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Research Paper No.54: A review of the global and local securities markets in 2013

17 January 2014

Executive Summary

1. In the US, the Dow, S&P and Nasdaq rose 27%, 30% and 38% respectively during 2013. The US market rose on rising hopes for a continuation of stimulus measures by the Fed and improving economic outlook in the US. The Dow and S&P rose to their record highs whilst the Nasdaq also rose to a 13-year high. The market remained volatile given worries about tapering of stimulus and the debt ceiling problem. The US Fed announced a modest tapering plan, and reaffirmed its commitment about maintaining an accommodative monetary policy. However, investors remained cautious about the implications of the tapering on the economy and possible shift in fund flows. The US Senate passed a budget deal which would ease automatic spending cuts. However, as the debt limit was raised until early 2014, worries about the problem would likely re-surface later.
2. In Europe, the FTSE, DAX and CAC rose 14%, 26% and 18% respectively. Major European markets rose on better corporate earnings in the Eurozone and robust economic data in the US. The DAX rose to a record high. Market sentiment was boosted given the European Central Bank's (ECB) commitment to loose monetary policies. However, uncertainties about the economic outlook in the Eurozone continued to weigh on the market.
3. In Asia, the Nikkei 225 Index rose 57%. The performance of other major regional markets was mixed, ranging from a 7% loss in Thailand to a 22% increase in Vietnam. In Japan, a weaker yen and the new cabinet's commitment to stimulus plans provided support. However, investor sentiment remained fragile given uncertainties about economic recovery. In other Asian markets, market sentiment was boosted as central banks adopted accommodative monetary policies. However, concerns about possible capital outflows capped the gains.
4. On the Mainland, the Shanghai Composite Index fell 7%. The Mainland market dropped given worries about slower economic growth. Concerns about tightening liquidity conditions in the credit market and worries about resumption of initial public offerings (IPOs) also affected investor sentiment. There were also uncertainties about policies to curb rising property prices. Reform policies released after the Third Plenum in November beat market expectations and provided some support.
5. In Hong Kong, the Hang Seng Index (HSI) rose 3%, but the Hang Seng China Enterprises Index (HSCEI) dropped 5%. Despite the strong rallies of US and European markets, the Hong Kong market underperformed, given worries about the Mainland's economic growth and credit conditions. H-shares dropped, tracking the decline in the Mainland market. The local market once rose sharply after the announcement of Mainland reform measures in November. However, uncertainties remained over the precise pace of the exit of quantitative easing (QE) programme in the US and the Mainland's economic outlook.
6. In 2013, the Hong Kong market posted only a slight gain despite rallies in major overseas markets. Looking forward, the market may face risks and uncertainties including:

   (a) Reversal of accumulated gains – During 2013, major stock markets rose to their record highs. Investors are concerned that after accumulating substantial gains, the markets are vulnerable to downward corrections. Any disappointing news about economic performance or policy changes may trigger selloffs, and worries about a possible downturn may add volatility to the market.

   (b) Worries about the tapering of Fed stimulus and the US fiscal debt problem – Given the nomination of Janet Yellen as the next Fed Chairman, it is widely anticipated that a dovish monetary policy might continue in the medium term. However, investors remain cautious about the precise pace for the Fed's tapering. The debt ceiling problem was only temporarily resolved and further debates in coming months may affect market volatility.

(c) Movements of capital flows – The global market rally was supported by abundant liquidity given loose monetary policies in major markets. As the local market has recorded capital inflows after the start of the QE of the US, upon a tapering of the stimulus, capital inflows may recede or even reverse. Possible reversals of fund flows from the Asian markets may pose a contagion impact on the local stock market as well. As an open market, the Hong Kong stock market is prone to risks of volatile capital flows.

(d) Global macro risks – Despite signs of improving economic data, the outlook for global economic growth remains uncertain. In Europe, unemployment rates and debt ratios remain high, and there are worries about deflation risks. Sovereign ratings are still susceptible to downgrades. In Japan, economic recovery remains fragile despite continuous supportive policies. On the Mainland, investors are also concerned about the slowdown in economic growth.

The Hong Kong stock market performance has referenced both the performance of the US and the Mainland markets. Looking forward, as the Mainland economic outlook remains uncertain, and the US Fed will taper its stimulus measures, these developments may weigh on the Hong Kong market.

7. Trading in both the cash market and exchange-traded derivatives rose. The average daily trading in the cash market rose 16%, while that in futures and options increased 10% and 9% respectively from that in 2012.

Performance of stock markets during 2013

8. During 2013, major markets rose to their record or multi-year highs on improved global economic outlook, abundant market liquidity and easing worries over an early exit of stimulus measures by the US Fed. The Japanese market outperformed on optimism about government supportive measures and a weaker yen. However, the Mainland market fell given uncertainties about the economic outlook and worries over the liquidity conditions in the market. The Hong Kong market underperformed major overseas markets.

The US

9. After gaining 7-16% in 2012, the Dow, S&P and Nasdaq rose 27%, 30% and 38% respectively in 2013 on rising hopes for a continuation of stimulus measures by the Fed and improving economic outlook in the US. The Dow and S&P rose to their record highs whilst the Nasdaq also rose to its highest level in 13 years (**Box 1**).

