

**Business Activities Surveys  
on Securities / Futures Intermediaries  
and Exempt Persons**

證券/期貨中介機構及  
獲豁免人士  
業務調查

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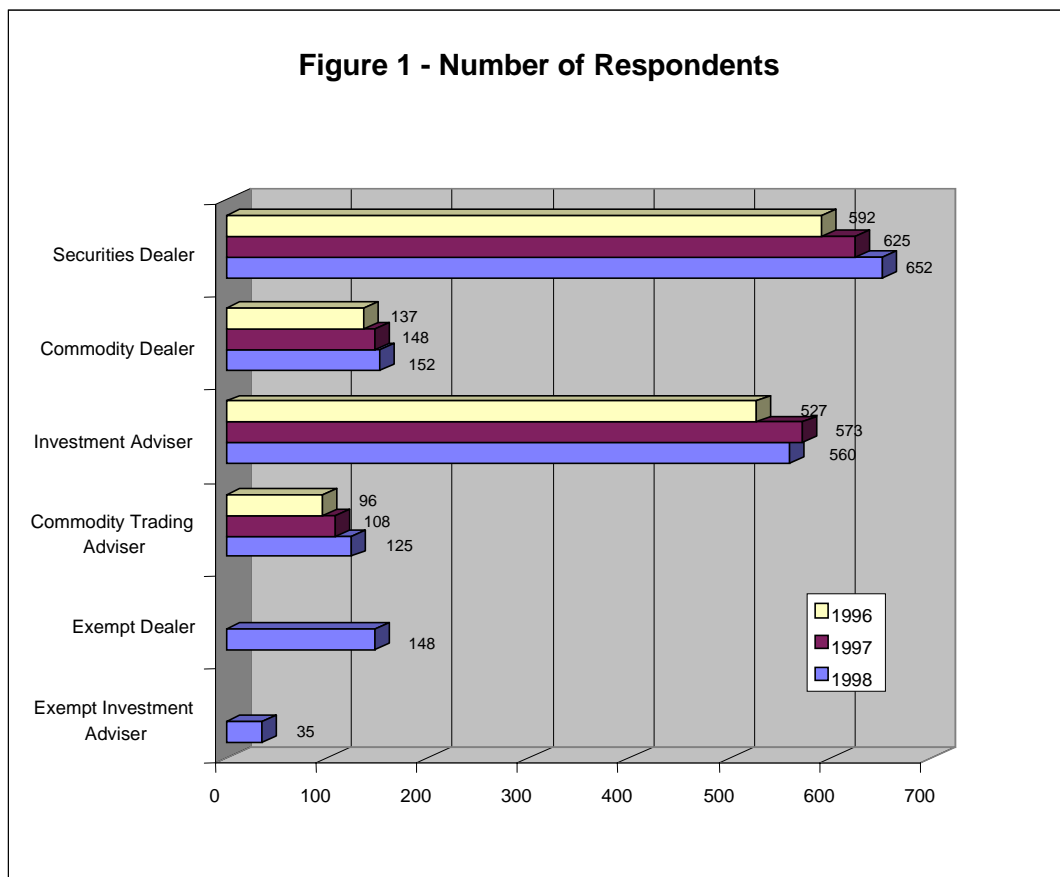
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## 1. Introduction

- (1) With a view to maintaining an up to date picture of the business profiles of securities and futures intermediaries in Hong Kong, the Securities and Futures Commission has again conducted its annual survey on the activities undertaken by registered firms in the first quarter of 1999. The scope of this year survey has been extended to cover exempt persons for the first time. The categories of registered or exempted business entities surveyed are outlined in Figure 1.
- (2) 1,463 questionnaires were issued, covering all registered and exempted firms, ranging from sole-proprietorships and partnerships to corporations. The response rate for 1998 was 93%, which showed an improvement over that of 1996 (86%) and 1997 (91%). The higher response rate makes this year survey results more representative.

The chart below (figure 1) shows the breakdown of the number of replies by type of registration / exemption status from 1996 to 1998.



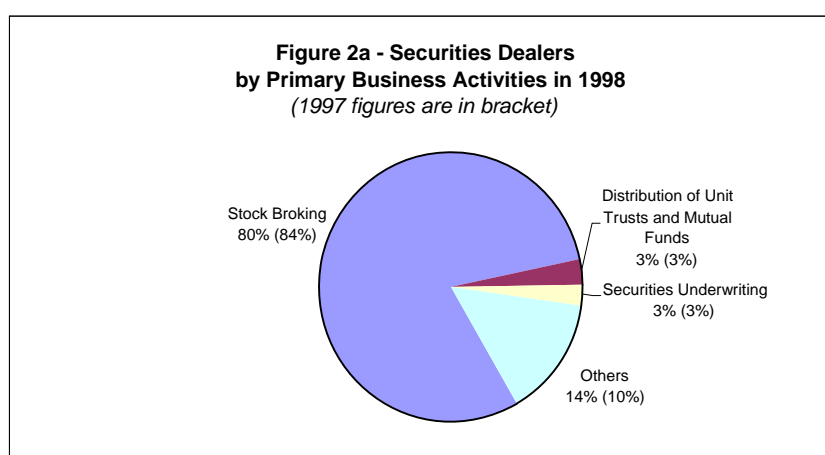
## 2 Main Findings of Surveys

### 2.1 Common Parameters

The main findings of the surveys about the above six types of business entities are presented in accordance with common parameters for easy comparison and reference. The parameters include primary business activity, market share, client profile, profile on margin financing of securities, custody of client assets by intermediaries, human resources profile, financial performance and business development.

