



**SECURITIES AND FUTURES COMMISSION**  
證券及期貨事務監察委員會

## **Survey on Sale of Non-exchange Traded Investment Products**

For the year ended 31 March 2012



## Introduction

1. The Securities and Futures Commission (SFC) conducted a fact finding survey on the sale of non-exchange traded investment products (investment products) to individual investors by SFC-licensed corporations from 1 April 2011 to 31 March 2012 (the reporting period).

## Objectives

2. The survey was designed to collect, among others, information relating to the types and value of investment products sold by the SFC's licensed corporations. The information assists the SFC in supervising the selling practices of licensed firms. The findings also provide useful information to market participants.

## Scope

3. The survey focuses on the selling and distribution of investment products to individual investors (including investment vehicles owned by individuals), who had opened accounts with licensed corporations or their overseas affiliates and to whom investment products had been sold or distributed by licensed representatives in Hong Kong. Sales to market professionals<sup>1</sup> such as banks were not within the scope of this survey.
4. The investment products covered in this survey include unit trusts, mutual funds and other collective investment schemes (CIS), government and corporate bonds, structured investment products, hedge funds, swaps, swap options and repos. Products which were excluded in this survey included leveraged foreign exchange products, insurance products, mandatory provident funds, pooled retirement funds, exchange-traded funds and listed securities.

## Questionnaires sent and responses

5. The survey was sent to 1,423 corporations licensed to deal in and/or advise on securities and/or futures. We received 1,380 replies, representing a response rate of 97%. A total of 187 licensed corporations reported that they had sold investment products to individual investors during the reporting period.

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<sup>1</sup> Market professionals in this report refer to professional investors as defined under paragraphs (a) to (i) of the definition of "professional investor" in Part 1 of Schedule 1 to the Securities and Future Ordinance.



## Key findings

### **An active market comprising a wide variety of players and products**

6. A total of 187 licensed corporations, including investment advisors, asset management firms, brokers and international financial conglomerates, sold investment products to 54,675 clients. The aggregate transaction amount<sup>2</sup> of investment products sold for the year ended 31 March 2012 amounted to \$584 billion, which included mutual funds, corporate and sovereign bonds and structured investment products. As at 31 March 2012, the total market value of outstanding positions was \$429 billion.

### **The market is dominated by a small number of firms**

7. The top 10 firms accounted for 82% of the aggregate transaction amount of investment products sold in Hong Kong. They or their related companies were also major issuers of structured investment products or unit trusts, mutual funds and other CIS.
8. Five out of the top 10 firms were part of major international financial conglomerates and accounted for 65% of the aggregate transaction amount.

### **Structured investment products were mostly sold by international firms while other firms sold unit trusts, mutual funds and other CIS and fixed income products**

9. More than half of the investment products sold were structured investment products, and about 65% of these were currency-linked. Approximately 90% of structured investment products were sold by the five major international financial conglomerates as noted above.
10. The survey results show that firms focused on specific types of investment products matching their own scale and expertise. For example, investment advisors/asset management firms were responsible for the majority of sales of unit trusts and mutual funds to investors. A very small proportion of local stockbrokers, in addition to dealing in listed securities, also participated in the selling of investment products (mainly bonds) accounting for about 1% of the aggregate transaction amount.

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<sup>2</sup> Transaction amount in this survey refers to the amount paid or payable by investors for investment products. For leveraged products, the transaction amount represents the maximum exposure of the contracts. In this survey, licensed corporations were requested to report only one-sided transactions. For example, in switching transactions, only the buy orders of individual investors were included. Transaction amounts of rollover, redemption, close-out positions were excluded from the transaction amount.



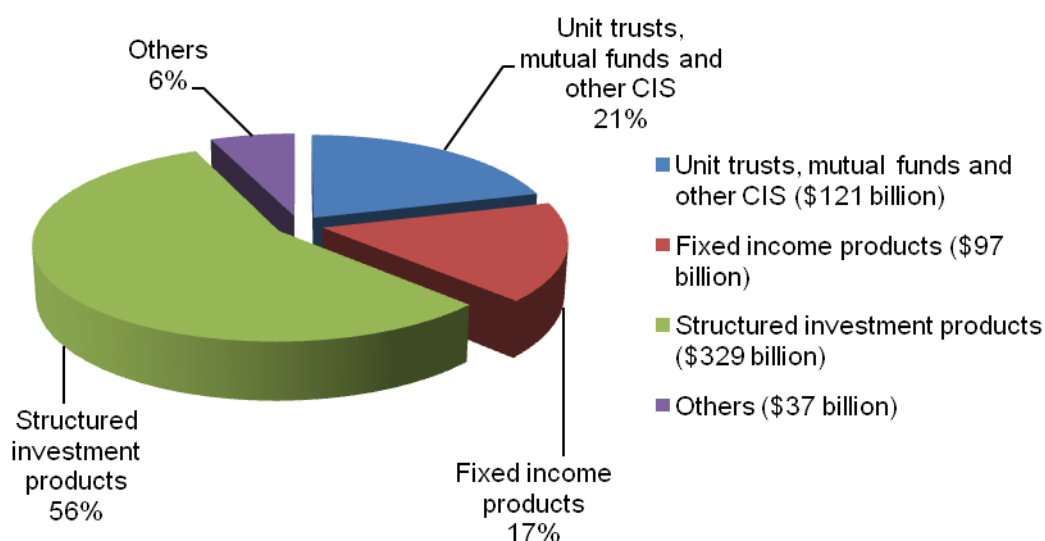
## Detailed findings

### Aggregate transaction amount: \$584 billion

#### Overview

11. For the year ended 31 March 2012, \$584 billion worth of investment products were reported to have been sold to individual investors by 187 licensed corporations, with structured investment products accounting for about 56% of the aggregate transaction amount. Unit trusts/mutual funds and fixed income products accounted for 21% and 17% respectively of the aggregate transaction amount. Chart 1 shows the distribution of various investment products. (See the next section for an analysis by product types).

