Hong Kong is the first and only place outside Mainland China that has developed a RMB bond market. Since 2007, there have been 13 RMB bond issues in Hong Kong, totalling RMB 38 billion (including RMB 6 billion of sovereign bonds launched for the first time in 2009). The RMB Trade Settlement Scheme was launched in July 2009, fully leveraging our RMB settlement and clearing platform, which is the most effective and largest outside the Mainland. Under this scheme, we provide RMB trade settlement services for enterprises in the Mainland trading with Hong Kong and ASEAN members.

To further develop Hong Kong as an offshore RMB centre, we have adopted a three-prong approach -

- First, attracting RMB liquidity. Since last February, the RMB Trade Settlement Scheme has been expanded to cross-border trade in services. We seek to cover more enterprises in the Mainland and other trading partners as we go forward.
- Second, developing more RMB denominated products. These would require joint efforts with the market in issuing corporate bonds, ETFs and other funds, insurance policies, etc.
- Third, allowing more RMB market players to perform an effective intermediation role. These would require modification of existing regulations governing transfer of RMB between accounts in Hong Kong.

With greater liquidity, more products and more market players, we expect to anchor a critical mass of RMB business in Hong Kong.

Hong Kong as an asset management centre

Second, Hong Kong as an asset management centre.

We have a sizeable fund management business, over 64% of which is sourced from overseas investors. We are an attractive location for overseas fund managers to conduct asset management business. We have no tax on sales, capital gains or dividends. We have abolished estate duty and exempted offshore funds from profits tax since 2006.

Further fiscal incentives for the fund management industry were announced in our Budget in February this year.

After the financial tsunami, the strong rebound of China's economy has spearheaded the overall economic recovery of Asia and created abundant investment opportunities in the region. Asia is now the bright spot in the eyes of global institutional investors.

More global institutional investors are giving greater weight to Asia in their investment portfolios. At the same time, there is a growing demand for wealth management services for Mainland investors. Hong Kong is well placed to serve both, with our access to the Mainland and international markets.

To further promote our asset management business, we shall continue to step up our marketing efforts, enhance market quality and facilitate market development, which I would talk about in a moment.

Hong Kong as a capital formation centre

Turning to Hong Kong as a capital formation centre, we were the most active market for IPO funds raised in 2009. We raised US\$31.3 billion through IPOs, putting us as number one in the world. A total of 73 companies were newly listed on HKEx. They included Mainland companies, as well as overseas companies with business operations in China. They are attracted by our liquidity, valuations, access to international investors, and corporate governance.

We are committed to broadening the source of listed companies. To this end, our stock exchange has accepted a number of new jurisdictions as issuers' place of incorporation and tailor-made IPO vetting practices for overseas companies to facilitate their listing. Over the last few months, we have seen newly listed companies coming from Russia, Canada, France and the UK, in addition to the Mainland.

We shall continue to attract quality overseas companies to list in Hong Kong by streamlining the listing process.

For example, HKEx has just implemented a set of improved Listing Rules for mineral and exploration companies last week. Our aim is to bring such Rules more in line with international standards, and to ensure that investors will be provided with material and reliable information.

IFC Strategic Positioning – Market Quality

In parallel, we attach importance to upgrading our regulatory regime to ensure market quality. We believe that only a quality market can be a sustainable market in attracting quality products and players.

Here, I would highlight a few financial market reform initiatives that are in different stages of implementation in Hong Kong.

Strengthening Investor Protection

First, strengthening investor protection.

Under our current system, financial regulators have full power to handle complaints against the conduct of market intermediaries, but not monetary disputes with their clients. We have therefore proposed setting up a Financial Dispute Resolution Centre to help aggrieved investors to have such disputes with financial institutions settled through a simple and quick resolution mechanism. We have just consulted the public and are drawing up conclusions for implementation.

To further improve the transparency of our stock market, we are consulting the market on a legislative proposal to oblige timely disclosure of price sensitive information by listed companies. We are committed to cultivating a continuous disclosure culture among the directors and senior management of the issuers.