### 2.2 Primary Business Activity

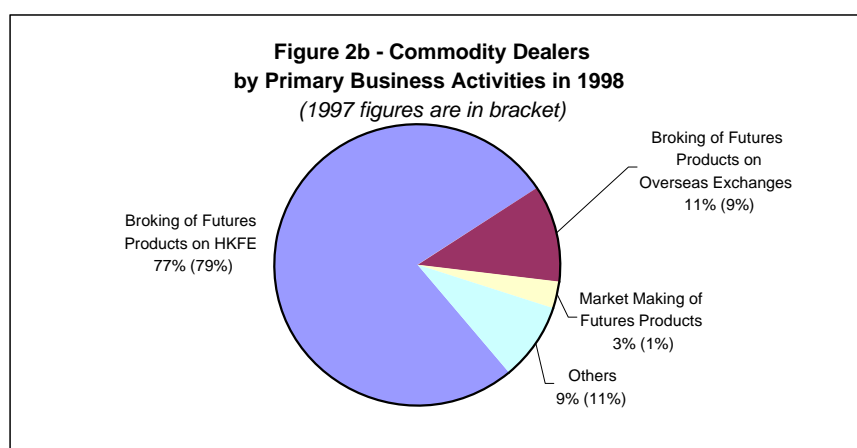
- (1) Broking activities constituted the main business function of securities dealers. 80% (1997: 84%) of securities dealers cited stock broking (figure 2a) as their primary business activity. 91% of these stockbrokers principally engage in broking activities on SEHK.



- (2) Similar to securities dealers, a majority of the commodity dealers considered broking activities as their main business function.

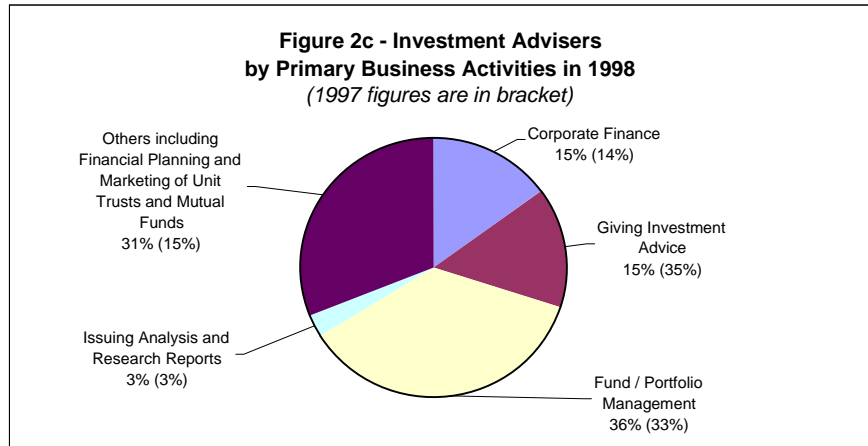
77% (1997: 79%) of the commodity dealers cited broking of futures/options contracts traded on the HKFE (figure 2b) as their primary business activity.

11% (1997: 9%) of the commodity dealers were established primarily to act as agents for trading overseas futures/options contracts.



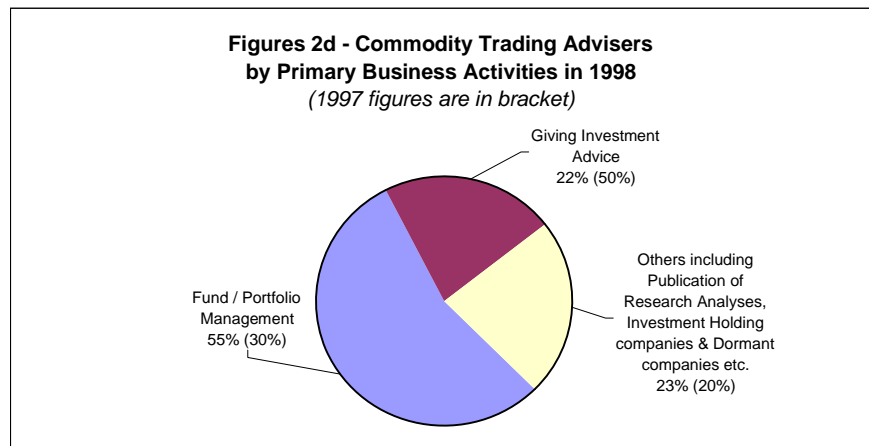
- (3) 36% of the investment advisers were either fund managers or advisers to funds whilst 15% were plain advisers to clients on securities (figure 2c). For 1997, firms giving advice to funds were grouped under the category of plain advisers.