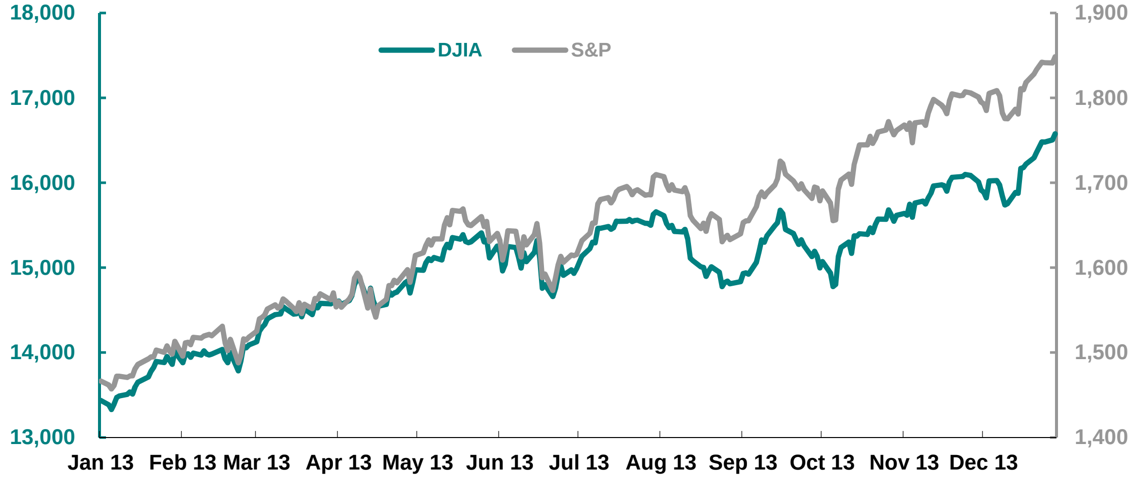
10. In early 2013, the market rose on solid earnings and encouraging economic data. Later, the market turned somewhat sluggish on worries over an early exit of stimulus measures and nuclear confrontation in the Korean peninsula. The market experienced some sell-off in mid-2013 after the Fed indicated that it would start scaling back its bond-buying programme. Later, some losses were recouped on solid economic data, which fuelled optimism that the economy might withstand the tapering of stimulus.

11. In August, the market corrected amid concerns about military actions led by the US against Syria. However, the impact on the market was short-lived.

12. During early October, the market was volatile as the Congress failed to reach a budget agreement and the US government was shut down partially (**Box 2**). The Congress eventually raised the debt limit until 7 February 2014 and re-opened the government. As the shut-down was brief and largely anticipated, the impact of the shutdown on the US economy appeared to be limited. The market seemed to be complacent given expectation that the Fed stimulus might be maintained for a prolonged period, offsetting the impact of the debt problem.

13. In late October, the Fed's surprise announcement to keep on buying US$85 billion of bonds per month eased some worries over an early exit of the tapering. The nomination of Janet Yellen as the next Fed Chairman further raised hopes for continuity of monetary stimulus by the Fed.

14. In December, the US Fed decided to trim the size of its monthly asset purchase from US$85 billion to US$75 billion, and reaffirmed that the interest rate might remain low even if the unemployment rate fell below 6.5%. The tapering was considered modest in scale, and signalled a better prospect of the US economy. An unexpectedly strong GDP growth at 4.1% for the third quarter (vs 2.5% in the second quarter) propelled the market higher. The US Senate also passed a budget deal which would ease automatic spending cuts, further boosting investor sentiment.



Performance of DJIA and S&P during 2013

Source: Bloomberg

Performance of Major stock markets

		End 2013	% change			PE Ratios
		Index Level	2013	2012	2011	End-2013
Hong Kong and the Mainland						
HK	-HSI	23,306.39	2.9%	22.9%	-20.0%	10.57
	-HSCEI	10,816.14	-5.4%	15.1%	-21.7%	8.02
Mainland	-Shanghai Comp	2,115.98	-6.7%	3.2%	-21.7%	10.63
	-Shenzhen Comp	1,057.67	20.0%	1.7%	-32.9%	28.80
Asia						
Japan	-Nikkei 225	16,291.31	56.7%	22.9%	-17.3%	23.54
Australia	-AOI	5,353.10	14.8%	13.5%	-15.2%	25.01
Taiwan	-TWSE	8,611.51	11.8%	8.9%	-21.2%	24.57
Korea	-KOSPI	2,011.34	0.7%	9.4%	-11.0%	17.04
Singapore	-STI	3,167.43	0.0%	19.7%	-17.0%	13.54
Thailand	-SET	1,298.71	-6.7%	35.8%	-0.7%	14.46
Malaysia	-KLCI	1,866.96	10.5%	10.3%	0.8%	18.03
Indonesia	-JCI	4,274.18	-1.0%	12.9%	3.2%	19.48
India	-Nifty	6,304.00	6.8%	27.7%	-24.6%	16.82
Philippines	-PCOMP	5,889.83	1.3%	33.0%	4.1%	17.17
Vietnam	-VN	504.63	22.0%	17.7%	-27.5%	12.59
US						
US	-Dow	16,576.66	26.5%	7.3%	5.5%	16.03
	-Nasdaq	4,176.59	38.3%	15.9%	-1.8%	25.74
	-S&P	1,848.36	29.6%	13.4%	-0.0%	17.44
Europe						
UK	-FTSE100	6,749.09	14.4%	5.8%	-5.6%	16.63
Germany	-DAX	9,552.16	25.5%	29.1%	-14.7%	16.22
France	-CAC	4,295.95	18.0%	15.2%	-17.0%	18.41
PIIGS and Hungary						
Portugal	-PSI20	6,558.85	16.0%	2.9%	-27.6%	N/A
Italy	-FTSEMIB	18,967.71	16.6%	7.8%	-25.2%	N/A
Ireland	-ISEQ	4,539.43	33.6%	17.1%	0.6%	N/A
Greece	-ASE	1,162.68	28.1%	33.4%	-51.9%	17.57
Spain	-IBEX	9,916.70	21.4%	-4.7%	-13.1%	N/A
Hungary	-BUX	18,564.08	2.2%	7.1%	-20.4%	19.55
Middle East and North Africa						
Egypt	-EGX30	6,782.84	24.2%	50.8%	-49.3%	N/A
Dubai	-DFMGI	3,369.81	107.7%	19.9%	-17.0%	19.90
Other BRIC markets						
Brazil	-IBOV	51,507.16	-15.5%	7.4%	-18.1%	N/A
Russia	-MICEX	1,503.39	2.0%	5.4%	-16.9%	6.12

Source: Bloomberg

Box 1: Sustainability of global market gains

Background

15. Accommodative monetary policies by major central banks have provided support to the global financial markets, which have accumulated substantial gains since the financial crisis in 2008. The US Dow and German DAX rose to historical highs and the Nikkei in Japan increased 57% in 2013, the largest yearly gain since 1972. These indices, together with the HSI, have gained over 100% from their troughs in 2009. Worries about possible corrections have heightened.

