Speech

Speech by SFST at ASIFMA Annual Conference 2013 (English only)

Wednesday, November 20, 2013

Following is the speech by the Secretary for Financial Services and the Treasury, Professor K C Chan, "Financial Markets Development: Opportunities and Challenges for Asia" at the Asia Securities Industry & Financial Markets Association (ASIFMA) Annual Conference 2013 today (November 20):

Mr (David) Ratliff (Chairman, ASIFMA), Mr (Mark) Austen (CEO, ASIFMA), Mr (Takehiko) Nakao (President, Asian Development Bank), distinguished guests, ladies and gentlemen,

Good morning. I am pleased to join you all today at the inaugural ASIFMA Annual Conference. I would also like to thank the ASIFMA for hosting the conference in Hong Kong. A warm welcome to everyone, in particular those who have flown all the way here.

The focus of the conference is on "Developing Asia's Capital Markets". It is fair to say capital markets in Asia are less developed, both in terms of the sizes and the stages of development, in relation to the physical sizes of their economies. The reasons for this phenomenon are many.

Firstly, Asian finances are still being dominated by banks. Then, in an attempt to facilitate capital market development, the drawing up of rules and regulations to attract capital on one hand, and to regulate market activities to protect investors' interests on the other, while maintaining financial market stability is often lagging behind the development of regulations required for trading of physical goods in the region.

Furthermore, financial integration also lags behind the integration in trade and the real economy in Asia. This in turn limits the growth of individual countries' capital markets, as well as the potential size of the region's capital market as a whole. The factors causing the slow progress in financial market integration include different degrees of financial infrastructure development in different Asian economies, restrictions on capital movements, the differences in regulation, and market fragmentation.

It is of vital importance that Asia's financial market must grow in breadth and depth if Asia is to keep the momentum of growth at the rate experienced in recent years. Expanding economies in Asia have continuous needs to tap investment funding to finance infrastructure and industrial development. Financial market development is essential for an efficient allocation of capital to support economic growth.

While more effort is needed to deepen the development in individual capital markets in Asia, more emphasis should also be put on cross-border financial integration, which will further improve the efficiency of these financial markets. With greater deepening of individual markets and market integration on a regional level, we can better channel the savings to serve the investment needs. We can also diversify the funding sources for our region to the extent that longer term funding sources can be tapped, to counter the effects of short-term capital flows originating from outside the region.

For policymakers, attention should be focused on building up the financial market infrastructure because financial development can only take place in well-functioning markets. In addition, we should encourage standardisation in market practices and regulation across countries to facilitate cross-border financial activities. For instance, standardisation of documentation and regulatory practices could lower the costs incurred in issuing local currency bonds and selling them across the region. Projects such as cross-border recognition of mutual funds products are good ones to take on to broaden the sizes of the funds markets in the region.

In Hong Kong, we are working very closely with the Mainland authorities to study the feasibility of mutual recognition and cross-border offering of funds between Hong Kong and the Mainland. This initiative, once implemented, will greatly expand the investor bases for funds and securities in both jurisdictions.

Turning to the various building blocks in the Asian capital market, we can see that the equity markets in general are more developed but the bond market is less developed. I do think that more focus should be put on developing a healthy private pension fund industry to improve the depth of our regional capital market. So, let's take a closer look at these markets.

In the past two decades, equity markets in Asia have grown rapidly in size and sophistication, even though they are still lagging behind many advanced economies in terms of depth and cross-border integration. Many Asian companies have successfully tapped our equity markets to fund their growth. Some centres, Hong Kong inclusive, are building up their equity markets which are globally significant. There is also some movement in the linking up of equity markets through the cross-listing of equity products or listing of cross-market exchange-traded funds.

The Asian bond markets, however, have much room for development. After the Asian Financial Crisis in the 1990s, Asian countries have embarked on projects such as the Asian Bond Markets Initiative, which aimed to develop efficient local currency bond markets, to enable more efficient utilisation of the region's savings. The scale of these initiatives, however, remains relatively small as compared to the size of the region's economies.

In Hong Kong, measures have been taken to promote the local bond market. In 2009, we launched the Government Bond Programme and have since doubled the programme size to HK$200 billion. We have also updated our regulations to enhance Hong Kong's competitiveness as a platform for the Islamic bonds, or sukuk, market by providing a level playing field vis-à-vis conventional bonds.

The rise of the offshore RMB markets has given a fresh impetus to our bond market initiative. Starting from scratch in 2004, Hong Kong is now the world's largest offshore RMB business hub, with the world's largest offshore pool of RMB funds, standing at RMB908 billion at the end of September. We have seen steady growth in the market for Hong Kong offshore RMB bonds, dubbed the "dim sum" bonds, since its birth in 2007. A total of 89 "dim sum" bonds had been issued in the first 10 months of this year, valued at RMB80 billion.