Similar to 1997, 15% of the investment advisers were engaged primarily in corporate finance advisory activities. Only a relatively small number of firms (3%) considered the issue of research analyses and reports as their primary business.



- (4) The majority of the commodity trading advisers considered their commodity trading advisory activities to be incidental to their core businesses such as futures trading, fund management...etc.

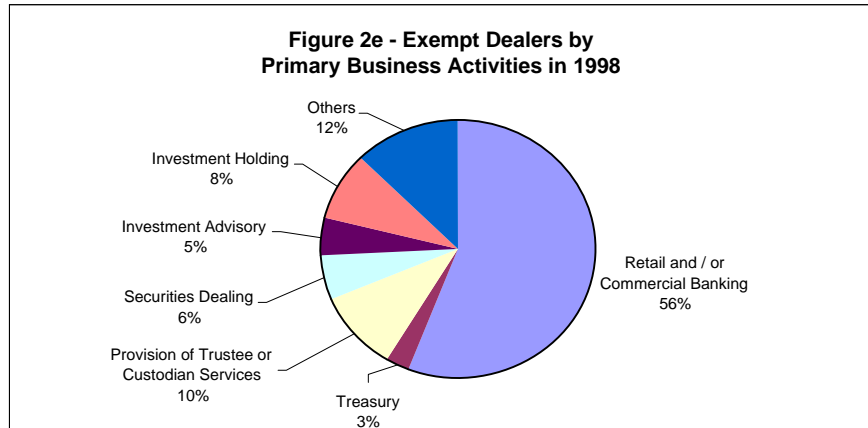
55% of the commodity trading advisers were either fund managers or advisers to funds whilst 22% were plain advisers to clients on commodities and futures contracts (figure 2d).



(5) 56% of the exempt dealers cited retail and /or commercial banking as their primary business activities. 10% of the respondents principally provide trustee or custodian services to clients (figure 2e).

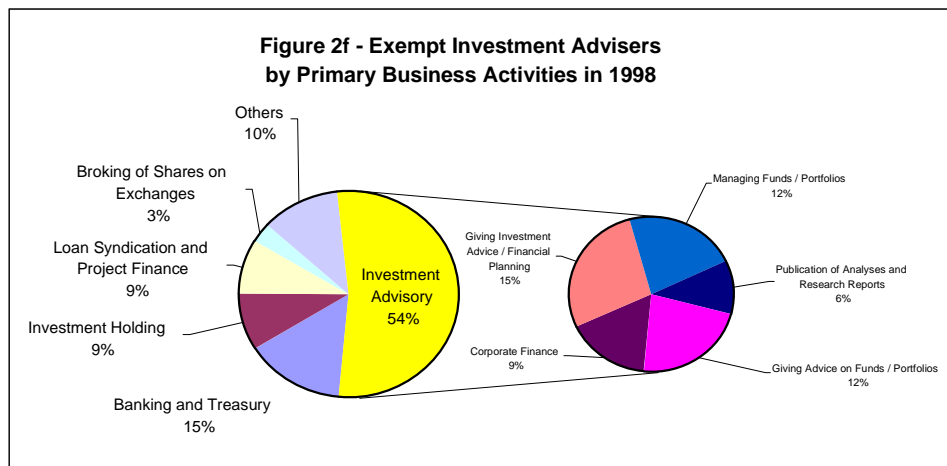
For firms selecting securities dealing as their primary business activities, they mainly participated in stock broking and securities underwriting businesses.

Firms selecting investment advisory as their primary business activities mainly participated in fund management business.



(6) 54% of the exempt investment advisers considered investment advisory activities as their primary activities. The types of advisory activities were distributed as shown in figure 2f.

For firms not selecting investment advisory activities as their primary business, all of them have both exempt dealer and exempt investment adviser status. As such, their principal business is not restricted to the provision of investment advisory service.



## 2.3 Market Share

- (1) The total gross operating income earned by each type of registered / exempted business entities is as follow:

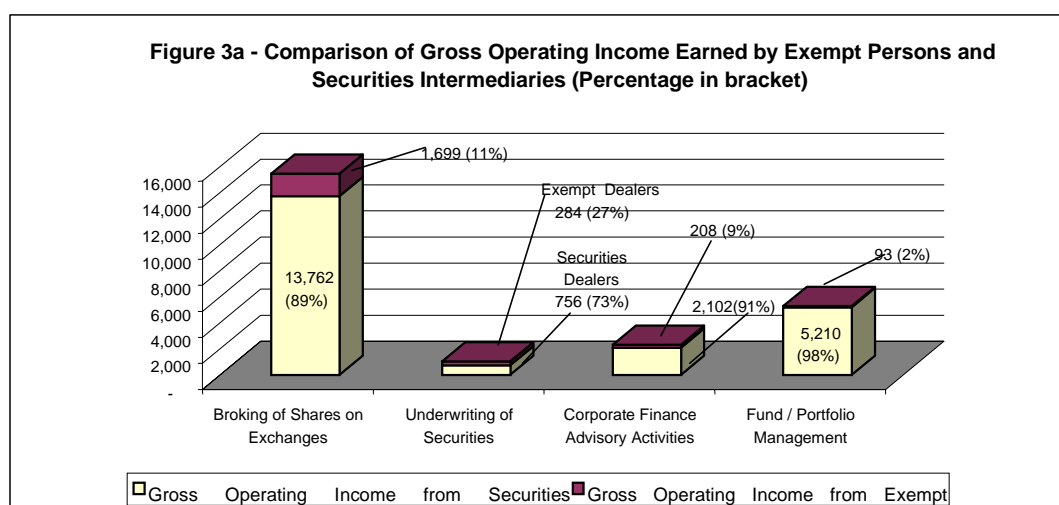
Type of Activities carried out by :	1998 HK\$'million	1997 HK\$'million	1996 HK\$'million
Securities Dealer	20,019	34,933	25,781
Commodity Dealer	2,185	2,208	1,218
Investment Adviser	9,468	9,825	4,956
Commodity Trading Adviser	63	*	*
Exempt Dealer	3,675	*	*
Exempt Investment Adviser	274	*	*
	<u>35,684</u>	<u>46,966</u>	<u>31,955</u>

\* - the corresponding figures were not available for 1996 and 1997

The securities and futures industry (excluding activities carried out by exempt persons) experienced an overall drop of 32% (HK\$15 billion) in gross operating income in 1998 as compared to 1997. It is mainly attributable to the decrease in commission received from broking of stocks on SEHK (HK\$10 billion) and overseas exchanges (HK\$2 billion). The fall in brokerage income is in line with the prevailing weak market sentiment following the financial crisis in late 1997.

The total gross operating income of exempt dealers and exempt investment advisers only referred to the income earned from their securities dealing and investment advisory activities carried out under the relevant exemption declarations. The income generated by these exempt persons accounted for only 13% of that earned by the securities intermediaries.

A comparison of the gross operating income earned by securities intermediaries and exempt persons, from broking of shares on exchanges, underwriting of securities, corporate finance advisory activities and fund/portfolio management activities, is shown in figure 3a below.



(2) Contribution to the 1998 total gross operating income by the top 10 and top 5% income earners in their respective categories are as follow:

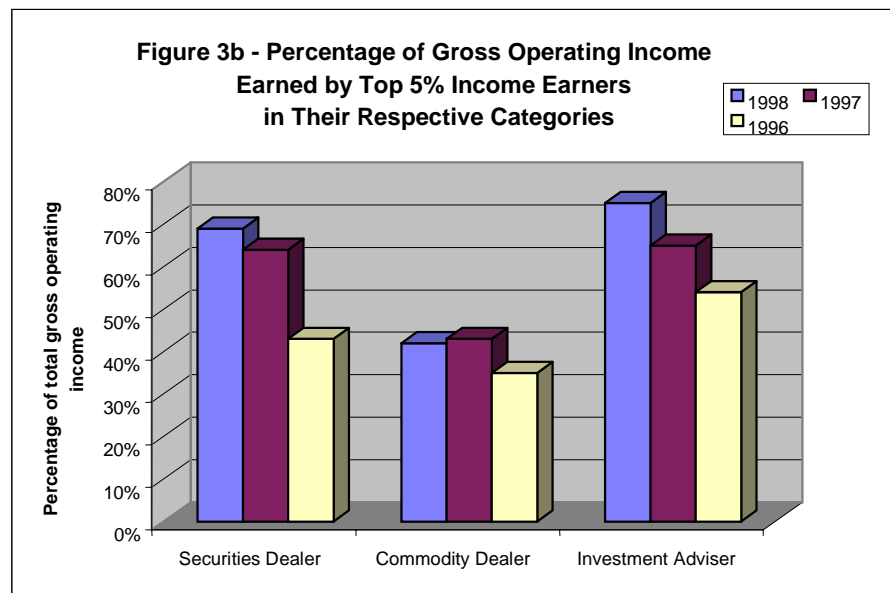
Type of Activities carried out by:	Top 10	Top 5%
	Income Earners	Income Earners
	% Contribution	% Contribution
Securities Dealer	42%	69%
Commodity Dealer	49%	42%*
Investment Adviser	60%	75%
Commodity Trading Adviser	99%	98%*
Exempt Dealer	126%#	115%*#
Exempt Investment Adviser	79%	32%*

# - The % contribution from the top 10 and top 5% exempt dealers exceeded 100% because some of the responding exempt dealers incurred significant losses from securities dealing / advisory activities in 1998.