		End-2013 Index Level	% change from the trough in 2009
Hong Kong and Mainland			
Hong Kong	-HSI	23,306.39	105%
	-HSCEI	10,816.14	64%
Mainland	-Shanghai Comp	2,115.98	14%
Asia			
Japan	-Nikkei 225	16,291.31	131%
Taiwan	-TWSE	8,611.51	103%
Korea	-KOSPI	2,011.34	97%
Singapore	-STI	3,167.43	117%
US			
US	-Dow	16,576.66	153%
	-Nasdaq	4,176.59	229%
	-S&P	1,848.36	173%
Europe			
UK	-FTSE100	6,749.09	92%
Germany	-DAX	9,552.16	161%
France	-CAC	4,295.95	71%

Source: Bloomberg

16. The low interest rates may have generated side-effects of excessive leverage and possibly portfolio shifts to risky assets to seek high yields. Imbalances may have built up in the financial system, posing further risks to the market when the easing policies eventually unwind.

Tapering of stimulus in the US

17. The sustainability of the global market rally remains uncertain, as it has been partly supported by low interest rates and high liquidity. When such stimulus measures are phased out, market volatility will likely increase.

- In the US, in December 2013, the Feb decided to trim the size of its monthly asset purchase, and reaffirmed that it might keep the interest rate low even if the unemployment rate fell below 6.5%. Depending on the economic situations, the Fed might speed up the pace of stimulus withdrawal, which might affect market sentiment.
- In Europe, the ECB cut the benchmark interest rate twice in 2013 given concerns about deflation risks and high unemployment. While it signalled that negative interest rate is possible, the effectiveness of the rate cut in supporting the economy is in doubt. Policy uncertainties remain given divergent economic momentum of different Eurozone markets.
- In Japan, there was a strong commitment to the Abenomics framework, consisting of the three arrows of monetary stimulus, flexible fiscal policy and structural reforms. The government targets pushing up inflation rate to 2%. However, further political support is needed to pursue those measures.

18. Whilst the US Fed announced its initial plan to trim the size of stimulus, further reductions may continue. The precise timing, pace and magnitude of tapering of other major central banks remain uncertain. Some market participants believe that major central banks may raise interest rates during or after 2015.

19. Investors have been highly sensitive to signals about possible pullback of stimulus. In mid-2013, after the Fed signalled its plan for tapering the QE, Asian markets, including Hong Kong, experienced sharp corrections, given concerns about capital outflows. Subsequently, the markets resumed upward momentum after Fed's assurance of accommodative stance for an extended period. Later, the bullish market sentiment in the US was further underpinned by the Fed's decision of a modest tapering plan given anticipation of an improving economic outlook in the US. As the gains have further accelerated, the markets may be subject to growing risks of downward adjustments.

Assessment

20. Whilst the US Fed started to trim the size of stimulus, further withdrawal of stimulus outside market expectations could cause a disorderly market correction. Although the market expects stimulus to further taper when the economies gather sufficient strength, investor sentiment could be fragile in the face of differing views of economic conditions and a confluence of factors. While clear communication and credible policies help to guide markets, investor sentiment could diverge and cause a decline in market liquidity and lead to financial strains which could spread across the globe.

21. The withdrawal of stimulus in advanced economies may negatively impact emerging markets, which have been recipients of massive capital inflows and therefore vulnerable to sudden outflows. The rise in interest rates as a result of the reduced stimulus would trigger reallocation of investments among currencies, stocks and bonds, and add volatility to the global markets.

22. In case of higher volatility of overseas and regional markets, the Hong Kong market is likely to be affected by spillover effects, and capital inflows may recede or even reverse. Uncertainties about the Mainland market outlook may further weigh on the market and affect local market performance.

Box 2: The US debt ceiling impasse

Background

23. In early October 2013, the US Congress failed to reach an agreement on the debt ceiling problem. The US government was partially closed for two weeks. In mid-October, the US Congress passed a deal to temporarily re-open the government. The deal eased worries about a default of the US government debt but concerns about the problem might re-surface in coming months.

Comparison with the situation in 2011

24. In 2011, worries about the debt problem triggered a downgrading of the US credit rating by S&P's. The Dow fell 635 points on 8 August 2011, the day after the S&P downgrade, recording one of its worst single-day drops in history. Indeed, it dropped some 2,000 points within two weeks from late July 2011.

25. Compared to 2011, the debt ceiling debate had a relatively moderate impact in 2013. Investors seemed to shrug off the negative news, given hopes that the Fed might delay an exit of stimulus to offset the effect. However, there are concerns that market volatility may increase ahead of the next deadline in early 2014. We have assessed the latest market situation compared to 2011.

- ➢ Unlike the 2011 impasse, both S&P's and Moody's have been relatively optimistic about the current situation. This was in contrast to their warnings about a downgrade of the US credit rating several months before the debt ceiling deadline in August 2011. In June 2013, S&P's raised the outlook of the US credit rating to stable from negative. S&P's also commented that the AA+ rating of the US is unlikely to be changed due to the debt ceiling debate. In July 2013, Moody's raised the outlook of the US credit rating to stable from negative and affirmed its Aaa rating.
- ➢ Most economic data in 2013, such as job data, manufacturing data, housing data, consumer confidence, were stronger than in 2011.
- ➢ The stock market situation during the 2013 impasse was more bullish than that in 2011.
  - In 2013, the US benchmark indices hovered around record highs. During the year, market volatility was very much affected by uncertainties over the tapering of the Fed's stimulus. Yet, concerns over the tapering schedule eased after the nomination of Janet Yellen as the next Fed Chairman.
  - In 2011, the US benchmark indices were at about three-year highs, recovering from the troughs after the financial crisis in 2008. However, the markets were volatile during the year due to the downgrade of the US credit rating amid its huge budget deficit, possible contagion of the Eurozone debt crisis and political unrest in the Middle East and North Africa.