**Chart 1: Total transaction amount by product type**



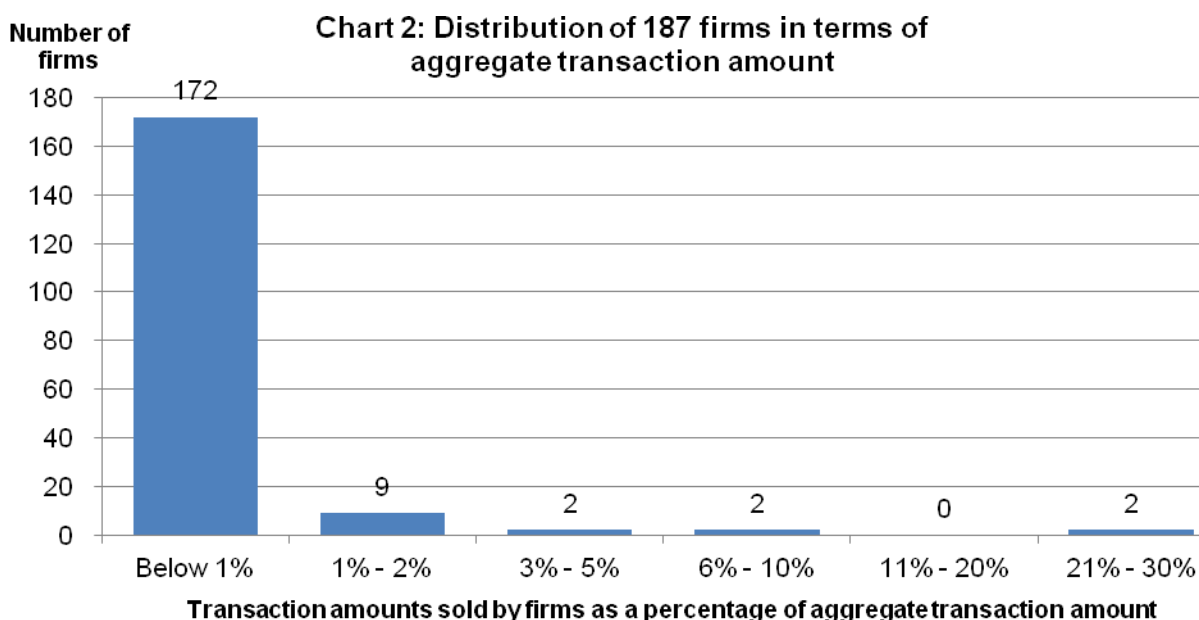
Product types	Transaction amount (Apr 2011 – Mar 2012) (in \$ million)			No. of firms engaged in sale	
	Authorized products	Unauthorized products	Total		
Unit trusts, mutual funds and other CIS	107,825	13,179	121,004	21%	138
Fixed income products	27	96,618	96,645	17%	74
Structured investment products	286	328,700	328,986	56%	47
Others <sup>3</sup>	222	37,111	37,333	6%	64
<b>Total</b>	<b>108,360</b>	<b>475,608</b>	<b>583,968</b>	<b>100%</b>	<b>187</b>

<sup>3</sup> Others included hedge funds, swap, swap options, repo, etc.

