Keynote Speech at the Beijing-Hong Kong Financial Services Co-operation Forum

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Ladies and gentlemen, good afternoon.

I am very honoured to be here today.

In a special report titled "Doing Business in Hong Kong" on 14 October, the Financial Times extolled Hong Kong's can-do spirit and robust framework conducive to business and investment. Hong Kong's favourable environment is built upon a unique blend of essential strengths such as:

- a reliable legal system;
- the transparent and sound regulation of the market;
- administrative bodies which operate with discipline, efficiency and adaptability;
- market participants that embrace international norms and practices;
- a flexible international platform;
- the free and unfettered flow of capital and talents; and
- a simple tax regime, etc.

This host of favourable factors are actually valuable assets to Hong Kong, and Hong Kong being a part of China, they are invaluable to the nation as a whole.

Today, I wish to elaborate on the strengths of the Hong Kong market in two specific areas, and how we may put them at the best service of the State:

1. Hong Kong as an international platform - provides a fertile ground to facilitate financing activities and to help foster the growth of Mainland financial institutions in size and strength; and

2. Hong Kong as an asset management hub – harbours a diverse range of investment products and relevant professional talents.

Hong Kong as an international platform

Facilitating financing activities

First, on financing, Hong Kong has to date raised massive capital for a large number of Mainland enterprises, enabling them to expand their business, open up overseas markets as well as raise the international profile of their products at the pivotal point of China's rapid economic growth. I am sure our audience here are very familiar with the subject concerning the listing of H-shares and red chips in Hong Kong and so I shall skip the details. Focussing instead on the theme of Beijing-Hong Kong financial services co-operation today, I wish to highlight the example of Beijing Enterprises Holdings Ltd, which went public in Hong Kong as a red chip back in 1997.

At that time, the Beijing Municipal Committee of the Communist Party of China and the people's Government of Beijing Municipality, established the "Beijing Enterprises Holdings Ltd" by way of asset restructuring to seek listing status in Hong Kong to raise $2.7 billion. This landmark initiative received enthusiastic response from Hong Kong's stock market, making headline news with a positive note in the international press. The fund-raising project at the time played a supportive role in the construction of the capital's infrastructure, including the provision of funding for an array of development projects with far-reaching impact under Beijing Enterprises such as the Beijing Capital Airport Expressway project. The listing of Beijing Enterprise has symbolic significance: not only did it enable Beijing to raise funds in Hong Kong for its infrastructure projects, more importantly, it also served to explore new models for the economic development of the capital and other Mainland cities, and for opening up a new avenue for the same.

Helping Mainland financial institutions to grow in size and strength

With the rapid growth of China as an emerging economic power, Mainland financial intermediaries will no doubt play an important role in the international financial arena. In this evolving process, Hong Kong may provide a fertile ground within a foreseeable future for Mainland intermediaries to grow in size and strength and compete with world class talents of the industry pursuant to international best practices. Meanwhile, we also look forward to seeing Mainland institutions emerging as major players in Hong Kong's financial industry.

Pursuant to the undertakings under the Closer Economic Partnership Arrangement (CEPA) between Hong Kong and the Mainland, Mainland securities and futures companies as well as asset managers can operate in Hong Kong. At present, financial intermediaries that have established operations in Hong Kong come from a number of major Mainland groups. Those from Beijing include for example China International Capital Corporation, China Asset Management Company and China Life Insurance Group etc. In sum, there are as many as over 110 financial intermediaries with Mainland background operating in Hong Kong.

The SFC will continue to support the overseas expansion of China's financial institutions using Hong Kong as a platform. We will ensure sound regulation through consistent application of regulatory standards to these entities.

Hong Kong as an asset management hub

To become an important asset management hub in Asia and in the world, it is necessary not only to attract capital from various sources but also to have a critical mass of investment products and talents. In terms of capital, Hong Kong is endowed with an indisputable capability of attracting abundant overseas capital. Our survey shows that, more than 60% of the funds under management in Hong Kong was sourced from overseas investors as at the end of 2008. Meanwhile, Hong Kong also acts as the gateway linking up Mainland capital and overseas investment opportunities. Through the introduction of the Qualified Domestic

Institutional Investors (QDII) scheme by the Mainland in 2006, Hong Kong can provide Mainland investors with an effective overseas investment channel for the orderly outflow of funds from the Mainland to cater to their huge investment demand.

We have been encouraging market participants to effectively integrate the Qualified Foreign Institutional Investors (QFII) and QDII concepts with a view to creating innovative fund products for Hong Kong and international investors. Mainland's intermediaries are evidently equipped with expertise in the A-share market. Should they wish to fully capitalise on such expertise, Hong Kong is truly an excellent platform providing them with great room for development. The SFC will spare no effort to render our full effort and co-operation assistance in this regard. In fact, we are very much looking forward to authorising the first cross-border investment product to be offered to the public which is and managed by Hong Kong licensed intermediaries with Mainland background.

I will now briefly discuss the efforts to enhance Mainland-Hong Kong co-operation in developing the Exchange Traded Funds (ETF) market to expand the growth potential of Mainland financial intermediaries operating in Hong Kong.