Longer-term risks and assessment

26. However, unlike the lift of the debt ceiling in August 2011 which was valid for about two years, the latest deal offers a short period of relief for months only. The short-term deal only relieves market strains temporarily. The delay does not guarantee a long-term resolution to the underlying structural problem of the US economy.

27. The country's high debt-to-GDP ratio of over 100% remains a major concern. The room for the government to exercise countercyclical policy to cope with downturns of the economy is reducing. Rising structural deficits and high public debt burden may result in growing political pressures. The difficulty in managing the political policy process may pose threats to market stability. Risks of future government shutdowns and debt limit

standoffs remain, unless longer-term solutions are derived to address ultimate cause of the debt problem.

28. While immediate risks for a US default are generally considered limited, concerns about credit risks and uncertainties about the Fed's monetary policy may continue to affect the economic outlook and bring volatility to the financial markets.

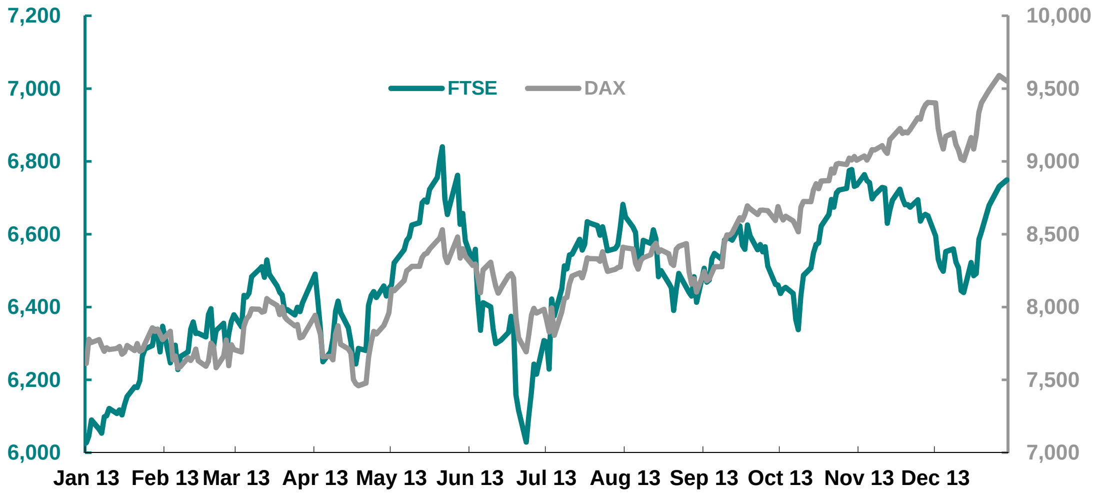
Europe

29. Major European markets advanced given optimism about monetary easing. During 2013, the FTSE, DAX and CAC rose 14%, 26% and 18% respectively, following the gains of 6%, 29% and 15% respectively in 2012. The DAX rose to a record high.

30. In early 2013, major European markets rose on robust economic data in the Eurozone and the US. Investor sentiment improved given news that banks would repay the ECB crisis loans early and the repayment amount was larger than expected.

31. In mid-2013, the markets retreated amid concerns about a sooner-than-expected tapering of stimulus by the US Fed. Yet, losses recouped later as the ECB and Bank of England pledged to extend their stimulus plans for a prolonged period of time. In early July, Italy's rating was downgraded by S&P's from BBB+ to BBB but the market impact seemed limited. In September, the victory of German's ruling party in the federal election boosted hopes for the continuity of loose monetary policies.

32. In early November, S&P's downgraded France's credit rating to AA from AA+, given concerns about unemployment. Later, market sentiment was boosted after the ECB unexpectedly cut the benchmark interest rate by 25 bps from 0.5% (after the 25bp cut in May) to a historical low of 0.25%. It also affirmed that interest rates would likely remain "at present or lower levels for an extended period of time". In late December, S&P lowered the rating on the European Union from AAA to AA+, citing rising tensions on budget negotiations, but the market impact seemed limited.