\* - The % contribution from these top 5% earners was less than that of the top 10 earners because the number of firms making up these top 5% was less than 10.

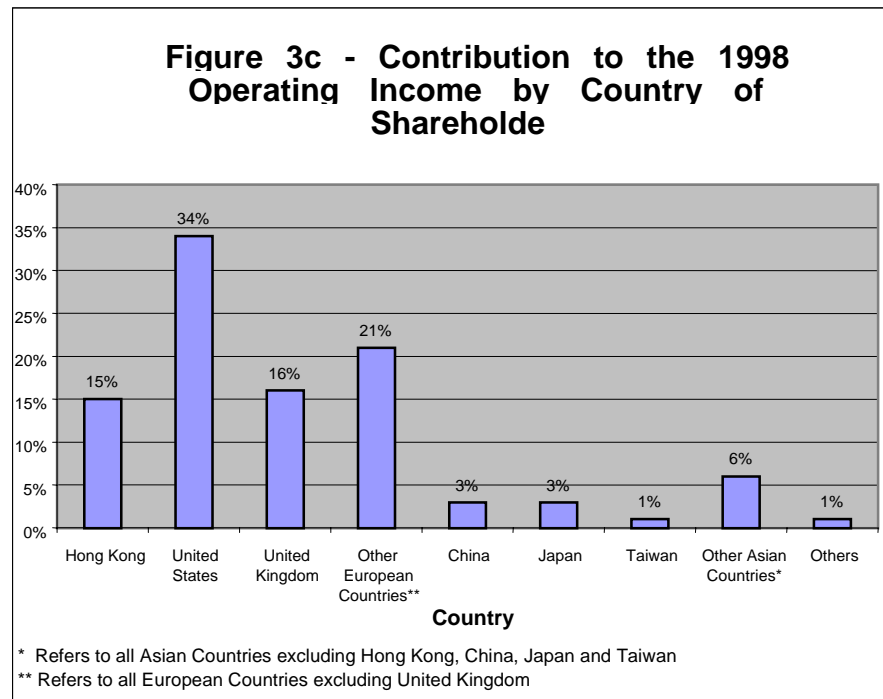
Registered firms constituting the top 10 and top 5% gross operating income earners accounted for at least over 30% of the revenue reported by all respondents in their respective categories in 1998.

A comparison on the percentage of gross operating income earned by the top 5% securities dealers, commodity dealers and investment advisers for the past three years is shown in figure 3b which shows the trend that gross operating income is concentrated in the hands of the large players.





- (3) The figure below (figure 3c) shows the 1998 total gross operating income generated by the responding intermediaries with reference to the country of domicile of their controlling shareholders.



Intermediaries controlled by United States and European countries appear to have dominated the securities and futures markets. They together attained a 71% share in the markets. These European intermediaries were mainly controlled by United Kingdom, Switzerland, France and Netherlands shareholders.

## 2.4 Client Profile

The number of active clients participating in the securities and futures industry as at 1998 year end is as follows:

Type of Activities :	1998	% to total
Securities Dealer	455,127	58
Commodity Dealer	15,471	2
Investment Adviser	12,000	2
Commodity Trading Adviser	476	-
Exempt Dealer	300,607	38
Exempt Investment Adviser	254	-
	<u>783,935</u>	<u>100</u>

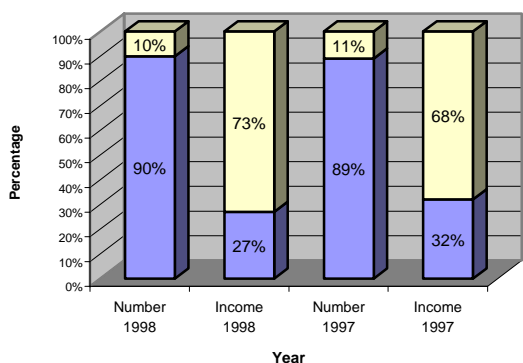
- (1) For dealers, the number of active clients refers mainly to those who participate in trading activities on various exchanges.
- (2) For advisers, the number of active clients listed above refers only to those who receive investment advice from the adviser firms. This figure excludes clients of the advisers engaging in corporate finance and fund advisory/fund management activities. Client profile of these advisers, which is assessed in terms of number of deals effected and number of funds under management respectively, is described at (4)(b)(ii) and (iii).
- (3) The number of active clients served by commodity trading advisers was significantly lower than that of the commodity dealers and investment advisers. It is because 87% of the commodity trading advisers were also registered as commodity dealers or investment advisers. Most of them were unable to separate their number of clients relating solely to the provision of commodity trading advisory service as this type of service is generally incidental to their commodity dealing or investment advisory functions.
- (4) Analysis of Clientele

Clientele for both securities and futures intermediaries are mainly analyzed by type (retails/institutional clients) and by location (local/PRC/overseas clients) in terms of number of active clients and gross operating income earned from the respective clients.