Development of ETFs in Hong Kong

I believe you have a good grasp of ETF's attractive features. Hong Kong is well placed in the following six areas when it comes to developing the ETF market:

- we have an established ETF market: we have come a long way over the past ten years since the Tracker Fund was authorised in late 1999;
- we have a robust regulatory regime: relevant rules and codes have been updated on a timely basis to keep abreast of the development of ETFs;
- we have an active market with a high turnover, reflecting investor recognition: Hong Kong is the second largest ETF market in Asia, ranking second to the Mainland in terms of turnover and also second to Japan in terms of aggregate market capitalisation. The turnover of ETFs for August 2009 accounted for 4.5% of the total turnover on the Stock Exchange of Hong Kong (SEHK);
- Our ETFs offer wide investment exposure : our ETFs provide geographical exposure to Hong Kong, the Mainland, Japan, Korea, Russia, India, Taiwan and emerging markets generally. These ETFs track equities, bonds, gold, currencies or a specific commodity index respectively;
- Our ETFs are diversified and witness continuous innovation. Hong Kong saw:
  - the first ETF tracking the China A-share market (the iShares FTSE/Xinhua A50 China Tracker) in 2004, the first ETF in the world to offer investors outside the Mainland access to the A-share market in China;
  - the first bond ETF in 2005;
  - the first local ETF tracking a foreign stock market (in this case the BSE SENSEX in India) in 2006;
  - the first commodity futures ETF in 2007;
  - the first gold bullion ETF in 2008 (last year); and
- We have a suitable cultural profile: as a melting pot where East meets West in terms of language and culture, Hong Kong is able to foster the development of products for

cross-listing in the Mainland as well as overseas markets. Our rich cultural profile also renders it easier to attract domestic and international investors.

Last year, the number of ETFs and the aggregate market capitalisation increased by 54% and 50% respectively. As of the end of September 2009, there were 37 SFC-authorised ETFs traded on the SEHK, with a total market capitalisation (excluding the gold ETF) of USD20.89 billion or 1.1% of total market capitalisation of all companies listed on the SEHK.

We are committed to enhancing the ETF platform in Hong Kong, which is one of our top priorities. We will continue to discuss with the relevant Mainland authorities and explore the possibility of cross-border trading of ETFs on exchanges in Shanghai, Shenzhen and the Hong Kong SAR. With the support of the Central Government, CEPA Supplementary Agreement VI signed in May this year included an initiative to actively explore the introduction of e ETFs tracking Hong Kong listed equities in the Mainland. In that regard, we will work closely with ETF managers in Hong Kong and our Mainland regulatory counterparts to actively explore the introduction of the listing of ETFs, of which portfolios are constituted by Hong Kong listed stocks, on Mainland exchanges.

In particular, we seek to encourage Mainland financial institutions in Hong Kong, especially those with subsidiaries in the Hong Kong SAR, to use Hong Kong's platform to actively develop ETF-related products. Through operating in Hong Kong and competing in an open environment, they may keep enhancing their services by picking up new tools such as the state-of-the-art investment strategies and skills etc. We look forward to opportunities for Hong Kong to effectively assist Mainland financial institutions in becoming the leading multinational groups in the world.

Major breakthrough for the Hong Kong ETF market – building externality with Taiwan

In May this year, we achieved a breakthrough for cross-listing of Taiwan and Hong Kong ETFs. We signed with the Taiwan Financial Supervisory Commission in May this year a Side Letter to our 1996 bilateral Memorandum of Understanding to provide the necessary regulatory framework for cross-listing of ETFs. In August this year, thanks to the joint efforts of all parties involved, three Hong Kong ETFs, namely Hang Seng Index ETF, Hang Seng H-Share Index ETF and W.I.S.E. CSI 300 China Tracker, were listed in Taiwan, whereas the first Taiwan ETF was listed on the SEHK on 19 August 2009.

The cross-listing of Hong Kong and Taiwan ETFs has landmark significance. On one hand, it serves to channel Hong Kong funds to the Taiwan market as well as to attract more Taiwan funds to invest in Hong Kong's investment products. This will further fortify Hong Kong's leading position as an asset management hub in Asia. On the other hand, Hong Kong ETFs cross-listed in Taiwan allow Taiwan investors easier access to the increasingly active securities markets in the Mainland and Hong Kong. This signifies further progress in truly linking up the securities markets in Mainland and Taiwan with Hong Kong serving as the bridge, as well as a first step toward the gradual integration of the financial markets across the straits.

Hong Kong ETFs recorded stellar performance upon their listing in Taiwan. The three Hong Kong ETFs together accounted for 38% and 25% of the volume and value of turnover of the Taiwan ETFs respectively for the period from launch until the end of September 2009, with the W.I.S.E. CSI 300 China Tracker contributing the lion's share. This fund ranked second in terms of daily average turnover in the Taiwan ETF market in September 2009, demonstrating

Taiwan investors' huge interest in Mainland securities market and their confidence in its growth potential.

Linking up the markets and opening up new horizons for cross-listing

Investors from all corners of the world have extremely strong appetite for A-shares related ETF. The existing three ETFs tracking the A-share market in Hong Kong together constituted 82% of the total turnover of the Hong Kong ETF market in September 2009. The A50's daily turnover in September accounted for 75% of the average daily turnover for all ETFs in Hong Kong. ETFs listed in Hong Kong tracking A-shares are not only popular among Hong Kong investors but also a premier choice much sought after by international investors (including institutional investors) interested in the A-share market. On the regulatory front, we attach great importance to the risk management of the existing three ETFs on A-shares. Despite the financial turmoil in the past 12 months, the trading of ETF has remained stable.

Conclusion

It has been our mission to uphold the principle of supporting and serving the nation while maintaining our open and global markets. To this end, we seek to build a critical mass of capital and talents from all over the world and establish close co-operation with Mainland and overseas markets and regulators.

Looking forward, we will continue to devote our efforts to assisting the macro development of the nation, and use our best endeavours to leverage on our strengths and help Mainland enterprises pursue their goals of "going out". In the meantime, we are committed to providing a sound regulatory framework that provides a conducive environment for issuers and a broad spectrum of products, and gives each player room to grow. The SFC will also keep forging ahead to strengthen Hong Kong's position as a fund-raising centre for Mainland enterprises.

Thank you very much. I wish the Forum today every success.