Performance of FTSE and DAX during 2013

Source: Bloomberg

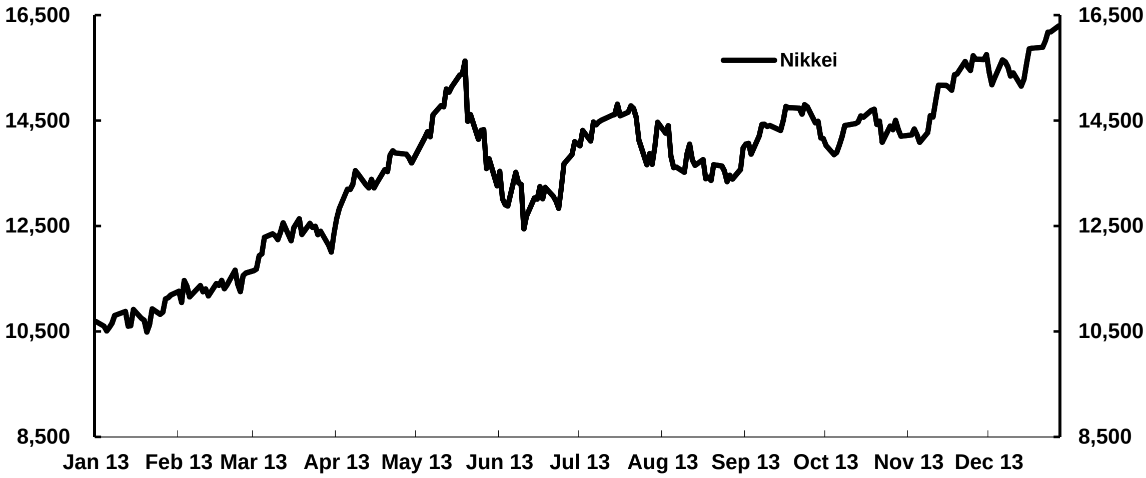
Asia

33. In Japan, the Nikkei 225 Index was the best performing benchmark index in Asia, posting a 57% gain during 2013, following a rise of 23% in 2012. The new cabinet indicated its commitment to supportive plans, which include fiscal and monetary stimulus, as well as structural reforms to boost the country's competitiveness. This boosted optimism about an economic recovery. In early April, the Bank of Japan announced its plan to inject US$1.4 trillion to buy government bonds and exchange-traded funds (ETFs). A weaker yen paced gains in the stock market. Investor sentiment was further lifted on Tokyo winning the bid to host the 2020 Olympics. Japan recorded four successive quarters of GDP growth, the best run in three years. The Nikkei rose to a six-year high.

34. Following gains of 9% to 36% in 2012, the performance of other major regional markets was mixed, ranging from a 7% loss in Thailand to a 22% increase in Vietnam during 2013.

35. Initially, investor sentiment was boosted as central banks in Asia adopted accommodative monetary policies—central banks in Australia, Thailand, Korea, Vietnam and India all cut interest rates, with those in Australia and Vietnam down to a record-low and three-year low respectively. Regional stock markets rose, with the SET (Thailand) and AOI (Australia) hitting their highest levels in 18 years and five years respectively.

36. Later, the markets turned volatile on concerns about capital outflows from the region. In Thailand, GDP shrank for two consecutive quarters for the first time since the global financial crisis. Given recession concerns and political uncertainties, the Thai Baht fell to a one-year low. Indonesia recorded a large current account deficit. India's rupee and Indonesian rupiah dropped to a record-low and four-year low respectively. Most major stock markets in Asia bottomed in August. Later, the markets recovered amid optimism about a continuation of stimulus measures in the US. However, some markets gave up gains in November given political uncertainties in Thailand.



Performance of Nikkei during 2013

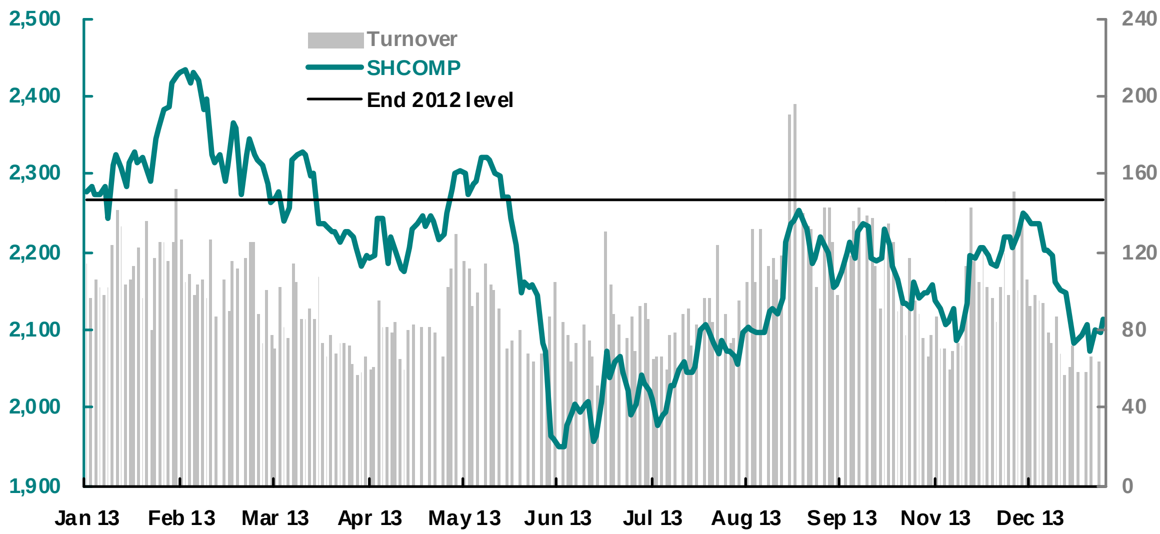
Source: Bloomberg

The Mainland

37. Following a rise of 3% in 2012, the Shanghai Composite Index fell 7% during 2013. It once rose to an eight-month high in February given solid economic growth data. Market sentiment was also boosted amid optimism about the possible increase in foreign investors' quotas to invest in the A-share market under the Qualified Foreign Institutional Investor (QFII) and Renminbi Qualified Foreign Institutional Investors (RQFII) schemes. Later, some gains were erased given worries about a possible hard landing amid weaker-than-expected economic data.

38. In mid-2013, the market corrected as rising interbank rates heightened worries over a credit crunch. The overnight Shanghai Interbank Offered Rate peaked at around 13% on 20 June compared to around 2-4% during January to May. Worries about possible measures to combat shadow banking activities added to concerns about tighter credit conditions. In July, the market posted the biggest monthly decline since August 2009.

39. Later, losses were trimmed as interbank interest rate stabilised. Better-than-expected GDP growth also lent support. The market posted a strong gain later as a detailed economic and social reform plan was released after the Third Plenary Session of the 18th Central Committee of the Communist Party of China. Yet, the upside was limited given investor concerns about IPO resumption and measures for curbing increases in property prices.