### (a) Dealing Activities

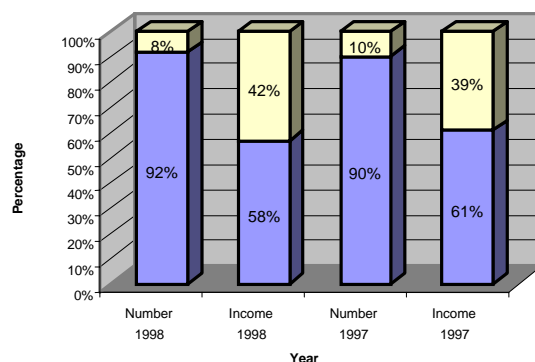
The analyses of the clients by type and by location for securities dealers and commodity dealers is depicted at figures 4a & 4b and figures 4c & 4d respectively.

**Figure 4a - Clientele of Securities Dealers  
(Retail/Institutional Clients 1997-98)**



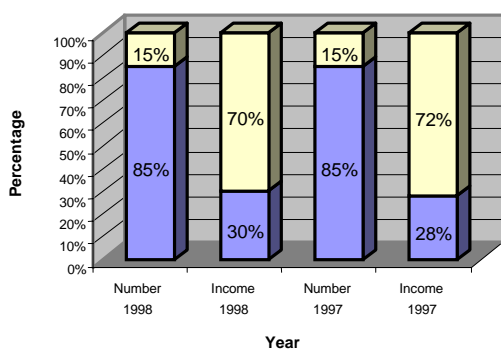
■ Retail Clients ■ Institutional & High Net-Worth Clients

**Figure 4b - Clientele of Securities Dealers  
(Local/PRC and Overseas Clients 1997-98)**



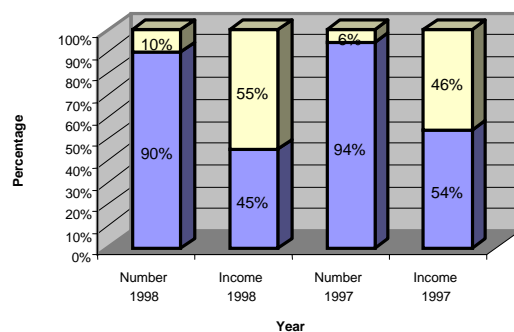
■ Local Clients ■ PRC and Overseas Clients

**Figure 4c - Clientele of Commodity Dealers  
(Retail/Institutional Clients 1997-98)**



■ Retail Clients ■ Institutional & High Net-Worth Clients

**Figure 4d - Clientele of Commodity Dealers  
(Local/PRC and Overseas Clients 1997-98)**



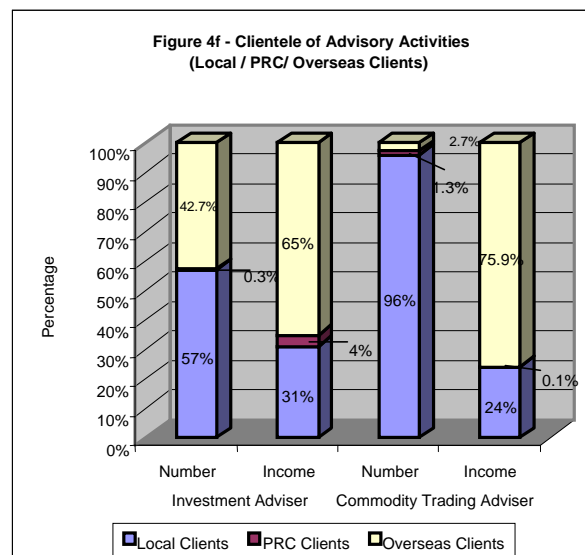
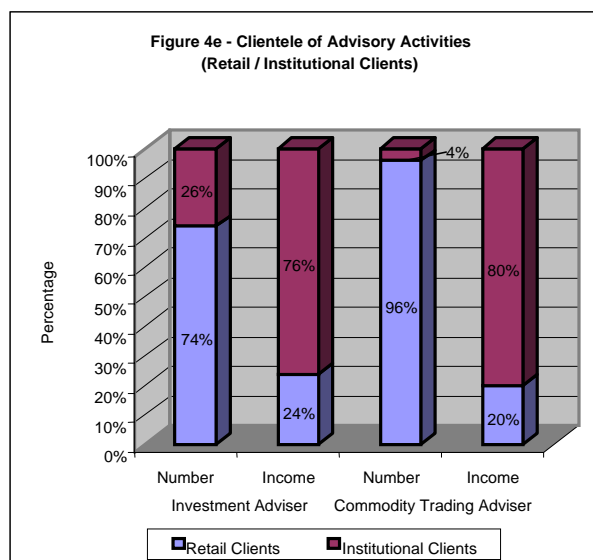
■ Local Clients ■ PRC and Overseas Clients

- (i) Institutional clients, despite the lesser in number as compared to retail clients, are the major contributors to the income of both securities dealers and commodity dealers.
- (ii) Similarly, although the number of overseas clients is much smaller than that of local clients, the importance of overseas investment can be illustrated by the fact that overseas clients contribute 42-55% of the income earned by both securities and commodity dealers.
- (iii) The clients of securities dealers have also been categorised into cash/margin clients and discretionary / non-discretionary clients. Both cash clients and non-discretionary clients dominate the others. Cash clients accounted for about 86% in terms of number of clients and 88% in term of gross operating income generated. Non-discretionary clients represented over 99% of the total number of clients and contributed about 99% of the gross operating income earned.