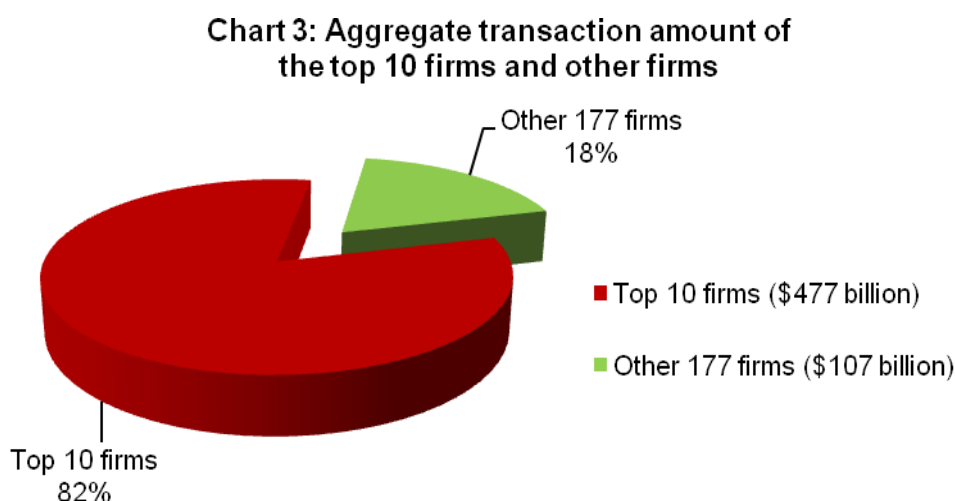


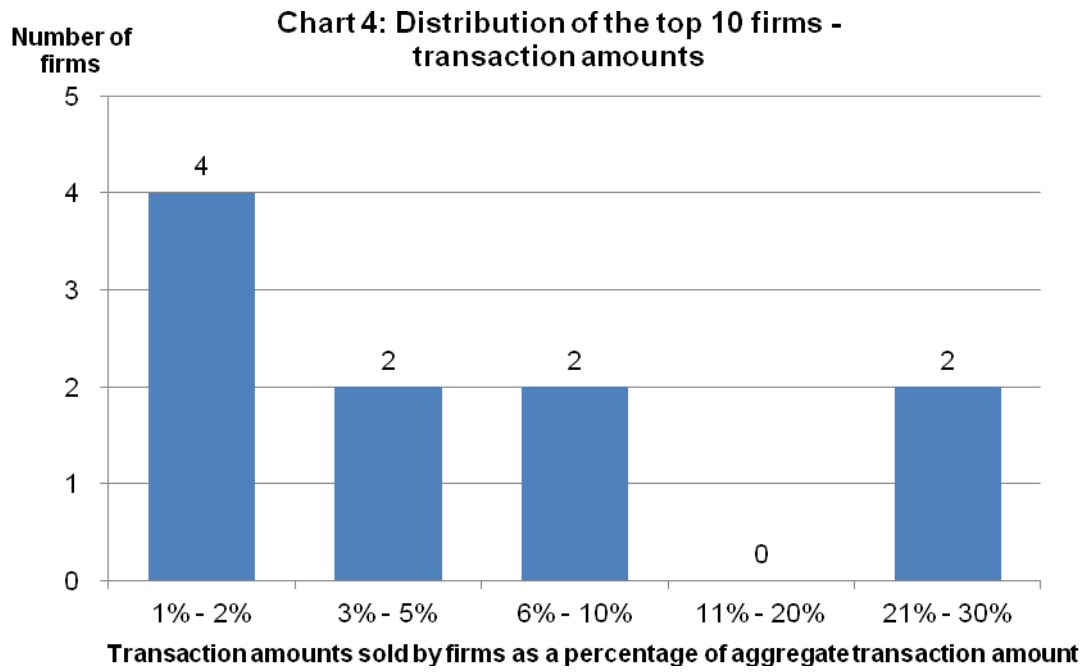
The top 10 firms selling investment products to individual investors contributed 82% of the aggregate transaction amount

12. As shown in Chart 2, the majority of the firms accounted for less than 1% of the aggregate transaction amount. A small number of firms dominated the market.



13. The top 10 firms were responsible for the sale of the bulk of investment products and accounted for 82% of the aggregate transaction amount. Five were part of major international financial conglomerates, three were Mainland or Taiwan securities brokers and two were asset management firms with controlling shareholders from the United States. The five international financial conglomerates generally did not deal with retail investors and accounted for about 65% of the aggregate transaction amount.
14. The remaining 177 firms sold about \$107 billion worth of investment products or 18% of the aggregate transaction amount. The majority were investment advisors, financial planners and asset management firms. The investment products sold by them were mainly unit trusts and mutual funds and fixed income products, which accounted for about 70% of the total transaction amount of these 177 firms.