Shanghai Composite Index and Market Turnover during 2013 (Rmb billion)

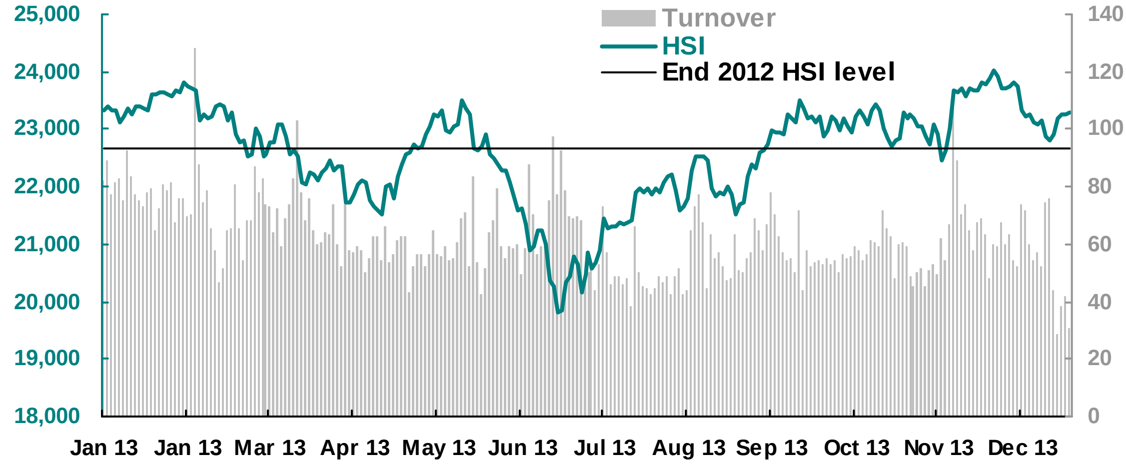
Source: Bloomberg

Hong Kong

40. During 2013, the HSI rose 3% but the HSCEI dropped 5%, following increases of 23% and 15% respectively in 2012. The Hong Kong market underperformed major overseas markets given concerns about the Mainland economic outlook.

41. In early 2013, the Hong Kong market rose on solid Mainland economic data. The HSI reached a 21-month high of about 23,800 points in late January. Yet, the market later retreated amid worries over a credit crunch on the Mainland. Concerns over a tapering of stimulus policy in the US and geopolitical tension on the Korean Peninsula also weighed on the market. The HSI once fell to a nine-month low of below 20,000 points in late June.

42. In July, the market rebounded on easing worries over liquidity conditions on the Mainland and an early exit of the QE programme in the US. Sentiment improved after the release of detailed reform policies on the Mainland. Mainland financial stocks paced gains, given optimism about reform plans in the sector. Upbeat Mainland and US economic data, such as manufacturing and economic growth data, also provided support. In late November, the HSI rose to the highest level in two years and a half.



HSI and Market Turnover during 2013 ($ billion)

Source: Bloomberg

Risks and uncertainties facing the Hong Kong market

43. In 2013, the Hong Kong market posted only a slight gain despite strong rallies in major overseas markets. Looking forward, the market may face risks and uncertainties including:

(a) Reversal of accumulated gains – During 2013, major stock markets rose to their record highs. Investors are concerned that after accumulating substantial gains, the markets are vulnerable to downward corrections. Any disappointing news about economic performance or policy changes may trigger selloffs and worries about a possible downturn may add volatility to the market.

(b) Worries about the tapering of Fed stimulus and fiscal debt problem – Given the nomination of Janet Yellen as the next Fed Chairman, a dovish monetary policy is widely anticipated to continue in the medium term. However, investors remain cautious about the precise pace for the Fed's tapering. The debt ceiling problem was only temporarily resolved and further debates in coming months may affect market volatility.

(c) Movements of capital flows – The global market rally was supported by abundant liquidity amid easy monetary policies in major markets. As the local market has recorded capital inflows after the start of the QE of the US, upon a tapering of the stimulus, capital inflows may recede or even reverse. Possible reversals of fund flows from the Asian markets may pose a contagion impact on the local stock market as well. As an open market, the Hong Kong stock market is prone to risks of volatile capital flows.

(d) Global macro risks – Despite signs of improving economic data, the outlook for global economic growth remains uncertain. In Europe, unemployment rates and debt ratios remain high, and there are worries about deflation risks. Sovereign ratings are still susceptible to downgrades. In Japan, economic recovery remains fragile despite continued supportive policies. On the Mainland, investors are also concerned about the slowdown in economic growth.

44. Hong Kong is affected by the economic performance of the Mainland and the US, given that Hong Kong is an open economy with close economic linkages with the Mainland, and the Hong Kong dollar is linked to the US dollar under the currency board system and Hong Kong interest rates follow those in the US. For the Hong Kong stock market, it has a large Mainland component in terms of issuers but an international and institutional investor base. As such, the Hong Kong stock market performance has also referenced the performance of both the US and Mainland markets. During periods when the US and Mainland markets moved in opposite directions, the rise in one market was offset by the decline in the other. However, if these two markets move in the same direction, the Hong Kong market will track their movements and experience increased volatility. Looking forward:

    (a) On the Mainland, GDP growth is forecast to slow down from 7.6% in 2013 to 7.3% in 2014, according to the International Monetary Fund (IMF). Although a hard landing seems unlikely, slowing economic growth on the Mainland may adversely affect the Hong Kong market.

    (b) In the US, GDP growth is expected to rise from 1.6% in 2013 to 2.6% in 2014. The Fed has announced its plan of tapering of monthly bond purchases starting in January 2014 and might continue scaling back its stimulus at a measured pace depending on signs of improvement in economic data.

    It is likely that uncertainties in the US and the Mainland may weigh on the stock market outlook for Hong Kong.