- (iv) For exempt dealers, retail clients, mainly private bank clients served by major banks in Hong Kong, represented 98% of the total number of clients of the exempt dealer firms while institutional and professional clients etc. accounted for only 2% of the total number of clients.

(b) Advisory Activities

- (i) The classification of clients who receive investment advice from the adviser firms, by type and by location is depicted at figure 4e and figure 4f below.



*(The corresponding information for year 1997 is not available as different classification was used for 1997 and 1998.)*

As in the case of dealers, institutional clients and overseas clients are the major contributors to the income of both investment advisers and commodity trading advisers.

- (ii) For firms engaging in corporate finance activities, their clientele is analyzed in terms of number of deals effected.

There were 953 deals effected for Local/PRC/Overseas clients. Out of the total number of deals effected, 69% were executed for local clients. The remaining 18% and 13% were transactions executed for overseas and PRC clients respectively.

However, overseas clients are the major contributors to the gross operating income generated from corporate finance activities. They contributed 68% of the income earned, followed by 22% from local clients and 10% from PRC clients.

- (iii) For firms engaging in fund advisory and fund management activities, their clientele is analyzed in terms of number of funds managed.

There were about 10,800 funds managed by the firms. Of the 10,800 funds, 13% are pooled funds while 87% are non-pooled funds. The majority of the pooled funds are retail public funds and institutional funds whilst the majority non-pooled funds are discretionary private client funds.

2.5 *Profile on Margin Financing of Securities*

- (1) As at 31 December 1998, the survey found 290 (1997: 296) securities dealer firms providing margin financing to clients either by themselves or through their related companies. The breakdown is shown as below:

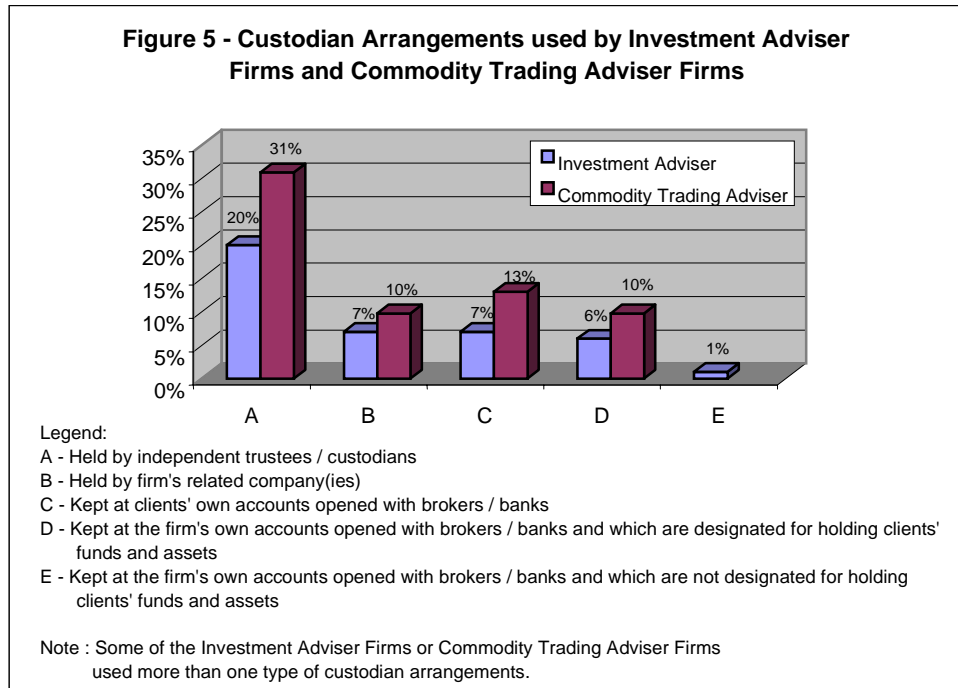
Margin financing provided :	-----Number of firms-----		
	1998	1997	1996
By the firm itself	174	164	161
Through the firm's related companies	88	112	72
By both the firm and its related companies	28	20	6
	<u>290</u>	<u>296</u>	<u>239</u>

Although the total number of firms providing margin financing in 1998 was comparable to that of 1997, there appears to be a trend that firms are shifting their margin financing business from their related companies (mainly the finance companies) back to the dealer firm itself.