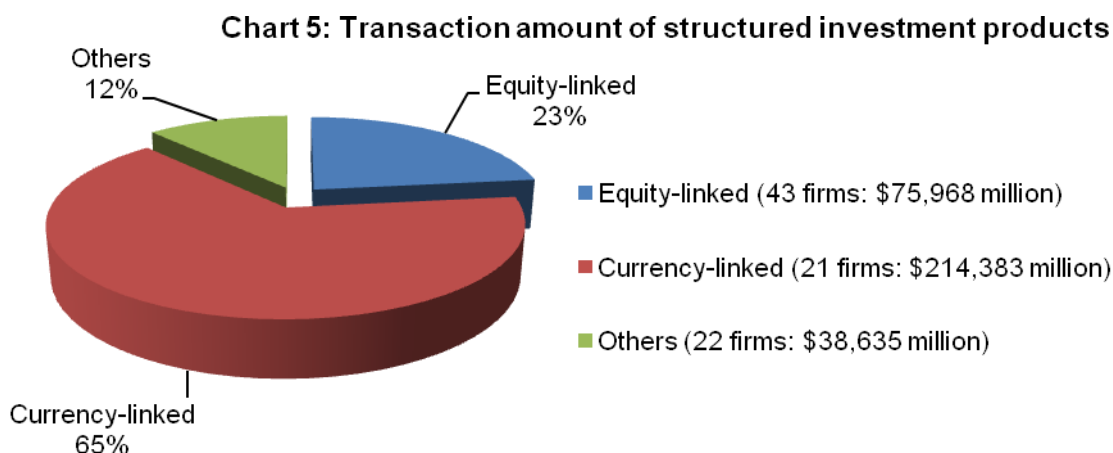




## Analysis by product types

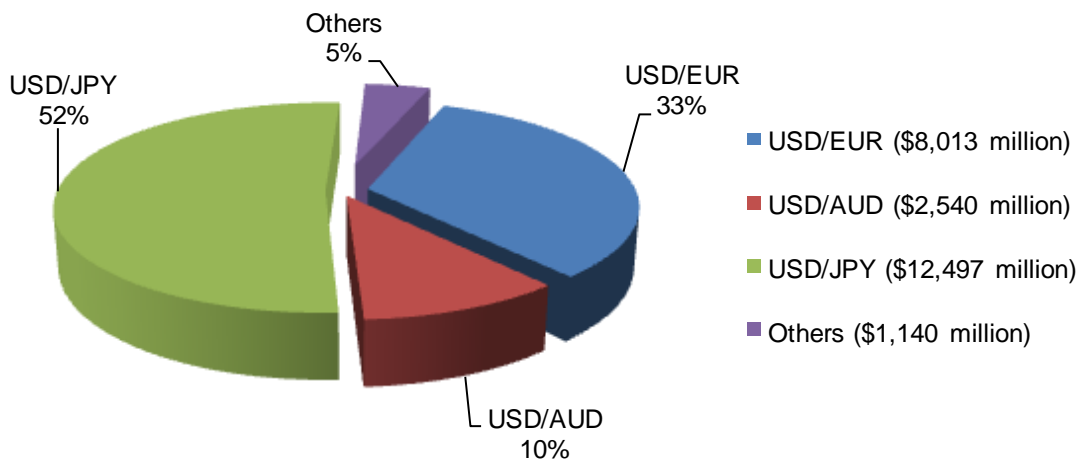
### Structured investment products (47 firms, total transaction amount: \$329 billion)

15. Currency-linked structured products were the most common type of structured investment products sold, with a total transaction amount of \$214 billion. Equity-linked structured products were the second most common, accounting for \$76 billion. Other structured investment products included commodity-linked, index-linked and interest rate-linked products.



16. As seen in Chart 5, about 65% of the structured investment products sold were currency-linked products. The high turnover of currency-linked structured products was probably due to relatively short duration and the tendency of investors to open new positions upon expiry.
17. In terms of currency and based on the top five currency-linked products reported<sup>4</sup>, the US dollar was consistently traded in currency pairs against the Japanese yen (52%), Euro (33%) and Australian dollar (10%).

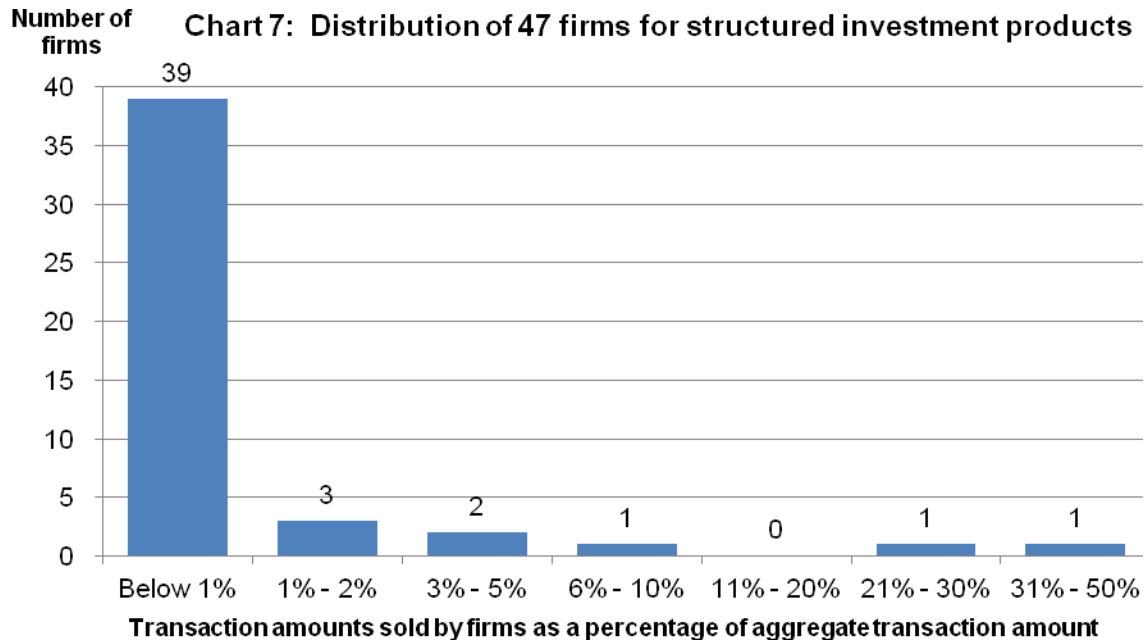
**Chart 6: Transaction amount of currency-linked structured products by pairs of currencies**



<sup>4</sup> In the design of the survey, firms were requested to provide further details, eg, names, issuers, etc, of the top five products which accounted for the highest transaction amount of each type of the products. The details enabled further analysis of the major products sold, eg, features.



18. The top 10 firms accounted for the majority (92%) of the total transaction amount for structured investment products sold. About 90% of these structured investment products were sold by five of the top 10 firms. These five firms were part of major international financial conglomerates.
19. Only six local stockbrokers reported to have sold structured investment products, amounting to a total of \$2.5 billion or less than 1% of the total transaction amount for structured investment products.