Real GDP Growth for Major Economies **(%)**

Country	**2012**	**2013 (forecast)**	**2014 (forecast)**
The Mainland	7.7	7.6	7.3
Japan	2.0	2.0	1.2
US	2.8	1.6	2.6
Euro area	-0.6	-0.4	1.0

Source: IMF World Economic Outlook, October 2013

Major statistics of Hong Kong securities market in 2013

Trading activity in the local stock market

45. Trading in the local stock market increased. During 2013, the average daily turnover amounted to $63 billion[1], 16% higher than its $54 billion level in 2012.

46. Mainland stocks remained the most actively traded stocks. Its share of total market turnover was 39% in 2013 (same as 2012), while that of HSI stocks (excluding H-shares and red chips) was about 16% (same as 2012).

Average Daily Turnover ($ billion)

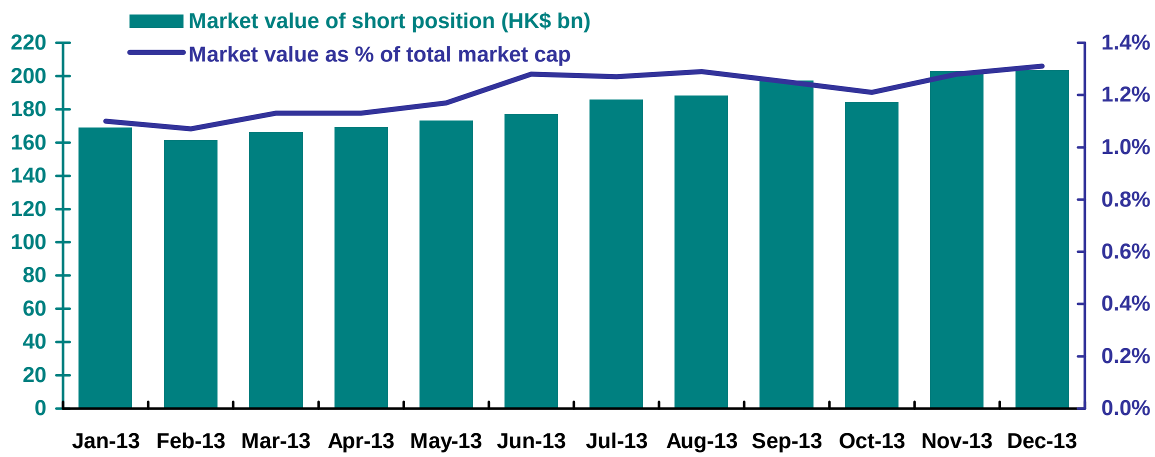
	2013		2012		% change over 2012
HSI (ex H shares & red chips)	9.8	(16%)	8.5	(16%)	15%
Mainland Stocks	24.3	(39%)	20.8	(39%)	*17%*
H-shares	*17.3*	(28%)	*14.9*	(28%)	*16%*
Red chips	*7.0*	(11%)	*5.9*	(11%)	19%
Derivative Warrants	7.3	(12%)	6.7	(12%)	9%
CBBCs	5.2	(8%)	6.2	(12%)	-16%
ETFs	3.7	(6%)	2.1	(4%)	75%
Others	12.3	(20%)	9.5	(18%)	29%
Market Total	**62.6**	**(100%)**	**53.8**	(100%)	**16%**

Remark: Percentages in parenthesis denote market share.
Sources: HKEx and SFC Research

Short-selling activity

47. Short-selling activity rose during 2013. Compared to 2012, short selling was higher in both absolute terms and as a percentage of total market turnover. The average daily short selling was $6,117 million, or 9.8% of the total market turnover during 2013. In 2012, the average daily short selling was $4,864 million, or 9.0% of the total market turnover.

48. Based on the data submitted, as at 27 December 2013, the aggregated short positions amounted to $204 billion (or 1.3% of the market cap of the reported stocks).



Aggregated short positions ($ billion)

Sources: HKEx and SFC Research

[1] Unless otherwise specified, the currency referred to in this report is the Hong Kong dollar.

Initial public offerings (IPOs)

49. There were 102 IPOs in Hong Kong during 2013. Total IPO funds raised amounted to $169.0 billion. This compared to 62 IPOs ($90.0 billion) in 2012. IPO funds raised by Mainland companies accounted for 91% of the market total during 2013. Hong Kong ranked the 2nd in IPO activities worldwide this year and the 4th in 2012.

Top 10 Stock Markets in the World, by Equity Funds Raised through IPOs (2013)

	Equity Funds Raised through IPO		
	US$ billion	**Worldwide Ranking**	**Asia Ranking**
US (NYSE Euronext)	46.58	1	-
Hong Kong	21.77	2	1
UK (London)	20.15	3	-
US (Nasdaq OMX)	18.14	4	-
Japan (Tokyo)	10.15	5	2
Australia	9.80	6	3
Brazil (BM&FBOVESPA)	8.43	7	-
Mexico	5.24	8	-
Singapore	5.17	9	4
Thailand	5.09	10	5