- (2) As at 31 December 1998, credit facilities totalling HK\$57 billion was granted, out of which HK\$17 billion was utilized. This represented a utilization rate of 30% (1997: 37%).

2.6 *Custody of Client Assets by Intermediaries*

- (1) The majority of securities dealers (79%) and a significant number of advisers (securities investment advisers: 32% ; commodity trading advisers: 45%) held client assets in 1998.
- (2) The use of an independent trustee or custodian was the most common form of custodian arrangement. Figure 5 below shows the profile of custodian arrangements by advisers in 1998, which was close to that in 1997.



## 2.7 Human Resources Profile

- (1) The number of staff employed by responding firms in 1998 was around 22,779.
- (2) When compared with 1997, there is a very significant 25% drop in number of staff employed. Over 70% of the drop relates to the cut down of back office staff particularly in the securities intermediaries.

This trend is in line with the general economic downturn resulting in retrenchment and rationalization during the year. The effect is most significant in local, UK, Japan and US controlled entities.

- (3) The distribution of manpower among different types of registered firms was more or less the same as that in 1996 and 1997. A majority of the staff employed by securities and futures intermediaries were registered persons.
- (4) Securities Dealers and Commodity Dealers
  - (a) The securities and commodity dealers together employed about 17,559 staff representing 77% of the bulk workforce.
  - (b) In 1998, dealing and marketing staff accounted for 53% of the workforce of securities dealers and commodity dealers. Around half of these marketing staff are acting for the firms on agency contracts or by other arrangements.
  - (c) With regard to the working experience of these dealing and marketing staff, only a quarter of them have over 10 years industry experience. About 43% of the participants have less than five years relevant experience.
  - (d) The number of staff employs by the dealers can be analysed as follows:

	No of staff	% to total
Small sized firms with less than 50 staff	9,298	53
Medium sized firms with staff number range from 51 to 200	5,752	33
Large sized firms with over 200 staff	2,509	14
	<u>17,559</u>	<u>100</u>

(5) Investment Advisers and Commodity Trading Advisers

- (a) The advisory sector together employs about 5,220 staff representing 23% of the bulk workforce.
- (b) Fund management and corporate finance staff accounted for 31% of the workforce of investment advisers.

With regard to these fund management staff, 39% of them has over 10 years industry experience whilst 29% has less than five years relevant experience.

With regard to the corporate finance staff, only 17% of them has over 10 years industry experience. 43% of these employees has less than five years relevant experience.

- (c) The number of staff employs by the investment advisers can be analysed as follows:

	No of staff	% to total
Small sized firms with less than 30 staff	2,709	53
Medium sized firms with staff number range from 31 to 100 staff	1,343	26
Large sized firms with over 100 staff	1,056	21
	<u>5,108</u>	<u>100</u>

2.8 *Financial Performance*

The securities and futures intermediaries had provided the following financial information for year 1997 and 1998 with reference to their audited or management accounts:

	1998 HK\$' million	1997 HK\$' million
Total Profit / (Loss) after tax :		
Securities Dealer	(762)	8,346
Commodity Dealer	545	427
Investment Adviser	(233)	4,704
Commodity Trading Adviser	106	1,014
	<u>          </u>	<u>          </u>

- (1) As at 31 December 1998, there were 442 (38%) intermediaries incurring loss which represent a 118% increase over that of last year. A majority of the loss making firms are either securities dealers or investment advisers.
- (2) The financial performance of commodity dealers remains rather stable for both year 1997 and 1998. Only 33 (1997: 30) commodity dealers suffered losses in this year.

## 2.9 Business Development

### (1) Internet Trading

With the advance of technology, an increasing number of securities and futures intermediaries have been providing or plan to provide dealing or advisory services over the internet.

Up to 31 December 1998, the number of firms providing the following services over the internet is as follows:

	<u>No. of firms</u>
Order routing	4
Research Data and Market Information	16
General / Company Information	15

There are also 71 firms who reported in the survey that they are planning to provide service on the internet. These firms are mainly securities dealers and investment advisers.

By June 1999, the number of registered firms and applicants that have advised the Commission regarding their plans to use internet as a medium of order routing is as follows:

	<u>Registered Firm</u>	<u>Applicants</u>
Securities Dealer	18	2
Commodity Dealer	1	1

### (2) Relocation of Business

Some of the securities and futures intermediaries have relocated or planned to relocate part of their operation outside Hong Kong. The most popular destinations are Singapore, United States and Japan.

In 1998, 18 dealers and advisers relocated their operation outside Hong Kong. Of the 18 firms, 13 of them have relocated part of their trading/advisory functions while the remaining have relocated their back offices and sales and marketing functions.

The distribution of the firms relocating or planning to relocate part of their operations outside Hong Kong are shown as below:

	<u>No. of firms</u>	<u>% to responding firms</u>
Securities Dealer	12	2%
Commodity Dealer	5	3%
Investment Adviser	20	4%