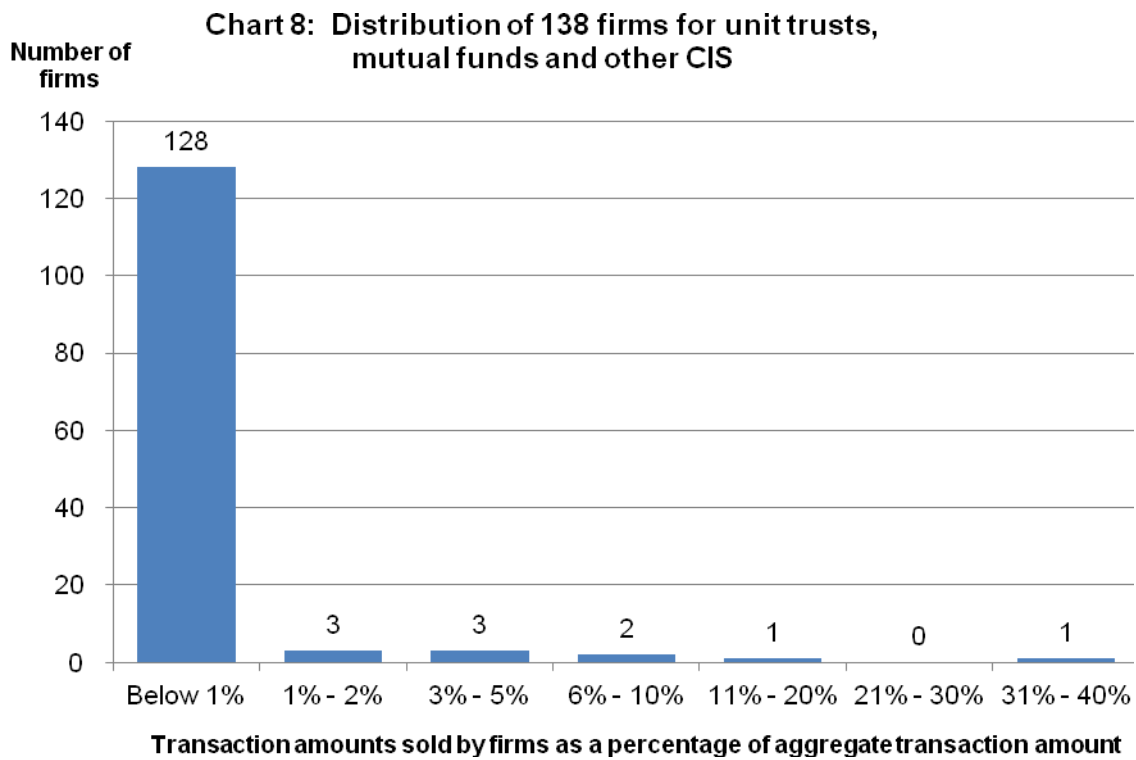






**Unit trusts, mutual funds and other CIS (138 firms, total transaction amount: \$121 billion)**

- 20. For unit trusts, mutual funds and other CIS, 89% (\$108 billion) of these products were SFC-authorized funds.
- 21. The two asset management firms among the top 10 firms sold a combined total of \$67 billion of unit trusts, mutual funds and other CIS to individual investors, accounting for 55% of the total transaction amount. These were funds managed by the firms themselves or their related companies. The top 10 firms accounted for 69% of the total transaction amount of unit trusts, mutual funds and other CIS sold.