Remarks: Data is provisional only.
Source: HKEx

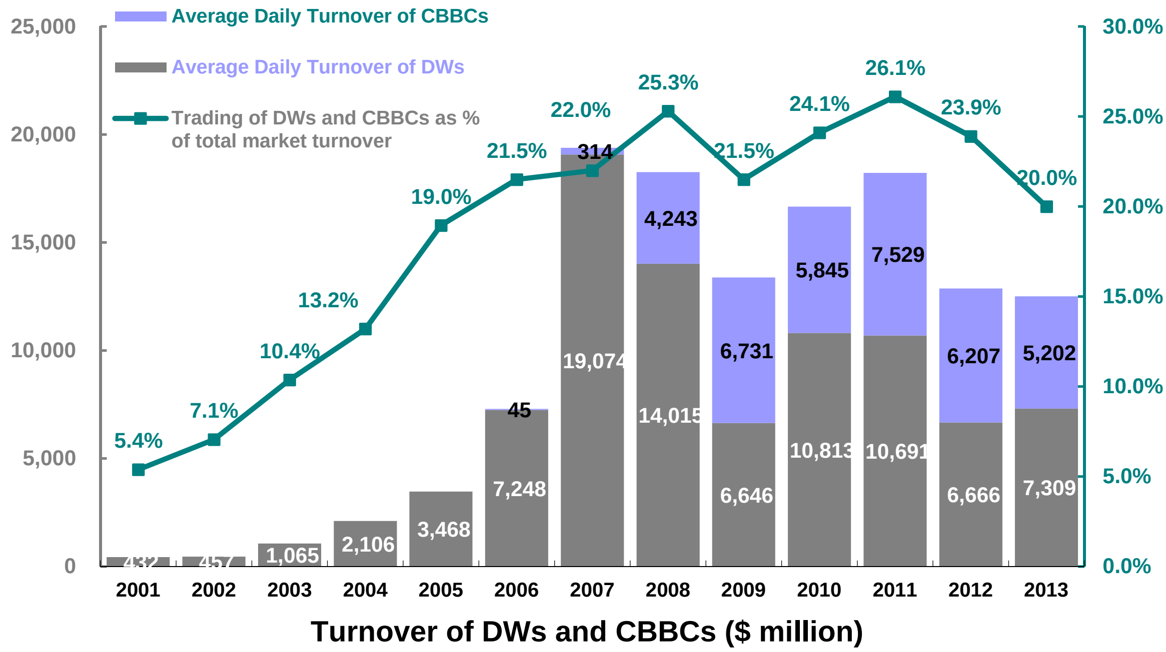
Exchange-traded funds (ETFs)

50. The number of ETFs rose to 116 as at end-2013 from 100 as at end-2012. Their average daily turnover was $3.7 billion in 2013, which was 75% higher than the $2.1 billion in 2012. ETFs accounted for 6.0% of the total market turnover in 2013 (compared to 3.9% in 2012). The increase in ETF turnover was largely due to the strong growth of A-shares ETFs. The average daily turnover of A-shares ETFs rose 95.5% to $2.7 billion, contributing to 73.9% of total ETF turnover (compared to $1.4 billion and 66% in 2012).

Derivative warrants (DWs) and callable bull/bear contracts (CBBCs)

51. During 2013, trading in DWs increased in absolute terms, but dropped as a percentage of the total market turnover. The average daily turnover of DWs rose to $7.3 billion (11.7% of total market turnover), compared to $6.7 billion (12.4% of total market turnover) in 2012.

52. Trading in CBBCs decreased in both absolute terms and as a percentage of the total market turnover. The average daily turnover of CBBCs decreased to $5.2 billion (8.3% of total market turnover) in 2013, compared to $6.2 billion (11.5% of total market turnover) in 2012.



Source: SFC Research

Exchange-traded derivatives

53. During 2013, the average daily trading in exchange-traded derivatives increased 9% compared to the 2012 level. Average daily trading in futures products rose 10%. Among the futures products, HSI futures and HSCEI futures were the most actively traded contracts. They each accounted for about 38% and 41% of all futures trading respectively. Whilst the average daily trading volume of the HSI futures dropped by 3%, that of the HSCEI futures increased by 32% from the 2012 level.

54. Average daily trading in options rose 9% in 2013. Stock options remained the most actively traded options product and trading volume rose 9%, compared to the 2012 level.

Average daily trading volume of derivatives traded on HKEx by product type (contracts)

		2013	2012	2011
Futures	HSI Futures	80,247	82,905	94,036
	Mini-HSI Futures	32,188	34,810	41,933
	HSCEI Futures	85,538	64,863	61,116
	Mini-HSCEI Futures	9,232	6,356	7,516
	Stock Futures	1,882	1,315	1,809
	3-Month HIBOR Futures	0	1	2
	Renminbi Currency Futures ^	568	290	
	Gold Futures	0	0	15
	Other futures products*	1,214	767	263
	Total Futures	**210,869**	**191,176**	**206,688**
Options	HSI Options	35,252	37,597	43,452
	Mini-HSI Options	4,743	5,014	3,888
	HSCEI Options	32,899	25,666	15,364
	Stock Options	249,295	228,438	302,750
	Other options products**	164	103	133
	Total Options	**322,353**	**296,818**	**365,586**
Total Futures and Options		**533,222**	**487,994**	**572,275**

Remarks:

The average daily trading volume was based on the number of trading days after the product was launched.

^ Renminbi Currency Futures commenced trading on 17 September 2012

* One-Month HIBOR Futures, Three-year Exchange Fund Note Futures, HSI Dividend Point Index Futures, HSCEI Dividend Point Index Futures, HSI Volatility Index Futures (launched on 20 Feb 2012), IBOVESPA Futures (launched on 30 Mar 2012), MICEX Index Futures (launched on 30 Mar 2012), Sensex Index Futures (launched on 30 Mar 2012) and FTSE/JSE Top40 Futures (launched on 30 Mar 2012).

** Flexible Hang Seng Index Options and Flexible H-shares Index Options

Sources: HKEx and SFC Research

After-Hours Futures Trading (AHFT)

55. The After-Hours Futures Trading (AHFT) session on Hong Kong Exchanges and Clearing Limited commenced trading on 8 April 2013. HSI and HSCEI futures contracts are available for trading during 5:00-11:00pm (Hong Kong time). From 8 April to 31 December, the average daily turnover of the HSI and HSCEI futures during the AHFT session amounted to 3,240 contracts and 3,396 contracts, which were about 4.2% and 4.0% respectively of the trading during the daytime trading session. This compared to around 15-37% in major overseas markets. The average intraday volatility during the AHFT session was 0.6% for HSI futures and 0.8% for HSCEI futures, compared to 1.2% and 1.8% during the daytime trading session respectively. More than 100 brokers have participated during the AHFT session, including both local and international brokers.