Speech

Speech by SFST at "Hong Kong: China's Global Financial Centre Conference" in London
(English only)

Tuesday, November 16, 2010

Following is the speech by the Secretary for Financial Services and the Treasury, Professor K C Chan, at the "Hong Kong: China's Global Financial Centre Conference" in London today (November 16, London time):

Distinguished guests, ladies and gentlemen,

It is a great pleasure to return to London for the second time this year. The vitality of the city is something that hits you as soon as you step off the plane.

London has always led the global financial markets. It is the trend-setter on the direction of financial services and the innovator of financial products. It is also the benchmark-maker when it comes to regulating the financial industry. Everyone including myself is at awe with the international talent pool London has been able to attract. London is the role model for what a financial hub should entail.

Today, post-financial crisis, some people question whether London could retain its glory as a global financial centre. I, for one, believe that any such worry is much misplaced. London will always remain an important international financial centre for the world and especially for Europe because of the solid foundation it has laid on its financial infrastructure, the strength of its financial regulation and the openness of its market.

The global financial crisis has caused a set back in the development of our global financial services industry. New regulation formulated post-crisis added uncertainty and costs to the industry. But I believe nothing will detract the financial market from being an important pillar of our global economy because we need it to facilitate economic growth and add value to businesses. The basic economic reasons for the emergence of global financial centres have not been shaken by the crisis. I have confidence in London to continue to fulfil this role.

<u>Hong Kong</u>

We believe in Hong Kong's potential as an international financial centre. There is a great deal of similarities between London and Hong Kong. We have many strengths in common and they lay the foundation to an international financial centre. These include freedom of the flows of capital and information, a common law system, and a robust regulatory regime.

Hong Kong's unique simple and transparent taxation system, and our time zone advantage in a global trading platform, add to our appeal as an international financial centre.

Hong Kong and London have always followed similar paths on market development. We consistently rank alongside each other as an international financial centre.

We are two out of the top three global financial centres ranked by the Global Financial Centres Index compiled by Z/Yen Group.

We are two out of three leading global financial centres referred to as "Nylonkong".

We are both huge asset management centres managing significant amount of overseas money.

The relatively recent development of the offshore Renminbi (RMB) business has added yet another resemblance between this city and ours. We are both offshore markets to a major currency not our own.

Half a century ago, the Eurodollar market started to develop in London. Today, the amount of US dollar in circulation in London is 2-3 times the amount of US dollar in US' domestic banking sector.

Hong Kong's offshore RMB market is still at its infancy stage. The size of the RMB market in Hong Kong is 1/500 of onshore RMB deposits, but this only goes to show the potential our offshore RMB business has installed for us.

While our two markets may compete in some aspects of global business, the primary focus of our two centres is to serve our respective regional economies.

Hong Kong will always play an important role for Asia and China much like what London has done for the EU.

The British Chancellor of the Exchequer Mr Osborne remarked in Hong Kong last week, London is a partner of Hong Kong. I can't agree more. We are both pulling our weights in our respective markets, but we can serve our clients even better when we partner up.

<u>Hong Kong's role for China</u>

Hong Kong has often been described as a gateway to China. That is certainly correct if you think of the movement of goods, people and even capital – as Hong Kong is the largest foreign direct investment (FDI) provider to China.

But Hong Kong serves as a gateway in another sense. Hong Kong has always been a testing ground for new ideas in the opening of China's financial market. Experimentation done in Hong Kong heralded much bolder reforms that have contributed to the success of the China's economic development strategy.

Take a look at the history of the listing of Chinese companies' shares in the Hong Kong market. In 1993, we saw the first mainland state - owned enterprise listed on the Hong Kong Stock Exchange - that is the historic listing of Tsingtao Brewery. Back then, China had no capital market and most companies were state-owned. Those mainland companies had no corporate governance structure nor did they comply with international accounting standards. Hong Kong saw the opportunity and actively lobbied for Chinese companies to be listed on our stock exchange.

The Central Government appreciates that having a Hong Kong listing would bestow investors' confidence on these mainland companies. The established market discipline in Hong Kong brings them international best practice standards in corporate governance, accounting, disclosure and management. Hong Kong listing also gives them attractive valuations and access to a deep international liquidity pool and we have professionals to advise along the way.