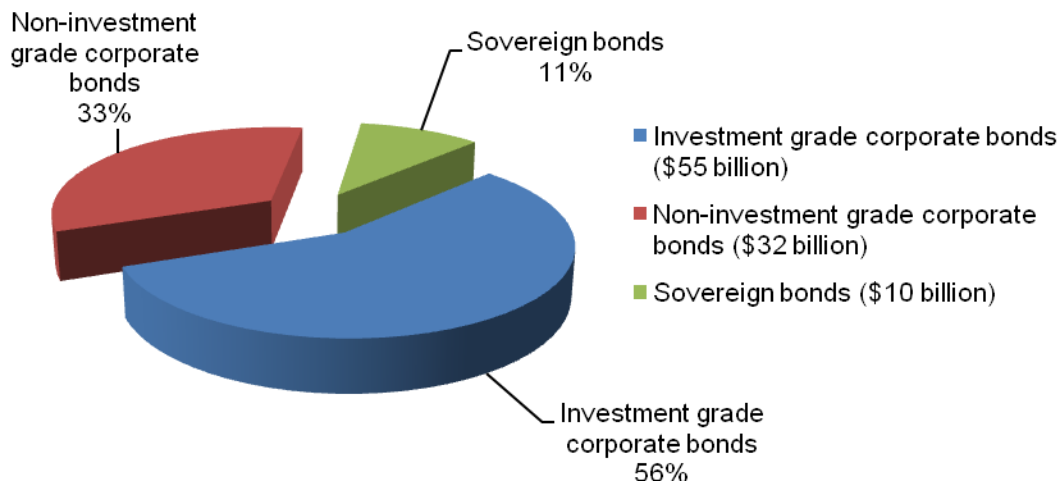




**Fixed income products (74 firms, total transaction amount: \$97 billion)**

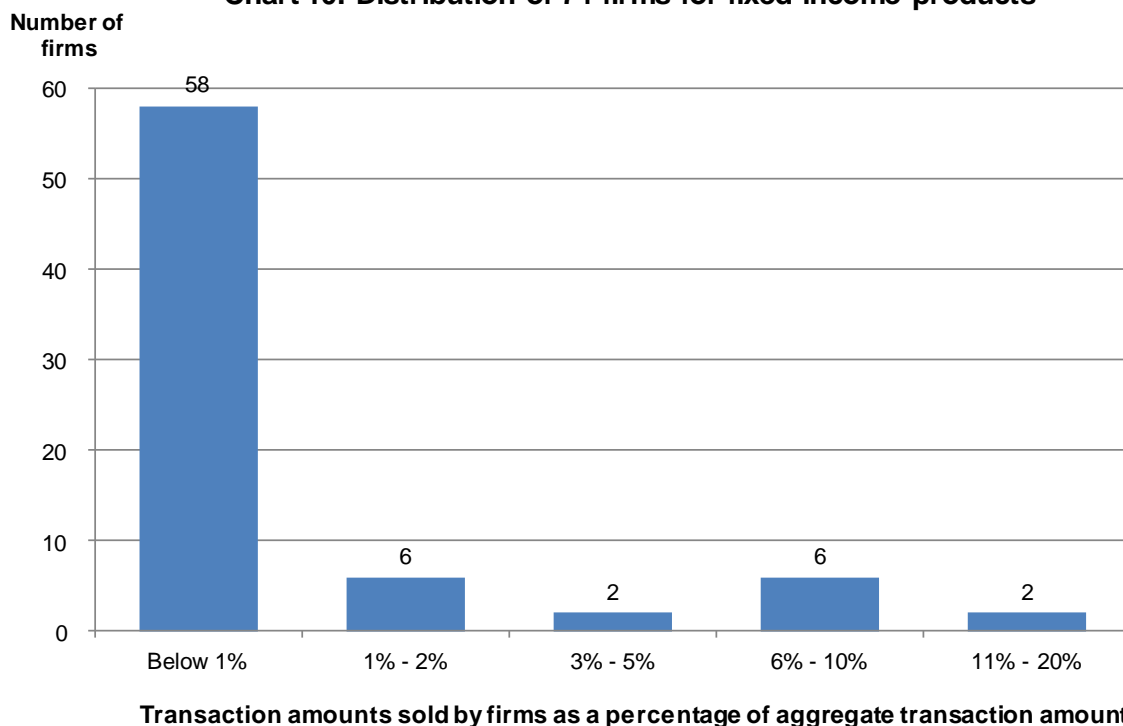
22. The transaction amount of fixed income products is composed of the following:

**Chart 9: Transaction amount for fixed income products**



23. Corporate bonds outsold sovereign bonds by seven times as measured by transaction amount. More than half of the corporate bonds were investment grade. Selling of fixed income products by the top 10 firms accounted for about 62% of the total value.