We are also tightening the regulation of the sale conduct of financial intermediaries. New measures include requirements to clearly segregate banks' business in deposit-taking and securities investment for retail clients; to audio-record the sales

process; to disclose commissions and fees in the sale of investment products, and to introduce a cooling-off period for unlisted structured products.

Better Safety Nets

Second, better safety nets.

Starting from January next year, the compensation ceiling under our Deposit Protection Scheme will be raised five times higher to HK\$500,000, or nearly C\$65,000 at 7.6. This will tie in well with our exit from the 100% deposit guarantee introduced at the height of the tsunami in late 2008.

At the same time, we propose to establish a Policyholders' Protection Fund for the insurance sector to improve insurance market stability and safeguard the interest of policyholders if an insurer defaults. We aim to consult the public later this year.

Modernising Legislative Framework

Third, modernising legislative framework.

We recognise the need to update our laws to allow them to evolve with market needs. For instance, we are modernising our company law to enhance corporate governance, facilitate business operation and save business costs.

We are also reviewing our trust law to strengthen the competitiveness of our trust service industry.

With growing interest in China-related products, Hong Kong is well placed to tap the opportunities of Islamic finance. We are changing our laws to facilitate the issue of Islamic bonds in light of their special share-pain-share-gain features.

These are some ongoing efforts to ensure that our legislative framework is user-friendly for market participants.

Evolving International Standards

Fourth, as an IFC, Hong Kong has the duty to fulfil international obligations and comply with international requirements.

For example, we are preparing legislation to enhance our anti-money laundering regime by imposing customer due diligence and record-keeping requirements on financial institutions, in line with the standards set by the Financial Action Task Force (FATF).

We have amended our law in March to facilitate information exchange between our tax authority and their counterparts overseas, in line with standards set by the Organisation for Economic Cooperation and Development (OECD). This has enabled us to enter into comprehensive agreement for the avoidance of double taxation with more economies (CDTA). We have signed 11 CDTAs and expect more to come. CDTAs help relief tax burden on individuals and enterprises and eliminate uncertainties over tax liabilities. They will therefore help improve the business environment and facilitate flows of trade, investment and talent between Hong Kong and the rest of the world.

Last but not least, we will ensure that our regulatory regime is in keeping with the evolving international standards. We are monitoring developments on the G20 front, including new regulations for systemically important financial institutions, OTC derivatives, hedge funds and credit rating agencies. These would have an impact on market players in Hong Kong who serve clients overseas. This is also part of the mission of my visit to the United States and Canada – to find out more about the latest regulatory landscape and consider need for adjustments to our own regime.

Closing

With my brief update just now, you could probably visualise how our financial services sector will develop further in the areas of offshore RMB business, asset management and capital formation, with the support of quality services on par with international standards. We see great potential for Hong Kong to flourish as an IFC with unlimited potential, provided that we continue to leverage and sharpen our strengths.

Ladies and gentlemen, I welcome you all to play a part in it. If you are looking for investment opportunities, Hong Kong is the prime location especially for tapping into Greater China. If you are looking for business expansion, Hong Kong is your definite choice for your regional foothold. If you need assistance in this regard, I am sure colleagues in our Economic and Trade Office here are more than happy to help.

Now, let's open to the floor. I'm most delighted for your questions and feedback. Thank you very much.



Miss Au King-chi, Permanent Secretary for Financial Services and the Treasury (Financial Services), today (June 11) speaks at a luncheon hosted by the Toronto section of the Hong Kong-Canada Business Association. She highlights government strategic focus on Renminbi offshore business, asset management activities and capital formation

services, in further developing Hong Kong as an international financial centre.



Miss Au King-chi, Permanent Secretary for Financial Services and the Treasury (Financial Services) of the Hong Kong SAR Government, today (June 11) visits Toronto after attending the International Organization of Securities Commissions' 35th Annual Conference in Montreal. Picture shows Miss Au, together with the leaders of the Toronto section of the Hong Kong-Canada Business Association (HKCBA), at a luncheon seminar at the Royal York Hotel. (*From left to right*) David Matheson, Special Adviser to the Federation of Hong Kong Business Associations Worldwide; Ms Sonja Chong, former HKCBA President; Miss Au King-chi, and Bob Armstrong, current President of HKCBA Toronto.