China's state-owned banks were previously considered inefficient in operation and offered low rate of return for shareholders. Hong Kong played an important role in their reform. All four state-owned banks were successfully listed on Hong Kong's stock exchange in recent years. All the IPOs received good response from the market and the banks gained reputation on their corporate governance and regulatory standards.

There has been no stopping ever since the first H Shares listing in 1993. As of end-September 2010, 556 Mainland enterprises were listed in Hong Kong, raising a total of US$351 billion.

Last year, Hong Kong ranked number one in the world for IPO funds raised. Total funds raised in Hong Kong through IPOs exceeded US$31 billion in 2009. IPO funds raised this year will be even higher than in 2009.

Looking at history, Hong Kong has time and time again contributed to market reform in Mainland China. Hong Kong will continue to do so in the future as the Central Government has reiterated on various occasions that it supports consolidating Hong Kong's role as an international financial centre, and leveraging Hong Kong's advantage in serving as the testing ground for the Mainland's financial reform and liberalisation.

Potential for RMB trade settlement

A new phase of the market reform in China is the internationalisation of the RMB and the gradual opening-up of the capital account.

And how does that happen? It is through the use of RMB to settle cross-border trades, and with that, to build up a pool of RMB liquidity offshore. The RMB residing offshore can be used to finance direct investments on approved projects in China, in addition to the trade settlement use. An offshore financial market will develop to offer banking facilities on trade settlement, capital market products for fund raising and wealth management products desired by investors holding the RMB.

There is no better place than Hong Kong to become the offshore RMB centre.

Hong Kong is in a good position to facilitate RMB trade settlement because we have a well established international banking centre with about 70 of the world's 100 largest banks operating in our city and networks sprawling across Mainland and rest of Asia.

What is the potential magnitude of RMB trade settlement? Mainland China is the world's leading exporter, and Hong Kong handles about 25% of mainland China's exports. HSBC's global trade survey estimates that about 20% of Hong Kong's mainland China's trades would be settled in RMB. On that basis, RMB trade settlement in Hong Kong has the upside potential of increasing by 40 folds over the medium term from the modest RMB40 billion a year we saw from the inception of the scheme last year.

Hong Kong is also the largest provider for direct investment into China, the traditional conduit for capital movement into China. About 51% of China's direct investment is originated from Hong Kong, reaching US$46.1 billion in 2009. About 63% of China's overseas direct investment is also conducted through Hong Kong, reaching US$35.6 billion in 2009.

Hong Kong has the policy blessing from the Central Government to develop our off-shore business. Since the introduction of the cross-border RMB trade settlement scheme, we have seen a rapid growth in the RMB interbank market, RMB deposits, and the offer of RMB-denominated financial products in Hong Kong. There is a strong appetite for RMB investment products and we have the infrastructure in place for trading these products.

Hong Kong being a distinct market insulated from the Mainland and with the advantages of having a freely convertible currency and an established RMB business and banking infrastructure provides the ideal testing platform for mainland's capital account liberalisation. The development of an offshore market in Hong Kong is also able to provide some benchmarks for policymakers to consider the next step in the liberalisation of the capital accounts.

Hong Kong v. Shanghai

There has been lots of reporting on rivalry between Shanghai and Hong Kong on who is to become the most important international financial centre of China. But what some reports have missed, and I don't blame them, because the co-ordination has gone without glitches, is Hong Kong and Shanghai's joint development of China's capital market in the past. Our two cities have the perfect collaborative relationship to our mutual advantage.

With the mainland A shares listing, Shanghai was able to help mainland enterprises raise onshore funds. The same enterprises would come to Hong Kong for a H shares listing to get access to international investors. Through dual listing, these mainland enterprises have the best of both worlds - they are able to tap a diversified investors' base to their fullest advantage.

The teamwork which Hong Kong and Shanghai showcased on the listing of A/H shares is just the beginning of our financial collaboration. We expect this partnership to continue into other financial services including the development of RMB business.

Why Hong Kong?

Why Hong Kong? Hong Kong to Asia and China is what London is to Europe. Like London, our regulations are of a high standard. Like London, we have a free and open economy. Like London, we have the infrastructure and professional talent to support our financial services. Add to that, our relationship with China and proximity to the rest of Asia. I need say no more.

Let's partner up London, and mark our places in the league of tomorrow's leading global financial centres.

Thank You.

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