**Chart 10: Distribution of 74 firms for fixed income products**



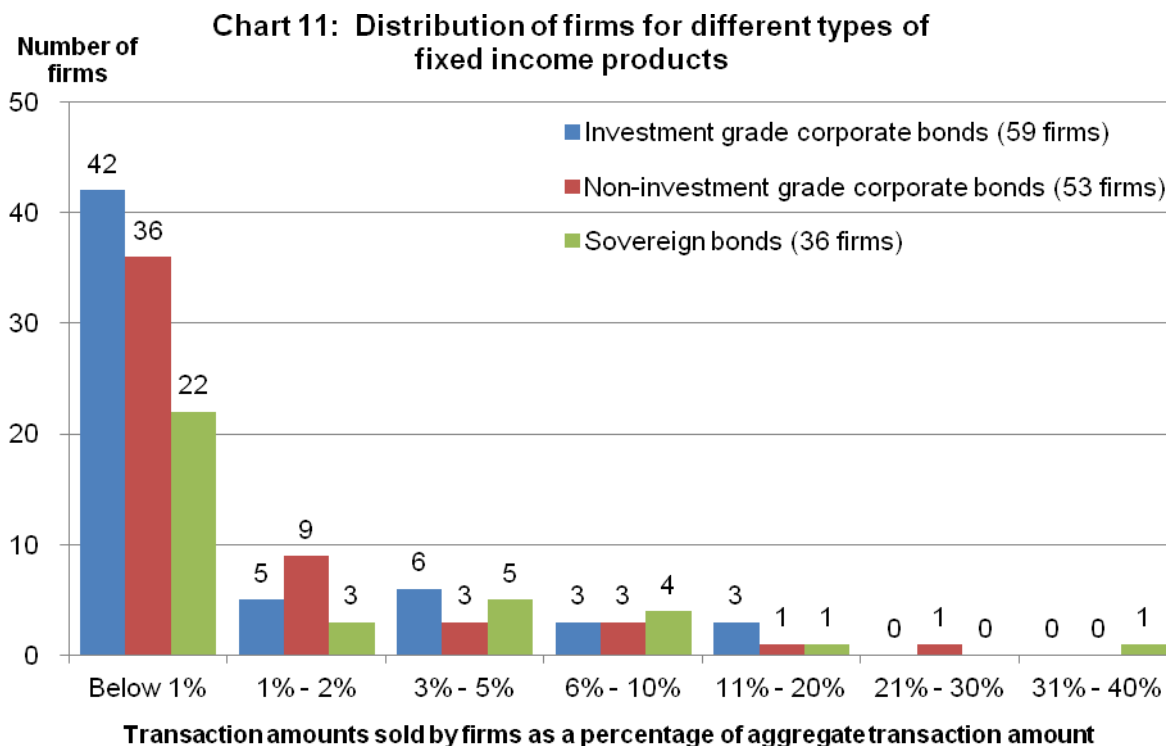


*Corporate bonds (72 firms, total transaction amount: \$87 billion)*

24. Based on the top five investment grade and non-investment grade corporate bonds<sup>4</sup> reported (\$14 billion and \$12 billion in total respectively), Hong Kong and the Mainland were the top issuers of both investment grade and non-investment grade corporate bonds, accounting for \$7.1 billion and \$5.6 billion respectively.
25. Based on the top five corporate bonds<sup>4</sup> reported, \$7.3 billion worth of investment grade corporate bonds and \$2.5 billion of non-investment grade corporate bonds (sold by 36 firms) were found to be subordinated and/or perpetual bonds. Almost all of these bonds had a minimum coupon rate of 4%, and 81% of these bonds had a coupon rate above 6%. About 75% of these subordinated and/or perpetual bonds were sold by the top 10 firms.

*Sovereign bonds (36 firms, total transaction amount: \$10 billion)*

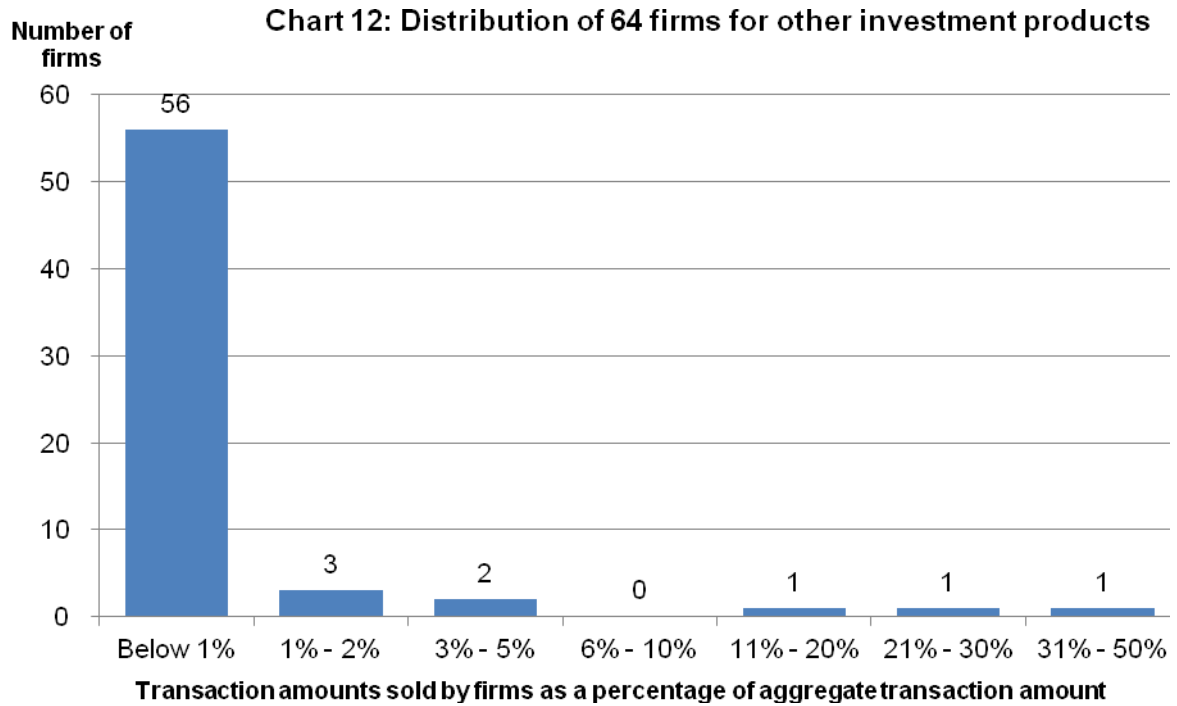
26. Based on the top five sovereign bonds<sup>4</sup> (total \$6 billion) reported, Hong Kong and US government bonds were the most common sovereign bonds purchased by individual investors (\$4 billion out of \$6 billion). Other sovereign debt exposures included Germany, Canada, Singapore and other Asia Pacific countries. Individual investors were reported to have a small exposure to Greek and Spanish sovereign bonds (\$159 million).





**Other products, including hedge funds, swaps, swap options, repos (64 firms, total transaction amount: \$37 billion)**

27. \$33 billion or 88% of other products were sold by the top 10 firms, and mainly consisted of hedge funds, swaps (interest rate swaps and equity swaps), swap options, repos and private equity funds.