The Chinese Ministry of Finance has also been offering RMB denominated bonds in Hong Kong since 2009, with a total notional amount of RMB80 billion and maturities up to 30 years. The latest batch of RMB10 billion will be issued, in fact, tomorrow. The China Development Bank has also offered the first public floating notes linked to the CNH HIBOR benchmark from a Chinese issuer this month.

In Hong Kong, as in other parts of Asia, the bond market is still small and less developed relative to our robust financial market. But by encouraging the growth of a bond market denominated in RMB, the growth of the RMB as a significant international currency can boost up the market.

Another area that deserves our attention is the development of our pension fund industry. Saving for retirement represents a long-term challenge for most economies in the world, as we are all facing the inevitable prospect of an ageing population. This is even more true for Asia, and it should be our goal to develop a healthy pension fund industry to help our people to save for the future.

A vibrant pension fund industry is an important component of our capital market, for it helps in channelling savings to a productive use. From a policy perspective, a private pension fund industry with a high level of participation from the working population is an important pillar of our retirement system to provide the necessary safety net for our community. It encourages private individuals to take responsibility for their future retirement needs, and lessens the burden on the state as well as on taxpayers in the future. It is an example of how to make use of finance to serve the real economy and meet the real needs of our working population.

In Hong Kong, we launched the Mandatory Provident Fund (MPF) Scheme in 2000 as an important pillar of the retirement system for our working population. Employees and employers are required to set aside a portion of one's salary in a separate trust account. Each employee is able to invest the funds in his name in a variety of funds provided by private scheme operators. Scheme members can withdraw the funds after they turn 65.

With a short history of a little more than 10 years, the Mandatory Provident Fund Schemes Authority (MPFA) is still in a developmental stage. But our experience so far reveals two challenges to be tackled. First, many scheme members have difficulties in knowing what funds to invest in, and some adopt an active investment style with too much switching in and out of funds rather than taking a more patient long-term approach. Second, the fees of the funds are high, probably reflecting the high administrative costs of the scheme, partly due to the flexibilities provided by the scheme.

I mention our experience of our MPF Scheme because in our case, even though our financial market can provide a solution to some real problems, a lack of a good understanding of the basic financial principles by members of the public might have a negative impact on the public acceptance of the system.

The Government and the MPFA are working to improve the MPF System. I think the solution lies in the introduction of some relatively low-cost funds that are designed for long-term investing. There should also be public education about what funds are suitable for retirement planning purposes, and the benefits of long-term investing. When we have some concrete proposals we will bring them to the public for consultation.

One lesson I draw from our experience with the MPF Scheme is that public confidence in the pension fund industry is key to the success of the industry. And generally, the development of the capital market hinges upon the public's confidence in our financial market and its ability to help us solve the society's problems.

Finally, I would like to touch on the work we are doing on the regulatory front. To facilitate the continued development of our market and its integration with the rest of the world, it is important that we uphold the highest international standards for risk management and investor protection. We have commenced the legislative process to implement the G20 commitments on over-the-counter (OTC) derivatives regulatory reform. The Hong Kong Stock Exchange has taken the lead to set up OTC Clear, the local central counterparty, which is expected to commence operation this month. The Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) are working closely with their overseas counterparts to ensure smooth transition to the new regime.

The HKMA and the SFC are also active participants in cross-border co-ordination efforts. The SFC co-chairs the Working Group on Margining Requirements of the Basel Committee on Banking Supervision and the International Organization of Securities Commissions (IOSCO) for non-centrally cleared derivatives, with the HKMA as a member of the working group. The HKMA is a member of the Financial Stability Board's OTC Derivatives Working Group, whereas both the HKMA and the SFC are members of the Committee on Payment and Settlement Systems - IOSCO Task Force. The SFC also chairs the IOSCO Asia-Pacific Regional Committee and participates in the OTC Derivatives Regulators Group. There is a need for all Asian regulators to participate in global discussions to address issues of global challenges. We need to have an Asian voice in the global regulatory reform process. Your participation and input are very welcome.

We are working together with local regulators to draw up proposals to bridge the gaps which exist in our current resolution regimes for different types of financial institutions relative to the Key Attributes of Effective Resolution Regimes for Financial Institutions published by the Financial Stability Board in 2011. In drawing up the proposal for the resolution regime, one of the key areas is cross-border co-operation, which is crucial to the effective enforcement of resolution. We aim to consult the public and the financial services sector in dealing with large and complex financial institutes and cross-border groups before the end of this year.

I hope I have made it clear to you why it is important for Asia to further develop its financial markets and what we have been doing in Hong Kong to further improve the quality of our financial markets, and to foster cross-border use of the RMB and to facilitate global regulatory reforms.

I would like to congratulate the ASIFMA on the successful organisation of your inaugural ASIFMA conference here. The remainder of what is a very packed two-day programme will no doubt give us much food for thought in this age of economic shifts and regulatory changes. But please don't forget to spare some time to go out to see and appreciate what Asia's world city can offer.

Thank you.

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