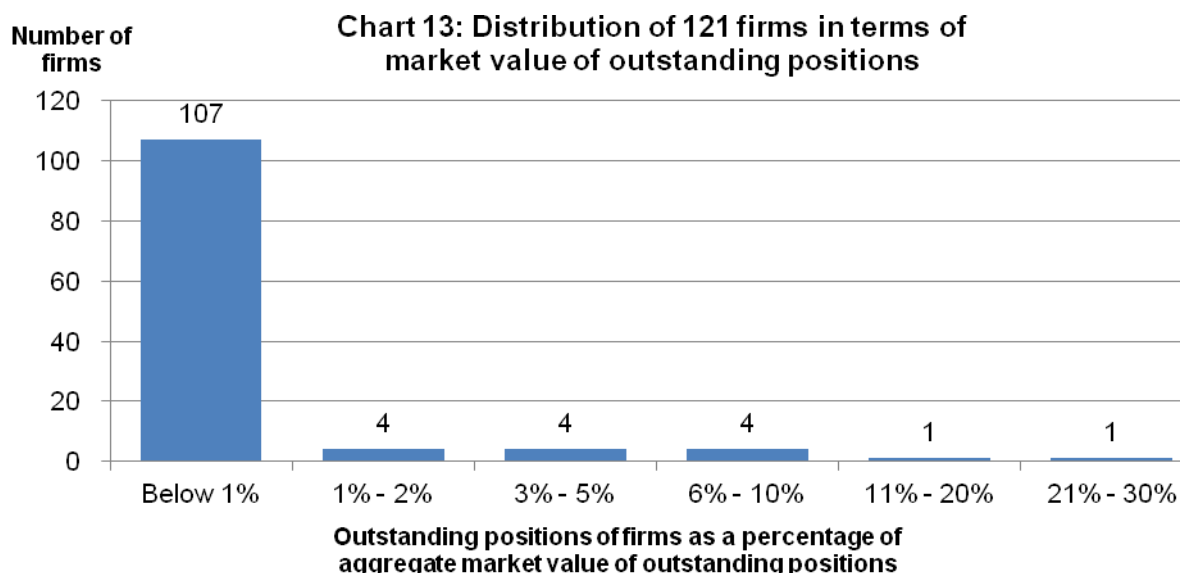


## Outstanding contracts

28. Among the 187 licensed corporations, 121 held outstanding positions on behalf of their clients or as a contracting party themselves or their related companies (including the top 10 firms). The market value of outstanding positions held by these licensed corporations amounted to \$429 billion.

Product type	Market value of outstanding positions (in \$ million)			
	Authorized products	Unauthorized products	Total	
Unit trusts, mutual funds and other CIS	107,104	29,597	136,701	32%
Fixed income products	27	154,962	154,989	36%
- Investment grade corporate bonds	27	100,692	100,719	23%
- Non-investment grade corporate bonds	0	45,955	45,955	11%
- Sovereign bonds	0	8,315	8,315	2%
Structured investment products	22	91,740	91,762	21%
- Equity-linked	22	24,727	24,749	6%
- Currency-linked	0	57,151	57,151	13%
- Others	0	9,862	9,862	2%
Others	569	45,274	45,843	11%
<b>Total</b>	<b>107,722</b>	<b>321,573</b>	<b>429,295</b>	<b>100%</b>

29. Unit trusts/mutual funds and fixed income products had the highest market value of outstanding positions. With regard to structured investment products, the value of outstanding positions was smaller than their transaction amount. As mentioned in paragraph 16, this was probably due to the relatively short duration of the majority of structured investment products sold.
30. The top 10 firms accounted for 60% of the aggregate market value of outstanding positions, consistent with the sale of investment products dominated by the top 10 firms.





## Active clientele

31. The 187 licensed corporations reported a total of 54,675 clients who had conducted transactions in investment products. The top 10 firms reported a total of 20,373 clients, representing about 37% of total clients.
32. Some 83% of the firms (155 out of 187 firms) reported that clients had opened accounts directly with them. Approximately 17% of the firms (32 out of 187 firms) reported that they also served 4,723 clients (about 8% of the total clients) who had opened accounts with their overseas affiliates.
33. About 6% or 3,477 clients had been treated as professional investors under the Code of Conduct.

	<b>Top 10 firms</b>	<b>Other firms</b>	<b>Total</b>
<b>No. of firms</b>	10	177	187
- No. of clients	20,373	34,302	54,675
- No. of clients treated as professional investor under the Code of Conduct	1,114	2,363	3,477
<b>No. of firms</b>	4	28	32
- No. of clients opened accounts with overseas affiliates	2,886	1,837	4,723
- % of overseas affiliates' clients	14%	5%	8%

## Product issuers

*Top product issuers concentrated in the top 10 firms or their related companies*

34. Besides being the major sellers of investment products, the top 10 firms or their related companies were also the major product issuers. These were mainly structured investment products or unit trusts, mutual funds and other CIS.
35. Based on the names of the top five product issuers<sup>5</sup> reported by each firm (total: \$447 billion), \$367 billion or 82% were issued by the top 10 firms or their related companies.

## Manpower

36. As at 31 March 2012, 6,736 licensed representatives were reported to be engaged in the sale of investment products. The top 10 firms reported 1,649 licensed representatives engaged in the sale of investment products, accounting for 24% of the total.

<sup>5</sup> The survey requested each firm to state the top five product issuers for the products it sold.